PRAETORIAN GUARD[SM]

QUARTERLY NEWSLETTER
2ND QUARTER 2020

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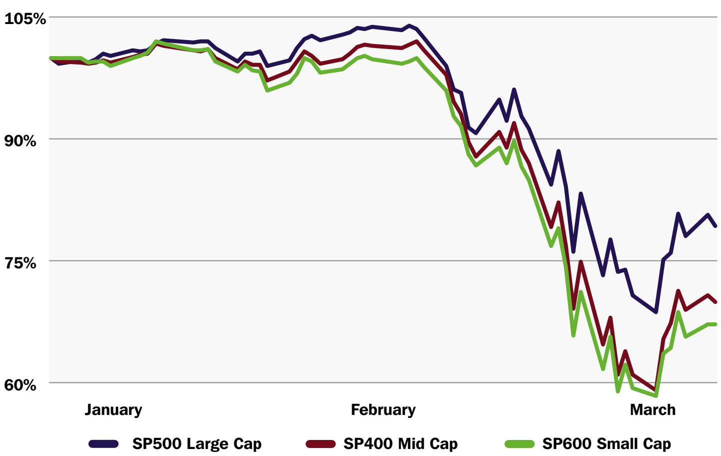
FIRST QUARTER 2020 MARKET COMMENTARY

By **Richard A. Hewitt**

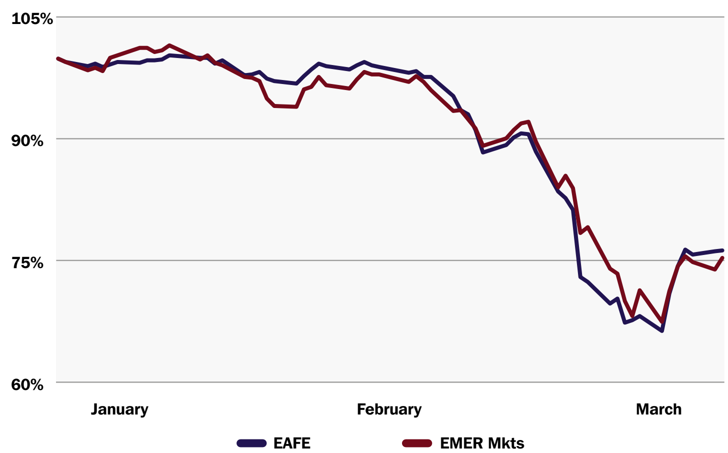
To call the last 45 days of market performance a "violent reaction" is an understatement. From the new market all-time highs on February 19th to the low on March 23rd, the S&P 500 Large Cap declined almost 34%. All other indices (S&P 400 Mid Cap, S&P 600 Small Cap and international markets) were down at least that much.

U.S. Equity Market Performance Q1 2020



Source: Yahoo! Finance

International Equity Market Performance Q1 2020



Source: Yahoo! Finance

During that period, we experienced *both* the six largest point declines ever in the Dow Jones Industrial Average and the six largest point gains as the collective market participants sought to find their footing. More relevant to our analysis are the percentage changes. There we find that the second biggest decline (next to 1987) was on March 16th and the fourth largest gain was on March 24th. Overall, the early 1930s were more volatile on a percentage basis. Significance? There are several:

1. *Risk.* The only constant in the market—it is always present, and the variation is only in magnitude. As investors, risk is not always at the forefront of our mind. When markets are advancing consistently, we are all bold and brave. However, when we experience periods similar to the last six weeks, we extrapolate today's conditions to the end of time. It is almost impossible to remember that *both* Bull and Bear markets end.

2. *Risk Tolerance.* This is where risk and you intersect. Three components to be aware of in determining your own risk tolerance:

Risk Requirement: How much risk must you accept in order to earn the long-term returns required to achieve your goals? Start young, the requirement is lower; start later in life, it will be higher.

Risk Capacity: How much risk can you financially afford/accept? Think of it this way: if I am down 45% and can still achieve my goals, I have a high-risk capacity. Conversely, if a 10% decline threatens to derail my entire financial situation, I have little capacity to absorb the inevitable volatility of the market.

Risk Tolerance: How do I FEEL about the risk I am experiencing today? This aspect is emotional and difficult to measure because it changes both over time and in response to the last headline or check of your portfolio. *(continued on page 2)*

TAX CONSIDERATIONS FOR MORTGAGE REFINANCING

By **Marc A. Wehmeyer**

Many homeowners have been conditioned to expect tax savings from the deduction of mortgage interest on their tax returns. This is no longer the case for some homeowners because of changes in the tax law resulting from the Tax Cut and Jobs Act of 2017 (TCJA). The law greatly increased the standard deduction and eliminated personal exemptions. The standard deduction in 2020 is $12,400 for singles and married couples filing separate returns; $24,800 for married couples filing a joint return; and $18,650 for head of household. The standard deduction is higher for taxpayers who are over 65 or blind.

Additionally, the TCJA reduced the amount of mortgage interest you can deduct. For homes purchased after December 15, 2017, homeowners can deduct interest on the first $750,000 of home acquisition debt for married couples filing a joint return ($375,000 for married filing separately). The $750,000 limit applies to home acquisition debt on your main home and second home, if applicable. The old limit was $1,000,000 ($500,000 for married filing separately) for debt secured after October 13, 1987 and until December 15, 2017. The TCJA also eliminated the deductibility of interest on home equity loans and lines of credit unless the proceeds were used to buy, build, or substantially improve your home and the debt is secured by that home. As a result of the changes, some homeowners no longer benefit from deducting their mortgage interest and find they are better off taking the standard deduction.

If you refinance a mortgage for a property purchased after October 13, 1987 and before December 15, 2017, you can still retain the $1,000,000 limit on home acquisition debt up to the amount of the mortgage principal balance just before the refinancing. There are separate considerations regarding the deductibility of mortgage debt used to make home improvements that exceed the scope of this article.

Tax considerations alone shouldn't stop you from taking out a new mortgage or refinancing your existing ones. Mortgage rates remain at historically low levels and the opportunity for refinancing is real. Everyone's personal circumstances are different and there are multiple options to consider – such as the length of the new mortgage (typically 30-year or 15-year) compared to your existing mortgage, the type of interest rate (fixed or adjustable), the type of ownership (primary residence, second home, or rental property), whether or not it makes sense to refinance the existing balance or do a cash-out refinance, how much regular income you have, and the length of time you expect to own the property.

Please reach out to us if you would like assistance in determining whether a mortgage refinance would make sense for you and your situation.

FIRST QUARTER MARKET COMMENTARY

(CONTINUED FROM PAGE 1)

THERE IS A REASON THE RULE IS BUY LOW/SELL HIGH AND MOST INDIVIDUALS DO EXACTLY THE OPPOSITE. THEY GET IN FOR "FEAR OF MISSING OUT" (FOMO) AND SELL WHEN THEY "CAN'T TAKE IT ANYMORE."

3. ***Avoiding being my own worst enemy.*** If one accepts the above two observations as accurate, then the variable most in your control is YOU. Step outside yourself and you may be able to see that your own reaction to the current day's market closing number is driving you to "do something" (sell, go to cash or something else). The driver is NOT the market activity but your perceived, immediate reaction to it.

There is a reason the rule is buy low/sell high and most individuals do exactly the opposite. They get in for "fear of missing out" (FOMO) and sell when they "can't take it anymore." Translation: buy high/sell low. The only way to avoid making that mistake is to know how risk impacts your short-term decision making, slowdown that decision making and make fact-based decisions (not emotional ones).

PRESIDENT'S COMMENTARY

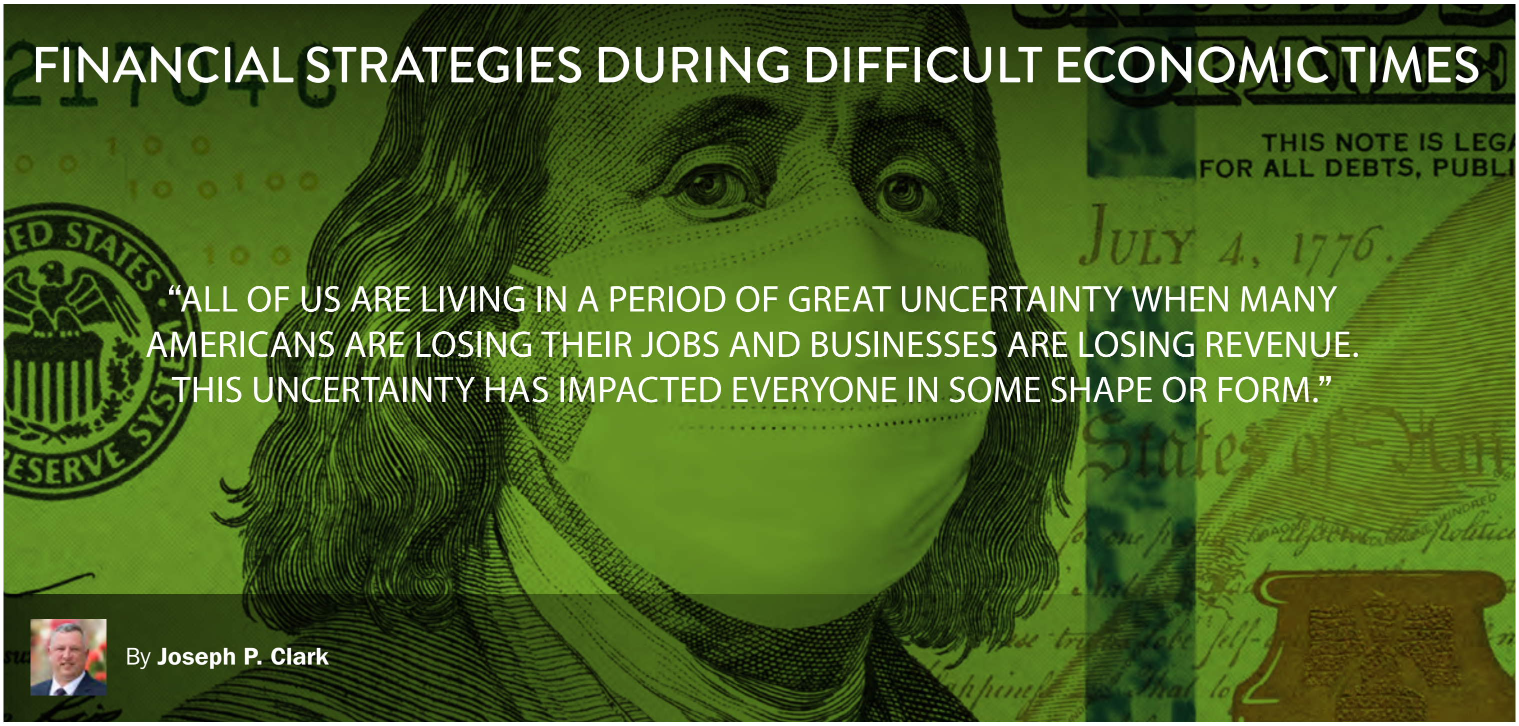
The world certainly is different than just 90 days ago—both for worse and better simultaneously.

The "worse" aspect is well known by all today: strained health care systems, exhausted first responders and care givers, and what I am calling the "Economic Shelter Down"- ending a multi-year period of sustained growth. All of those problems are fixable and have been or are in the process of being addressed.

The "better" aspect is that the United States once again is doing what we are really good at: figuring out how to use all of our talents and resources for the common need in a crisis. We have done this many times before in our history: December 7, 1941; September 11, 2001; and now February 2020.

Changing the production of distilled booze to hand sanitizer, modifying existing equipment to perform as ventilators and thousands of other stories. Our country's greatest comparative advantage is not just our vast resources, but the creative genius of 327 million of us, each of who knows something of value and thinks slightly differently. Therefore, collectively we solve problems faster and more creatively than Artificial Intelligence (AI) will ever be able to do. That will get us through "today" and serve us well "tomorrow" and every day thereafter.

FINANCIAL STRATEGIES DURING DIFFICULT ECONOMIC TIMES



"ALL OF US ARE LIVING IN A PERIOD OF GREAT UNCERTAINTY WHEN MANY AMERICANS ARE LOSING THEIR JOBS AND BUSINESSES ARE LOSING REVENUE. THIS UNCERTAINTY HAS IMPACTED EVERYONE IN SOME SHAPE OR FORM."

By **Joseph P. Clark**

All of us are living in a period of great uncertainty when many Americans are losing their jobs and businesses are losing revenue. This uncertainty has impacted everyone in some shape or form. People are asking themselves what they might do to minimize the negative effects of a very difficult market and potentially even take advantage of the situation financially. Here are some points to consider:

1. ***Keep investing for retirement.*** If you are not yet retired, this is not the time to stop investing. For those who were working during the financial crisis of 2008, you know that staying the course and focusing on your long-term strategy was tantamount to success. During that bear market some investors saw their investment accounts cut nearly in half, but those who continued to invest were rewarded with a bull market that ran for over a decade. In the words of Warren Buffet, "The stock market is a device to transfer money from the impatient to patient." Simply continue to invest on a regular basis and you will be buying more shares at lower prices. Don't forget to rebalance your employment retirement plans on a quarterly basis so you are systematically buying more of assets that have underperformed (buying low) and selling assets that have outperformed (selling high). Staying the course now will lead you to success later. Famed investor Shelby Davis said, "You make most of your money in a bear market; you just don't realize it at the time."

2. ***Reevaluate your asset allocation and your overall financial plan.*** Asset allocation refers to how you allocate your investments among stocks, bonds, real estate, and cash. The asset allocation decision is impacted by several factors such as investment time horizon and risk tolerance. The current market has caused many people to reassess their risk tolerance. For those in or near retirement, an allocation in bonds ensures it will be many years before you would be required to sell equity positions to fund your retirement income. Please work with your advisor to update your financial plan and risk tolerance to see if you are still on track to meet all your financial goals.

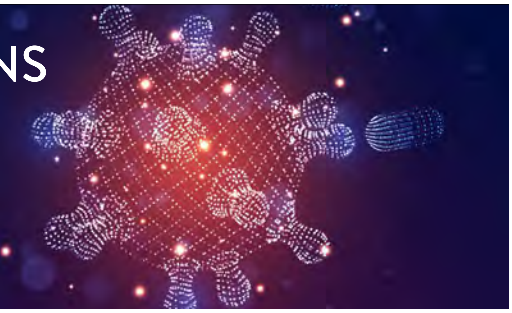
3. ***Revisit Mortgage Refinancing.*** Interest rates are near record lows so this is something everyone should explore with your current lender and other mortgage companies that focus on refinancing. Let's say you owe about $660,000 on a 30-year fixed rate mortgage at 3.625% that you have been paying on for almost three years. The original balance was $700,000. Your current monthly payments for principal and interest only are $3,192. You have the opportunity to refinance that $660,000 balance at 3.25% for 30 years, giving you a new monthly payment for principal and interest only of $2,872—a monthly savings of $320. Assuming the current average cost of refinancing a mortgage is $4,535, then it would take about 14 months to recoup the refinancing cost and break even. This is just an example calculation. We can assist in exploring this option to include the costs and benefits of a 15-year vs. 30-year mortgage.

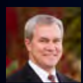
4. ***Student Loan Consolidation.*** For the 2019-2020 academic year the rate on undergraduate Stafford loans is 4.5%. However, these rates are based on the government's cost of borrowing. On May 12, 2020, a government auction of 10- year Treasury notes will determine rates on new federal loans taken out after July 1, 2020. Given 10-year Treasury yields at or below 1%, the rates for these new loans could fall below 3% (which is near the record lows set in 2005). Private loans may be fixed or may have a variable rate tied to LIBOR, prime or T-bill rates. When the Federal Reserve cut rates to essentially zero, borrowers with private loans also paid less in interest too. Rates on private variable loans have fallen to 2.4% and 10-year fixed-rate loans are as low as almost 3.8%, down from a July 2018 peak of 6.05% on average. This may be the perfect time to consider consolidation and refinancing into a new fixed rate loan to lock in near record low rates.

5. ***Roth Conversions.*** The recent market downturn lessens the tax expense of converting from traditional pre-tax retirement accounts to after-tax Roth funds. Tax rates are also favorable under the 2017 Tax Cuts and Jobs Act. Investors who own traditional accounts defer income tax on their savings until withdrawing the money in retirement. Roth savers pay tax up front and don't pay later. Taking Roth distributions could decrease Social Security taxes and Medicare premiums, which are pegged to one's modified adjusted gross income. In addition, having at least some portion of your assets in Roth accounts reduces the risk associated with unknown future tax rates.

These are just some examples of actions you might consider during this period of uncertainty. Stay in close contact with your advisor to determine what steps might be appropriate given your specific financial situation.

THE POLITICAL AND ECONOMIC LESSONS FROM Q1 2020 AS WE GO FORWARD





By **Richard A. Hewitt**

Very few missed the quote from Rahm Emanuel regarding crises. There is a parallel that we need to learn and apply in the months and years ahead: "Never let a crisis end without making sure you don't revert to doing things the same dumb way." That quote is attributed to the guy in the above photo.

What do I mean? A few straightforward examples where we should not revert to the previous mindset:

1. The FDA should have side by side clinical trials of drugs that are already approved for medical use (and we are just trying them on an "off label" manner)
2. Restaurants need to apply for an additional license in order to serve take out or have curbside pickup.
3. Medical practitioners (using telemedicine with patients and states) should recognize their licenses across state lines, at least in contiguous states.

We should demand and hold accountable the Federal, State and local governments who had to waive a host of rules and regulations in order to respond to this COVID-19 pandemic—why do ALL of those need to be reinstated? I surmise many (most?) do not and the economy will be more efficient and responsive for it. Governments will be better prepared for the inevitable future crisis.

Additionally, the Preamble to the U.S. Constitution is clear: "provide for the common defence and promote the general welfare" are two of the six reasons for the establishment of the U.S. Constitution. The COVID-19 virus will not be the last time we deal with a national pandemic. At the Federal, State and local levels we cannot wait to replenish reserve stockpiles of supplies. We need to understand the lessons learned the hard way from hospitals, testing centers, first responders (who are on the front lines) and any others and apply them. If we do, when next time arrives, we won't make the same mistakes but make new/different mistakes. Repeating the same errors would be inexcusable.

Finally, and related to the second point above, we should expand the definition and application of manufacturing that is required for national defense. Producing planes, tanks, ships, etc. are all what we "normally" think of the defense industrial base. We need to enlarge the definition to realize it also includes medical defense against an enemy as dangerous (or potentially more) who does not wear an identifiable uniform or carry a rifle. The U.S. should bring back vital manufacturing capacity from overseas, especially China, so we are not at risk of being held hostage due to basic medicine inputs or supplies that we outsourced to save "money."

In closing, this was a wakeup call. Even with all our advancements in technology, knowledge and research we can still be brought to a near standstill by a virus (just like our ancestors). The difference is that we can learn, share and adjust our future responses to be superior to that of 2020. Thank God we live in the United States of America.

FEAR AND GREED

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CLOSING THOUGHT

"The world doesn't end that often."

—Benjamin Graham

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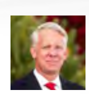
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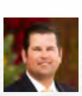
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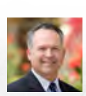
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