HEMSLEY EST. 1993 ADVISORS

The Advisor

QUARTERLY NEWSLETTER

2021 Q2 REVIEW:

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GENERAL MARKET COMMENTARY

In typical stock market fashion, Q2 was filled with numerous market-moving events that investors had to analyze, discern, and translate into current and future stock valuations.

The quarter began with overall impressive corporate earnings reports and positive outlooks for the full year, or for at least the upcoming quarter. This caused the continued appreciation in interest-sensitive value stocks such as banks and industrial companies like Dow Inc., Deere & Company, Honeywell International Inc., and many others. Energy-related stock valuations increased throughout the quarter as an expanding and reopening U.S. economy increased the demand for energy.

Also, dividend yields in excess of 5% attracted investors to big oil companies and pipeline companies. By quarter's end, despite growing inflationary concerns, the market averages ended with year to date gains for the Dow Jones Industrial Average, the Standard & Poor's 500 Stock Index, and the NASDAQ Composite Index of 12.7%, 14.4% and 12.5%, respectively.

Inflationary concerns and questions as to when the Federal Reserve might raise interest rates became a lively topic in the last half of the quarter. These concerns were fueled by pandemic ending, unprecedented consumer demand for goods and services. The economy is also suffering through continuous supply shortages from coffee cups and splash sticks at Starbucks to larger items such as automobiles and housing. The Federal Reserve Chairman, Mr. Jerome Powell, states that the inflationary forces will recede once the pandemic-induced demand is reduced and supply shortages are normalized. There are clearly many skeptics on inflation's prospects, but the Fed has established credibility based on the job they have done steering the economy from the depths of the pandemic through today's reopening.

However, if inflation persists, which is now running at approximately an annual rate of 3.4% (3.9% when food and energy are included), interest rates will increase sooner than late 2022 or early 2023. Daily stock market activity will become more volatile, and appreciation will be more difficult. Bouts of rising prices reduce individuals' purchasing power and erode corporate profit margins that eventually affect earnings.

Ultimately, after the price increases have subsided, individuals' purchasing power and corporate profit margins are rebuilt.

This creates a more normalized ebb and flow in the daily financial markets with appreciation over time. For most of this century, we have experienced a disinflationary environment, i.e., economic growth with little or no inflation. This is an ideal environment for real wage increases for workers and creates a very favorable outlook for stock market appreciation. This is a trend that has benefited people all over the world.

Despite inflationary concerns, it was very noticeable that the 10-year Treasury Note yield drifted lower throughout the quarter instead of up as one would expect. It ended at 1.44%. Short-term rates are not only near 0% but it is even difficult to find bonds to buy. Investors must go out 3 years to begin to see rates above 1% on lower quality investment grade bonds.

These rates are kept low by the Fed's continued quantitative easing (buying bonds and mortgages) and the trillions of dollars of money in personal and corporate bank accounts. One can easily see the massive amounts of cash looking for yield by the recent sale of 3-year notes by Salesforce.com, Inc. Due to their corporate bond rating of A, the sale was oversubscribed. The planned interest rate was .4% but due to very strong demand, the effective interest rate yield was decreased to .18%.

When one hears that the Fed is beginning to reduce their bond buying, that will be a sign that rates will begin moving higher. In the meantime, as we have mentioned before, don't just look at the low level of interest rates and become frustrated. It is partly due to these low rates that the stock market continues to appreciate. One positive from the low interest rate environment is the increase in corporate dividends.

A year ago, we were concerned by potential dividend reductions and the effect on one's cash flow. Here we are a year later, and many companies have raised their dividends from mid-single digits to low double-digit increases. Just prior to the Independence Day holiday, many banks announced very significant dividend increases of 10% and higher. These dividends provide new monies that can be invested into a portfolio, provide income for retired individuals, and provide a hedge against inflation. Should inflation cause stock prices to stagnant and increase frustration with investors, it will be the attractiveness of dividends that enhance performance and investment opportunities.

We are amazed at the appreciation in account values over the last 10 years. This appreciation has enhanced one's future financial security, particularly when a decade ago one might have been concerned about their ability to retire. But perhaps now they can look forward to retiring with a higher degree of financial security. It also shows the importance of always staying fully invested and living within your means. To summarize: Keep saving, investing, watch how your money is spent, and pay attention to inflationary trends and interest rates.

FINANCIAL PLANNING – A MILLION-DOLLAR ROTH

Clients regularly ask if they should contribute to their 401(k) plan and other qualified retirement accounts via pre-tax deductible contributions or after-tax contributions.

After-tax contributions are made to either a Roth IRA or a Roth 401(k) (if offered by your employer).

WHAT IS THE DIFFERENCE?

If you are just focusing on taxes, the pre-tax contribution option will likely result in an annual tax savings of $1,000 to $8,000 per year. The actual amount depends on the participant's age, amount of contributions, and, of course, their tax bracket. While the after-tax dollars contribution will reduce your take home pay, the benefit is when you reach age 59 ½ when any money withdrawn will be income tax free.

There are numerous benefits of having part of one's retirement money be income tax free. First, there is no required minimum account distribution. This creates lower taxable income, avoids bracket creep, makes more income-based deductions available, and your Medicare Part B premium charges, which are a function of Adjusted Gross Income (AGI), could possibly be reduced.

Another benefit is it gives you options in managing and planning your personal cash flow. While the primary objective of the account would be to provide monthly retirement income, part of the account could be separated and considered a long-term care emergency fund. These funds could be used to provide in-home care in the later years of life allowing an individual or couple to remain in their home. These tax-free monies could also be used for when a car down payment is needed, a large home repair is necessary, major dental expenses are incurred, or other one-time expenses are contemplated.

> According to 2018 IRS data, it is estimated that 4.4 million taxpayers contributed to a Traditional IRA and 7.1 million taxpayers contributed to a Roth IRA.

Today more entities are allowing participants to split their 401(k) contributions between a pre-tax account plan and a Roth or non-deductible account. We encourage you to consider this option if available at your place of employment. Splitting your contributions allows tax savings today and tax-free income at retirement.

But how much of one's salary should be contributed? The general advice typically given to young workers is to contribute a total of 10% of their salary, either all in one type of account or split between the pre-tax and after-tax portion of the 401(k). Then, as your salary increases, so should your contribution: first to 12% then 15%.

In addition to the Roth 401(k), there are also Roth IRAs available to investors that have many of the same benefits of a Roth 401(k). One difference between a Roth 401(k) and Roth IRA, is that with a Roth IRA, you can withdraw $10,000 of earnings tax-free if you are a first-time homebuyer. Younger individuals with small traditional IRAs may want to consider converting them to a Roth IRA. Yes, you would incur taxes today, but if you are in a low tax bracket, the cost is negligible when you consider the potential future account value and the benefit of tax-free withdrawals.

For higher earners who have fully funded their 401(k) for the year but want to set aside additional funds for retirement, there is a way to contribute to a Roth IRA. First a non-deductible contribution is made to a traditional IRA and then immediately is converted into a Roth IRA. This conversion would be tax-free if done quickly and is referred to as "a back door funding method." Although this process may seem complicated, it is perfectly legal and a great tax planning strategy.

Just like other areas of one's life, we believe investors should establish a goal for their future Roth IRA or Roth 401(k) account balance. We like to say everyone should set a goal of a million-dollar Roth when they retire. While this may seem lofty, it is not too difficult for someone in their 20s or 30s to obtain if they are savers. It's also possible for a worker in their 40s or early 50s assuming they have made some previous Roth IRA contributions or conversions.

Why a million-dollar Roth? Because the owner could potentially receive $50,000 per year or $4,167 per month in tax free retirement income assuming a 5% distribution rate.

We realize that a million dollars in the future may not have the same purchasing power as it does today. But we also know that once the discipline of saving is established today, the account may be worth even more. Truthfully, the million dollar objective is a random number. The important point is for you to have a goal, whether it be $100,000, $500,000, $1,500,000, or any other number, and work to obtain it. This creates discipline as well as causes millennial and mid-career workers to focus on their financial well-being and income in retirement. Once you have established a goal, we can then help you to adjust your contributions to both meet the goal and to maximize your tax efficiency.

Last, parents and grandparents can help set their child or grandchild up for future financial security. If the child or grandchild has a part-time job throughout the year or summer employment, don't hesitate to establish a Roth IRA for them. A Roth contribution can be made as long as they have taxable wages. The funding would be done from the parents or grandparents via a gift up to $6,000 but not more than the child's earnings.

No matter the amount, even if it is only $1,000 or $1,500 per year, the educational benefits of showing the child or grandchild the benefits of saving today for their future security are significant and should be considered.

> In spring 2020, car rental agencies sold more than 770,000 cars. This means 1 out of every 3 rental cars is no longer available.

FINANCIAL PLANNING – SUMMER TRAVEL

Vacation travel is back. As many people may have experienced, airports are crowded, and airplanes today are usually 80% if not 100% full. Not only can it be difficult to reserve a car for the date and time needed, but be prepared for sticker shock when you see the cost! Our recommendation is to immediately book your rental car when you have established your travel itinerary — not two weeks prior to leaving on your trip like most of us have done in the past.

There is also a new reality once you reach your destination. Rental car lines are very long. Waiting times can be 30 – 90 minutes just to get to the counter. One way we have found to avoid these long lines is to become a member of the rental company's advantage program. This allows you to skip the long waiting lines and go right to the rental garage to pick up your car. You will be well compensated for the small amount of time and energy spent signing up. Make sure you put your member number in the reservation prior to picking up your car. By doing so, your paperwork is already for you to go.

Most of us who have a Costco membership find that their rental prices are hard to beat. Avis, which is an option using Costco, has also partnered with Amazon. Prime members typically get almost 30% off and sometimes an Amazon gift card once the rental is complete. We suggest you compare to get the best possible car rental rate.

Finally, if your rental has free cancellation, keep checking the rental price with your company and others. There have been times we have seen anywhere from a reduction of $10-$40 and sometimes even more. These savings can be spent on your trip.

FINANCIAL PLANNING – EVENT INSURANCE

Given the numerous weddings and social events that were postponed during COVID and rescheduled to 2021, we would like to remind you about obtaining event insurance for your next event. This type of policy (liability protection) covers events and social gatherings outside of your home. This is different than wedding insurance, which covers a vendor not showing up or in the unfortunate case the wedding is cancelled.

Most people do not realize that if the event is NOT in your home or on your property, say it's in a clubhouse or social room, typically your homeowner's policy will not cover the event should something happen. First your coverage should be confirmed with your insurance agent. Then consideration should be given to getting event insurance, and if liquor is being served, it covers your liability as a host. The purpose of the coverage is to protect your hard-earned net worth against many perils such as a guest who slips and falls, develops food poisoning, consumes too much liquor, etc.

The cost for event insurance will vary depending on the type of event, the duration, and the number of people attending. For instance, a one-night party in the association's club house may cost around $300 for $1,000,000 to $2,000,000 in liability coverage. If you are hosting a wedding that could extend over three days of entertaining out of town guests, then a likely fee could run $600 to $900. No matter the size of your event, you never know when the worst-case scenario could become reality. Liability coverage is very inexpensive and will provide you with peace of mind.

GO PAPERLESS!

As a reminder, you have the option to receive your quarterly portfolio statements and newsletter electronically. Receiving this mailing electronically is especially convenient if you are traveling or spend time at a second home (not to mention it ensures prompt receipt knowing the difficulty some people recently have been experiencing with the mail service).

If you would like to go paperless, please contact Nick directly at nmartin@hemsleyadvisors.com or give us a call. Nick will send you the appropriate document to sign. This document must be returned to us before we can send your portfolio reports electronically.

As always, we are always here to assist you. Helping clients with their finances so they can achieve their goals, get to retirement and through retirement is very rewarding for us and is why we enjoy coming to work every day. Do not hesitate to call with any questions or concerns.

Have a wonderful summer!

NEWSLETTER DISCLOSURES:

1. This newsletter may include forward-looking statements. All statements other than statements of historical fact are forward-looking statements (including words such as "believe," "estimate," "anticipate," "may," "will," "should," and "expect"). Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. Various factors could cause actual results or performance to differ materially from those discussed in such forward-looking statements.

2. Past performance is not indicative of any specific investment or future results. Views regarding the economy, securities markets or other specialized areas, like all predictors of future events, cannot be guaranteed to be accurate and may result in economic loss to the investor.

3. Inclusion of index information is not intended to suggest that its performance is equivalent or similar to that of the historical investments whose returns are presented or that investment with our firm is an absolute alternative to investments in the index (if such investment were possible). Investors should be aware that the referenced benchmark funds may have a different composition, volatility, risk, investment philosophy, holding times, and/or other investment related factors that may affect the benchmark funds' ultimate performance results. Therefore, an investor's individual results may vary significantly from the benchmark's performance.

4. Any information provided by Adviser regarding historical market performance is for illustrative and education purposes only. Clients or prospective clients should not assume that their performance will equal or exceed historical market results and/or averages.

5. This newsletter is intended to provide general information only and should not be construed as an offer of specifically tailored individualized advice.