3Q19

The Financial Solutions Advisor

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Contact us:

8700 W. Bryn Mawr Ave.
Suite 410-N
Chicago, Illinois 60631
773.714.1540 *Main*
773.714.1550 *Facsimile*
www.fsadvisorygroup.com

Economic & Market Perspectives

The first half of 2019 has been an odd period for investors. Coming off the sharp 20% correction that dominated the end of 2018, stocks and other risk assets rose strongly to start the year and have been bouncing up and down while mostly trading sideways.

Trade uncertainty continued in the second quarter, raising concerns about the potential for a broad slowdown in the pace of global economic activity. This development led global central banks to signal monetary easing in the months ahead; helping U.S. large-caps and developed market stocks to recoup their May losses and finished the quarter up 4.3% and 4.0%, respectively.

Although U.S. stock markets finished the quarter back at the high ends of their 18-month trading range, investors are focused on a number of downside risks, including trade and other geopolitical issues and signs of slowing in the global economy and corporate earnings backdrop.

Emerging stock markets struggled against a weaker economic backdrop, and ended the quarter at 0.7%. Commodity prices fell 1.2%, driven by a decline in metal prices due to expectations for softer demand. U.S. core bonds returned 3.1%, as the U.S. 10-year Treasury yield fell 42 basis points over the course of the quarter.

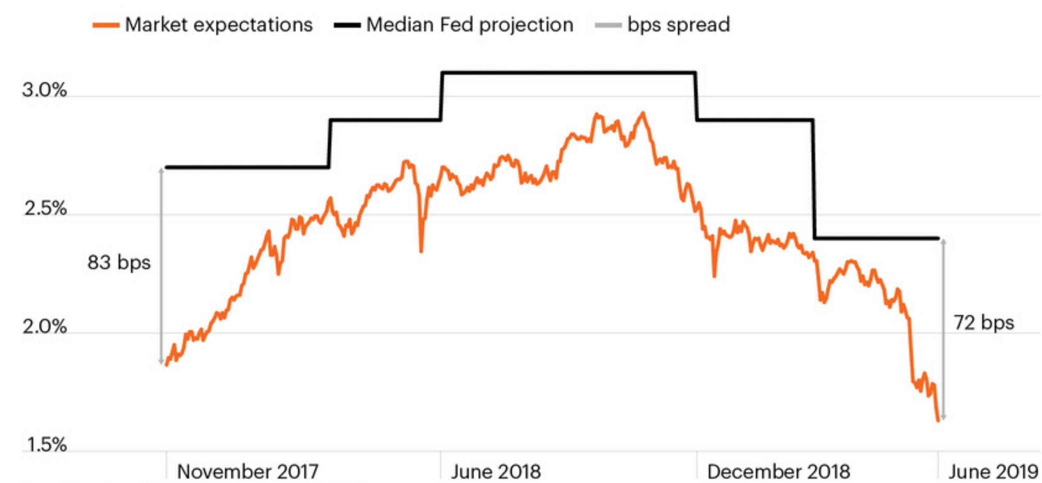
Looking at the remainder of 2019, it seems unlikely that trade tensions will dissipate, and investors will be closely watching how negotiations evolve over the coming months. Beyond politics, the Federal Reserve is expected to cut rates in the second half of the year and global central banks will likely follow suit. While the prospect of lower interest rates clearly helped risk assets in the second quarter, the issues that are driving them lower suggest a more defensive strategy going forward.

Sources: Nuveen, J.P. Morgan Asset Management

2019 Returns

S&P 500	*18.54%*
NASDAQ	*21.85%*
Russell Small Cap	*16.98%*
Russell Mid Cap	*21.35%*
MSCI EAFE	*14.03%*
MSCI World	*16.98%*
Barclay US Agg. Bond	*6.11%*
Barclay Municipal Bond	*5.09%*

Gap in Rate Expectations Signaling Market Volatility Ahead?



According to the Fed's dot plot, eight Fed governors forecast at least one rate cut for this year. But the median Fed forecast for rates in 2019 held steady at 2.4%.[2] Within this context, it's important to remember that market expectations for the Fed funds rate have been consistently lower than the Fed's own projections.

As the chart shows, this was true when investors expected rates to rise in late 2017 and has been equally true in today's environment. In fact, investors currently expect the target Fed funds rate to finish 2019 at approximately 1.75%, which implies more than three rate cuts within the next six months.[1]

Since December 2017, the divergence between market expectations and Fed projections has never been wider, creating the potential for significant volatility should the size of this rift persist.

1 *Bloomberg, as of June 20, 2019*
2 *Fed Reserve Summary of Economic Projections*

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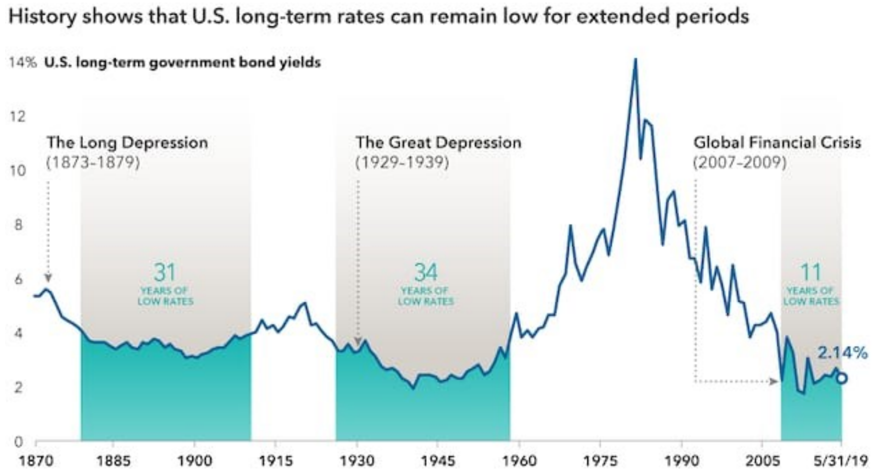
History Shows U.S. Long Term Rates Can Remain Low



Sources: Federal Reserve, FactSet, Robert Shiller, Thomson Reuters. Data for 1871–1961 represents average monthly U.S. long-term government bond yields compiled by Robert Shiller. Data for 1962–2018 represents 10-year Treasury yields as of December 31 each year within the period. 2019 data as of 5/31/19. Length of low rate periods above are consecutive years with rates below 4%.

Rising Labor Costs Add Pressure to Corporate Profits

Sources: Bureau of Labor Statistics, Thomson Reuters. Employment Cost Index uses quarterly data as of 3/31/19. Unemployment rate uses monthly data as of 4/30/19.

Using IRAs to Make Charitable Donations

Many retirees are disappointed to find out they will not deduct their charitable gifts for income tax purposes this year. That's because the 2017 Tax Cuts and Jobs Act sharply cut the number of filers who itemize by nearly doubling the standard deduction.

Just 8% of filers are expected to take a charitable deduction this year, down from 20% in the past, according to the Tax Policy Center in Washington, D.C.

But all is not lost for retirees with a charitable bent: Those over 70 ½ can use a workaround that preserves the tax benefits of giving, even if they don't itemize. In what's called a qualified charitable distribution (QCD), retirees can donate all or a portion of their required minimum distributions (RMDs) from IRAs – up to $100,000 a year – directly to charity.

"The QCD comes right off the top of adjusted gross income, which is attractive from a tax-planning perspective" said Peter P. DeVito, a partner with Cleveland-based Fairport Asset Management. "With the loss of the charitable deduction, QCDs are becoming very popular now, predominantly with clients who don't need all of part of their RMD income."

While retirees don't get a write-off for their charitable gift QCD, they also don't owe taxes on their retirement-account distributions they donate this way.

For a taxpayer in the 22% bracket, funneling a $5,000 RMD to a qualified charitable distribution saves $1,100 in income taxes, the same as if you'd been able to deduct it. Even though this rule became a permanent part of the tax code in 2015, the 2017 tax law raising the standard deduction made it that much more attractive, DeVito said.

"We have clients who donate as little as a couple thousand dollars up to $100,000 in QCDs. I think you'll see people using them more and more beginning this year," he added.

A smaller tax bill is not the only potential benefit. By donating their required minimum distribution, retirees reduce their adjusted gross income, which can mean less of their Social Security is taxed and they could see a reduction in their Medicare premiums.
There's yet another tax-planning perk; "For states that don't allow itemized deductions, retirees who use QCDs will also pay less in state taxes," DeVito added.

To do a qualified charitable distribution, retirees must instruct the firm that manages their IRA to direct some or all of their RMD to one or more charities. The firm must send the money directly to the charity or send the retiree a check made out to the charity, which then must be forwarded.

The IRS does not allow taxpayers to collect the money first and then donate it for the qualified charitable distribution.
The QCD donation must be made during the calendar year for which a retiree is filing a tax return.

"We have quite a few clients who are using QCDs," said Tim Steffen, director of advanced planning at Milwaukee-based Baird Private Wealth Management.

But retirees must be careful to report QCD donations correctly on returns, which can be a bit of a filing headache that even confuses accountants, Steffen said. That's because the brokerage or fund company that holds your IRA will report it on Form 1099-R as a regular IRA distribution. Taxpayers have to note on their returns that it's a QCD and not taxable.

It is also up to the taxpayer, not the broker-dealer, to make sure a charity qualifies. For record-keeping purposes, it's a good idea to get a letter from the charity documenting each gift, Steffen said.

Source: Financial Advisor Magazine

Five Retirement-Planning Myths

Saving for the retirement you've been dreaming about is entirely possible. It begins with judicious saving and an awareness of potential obstacles you might encounter along the way.

If you've already crunched numbers on retirement, you're ahead of most. According to The Employee Benefit Research Institute's (EBRI) 2019 Retirement Confidence Survey, only 42% of working-age people have tried to calculate how much they'll need to save to live comfortably in retirement.

The survey also found that retirees are considerably more likely to say their expenses in retirement are higher than expected (30%) rather than lower (15%).

It's not hard to see why there's disconnect between expectations and reality: you have to make *a lot* of assumptions about your health, longevity and lifestyle in retirement. Below are five assumptions about retirement and the caveats that come with them.

Myth #1: You can always keep working.
The EBRI survey found that 80% of workers are planning to continue doing some kind of work for pay after they retire. It's true that people are living longer and are generally healthier these days, and many retirees find they want to continue working because they like it. But many of the survey's respondents also gave financial reasons: 75% said they'll continue working as a source of income in retirement.

The risk is that working in retirement isn't always possible. The survey found many retirees end up leaving the workforce earlier than planned—43% of the retired respondents in 2019 said they had retired unexpectedly. Sometimes, workers find they have enough money to retire early (33%).

More often, people have to stop working due to health problems (35%), company downsizing or workplace closures (35%, up from 26% in 2017). Retiring for any of these reasons could pose serious problems for those who don't have adequate savings.

Of course, some people continue to work into their 80s or even their 90s. But you're probably better off structuring your savings plans so that working in retirement is a matter of choice, not necessity.

Myth #2: You'll need only 70–80% of your pre-retirement income.
If you were saving 20–30% of your pre-retirement income, then the 70–80% income-replacement rule is a good place to start. Otherwise, this old rule of thumb may have outlived its usefulness. It may assume that retiring will free you from any work-related expenses and taxes, that you've paid off your mortgage and that your children will be financially independent.

However, even if these expenses go away, you should still prepare for other costs to go up. For instance, major health care expenses can be difficult to plan for. Medicare doesn't cover everything, and health care expenses that Medicare doesn't cover—such as long-term care—can add up quickly.

The bottom line is that it's safer to aim at covering 100% of your pre-retirement income, *less whatever you're saving for retirement*. As with any general rule, there are plenty of exceptions.

Myth #3: You'll be in a lower tax bracket once you retire.
Even before recent changes, marginal tax rates have been near post-WWII lows, and while it's possible, it's not a given that you'll move to a lower bracket in retirement. Even if they do, the change will likely be just a few percentage points rather than a major shift. For example, for 2019 a couple with a pre-retirement income of $157,500 would have to earn about 48% less to move from the 24% bracket to the 22% bracket and about 75% less to move to the 12% bracket.

Sure, your salary will be going away (as will FICA taxes), but you will still have income, such as distributions from retirement accounts and Social Security benefits. (For married couples filing jointly, up to 85% of your Social Security income may be taxable if your modified adjusted gross income is more than $44,000.)

You should remember that as recently as the 1980s, the top federal tax bracket was a whopping 70%. While tax rates aren't likely to return to that level anytime soon, it is possible rates could rise in the future. So if your taxable income remains the same in retirement as when you were working, higher rates in the future could boost your tax liability.

Unless you have a very high pre-retirement income, it's safer to assume that you will keep paying taxes at roughly the same rate after you stop working.

Myth #4: The stock market will save you.
The market declines of 2002 and 2008 should have convinced most people that this is not a reliable assumption, at least if you don't have time to potentially recover from a downturn. But with the market performing relatively well since, it's easy to forget that you may not see the kinds of returns going forward that you saw in the 30 years prior to 2000.

It's always better to be cautious when making assumptions about the market's performance and to have some cash and more stable investments in your portfolio to help you weather a bear market.

Whatever your risk tolerance and risk capacity, your retirement spending plan should consider a range of reasonable portfolio outcomes. Based on our capital market expectations, you could plan for five to seven percent returns for stocks and about three percent for bonds.

Market gains can help your savings go further in retirement, but they aren't a replacement for pre-retirement saving. Working with an advisor to complete or update a retirement plan can help.

Myth #5: There's always Social Security.
Some people head into retirement thinking they'll be able to rely on Social Security to cover most of their needs. Others doubt that Social Security will even exist by the time they retire. Both scenarios are highly unlikely. The Social Security Administration projects that the current system will be depleted by 2035 assuming no changes. One option would be to reduce benefits for future retirees or tax Social Security benefits at a higher rate.

Social Security is likely to be a valuable resource for many retirees, but don't get carried away. No matter what, Social Security is going to cover only a portion of your retirement spending, and you will need additional savings to bridge the gap.

The bottom line: Be flexible
All things considered, it's important to start with a plan, but be ready to adjust your plans when needed. Don't get into a situation where your retirement works only if one set of assumptions turns out to be true.

Stress-testing your plan and keeping these retirement myths in mind will go a long way toward putting you on the path to your ideal retirement.

Source: Schwab Highlights, 3Q 2018

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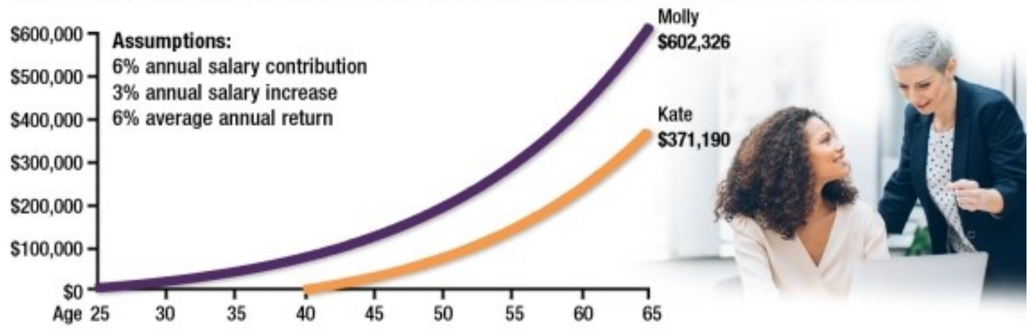
8700 W. Bryn Mawr Ave.
Suite 410-N
Chicago, Illinois 60631
773.714.1540 *Main*
773.714.1550 *Facsimile*
www.fsadvisorygroup.com

Why Not Do it Now? New Research on Procrastination

Do you have a tendency to push off important tasks? Do you do things at the last minute, or maybe not do them at all? If so, you're not alone. About one in five adults is a chronic procrastinator.[1]

Advantage of an Early Start

Molly begins saving at age 25 when she earns a $40,000 salary, and Kate begins at age 40 when she earns an $80,000 salary. At age 65, Molly's savings total would be more than 60% higher than Kate's total.



Procrastination can be frustrating in the short term for even the simplest tasks. But it can have far-reaching effects on important activities and decisions such as completing work projects, obtaining medical treatment, and saving for retirement. Recent research offers insights that may be helpful if you or someone you know has a tendency to procrastinate.

Blame the brain

A study using brain scans found that the amygdala, the almond-shaped structure in the temporal lobe of the brain that processes emotions (including fear), was larger in chronic procrastinators, and there were weaker connections between the amygdala and a part of the brain called the dorsal anterior cingulate cortex (DACC). The amygdala warns of potential dangers, and the DACC processes information from the amygdala and decides what action a body will take.[2]

According to the researchers, procrastinators may feel more anxiety about the potential negative effects of an action and be less able to filter out interfering emotions and distractions. The good news is that it is possible to shrink the amygdala and improve brain connectivity through mindfulness meditation exercises.[3]

What's important to you?

Another recent study found that people were less likely to procrastinate about tasks that they personally considered important and were within their own control, as opposed to tasks that were assigned to them and/or controlled by others. This is probably not surprising, but it suggests that procrastination may not be a "weakness" but rather a result of personal values and choices.[4]

Tips for procrastinators

Here are a few suggestions that may help overcome a tendency to procrastinate.

Consider the triggers

One researcher found that people are more likely to procrastinate if a task is characterized by one or more of these seven triggers: boring, frustrating, difficult, ambiguous, unstructured, not intrinsically rewarding, or lacking in personal meaning.[5] You might try to identify the triggers that are holding you back and take steps to address those specific problems. For example, if a task seems too difficult, ambiguous, or unstructured, you could break it down into smaller, more definite, and manageable tasks.

Meet your resistance

If you don't want to work on a task for an hour, determine how long you are willing to work on it. Can you work on it for 30 minutes? What about 15? If you don't want to do it today, what day would be better?

List the costs and benefits

For big projects, such as saving for retirement, make a list of all the negative ways not making progress could affect your life and all the positive outcomes if you were to achieve your objectives. Imagine yourself succeeding.

Take the plunge

Although a big project may seem daunting, getting a start — any start — could reduce the anxiety. This might be just a small first step: a list, a phone call, an email, or some Internet research. For a written project, you might start with a rough draft, knowing you can polish and improve it later.

Forgive yourself

If you've postponed a task, don't waste time feeling guilty. In most cases, "better late than never" really does apply!

[1] *Frontiers in Psychology,* July 5, 2018

[2-3] BBC News, August 26, 2018

[4] *Psychology Today,* January 9, 2018

[5] *Harvard Business Review,* October 4, 2017

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