

3Q20

The Financial Solutions Advisor

Inside this issue:

- Economic & Market Perspectives** 1
- State Population: Winners and Losers** 1
- Tapping Retirement Savings During a Financial Crisis** 2
- Top Performing Sectors Year-To-Date** 3
- Higher Income Now Entails Higher Risks** 3
- Managing Your Workplace Retirement Plans** 4

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

Stock prices have roared back strongly through the second quarter, as investors grew increasingly optimistic over prospects for economic reopening and the unprecedented monetary policy support that provided a strong tailwind for equities. At this point, however, stocks are looking somewhat richly valued and we think investors may be looking past some key risks. We think long-term prospects for stocks remain compelling, but markets may be in for prolonged volatility and a possible setback over the next few months.

The coronavirus pandemic and accompanying economic shut downs have undoubtedly caused a deep recession. Per the IMF, U.S. GDP will fall 8% and global GDP 5% in 2020. U.S. industrial production is 16% below its high, and the unemployment rate stands at 13% or 16% depending on how furloughed workers are counted.

The situation would clearly be worse were it not for extraordinary fiscal and monetary stimulus. The U.S. has increased federal spending by \$3 trillion since the pandemic began and there is expected to be another \$1 to \$1.5 trillion package before the end of summer. Governments around the world have also been pumping money into their economies.

At the same time, the Federal Reserve and other central banks have slashed rates to zero or below and allowed real rates to collapse. Forward guidance suggests rates will remain zero-bound through at least the end of 2022. Monetary policy, however, has already become about as accommodated as it can. Central banks are continuing to ease, but that easing is no longer accelerating.

The S&P 500 is less than 10% below its February all time high. At this point, we see several reasons for caution. The first is valuation. The 12 month forward PE ratio for the S&P 500 has climbed from a low of 13.4X on March 23 to 21.4X now, as investors have undoubtedly priced in an optimistic scenario for the next 18 months: no serious second virus wave, a strong recovery in corporate profits and near zero interest rates across the developed world. Such an acceleration is probably setting investors up for possible disappointments. Despite rising equity market volatility, stocks are not likely to retest their March lows because a return to that level of panic remains unlikely.

We are also concerned about political risks, which will likely heat up in coming months, and the deteriorating U.S. / China relationship and trade disputes

2020 Returns

S&P 500	-3.08%
NASDAQ	16.89%
Russell Small Cap	-12.98%
Russell Mid Cap	-9.13%
MSCI EAFE	-11.34%
MSCI World	-5.77%
Barclay US Agg. Bond	6.14%
Barclay Municipal Bond	2.08%

with Europe.

Additionally, the future path of the coronavirus itself remains a wild card. Investors are likely to continue to be rattled by news of new spikes and a slow down or reversal of reopening policies.

At this point, stocks appear to be fully valued, but difficult to fully value due to analysts not having clear views on earnings outlooks.

We expect stocks to continue trading in a trendless and volatile manner. Additional clarity on the political front, news of an affective treatment for the virus, and clearer views on earnings outlooks would all help stocks to breakout to the upside.

Non-U.S. stocks are expected to start outperforming U.S. stocks on a relative basis, due to better valuations, especially if we see continued weakness in the U.S. dollar.

Since the early 1980s, long-term inflation has been falling, providing a tailwind for the bond market. But inflation now appears to be bottoming, which spells trouble for Fixed Income markets. We expect stocks will outperform bonds over the coming years, but that will provide a little solace for equity investors if their returns are limited as well.

Source: Nuveen

State Population: Winners and Losers



The U.S. population was 328,239,523 in 2019, an increase of 0.5% over 2018. This was the fourth consecutive year of slowing population growth due to fewer births, more deaths, and lower immigration from other countries. Forty states gained population, while 10 states lost population. Here are the winners and losers based on percentage increase or decrease.

Source: U.S. Census Bureau, 2019

Tapping Retirement Savings During a Financial Crisis

As the number of COVID-19 cases began to skyrocket in March 2020, Congress passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The legislation may make it easier for Americans to access money in their retirement plans, temporarily waiving the 10% early-withdrawal penalty and increasing the amount they could borrow. Understanding these new guidelines and the other rules for loans and early withdrawals may help you determine if they are appropriate options during a financial crisis. (Remember that tapping retirement savings now could risk your financial situation in the future.)

Penalty-Free Withdrawals

The newest exception to the 10% early-withdrawal penalty allows IRA account

holders and retirement plan participants to take distributions of up to \$100,000 in 2020 for a "coronavirus-related" reason.* These situations include a diagnosis of COVID-19 for account owners and certain family members; a financial setback due to a quarantine, furlough, layoff, or reduced work hours, and in the case of business owners, due to closures or reduced hours; or an inability to work due to lack of child care as a result of the virus. This temporary exception augments the other circumstances for which a penalty-free distribution is typically allowed:

- Death / disability of the account owner
- Unreimbursed medical expenses exceeding 7.5% of adjusted gross income (increases to 10% in 2021)

- A series of "substantially equal periodic payments" over your life expectancy or the joint life expectancy of you and your spouse
- Birth or adoption of a child, up to \$5,000 per account owner
- Certain cases when military reservists are called to active duty

In addition, IRAs (but not work-based plans) allow penalty-free withdrawals for a first-time home purchase (\$10,000 lifetime limit), qualified higher-education expenses, and payments of health insurance premiums in the event of a layoff.

Here are the five industries most likely to offer Retirement Plan loans:



Work-based plans allow exceptions for those who separate from service after age 55 (50 in the case of qualified public safety employees) and distributions as part of a qualified domestic relations order.

Tax Consequences

Penalty-free does not mean tax-free, however. In most cases, when you take a penalty-free distribution, you must report the full amount of the distribution on your income tax return for that year. However, the income associated with a coronavirus-related distribution can be spread over three years for tax purposes, with up to three years to reinvest the money.¹

Retirement Plan Loans

If your work-based retirement plan allows loans, you typically can borrow up to the lesser of 50% of your vested balance or \$50,000. Most loans must be repaid within five years, but if the money is used to purchase a primary residence, the repay-

ment period may be longer. The CARES Act permits employers to increase this amount to the lesser of 100% of the vested balance or \$100,000 for loans to coronavirus-affected individuals made between March 27, 2020, and September 22, 2020.*



Affected participants who have outstanding loans on or after March 27, 2020, will be able to delay any payments due in 2020 by one year.²

Hardship Withdrawals

Many work-based retirement plans also permit hardship withdrawals in certain

circumstances. Although these distributions are not exempt from the 10% early-withdrawal penalty, they can be a lifeline for people who need money in an emergency.

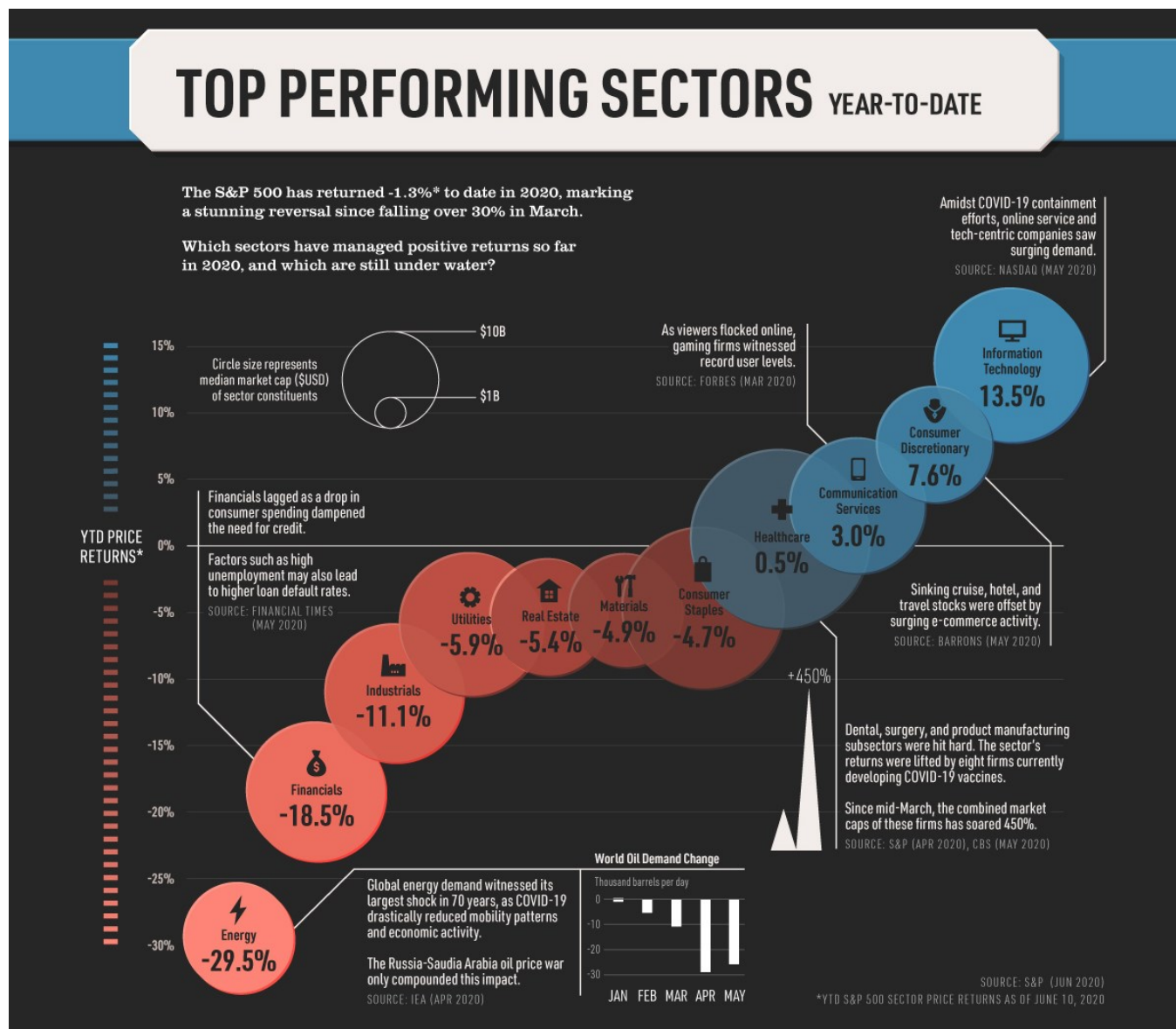
For more information about your options, contact your IRA or retirement plan administrator.

**Employers do not have to adopt the new withdrawal and loan provisions.*

- 1) *Amounts reinvested may reduce your tax obligation on the distributions; however, due to the timing of distributions and required tax filings, you may have to file an amended return to seek a refund on any taxes previously paid on withdrawn amounts.*
- 2) *The original five-year repayment period will be extended for the delay, but interest will continue to accrue.*

Source: Plan Sponsor Council of America, 2019 (2018 data)

Top Performing Sectors Year-To-Date



Higher Income Now Entails Higher Risks



Data Source: Bloomberg, LP
21-Mar-1997 and 31-Mar-2020

Representative Indexes:

1-3 Year US Treasury:
S&P US Treasury Bond 1-3 Year

7-10 Year US Treasury:
S&P US Treasury Bond 7-10 Year

Core US Fixed Income:
Barclays US Aggregate Bond Index

Corporate High Yield:
Barclay's Corporate High Yield 2% Issuer Capped Index

US Equity:
S&P 500 Index

Past performance is no guarantee of future results

Managing Your Workplace Retirement Plans

About 80 million Americans actively participate in employer-sponsored defined contribution plans such as 401(k), 403(b), and 457(b) plans.¹ If you are among this group, you've taken a big step on the road to retirement, but as with any investment, it's important that you understand your plan and what it can do for you. Here are a few ways to make the most of this workplace benefit.

Take the free money. Many companies match a percentage of employee contributions, so at a minimum you may want to save enough to receive a full company match and any available profit sharing. Some workplace plans have a vesting policy, requiring that workers be employed by the company for a certain period of time before they can keep the matching funds. Even if you meet the basic vesting period, funds contributed by your employer during a given year might not be vested unless you work until the end of that year. Be sure you understand these rules if you decide to leave your current employer.

Reasons to Contribute

Percentage of households with assets in defined contribution plans who agreed with the following statements:

Bump up your contributions.

Saving at least 10% to 15% of your salary for retirement (including any matching funds) is a typical guideline, but your personal target could be more or less depending on your income and expenses. A traditional employer-sponsored plan lets you defer income taxes on the money you save for retirement, which could enable you to save more. In 2020, the maximum employee contribution to a 401(k), 403(b), or 457(b) plan is \$19,500 (\$26,000 for those age 50 and older).² Some plans offer an automatic escalation feature that increases contributions by 1% each year, up to a certain percentage.



Payroll deduction makes it easier for me to save
92%



My employer-sponsored retirement plan helps me think about the long term, not just my current needs
91%



My employer-sponsored retirement plan offers me a good lineup of investment options
83%



The tax treatment of my retirement plan is a big incentive to contribute
82%

Rebalance periodically. Your asset allocation — the percentage of your portfolio dedicated to certain types of investments — should generally be based on your risk tolerance and your planned retirement timeline. But the allocation of your investments can drift over time due to market performance. Rebalancing (selling some investments to buy others) returns a portfolio to its original risk profile and does not incur a tax liability when done inside a retirement plan. Consider reviewing your portfolio at least annually. Some workplace plans offer automatic rebalancing.

Know your investments. Examine your investment options and choose according to your personal situation and preferences; some employer-sponsored plans may automatically set up new employees in default investments. Many plans have a limited number of options that may not suit all of your needs and objectives, so you might want to invest additional funds outside of your workplace plan. If you do, consider the risk and overall balance of your portfolio, including investments inside and outside your plan.

Keep your portfolio working. Some employer plans allow you to borrow from your account. It is generally not wise to use this option, but if you must do so, try to pay back your loan as soon as possible in order to give your investments the potential to grow. Plans typically have a five-year maximum repayment period.

All investments are subject to market fluctuation, risk, and loss of principal. When sold, investments may be worth more or less than their original cost. Asset allocation is a method used to help manage investment risk; it does not guarantee a profit or protect against investment loss. Distributions from employer-sponsored retirement plans are generally taxed as ordinary income. Withdrawals prior to age 59½ may be subject to a 10% federal income tax penalty.

1) American Benefits Council, 2019

2) Employer contributions are not included in these annual employee limits for 401(k) and 403(b) plans. Employers typically do not contribute to 457(b) plans, but any such contributions will count toward the employee limit. There may be additional catch-up contribution opportunities for 403(b) and 457(b) plans.

At Financial Solutions you'll find a fee-only Registered Investment Advisor (RIA) committed to putting your interests and your needs first, eliminating the commissions and self-serving incentives that get in the way of solid, successful financial planning and investment management.

Please contact us if you would like to receive this publication by e-mail.

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