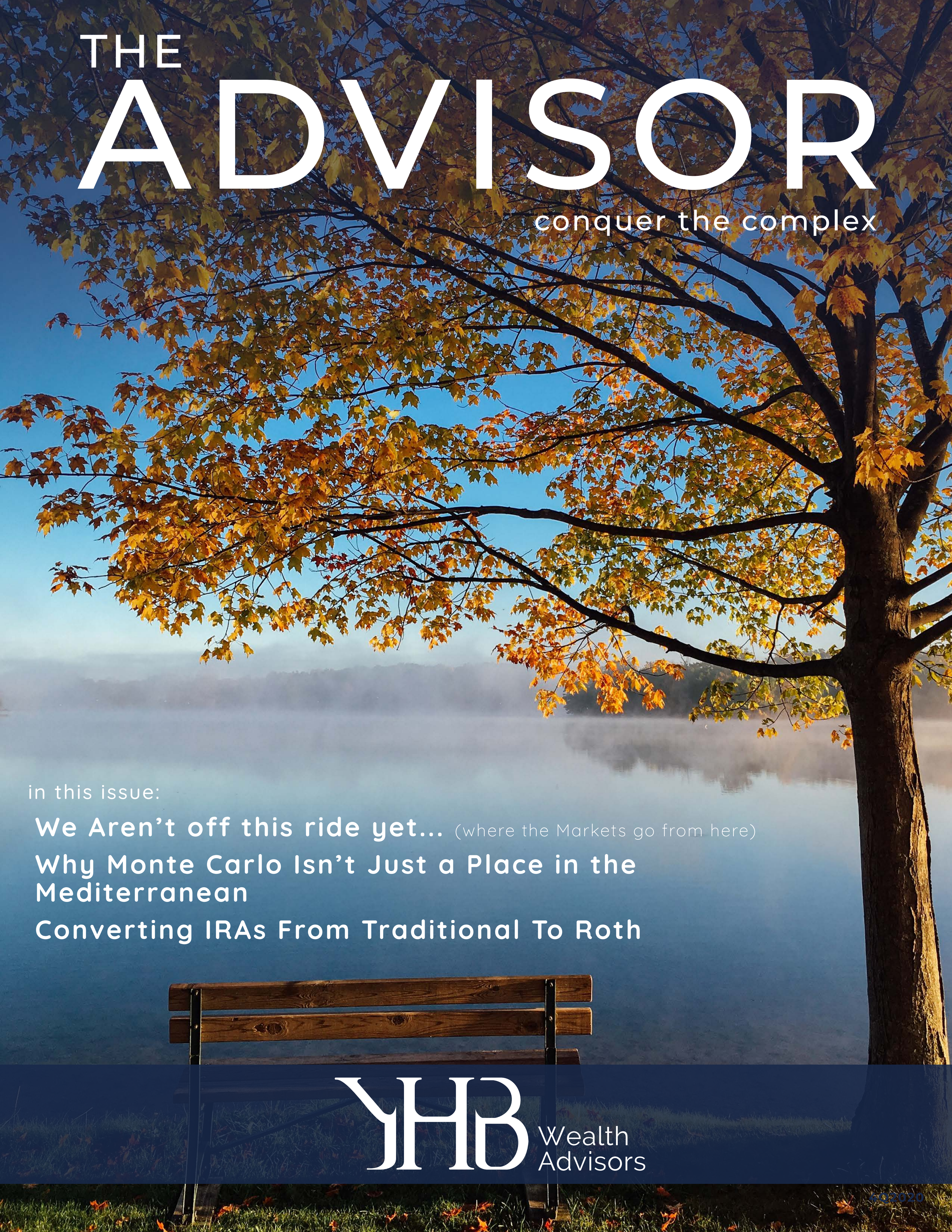


THE

ADVISOR

conquer the complex

in this issue:

KHB Wealth Advisors

4Q2020

Year End Financial Planning Tips

Developing a plan and sticking to it is a crucial step toward a sound financial future. Here are a few tips to make sure you stay on track.

October

- If you filed an extension in April, your tax return is due by October 15th.
- Typically October starts open enrollment season for those eligible for Medicare Part D prescription drug coverage or Advantage Plans. Be sure to review any changes to your private company health plans and determine if there are advantages to using an HAS or PSA (if available from your employer).
- It's also time to grab that final free credit report.

November

- Review you budget for the upcoming holidays. It's easy to blow your whole plan by over spending at year end.
- Review your charitable giving program and decide if there is room for more.
- Review any pre-tax flexible spending accounts against actual expense and determine if you need to make adjustments for the next year.

December

- Time to review your budget versus actual income and expenses. Track where spending didn't match your estimates and determine if you just over spent, or under estimated so your plan for the following year will be more accurate.
- This is the last month you can make changes to your investment portfolio that will have any impact on your tax situation. Review your portfolio with your investment manager and decide if taking tax losses makes sense.

January

- Get your important documents and records organized for the coming year. Time to clean out current files to make room for this year's new additions, and move the older files to storage boxes for safe keeping.
- Update your Net Worth Statement and put the final touches to your budget and cash flow planning for the New Year. Make a final review of your budget from the previous year and grade your performance against the plan.
- Double check your employer retirement plan to ensure you are contributing enough to get the full employer match.
- Make sure you have an emergency fund in place (typically six months of income), and if it's less than it should be, earmark additional savings to this reserve.

Converting IRAs From Traditional To Roth

Converting your traditional IRA funds into a Roth IRA could have significant tax benefits to yourself and your family members, if planned correctly. Thanks to the Tax Cuts and Jobs Act (TCJA), there is an opportunity to take advantage of historically low tax rates before the rates are scheduled to reset to the previous levels by the end of 2025.

The basic concept behind Roth IRAs is that, generally, the income and gains generated in the Roth account, as well as distributions to the owner, are tax-exempt. In addition, the account owners are not subject to required minimum distributions (RMDs) during their lifetime. There are RMDs for non-spouse beneficiaries of the Roth IRA once the original account owner passes away, but those RMDs are still tax-exempt to the beneficiary.

The primary benefit of a Roth conversion is the ability to manage your taxable income and keep as much of the converted funds in the lowest possible tax bracket at the time of the conversion. The TCJA revised the tax brackets to be much more taxpayer friendly compared to the old law, resulting in taxpayers generally having more income taxed in lower brackets.

For example, under the current law, a married couple filing jointly can have taxable income up to $315,000 and be subject to an upper tax bracket of 24%. Whereas under the prior law, if the married couple had taxable income of $315,000, they would have been subject to an upper tax bracket of 33%. As noted before, these tax brackets are scheduled to sunset after tax year 2025, so it is important to keep that in mind when reviewing your current tax rates versus your expected future tax rates.

Managing taxable income can be a difficult task if your income is inconsistent from year-to-year and is dependent on factors outside of your control. One way to make the task easier is to review your charitable giving goals in conjunction with the Roth conversion planning.

Assuming you take itemized deductions, pairing income from the Roth conversion with a larger charitable deduction in the same tax year might be a good strategy to consider. Depending on your charitable goals and the nature of your investments, utilizing a donor-advised fund could be another possible strategy to review.

Beyond the tax bracket discussion, there are some other considerations to take into account in order to maximize the benefits of Roth conversion, including:

1) Your current tax rates vs. your expected future rates
2) The ability to pay the additional tax liability generated by the Roth conversion with non-IRA funds
3) Understanding your current and future living expenses, so that the converted funds can remain untouched as much as possible
4) Your time horizon for retirement and remaining life expectancy

Remember, the overarching goal of a Roth conversion is to get as much money into the Roth account at the lowest possible tax bracket. This allows the converted funds to grow tax-free for as long as possible. Therefore, it is important to consider if your overall financial situation will allow you to set aside funds in a Roth and leave them enough time to realize a worthwhile return on the investment.

Roth conversions can potentially be a very powerful tool to shift income from taxable to tax-exempt. There are many different factors to review when considering this strategy, however, and it may not make sense in all situations. It is important to plan carefully and have a discussion with your tax advisor before executing this strategy so that you can maximize the benefits for yourself, your spouse, and your future beneficiaries.

Alex Fleming, CPA

WE AREN'T OFF THIS RIDE YET...

"Don't follow the crowd, because nobody goes there anymore. It's too crowded." – Yogi Berra

Equity investors have been on quite a roller-coaster ride this year. After hitting an all-time high in February, the S&P 500 Index plunged a gut-wrenching 34% over the next month, marking the quickest bear market in U.S. history. Smaller company stocks did even worse during that period, losing more than 40%. Thankfully, because our client portfolios were not fully invested in equities prior to the decline, our average client account did not experience the full brunt of the volatility. However, the flip side of that conservative allocation means we also didn't experience the equally surprising and gravity-defying upturn. From the March low, the market roared back to make a new high in September. Talk about whiplash.

However, there is a major bifurcation beneath the surface. The tech heavy Russell 1000 Growth Index is up 15% on the year, but its more conservative Value sibling is down 14%. That's a stunning 29-percentage-point difference and ranks as one of the widest variations in style returns ever. Historically, wide variations in style differences have been resolved by reversion to the mean over time. If it holds true in this case, either Growth will see future weakness, or Value will strengthen, or some combination of the two.

We don't rule out the possibility U.S. stocks could revisit their March lows (2,237 on the S&P 500) and if it appears that possibility becomes likely, we would be ready to adjust portfolios as necessary to ensure their long term stability. In the meantime, we like how our portfolios are positioned with attractive medium- to longer-term return opportunities, balanced with shorter term income protections.

WHERE DO WE GO FROM HERE?

THE PRESIDENTIAL ELECTION COULD CAUSE INCREASED VOLATILITY

Between now and year end, there is a risk of increased volatility from the uncertain outcome of the Presidential election. At present, it appears from polling the race is becoming more closely contested. All indications point to a much larger than usual mail in vote as a result of virus concerns, and the biggest risk to the market is a very drawn out and contentious vote count that leads to a narrow victory by either party. That outcome could instigate a legal battle that might even extend into the New Year. The investment markets can thrive under either political party, and actually perform best with a split government of checks and balances, but will react negatively to extended uncertainty.

COVID-19 IS THE MOST IMPORTANT VARIABLE EXTENDING INTO 2021

As always, we see a range of potential economic and financial market outcomes looking ahead over the next six to 12 months and beyond. What is unique about the current environment is how dependent the outcomes are on the course of COVID-19. Significant uncertainty remains as to the virus's progression, even as economies around the globe have begun varying phases of reopening and relaxing social distancing standards. The timing, availability and effectiveness of treatments and vaccines are also highly uncertain but crucial variables for the economic outlook.

In our view, the key risk to the economy and financial markets is the potential for a widespread second wave of COVID-19 infections, hospitalizations, and deaths that force another large-scale economic shutdown. In that event, stocks could re-test their March lows. But absent a severe second wave (or some other major exogenous shock), and even assuming there are smaller localized outbreaks, we think an uneven but steadfast economic recovery is the most likely scenario looking out over the next six to 12 months at least.

MONETARY & FISCAL POLICY ARE ALSO KEY

While we view the progression of COVID-19 as the most important driver of the 6 to 12 month economic and market outlook, monetary and fiscal policy are second-most in importance. And, in the policy sphere, the Fed is key.

After the Federal Open Market Committee (FOMC) meeting in September, Fed chair Jerome Powell made it very clear the Fed intends to keep monetary policy extremely accommodative at least until 2023. Powell said, "We are not thinking about raising rates. We are not even thinking about thinking about raising rates."

In order to achieve that accommodative policy however, global central bank balance sheets, in aggregate, have increased to a record 38% of global GDP. The Fed's balance sheet stands at a record 33% of U.S. GDP and climbing. Similarly, the European Central Bank stands at 44% of GDP and the Bank of Japan's balance sheet sits at a whopping 118% of Japan's GDP.

GIVEN ALL THIS STIMULUS, IS INFLATION A RISK? NOT NOW, PROBABLY LATER

We do not view wide ranging inflation as a near-term risk because there is too much slack in the economy due to the demand shock from COVID-19. It will take a while—likely a few years at least—for the economy to get back to operating at full capacity and full employment. While there is evidence of inflated prices in certain portions of the supply chain (a single 2x4 costs $6 today for example), the slack should restrain consumer price inflation and wage inflation.

As we saw in the aftermath of the 2008 financial crisis, the Fed's liquidity largesse showed up in price appreciation for financial assets, rather than in price inflation in the real economy. We see this as likely to replay again.

However, there is a strong risk these policies will translate into inflation if they remain extremely loose after the economy reaches full capacity and full employment. The Fed is signaling it won't act preemptively to curb inflation in this cycle and has even stated its outright intention to let the inflation rate "run a little hot" if necessary to ensure economic recovery.

The Fed is also apparently content to effectively monetize the debt created by government deficit spending. If the Fed continues these policies beyond the COVID-19 crisis, it runs the risk of falling behind the inflation curve. This could lead to an inflationary surprise and a sharp repricing of assets. We will be watching closely for evidence of inflation as this cycle unfolds and we have added inflation protection to most client portfolios in the form of Treasury Inflation protected Securities and gold.

SO WHERE DOES THIS LEAVE US?

We hold a cautiously optimistic view that even with an inevitable uptick in COVID-19 cases in coming months, the overall social policy response won't need to be as draconian, and therefore the economic impact won't be as bad as during this first wave. If the latter public health scenario plays out against a backdrop of extremely loose fiscal and monetary policy, there is a good chance we'll get a sustainable, albeit uneven, global economic recovery.

If so, corporate earnings are likely to rebound as well. Measured against very low interest rates—and with fears of severe recession (or worse) off the table thanks to the policy response—this would support the view that equities and fixed-income credit sectors are attractive compared to short term cash.

We would also not be surprised to see a continued reopening of global economies, and increased earnings growth spur value/cyclical stocks to take the leadership reigns from growth stocks, potentially marking a new cycle of relative performance in favor of value. Our portfolios would benefit from this change in leadership.

As always, it is important to be invested in a portfolio aligned with your risk tolerance and financial goals. Please don't hesitate to reach out to our team to update your financial plan or discuss your individual portfolio at any time.

RANDY BEEMAN

Jamie Brothers

Jamie leads YHB Wealth Advisors' Client Services. She has over 20 years' experience in the wealth management and finance industry.

Jamie handles daily client service interactions including opening new accounts, processing the transfer of assets between custodial firms, submitting requests for disbursement of funds, working with compliance staff, and handling all client service inquiries.

Jamie serves as a Notary Public for verification of YHB Wealth client identity and signatures when required.

jamie.brothers@YHBwealth.com
540.545.8702

Randy Beeman

Randy serves as the Director of YHB Wealth Advisors, overseeing client asset management as well as strategic direction of the firm. He has more than 15 years of experience managing financial assets for individuals, retirement plans and businesses.

Randy works with you to develop a personal investment policy statement that leverages your financial plan to produce a portfolio allocation that meets your goals. Randy's disciplined investing focused strategy insures you have a long-term plan to be confident in.

He is also the host of the monthly Podcast "Let's Talk Investing".

randy.beeman@YHBwealth.com
540.545.8702

JT Trimble

JT Trimble, CFP®, serves as YHB Wealth Advisors' Client Account Manager. Prior to joining YHB, JT worked with Charles Schwab & Co., Inc. as a Financial Services Representative for high net worth clients.

JT works with clients to develop and update their personalized financial plan, which includes initial and annual meetings. JT starts the process with a comprehensive evaluation of your current and future financial state so you can be confident you will meet your financial goals and objectives.

jt.trimble@YHBwealth.com
703.840.0702

Why Monte Carlo Isn't Just a Place in the Mediterranean

We have all seen the allure. All of those yachts and mega yachts docked in the cove, the Indy car races in the street and especially the James Bond-esque scenes at the casino tables. Who wouldn't want to spend any amount of time in Monte Carlo?! I thankfully get to spend an exceptional amount of time in Monte Carlo. However, mine is a financial planning analysis tool, not the elegant hillside oasis, on the coast of the Mediterranean in Monaco. If I am being honest, Monaco sounds like a great reprieve from all that 2020 has brought us thus far and may still yet bring. Yet my goal here is to show you how the financial planning tool is more relevant and encouraging to you than the coastal resort could ever be.

Investopedia provides a rather academic definition of the Monte Carlo Simulation, "Monte Carlo simulations are used to model the probability of different outcomes in a process that cannot easily be predicted due to the intervention of random variables. It is a technique used to understand the impact of risk and uncertainty in prediction and forecasting models." Before the thought is solicited to your mind that this is far too academic, allow me to simplify: Monte Carlo analysis is used to analyze different investment returns, over time, to estimate confidence in maintaining a given amount of cash flow. The stock market is highly unpredictable. Nobody knows what direction the market, or individual stock prices, will run over time. We may certainly make educated evaluations and perform calculated analyses, but we don't definitively know. That is why when we create a given asset allocation, based upon your risk tolerance, we run the Monte Carlo analysis to see what happens when, not if, investment returns vary over time.

So, this brings us to 2020 where COVID-19 wreaked havoc upon the investment markets, brought uncertainty to employers and employees, multiple hurricanes, forest fires, and to top it off is the political turmoil of it being an election year. This much uncertainty without question impacts investment markets. Yet our use of Monte Carlo analysis should provide some confidence in the decisions we make about our financial lives.

This is where the value of Monte Carlo analysis should bring confidence to your financial life as you encounter the uncertainty regardless of the year or form. The higher the confidence, the smaller the impact a market correction should have on your financial life. This is why it is important to continually update your financial plan, as opposed to simply creating one financial plan and leaving it alone. Our lives change and it is possible for them to change in an instant. The value in any financial plan is in continually updating it year over year so that we are increasing our confidence in being able to live the life we want to live, as we live it, regardless of what happens in the world around us. This isn't to say that we won't ever pivot or make adjustments to the plan. Certainly, we will. We may want to make these adjustments, or they may be necessary. We may need to delay retirement. We may need, or be able, to accelerate retirement. These are decisions that I believe we need more data to filter through rather than relying on our emotions. The data is probably less likely to change as quickly as my emotions will. So, while I clearly need to understand how I feel when processing certain decisions, I definitively need to seek more information by which to process what pivots and adjustments are needed.

While no model can perfectly forecast the market, the Monte Carlo analysis is one key aspect of our financial plan that enables us to sleep well at night knowing that we have a plan that is working for us. Not only is it working for us but it gives us the flexibility to react and adjust to whatever 2020, or any other year, throws at us. We want you to be confident not just in how your money is invested but in how your financial life is situated. We would much rather be vaguely right than exactly wrong. The higher our confidence the more right we will eventually be. So while it would be enjoyable to eventually end up on the coast of Monaco at some point, it is more enjoyable to live our lives with the peace of mind the Monte Carlo analysis provides.

JT TRIMBLE

YHB Wealth Advisors

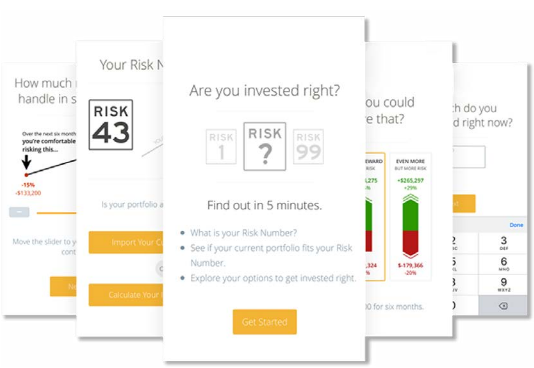
50 S. Cameron St.
Winchester, VA 22601

RANDY BEEMAN
randy.beeman@YHBwealth.com
540.545.8702

JT TRIMBLE, CFP®
jt.trimble@YHBwealth.com
703.840.0702

JAMIE BROTHERS
jamie.brothers@YHBwealth.com
540.545.8702

What is your Risk Tolerance?



Riskalyze helps you understand your risk tolerance and align your investment strategy to provide you peace of mind. As a friend of YHB Wealth you complimentary access to a Risk Number-centric view of your wealth.

This complimentary survey explains your risk score, while also providing:

- Perspective on aligning your portfolio allocation to match your personal preferences and priorities
- A comfort zone of how you should expect a portfolio to perform based upon your risk score
- The opportunity to discuss the results with a qualified YHB Wealth Advisor

Get Your Score at YHBcpa.com/riskalyze