THE STRATEGIST

FALL 2018

Are you RECESSION READY?

Seventy five percent of private sector economists recently polled by the Wall Street Journal expect the US economy to recess within the next two years. But… Don't Panic! Recessions act like rejuvenating economic detoxes that, while painful in the short run, create much healthier systems in the long run. The amount of short run pain the economy endures depends on the level of toxins within the system. The 2007 economy required a near fatal cleanse while the 2002 economy only needed some rest. Our current economic advance may have grown old, but it hasn't grown particularly excessive. Bubbles exist in Cryptos, cannabis, private equity and private debt, but none of these asset classes alone hold a 2007-esque systematic threat. Therefore, a normal garden variety recession awaits us. Question is, what are you going to do about it?

For individual investors, proper financial planning should produce a personalized asset allocation blueprint drawn to weather cyclical storms. Often, however, asset allocations can drift and/or margin lines expand after long expansions. To prepare for the coming recession, rebalance your asset allocations and pay down your investment credit lines.

For holders of illiquid assets like closely held businesses or speculative real estate, a seller's market can quickly become a buyer's market. Transaction multiples have reached record highs given the bubbles in private equity and private debt, making now as good as it gets for peddlers. Passing on today's buyout multiples means waiting for the return of near perfect conditions… and that could be a while. To prepare for the coming recession, consider selling closely held businesses and real estate you don't want to own for the next decade.

For business owners, you should "war game" out a budget that contemplates a 20% revenue reduction. Inevitably this will lead you to lighten inventories, shorten your receivables, delay big ticket purchases, delay payroll additions, and refrain from entering into burdensome long-term contracts. Additionally, pro-actively parting with misfit staff in a robust job market provides greater re-employment opportunities for them and dry powder for you to use in pursuit of potential stars mid-recession. Most importantly, while you can, **RAISE YOUR PRICES**. This will enable you to offer discounts during the recession to steal market share and provide more margin to spend on advertising and communications while your competition recoils. Lastly, if you have an interest in acquisitions, having financial wherewithal while others don't makes you winsome and equipped. To prepare for the coming recession, business owners need to boost profit margins and then spend wisely when property, people and equipment go on sale.

Recessions happen. The pain you endure depends upon your willingness to prepare. **The Chinese use two symbols to represent crisis, danger and opportunity.** Which definition will define you?

To prepare for the coming recession, business owners need to boost profit margins and then spend wisely when property, people and equipment go on sale.

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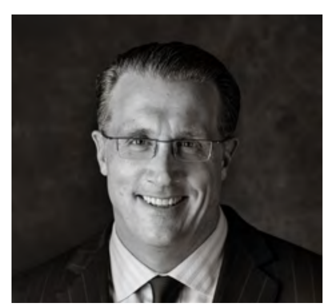
David Waddell, CFP®
PRESIDENT & CEO
Chief Investment Strategist



LETTERS *and* NUMBERS *for* Kids

ESA – *Education Savings Account, aka Coverdell Savings Account*
After tax contributions, tax free growth with qualified withdrawals, goes to the child at age 30 if not used for education, flexible investments

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CAN BE USED FOR ELEMENTARY SCHOOL, HIGH SCHOOL AND COLLEGE QUALIFIED EDUCATION EXPENSES, TAX CONSEQUENCES IF FUNDS USED FOR OTHER PURPOSES

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CONTRIBUTIONS FROM ALL SOURCES LIMITED TO $2,000 PER YEAR

529 – *College Savings Plan* | After tax contributions, tax free growth with qualified withdrawals, goes back to the owner if not used for education, limited investments

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PRIOR TO RECENT TAX CUT, WAS ONLY ELIGIBLE FOR COLLEGE EXPENSES. NOW AVAILABLE FOR QUALIFIED EXPENSES FOR ELEMENTARY SCHOOL, HIGH SCHOOL AND COLLEGE, TAX CONSEQUENCES IF FUNDS USED FOR OTHER PURPOSES

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CONTRIBUTIONS LIMITED BY STATE BUT ARE VERY GENEROUS

UGMA/UTMA – *Uniform Gift to Minors Act or Uniform Transfer to Minors Act Accounts* | After tax contributions, irrevocable gift to the minor, transactional income taxed yearly, child receives all assets at age of majority in state of residence, flexible investments

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CAN BE USED FOR ANY EXPENSES FOR THE CHILD, NOT JUST EDUCATION

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NO LIMIT ON CONTRIBUTIONS, BUT COULD BE SUBJECT TO GIFT TAX

EE AND I – *U.S. Savings bonds, Series EE and I* | After tax purchase, guaranteed interest, taxation either yearly or at maturity/sale, very low interest but considered safest investment

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CAN BE USED FOR ANY EXPENSES FOR THE CHILD

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$10,000 PURCHASE LIMIT PER CHILD PER YEAR

All contribution limits are as of October 2018 and are subject to change.

Kathy Williams, CFP®, CDFA®
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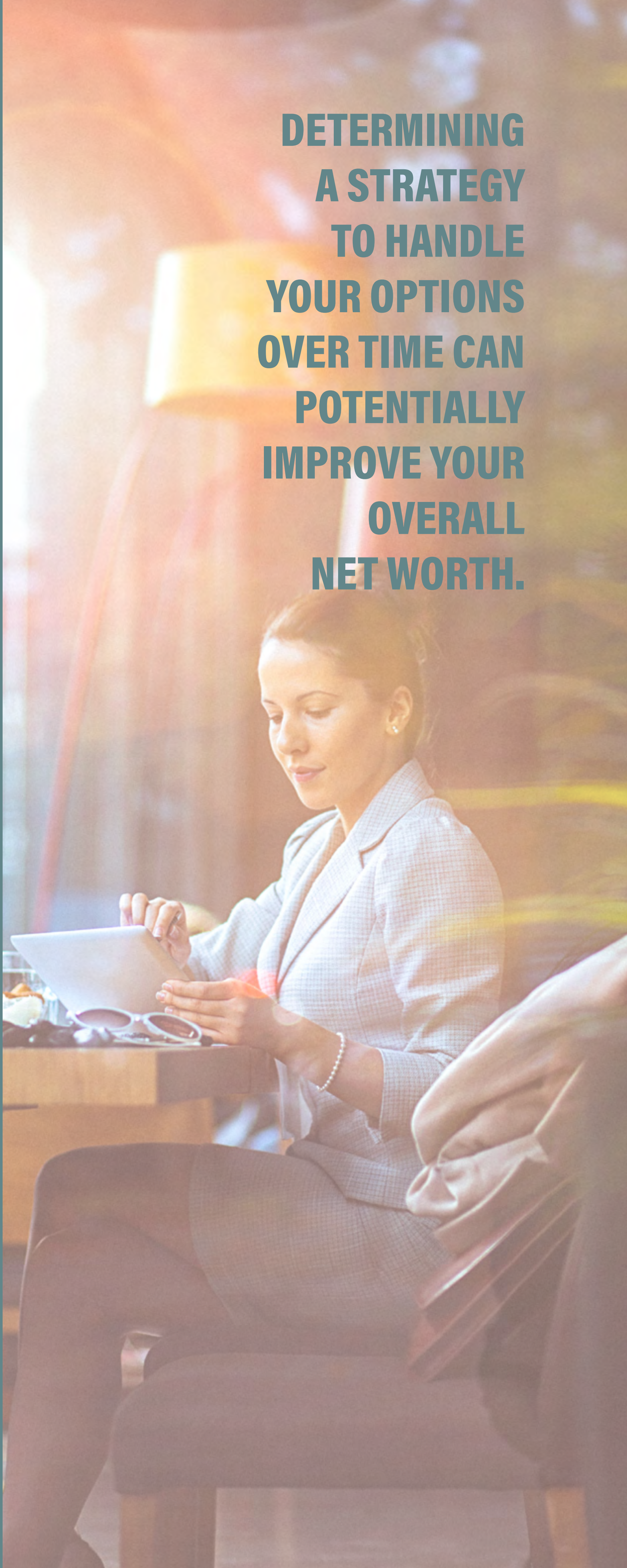
Senior Wealth Strategist
NATIONAL SOCIAL SECURITY ADVISOR
CERTIFICATE HOLDER



ARE YOU MAKING THE RIGHT DECISIONS WITH YOUR STOCK OPTIONS?

Stock options are a common form of compensation given to attract and retain quality employees. Receiving company equity can provide a great opportunity to accumulate wealth. In reviewing your overall financial plan, it's important to frequently analyze and set goals with your stock options. Determining a strategy to handle your options over time can greatly improve your overall net worth. *Let's review several important things to consider before taking action:*

UNDERSTANDING THE BASICS Stock options give you the right to buy a specific number of your company's shares during a specified time period (vesting schedule) and price (grant price) set by your employer. Each grant will have an expiration date at which point you can no longer exercise the options and they become worthless. The grant price will coincide with the price of the company stock at the time of the grant. The hope is that the stock will increase in value, allowing you to purchase shares at the grant price and sell at the appreciated price (in the money). Of course, the value of the stock can decrease in value (out of the money), at which point it would make more sense to purchase the shares in the open market at the lower price and let the devalued options expire.

THERE ARE TWO TYPES OF EMPLOYEE STOCK OPTIONS: NON-QUALIFIED STOCK OPTION **(NSO)** OR INCENTIVE STOCK OPTION **(ISO)**. IT IS IMPORTANT TO KNOW THE TYPE YOU RECEIVE SO YOU CAN WORK THE TAX CONSEQUENCES INTO YOUR FINANCIAL PLAN.

NSO - Ordinary income tax is recognized when exercising based on the excess (if any) of the fair market value of the stock on the date of exercise over the grant price.

ISO - No federal income tax is recognized when exercising if you hold the shares for more than one year after exercise and at least two years after the grant date. Under these circumstances, any gain or loss on the sale will be taxed at long-term capital gains rates.

Stock options typically generate ordinary taxable income when exercised because they are NSOs or they are ISOs that are sold immediately. The cashless transaction is the most common method for exercising options, which involves immediately exercising and selling some of your shares to pay for the stock and possible taxes. How many shares you will need to sell depends on the grant price and the current price of the stock.

PLANNING STRATEGIES When your options vest and are in the money (share's grant price is below current market price), should you exercise them immediately and take the gain or hold them longer for possible higher profits? There are several important factors to consider when determining the best strategy.

TIMING ISSUES

The expiration date of your stock options is one of the most important events to monitor. As the expiration date approaches, your planning strategies are significantly limited. If you wait too long and your stock declines in value before you exercise, you may lose a portion (or all) of the options value, and this becomes even more critical as we approach year ten of this current bull market. Several years before expiration, it makes sense to consider implementing a staggered selling strategy.

If you leave your company for a new job, you are terminated or you (happily) retire, you will typically have no more than 90 days to exercise your option grants. To gain an understanding of your specific grant's complexities, it's important to review the plan document and grant agreement with your advisor.

FINANCIAL GOALS

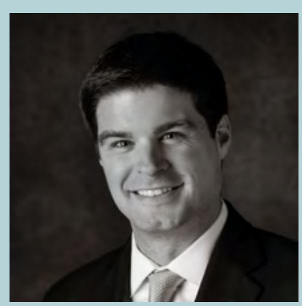
Defining and prioritizing your financial goals will help determine the best use of this asset. Do you need the proceeds to pay for a child's education or a wedding in five years? Are the options a key part to your retirement portfolio? Selling immediately and using the proceeds for a beneficial alternative (paying down high interest debt) could make more sense than relying heavily on the performance of your company's stock.

CONCENTRATION RISK

If your company's stock makes up more than 10 to 15 percent of your overall assets, a significant downturn in the stock could be detrimental to your financial plan. Diversifying a portion of your concentrated stock options could significantly reduce this risk. It's also important to factor in future vesting events.

If concentration risk is not a factor, the proceeds aren't needed immediately, and you have confidence in the prospects of your company's stock price, you may not want to immediately exercise the options. You can potentially experience the upside leverage without a cash investment, and the spread between your grant price and the rising stock price grows without taxation. You should closely monitor the current company and market environment as the expiration date approaches to determine the best strategy.

It's important to design and systematically revisit a specific plan for each grant on your balance sheet in order to take full advantage of this incentive. Details matter in the world of stock options. Make sure your strategy reflects your needs and takes into account every detail.



Sean Gould, CPA/PFS, CFP®
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The Cost of **OPPORTUNITY**

Teresa Bailey, CFP®, CDFA®
Wealth & Development Strategist

ECON WHIZZES often discuss "opportunity cost" in relation to consumer choices. For example, when you stand in the grocery store and make up your mind to go with the jar of chunky peanut butter instead of the smooth peanut butter, your opportunity cost is forgoing ownership of the jar of smooth peanut butter - and missing out on the experience of a creamy PB&J sandwich that afternoon.

INVESTMENT WHIZZES often discuss opportunity cost in relationship to choices made with investing capital. For example, when you decide to leave cash in your non-interest bearing checking account instead of moving it over to your interest bearing savings account, your opportunity cost of the decision is the interest you could have earned if the funds were in the savings account. Also the use of that interest, and so on.

Finally, **FINANCIAL PLANNING** and **WEALTH MANAGEMENT** WHIZZES discuss opportunity cost across an entire family's financial future. For example, if you decide to forgo retirement savings and instead find ways each year to spend that income on the "NOW" you, "FUTURE" you in retirement will suffer the opportunity cost of not having supplemental income from the forgone retirement investments. The entire family is often impacted by these decisions, so as you can imagine, it's a pretty intense focus for the industry and for consumers.

The conversation that I believe is the most important, especially for high-drive, ambitious individuals, is the intangible cost of each opportunity taken, not missed. We'll all very quickly jump to calculate the mathematical impact of that awesome promotion on your balance sheet now, and the balance sheet of twenty-years-from-now future you. But what about the impact of the stress of that new role? What about the loss of freedom as you climb the ladder? Sleepless nights? Travel fatigue? Travel diet? These are all intangible impacts, but let's take it a step further to satisfy the math nerds among us - what financial impact could this potential unhappiness have on your life through your health? *According to Stanford professor Jeffrey Pfeffer, workplace stress accounts for $180 billion additional health-care expenditures. That's approximately 8 percent of the total health-care spending.*

Even with the size of the potential financial impact on our lives through our health, as indicated from the number above, we do still tend to make these strategic decisions and focus only on the "easy" math. Recently I stumbled upon another Stanford research study about our own view of the stress in our lives, and the following thought from the study was incredibly compelling to me in application to conversations with clients: "STRESS IS MOST LIKELY TO BE HARMFUL WHEN THE FOLLOWING CONDITIONS ARE PRESENT: IT FEELS AGAINST YOUR WILL, OUT OF YOUR CONTROL, AND UTTERLY DEVOID OF MEANING."

Maybe what we now miss in these busy times, as we speed through the moments of quick capitalization of every opportunity that comes along, are the calmer moments of contemplation about what opportunities might lie ahead if we would say no to the less meaningful ones?