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2023 Second Quarter Newsletter and Outlook

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In this newsletter, I'm going to keep my investment comments brief to offer some observations, and resources to consider, when you or a loved one is in the 9th inning of life. For those clients who are too young for this to be a consideration, this may be useful information when you are talking to your parents.

For the first quarter of 2023 (if MCS clients' investments were treated as one large portfolio including their cash), on average clients gained 1.76%, after fees. For comparison purposes, the S&P 500 Total Return Stock Index (S&P 500) and the Bloomberg Barclays Aggregate Bond Index both extended their rebound from last year's double-digit losses, gaining 16.89% and 2.09%, respectively. The range of MCS individual client returns was from a gain of 8.31% to a loss of 0.31%.*

The clients with the lowest returns had overweight inherited stock exposure in financial and retail stocks. Clients with the highest returns had higher stock exposure, especially in technology stocks. Overall MCS client portfolios have much less volatility due to a very large allocation to state income tax-exempt, US Treasury Bills yielding 4.6% to 5.0%.

Second Quarter Market Review

The recent stock market performance is well summed up by this quote:

> *The performance of the S&P 500 index is now the most concentrated it has been since the 1970s. Seven of the biggest constituents — Apple, Microsoft, Google owner Alphabet, Amazon, Nvidia, Tesla and Meta — have ripped higher, gaining between 40 per cent and 180 per cent this year. The remaining 493 companies are, in aggregate, flat.*[1]

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* MCS Family Wealth Advisors (MCS) consolidated client returns are dollar-weighted, net of investment management fees unless stated otherwise, include reinvestment of dividends and capital gains and represent all clients with fully discretionary accounts under management for at least one full month in 2023. These accounts represent 99% of MCS's discretionary assets under management as of 06/30/2023 and were invested primarily in US stocks and bonds (3% of client assets on 06/30/2023 were invested in tax-exempt municipal bonds). The Stock Index values are based on the S&P 500 Total Return Index, which measures the large-capitalization US equity market (including reinvested dividends). The Bond Index values are based on the Bloomberg Barclays US Aggregate Bond Index, which measures the US investment-grade bond market. Index values are for comparison purposes only. The report is for information purposes only and does not consider the specific investment objective, financial situation, or needs of any recipient, nor is it to be construed as an offer to sell or solicit investment management or any other services. Past performance is not indicative of future results.

If inflation is coming to an end without a recession, then stocks and long-term bonds could have more room to increase in price. Honestly, I don't know. It's not a bet I'd make with my own money. It's not at all clear to me that inflation is headed for 2-2.5% to stay. To the extent the market believes that outcome and it comes true, the 493 companies that are flat could join the rally.

The Artificial Intelligence (AI) rally (or mania?) that helped propel stocks like Microsoft, Google, and Nvidia is real, but it's difficult to analyze what to pay for exposure to the sector. I'm not inclined to chase big price moves because 1.) too often those short-term gains turn into losses when the future doesn't turn out as projected 2.) it's quite hard to determine, early on, the winners and losers of big technological breakthroughs.

AI companies are being sued for using copyrighted information to compose the AI response.
See https://hbr.org/2023/04/generative-ai-has-an-intellectual-property-problem.

An AI investment consideration is that many brilliant AI people are leaving their big company employers for their own start-ups. There is so much money chasing this investment theme that these employees can't afford not to. When companies lose their best people to new competitors, it means those companies may not be the leaders in the future. Alphabet aka Google which is up 38% since this year, lost eight of its top AI people. It was these Google employees that published a research paper in 2017 called 'Attention is All You Need'.

> *"The paper's eight authors had created the Transformer, a system that made it possible for machines to generate humanlike text, images, DNA sequences and many other kinds of data more efficiently than ever before. Their paper would eventually be cited more than 80,00 times by other researchers, and the AI architecture they designed would underpin OpenAI's ChatGPT (the "T" stands for Transformer), image-generating tools like Midjourney and more.*[2]

Finally, it is possible to see very speculative behavior in stocks, simply by looking at a chart.

When you see a stock chart showing a large percentage gain over a short period of time, that should be considered a warning about the game you are about to get in.

Many investors and Wall Street analysts enthusiastically project recent positive changes in a company's earnings years into the future. This 'exciting' new outlook bids the stock price up to high levels in a short period of time. Good examples of this were the valuations of Pfizer (COVID vaccine profits!) or Zoom (Tech that enables everyone to work from home!) during the pandemic. Well, here we are 3 years later, and all those gains have been lost.

Think of the following charts as waves on an ocean:

Figure 1

Pfizer: Big Swells

Source: Bloomberg

Figure 2

Zoom: The Monster Wave

Source: Bloomberg

There is an investment 'strategy' that I call 'surf the momentum or sentiment' which is essentially catching the wave of excitement and then bailing before it peters out. It is not long-term investing. Many investors apply the wrong investment framework, mistaking long-term investing from catching the wave and riding the price momentum up and back down to below what they paid.

If you are enthusiastic about joining the latest AI wave / market surge, please call me at 541-345-7023 or email michael@mcsfwa.com. I have no idea how big this wave could get. This investment ocean is a complex system and waves that are big now may shrink to be replaced by other waves. Interestingly, the ETFs (exchange traded funds) that specialize in AI/robotics have not surged nearly as much as Microsoft, which has price momentum from its investment in ChatGPT.

Many client portfolios have room for a little 'play money' now that we're earning more interest. My job description as a fiduciary precludes me from surfing momentum / speculating with your money, but it is your money and I'm happy to offer guidance as long as the strategy is understood, you will be watching it, and the price for being wrong is modest or not too upsetting.

Current Portfolio Position

When rates were very low, I bought very short term (1-2 year) bonds, which are bonds that mature very quickly so we would not be locked into low rates for 5 to 20 years. As a result, we have been taking advantage of much higher yields as these investments have matured over the past year. The last of the large, low yield CDs mature in August and September, and we will be able to reinvest that cash in much higher yielding securities.

Endnotes

[1] Martin, Katie and Megaw, Nicholas; "The seven companies driving the US stock market rally"; Financial Times; June 14, 2023; https://www.ft.com/content/b5281dfd-54a1-42fa-b01d-88b3aa8f3272

[2] Source: Olson, Parmy; "Meet the $4 Billion AI Superstars That Google Lost" July 13, 2023; Bloomberg

Life and Death

Lessons from our experience with clients as they age and through the settlement of their estates.

Over the past thirty-plus years, we have had the challenge and privilege of assisting many clients through their 8th and 9th innings of life, and then assisting their families through the estate settlement process. To help you prepare for this time, I want to share what we have learned so far. Whether you are the oldest generation of your family or the next generation and thinking about your parents, the following recommendations may help you navigate this with fewer surprises.

Make the most of the final innings.

As we approach the last decades of life, there are two situations we must come to terms with. First, who will help me with daily activities when I am no longer able to do them myself? Second, who will manage my finances when I can no longer keep up? If we are lucky, we won't face these needs until our 8th or 9th decade, but to make the most of those years we should have a plan in place ahead of time. That means identifying who these helpers will be, preparing them to take on their roles when the time comes, and empowering them with the proper legal documents and contractual relationships. Finally, there is the important step of preparing ourselves emotionally for this time of life.

Caregivers

More than ever, there is a shortage of quality eldercare workers. If you feel that you or a family member will need assistance, do not wait until a medical event requires care giver services. If you do, you forgo the luxury of choosing someone best suited to your needs and instead will be choosing from who is available now, or you may have to provide care yourself while you wait until an eldercare worker becomes available.

To better the odds of getting the eldercare you want (note I did not say guarantee), establish a relationship with a geriatric care manager well before you need them. Start by having them do a physical and cognitive assessment, and update that assessment annually. Let them track your inevitable decline through the years. Allow them to have a medical file already in place so that when the time comes, they know exactly who they will care for.

If you plan on staying at home as long as possible, hire a caregiver to provide some assistance even if you'd normally opt for muddling through on your own. If you are fortunate, you may find some amazing people who see caring for the elderly as a calling. At the same time, be mindful of any 'not quite right' situations and tell a family member and the agency. Not everyone in the eldercare business is an angel.

Sometimes clients will hire an individual caregiver unaffiliated with any care management company. This can work but if you are employing an individual, it is more complicated (especially if you are paying them under the table). Legally you must report more than $600 of income paid to them. Other than reporting someone to the authorities, you may have no recourse if you pick a 'bad egg' to help you. Meanwhile, your family may be left scrambling to undo the damage.

Michael's Experience

In 2016, after he was hospitalized, I convinced my dad (then 83) to hire a geriatric care management company for himself and my stepmom. The geriatric care manager came to the house and assessed not only my parents physical and cognitive abilities but also their surroundings for risks like tripping hazards to signs that their personal care might be slipping. Here is a link to a web page that helped my family and me. The "Guide to Home Care" and "Know When Your Loved One May Need Senior Care & Housing" are particularly useful, but there are many excellent articles here.

Because health declines are often episodic, during a period of stability dad fired our geriatric care manger/nurse, Jennifer, because he thought it was a waste of money. (She was checking in about once a month. Since he insisted on living at home, I thought it was prudent to have a geriatric care professional put eyes on my parents proactively.) I eventually hired her back, this time at my expense, to support my stepmom. At the same time, Jennifer also kept an eye on my dad. She was invaluable in sorting out my stepmom's medications and identifying the poly-pharmacological implications. With Jennifer's input, we were able to reduce my stepmom's meds.

Later, when my stepmother was hospitalized, it was Jennifer who was able to go to the ER, stay late, get the doctors' reports, report to the family, and coordinate care until my brother could arrive. My dad didn't have the stamina to stay at the hospital after his wife was admitted. Jennifer and a few other care providers were essential to enabling my parents to live at home as long as possible. We consciously built relationships with these wonderful people before my parent's health events became acute.

Prepare Your Core Care Team

Identify who your care team will be, beyond the geriatric care manager and your caregiver. Do you have adult children, grandchildren, other relatives, or close friends you can turn to? If so, bring them into the process. Put them in a position to help before their help is needed. If possible, make sure your care manager or caregivers have their contact information and that you have authorized them to talk to each other.

Tell your team, and your doctor, about your preparations for when you or your spouse may need assistance. They may already be concerned about you but not know how to bring up or discuss the topic. Keep in mind that these discussions are emotionally stressful, especially for adult children, because they are discussing your potential disability or death. They may not fully process what you are saying or remember it. Have your key points / questions written down for them. Let them know that this will be an ongoing conversation as things come up or change. Have this same discussion with your doctor.

In both discussions, ask these questions:

- What do you see as the pros and cons for me regarding my plans?
- How do my plans affect you from your perspective?
- What are the pros and cons for you about your role?
- What alternatives would you consider if you were in my position?

Prepare Your Financial Care Team

Who will you choose to handle your finances once you lose the capacity to do so, even on a temporary basis? For some people, this decision is even more daunting than deciding who will care for them. The though of giving up control of your nest egg can be paralyzing. On the other hand, if you do not choose someone, at some point this choice will be made for you. Like your eldercare team, your financial care team should be chosen carefully from people you trust (and who are younger than you).

Empower Your Team

Once you have decided who your core care team should be, empower them with legal documents that will grant them authority to make decisions on your behalf, such as Medical Powers of Attorney, Advanced Care Directives, Financial Durable Powers of Attorney (DPOAs), and Trusts. Medical Powers of Attorney grant medical decision-making authority and Advanced Care Directives provide guidelines for those medical decisions. Trusts and DPOAs give third parties (such as a family member, friend, or corporate entity like a bank trust department) the ability to use your assets for your benefit.

The ability of third parties to act depends on whether they are named as a trustee/agent or successor trustee/agent.

- A trustee/agent has the same current authority to handle your affairs as you
- A successor trustee/agent has authority to handle your affairs only after an event occurs (i.e. you become or are deemed incapacitated)

While many attorneys recommend naming successor trustees rather than co-trustees (or successor agents rather than co-agents), in our 30+ years advising clients we have found significant benefits to empowering your financial team sooner rather than after it becomes a necessity. This means changing your *successor* trustee to a **co-trustee**.

While the successor trustee or successor co-agent may seem logical, *(Why should I appoint someone before I need them?)* in practice determining incapacity is fraught with problems. First, incapacity comes in many forms: physical or cognitive, gradual or sudden, temporary or permanent, mild, moderate, or severe. Most legal documents require one or more doctors to certify that your incapacity is severe, and it can be difficult (especially in gradual incapacity) to find doctors to make this call.

We have observed in the families we have worked with that the healthiest, least stressful route (assuming the successor is competent and trustworthy) is to empower your team before you need them. By skipping the requirement that the current trustee must first be deemed incapacitated to get a successor's help with their finances, the trustee and family also skips the baggage that goes with it. They give their successors the same authority as they have on their own accounts years before they become incapacitated.

This does not mean that they give up control of their finances. Nor do they give up any independence. Naming a team to act for them early means that they can gradually introduce their successors to their financial situation and to their advisors. It gives them the chance to mentor their successors in good financial management and pass on their financial wisdom.

Preparing Yourself

You may be thinking, "They give their successors immediate access to their assets?! I'm not ready to have my kids in my business!" Okay, take a deep breath and exhale slowly, please. Try to get in 'third person mode' and ask yourself, why did I react like that?

For many clients, this is the most difficult step of all. Accepting the universal truth of aging goes against our culture's obsession with youth and its portrayal of the inevitable stages of aging as weakness. Our self-image of nurturer, provider, and strong, independent individual becomes threatened when we are forced to rely on others.

Understand that this a normal reaction. No one wants to lose their independence.

That said, your next generation co-trustee does not want you to lose your independence, either. And the last thing they want to do is to feel forced at some point down the line to declare someone they love; someone whose competence was never in doubt, as now incompetent. That would be painful to everyone involved. Typically, successors want to help only when it is needed, to support you when things get complicated and get the situation under control, then get back to juggling their own obligations.

For some, their feelings about privacy when it comes to their money are a stumbling block. Cultural taboos around talking about money may be inhibiting. They are uncomfortable that their children or successors, once granted access to their accounts, will pry into their business. On the contrary, what we have experienced when adult children or trusted friends become co-trustees is… nothing. And by nothing we mean that co-trustees or agents of DPOAs don't call us and ask, even though they are authorized to, about our clients' money. They don't try to access the account. They basically leave it alone and wait until they are needed.

When we do get a call is when something unfortunate has happened, and the authorized person wants to know what is available and how to get it if its needed.

Finally, you can work on practices to prepare yourself for the inevitable changes that come in the final decades of life. Practice saying what you feel and being vulnerable. Start with sentences like these:

- "I'm scared of…"
- "I'm feeling a little lonely…"
- "I want you to know …"
- I so appreciate…

I expect this will be harder for men – we aren't conditioned to show our vulnerability – but if you can pull it off, you may greatly enhance your legacy. Also, resist taking out your frustrations with aging on those who are there to help you – that includes your own family. Treat them well, you are their model for this stage of life.

In summary, preparing to enjoy your final decades begins with putting the team in place before you think you will need it. Establish relationships with eldercare providers, assemble your core team, prepare the legal framework that will empower your team, gradually involve them in the process, and start practicing communication skills that will help you and your loved ones navigate this powerful stage of life.

Conclusion

If you feel ready to update your estate planning documents, please reach out to us. We have worked with scores of attorneys and their documents, and we prefer to review them before you sign them (to make sure that they are drafted in a way that meets your wishes and Schwab's requirements). We will also prepare the proper forms for submission to Schwab to update your accounts and add your co-trustees to your trust or co-agents to your Durable Powers of Attorney.

Finally, there is not a one size fits all strategy for the 9th inning. Please let us know **your** insights and recommendations for navigating these waters. Many clients are retired doctors, and your observations and insights would be appreciated. Many of you have had the experience of caring for a loved one in the 9th inning of life or are there yourselves.

Please call us at 541-345-7023, or send an email to michael@mcsfwa.com or jeff@mcsfwa.com, if you feel you have something important to add to these recommendations.