SPRING 2021

THE JENTNER REPORT

Wealth Management Strategies from Jentner Wealth Management

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Did History Repeat Itself?

Each year, we look back at the data to see how the active managers faired compared to a passively engineered investment strategy.

During the first quarter or 2021, many investment analysts began to sift through the previous year's returns and data. Once again, history repeated itself: most active managers underperformed their benchmark. New data from the S&P Dow Jones Indices shows that 60% of large-cap equity fund managers underperformed the S&P 500 Index in 2020. Yahoo Finance writers Myles Udland and Sam Ro noted, "This is the 11th straight year that pros lagged that benchmark."

Of course, this is not breaking news. Jentner has been tracking this trend since the 1990s. As the following graph illustrates, the trend is not improving for active managers. In the last 20 years, 2009 was the best year for managers beating the index; yet 40.7% still underperformed the benchmark. Those are risky odds.

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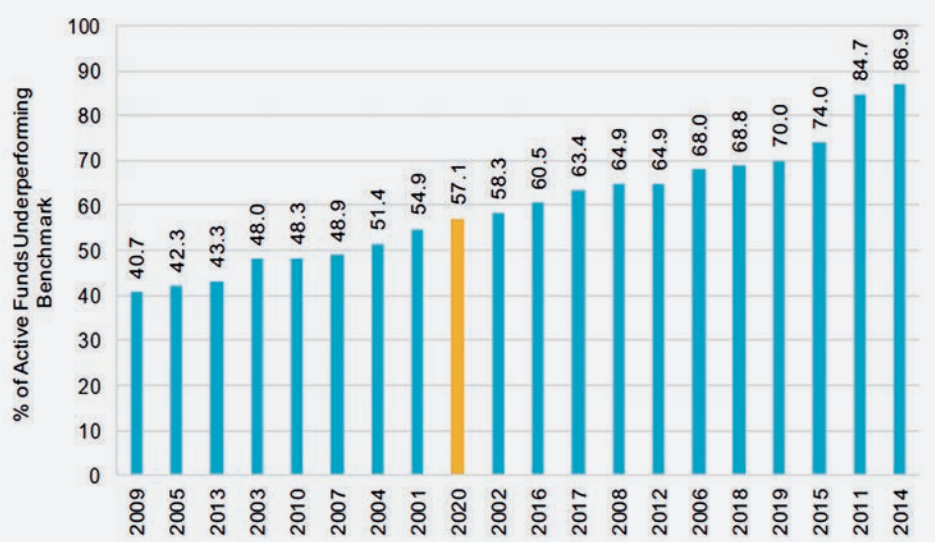
Percentage of Domestic Equity Funds Underperforming the S&P Composite 1500



Source: S&P Dow Jones Indices LLC. Data as of Dec. 31, 2020. Past performance is no guarantee of future results. Chart is provided for illustrative purposes.

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JENTNER WEALTH MANAGEMENT

THE PRESIDENT'S WORD

President Biden's Tax Plan

A look at Biden's proposed tax plan and how those changes could affect you.

Bruce Jentner, CFP®, Chairman

In 1789, Benjamin Franklin wrote, "Our new Constitution is now established, and has an appearance that promises permanency; but in this world nothing can be said to be certain, except death and taxes." Truer words have rarely been expressed. It appears that President Biden and Congress are gearing up for tax-law changes that will affect many now and at death. Let's look at the proposed changes according to the Tax Foundation.

Social Security Payroll Tax

Currently, income greater than $137,700 is exempt from the Old-Age, Survivors, and Disability Insurance program. The Biden administration is looking to add OASDI payroll tax on income above $400,000 split evenly between the employee and employer. Essentially, this would create a "donut hole" for wage earners between those two levels of income.

Top Tax Rates

The top bracket would be raised to the pre-Tax Cuts and Jobs Act level: 39.6%. Currently, the top tax rate is 37%.

Estate Tax

Biden's plan proposes returning to the 2009 estate-tax and exemptions amounts. Currently, estates less than $11,700,000 per individual are exempt from any estate tax. Biden's proposal lowers the exemption to $3,500,000. Under both scenarios, any estate exceeding this amount would be taxed at 40%. Though not in the current plan, there are discussions to bump the estate tax rate to 45%.

Deductions from Income

Those earning $400,000 or more could see their itemized deductions phased out. Additionally, business owners in that higher-income bracket could also lose their Qualified Business Income Deduction.

Capital Gains

It appears the Biden administration will also take some aim at capital gains, qualified dividends, and estate transfers. Lower tax rates for capital gains and qualified dividends would be eliminated for those whose taxable income exceeds $1,000,000. Currently, capital-gains tax rates are 0%, 15%, and 20% depending into what bracket the taxpayer's adjusted gross income falls.

Expands Tax Credits

Under the new plan, the Earned Income Tax Credit, Renewable Energy Tax Credits, and Child and Dependent Care Tax Credit (CDCTC) will see revisions. The plan would also reestablish the First-Time Home Buyer's Tax Credit up to $15,000 for first-time home buyers. Furthermore, the plan proposes increasing the Affordable Care Act's premium tax credit and increasing the Low-Income Housing Tax Credit.

Many other revisions are also being discussed; however, the above-outlined items are receiving extra scrutiny. With the Senate split 50/50 and Vice President Harris as the tie breaker, the path for any tax-law changes is not clear, and we suspect some revisions to the proposed tax plan will be made. While we anticipate the estate-tax exemption amount being revised, we do not foresee a reversion back to the 2009 exemption level. Additionally, we could see top marginal rates creeping back to pre-2017 levels and some additional FICA tax-law changes.

Revisions to state- and local-tax deductions are not addressed in Biden's tax plan. The Trump Tax Act in 2017 capped the state and local tax deduction at $10,000. This hit wealthy Americans in states with the highest taxes. Many of these states have Democrat senators who are anxious to repeal the cap. It is unclear how this will affect negotiations on other tax revisions.

What remains clear to us is the need for tax coordination between your investment and tax-planning strategies. Navigating the ever-changing tax landscape alone could spell disaster to the uninitiated. While we can't control death and taxes, we can certainly plan well for either event.

Don't Give Up on Bonds

Bonds had a great 2020 but are lagging in 2021. Is now the time to move away from bonds and into stocks?

The 2020 pandemic-linked market crash and subsequent flight to safety lifted the Bloomberg Barclays U.S. Aggregate Bond index 7.5% last year. However, with the federal-funds rate hovering near zero and equity markets soaring, bonds are lagging so far in 2021. Recent performance coupled with the prospect of rising rates in the coming years have many investors bearish on holding bonds. We say not so fast. Despite possible headwinds for fixed-income investors, bonds still play an integral role in a well-diversified portfolio.

If a long-term investor could ignore market declines, even when significant, one could make an argument for holding a stock-only investment portfolio. This approach looks even more appealing when stock markets are on a bull run. However, we know a bull market will not last, and most investors cannot emotionally stomach the roller-coaster ride of a 100%-stock portfolio. Look at the tech crash of 2001, the housing crash of 2008, and the recent pandemic crash, which all caused some investors to exit stocks all together. The more prudent course of action is to manage the ups and downs by diversifying an investment portfolio with bonds.

Generally, when stocks are declining rapidly, bonds increase in value. Many call this the flight to safety. In 2008, large-cap stocks declined 37%, and conversely, the aggregate bond index rose 5.2%. Having a portion of our client's portfolio in bonds during that time proved wise as it gave clients some level of comfort and a relatively stable source of funds to buy stocks that were significantly on sale. Disciplined investment portfolio rebalancing coupled with staying fully invested proved successful.

A recent study published by JP Morgan in their Guide to the Markets shows the S&P 500 Index earned an annualized return of 6.1% over the last 20 years. By comparison, a portfolio consisting of 60% stock (S&P 500 Index) and 40% bonds (Bloomberg Barclays Agg Index) returned 5.6% over that same time span. An investor could have captured nearly all the returns of large-cap U.S. stocks with nearly half the risk. This is called risk-adjusted investing.

Of course, there are always investors who claim they can withstand the ups and downs of the stock markets by selling when markets drop and buying when they rebound. Dalbar, Inc. proved that not to be the case. It reviewed mutual-fund inflows and outflows over the last 20 years and concluded the average investor earned a disappointing 2.5% annualized return.

Our conclusion is investors are best served by holding a well-diversified portfolio of bonds and stocks. Yes, there will be times when bonds are out of favor. However, in years when storm clouds are gathering on the horizon for stocks, diversified investors can be steady at the helm. Their well-constructed portfolio should remain afloat.

Daniel J. Bloom, CFP®,
Vice President and Chief Administrative Officer

Did History Repeat Itself?

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What is more alarming for active managers is the trend worsens when looking back multiple years. Over a 10-year period, 80% of active managers fail to beat their respective index, and this only reflects the funds that survived those 10 years. Worse yet, Dow Jones goes on to report, "A paltry 4% of large-cap growth funds beat their benchmarks." Things were not much brighter for international-focused active managers with nearly 90% of managers underperforming their respective benchmarks.

Active managers often tout their ability to protect their portfolios during market declines and enhance them during market upswings. However, they fell short of delivering on that claim yet again in 2020.

We avoid betting on which manager can make it. Instead, we invest in low-cost asset-class funds with a good track record of capturing their respective market returns while keeping tax- and cost-efficiency in mind. While past performance cannot predict future returns, historically this method has proved successful for our clients.

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Is Gold A Good Investment?

With increasing discussion about inflation, you have probably heard advertisements encouraging people to invest in gold. But is gold really a good investment?

We acknowledge it can be tempting to purchase gold. But to us, a concentrated position in gold is not a prudent investment; it is a place to hide when things are scary. Much like Bitcoin, many are buying in, expecting to be bought out at a higher price. But gold produces no real value, so its price is dependent solely on new buyers. Once they stop coming in, the price can and has historically fallen sharply.

We find what Warren Buffett said in 2010 about gold interesting: "You could take all the gold that's ever been mined, and it would fill a cube 67 feet in each direction. For what that's worth at current gold prices, you could buy all—not some—of the farmland in the United States. Plus, you could buy 10 Exxon Mobils, plus have $1 trillion of walking-around money. Or you could have a big cube of metal. Which would you take? Which is going to produce more value?"

We would rather invest in companies that create things and add value, instead of something dependent on the whims of buyers. History lends credence to our philosophy. From January 2010 through December 2020, the ETF "GLD" returned 66%. However, the S&P 500 Index returned an impressive 235%.

Do we think precious metals can play a role in a diversified investment portfolio? Yes, but we prefer investing in a broad basket of producers of precious metals along with other stocks and bonds. Strategically placing these in a diversified portfolio and rebalancing each asset class when it is either over-weighted or under-weighted enables the prudent investor to chart a successful investment experience through challenging and opportunistic times.

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