FERGUSONJOHNSON
WEALTH MANAGEMENT

Thoughts on COVID-19 – How It's Affecting Our Clients and Our Firm

April 28, 2020

This is a rough time. There's really no way to sugar coat it. People around the world are falling ill. Many transactional businesses are severely imperiled. Lots of Americans are out of work. Even for those of us who have been fortunate enough to remain healthy and stay employed, things are still hard. Parents deal with the stress of juggling both children and work during the day. Grandparents can't hold their grandkids. I'm sure many of us are probably experiencing a touch of cabin fever. And of course, the specter that is the primary subject of this commentary, investments have yielded brutal returns the past several weeks.

Overall, I've been very impressed with the attitudes and discipline of the clients we've communicated with over the last month. The overwhelming majority of our clients have echoed a commitment to a long-term investment plan and are not allowing this crisis to affect the strategies we've put in place for their investments. For that, I commend each of you.

But I certainly can't fault anyone for worrying and wondering "should I move out of stocks to protect myself?" I think this is a good time to discuss how markets function in times of crisis.

Stocks are generally considered to be a leading indicator of the economy. What that means is a decline in the market can sometimes act as prelude to a recession (or recovery), but usually not the other way around. In the past, when we've been hit with recession, stock markets have tended to move down in advance of the recession's actual impact on the economy. By the time we feel the tangible effects of economic declines, markets have already priced assets lower. The opposite also has often been true. Markets typically recover in advance of the underlying economic fundamentals.

Let's take a moment to remember what happened in 2009. Unemployment surged, businesses shuttered, wages fell, and property values plummeted. Things were bad, and then they got worse. Despite on-going ruin of the economy, equity markets returned 64.83%1 from the low on March 9th through the end of 2009. If you had bailed out sometime in late 2008 or at the beginning of the year, perhaps waiting until "things we're looking a bit better", you would have missed that sharp recovery in markets. In fact, the economy didn't really start to look better until 2012 or 2013. That's a lot of missed gains in stock while sitting around waiting for an "all-clear signal".

We’re not worried about a drop in the market or a recession. We expect these events. It’s part of investing. It’s part of the natural order of economies. When we build financial plans, we plan for the eventuality of *several* significant market declines over the investing life of a client. What we don’t plan for is missing out on a recovery.

What if this time is different? What if this is the one were not coming back from? Honestly, if that’s the case, then your stocks, and bonds, and cash don’t really matter. If we’re in a situation where we, as a society, can’t pick up the pieces, then economic systems as we know them are irrelevant. Please know that I say that with tongue in cheek. We’ll get through this calamity the way we’ve gotten through hard times before. In 1945, Germany had been reduced to literal rubble. In only a few years following their surrender in World War II, they were back up to pre-war production levels and economic output. We’re a resilient species that craves progress. It might not seem like it if you focus on the day-to-day, but progress over the long-term has occurred and will continue to occur at a tremendous magnitude.
To borrow from our own blog post from a few months ago, this is what progress looks like:
Since 1981,

- The homicide rate in the United States has been cut in half2.
- Infant mortality has declined 54%3.
- Mortality resulting from heart disease has declined 58%4.
- Rates of Dementia have dropped by 44%5.

Do you want to bet against progress because a virus keeps us home for a few months? I think I’d rather bet that the pain we’re experiencing today will make us better prepared for tomorrow.
With all this in mind, let’s talk about the actions we have been and will be taking to ensure our clients assets are appropriately positioned for their goals:

- Rebalancing

  your portfolio when warranted, to stay on course toward your long-term goals.

- Tax-loss harvesting

  where practical, to offset the costs of recently incurred and/or future taxable gains.

- Roth IRA conversions

  when they may benefit your retirement planning.

- Seizing other opportunities

  when your plans call for it. For example, if you’ve been holding a concentrated stock position to avoid incurring taxable gains, now may be the perfect time to reduce your risks and strengthen your portfolio by selling all or part of that position.

The CARES Act, Economic Stimulus, and RMD Relief

One bit of welcome relief came at the beginning of the month with the passage of the CARES Act aimed to shore up the economy while many Americans are unable to carry out regular business. The stimulus provides for enhanced unemployment benefits, facilitation of potentially forgivable loans to small businesses, as well as rebating in the form of income tax relief. The specifics and application of many of the points of the law are outside the scope of this commentary. However, there is one item that I want to highlight which may affect many of our retired clients.

The CARES act provides a reprieve of the required minimum distribution obligations from retirement accounts for 2020. For those that do not need to take the full amount of their RMDs in order to meet income needs, this offers an opportunity to abstain from distributing as much (or anything) from an IRA this year.

For retirees with relatively high adjusted gross income to report this is beneficial on two fronts. First, this can directly reduce taxable income that would otherwise be paid at a family's highest marginal tax bracket. Second, another aspect of the law provides tax credit of up to $1,200 per individual (and $500 per child) with phase-outs for moderate-to-high income earners. By forgoing distributions from retirement accounts in 2020, a retiree may be able to qualify for the tax credit when they otherwise could not.

In the coming weeks, we will be reviewing our clients' RMD plans for the year and addressing potential adjustments with clients as needed.

Ferguson-Johnson Wealth Management

You may be wondering how these global developments have been affecting Ferguson-Johnson Wealth Management. We instituted our own work from home order several weeks ago and are practicing social distancing like the rest of the country.

As background, the SEC requires Registered Investment Advisers to have an emergency preparedness plan established in the event that employees are unable to reach their primary place of business. When regulators review advisers' contingency plans and procedures, they seek to ensure that clients will not be left in limbo from an adviser being unable to provide the services the client relies upon due to unforeseen circumstances. As a result (and, really I believe it's just appropriate business practice), we have long had systems and tools at the ready to conduct regular business operations remotely if and when an occasion such as this were to arise.

In short, we are giving the same care and attention to our client's accounts and plans as we were from our desks in Rockville a month ago. Honestly, without having to endure DC-area traffic on a day-to-day basis, we've been perhaps left with more time and energy to fulfill our duties to our clients.

We'll be right there, by your side, now and in what's to come.

1 Source: Morningstar, data from 3/9/2009 to 12/31/2009.
2 Federal Bureau of Investigation, "Crime in the United States, 2018".
https://ucr.fbi.gov/crime-in-the-u.s/2018/crime-in-the-u.s.-2018/topic-pages/murder. Accessed 1/5/2020.
3 Federal Reserve Economic Data. "Infant Mortality Rate for the United States".
https://fred.stlouisfed.org/series/SPDYNIMRTINUSA. Accessed 1/5/2020.
4 The Wall Street Journal. Archived web resources.
https://si.wsj.net/public/resources/images/NA-CM632_MORTAL_9U_20161207200907.jpg. Accessed 1/5/2020.
5 Claudia L. Satizabal, Ph.D., Alexa S. Beiser, Ph.D., Vincent Chouraki, M.D., Ph.D., Geneviève Chêne, M.D., Ph.D., Carole Dufouil, Ph.D., and Sudha Seshadri, M.D. "Incidence of Dementia over Three Decades in the Framingham Heart Study. The New England Journal of Medicine. February 11, 2016.