THE Wealth REPORT

PROSPECTS FOR INVESTING IN THE 2020s

Overview

They say hindsight is 20/20, but it's difficult to grasp that one day we could look back at this pandemic and recognize where we should have placed our investments. Perhaps a young researcher — sequestered in his home — will find a cure and a vaccine, start his own company and be the fastest-rising stock in history. Perhaps Amazon, a company currently soaring with order and delivery revenues, will be plagued by class-action lawsuits for not protecting its workforce and succumb to bankruptcy.

We don't know. Our best action is to focus on sustaining our own financial security and goals for the future. It's probably not a time to place all eggs in one basket, and hindsight may reveal — as it has in past crises — that it's likely also not a time to fully exit the investment markets.

While 2020 may have begun a new decade marked by historically low unemployment, benign inflation and a robust economy, it has now devolved into a challenge for investors to manage their portfolios through the swiftest stock market correction in history.

From an investment point of view, the tortoise is starting to look pretty good about now compared to the rapid growth pace of the hare.

Cautionary Tales: Expect the Unexpected

For the moment, both monetary and fiscal stimulus are rendered ineffective since both supply and demand have been so inordinately impacted by the worldwide COVID-19 outbreak. With much of the focus on containing the spread of the virus, there is little that can be done to revive the economy until the crisis has passed and we discover which companies — both large and small — were prepared enough to sustain their business models during the economic fallout.

A recession is traditionally defined as two consecutive quarters of negative economic growth. However, Federal Reserve Chairman Jerome Powell remarked in late March that the United States may well already be in a recession.[1] Some analysts are even projecting the possibility of another depression, which is when a country experiences a prolonged economic downturn measured by years — not months.[2]

Despite the foreboding circumstances, we can expect that investors and the investment markets will emerge with a very different perspective post-COVID-19. For example, high dividend-paying stalwarts in your portfolio may have reason to cut those income payouts. After all, companies that choose to apply for loans from the federal government, enabled by the $2 trillion CARES Act, will be restricted from paying out dividends for a year after the loans have been repaid in full.

This restriction obviously will not apply to companies that do not receive federal assistance, so it really comes down to how well capitalized various companies are and how they choose to mobilize that capital. It's worth recognizing, however, that even long-time steady growers are under pressure to shore up cash reserves, which may require deploying strategies such as reducing investment, suspending share buybacks and even cutting dividends.[3]

"We've been saying for quite some time now that it would be something totally unexpected that would take the market down … the coronavirus fits the bill in that regard. What a shock."[4]

Given that we are in generally unprecedented times, let's discuss time-tested strategies that have been helpful in times of volatility in the past.

Short-Term Strategies

Avoid Selling Now
If you didn't move money out of equities prior to or at the beginning of the market crash, you've likely lost earnings. However, unless you need to access that money in the very near future, it's probably best not to sell now. Once you're inside a bear market, the general rule of thumb is to focus on long-term recovery.

Keep in mind that markets tend to gain the most ground in the months just after the initial tide turns, based on analysis of the 14 bull markets the U.S. has experienced since 1930.[5] If you sell now, paper losses will become permanent and you may not be positioned to benefit at the start of the recovery.

Stocks: Winners and Losers
If you are in a position to make trades, it may be worth restoring your equity allocation with near-term winners and losers in mind. For example, retail, auto manufacturing, travel and tourism, global delivery and oil prices are likely to experience detrimental short-term impacts from the crisis.

On the other hand, it may be a good time to pick up holdings poised to benefit from the pandemic while prices are low. This includes the so-called FAANG stocks (Facebook, Apple, Amazon, Netflix and Google), when you consider their delivery models are quarantine-friendly while people are largely stuck at home. It's also a good time to look at consumer staples since they are the products of essential services, like pre-packaged groceries and household items.

Long-Term Strategies

Inflation Defense
Ongoing stimulus deployed by the Federal Reserve will flood the economy with more capital. This involves printing more money, which generally leads

to higher inflation. On the flip side, confinement required by the coronavirus will lead to reduced labor and production, so a lower supply of high-demand products will also generate inflated prices. A traditional hedge for inflation has been Treasury Inflation-Protected Securities (TIPS) and commodities.[6]

Demographic Considerations

It's important to take a look at how demographics will drive the economy of the future. First, the millennial generation has already overtaken baby boomers as the largest demographic in both the overall population and in the workforce. In a post-pandemic world, imagine this group expanding into the resurging real estate market, a deeper concentration of technology companies and more prolific retail sales via the internet.

It's also possible that the recent health crisis, combined with the rise in unemployment, may accelerate legislation to decouple health care coverage from the employer job market. This move could lead to higher numbers of new small businesses, which, unshackled from the responsibility of providing health insurance to workers, could make them more nimble and competitive in both domestic and global markets.[7]

It's interesting to consider what different demographics will take away from this most recent decline. For example, younger generations have experienced back-to-back-to-back tragedies of serious magnitude, from Sept. 11 and the Great Recession to hundreds of terrifying mass shootings, a couple of presidential impeachments, heightened threats of war with Iran and North Korea, and now a global pandemic.

Generation X and the millennials, with their 24/7 connection to real-time news and information, are battle-scarred, resilient and undaunted. They know what can happen, they've learned to expect it and they may be hard-wired to prepare for it.

IRA Conversion

One of the things you could do right now is plan for lower taxes during retirement. To this end, it may be a good time to consider converting a traditional IRA to a Roth. Now that prices have sunk, you'll owe fewer taxes and can reposition those holdings into a Roth IRA. Once the market recovers, future gains will grow tax-free, and you'll be able to draw tax-free income during retirement. The taxes you owe will be based on the date of the conversion. This means that by next year when you file a 2020 return, you may already be benefiting from a market rebound.[8]

Please remember that converting an employer plan account to a Roth IRA is a taxable event. Increased taxable income from the Roth IRA conversion may have several consequences, including (but not limited to) a need for additional tax withholding or estimated tax payments, the loss of certain tax deductions and credits, higher taxes on Social Security benefits and higher Medicare premiums. Be sure to consult with a qualified tax advisor before making any decisions regarding your IRA.

It is generally preferable that you have funds to pay the taxes due upon conversion from funds outside of your IRA. If you elect to take a distribution from your IRA to pay the conversion taxes, please keep in mind the potential consequences, such as an assessment of product surrender charges or additional IRS penalties for premature distributions.

Guaranteed Income
If you've had just about enough stock market volatility for this lifetime, consider repositioning some of your assets to purchase an annuity. This way, you can receive issuer-guaranteed payments to supplement your Social Security benefits, so retirement is less likely to be as nerve-wracking as relying on dividends and market prices to support your basic living expenses.

Annuities are insurance contracts designed for retirement or other long-term needs. They provide guarantees of principal and credited interest, subject to surrender charges. Annuity guarantees and protections are backed by the financial strength and claims-paying ability of the issuing insurer. Annuities are not a deposit of, nor are they insured by, any bank, the FDIC, NCUA or any federal government agency.

Final Thoughts

The fact that consumer spending drives 70% of the economy presents an inherent dichotomy with the average household's need to aggressively save money to buy a home, pay for college and fund a comfortable retirement.[9]

For many people, it's impossible to support both efforts. For the duration of this health and financial crisis, we offer this advice: Spend only on what you need. Use discretion. Tighten the belt when times are tough so you have plenty to share when the economy recovers.

As always, we recommend that you consult with your financial advisor for advice tailored to your unique circumstances.

[1] Megan Henney. Fox Business. March 26, 2020. "Fed's Powell says US economy may already be in a recession." https://www.foxbusiness.com/economy/jerome-powell-coronavirus-economy. Accessed April 8, 2020.
[2] Patricia Sabga. Aljazeera. March 30, 2020. "Coronavirus economy: Recession or depression?" https://www.aljazeera.com/ajimpact/coronavirus-economy-recession-depression-200324161905531.html. Accessed April 8, 2020.
[3] Phillip van Doorn. MarketWatch. April 6, 2020. "These 60 large U.S. companies are 'susceptible to a dividend cut,' according to Jefferies." https://www.marketwatch.com/story/these-60-large-us-companies-are-susceptible-to-a-dividend-cut-according-to-jefferies-2020-03-31. Accessed April 8, 2020.
[4] Ashby Daniels. MarketWatch. March 30, 2020. "5 actions you can take during a bear market." https://www.marketwatch.com/story/5-actions-you-can-take-during-a-bear-market-2020-03-30?mod=home-page. Accessed April 8, 2020.
[5] Dana Anspach. The Balance. March 20, 2020. "U.S. Stock Bear Markets and Their Subsequent Recoveries." https://www.thebalance.com/u-s-stock-bear-markets-and-their-subsequent-recoveries-2388520. Accessed April 8, 2020.
[6] Jurrien Timmer. Fidelity. Dec. 11, 2019. "What's ahead in the 2020s?" https://www.fidelity.com/learning-center/trading-investing/markets-sectors/market-outlook-for-2020s. Accessed April 8, 2020.
[7] Josh Bivens. Economic Policy Institute. March 5, 2020. "Fundamental health reform like 'Medicare for All' would help the labor market." https://www.epi.org/publication/medicare-for-all-would-help-the-labor-market. Accessed April 8, 2020.
[8] Ashby Daniels. MarketWatch. March 30, 2020. "5 actions you can take during a bear market." https://www.marketwatch.com/story/5-actions-you-can-take-during-a-bear-market-2020-03-30?mod=home-page. Accessed April 8, 2020.
[9] Mark Muro, Robert Maxim and Jacob Whiton. The Brookings Institution. March 17, 2020. "The places a COVID-19 recession will likely hit hardest." https://www.brookings.edu/blog/the-avenue/2020/03/17/the-places-a-covid-19-recession-will-likely-hit-hardest/. Accessed April 8, 2020.
