Quarterly Newsletter

Roth FINANCIAL PARTNERS

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Where We've Been

By: Eric Johnson
Wealth Advisor

My wife, Ellie, and I have noted that our lives will never be the same. We're sleeping less, washing our hands more frequently than we ever have before, and canceling all of our plans outside of the house. In our case, these changes have little to do with the circumstances related to COVID-19; for us, it's more about learning how to live with a newborn. Our son, Abram ("Abe") Martin Johnson, was born Monday, February 3rd. As we prepared for his arrival through the usual routines of baby showers and filling his nursery with Astros gear (we were in peak nursery-mode in October before the scandal broke!), I also began planning for the moment for which all young financial planners with children dream: setting up his or her child's 529 savings plan for college.

Over the nine months in which Ellie was pregnant, we saved up a meaningful amount that we planned to contribute as an initial lump-sum in his 529 account, and then begin a "dollar-cost average" program for future contributions. Because Abe is 18 or 19 years from beginning college and we plan on regularly contributing to the 529 account, we felt comfortable with our ability to handle risk ("risk tolerance") as well as our ability to pursue risk ("risk capacity") and therefore invested the lump-sum fully in a globally-diversified basket of equity funds. Knowing that college tuition inflates at a rate at least twice the rate of inflation, a healthy dose of stocks seemed appropriate right out of the gate.

We don't believe that any investor can time the market consistently and as it so happens, I invested the lump-sum on Wednesday, February 19th, the same day as the recent all-time high (on a closing price basis) of the S&P 500 index.

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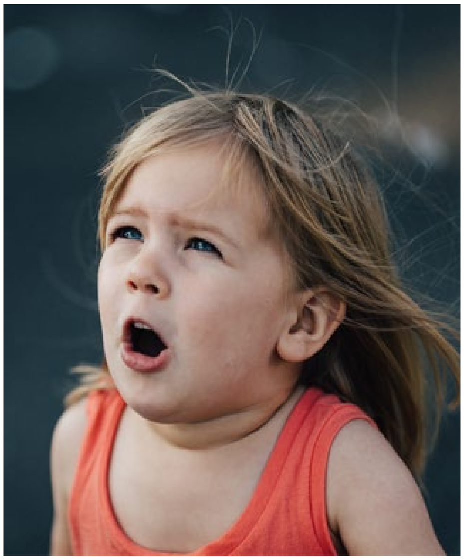
So, what has happened in the markets in the almost month and a half since that account was opened?

- At its max, the S&P 500 had a recent peak-to-trough drawdown of almost 34%, though it ended the quarter on a bit of an upswing with a just under 20% loss for the quarter ended 3/31/2020.
- The velocity of the drawdown was swift, declining in a little over four weeks. During the Great Financial Crisis beginning in late 2007, it took twelve months for the (initial) 30% drawdown to occur. The longest-ever bull market in U.S. history (beginning in 2009) turned what felt like overnight into the fastest bear market in our history.
- Within a two-week span, the index had two days with over a 9% gain (the third and fourth best performing days in the index since 1950) as well as the second and third worst performing days since 1950 (losses of 11.98% and 9.51%, respectively – the worst day being "Black Monday" 10/19/1987 with a 20.47% daily loss).
- Small-cap US stocks (as represented by the Russell 2000 index) were down 30.61% for the quarter, while non-US stocks (as represented by the MSCI EAFE index) fell 22.83%.
- Though it ended up with a gain for the quarter, the Bloomberg Barclays Aggregate Bond index (the de-facto index for bond investors) even had a drawdown of over 6%, due to a "rush to cash" during the most volatile days in which the demand to sell even the most credit-worthy bond issuances outpaced the demand to buy, causing prices to swoon temporarily.
- From a non-markets perspective, about one in five people in the U.S. have lost jobs or had their hours reduced and the medical toll due to the virus has been daunting.



How Do We Respond?

As Pete noted in his email to our clients in mid-March, one of our main investment guiding principles is that God wired us to be emotional human beings, which leads to investors having the propensity to be irrational in the short-term. I will admit that I found myself questioning my decision to begin the account with an initial lump-sum as opposed to dollar-cost averaging. In the grand scheme of things, though, it's important to note that investing in equities always provides opportunities to second-guess (or third, or fourth, or…) your decisions. If you try to time things and buy "too early," you'll feel regret watching the barrage of red numbers on your screen. If you try to time things and buy "too late," you'll regret not having the gumption to buy "when you felt it in your gut." For both attempts at timing the market, hindsight bias, where we try to re-write our own thinking to match what actually ended up happening, runs rampant.

For Abe's 529 account, we probably have two decades of contributions to make and as we get closer to actually needing the funds in the account, we plan to update our asset allocation to include more fixed income. Portfolio management requires a view of when the funds in the portfolio will be needed and matching those needs to certain parts of the portfolio (usually cash and short-term bonds.) At the beginning of every meeting, one of the first questions we ask is "Are there any short-term needs from the portfolio that we don't know about?" – this is asked to ensure that we do not need to sell any equities during chaotic periods like these past couple of weeks.

For retired clients making net withdrawals from portfolios, rebalancing is the closest thing to making additional contributions and taking advantage of equity downturns. Rebalancing shouldn't be an emotional decision, as difficult as that is to practice. Investing is not like racing; there's no "green flag" to signal that all is clear. By the time good news is more rampant as it relates to COVID-19 (from both a health and economic standpoint), the market will probably have bottomed a bit before (though it's a good idea to remember that even before this virus came into being, "good news" was hard to find from our media outlets!)

It can be uncomfortable to rebalance, especially if it feels like wading further into the "unknown" by selling some stability (funds that have outperformed – most recently, high-quality fixed income investments) and purchasing what may have recently been more volatile to the downside. However, as long as risk tolerances are continually discussed and are in still in line with the plan we've set forth, some of the emotions related to rebalancing should be alleviated.

Like Abe's 529 account, the same investment principal applies to your portfolios – the equities (stocks) you hold are intended to be long-term investments that help protect you from inflation. The reason stocks have provided the opportunity for greater substantial returns (over bonds or cash), is because they have substantially greater short term risk (volatility).

To re-iterate from Pete's prior email, we do not know the duration and "final answer" on how this all shakes out. We are not epidemiologists (and don't play one on TV!) and do not know how deep this dip both in economic activity and in equity markets will be. We do know, however, that your financial plans were not built solely on the levels of returns (higher than average) and volatility (lower than average) of the decade prior to this year, meaning that volatility and bear markets are a feature, not a bug, of investing for the long-term.

Silver Linings

By: Jimmy Roth
Wealth Advisor

Growing up, I was always fascinated with astronomy and space exploration. In fact, when I was in 5th grade I was lucky enough to visit Cape Canaveral and witness the Space Shuttle carry the very first piece of the International Space Station into orbit. The launch itself took place in the middle of the night and I will never forget that sensation of awe as I watched the countdown clock reach zero. As the shuttle roared off the launch pad, the sky quickly morphed from pitch black to broad daylight. The sound was deafening and sheer power of the soundwaves thundering across the lake gave the sensation of someone performing CPR on my chest. To date, it is one of the coolest experiences of my entire life.

It's easy to forget or misplace the wonders of man's ingenuity. Think back to the late 1960s when we put on a man on the moon. Back then, those astronauts sat atop the Saturn V rocket, one of the biggest ever built. It was nearly 36 stories tall, weighed roughly 6.2 million pounds, and generated about 7.6 million pounds of thrust at launch (for reference, it created more power than 85 Hoover Dams). What's even crazier is that the computer which landed Apollo 11 on the moon was about as powerful as a contemporary pocket calculator. Incredible.

As smart as the engineers were back then, there was still so much fear and risk due to the unknown. Most of their concerns seem very tangible and reasonable - what if something goes wrong during a launch? What if the calculations are off? What if an astronaut gets hurt or sick in space? What if there is a mechanical failure on the spacecraft during the mission? (i.e. Apollo 13).

Then there were other concerns that derived from the fact that we just didn't know what else was out there. For example, could it be possible that there are viruses or bacteria in space? And what if an astronaut somehow catches a foreign virus and brings it back to earth? We might laugh at that question today given what we now know about space exploration, but back then it was a very real concern. In fact, it was such a real concern that when the Apollo astronauts returned home from a mission, it was commonplace for them to be quarantined away from people for three weeks as a precaution against an uncertain threat of a contagion.

The idea of being isolated in quarantine is nothing new, but it has somehow always felt like a practice that was solely intended for an astronaut or a laboratory scientist in a movie; you never think you'll be the one to undergo a quarantine yourself. And in the cases of the Apollo astronauts, they weren't able to spend their quarantine time with family, much less stay in their own homes. (They also didn't have the internet, but I figure that goes without saying).

Fast forward to today. Here we are, most of us are operating from home as we adapt to this strange season of self-quarantining or "social distancing." It's odd, isn't it? It's a shock to our norm. Simple tasks that we have grown accustomed to doing on a daily basis have been disrupted and that tends to make us uncomfortable. But unlike the Apollo astronauts, we have the luxury of being in the comfort of our own homes.

We have the internet (that's a huge bonus!), we can stream countless hours of TV shows on Netflix, we can still buy groceries (or have them delivered), we can still pick up dinner from restaurants (or also have it delivered), and we can still take walks or bike rides (so long as we stay 6 feet apart from others). There are silver linings to be found in this time of social distancing.

Virtual conferencing applications like Zoom and FaceTime have given us the ability to connect with others in a time of isolation. Every Monday afternoon, I watch my two and a half year old, Kaylee, attend her weekly dance class by way of Zoom from our living room and she loves it! We are also able to connect with our small group at church each Sunday morning as well as livestream our Pastor's sermon. Sure, it's not the same as being there in person, but I'm so grateful for the ability to still connect with people. I'm sure the Apollo astronauts would have enjoyed having Zoom back then.

Some other silver linings I've noticed during this season - I have gone on more walks with my wife and daughters than I can count. And while we are out and about, I see many others (don't worry, all from a safe distance) doing the same – enjoying this newfound time with their families. On top of that, I exchange a friendly wave with nearly every driver who passes us (I know, that's already a common practice here in Texas, but it happens almost every time we pass a car now). I have seen teachers, families, and friends organize car parades and drive by houses of those they love so they can shout, "Happy Birthday!" or simply say, "Hi, I miss seeing you!" I have received phone calls from friends I haven't spoken within months, and my wife and I have built countless Lego castles for Kaylee's dolls (all while our newborn daughter, Maggie, snoozes on). Evenings with our girls are filled with music, dancing, games, and stories. While the headlines paint a frightening picture of the world outside (and it is a bit scary), I'm relishing the precious family time that's taking place within my home. Sure, the circumstances are strange, but I wouldn't trade these moments with my girls for anything.

In the meantime, I continue to see and believe in both the kindness of people and the ingenuity of man. There is a famous line from Mr. Rogers that Sandi and I use when talking to our daughter, Kaylee, about what's going on in the world. He famously said, "When I was a boy and I would see scary things in the news, my mother would say to me, 'Look for the helpers. You will always find people who are helping.'" If you look closely in the news, you will find people across the world doing amazing things to help others in this time of uncertainty and need. Schools are still finding ways to provide pick-up meals to families whose kids who depend on them for food, athletes donating large portions of their paychecks to non-profits, food banks, and workers. Companies like Tesla are getting creative and building ventilators for patients out of car parts. Some grocery store chains have set up designated hours so that people in the community who are at-risk for COVID-19 can shop without the fear of being around large crowds. People are sewing homemade masks for medical workers and first responders, and all the while, those first responders and doctors are working tirelessly around the clock to help people who are sick.

This is indeed a strange time and it's easy to feel a sense of hopelessness or even some level of anxiety about what's going on, particularly in isolation. However, I truly believe that this season shall come to pass. There is still a lot of good and resolve embedded within people during these trying times. If we can send man to the moon and back during the late 1960s, consider what we can do with the knowledge and tools we have today. And as we weather the storm, let us pause for a moment, consider the blessings we have, be thankful, and not take them for granted. As it has always been with prior world events (even odd ones such as this), I believe this is temporary, I believe we will get through this, and I also believe there are going to be a lot of happy and excited people out there when we do (myself included).

I pray that each of you and your families stay safe and enjoy the time you have with one another.

Around The Office Updates

Operations update:

As we previously noted during our email to you mid-March, our office remains open; however, we continue to work with a limited staff physically in the office while others operate from their homes. Additionally, while we have cancelled all in-person reviews and meetings until further notice, we are continuing to conduct meetings by way of phone or virtual conferencing (i.e. Zoom). We will continue to keep in touch with updates if and when the circumstances change. The best way to contact us remains the same – by email or phone.

Sister, Sister!

It is been quite a busy start to the year. Jimmy and Sandi welcomed their 2nd daughter, Maggie Belle Roth, into the world on Jan. 30th, 2020 (almost a week late from her original due date!). Upon bringing her home, Kaylee was a bit skeptical of her new sister but has since come to fully embrace her. While they look forward to the day where they can confidently leave them two of them in a room alone together, there is still some work to be done. (Kaylee recently approached mom and dad claiming that baby Maggie was asking for more Disney princess tattoos). They have their work cut out for them.

Man's Best Friend

As mentioned earlier in the letter, Eric and Ellie welcomed their first son, Abram ("Abe") Martin Johnson, in the world on Feb. 3rd. As for their family, Sprout, the family dog, has taken it upon himself to make sure Abe gets a bath multiple times a day. Everyone is adjusting well as Abe continues to grow and show off his flashy smile!

Spring Is In The Air!

Cindy and Stephanie are each enjoy the spring weather by taking care of their gardens and grandchildren. Prior to the COVID-19 outbreak, Stephanie and her family enjoyed a fun week at Disneyworld where they rode "It's a Small World" over and over and over. We are happy to report that everyone is staying healthy and doing well!

New Hobbies

Pete has taken a small break from making his current guitar to embark on a new hobby that his daughter, Kellie, has gotten into – Legos for adults! Recently, they built a Disney castle and a large robotic excavator. Silly as it may sound, they say the process of building them is wonderfully gratifying and also nostalgic. (It's impressive to see the size and complexity of these sets).

Looking Into Q2

Federal Income Tax Deadline Extension:

As you may have heard, The Treasury Department and Internal Revenue Service have announced that the federal income tax filing due date is automatically extended from April 15, 2020, to July 15, 2020.

Taxpayers can also defer federal income tax payments due on April 15, 2020, to July 15, 2020, without penalties and interest, regardless of the amount owed. This deferment applies to all taxpayers, including individuals, trusts and estates, corporations and other non-corporate tax filers as well as those who pay self-employment tax.

Taxpayers do not need to file any additional forms or call the IRS to qualify for this automatic federal tax filing and payment relief. Individual taxpayers who need additional time to file beyond the July 15 deadline, can request a filing extension by filing Form 4868 through their tax professional, tax software or using the Free File link on IRS.gov. Businesses who need additional time must file Form 7004.

Updates on Regulations and Changes

CARES Act:

On March 27th, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act"), a $2.2 trillion stimulus package meant to assist in the effort to offset some of the economic damage brought about by COVID-19. Like many Americans, I find myself frustrated by partisan bickering and the seeming lack of ability for our elected officials to work with others across party lines, but even though there were the usual attempts to sneak in line-items related to specific Republican or Democrat platforms (also known as "pork",) the CARES Act was able to pass almost unanimously in the House and Senate. Many major groups are represented/aided in the bill: big businesses (specifically related to airlines and cargo industries), small businesses, individuals (retired, employed, or unemployed), state & local governments, hospitals, and more.

Below is a list of items included in the CARES Act that could play a role in potentially adjusting your financial plan, at least in the short-term. As a quick note, though I am a CPA and we consider taxes extensively when working on your financial plan, the below comments should not be considered as "tax advice" in the legal sense, so please discuss with a tax professional for further applicability to your situation.

- **Recovery Rebates**

  Individuals are provided a refundable income tax credit against 2020 income tax of up to $2,400 for married couples filing jointly, while other filers begin with a credit of $1,200 – the CARES Act calls these "Recovery Rebates." If you have children under the age of 17, an additional $500 credit could be provided. These credits are based on the adjusted gross income ("AGI") that you list on your tax returns, so if you made more than $150,000 as a married couple or $75,000 as a single filer, the credit may be reduced or eliminated altogether.

  I use the word "income tax credit" because even though it could be sent to you via direct deposit in your bank account or via check in the mail in the next weeks/months, there's a slightly confusing way that the amount of rebate is being calculated. The initial amount paid will be based on either your 2018- or 2019-income tax return (whichever year you more recently filed), but it will ultimately be "trued up" when you file your 2020 tax return next year. So, for example, if your AGI was more than $150,000 as a married couple in 2018 but you have since retired and will only have $100,000 of AGI in 2020, you will still receive the $2,400 credit – it will just be in 2021 when file your 2020 tax return as opposed to in the next weeks/months.

  As far as we know (and I believe we may still be awaiting confirmation on this), there is no "claw-back" provision if the opposite situation occurs ($100,000 AGI in 2018, $150,000 AGI in 2020) so if you receive a rebate based on 2018, you shouldn't have to pay it back via your 2020 return.

- **Coronavirus-Related Distributions**

  If you have been impacted by COVID-19 in one of a multitude of ways (diagnosis of you or a spouse/dependent with the virus, experience of financial consequences based on job changes due to the virus, etc.) you can make up to $100,000 in distributions from your IRA or 401(k) without the 10% penalty (if under the age of 59 ½) and are eligible to either 1) repay the distribution back to your IRA or 401(k) within three years or 2) be taxed on the distribution evenly over three years. For example, if you need $60,000 from your IRA due to being let go from your job due to economic strains from the virus and decide not to repay the distribution, you can take the distribution and pick up $20,000 in taxable income on each of your 2020 – 2022 tax returns.

  Before automatically going with this option, it would be prudent to review to see if there are other sources of cash that may be more appropriate based on your situation.

- **Waiver of 2020 Required Minimum Distributions**

  The CARES Act removes the requirement for IRA owners to take his/her required minimum distribution ("RMD") that would be taken in 2020 (both for retirement account owners as well as owners of beneficiary IRAs.) This part of the Act is one that we will definitely want to review, as some clients take the distributions purely because they are required to by law as opposed to any specific cash flow need. For the remaining nine months, it may make sense to adjust the source of cash flows if a distribution from an IRA is not necessary for daily expenses and your goals.

  If you have already taken any part of your RMD so far in 2020 and do not need to do so based on the CARES Act, you can rollover that amount back into your IRA if within sixty days of the initial distribution. There's also RMD relief related to the "Coronavirus-Related Distributions" section above. Unfortunately, this rollover is not applicable for owners of beneficiary IRAs.

These are just three aspects of a very large bill that will continue to be digested in the weeks and months to come. If you have any questions about the above or other elements of the Act, please let us know.