Blue Bell

PRIVATE WEALTH MANAGEMENT

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Patience Is Bitter, But Its Fruit Is Sweet

In our summer newsletter we touched on the Brexit vote held June 23rd, a day that will change the course of history. The CNN headline story on June 28th read "A record $3 trillion was wiped out from global markets on Friday and Monday" due to the vote. The story went on to say, "That means more money vaporized as a result of the Brexit crash than in any previous two day period ever according to the S&P and Dow Jones indices."

Aren't you glad you ignored the headlines? Americans are faced with our own major vote in November, an election that carries significant emotions on both sides. Over the short term, stock market levels are driven by emotions, however over the longer term, the market is a fairly efficient vehicle in measuring economic fundamentals. We expect meaningful volatility surrounding the election as emotions boil over ,and like the Brexit vote, we recommend steering clear of the emotional fray as short term emotions are never a reason to alter your investment plan. There are many questions without easy answers.

According to decades of research, behavioral finance experts found that underperformance is caused by a variety of factors including poor timing, psychological traps and misconceptions. We are not behavioral scientists but in our experience most underperformance is caused by fear and greed. These reactions in some instances are actually caused by the sales and marketing efforts of financial product manufacturers and their brokerage agents looking to earn commissions or win sales contests. For commissioned brokers, it is always easier to "sell" what just did well by touting past investment results but often this is not a good indication of what is going to do well in the future. Usually it's the intervention of an ill-timed brokerage sales call that causes investors to experience market timing losses. Others are persuaded by sensationalized media headlines designed to attract more readers rather than provide personalized investment advice.

As we enter the final quarter of 2016, the major investing themes have not changed but rather have intensified. Interest rates remain at historic lows which certainly affects the equity markets. The stock market continues to react to oil fluctuations whose prices continue to remain at relatively low levels but with increased stability over the last few years. Who would have predicted that falling oil prices would be met with such negative market reactions? Gold has had a good year after suffering for the past 3-4 years as renewed fears about the US Dollar continues. The fact is that our dollar has not lost value because on a relative basis it is still considered the most stable currency in the world. Global uncertainty has only strengthened the US Dollar. The Pound Sterling has fallen to 1.26 versus the dollar; an all-time low. The question is not if the dollar will lose value but rather when. While our unemployment level is low as reported by the labor department, the labor participation rate is at the lowest level since the 1970s. Job growth in the US has improved but 50% of America's fastest growing jobs pay under $25,000, a cause for unrest among voters. The growth of our economy has slowed to less than 1% so far in 2016 and the rate of growth needs to improve and is expected to do so in the next few years. The big question is what the Federal Reserve will do with interest rates after the elections. It

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Is Your IRA Distribution Tax-Free? The Answer May Surprise You

In 2015 Congress voted to make Qualified Charitable Distributions (QCD) a permanent part of the tax code. If you have to take a required minimum distribution (RMD) from your IRA account (all of those over the age 70 ½ with traditional IRAs must take them each year), you have the ability to direct that distribution to the charity of your choice tax free. A QCD allows you to make a charitable donation via a direct transfer from your IRA of up to $100,000 annually. As a direct transfer from the IRA to the charity, the distribution is tax free and will not count toward your income tax for the year. The donation must be made to an organization that qualifies for charitable income tax deductions. This is a tax strategy that can help save you money without negatively impacting the charity.

There are several tax benefits associated with making a QCD rather than a regular taxable distribution which must be included when calculating your adjusted gross income (AGI) in any tax year. When a distribution is included in your AGI, income tax on social security benefits can increase, Medicare insurance premiums could rise, and limitations on charitable deductions and itemized deductions could reduce your tax benefit of gifting to charities.

Making a QCD is as easy as contacting the charity of your choice to see who the check should be made out to and then contacting your investment advisor and instructing them to transfer your RMD directly to the charity. The check must be made payable directly to the charity, not the owner of the IRA, or it will not qualify. Most advisors already have forms to do this and simply require a signature. Be sure to obtain the acknowledgement from the charity stating the amount of the donation after you send it and remember, it must be a charity that qualifies for a charitable income tax deduction of an individual.

On Medicare: Open Enrollment Provides an Opportunity for Savings

In recent years under Obamacare, the cost of health insurance on the marketplace has increased substantially. For many, the annual open enrollment period brings notices from insurance companies of price hikes and plan changes. However, for those on Medicare, Open Enrollment offers a unique opportunity for significant savings on health insurance premiums and prescription drugs.

Beginning October 15th, 2016, Medicare recipients can shop for new Medicare Supplement (Medigap) Plans and new Prescription Drug Plans. Medicare Supplement Plans are designed and regulated by the government, therefore all plans are exactly the same from one insurance company to the next. By switching insurance providers, it is possible to save over $1,200 per year in Medigap premiums while keeping the exact same plan and benefits. To do so, a Medicare recipient must apply with the new insurance company and be approved based on health history. Individuals in good health should absolutely check to be sure they have the lowest Medicare Supplement Plan rates.

It is all too important to review prescription drug plans each year during Open Enrollment. Prescriptions Drug Plans (PDPs) are unique to each individual because everyone takes different prescriptions. Therefore, everyone has different copays for their specific "blend" of drugs. Unfortunately, many people do not understand this and simply choose the prescription plan with the lowest monthly premium. This rarely works and is simply a way that insurance companies appeal to cus-

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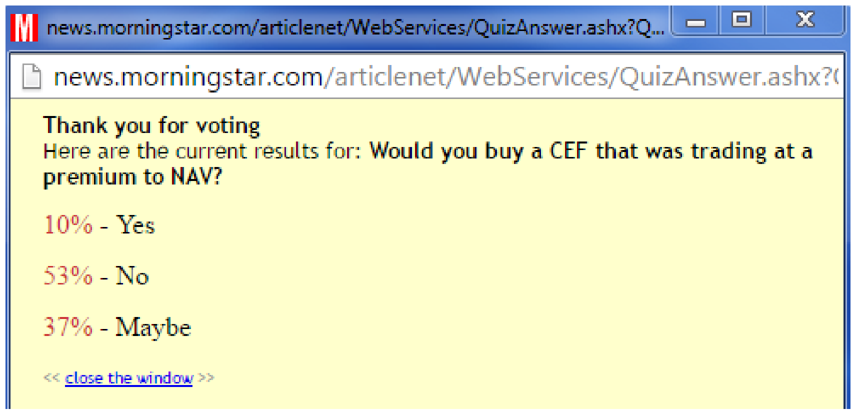
Purchasing CEFs At A Discount To Net Asset Value

Would you ever buy something worth $1 for $1.05 or more?

This is a question Morningstar recently posed in an article about Closed-End Funds (CEFs) on their website. The exact question was, “Would you ever buy a CEF that was trading at a premium to NAV?” Surprisingly, only 53% of respondents answered that they would not buy a CEF at a premium. The screenshot below shows the results from the poll that they conducted.

We would never advise anyone to purchase a CEF at a premium to net-asset value (NAV) and the results of the Morningstar poll show just how many investors don’t understand how these funds are valued or trade. Simply put, we ask why you would ever want to buy a fund for more than its basket of goods is worth, especially when you often can find a fund with a similar portfolio that is trading at a discount of $0.99 or less on the dollar.



Closed-end funds are investment companies that invest in a bundle of securities, similar to a mutual fund, that are publicly traded on exchanges. The Morningstar article has several key points we agree with when it comes to purchasing CEFs including never buying at the initial public offering (IPO) and purchasing at a good relative discount.

An investor would never want to purchase a CEF at the IPO because all of them trade at a premium. This is caused by all of the fees associated with opening a new fund including legal and underwriting fees. As an example, a fund sells a single share at the IPO at $20 and then pays $1 to cover all of the fees to open the fund. This leaves the fund manager to only invest $19 in the fund’s strategy. Therefore, you would have just purchased $19 worth of goods for $20. Investors often purchase CEFs at IPOs due to brokers who receive commissions for selling these funds and currently don’t have to adhere to a fiduciary standard.

A majority of CEFs trade at a discount to their net-asset value according to data from cefconnect.com. As of Sep. 2, there are 544 active CEFs and 415, or about 76%, of all funds trade at a discount to NAV. With the majority of funds trading at a discount to their NAV, using relative discounts helps uncover value in CEFs if you are able to purchase a fund trading at a discount to its average or high 52 week discount. For example, if a fund has a 52 week average discount to NAV of 10% and a 52 week high discount of 15% and is currently trading at a 14% discount, it is trading at a good relative discount as it is close to the highest discount it has been over the previous year. Using statistics also helps when measuring relative discounts and is explained more in the Morningstar article linked above.

Another advantage to purchasing CEFs at a discount is the yield advantage that an investor is able to obtain. The yield advantage from a CEF that pays distributions is a result of purchasing the fund at a discount, which in turn leads to a higher yield when calculated in actual dollars. For example, a mutual fund and CEF both have a yield of 5% to their NAV which is $20. If the CEF is purchased at a 10% discount to NAV or a price of $18, the yield will now be 5.56% or the distribution ($1) divided by the market price ($18). Although this is an advantage of purchasing CEFs at a discount, we never recommend buying a fund solely based on its yield.

These are just three of the several ways investors can profit from investing in closed-end funds. Price appreciation, narrowing of the discount, share buybacks, liquidation, rights offerings, tender offerings, and activism are all ways investors can make money in CEFs.

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should be no surprise that the Fed action or inaction will lead to major volatility in the US and world markets.

The most important thing to focus on is the long term growth of the companies we invest in, which is the true driver of stock market returns. Remember that over the short term, equity markets react to emotion, and over the long term equity markets react to fundamentals. Don't allow short-term emotional decisions and market movements derail your investment returns.

As investors age, it is natural for fear to play a growing role in their investment process. However, millennials have the opportunity to invest free of these fears as their investment time horizon may be decades. In the past, it was not fear that should have deterred these young investors but rather fees, commissions and other charges which hit the smallest accounts the hardest. The high fee dilemma is no longer a factor when invested properly with the right advisor. I encourage everyone reading our newsletter that knows a young investor just getting started to call and ask about our recommendations.

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tomers. The problem with doing this is that while you may have a lower monthly premium, your prescription copays are probably significantly higher than they would be with another company. Each year prescription plan premiums, copays, and deductibles may change; bringing an opportunity to change plan providers and save money.

When looking for new plans during Open Enrollment beware of insurance companies who advertise packaging Supplement Plans with Prescription Drug Plans. This typically leads to higher than usual prescription copays. Individuals on Medicare should consult with an unbiased professional who can help them navigate the Medigap and Prescription Drug Plan marketplace.

Reminders

- If you mail a check, please make the check payable to "Charles Schwab & Co, Inc." with your account number written on the check.
- Please let us know if you hold any IRA money outside of Schwab so that we may include this into our RMD calculation for 2016.
- Talk to your children about the benefits of starting a Roth IRA.
- SAVE NOW! Please consider setting up online access to view your accounts online and to receive your statements and trade confirmations electronically.