Mench Financial, Inc.

Market Thoughts

(513) 745-5111 Fourth Quarter 2021

A Crucial Investment Lesson From A Difficult 20 Years

The commemoration of 9/11 and pullout of U.S. troops from Afghanistan marked the passing of 20 difficult years. Historians will debate the lessons to be drawn from this tumultuous time for decades to come. For investors, however, a crucial investment lesson to be drawn is clear: In the past 20 years, amid the tumult and difficulties, broadly diversifying paid off, and quite convincingly at that!

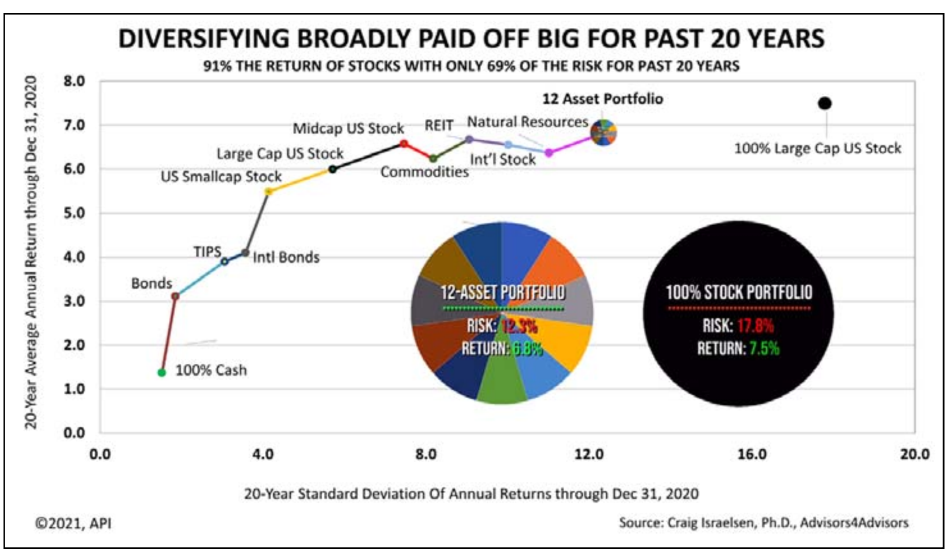
These are the chief findings of a study of the 12 asset classes for which risk and return data are available for at least 20 years. The author of the study, Craig Israelsen, Ph.D., is a professor of finance for over three decades and an expert on portfolio design.

According to Dr. Israelsen, the Standard & Poor's 500 stock index averaged a 7.5% return annually for the 20-year period ended December 31, 2020 and had a standard deviation – a measure of its risk – of 17.8%. In contrast, a broadly diversified portfolio comprised of 12 assets equally weighted delivered 91% of the return of stocks but with only 69% of the risk.

A portfolio with 12 equal weightings of different investments had a standard deviation of 12.3 and a return of 6.8%. That's a good tradeoff for investors: accepting about 10% less return with a 30% reduction in volatility.

It's clear evidence that, even over a 20-year period of world-shaking events, a strategic approach of broad diversification worked.

A one- asset portfolio having 100% in a high-risk, high-reward investment, like stocks, averaged a strong 7.5% annualized return, but you would have had to endure wild swings in the value of your portfolio that annually averaged 17.8%. For example, in the five-week Covid bear market of February-March 2020, instead of



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Stocks Averaged A 7.35% Premium Annually Over T-Bills For Past Two Decades

The stock market has been breaking new record highs for nearly a year now, and stocks are high-priced by some traditional historical measures, such as trailing 12-month earnings. With some pundits saying stock market risk is high, this is a good time to note how investors have been compensated for taking the extra risk of investing in stocks instead of parking cash in a so-called riskless asset like 90-day Treasury bills.

Stocks, as measured by the Standard & Poor's 500, in the 20 years ended June 30th, 2021, averaged an 8.61% annual return, compared to the meager 1.26% annual return on a the risk-free 90-day U.S Treasury Bill.

Since the T- Bill is backed by the full faith and credit of the U.S. Government, it is considered a riskless investment -- while the value of stocks is subject to ups and downs and, in theory, your entire investment could be lost in stocks. Subtracting the return on T- Bills from the return on stocks, the resulting 7.35% is the premium paid for taking the risk of owning U.S. stocks over the 20-year period. To be clear, investing in America's 500 largest publicly-held companies earned investors an average of 7.35% more annually than a risk-free investment.

This 20-year period encompassed three frightening bear markets -- the tech stock crash of 2002, the financial crisis of 2008, and the Covid downturn of early 2020. Past performance is no guarantee of your future results and that, paradoxically, is precisely why investors are paid a premium for owning stocks. Yes, stocks are risky and that's why they have had a higher return than guaranteed investments throughout history.

T.S.M.

Making A Life-Changing Financial Difference To A Spouse And Needy Loved Ones

Tax law and estate planning might bore you to death, but this brief tip could make a life-changing financial difference to your surviving spouse, and other loved ones, including disabled and chronically ill family or friends, as well any minor children in your life.

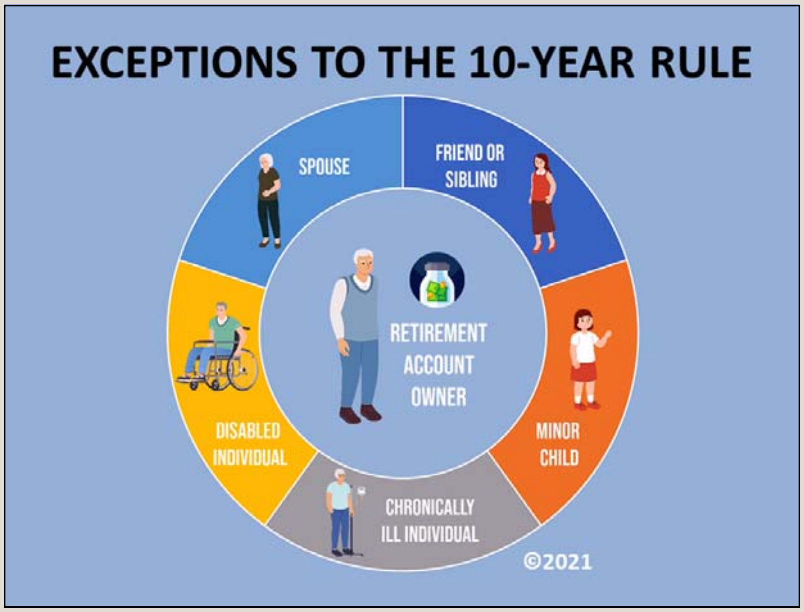
These individuals are among the five exceptions to the usual distribution rules on the inheritance of assets in IRA, 401(k), or other federally qualified retirement plans.

New rules, that went into effect on January 1st, 2020, with the enactment of The Secure Act, require the beneficiary of inherited IRA or 401(k) accounts to deplete the money in those accounts within 10 years. It was a technical change that many overlooked in the rush of tax law changes that occurred in 2020 during the pandemic. But it made a big difference in tax planning.

To be clear, until 2020, beneficiaries of an inherited IRA or 401(k) were not required to liquidate an inherited account within 10 years, as is now required, which had left open a major tax break: They had the option to stretch out distributions over their actuarial life expectancy, thus, leaving the assets to compound tax-free for a much longer period. The 10-year mandatory distribution rules carved out some key exceptions for certain individuals that now require attention, if you intend to pass on your retirement plan, IRA, or other qualified plan assets to a spouse, chronically ill or disabled individual or minor child.

For a disabled individual, who inherits federally qualified retirement assets, for instance, stretching out distributions over decades could transform the inheritance into an income stream for life. The same is true for a widower, chronically ill individual, or minor child that inherits your retirement account.

In addition, a fifth exception to the usual distribution rules applies to a beneficiary that is less than 11 years younger than the retirement account owner. A sibling or friend who is 10 years or less your junior, who inherits qualified retirement account assets, also may use their life expectancy -- instead of taking required distributions over 10 years.



If you own a sizable IRA, 401(k) or other qualified account, and your beneficiary is your spouse, a friend or sibling 10 years or less younger, an individual with a disability, chronic illness, or a minor child, the five exceptions to the 10-year rule pose complicated tax planning as well as legal and investment issues requiring personal advice from a professional that is beyond the scope of this article. ●

Why Now's A Great Time For A Financial Crisis Plan

For the five years through June 30, U.S. stocks were the No. 1 performing investment of major securities indexes! The S&P 500 index more than doubled in value, despite the pandemic! Remarkably, U.S. stocks were No. 1, not only for this five-year period through June 30, 2021, but for the past five five-year periods ended June 30! And, as the end of the third quarter neared, the S&P 500 kept breaking records.

This is precisely the right time to ask yourself: What could go wrong?

The stock market has been treating American investors to outsized gains year after year, and the party could continue -- the good times could roll for another five years or get even better! As professionals, however, we believe it's wise to plan for a stock market slump, to plan what you would do if things go wrong with your business, your job, or God-forbid, your health.

With the stock market and housing values sharply higher than a year ago, your net worth may be higher than ever, making this precisely the right moment to write a crisis plan. Your worst nightmare may be running out of money when you're older,

2021 Year End Tax Planning: Higher Stakes And More Confusing Than Ever

Year-end tax planning is more important than usual because it occurs concurrently with a turning point in U.S. tax policy. For the first time in 40 years, taxes on income and wealth transfers are headed higher.

Exactly what's about to happen – which provisions of the estate and income tax laws will be revised and the financial impact on high income and high net worth individuals – is uncertain. It depends on Congress, politics, the economy and financial markets, thus making it impossible to predict.

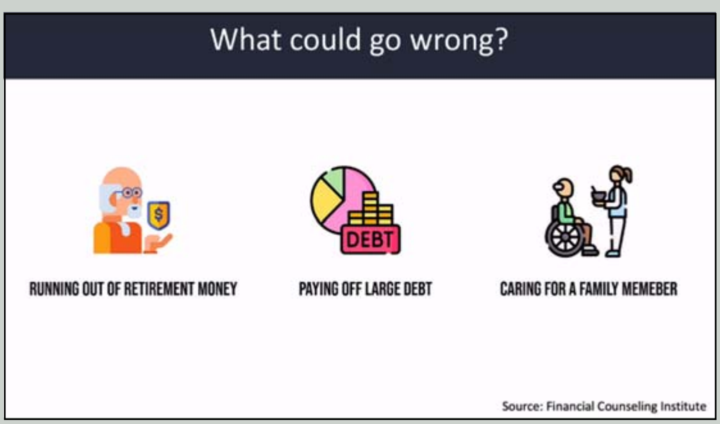
President Joseph R. Biden, Jr., was elected running on a platform that included a proposal to slash the estate tax exemption accorded individuals from $11.7 million to $3.5 million. By early September, however, fears of an imminent hike in estate taxes dissipated. Congress was expected to do nothing to change current estate tax law. Why?

Doing nothing is politically expedient. Neither party would be faulted for letting current lapse. The "sunset" of current estate tax rules would mean the 2021 individual exemption of $11.7 million would continue to rise with inflation annually until December 31, 2025. Starting January 1, 2026, however, the individual exemption from estate tax would revert to about $6 million (assuming inflation does not sharply escalate).

The $11.7 million exemption currently accorded individuals $23.4 million for couples – would be slashed by more than 50% – if Congress does not act. For estate planning purposes, individuals with taxable estates can relax a bit but need to stay informed through the end of 2021, just in case the situation changes.

Meanwhile, federal income tax hikes on high income individuals – specifically, tax-filers with more than $400,000 of income, are expected to be enacted by the end of 2021. President Biden campaigned on a proposal to raise income taxes on individuals with more than $400,000 of annual income. This makes income-tax planning more important while complicating the right moves to make now, in preparation.

This is a timely warning that year-end tax planning in 2021 will be a cliffhanger. It requires the attention of high-income/high-net worth individuals now. While details of the coming tax hikes are impossible to predict, one thing is certain: planning for the complex matrix of possible changes to the Tax Code, starting right now, would be smart. ●



or who will care for a child with special needs after you're gone. Or perhaps you've been prone to selling stocks after market plunges?

Your worst financial nightmare is based on your experiences and personality characteristics. So everyone has their own very personal reaction to life's risks. Even if your financial future is looking bright at this moment, writing your crisis plan now, rather than in the throes of a crisis, can help ensure you will continue to sleep soundly even if your worst financial nightmare were to come true. That's why now is the right time for financial crisis planning. ●

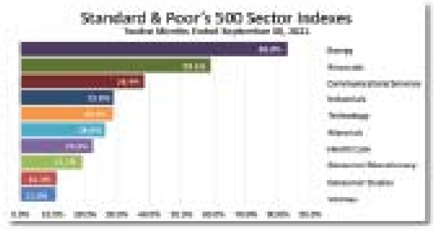
Market Data Bank: 3rd Quarter 2021 Ψ

S&P 500 SOARED AGAIN

For the quarter, the S&P 500 eked out a gain of 0.6%. It was the sixth consecutive quarter of gains since the -19.6% quarterly loss in 1Q2020, when the pandemic struck. Between the March 23, 2020 bear market low and end of 3Q2021, the S&P 500 total return, which includes dividends reinvested, was more than 60%.

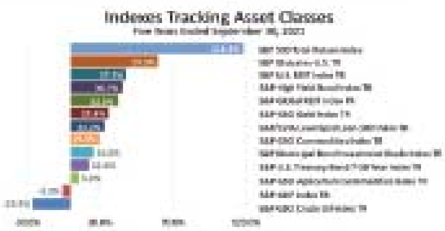
A 12-MONTH WALL OF WORRY

The S&P 500 gained 30% in the 12 months ended Sept. 30, 2021. The consumer economy, which accounts for 70% of gross domestic product growth, remained very strong, even as a surge of inflation, supply-chain bottlenecks, and price-to-earnings ratios above the historical norm raised doubts and fears.



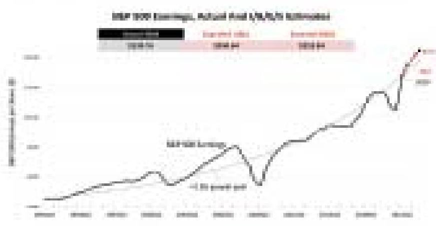
INDUSTRY SECTORS

Since the pandemic hit, tech was No. 1 of the 11 S&P 500 industry sectors for four consecutive quarters, but for the last two quarters it was a middling performer. Such shifts in leadership are not reliably predictable, which is one reason why rebalancing your portfolio can be so important.



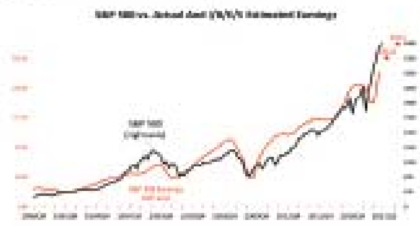
INDEXES TRACKING 13 ASSET CLASSES

Of these 13 indexes tracking a diverse group of investments, No. 1 by far for the five years ended Sept. 30, 2021, was the S&P 500. That's why U.S. stocks are the growth engine of retirement portfolios. The S&P global index excluding the U.S. returned half as much as U.S. stocks. It was a difficult period for bonds.



EARNINGS EXPECTED TO RISE

In 2020, actual earnings of the S&P 500 companies were $139.76 per share. Expected earnings in 2021, according to Wall Street analysts' estimates compiled by Institutional Brokers' Estimate System (IBES), are $200.64 per share and are expected to shoot up to $219.94 for 2022.



EARNINGS DRIVE STOCK PRICES

To show how earnings drive stock prices, the S&P 500 total Return index is added in the black line. This shows the strong correlation between stock prices and corporate profits. The 2021 and 2022 earnings forecasts, in the red dots, pull the black line higher, demonstrating that earnings drive stock prices.

Past performance is never a guarantee of your future results. Indices and ETFs representing asset classes are unmanaged and not recommendations. Foreign investing involves currency and political risk and political instability. Bonds offer a fixed rate of return while stocks fluctuate. Investing in emerging markets involves greater risk than investing in more liquid markets with a longer history. Indices are unmanaged and not available for direct investment. Investments with higher return potential carry greater risk of loss. Actual annual sector performance data from Standard and Poor's.

A Crucial Investment Lesson

(Continued from page 1)

suffering the 33.9% drop in value on the all-stock portfolio, the 12-asset portfolio suffered a much more tolerable 21% loss. Wild ups and downs make investors more prone to selling at market bottoms.

To better understand this concept so crucial to investor success, the multicolored line charts the standard deviation and return of each of the 12 asset classes for the 20 years ended December 31, 2020. Each dot plots the risk and return annually averaged for an asset class.

The risk and return statistics all are based on indexes that track the 12 assets. The 12 assets are tracked by Dr. Israelsen because they form a broadly diversified portfolio, meaning they have different characteristics that can be measured statistically. In addition, they are indexed and, thus, enable a low-expense investment management approach.

Starting with the least volatile of the 12 assets, the multicolored line shows what each of the 12 assets added to the portfolio. Adding each of the 12 assets in equal amounts for the 20-year period created the very favorable risk/return curve in this chart. The combination of all 12 asset classes yielded the most efficient portfolio, compared to any combination of one or more assets.

Strategically investing in a broad set of assets worked even during one of the most difficult 20 years of the modern era. ●