First Merchants
Private Wealth Advisors

PRIVATE WEALTH *perspectives*

VERSION 17.3

FIDUCIARY SERVICES

Estate Planning 101 - Trusts

Think about duct tape for a moment. Its original purpose was to seal the joints in the ductwork of your home heating/cooling system. But today, most duct tape is purchased because of its many other uses, such as making quick repairs, securing packages, patching holes, and generally just holding things together.

Trusts are the duct tape of the estate planning world. They are a versatile tool with many uses beyond just passing assets to your heirs.

Asset Management

Considerable time and skill are needed to properly manage your investments in today's ever more complicated markets. In addition, the danger of mental or physical disability as we get older is very real. Placing your assets in a trust can provide professional assistance to you now, and prudent and safe asset management in the event of your disability or death.

Special Needs

It is not uncommon for a child or other relative to have special health, education, or other needs. You can create a trust to see that those needs are met. This will ensure that any assets you place in trust are used exclusively to benefit your beneficiary, regardless of whether you are there to help or not. In some cases this can be coordinated with any government benefits they are already receiving to provide the best possible results without depleting trust assets unnecessarily.

Flexible Provisions

For many other reasons one or more of your heirs may not yet be ready to receive a large inheritance all at once. Or perhaps you are concerned that a gift to them will end ultimately end up in the hands of someone else. A trust can distribute income and principal gradually over time to your beneficiaries to help them learn how to deal with wealth gradually and to reduce the risk of your hard earned wealth being misspent or misappropriated.

Let Us Help

If you want to know more about how a trust might be of benefit to your financial situation, please feel free to contact First Merchants Private Wealth Advisors for a consultation.

David Forbes

INVESTMENT MANAGEMENT

Is the Amazon effect befuddling the Fed?

Inflation Fears

The Federal Reserve's open market and discount rates are set by its Open Market Committee (FOMC), but for convenience, throughout this piece I will refer to it as "the Fed." And as my colleague Jamie Wright has noted more than once, the Fed is walking a tightrope. It appears to us that the Fed dearly wants to get interest rates up to a "normal" level, whatever normal means these days, because members of the Fed are acknowledging the damage ultra-low rates have done to savers and perhaps to the economy as a whole. Heading off incipient inflation has been a key reason for the Fed to raise rates, and the inflation numbers just haven't been behaving. Inflation continues to trend below the Fed's target, and again as Jamie has noted, deflation still is not out of the question. So what's going on?

There are many things that go into making inflation forecasts, but prices, and price trends, play a prominent role. And in what sometimes is dubbed "the real economy," upward pressures on prices do not appear strong. Yes, there are certain economic sectors and industries where inflation seems to be a persistent issue, education and health care as examples (is it just coincidence that for decades, those two areas have had a high degree of government involvement or, as some would maintain, interference?). However, overall price pressures appear subdued. It is my opinion that the Fed may not be fully in tune with some of what is happening in "the real economy". This helps make the case for the Fed's board to have fewer economists and academics and more members who actually have run businesses, but that is for another article

The Pressure on Price

While Amazon may be the most prominent current example of a company with a relentless drive to hold down prices, it certainly is not the only or even the first to do so. Wal-Mart may be the best contemporary example in brick-and-mortar retail, but even before that company was Kmart and even Sears and so on back in time. What is relatively new (as in the past couple of decades) is the emphasis on "everyday low prices" in almost every line of business. As companies

and businesses have invested in more efficient procurement and distribution systems and e-commerce operations, price competition has gotten sharper. Now that smart phones are ubiquitous and consumers can immediately compare prices across a myriad of options, it is nearly impossible to hide or disguise price differences. The spread of e-commerce allows nearly everyone to be a “price discoverer” and that tends to hold prices down.

This is not happening only on the retail level; it is happening virtually everywhere throughout the supply chain. A very good example is cloud computing. In the fall of 2014, at Northern Trust’s FOCUS Conference the head of Investor Relations for Oracle, and he noted that his company firmly believed then that the cloud would be deflationary. That indeed is playing out. The cloud needs less hardware and maybe even less software to provide the same total volume of data creation, manipulation, and storage. The companies that sell that hardware and software now compete brutally on price. It is likely the cloud will keep a lid on many technology costs and prices for years to come.

What About Wages?

You may ask yourself, if the official unemployment rate is very low; won’t that lead to higher wages and therefore higher prices and therefore higher inflation? Possibly, but far from certainly. A key reason unemployment is low is that increasing numbers of people are leaving the workforce, voluntarily or otherwise. While there may be pockets of the economy where workers and potential workers are in such short supply that they can bargain for higher wages, that is not universal. In fact, the shortage of available workers is leading businesses to invest even more heavily in technology, which could simply speed up the downward spiral in the labor participation rate. There are ripple effects; the affected will spend less, making companies compete even harder on price, which means inflation will be tamped down just that little bit more, which means the Fed—well, see the first paragraph.

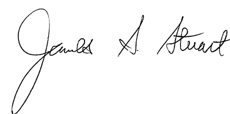
So Where Does That Leave Us?

This is not to suggest that an economic catastrophe of some sort is looming. Outright sustained deflation would be catastrophic, but sustained low inflation more likely would be “only” bothersome. It might make it more difficult for workers to demand raises, and it might appear to most that the economy as a whole would merely be “muddling through.” In comparison, that would be better than the depression that widespread deflation would bring. From an investment standpoint, if the past several years are any indication, sustained low inflation keeps bond prices relatively high and bond yields relatively low. The hunt for yield quite clearly has led to price inflation in at least one area, equity investments. In simplest terms, this has benefitted the asset rich over the asset poor. Ironic that former Fed Chair Ben Bernanke’s public espousal of higher equity prices as a way to stimulate the economy probably has generated results very different from his original intent. No governmental body in the world can repeal the law of unintended consequences.

I do not envy the Fed its job, but it looks like it will be a struggle for them to raise rates to “normal” levels without risking some unintended negative effects. There has been talk that low interest rates are the “new normal” in fixed income, which has led to further talk that current stock valuations that are above historical levels also are a “new normal.” There was similar talk before the tech, commodity and financials bubble burst. “New normals” rarely end up being normal and at the moment we are cautious when buying equities. We prefer to invest in those solid companies and/or industries where we believe we can find long-term value without overpaying for growth that may not materialize or buying stocks whose prices have been driven primarily by either the mad dash into indexing or the ultra-low rates of the last decade.

We will continue our efforts to be good stewards of our clients’ capital and we will continue to seek out those investments that we believe give you, our clients, a fighting chance to receive a competitive economic and financial return without running risks we believe are imprudent. It will take time and patience, and it won’t be flashy or exciting, but we believe in the long run it will work. Thank you for your business, and if at any time you have questions or want to discuss more of our services, do not hesitate to contact us.

NOTE: Any reference in this piece to an individual company should not be construed as a recommendation to buy, sell, or hold that company’s stock.



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