

## MARCH 2019 INSIGHTS

### INVESTMENT OVERVIEW

#### ROUNDTABLE ROUNDUP

Following one of the worst market declines in a decade and strongest subsequent starts to the year since 1987, McShane Partners hosted its annual portfolio manager panel event in early-February featuring five prominent panelists, each experts in their respective asset classes, with the express intent of facilitating a debate over positioning portfolios going into a controversial 2019. The panel succeeded in highlighting diverse perspectives, while also leaving investors unsure of a clear path going forward. As such, the Investment Team has summarized the salient topics into pertinent conclusions regarding the divergent expectations for economic growth, the various “sparks” that might start a recession, and the cloud surrounding the Federal Reserve.

This year’s panelists were surprisingly constructive on the market overall, despite the shocking correction experienced in the fourth quarter of 2018 (“4Q18”). That said, there was consistent acknowledgement of the precarious nature of certain data points, including the burdensome leverage (i.e., debt) across all major areas of the global economy that could be extremely uncomfortable to unwind.

In our most recent quarterly economic overview presentation, the Investment Team reviewed the pertinent information from this year’s panel, along with our own proprietary data points, to clarify portfolio positioning going into an uncertain 18-24 month economic cycle maturation.

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### WEALTH ADVISORY OVERVIEW

#### THE UNDERUTILIZED HEALTH SAVINGS ACCOUNT

A Health Savings Account (“HSA”) is a tax-advantaged personal savings account that helps those with HSA-qualified health plans save for out-of-pocket medical expenses like doctor visits, vision and dental care, as well as prescription drug costs. To be eligible to open and fund an HSA, the following requirements must be met:

- You must be covered under a high-deductible health plan (“HDHP”)
- You must *not* be enrolled in Medicare
- You must *not* be claimed as a dependent on someone else’s prior year income tax return

For each year you are enrolled in a high-deductible health insurance plan (“HDHP”), you are eligible to open and fund an HSA. For 2019, the IRS defines a HDHP for an individual as a plan with an out-of-pocket maximum of \$6,750 and a minimum deductible of \$1,350. For a family plan, the out-of-pocket maximum is \$13,500 and the minimum deductible is \$2,700 .

#### WHY A HEALTH SAVINGS ACCOUNT?

Saving to an HSA occurs on a pre-tax basis, similar to a traditional

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#### SPECIAL POINTS OF INTEREST

- [Monthly Index Review](#)
- [Stock & Strategy Spotlight](#)
- [Around McShane Partners](#)

INVESTMENT OVERVIEW

ROUNDTABLE ROUNDUP

DIVERGENT EXPECTATIONS FOR GDP GROWTH

The panel of five portfolio managers held a wide range of expectations for global economic growth, with most managers hugging tightly to consensus expectations of global gross domestic product (“GDP”) growth of **2.0-2.5%**. Our expert commodities portfolio manager panelist laid out a bullish thesis in support of a rebound in the commodity market cycle predicated on **4.0%** global GDP growth spurred by a resolution to trade and tariff wrangling spurring a capital investment expansion cycle having been stalled by conflict and uncertainty about trade policies.

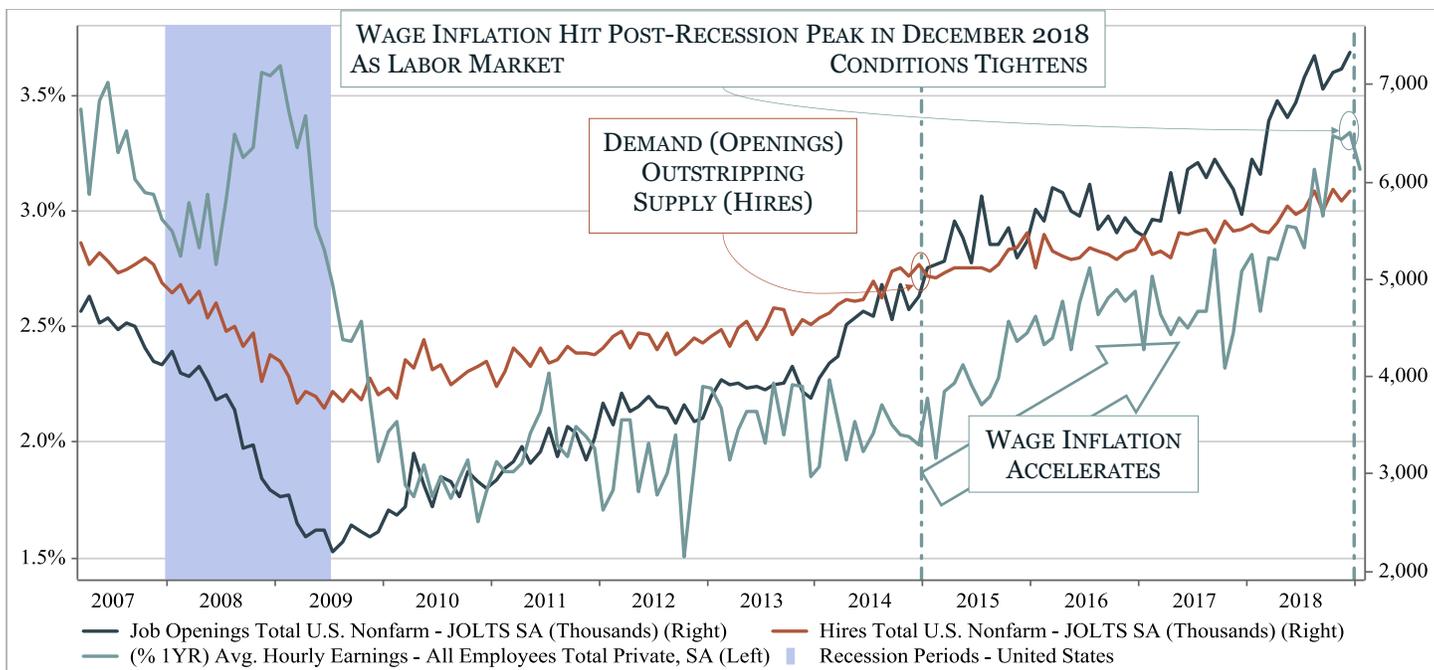
Other panelists felt like **2.0-2.5%** was more reasonable, and since we have yet to see 4.0% sustained synchronized GDP growth seems likely, we are suspicious of any thesis that requires an acceleration in GDP growth to succeed. Alternatively, we appreciated the unique expectation for a strong acceleration in growth and appreciate consensus contradiction. The majority of managers felt a continuation of slow, steady growth and were relatively optimistic about growth and risk in the market. There was one manager on the other end of the pendulum that felt the economy precariously close to a more severe correction given the data points acquired on his due diligence trips to visit with management teams globally.

SPARKS

Our most bullish panelist indicated that wage inflation is the main factor that could spiral the economy toward a recession and one of the main metrics he monitors. For the past few years, we have methodically monitored the labor supply and demand relationship for indicators of inflation. Below, Chart I depicts the causality of wage inflation. The Federal Reserve will face a serious quandary if inflation picks up as it will be unable to simultaneously support the political agenda of a liquidity fueled stock market (modest interest rates) and fulfill its stated goal of controlling inflation (i.e., raising interest rates).

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CHART I: LABOR MARKET CONDITIONS & WAGE INFLATION



Source: McShane Partners & FactSet Research Systems, Inc.

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ROUNDTABLE ROUNDUP

Given unemployment currently sits at **4.0%**, the lowest level since 2000 - excluding the recent Trump trough - with a political agenda assigned to suppress immigration, an obvious solution to the shortage of labor, we find it difficult to believe that we do not see wage inflation acceleration over the next twelve months which should necessitate a monetary policy reciprocation. Given the modest implied expectations for interest rate hikes at this point, the market could react negatively to a more hawkish Federal Reserve.

Given the wide range of outcomes with a cluster around consensus, the obvious path for global GDP growth that a recession is opaque; thus we plan to maintain a balanced approach to economic growth reiterating our long-term assumption for **2.0% GDP growth**, with portfolios positioned for a *deceleration* in growth.

*“The crisis takes a much longer time coming than you think, and then it happens much faster than you would have thought.” - Rüdiger Dornbusch*

UNCERTAINTY AROUND TRADE POLICIES

Counter to our supposition that the constant banter surrounding trade policy was not directly correlated with market moves, many of the panelist felt that a resolution to the global trade predicament would result in an unlocking of pent up capital expenditures and a clearer earnings trajectory for global companies. The consensus was that the uncertainty around the global trade pathway was inducing paralysis at the corporate executive level as well as the individual investor. We maintain that the heightened debt levels, and detrimental demographic trends combined with a global proclivity towards protectionist policies is naturally slowing growth despite society’s best efforts to ignore the inevitable.

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MONTHLY INDEX REVIEW  
USD TOTAL RETURN

DATA AS OF FEBRUARY 28 <sup>TH</sup> 2019	FEBRUARY 2019	2019 YTD	2018	2017
S&P 500®	+3.21%	+11.48%	-4.38%	+21.83%
Dow Jones Industrial Average	+4.03%	+11.62%	-3.48%	+28.11%
NASDAQ Composite	+3.60%	+13.74%	-2.84%	+29.64%
Russell 2000	<b>+5.20%</b>	<b>+17.03%</b>	-11.01%	+14.65%
MSCI Emerging Markets	+0.23%	+9.02%	<b>-14.24%</b>	<b>+37.75%</b>
MSCI EAFE	+2.56%	+9.32%	<b>-13.36%</b>	+25.62%
Bloomberg Barclays U.S. Agg. Bond Index	<b>-0.06%</b>	+1.00%	<b>+0.01%</b>	+3.54%

Source: McShane Partners & FactSet Research Systems, Inc.

ABOUT  
MCSHANE PARTNERS

McShane Partners is an experienced, boutique registered investment advisor dedicated to independent, comprehensive wealth management. Founded over 30 years ago, the firm, from its inception, has had a singular focus: to provide highly customized investment management and financial planning solutions to clients.

*Boutique Firm:*

Being a boutique wealth management firm allows us the flexibility to provide more personalized service and offer unique investment solutions to clients in a Fee-Only environment.

*Team Approach:*

Because each client’s situation is different, the team of advisors is hand-selected to ensure areas of expertise are appropriately aligned with the client’s specific needs and interests.

*Proprietary Investment Research:*

The differentiating factor of our portfolio management process is the proprietary investment research driving the portfolio construction. All investment research and analysis is done entirely in-house by our Investment Team.

INVESTMENT OVERVIEW

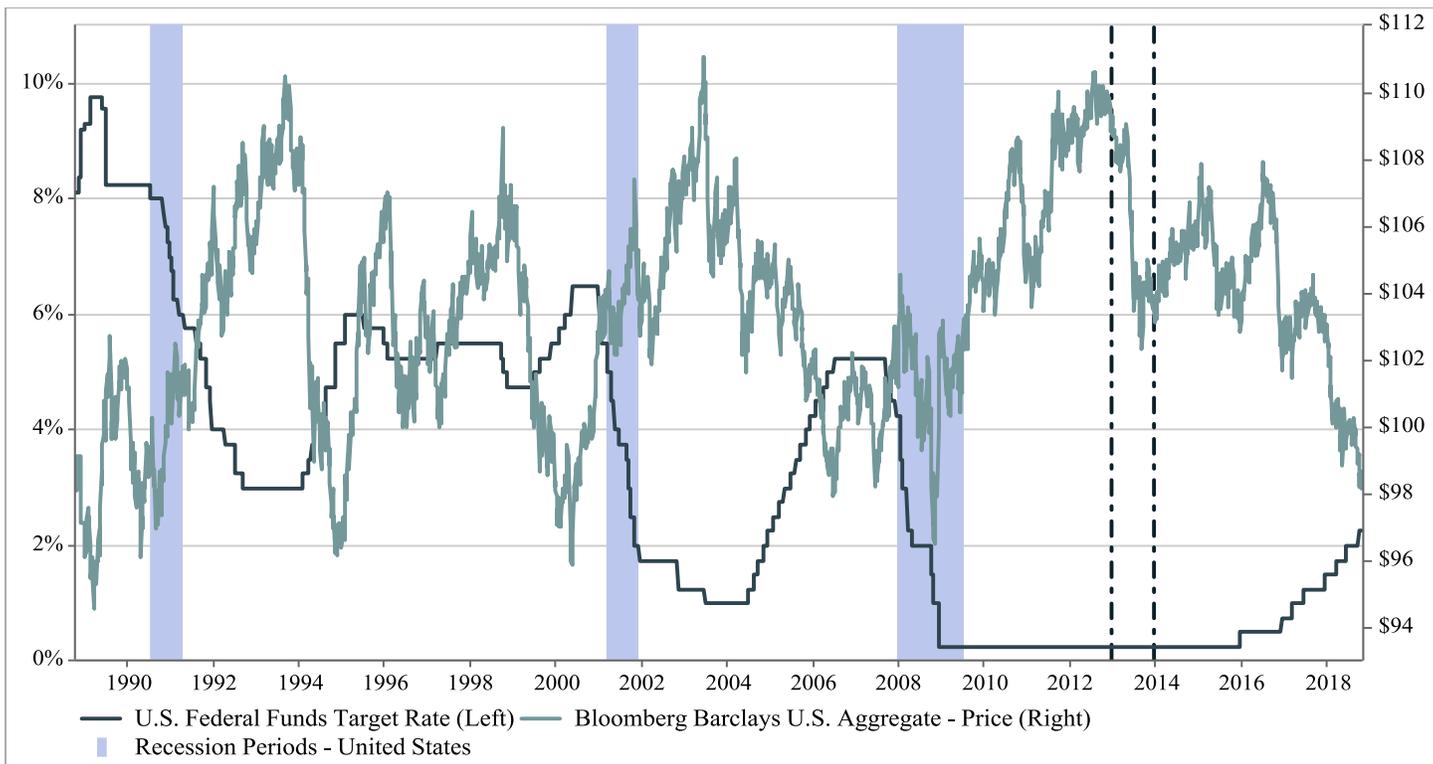
ROUNDTABLE ROUNDUP

CLOUD SURROUNDING THE FEDERAL RESERVE

Each panelist commented on the delicate relationship between the stock market and monetary policy. The power wielded by the Federal Reserve has become a popular point of contention for the media and market pundits. It is our belief that the Federal Reserve will ultimately be forced to adjust rates according to inflation, making it the singular most important wildcard for the year ahead. With consumer products companies raising prices to accommodate higher input costs and workers demanding higher wages, we see modest inflation as inevitable; we are concerned with the simultaneous appreciation of both fixed income and equity assets as signs of percolating inflation. Both are circumstances apt to pressure portfolios and mitigate the customary diversification benefits of the inverse correlation between bonds and stocks.

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CHART II: FEDERAL RESERVE VS. BOND MARKET



Source: McShane Partners & FactSet Research Systems, Inc.

## INVESTMENT OVERVIEW

## ROUNDTABLE ROUNDUP

## STOCK &amp; STRATEGY SPOTLIGHT

NAME	TICKER	2019 YTD
Kraft Heinz Co.	KHC	<b>-30.94%</b>

## DESCRIPTION &amp; INVESTMENT THESIS

Earlier this month, shares of Kraft Heinz Co. (“KHC”) plunged an unprecedented **-27.46%** in a single day after the company reported extremely disappointing fourth quarter 2018 (“4Q18”) and full year 2018 (“FY2018”) earnings results that fell short of consensus estimates, while also providing downward revisions to previously-issued financial guidance for calendar year 2019 (“CY2019”). Adding insult to injury for shareholders, KHC announced that it, in addition to recording a one-time, non-cash write-down/impairment charge of **±\$15.0 billion** related to its Kraft and Oscar Mayer brand portfolios, it would be cutting its quarterly dividend by **-36.0%** from **\$0.625 per share** to **\$0.40 per share** and disclosed that, in October 2018, the company received a subpoena from the U.S. Securities & Exchange Commission (“SEC”) regarding an investigation into the company’s accounting policies and procedures, which resulted in KHC recording a one-time *increase* to costs of goods sold (“COGS”) of **±\$25.0 million** in 4Q18.

The degree to which KHC surprised, shocked, and disappointed investors this past month with its “everything but the kitchen sink” report can be seen in the aforementioned **-27.46%** single-day sell-off in KHC shares, as well as the rapidity and number of associated/corresponding downgrades and price target cuts amongst sell-side analysts covering KHC: according to data from *FactSet Research Systems, Inc.*, investor sentiment has shifted dramatically over the past month, with the number of “Buy/Overweight” recommendations falling from **±62.5%** as of January 31<sup>st</sup> to just **±13.6%** as of February 28<sup>th</sup>.

After reading, reviewing, and analyzing all of the information and data released/reported by KHC, the Investment Team believes that the most alarming - and potentially calamitous - news released/reported by the company regarding the October 2018 SEC investigation appears to be confined to the one-time incident, which is somewhat reassuring to us as long-term shareholders/investors given the relatively limited scope/scale of the associated charge/penalty.

While cutting the quarterly dividend is undoubtedly disappointing, shares of KHC are still boasting an annual dividend yield of **±4.8%** as of February 28<sup>th</sup>: as the company uses the incremental cash flow to accelerate its debt reduction initiatives, KHC should be in a better long-term position to sustain a more reasonable dividend payout ratio through difficult business/operating environments and any impending economic slowdown/downturn. Lastly, the Investment Team finds some comfort/solace in the fact that 3G Capital Partners Ltd. and Berkshire Hathaway, Inc. still have a combined/aggregate **±48.9%** ownership interest in KHC, and both institutions have impressive track records, differentiated thought/investment processes, and longer investment horizons than the public markets. Working alongside the management team at KHC, they are making a long-term decision to get the balance sheet in shape *now* and improve the *future*, long-term business prospects of the company vs. keeping the dividend *too high* to appease short-term shareholders.

The Investment Team believes that, after adjusting our valuation multiples for KHC to reflect a *more conservative* margin profile for KHC going forward and the net impact of the goodwill impairment on historic multiples for industry-level peers over the past **±15 years**, we believe that the current share price accurately/appropriately reflects the broader economic headwinds and industry-level operating risks plaguing KHC and its “Food Products” and “Packaged Foods” peers. While the Investment Team believes that the incremental downside risk is limited at current price levels, shares of KHC are likely to be range bound, and upside potential is likely to be capped, until the company provides additional updates on and/or insights into its ongoing strategic initiatives.

## WEALTH ADVISORY OVERVIEW

### THE UNDERUTILIZED HEALTH SAVINGS ACCOUNT

IRA or 401(k) plan. However, while saving to an IRA or 401k requires earned income in order to make contributions, saving to an HSA does not have the same earned income requirement.

It is common for health insurance providers with high deductible plans to offer HSAs. In this case, the election to participate in the HSA through the employer's cafeteria plan allows the payroll provider to deduct the requested savings amount on a pre-tax basis from payroll, and deposit these funds into the individual's HSA account.

If the health provider does not offer an HSA option, an HSA can be opened at most financial institutions. Contributions can be made at any time during the year by writing a check and depositing these funds to the health savings account. In this case, a deduction from gross income would be taken on the individual's tax returns allowing these contributions to escape federal and state taxation.

It is important to note that while HSA contributions made individually will be not be subject to federal and/or state income tax, these contributions are still subject to Social Security and Medicare tax. However, contributions that are made through an employer's cafeteria plan are deductible for federal, state, Social Security and Medicare taxes.

#### MAXIMUM CONTRIBUTION AMOUNT & DEADLINE

Each year, you may decide how much to contribute to your HSA, though you cannot exceed government-mandated maximums. In 2019, these limits are \$3,500 for an individual (\$3,450 in 2018) and \$7,000 for a family (\$6,900 in 2018); adults over 55 can save an additional \$1,000 to their HSA. While contributions can be made all during the taxable year, the final deadline to make contributions for 2018 is April 15, 2019, the same as IRA contributions.

#### HOW DO I USE THE DOLLARS IN MY HSA TO PAY FOR MEDICAL EXPENSES?

Funds that are withdrawn to pay for qualified medical expenses are tax-free. Withdrawals for nonqualified expenses are taxable and subject to a penalty if you are under the age of 65. Typically, you will receive a debit card or checks linked to your HSA and you can use either to pay for eligible medical expenses. This includes deductibles, copays and coinsurance, plus other qualified medical expenses not covered by your health insurance plan. Be aware that insurance premiums usually cannot be paid for with HSA funds.

#### HEALTH SAVINGS ACCOUNTS VS. FLEXIBLE SPENDING ACCOUNT

Unlike a Flexible Spending Account ("FSA"), any funds remaining in your HSA may be rolled over from year to year, and continue to grow tax-free. This is a huge advantage over an FSA that requires that funds be spent each year or forfeited. However, if you are not covered by a HDHP, the FSA may be your only option to save for medical expenses on a pre-tax basis.

#### HEALTH SAVINGS ACCOUNT & MEDICARE

Once you are over age 65 and enrolled in Medicare, you can no longer contribute to an HSA. However, even though you are no longer eligible to make HSA contributions, you can still use the money within your HSA to pay for out-of-pocket medical expenses. If you use the money on non-eligible medical expenses, you have to pay income tax on that amount (plus a penalty if you are under 65).

#### CAN I INVEST MY HSA BALANCE?

Another benefit of HSAs is they can be invested in a multitude of investment options to include mutual funds, stocks and other investment vehicles. All earnings including interest, dividends and capital gains are tax-deferred within the HSA and if used for qualifying medical expenses when withdrawn, escape permanent taxation.

## AROUND MCSHANE PARTNERS

### 2019 PORTFOLIO MANAGER PANEL EVENT - INVESTING AT THE END OF A BULL MARKET

Thank you to everyone who was able to join us for our 5<sup>th</sup> Annual Portfolio Manager Panel Event this year!



Also, we would like to thank our five prominent panelists who provided and shared their Late-Cycle Investment & Portfolio Strategies expertise! The discussion was timely and the insight proprietary, with positive feedback from presenters and attendees alike.

We hope that those of you who were unable to make the event will join us next year, and we will start to assemble the program and have details regarding next year's event later in 2019.

### FOURTH QUARTER 2018 ECONOMIC OVERVIEW

Thank you to everyone who was able to attend our Fourth Quarter 2018 Economic Overview Webinar!

The webinar will be posted to the website by March 5<sup>th</sup> under the "Featured News" section.

### YWCA'S 2019 ANNUAL FUNDRAISING LUNCHEON

McShane Partners and guests attended the 2019 "We Believe" Luncheon for YWCA of the Central Carolinas. The luncheon brings together over 800 people annually to share in the successes of women, children and families that the YWCA serve. Taiwo Jaiyeoba, planning director for the City of Charlotte, was the keynote speaker this year.

### FOUNDATION FOR THE CAROLINAS



McShane Partners is honored to sponsor the 2019 Foundation for the Carolinas Annual Meeting on April 2<sup>nd</sup> at the Charlotte Convention Center. This is one of our region's premier nonprofit events, the Annual Meeting convenes nearly 1,500 leaders each year from the corporate, nonprofit and civic sectors, providing an unmatched opportunity for networking and fellowship.

The keynote speaker is Jose Andres. He is a culinary innovator, television personality and owner of ThinkFoodGroup, as well as a noted advocate for food and hunger issues. World Central Kitchen, the nonprofit he founded, along with #ChefsForPuertoRico, served 3.5 million meals in Puerto Rico following Hurricane Maria. Andrés and World Central Kitchen also responded to Hurricane Florence here in the Carolinas, feeding first responders and those impacted by the storm. Additionally, he was recently nominated for the 2019 Nobel Peace Prize.

### IN CALIFORNIA WITH CLIENTS

Every year, Daniele travels out West to meet with our clients in the PST zone. At one lunch meeting, the delectable, whimsical dessert feature was enjoyed by all.



## MCSHANE PARTNERS

Wealth management is our only business; therefore, our attention is undivided and our intentions are transparent.

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