MP McShane Partners

June 2023 Insights

Investment Overview

Trends in Real Estate

We recently attended the Nuveen Real Estate Group's annual meeting in Florida providing access to a breadth of extremely experienced professionals across all areas of real estate investing. In addition to checking in on our specific investments, we were able to aggregate critical data points relative to the interest rate cycle, the economy and single family housing dynamics.

The single largest near-term factor impacting real estate is the dramatic, rapid rise in interest rates. Financing is a critical component to real estate investments. Access to and cost of financing has become a major focus for investors as the rise in interest rates not only increased the cost of capital, but it also impacted the regional banking sector (i.e. Silicon Valley Bank and others) in a way that created a glitch in the flow of financing. Managers were scrambling to insure the dependability of existing credit lines. We were relieved to know that Nuveen has a dedicated individual whose only job is to scan and monitor attractive financing so the portfolio managers can focus on identifying attractive assets and managing the real estate portfolios.

While extreme interest rate volatility has slowed down procurement of new assets, returns in medical office space and public storage remain compelling and fueled by powerful demographic trends and scarcity. These sectors are also recession-resistant in our opinion given the non-discretionary nature of healthcare needs and the benefit to public storage. When economic growth slows people rely on public storage units when they have to downsize or abandon their primary residence due to financial pressures.

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Wealth Advisory Overview

Understanding Equity Compensation

Stock options

Stock options allow you to purchase shares in your company's stock at a predetermined price, also known as a strike price, for a limited number of years (usually 10). Like all equity compensation, they encourage you to stay with your employer longer because there's typically a vesting period before the options become exercisable. This means that you must be employed for a certain amount of time — determined by your employer — before you can exercise the option to buy the stock you were granted.

What is the benefit of having stock options? Ideally, if your company is performing well, the strike price of your stock will be lower than its fair market value by the time your options vest. This means you can buy your company stock for a lower price and sell it at the higher fair market value. This can be a significant financial gain if the price of your company stock grows over time. At the same time, if your company stock performs poorly and the price never increases above your strike price, your options can expire as worthless.

Until you exercise your stock, you're not putting any of your own capital at risk, so stock options allow you to have skin in the game without putting money down up front.

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Points of Interest

- Monthly Index Review
- Stock & Strategy Spotlight
- Around McShane Partners

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Interest rates have also created a severe dislocation in home ownership affordability, as can be seen in the chart below. The cost of home ownership is considerably higher than rent. In fact, home ownership is noticeably higher than it was in 2007 preceding one of the largest housing price corrections and associated recessions since the Great Depression. Obviously, there as been steady inflation in the cost of shelter, but the rapid acceleration in home ownership versus rent could signal a major reset in the housing market and real estate investors in single-family dwellings are cautious and going to the sidelines temporarily based on expectations of a price adjustment.

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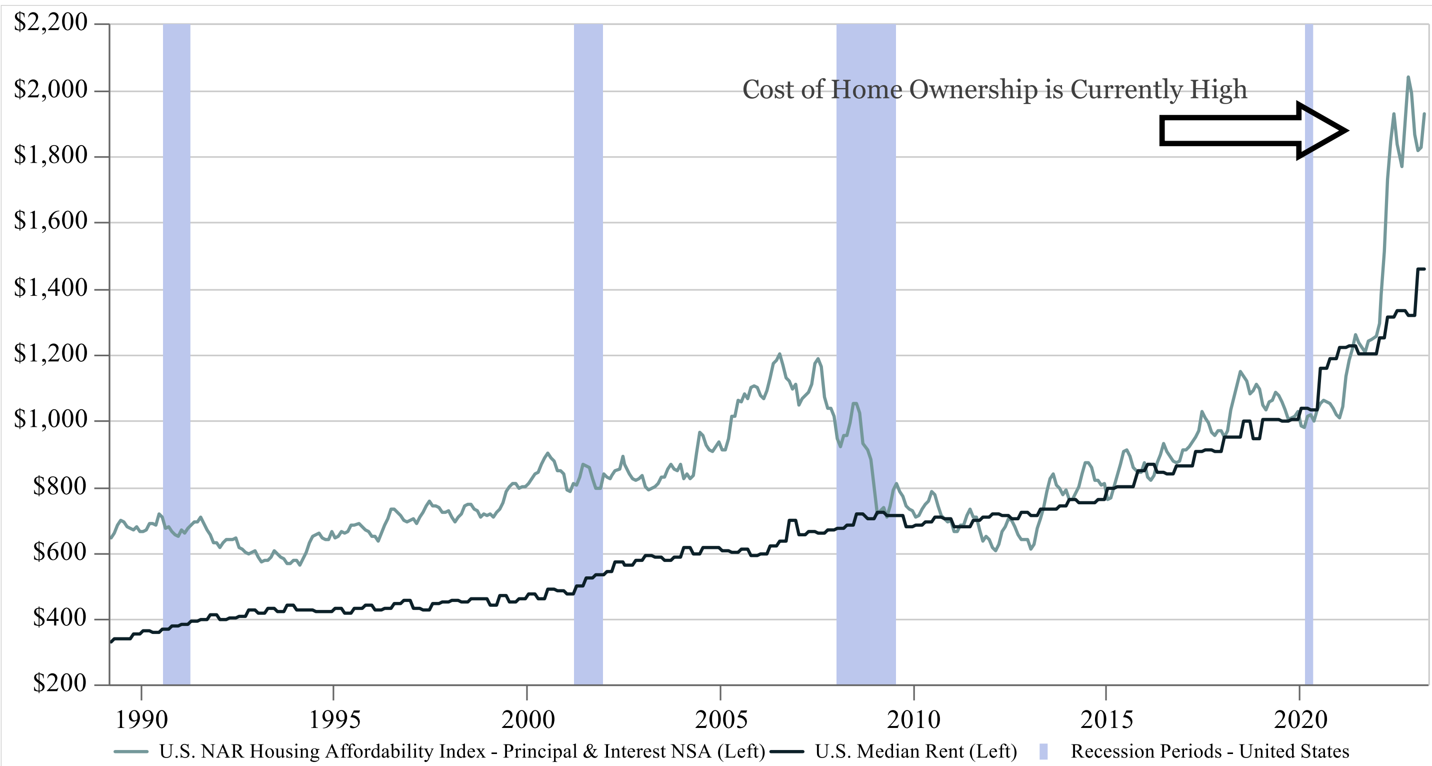
Chart I: U.S. Housing Market Costs - Own vs. Rent



Source: McShane Partners - FactSet Research Systems, Inc.

Monthly Index Review
USD Total Return

Data as of May 31st 2023	**May 2023**	**2023 YTD**	**2022**	**2021**
S&P 500® Index	**+0.43%**	**+9.65%**	-18.11%	**+28.71%**
Dow Jones Industrial Average	**-3.17%**	+0.25%	-6.86%	+20.95%
NASDAQ Composite	**+5.93%**	**+24.06%**	-32.54%	**+22.18%**
Russell 2000	-0.92%	**-0.04%**	-20.44%	+14.82%
Dow Jones U.S. Select REIT	-2.76%	+0.63%	-25.96%	**+45.91%**
MSCI Emerging Markets	-1.65%	+1.16%	-19.74%	**-2.22%**
MSCI EAFE	**-4.10%**	**+7.22%**	-14.01%	+11.78%
Bloomberg U.S. Aggregate Bond Index	-1.09%	+2.46%	-13.01%	**-1.54%**

Investment Overview

Trends in Real Estate

Not all areas of real estate are equal which is why we prefer unique real estate investments that benefit from a strong demographic trend separate from the vagaries of the economic cycle. Strategic, diversified real estate exposure provides compelling diversification to portfolios. A look a the gross levered IRR (means returns with debt considered) have been particularly strong in medical office and self storage while the single family rental segment has lagged due to the aforementioned dramatic increase in interest rates negatively impacting financing, valuations and home affordability.

Expanding our research and exposure to real estate has been enlightening and with the increased understanding of the sector trends and unique investment alternatives we find the investment opportunity increasingly compelling and are optimistic that the interest rate reset might provide a rest in asset prices and an opportunity to deploy capital into areas that can out perform over the long term.

"The world always looks nigh on impossible from the perspective of a desk. But once you get out into the world and if you have what I would call the entrepreneurial characteristics, I just think this country sill provides a very unique opportunity."

- Sam Zell

Table I: Nuveen U.S. Strategic Alternatives Fund I Performance Contribution Analysis As of December 31st 2022

Total Return Contribution			
Property Type	**Average Weight** [4]	**Gross Levered IRR** [1,2]	**Contribution** [5]
Self-Storage	43.5%	31.7%	13.0%
Medical Office	17.8%	81.7%	14.2%
Single-Family Rentals	38.7%	8.1%	2.4%
Property-Level Return	**100.0%**		**29.6%**
Net Fund IRR [3]			**33.1%**

As of December 31st 2022

[1] The Aggregate Property Type Investment IRRs were calculated assuming a hypothetical liquidation using actual monthly property-level cash flows through 31 December 2022 and each property's estimated fair market value as of 31 December 2022 based on third party appraisals, as approved by Nuveen Real Estate's internal appraisal group, less outstanding debt (where applicable) and estimated selling costs of 1.5%. Because IRRs included herein are based on a hypothetical liquidation of unrealized investments as of 31 December 2022, these figures do not account for actual target holding periods, the ultimate impact of ongoing business plans or the potential for appreciation and/or depreciation in the portfolio after 31 December 2022. The actual realized returns on the investments included in the track record will depend on, among other factors, the timing and manner of sale, future operating results, market conditions, the value of assets at the time of dispositions, any related transaction costs, and adverse impacts on economic and market conditions, the extent of which is not currently known.

[2] Gross Levered IRR is the excel XIRR formula, over the aggregate monthly investment cash flows (See Note 1 above) including the effects of property level financing. In situations where the fund invested in the property with a third party through a joint venture, cash flows are based on the Nuveen Real Estate ownership. Gross IRRs are net of property level expenses and fees (including joint venture fees, expenses and waterfalls) but do not take into account fund level expenses, management fees or carried interest.

[3] Net Fund IRR is the excel XIRR formula over the aggregated cash flows used for the fund's actual contributions, distributions and fair value NAV after calculation advisory fees and portfolio expenses (see Note 1 and Note 2 above).

[4] Average weight is the arithmetic average of the monthly weights for each property type investment within the fund. Each monthly weight is calculated by dividing the cumulative contributions of the investment in each period by the total cumulative contributions.

[4] The contribution to return is calculated by multiplying the individual IRR of the Aggregate Property Type IRR by the Average Weight (See Note 1, 2, and 4 above). The residual between the sum of the contribution and the actual aggregate return due to compounding is distributed according to the average weight of the investment.

Source: Nuveen Asset Management - Nuveen U.S. Strategic Alternatives Fund I, LP Annual Meeting Presentation (April 25th 2023)

Wealth Advisory Overview

Understanding equity compensation

Non-Qualified Stock Options vs. incentive stock options

There are two types of stock options: Non-Qualified Stock Options (NQSOs) and Incentive Stock Options (ISOs)

NQSOs give you the right to buy a certain number of shares at a predetermined strike price. You pay ordinary income tax on the difference between the strike price and the fair market price (also known as the bargain element). Usually, the initial tax event occurs when you exercise your options. The timing of this initial income recognition is based on whether the value of the option can be readily determined at the time of grant. Other conditions may apply, but generally an option has a readily determinable value if it is actively traded on an established market. That means the options are traded, not the underlying stock itself. These types of options are not very common outside of the tech industry.

For most NQSOs you won't recognize income until you exercise your options, which means you can control the timing and the amount (to some degree) and can exercise the option when it's most beneficial to your tax situation. For example, if you anticipate lower than usual income next year, it may be in your benefit to exercise your NQSOs in that year and recognize income. NQSOs usually expire 10 years after grant or within 90 days if you separate from your employer. Once you have exercised the options, you own the shares of stock. The sale of the shares will result in short term or long-term capital gain (or loss) depending on how long you hold the actual stock. Long term is anything held for mor than a year. Since long term capital gain rates range from 0% to 20%, the tax savings over ordinary income rates (15% - 37%) can be substantial.

ISOs are similar to NQSOs, but with the bonus of an additional tax benefit. ISOs come with two favorable tax measures: First, unlike NQSOs, there is no ordinary income tax at exercise (though you may owe alternative minimum tax, also known as AMT). Second, if the exercised shares are sold after two years from the date of grant and at least one year from exercise, the entire profit you make will be taxed at long-term capital gain rates. For example, if you were granted ISOs in January 2020 and you exercise your ISOs in January of 2021, you would need to wait to sell your exercised shares until January 2022 to meet the special holding period.

When to exercise

I'm frequently asked about when options should be exercised. There is no easy answer for the optimal time to exercise options. First, there is no benefit to exercising options that are "underwater". If the value of the stock has declined to a price where it is below the strike price, you would be "purchasing" stock for more than its value. The sale of the stock would generate a tax loss, but only $3,000 per year can offset other income, and since tax is not 100% it rarely makes sense to lose money for a tax benefit.

Second, if your company stock is not actively traded it may be a huge financial burden to pay the taxes on the stock option exercise. Prior to the tech bubble bursting, many privately held companies were granting employees options that were exercised as soon as they could be. As valuations multiplied with every round of financing, the allure of turning ordinary income into capital gains was overwhelming. Often the employee was surprised by the tax on exercise and could not come up with the cash with no market for the company stock. Even worse was when the bubble burst and the stock became worthless, after the tax had been paid on those high-flying valuations. For non-publicly traded stock, exercise your options in an amount that you can afford to pay tax on, and can afford to lose, unless you are absolutely positive that the value will continue to increase.

Many option plans provide for a "cashless" exercise but that is not often the case for non-publicly traded stock. A cashless exercise provides that the exercise or strike price, and sometimes the taxes as well, are subtracted from the value of the stock at the date of exercise. For example, if you have options for 4 shares at a $10 strike price you may decide to exercise the options when the stock is trading at $20/share. The gross value of the shares is $80 (4 shares @ $20), but you owe $40 to exercise them (4 shares @ $10). In a cashless exercise, the company

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Understanding equity compensation

would deposit 2 shares in your account for the net exercise (2 shares @ $20 = $40) without you having to pay cash for the exercise. Frequently you can elect to have shares liquidated to pay the taxes on the exercise as well. I generally recommend that rather than paying the tax out of pocket. That helps reduce the concentration risk of owning a significant amount of employer stock and the shares you are liquidating are at their fair market value so there is no loss of value.

Finally, if you believe that the stock price has been impacted negatively by overall market conditions and the growth outlook and fundamentals of the company are sound, it does make sense to exercise earlier rather than later and when the price is depressed for stock you intend to hold long term. An earlier exercise at a lower value increases the potential for more appreciation after exercise and ultimate taxation at a lower rate.

Equity compensation plans can be very complicated. For advice on your unique situation please contact your McShane Partners Wealth Advisor to discuss the tax implications and to develop a strategy that optimizes your financial impact from your stock options.

NexGen: Managing an Inheritance

Ryan Vaudrin, CFP®, CDFA®
Partner | Wealth Advisor

Receiving an inheritance can be an unexpected and overwhelming experience following the loss of a loved one. Along with grieving, it is important to take your time and implement a strategy when inheriting a partial or full estate. Listed below are a few key points to consider when the time comes to transition assets from an estate.

Asset Type – The Executor will work to determine the amount and types of assets included within the estate. If receiving cash, investing in high yield savings or federally insured bank accounts may be suitable options for holding the funds. This will provide time to decide the next move in the transition phase. When inheriting investment accounts, it is important to determine how the accounts were managed – i.e., does current management align with the beneficiary's risk tolerance and personal goals? Inheriting personal property has its own challenges as there may be emotional ties while trying to decide what keepsakes are important and what needs to be sold or given away.

Tax Implications – There could be tax implications from selling or taking distributions from the inherited assets depending on the type of account. If receiving personal property or a taxable investment account, it is important to elect step-up in cost basis. *Stepped up* cost basis resets the investment's tax basis to the decedent's date of death or six months after death. This tax strategy can help to mitigate potential gains which will allow the beneficiary to limit tax liability.

If receiving a retirement account, Required Minimum Distributions or RMDs may be required. These Required Minimum Distributions are the amount that must be distributed from the retirement account to the beneficiary to avoid tax consequences. The schedule would depend on the decedent's date of death – If they passed away after December 31, 2019, the entire account must be depleted by the 10th calendar year following the original owners date of death.

What Should You Do With the Inheritance? – The amount of the inheritance plays a key role in available options and how the beneficiary should proceed. While individual situations vary, common goals may include charitable giving, investing in personal accounts, building an emergency fund, or paying down debt.

Using a team of professionals can help to maximize the potential of an inheritance. Financial planning potential tax projections can help provide clarity and help navigate what to do next. Let your McShane Partners Wealth Advisor help answer any questions and provide the necessary guidance on how to move forward!

Senior Planning: Tips to help you prevent fraud

Lorri Tomlin, FPQP™
Partner | Wealth Advisor

Modern technology has changed the way we do many things in our daily lives, making transactions and communication quicker, more convenient, and more secure. However, this same technology is also used by hackers to scam individuals into giving them money or access to personal information and accounts. Therefore, it is important to take steps to protect your online security. We have provided tips in previous newsletters to help clients protect themselves from fraud, but feel it is important to review them from time to time.

In general, you should always be suspicious of *unexpected or unusual* emails or text messages from people or vendors. These emails and texts can be very official looking and even contain logos from vendors that you use. Again, do not respond to or click on links provided in these emails or texts and especially do not provide any information if you do click on a link.

Here are some suggested steps to further protect yourself from cyber criminals:

- Use strong passwords that do not include personal information. Use a combination of letters, numbers, and special characters that do not form words.
- Do not use the same password for important accounts. Create a unique password for these accounts.
- Change your passwords often. Especially if you think you may have had a security breach. One of your first steps should be to change your password.
- Use two factor identification or voice recognition if available.
- Do not open attachments or click on links in suspicious emails or text messages.
- Do not allow access to your computer or provide personal information unless it is a trusted source.
- Limit the personal information you share on social media or on websites.
- Review your accounts often to check for unauthorized transactions.
- Invest in antivirus software.
- Use “free” Wi-Fi with caution
- Make sure your devices are updated with the latest software versions and that the privacy and security settings are set up based on your security needs
- Use a personal monitoring service or enroll in “alerts” on accounts that notify you of any suspicious activity
- Enlist the services of a computer technician to do an annual checkup on your computer or help if you think you have had a security breach.

If you think you have been the victim of a scam, tell someone you trust. Your Wealth Advisor at McShane Partners can help if you think your accounts have been compromised. If you have lost money, report the incident to the local authorities. The Federal Trade Commission (FTC) collects scam reports. Report your scam online with the FTC complaint assistant or call 1-877-382-4357.

How much umbrella insurance do you need?

Sandy Carlson, CFP®, CPA, CDFA®
President | Partner | Wealth Advisor

Umbrella insurance is a type of personal liability coverage that protects you and your family from large claims or lawsuits that go above your homeowners, auto, and even boat insurance policies. It does so by filling the financial gap that your primary liability policy doesn't cover. Meaning if you are sued, and your auto insurance only covers up to $100,000, your umbrella policy will provide protection for any amount greater than $100,000, up to the umbrella policy limit.

Umbrella insurance covers these five main areas:

- Bodily Injury – Protects you from things like medical bills or lawsuits involving bodily injury.
- Legal fees – Umbrella insurance also kicks in if someone sues you, so that you don't have to pay attorney's fees out of pocket.
- Injury to Reputation – If you're sued for slander, libel or defamation your umbrella insurance will cover you for these expenses.
- Property Damages – Covers property in the event of car accidents, including the cost to repair someone else's property.
- Rental Property – Protects you as a landlord if you're sued after an accident on your rental property.

The amount of your umbrella insurance policy should match your entire net worth. Therefore, if your assets total $1 million, that is the amount of umbrella insurance you need. However, certain assets, like an employer-sponsored retirement account, are not at risk from most lawsuits due to federal regulations. Therefore, you can usually leave those out of your calculations. But it is still a good idea to ask your insurance agent to make sure that you are purchasing the correct amount for your specific situation.

NextGen: Maximizing Flexible Spending Accounts—Dependent Care

Daniel Hudspeth, CFP®
Wealth Associate

Flexible Spending Accounts, also known as FSAs, are tax-advantaged accounts which allow participants to fund qualifying expenses with pre-tax dollars. Qualifying expenses may include insurance deductibles, copayments, and medications including prescription and certain over-the-counter medicine (for a full list generally permitted expenses visit the IRS website here). FSAs also provide another wonderful benefit in addition to healthcare expenses: Dependent Care expenses.

The dependent care provision allows the use of pre-tax dollars to fund qualifying dependent care expenses for children under 13 years of age, parents in eldercare, as well as a disabled spouse. For this month's article, we will focus on daycare for qualifying dependents under 13 years of age.

For 2023, the maximum eligible dependent care contribution amount is $5,000 annually per household. As long as a participant (and spouse if filing jointly) has earned income, they are eligible to contribute. This means that up to $5,000 of daycare expenses can be funded with tax-advantaged dollars. These contributions can be made by the employee or the employer, although they are not required.

Once contributions are made to the account, participants are allowed to reimburse themselves for qualifying dependent care expenses. Submitting a reimbursement claim is one common method that is normally simple and straightforward. Participants file a claim through their FSA provider by completing a reimbursement form and uploading a receipt of the services provided along with service dates. Once completed, the account provider approves reimbursement and transfers the eligible funds into the participants linked bank account.

Stay tuned for next month's article which will highlight other benefits and uses for Flexible Spending Accounts. As always, please contact your McShane Partners Wealth Advisor with any questions or more information regarding the use of Flexible Spending Accounts for dependent care expenses.

Around McShane Partners

45th Annual Estate Planners Day

Lorri Tomlin, Daniel Hudspeth, Ryan Vaudrin, and Tracy Strickler attended the 45th Annual Estate Planners day on May 18th. McShane Partners was once again a Supporting Sponsor of the event. This year's presenters were excellent and topics included state and federal updates regarding estate planning, an economic update, the SECURE Act developments, fiduciary ESG investing, sophisticated insurance planning and business structuring and succession planning.

Female Financial Empowerment

Becky Hoover hosted the first in a multi-part series of diverse financial and investment topics for clients and friends of the firm on May 8th. The first topic addressed how to be comfortable being the boss of your financial future, whether you have ever handled your own money or not. Future seminars will include guest speakers and discuss topic such as cyber security, power of attorney, prenuptial agreements, and estate planning.

20th Annual Wells Fargo Championship

Sandy Carlson attended the popular golf tournament at Quail Hollow Country Club along with fellow clients during the first week of May. The tournament has been played in Charlotte for 18 of the past 20 years. This years winner was Wyndham Clark with 19 strokes under par.

McShane Partners

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

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