MP McShane Partners

April 2020 Insights

Investment Overview

Recognize, Replace, and Rebalance

It has been **±41 days** since the commencement of the worldwide descent into bear market territory from the record high on February 19th. The intensity and rapidity of the -33.5% correction in the S&P 500® Index, alongside the emotional impact of the rapidly spreading novel coronavirus ("COVID-19") around the world, has precipitated shocking declines in global financial markets, as well as a pronounced deceleration in economic activity, which has inevitably hastened a global recession. As clarity surrounding the virus' ramifications to the economy improves, market stabilization is possible. The near-term bottom of December 24th 2018 appears to represent downside support at this time. However the daily volatility makes effective repositioning difficult.

Initially, equity markets began testing and, eventually, broke through key levels of technical support, with the S&P 500® Index falling below its 50-day and 200-day moving averages ("MAVG") on February 24th and February 27th, respectively. The Investment Team laid out a near-term downside level of **2,351.10** that was initially established on December 24th 2018 which established the end of the correction in the fourth quarter of 2018 ("4Q18"). While the market tested this level, closing at **2,237.40** on March 23rd, it did manage to stage a brief bear market rally of **+15.57%** through month end, despite increasing anxiety and mounting

Continued on next page

Wealth Advisory Overview

Five Strategies for Divorce Settlement in a Volatile Market

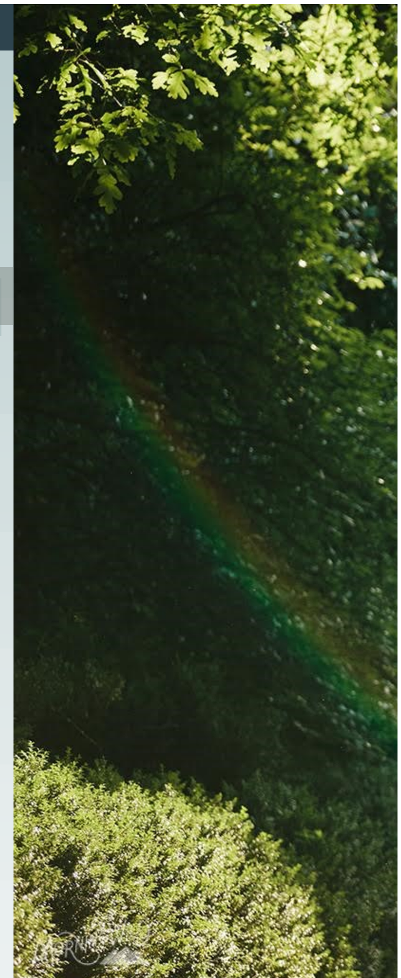
News coming from China is that there was a surge in divorce filings in Wuhan following the mandatory quarantine period. We haven't seen what will happen in the U.S., but many divorcing parties may already have a settlement offer or signed agreement that has been battered by rapidly changing values.

Divorce is always a painful process but adding to that pain right now is the volatility in the stock market and a home market that is temporarily on hold. What are the implications on settlement negotiations or recently signed agreements? How do you adjust to a constantly adjusting value?

The good (and bad) news is that orders for equitable distribution typically stand as a final division of assets and debt. Agreements regarding the division of assets and debts set forth in Separation & Property Settlement Agreements are also generally not modifiable by the Court. If both parties agree to revise the agreement you may be able to make adjustments. However, such a scenario is unlikely to happen when one party feels they have lost value and wants to "share" that loss. What can be modified are orders for spousal or child support due to a substantial change in circumstances, so the possibility of going back into negotiation may encourage cooperation on a temporary agreement while the financial markets roil.

While you can't compel your ex-spouse to revise your settlement or force him or her to consider your property's decline in value, we offer the following

Continued on page 6



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Points of Interest

Investment Overview

Recognize, Replace, and Rebalance

concerns over the extent of the socioeconomic damage from the persistent COVID-19 pandemic and based predominately on incremental optimism regarding the **±$1.3 trillion** in combined monetary and fiscal policy stimulus. Given this represents a certain level of short-term stability, the Investment Team is focusing on opportunities to ***recognize*** losses for tax purposes, ***replace*** underperforming positions with higher-quality names trading at a attractive discounts, and ***rebalance*** portfolios to optimize positioning relative to strategic asset allocations.

Below, Chart I shows the sharp sell-off in the S&P 500® Index and the dramatic descent into bear market territory, highlighting the key technical support levels, as well as the aforementioned near-term support level of **±2,351.10** for the S&P 500® Index and the rapid three-day assent back to a bull market.

Recognize

The strong upward move in equity markets over the past decade has made recognizing gains extremely difficult, and the Investment Team has exercised prudence in doing so by looking for short-term pullbacks or

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Chart I: S&P 500® Index (January 1st 2016 - March 31st 2020)

Source: McShane Partners - FactSet Research Systems, Inc.

Monthly Index Review
USD Total Return

Data as of March 31st 2020	March 2020	2020 YTD	2019	2018
S&P 500® Index	-12.35%	-19.60%	**+31.49%**	-4.38%
Dow Jones Industrial Average	-13.62%	-22.73%	+25.34%	-3.48%
NASDAQ Composite	-10.03%	-13.95%	**+36.69%**	-2.84%
Russell 2000	**-21.73%**	**-30.61%**	+25.52%	-11.01%
MSCI Emerging Markets	-15.38%	-23.57%	+18.88%	**-14.24%**
MSCI EAFE	-13.25%	-22.72%	+22.66%	-13.36%
Bloomberg Barclays U.S. Aggregate Bond Index	-0.59%	**+3.15%**	+8.72%	**+0.01%**

Investment Overview

Recognize, Replace, and Rebalance

corrections. Given the recent declines across global equity markets, we will be using *correlation matrices* to identify opportunities to sell existing equity holdings and positions that we believe have upside potential equivalent to an alternative in order to seamlessly capture a loss and mitigate incremental *equity market risk* (i.e., beta) exposures maintaining portfolio-level volatility and upside/(downside) capture. This has been critical given an average daily market “swing” of **±5.0%** in March, representing the highest on record: the previous record having been **±3.9%** for the month of **November 1929**. Day trading and irresponsible, unilateral repositioning could have severe near-term and long-term ramifications.

While *tax loss harvesting* can be extremely beneficial at a time like this, McShane Partners remains focused on long-term investment performance and believes that effective tax planning can be done in conjunction with investment portfolio optimization relative to long-term risk-return objectives. Our in-house, proprietary investment research and individual stock selection capabilities, as well as our independent mutual fund and exchange-traded fund (“ETF”) due diligence processes, enable us to do this quickly and efficiently across all client investment portfolios.

“If you want to have a better performance than the crowd, you must do things differently from the crowd.”
- Sir John Templeton

For example, the Investment Team took advantage of the short-term bounce in equities to recognize a loss in long-term positions in Kraft Heinz Co. (“KHC”) across U.S. Equity allocations. Given the sell-off in other higher-quality companies within our investable universe, we believed recognizing the losses in KHC, where applicable, was sufficiently valuable to justify replacing it with shares of other buy-rated stocks with superior balance sheets and above-average earnings growth that were now trading at attractive relative and absolute valuations. On further consideration, the Investment Team recognized that shares of KHC no longer represented one of our highest conviction investment ideas and decided that it was time to capitalize on the short-term rally in shares of KHC by selling all existing holdings and rotating the majority of the proceeds into other high-quality, attractively valued names offering better or similar relative upside potential vs. shares of KHC. Depending on the individual client’s underlying holdings, expected or anticipated cash flow needs, and strategic asset allocation, the Investment Team replaced positioning in KHC with shares of Accenture PLC ADR (“ACN”).

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Stock & Strategy Spotlight

Name	Ticker	2020 YTD
Accenture PLC Class A	ACN	**-22.09%**

Description & Investment Thesis

As indicated above, the Investment Team is reiterating our positive near-/intermediate-term outlook for shares of Accenture PLC Class A (“ACN”) following a reset in valuations after the company reported better-than-expected quarterly earnings on March 20th, at which time ACN also lowered its full year revenue growth guidance to reflect the broader economic headwinds. Shares of ACN, which typically trade at a double-digit premium to sector- and industry-level peers given the company’s established history of above-average earnings growth and healthy profitability, traded at their lowest relative valuation multiples vs. the S&P 500® Information Technology Sector Index in early-March (±1.06x PE NTM) and continue to trade well below their 5-/10-year historical average premium multiples. Furthermore, the company has a pristine balance sheet and significant flexibility in terms of its capacity to navigate a temporary slowdown in its primary businesses, although we would expect overall demand to demonstrate some resiliency given the key role the company plays in providing critical services across multiple verticals and a diverse set of end markets.

Investment Overview

Recognize, Replace, and Rebalance

Replace

Similarly, the Investment Team was able to capitalize on the recent relative outperformance of core positions in the Vanguard Consumer Staples ETF ("VDC"), which exhibited significantly better downside protection and lower volatility vs. higher-beta sectors and stocks, as well as the broader equity market, through the worst part of the sell-off. Specifically, the Investment Team identified selective opportunities to tactically sell positions in VDC and rotate the proceeds into ANSYS, Inc. ("ANSS") for applicable portfolios with negligible exposure to the stock as shares traded down to valuations that have historically represented extremely attractive entry points for long-term investors in this top technology company.

Below, Chart II illustrates the recent performance of both VDC and ANSS - with share prices indexed to 100 as of February 17th 2020 - and a comparative analysis of the net total return(s) generated by the VDC-ANSS replacement trade, using an effective transaction date of February 27th 2020 for both the sell and buy orders. As indicated in the chart, the VDC-ANSS replacement trade has generated approximately **+306.56** basis points ("bps") in positive relative contribution through month end. This is an example of a tactical rotation and replacement strategy that will continue to take place methodically over the coming weeks and months.

As the current bear market continues to evolve, and as we navigate through the progression of an economic recession, the Investment Team will remain vigilant in identifying opportunities to replace lower-growth, defensive stocks with higher-growth, cyclical names of comparable fundamental quality. However, this will be dictated by valuation as we will be diligent, methodical, prudent, and cost-conscious. Over the past few weeks, the Investment Team has been updating near-term and long-term "entry-point" price targets for several high-quality stocks. Prudence, process, and price point will keep us from chasing stocks up when the market haphazardly rises **+11.0%** in a single day: based on our careful valuation work and target return framework, such a move represents an entire year's worth of market returns for an investment portfolio!

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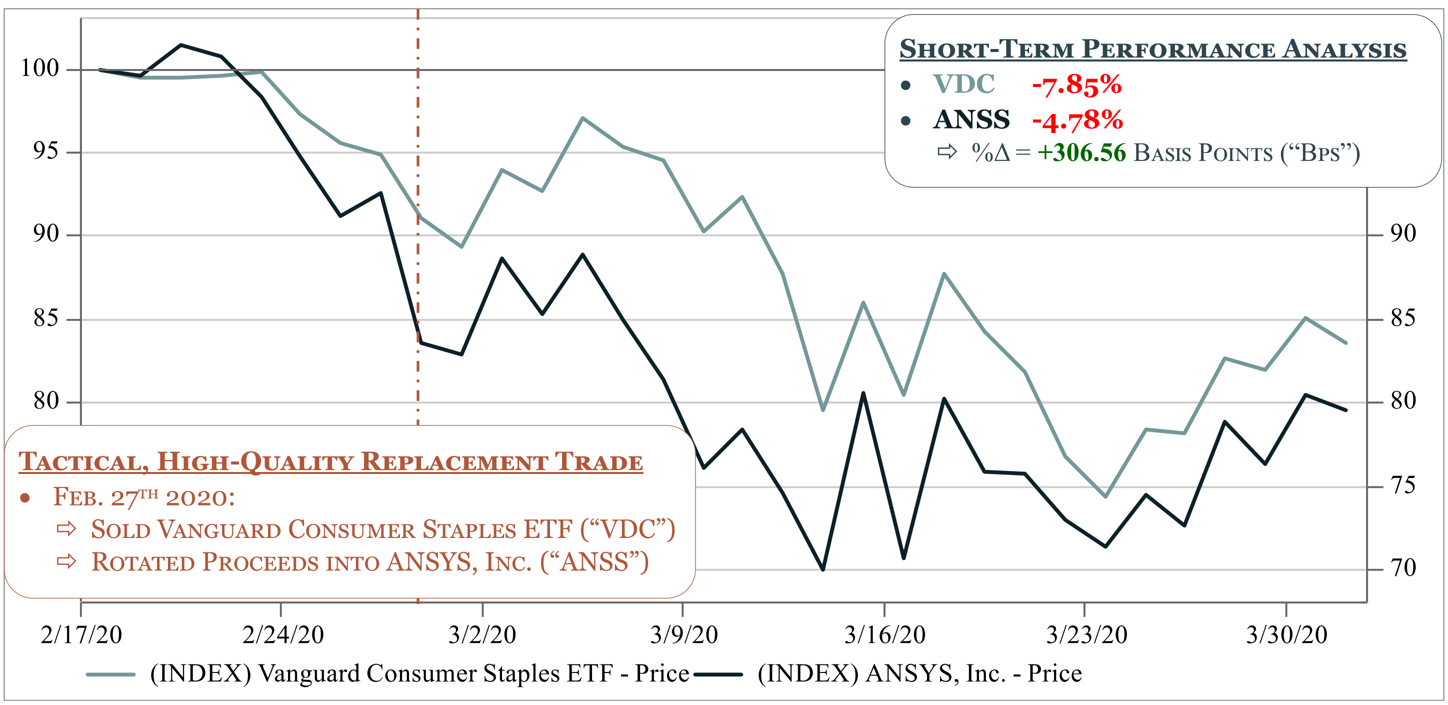
Chart II: Identifying Tactical Opportunities & High-Quality "Replacement" Trades



Source: McShane Partners - FactSet Research Systems, Inc.

Investment Overview

Recognize, Replace, and Rebalance

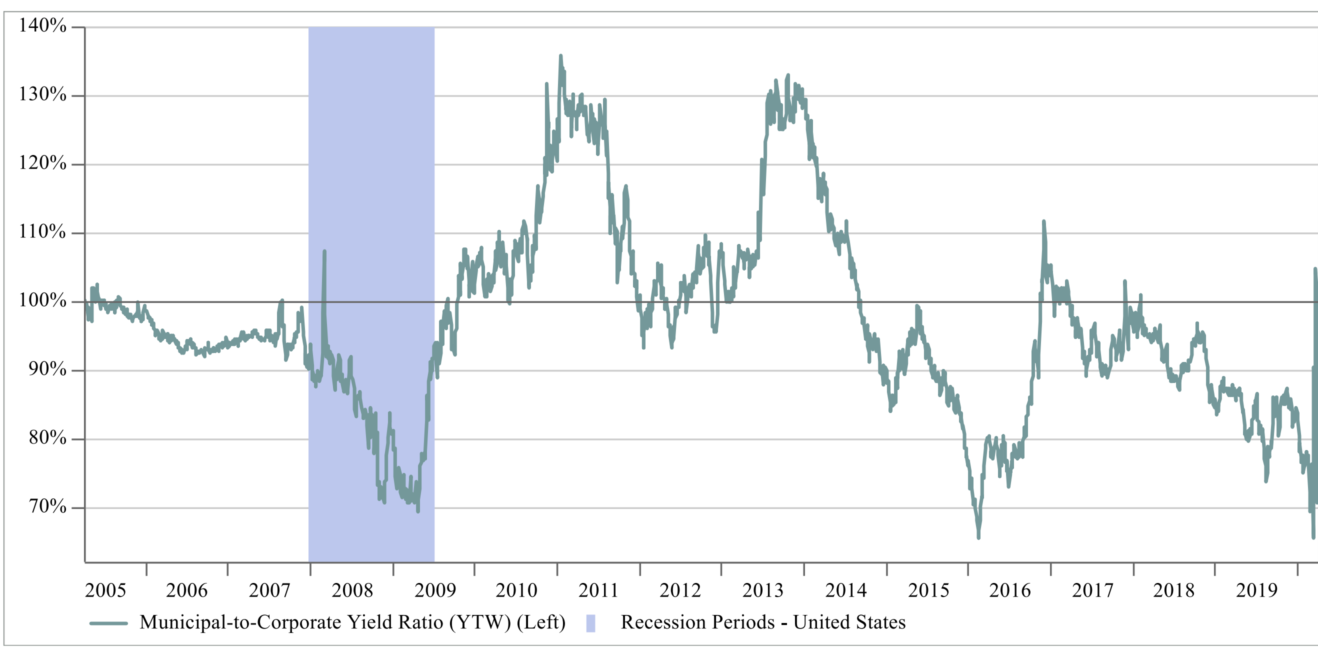
Rebalance

Entering this current market downturn, portfolios were generally overweight Cash & Cash Equivalents, underweight Fixed Income, and slightly overweight U.S. Equity relative to our long-term target allocations: this is a broad generalization of portfolio-level positioning and may not be entirely or exactly representative of every investment portfolio given the highly customized nature of the work we do for clients. Our rebalancing efforts had been constrained for the past ±12-18 months leading up to this market correction, as both fixed income (i.e., bonds) and equity assets had been moving higher together, making it imprudent to undertake broad-based rebalancing at a time when correlations across asset classes were precariously high, as the Investment Team highlighted in another newsletter late last year (*October 2019 INSIGHTS*).

As the market correction continued to pick up momentum throughout the month, negative investor sentiment and pervasive risk aversion adversely affected the municipal bond market due to the inherent illiquidity this particular segment/sector of the bond market. Essentially, the increase in activity exacerbated pricing pressure on a relatively limited supply of underlying issues available within the municipal bond market, which caused a sudden, indiscriminate sell-off across the entire municipal bond complex. Reactionary selling weighed on the prices of investment grade municipal bonds with solid fundamentals, as investors looked to quickly sell either lower-quality bonds with high debt levels and/or those with outsized exposure to COVID-19, such as New York and California.

The municipal bond market rarely offers opportunities to buy bonds at irrational discounts to U.S. Treasury bonds or high-quality, investment grade corporate bonds. The municipal-to-corporate yield ratio is an extremely effective indicator for quantifying and identifying these sporadic and brief periods that have historically offered excellent buying opportunities for long-term investors. Chart III, below, shows the outsized spike in this ratio during the recent market correction. At one point during the month, the Bloomberg Barclays Municipal Bond Index had sold off as much as **-11.24%**, only to quickly recover **+8.13%** over the following week. This correction was exacerbated by forced selling activity across exchange-traded funds ("ETFs") and mutual funds, which is why we recommend direct ownership of individual municipal bonds, where applicable/appropriate, to mitigate the impact of forced selling on municipal bond allocations.

Chart III: Municipal-to-Corporate Yield Ratio



Source: McShane Partners - FactSet Research Systems, Inc.

Wealth Advisory Overview

Five Strategies for Divorce Settlement in a Volatile Market

strategies for managing the situation. If the opposing party is amenable, entering into a private and separate amended agreement with your ex may be a cost-effective way to accomplish these objectives.

Real Estate – In recent conversations with real estate agents and mortgage brokers we have yet to see declining values in the real estate market. That may happen as the economy worsens. Right now, we have seen a virtual pause in the real estate market as showings are replaced with virtual tours and closings are delayed or curbed if the lender and attorney are creative enough.

1. **Negotiate an Agreement for Co-Ownership Until the Market Improves.** If your agreement calls for the sale of your home and it fails to sell, or the offers are far below the agreed upon value, you may want to ask your ex to enter into an agreement for an interim period. Consider issues such as:
   - Who pays for day-to-day expenses?
   - How are major repairs and expenses to be shared or reimbursed? Should there be a cap?
   - Should you share tax, utility and insurance fees equally or on a percentage basis?
   - What about a capital gains tax risk to the spouse who is not living at the former matrimonial home, and thus has another 'principal residence'?
   - If there is a present mortgage to be paid, should the cost be shared, and if so, what is the effect on child and/or spousal support payments?
   - What happens if one spouse is paying the mortgage down – should the other spouse benefit from the increase in equity that will gain over time?
   - If one party is occupying the home, should a rental payment be due?
2. **Delay Refinancing.** If you received a home through your property distribution and have not yet refinanced the mortgage into your own name you may want to negotiate a delay for a month or two. That may sound counter-intuitive, but mortgage rates have risen as the sheer volume of refinancings have overwhelmed the system. Consensus is that interest rates will remain at historical lows for a while, so you may get a better rate in a few months when demand declines.
3. **Consider a HELOC.** If you have a home with substantial equity, it may be beneficial to take cash out on a Home Equity Line of Credit (HELOC), rather than sell portfolio securities or refinance your mortgage to take out cash. The rates on home mortgages, including HELOCs, are low and the cash from a HELOC may give you time until the financial markets stabilize before selling stocks. Using a HELOC allows you the flexibility to take out cash and repay it without changing your mortgage payments for the long term. Be sure to check your existing agreement to confirm compliance if the home is still marital property as there is often a prohibition on creating additional debt on marital property.

Financial Markets – The value of stocks and bond portfolios are changing at a frenetic pace as we experience unprecedented volatility. If the bulk of your property settlement consists of stocks and bonds you are likely having a daily panic attack. It is important not to panic, as the market will eventually settle down. Suggestions to take advantage of or manage the down market in the interim include:

4. **Consider a Roth IRA Conversion.** If you have a regular IRA you may want to convert it to a Roth IRA. The tax liability will be due in the current year, but if you have the cash it might be beneficial. The value upon which you will be taxed is likely depressed. Along with what may already be a year with lower taxable income due to lower bonuses, gains, etc, your low effective rate in the current year is a potential opportunity.
5. **Actively Manage your Tax Bracket & Recognize Gains.** Although stocks have fallen

Continued on next page

Wealth Advisory Overview

Five Strategies for Divorce Settlement in a Volatile Market

significantly, many positions are still up over the longer term. At lower taxable income levels (under $40,000 for single filers and under $53,600 for head of household filers) you may recognize long term capital gains at a zero percent rate. There is no “wash sale” rule discouraging the repurchase of securities sold at a gain. Consider selling stocks with a gain and repurchasing them if you feel they are still a good investment. If you pay no capital gain you get a “free” step up in basis.

While this is not a comprehensive list, it hopefully provides comfort that there are strategies to help manage long term damage to your net worth from the current financial environment. Divorce is challenging for both parties and optimizing your share of the marital estate can make a huge impact on your financial security. Work with a qualified financial advisor who can assist you in creating strategies to help you be successful.

The information provided is not intended to be legal advice. You should consult an attorney for advice about your personal situation. Further, the thoughts and commentary about the law contained herein does not constitute solicitation or provision of legal advice and is not a substitute for legal advice.

Around McShane Partners

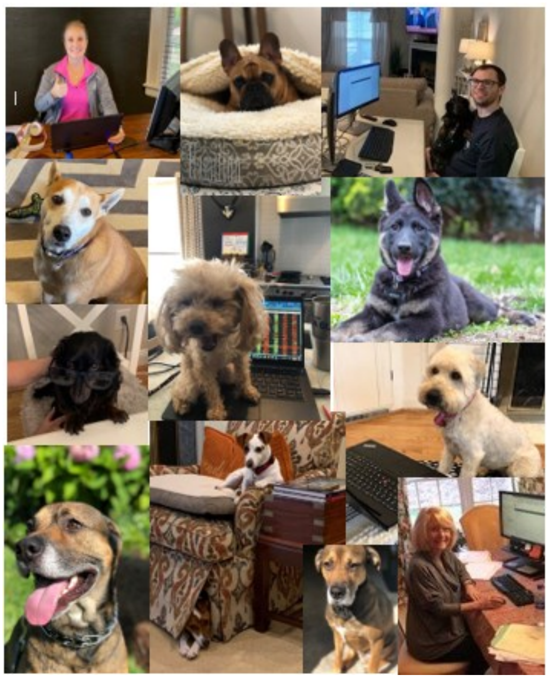
Investment Team Market Update: March 20th

A recording of McShane Partners' most recent market update and webinar presentation is now available on our website for your review and consideration.

To access and view the recording, as well as previous webinars and past newsletters, please click here, or go to the McShane Partners' website and click on the corresponding link included under our "Featured News" section.

Dog Days at McShane Partners: Your Team Hard at Work (from Home)

Our view may have changed over the past two weeks, but rest assured, we are still working hard! Check out some of our team hard at work.



Until one has loved an animal, a part of one's soul remains unawakened. - Anatole France

Stay Safe!

Be on the lookout for a small gift from your McShane Partners team (while supplies last)!

We are thinking of you all!

Happy Belated St. Patrick's Day!

Happy St. Patrick's Day!

McShane Partners' Managing Partner and Chief Investment Officer, Daniele Donahoe, celebrated St. Patrick's Day with her crew a week late. We have to be creative to have fun at home with the kids out of school until May!

McShane Partners

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

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