MP McShane Partners

# September 2018 Insights

## Investment Overview

### Cash Is (Always) King

Cash management has not been necessary for U.S. investors until only recently, as interest rates have risen sufficiently off the zero interest-rate policy ("ZIRP") levels of the post-Global Financial Crisis ("GFC") years. With the Federal Reserve expected to continue increasing the federal funds rate ("fed funds rate") over the coming 12-24 months, and with financial markets firmly entrenched in a period of *tightening* monetary policy, it is once again important to evaluate the various cash management options available to individual investors, as failing to appropriately manage cash allocations at this stage in the market cycle could be sacrificing **±1.0%-2.0%** of *lower-risk* return. Given the market's increasingly hearty risk appetite and associated lofty valuations alongside circumspect leading and lagging economic indicators, a tactical overweight allocation to cash might be prudent and responsibly achieving the best risk-adjusted return for cash investments is paramount.

Not all cash management solutions are created equal, however, and failure to analyze the available options carefully could result in investors assuming unintentional risks within an asset class that is presumed to be the most secure. For example, at the height of the GFC financial market meltdown in 2008, certain money market mutual funds saw their net asset value ("NAV") per share fall *below* $1.00: in the money market mutual fund industry, this is called "breaking the buck" and represents an extremely disconcerting situation. This phenomenon escalated

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## Wealth Advisory Overview

### The Evolution of Technology in Wealth Management

The wealth management industry has historically used paper-based processes that are quickly becoming archaic and cumbersome. Over the last several years, virtually every wealth management firm has been affected by advancements in technology. This new technology lightens the burdens of practice management, which frees up valuable time for advisors to provide better service to clients.

#### Wealth Window

As the digital world continues to take shape, wealth advisors need to use technology at various levels. For years, the wealth management industry was dominated by desktop-based systems. Within the last five to seven years, however, there has been a shift within the industry to systems that are more software-based. While converting software systems can be painful, wealth advisors who have embraced this change and converted to more portable and more efficient software have seen a notable shift in their practice. This shift has endowed wealth advisors with the ability to work from any device and from any location, opening up new forms of advisor-client interaction.

The ability to interact with clients through the use of technology at various levels is becoming increasingly important. This interaction includes digital on-boarding and document signing, asset aggregation, and the use of client portals.

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### Investment Team

Daniele Donahoe, CFA
*Chief Investment Officer*

Elliott Van Ness, CFA
*Director of Research | Portfolio Manager*

Thomas Mack
*Research Analyst*

### Wealth Advisory Team

Sandy Carlson, CFP®, CPA, CDFA™
*President | Wealth Advisor*

Leah Maybry, CPA
*Director of Tax & Family Office Services*

Lorri Tomlin, FPQP™
*Wealth Advisor*

Michael Means, CPA
*Wealth Advisor*

Ryan Vaudrin, CFP®
*Wealth Associate*

Lesley Burke
*Client Service Associate*


### Special Points of Interest

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an already tenuous financial market correction, with the ensuing panic leaving agitated investors fearful of the sanctity of their cash, as they had previously considered money market mutual funds to be "cash-equivalent" investments and were rapidly educated as to the important distinction. Qualifying cash held at banks is *insured*, while cash invested in money market mutual funds is not, so when the market value of the *commercial paper* (i.e., short-term unsecured promissory notes issued by corporations) owned by those money market mutual funds began to *deteriorate* in 2007-2008, the NAV of those money market mutual funds exhibited unanticipated volatility and downside risk, which was not sufficiently understood by investors seeking a safe repository for their cash.

### The Importance of FDIC Insurance

FDIC insurance becomes a crucial feature providing clients with incremental security while maintaining liquidity when there is a financial crisis. The Federal Deposit Insurance Corporation ("FDIC") was established in 1933 following the systemic, widespread failures of thousands of banks during the 1920s and early-1930s with the stated objective of promoting confidence in and mitigating systemic risks across the U.S. financial system. Banks and thrift institutions register with and pay premiums to the FDIC in order to be able to provide *deposit insurance coverage* to their customers on *depository accounts*. The FDIC provides standard insurance on deposits of ***$250,000 per depositor***, ***per insured bank***, meaning that if a bank or thrift institution fails, customers would still be entitled to ***100%*** of their FDIC-insured deposits up to $250,000. This was not the case in the years preceding the establishment of the FDIC when bank failures exposed systemic risks in the U.S. financial system triggering nationwide bank runs, as panicked customers rushed to withdraw their deposits from banks across the country, fearing the banks were, quite literally, running out of money.

FDIC insurance applies only to *cash deposits*; the FDIC does not provide deposit insurance to other asset classes such as bonds, equities, and funds. (*Source:* *www.fdic.gov*). Many of the major, diversified financial services institutions in the U.S. provide customers with access to FDIC-insured cash management option. Both Schwab and Fidelity offer FDIC-insured cash management options to clients through their respective direct or affiliate relationships with banks providing deposit insurance coverage.

### Alternative Access to FDIC Insurance: Traditional Banks vs. Online Banks

Despite the rising interest rate environment, the average interest rate offered on a retail depository account by traditional banking institutions, such as checking and savings accounts at both Bank of America Corp. ("BAC") and Wells Fargo & Co. ("WFC"), remain disappointing relative to comparable rates on depository accounts offered by *online banks,* such as Barclays PLC ("BARC-LON") and Goldman Sachs Group, Inc. ("GS"). These online options are increasingly compelling, with rapid upward adjustments in response to continued interest rate increases with rates far superior to those offered by traditional "brick-and-mortar" retail banks.

As can be seen below in Table I, this is an excellent option for investors seeking the safety and security of FDIC insurance coverage while earning a compelling risk-adjusted rate of return on excess cash with

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### Monthly Index Review
USD Total Return

| Data as of August 31st 2018 | August 2018 | 2018 YTD | 2017 | 2016 |
|---|---|---|---|---|
| S&P 500® | +3.26% | +9.94% | +21.83% | +11.96% |
| Dow Jones Industrial Average | +2.56% | +6.73% | +28.11% | +16.50% |
| NASDAQ Composite | **+5.85%** | **+18.31%** | +29.64% | +8.87% |
| Russell 2000 | +4.31% | +14.26% | +14.65% | **+21.31%** |
| MSCI Emerging Markets | **-2.67%** | **-6.93%** | **+37.75%** | +11.60% |
| MSCI EAFE | **-1.92%** | **-1.87%** | +25.62% | +1.51% |
| Bloomberg Barclays U.S. Aggregate Bond Index | +0.64% | **-0.96%** | +3.54% | +2.65% |

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limited interest in ancillary traditional banking services (e.g., onsite tellers, physical locations, etc.).

### Money Market Mutual Funds

Money market mutual funds, more commonly known as money market funds ("MMFs"), are pooled investment vehicles that typically invest in short-term, high-quality, and "lower-risk" fixed income securities, such as commercial paper, certificates of deposit ("CDs"), and/or U.S. Treasury bills. While many consider MMFs to be cash equivalences, investors in MMFs should be cognizant of the fact that MMFs are mutual funds with investment risks and underlying management fees. Just like fixed income and equity mutual funds, MMFs are regulated by the U.S. Securities & Exchange Commission ("SEC") and are not eligible for deposit insurance coverage from the FDIC.

Investors in MMFs are able to earn slightly *higher* interest income on their MMF investments relative to the interest earned on cash held in traditional depository accounts as a means of *compensation* for assuming incremental risks, including the potential loss of principal. Investors electing to allocate capital to and invest in MMFs are indicating their preference for *higher yield* and *interest income* at the expense of forfeiting the aforementioned principal protection afforded by FDIC insurance.

The average rates on money market funds at Fidelity and Schwab are 1.72% and 1.68%, respectively. Given online bank options (highlighted in Table I) offer higher rates and FDIC insurance, MMFs, which also incur a management fee, appear increasingly *less* attractive than online bank deposit options.

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*"More money has been lost reaching for yield than at the point of a gun."*

*- Warren Buffett*

### Table I: FDIC-Insured Cash Management Solutions

| Company Name | Account Types & Features | Annual Percentage Yield ("APY") |
|---|---|---|
| Charles Schwab & Co., Inc. | Brokerage Account - Bank Sweep | 0.22% - 0.52% |
| Fidelity Brokerage Services LLC | Cash Management Account | 0.25% |
| Bank of America Corp. | Savings | 0.03% |
| Wells Fargo & Co. | Savings | 0.01% |
| BB&T Corp. | Savings | 0.03% |
| Barclays PLC | Online Savings | 1.85% |
| Goldman Sachs Group, Inc. | Online Savings | 1.85% |

*Source: Charles Schwab & Co., Inc., National Financial Services LLC, Bankrate, LLC (www.bankrate.com)*
*Based on Standardized Results - Not Reflective of Account Minimums and/or Associated Fees*

### 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.

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### Certificates of Deposit ("CDs"): Laddered CD Portfolios

For considerable cash positions within Conservative and Ultra Conservative investment portfolios, laddering *certificates of deposit* ("CDs") is a viable management strategy in a rising rate environment, as the ladder can be deployed in longer-term bonds at higher rates as the CDs mature. By investing in a portfolio of short-term CDs with "laddered" maturities over a time horizon of ±9-12 months, investors with Conservative and/or Ultra Conservative investment portfolios may be able to mitigate the excessive and deleterious impact of the inverse relationship between the price of bonds and interest rates given their sizable strategic allocations to traditional fixed income assets. The downside of this strategy is that the cash is committed for the duration of the purchased CD.

As the whirlwind of inflation, rising interest rates, and strong economic performance creates a dynamic environment, we will keep slightly elevated cash levels invested responsibly in FDIC-insured vehicles when possible. Patience and astute cash management are dual recommendations as we navigate the later stages of this robust market cycle. Please feel free to reach out to the Investment Team with questions or dialog around cash balances.

### Table II: Certificates of Deposit ("CDs")

| Fixed Rate New-Issue (Non-Callable) | 3-Mo. | 6-Mo. | 9-Mo. | 9-Mo. Blended Ladder Weighted Avg. Yield-to-Maturity ("YTM") |
|---|---|---|---|---|
| **Fidelity** | | | | |
| Avg. Yield/Coupon | 1.85% | 2.05% | 2.15% | 2.02% |
| **Schwab** | | | | |
| Avg. Yield/Coupon | 1.85% | 2.00% | 2.15% | 2.02% |

*Source: Charles Schwab & Co., Inc. & National Financial Services LLC*

### Stock & Strategy Spotlight

| Name | Ticker | 2018 YTD |
|---|---|---|
| Target Corp. | TGT | **+36.98%** |

**Description & Investment Thesis**

At the beginning of the third quarter of 2017 ("3Q17"), shares of Target Corp. ("TGT") were trading at their lowest levels in over **±5 years** in terms of share price, as well as both absolute and relative valuations, as market/investor sentiment surrounding the stock waned in response to stagnant revenue growth, lackluster earnings results, and uninspiring near-term operating/business/financial guidance. While TGT appeared to be successfully managing through the public relations fallout from its massive customer data breach in late-2013, the impact on the company's business/operating activity came under increased scrutiny amidst renewed market/investor optimism and resurgent positive sentiment surrounding shares of the company's largest competitor - and one of the Investment Team's core long-term U.S. equity holdings - Walmart, Inc. ("WMT"), at a time when WMT was simply outperforming TGT from an operational standpoint through the execution of several strategic initiatives, such as WMT's **$3.3 billion** acquisition of Jet.com, Inc. in September 2016. Throughout 2017, shares of TGT traded at an average relative discount of **±25.0%** vs. shares of WMT, despite historically trading at a comparable/in-line price-to-earnings next twelve months' ("PE NTM") multiple - in November 2017, this relative discount increased to as much as **±41.0%**. Given the dramatic deviation in relative valuations from historical trends, the Investment Team decided that shares of TGT offered better risk-adjusted upside potential vs. shares of WMT, despite the fundamentally positive outlook for WMT. As such, the Investment Team initiated positions in shares of TGT across applicable client investment portfolios, including the firm's concentrated, high-conviction MP Core 20 Equity Portfolios, in September and October 2017. While shares of WMT continued to outperform through year-end 2017, shares of TGT have significantly outperformed WMT and the broader market year-to-date ("YTD") in 2018, returning **+36.98%** vs. **-1.35%** for WMT and **+9.94%** for the S&P 500® Index.

## Wealth Advisory Overview

# The Evolution of Technology in Wealth Management

### Technology Integration

Clients are becoming increasingly aware of, and have a vested interest in, their assets under management and how their portfolio is being managed. Therefore, a couple of years ago we launched the "Client Investment Portal." This portal gave clients access to performance information in real-time. Today, most individuals are on-the-go and seek a smart, quick, portable technology that can help keep up with their hectic lifestyles. They seek newer technologies that can provide real-time information about *all* of their assets, not just their assets under management, which can open up the lines of communication between advisors and clients. They want to know what is going on with all of their financial assets anytime and from any location.

In response to this request, we have been in the process of launching our "Wealth Advisory Portal." A key component of the new Wealth Advisory Portal is that it has the ability to provide data aggregation for clients. Data aggregation is the process of compiling information from various different custodians and consolidating it into one concise format. The ability to pull together this information and provide it to clients as a living balance sheet is valuable both to the client, as well as the wealth advisor because it allows a holistic view of a client's entire financial profile and provides the wealth advisor with the ability to provide comprehensive advice.

### What is the Client Portal?

We have been talking about the client portal since we launched the investment advisory website a couple of years ago. However, we wanted to revisit what the portal is, as well as how it is to be used. A client portal is a way of bridging the gap between the client and their wealth and investment advisory firm. According to the 2017 InvestmentNews Adviser Technology Study, 85.0% of "innovator" advisory firms - defined by InvestmentNews as firms that use technology to the fullest - offer a client portal. The client portal is a way of consolidating and organizing client data in an electronic format that is accessible to both the wealth advisor, as well as the client.

### Budgeting Tools

In addition to adding the data aggregation feature, the new Wealth Advisory Portal utilizes the transactional data from a client's linked accounts to categorize spending patterns and assist with budget development. This is an extremely valuable tool to provide clients who have not yet developed a budget with the constructs on where their cash flow is currently being directed.

### Training Opportunities

This month we are offering three in-house training sessions on how to navigate the Wealth Advisory Portal. Please look for upcoming correspondence regarding the details on how to sign up for these training sessions. These sessions will provide an overview of how to navigate the system, link accounts held at outside custodians, as well as how to best use the budget feature and client vault.

The continued adaption to the use of technology by the Wealth Advisory group is an important component in making sure that we maintain the highest standards in our concierge service delivery model. However, we understand that while clients may adapt to the use of technology, when it comes to making decisions and being reassured that they are on the right path, it is the interaction with their Wealth Advisor, not technology that delivers the most value.

## Around McShane Partners

### Wealth Advisory Portal Lunch & Learn Seminars

Please join us for an informational opportunity to learn how to navigate & understand your wealth advisory portal. Learn how to link outside accounts, utilize electronic vault storage, and access both wealth advisory and investment portals with one login.

Please choose from one of the following available informational sessions:

**Tuesday, September 11th**
11:00 AM - 1:00 PM (Lunch Provided)

**Wednesday, September 12th**
11:00 AM - 1:00 PM (Lunch Provided)

**Wednesday, September 12th**
4:00 PM - 6:00 PM (Light Refreshments Provided)

**If possible, please bring your laptop computer or tablet with you.*

RSVP to Lesley Burke at lburke@mschanepartners.com
or 980.585.3368

### Happy Birthday Sandy!

Sandy Carlson and her husband, Justin, celebrated her birthday in NYC at her favorite Greek restaurant - Loi Estiatorio. Sandy is pictured below with Chef Maria Loi!

### Second Quarter 2018 Economic Overview Luncheon Presentation

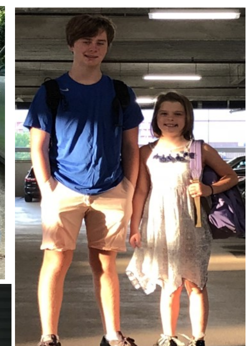
We would like to invite you to join us for lunch and presentation of McShane Partners' Second Quarter 2018 Economic Overview Webinar on Tuesday, September 18th by CIO Daniele Donahoe.

We will be discussing our thoughts on the significant financial, economic, and political developments throughout the second quarter of 2018.

RSVP to Lesley Burke at lburke@mschanepartners.com
or 980.585.3368

### Goodbye to Summer & Hello to a New School Year!

Below are the McShane Partners' little people heading eagerly back to school. At this rate, Christmas will be here before we know it.



**McShane Partners**

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

521 East Morehead Street | Suite 580
Charlotte, NC 28202
Phone: (980) 585-3373
Fax: (980) 265-1274
Email: mcshane@mcshanepartners.com

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