Commentary January 1st, 2018

Writer Ben Levisohn of Barron's described 2017 as a "perfect year" for stocks. The Dow Jones Industrial Average gained 25%, while the S&P 500 Index rose 19% and the tech heavy NASDAQ 100 climbed 28%. The S&P 500 finished in positive territory each month on a total return basis, while the DJIA was up for the last 9 months of 2017. The NASDAQ 100 did not set any monthly marks, but closed higher for the sixth consecutive year. (Barron's January 1st2018)

While U.S. stocks posted exceptional gains for 2017, international stocks did even better. The Index of Foreign Developed Countries excluding the U.S. and Canada increased by 25% and Emerging Markets surged 29%. (Financial Times January 1st2018)

These gains are the result of synchronized global economic growth, benign inflation, regulatory climates more disposed to business and expectations for reduced corporate tax rates in the U.S. The market once again showed it does not care about FBI investigations, fighting among Democrats and Republicans or North Korean missiles as long as these matters do not affect corporate profits, and none of them has thus far.

Companies in the S&P 500 are now trading at roughly 23 times their past 12 months of earnings, ahead of the 10-year average of 17 times earnings, according to FactSet. (Wall St. Journal December 30th 2017) With valuations stretched and investor complacency high, the margin of error declines. The market is vulnerable to an earnings miss from a large tech company, Trump's threats to rescind trade agreements and upward pressure on interest rates. Some investors simply question how much more room there is to grow after such a year of large advances.

There are also analysts worried that the potential benefits from a tax bill are already priced into shares, limiting further upside. While this is certainly cause for concern from an investment perspective, the impact of tax reform on our individual tax circumstances is also worthy of attention. Thanks to massive new tax legislation Republican lawmakers enacted at warp speed, significant revisions are going into effect in 2018. Most changes will not affect 2017 returns still to be filed, but prudent planning presages that changes in the code should be assessed at this time.

Standard deductions nearly double to $24,000 for couples, $12,000 for singles and $18,000 for household heads. Folks age 65 or up and blind people receive $1250 more per person. Given these higher amounts, it's a sure bet that far fewer people will itemize. Personal exemptions for individual files and their dependents are repealed. Home mortgages are nicked, as interest can be deducted on up to $750,000 of new acquisition debt on primary or secondary residences, down from $1,000,000. The popular deduction for state and local taxes is being squeezed, and people in high property tax - high income areas are naturally upset. Taxpayers will be able to deduct any combination of residential property taxes and income or sales taxes up to a $10,000 cap. Property taxes remain fully deductible for taxpayers in a business activity i.e. rental realty. (Kiplinger's Tax Letter December 29th 2017)

Several other write-offs are eliminated: Deductions for job-related moves, other than the military. All miscellaneous deductions subject to the 2% of AGI threshold, including employee business expenses, are gone. (Kiplinger's Tax Letter December 29th 2017)

Not all the news regarding itemized deductions is bad. The medical expense deduction is enhanced, as the threshold is lowered from 10% of AGI to 7.5%, for 2017 and 2018, while the charitable contribution deduction is preserved, with some minor revisions. (Kiplinger's Tax Letter December 29th 2017)

Those who utilize 529 accounts to save for college can now withdraw up to $10,000 for tuition at elementary and secondary educational institutions, making these vehicles even more appealing. (Kiplinger's Tax Letter December 29th 2017)

We trust you will find the broad-brush summary of the new law helpful. The bill is hundreds of pages, and we only touched the surface, but will cover various aspects of the law in more detail in future commentaries.

It is a propitious time for those with a designated allocation of stocks and bonds to review their accounts, as the stock weighting is probably higher than the target established, and a rebalancing in order.

We invite and encourage clients to contact us with questions and concerns and are available to meet at your convenience.