NEWSLETTER | SPRING 2021

Financial Planning Tips

Required Minimum Distributions (RMDs)

Although the CARES Act waived RMDs last year, RMDs are required this year and going forward. As in previous years, if the RMD isn't fully taken by calendar year-end, a 50% tax penalty is applied.

Year-end Tax Package Extends Charitable Deduction through 2021

Charitable contributions of cash—up to $300 for an individual, or $600 for joint filers—will be allowed in 2021 as an "above line deduction." You may take this deduction even if you do not itemize. Gifts to donor-advised funds and private foundations are not eligible.

Annual Exclusion Limit

For 2021, the annual gift exclusion amount remains at $15,000, but the lifetime gift exclusion increased from $11.58 million to $11.7 million per person.

Financial Plan and Estate Plan Review

The pandemic has highlighted the importance of planning—especially in the event of unforeseen change. In addition to providing individual, goals-based financial planning for our clients and their families, we also conduct detailed reviews of estate plan documents, such as Trusts, Wills, Powers of Attorney, and HealthCare Proxies. A financial plan aligns your unique risk tolerance and investment allocations with stated goals, and incorporates end-of-life priorities with tax and other regulatory considerations.

Looking Back and Forging Ahead

2020 was an atypical year with economic activity and equity markets plummeting at the onset of the health crisis. Forward-looking equity markets subsequently rebounded, driven by companies that were uniquely positioned to thrive in a work-from-home, shelter-in-place economy, but economic conditions continued to struggle. Looking ahead, we expect unique and ongoing challenges in 2021. On the one hand, pent-up demand will be a likely driver of economic growth, assuming vaccines are implemented successfully. On the other hand, policy measures, including additional stimulus likely to be passed by Congress in March, and increasing prospects of inflation will also influence markets and the economy. Despite an uncertain timeline for major market triggers, we believe it's critical to manage for the long-term—with a focus on sustainable growth, quality, and diversification.

A Passive Aggressive Approach

Markets experienced a roller coaster ride over the past year. After falling 34% following news of pandemic-related shutdowns in late February and early March 2020, the S&P 500 rallied nearly 70% through year-end from the March bottom. As of this writing, the S&P 500 index has increased by nearly 20% just since the election in November 2020—and investors have started taking notice. Although flows into equity based mutual funds and exchange traded funds (ETFs) were anemic for most of the past two years, investor appetite for stocks has picked up in earnest since the election. During the past 65 trading days, nearly $200 billion has flowed into equity based exchange traded funds.

Many investors are now chasing last year's impressive returns in the S&P 500, and they are doing so through the use of ETFs. There are three primary reasons why investors choose to invest in passive ETFs: equity exposure to the stock market, relatively low expenses, and broad diversification. Passive ETFs are investment vehicles designed to mirror an index or market segment. They are unlike actively managed investments, where a manager is paid to manage risk, diversification, and performance. Because they are unmanaged, they are an effective and cost-efficient way for investors to participate in the broader market. Among the most popular of these ETFs is the State Street S&P 500 ETF Trust (SPY), which tracks the S&P 500 index.

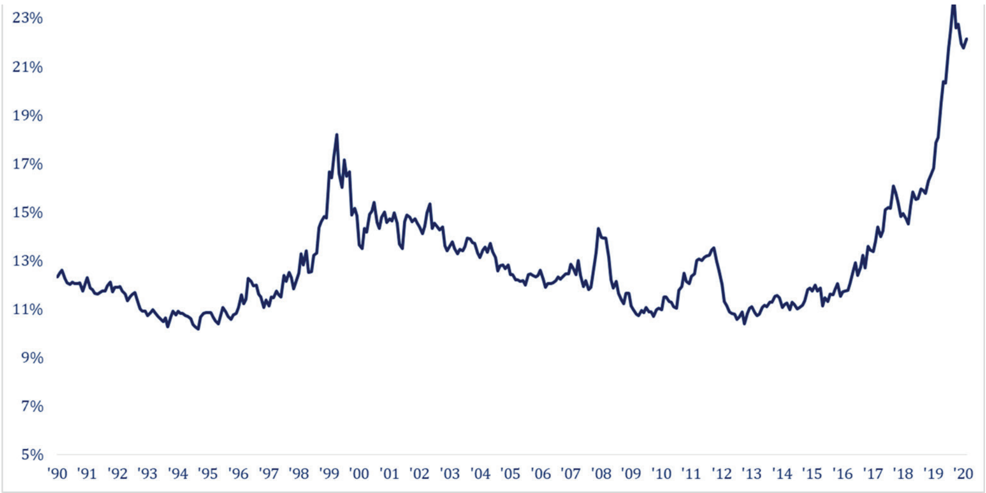
The Downside: A Game of Concentration

Over the past year, the diversification benefits gained from using passive ETFs like SPY have diminished greatly. The S&P 500 Index, which SPY aims to replicate, is a market capitalization weighted index, meaning the larger a company grows according to the value of its stock, the greater the proportion it holds in the index. Currently, the five largest companies in the index constitute approximately 22% of its overall value (see chart on reverse page). This is a higher concentration than at any other time, including the dot com boom when a small handful of technology stocks carried the S&P to dizzying heights.

Continued on reverse side

How did this happen? With the onset of the pandemic, the government responded with over $4 trillion of fiscal and monetary stimulus. Given the depths of the recession, only a small cadre of companies were able to produce meaningful growth, and the markets, flush with liquidity, placed a high premium on their shares. Companies such as Amazon and Facebook benefitted from stay-at-home protocols, and others, including Apple and Google, have had stable growth despite the pandemic. Never before have the fortunes of such a large index been tied to such a small group of companies.

Concentration Risks: Combined Weight of the Five Largest Stocks in the S&P 500



Source: Strategas Research

On the Move

We're pleased to share that our Portland office location has moved up the street, from 5 Milk Street to 2 Canal Plaza. We look forward to welcoming you to our new space. Our team continues to work remotely, but we are available to meet in person using social distancing at our offices or one of our many banking centers. Phone calls, emails, and video conferencing are always available.

Human nature tends to lure investors into funds or styles that have performed well in the previous year. Last year's winners, however, are not necessarily the next year's top performers. History has taught us that pullbacks are a natural part of the ebb and flow of the markets. While active managers work to mitigate the risks born by shifting market dynamics, those invested in the indexes are held captive, now more than ever, by the dependence on the performance of just a handful of companies. With concentrations in the indexes as high as they are, investors are increasingly exchanging broad market risk for company-specific risk, which can run counter to one of the underlying tenets of investing in passive ETFs – diversification, which seeks to mitigate company-specific risk.

Active Pursuits Ahead

As vaccinations roll out and prospects for an open economy grow, we are closely watching the recent increase in interest rates. The 10-year U.S. Treasury bond, a benchmark rate for long-term investors, started the year near .90% and, as of this writing, is approaching 1.60%. Though the numbers are small, the pace of the increase is meaningful. While some sectors of the economy benefit from rising interest rates (for example, banks and insurance companies), others are subject to increasing headwinds. Price levels that investors are willing to pay for high growth companies can become vulnerable to downward pressure as interest rates increase. If investors become more price-sensitive in the face of rising interest rates and shift toward companies more levered to economic recovery, then the five companies that fueled so much index growth in 2020 could face mounting pressure.

This dynamic suggests the benefits of active management—with direct attention to diversification, quality, sustainable growth and the risk-reward tradeoff—will become increasingly important and present an opportunity to simultaneously enhance returns and lower risk in 2021.

Camden National Wealth Management provides investment management, goals-based financial planning, and trust and estate services to individual and institutional clients in Maine and throughout the United States. Our highly credentialed team averages 25 years in the business and includes Chartered Financial Analysts, estate planning attorneys, CTFA trust specialists, and financial planners. Together, we bring a customized investment and planning approach to meet each client's unique financial needs.

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