Trust Company *of* Vermont
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Brattleboro ◆ Burlington ◆ Rutland ◆ Manchester

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There is No Such Thing as a Risk-Free Lunch

Paul Copeland, CFA & Portfolio Manager

Like many people, I was surprised by a refund check from my insurance company as COVID-19 stay-at-home orders have led to fewer accidents. While I'm driving much less, I do drive to the supermarket as I've had more opportunity to make meals these last few months. Driving is the number one cause of death in most age groups, so while gathering food is probably safer today than in previous centuries, it's not without risk. Even with many precautions supermarkets are taking, the risk of catching the corona virus is staring me in my masked face while I'm picking out food. Accident and disease are not the only risks I think about either. There's the risk of rejection as my kids remind me in subtle and not-so-subtle ways that Mom's a better cook. To please the young judges, I'm tempted to cheat and add lots of butter and/or sugar. Thankfully, my wife has educated me to the long-term risks of unhealthy foods. My colleague, Todd Gray, can confirm that unhealthy foods have short-term risks as well. He almost died choking on a chocolate truffle. We might tell Todd to eat more kale, but he could easily choke on that too.

The last few months have reminded me that investments are like my lunch. There's risk in whatever I choose.

We were reminded of the risks of stocks on March 9th when the S&P 500 index was down 7.6%, and again three days later on the 12th (down 9.5%). After a weekend break to enjoy some social distancing, we were hit with another punch in the stomach on the 16th (down 12%). In just over a week, we experienced 3 of the 20 all-time worst daily percentage drops for the S&P 500. To be fair to March 2020, it wasn't all bad in the markets. On the 13th and 24th the S&P regained about 9.3% and 9.4%, respectively, both days registering among the 20 all-time best daily percentage increases for the S&P. These movements up and down were impossible to predict and often difficult to explain, even in hindsight. Many positive days in the market coincided with negative economic news. After a 34% drop in the S&P from the high point through March 23rd, and the 9.4% increase on the 24th, one of the front-page headlines from the NY Times read: **"Coronavirus in N.Y.: 'Astronomical' Surge Leads to Quarantine Warning"**. Many braced themselves for another market drop, but instead, stocks climbed almost 30% over the following six weeks. We were likewise recently reminded of one of the many risks in bonds – credit risk. Corporate bonds displayed this risk with companies such as JCPenney filing for bankruptcy. This risk was also discussed in government issued bonds. The most memorable example was the political rhetoric suggesting that maybe states should consider bankruptcy. There is also the more likely possibility that certain municipal revenue bonds could have trouble making payments. Meanwhile, many developing countries don't have the healthcare and other resources to deal well with COVID-19. Investors are questioning some governments' ability and willingness to repay debt during a crisis.

The risk in "risk-free assets" is not as striking, but it is very real. The 3-Month Treasury Bill is often used as the risk-free rate. Early June it was 0.15%. A year ago, the yield was 2.28%. The rate on cash invested in money markets is similar. For some investors there is a short-term risk referred to as FOMO (Fear Of Missing Out). They liquidate their cash stores, typically used to cover near-term expenses, in order to jump into the surging stock market. The last few months have led others to sacrifice long-term growth potential to sit in a perceived bunker of safety, where the very real risk for them is the long-term negative impact of inflation.

I recently bought a plane ticket to Chicago for my 25-year college reunion (that may or may not happen) this fall. The ticket was cheaper than many of the same flights I took more than 25 years ago. Similarly, present computer costs are about 20% what my computer in college cost. Yet while some items do get cheaper due to better technology, the overall cost of living continues to rise. The dollar from when I started college is worth about 52 cents today. Sometimes it's easy to forget about inflation, but it is a very real risk to people's ability to meet financial goals, such as helping kids or grandkids with their education. Tuition at my college has risen about 400% since I was there.

While inflation has come down this past year (and it's only been this low a few times in the past 50 years), it is still at 1.4%. Subtract this from the risk-free rate of 0.15% and you are losing out every year. This negative real yield can go positive, as it has often been historically, but a low interest rate environment highlights the risk of inflation to "risk free" investments. More discouraging for investors looking for safety is that the 10-year Treasury is only yielding about 0.7%. Therefore, the safe bet is that adjusted for inflation, you will lose money by investing in a US Treasury Bond maturing in 2030.

Life is full of risks. While we can't eliminate all risks in our lunch, we can mitigate them by doing things such as wearing a mask at the supermarket. Likewise, we can lower risks in our financial "lunch" by allocating assets with time horizon in mind, knowing that the stock market has greater short-term risk and the money market has greater long-term risk.

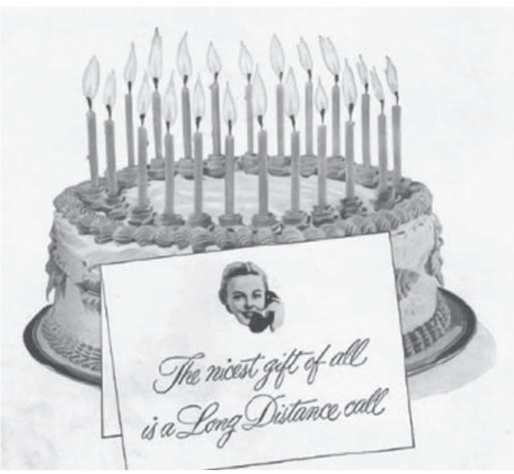
Money needed in the next few years should be kept in stable investments (cash and short-term bonds), with low chance of losing value. This allows other money to stay invested in a longer-term allocation of stocks and fixed income that should beat inflation and increase the probability of meeting longer term goals.

Estate Planning & Privacy

Jack Davidson

Communication and the cost of privacy

Understanding communication in the early sixties was a challenging issue for college students. As a first-year student faced with learning liberal arts, understanding mathematics was a critical piece for survival. Do I write a long letter to my parents that will cost 4 cents, or do I make a long distance call that will cost $3.50, if I don't talk over 3 minutes?



In those days, gas would cost perhaps 30 cents, but many college students did not own cars so the analysis of when to call home, or travel home, was an issue. The bus or train might be helpful, but not often used by many students until Thanksgiving.

In my first semester, I made a profound financial decision. Should I call my girlfriend or my parents? Communication can be very complex.

After my arrival in Vermont, in 1971 I moved from Brattleboro to East Dummerston and discovered another complexity: phone party lines. As I recall, I did not have a choice. The service was common in sparsely populated areas where remote properties were spread across larger distances. In my neighborhood, we had three neighbors who shared the same phone line, so I could listen to their calls and they

could listen to mine. One day I called a friend, and as a joke, I said "Joe, I think one of my neighbors is listening". I did not think that any of my neighbors were listening until I heard an angry "Oh really?" and one of my neighbors exited with some anger, based on the sound of a slamming phone.

It has become evident during this pandemic crisis, that communication is very important. For the most part, Zoom® calls are cost effective and a wonderful way to bring families and friends together, but privacy may be an issue. Our smartphones are a

wonderful and cost effective way to communicate, but they may not be as private as one might think.

Privacy in estate planning has many pluses, and perhaps a few negatives. Many planners recommend a Living Trust and a Pour-Over Will to not only save probate costs, but to ensure privacy. The Will, which is a public record, simply says everything goes to a non-testamentary Trust, called a Living Trust, which will insure the provisions of the trust and the administration of the trust assets will remain private. Only assets passing through the estate will become public, and many planners will address this issue as well. For example, lawyers might suggest that the client be the trustee of their revocable living trust and transfer many, if not most, of their assets to the trust, naming the client as trustee. The client can still control the account as if the trust did not exist, and in most cases, the name change will not require a separate tax return. The assets will continue to be taxed on the client's income tax return as if the trust did not exist, until death of the client.

One negative of privacy is the behavior of the trustee. Some trustees may be inclined to benefit themselves

rather than the beneficiaries. Some trustees may unknowingly misbehave. A trustee needs to comply with complex fiduciary and tax laws. Selecting corporate trustees will insure privacy, and will be privately supervised by regulatory authorities. For example, in Vermont, the Department of Financial Regulation monitors the Trust Company of Vermont.

Another factor to consider is the relationship between an individual trustee and the lawyer who drafted the document and/or the firm, especially if the lawyer is older than the client. Individual trustees have to deal with complex legal laws and fiduciary tax returns, and the periodic guidance of an experienced advisor is important.

When creating or revisiting your estate plan, consider those who will receive accountings each year. If they

see misbehavior, they can ask the Probate Court to review the actions of the trustee. Also consider a Trust Protector (14A V.S.A. § 1101), for example, a family friend, who can monitor the actions of the trustee.

In summary, privacy and cost of supervision is often an important aspect of planning. Laws are built on a foundation of rationality. Communication is very important and communication is complex.

I still ponder my decision to call my girlfriend rather than my family. In my first year of college, my absent-minded brain was, unfortunately, fully formed. I found a phone booth, inserted many quarters and absent-mindedly dialed my home number rather than my girlfriend's number. At the time, my parents were challenged by the financial crisis of having three of their five children in college, all subject to the expense of long distance calls. When I heard my mother's hello

I thought "what is she doing at my girlfriend's house?" "Hello?" she said once again. In those days, you could not tell who was calling. She only heard silence. And then she said "Jack, you were calling Mary Ann, weren't you?"

In Memory

Ernest W. Gibson III was a founding director of the Trust Company of Vermont. His erudition, gentle wit and careful counsel left a deep impression on all of us who knew him. Careful with his words, he could command a room with a natural gravitas, befitting the Justice he was. He contributed generously to our company's early days and will always be missed and fondly remembered.

Congratulations to John Abel!

John Abel, a founder of Trust Company of Vermont, recently retired. John was an integral part of our company, and his contributions will always be valued and remembered. His skills, hard work, commitment, and dedication were very important to us and he will be greatly missed.

We wish him all the best!