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# BKMWM Newsletter September 2023

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## Topics:

1. Stock Market Update
2. Diversification
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5. Inherited IRA News
6. Technology Changes

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## 1) Stock Market Update

In our June newsletter, we cautioned that the S&P 500 index was being driven by a small number of very large, tech-oriented stocks. This continues to be the case, so we will repeat ourselves a bit.

*"So far this year, the (Magnificent Seven) – Apple, Microsoft, Google parent Alphabet, Amazon, Tesla, Nvidia and Facebook parent Meta – are responsible for three-quarters of the S&P 500's gains. It has been a dazzling display." – Michael O'Rourke, JonesTrading Strategist<sup>1</sup>*

On average, those seven stocks are up roughly 89% year-to-date and the tech-heavy Nasdaq 100 index is up over 37%. Meanwhile, the average stock in the S&P 500 is up less than 5% (as measured by the Invesco S&P 500 Equal Weight ETF). The "Magnificent Seven" are valued at 58 times their trailing 12 month earnings and 40 times their expected forward 12 month earnings.<sup>2</sup>



Chart Source: Market Watch/FACTSET 08/28/2023

We continue to encourage clients to diversify beyond the S&P 500 index. Consider small to mid-size companies and international stocks. Additionally, with short-term interest rates exceeding 5% on bank CDs and U.S. Government treasury bills and money market funds, there are ways to get inflation fighting and wealth building returns outside of stocks. Diversifying should reduce your portfolio's volatility, risk, and help you avoid emotional decision-making.

Contact us to discuss how we are positioning portfolios.

<sup>1</sup> Source: "US stock market needs more than the Magnificent Seven". Financial Times, Jennifer Hughes. August 25, 2023

<sup>2</sup> Thomson Reuters Quotes & Markets. Smartstation August 28, 2023.

## 2) The Value of Diversification

It is a basic principle of investing that a portfolio benefits from diversification. However, we often oversimplify the value of diversification by boiling it down to, "don't put all your eggs in one basket." Intuitively, you reduce your risk by spreading exposure across several investments so that if any single investment does not work out, it will not collapse your entire portfolio.

However, there is more to it than that. Diversification not only reduces the likelihood that one bad apple spoils the whole bunch, but it can also reduce the volatility of your portfolio. Reduced volatility helps minimize market-timing risk, which can lead to better, more consistent performance over time.

Common questions regarding diversification include, "Why would I want to own both ABC and XYZ, when ABC returned 10% while XYZ only returned 5%?", or "Why do I want to own securities that move in opposite directions, when that means something will always be going down?". Different assets perform well in various economic and market conditions. Therefore, holding a mix of assets can increase the likelihood that at least some of them will perform well even as others might lag, potentially leading to more consistent overall returns.

Moreover, diversification can help prevent emotional decision-making. When investors see a particular asset performing well, they might be tempted to concentrate more of their portfolio in that asset, chasing recent gains. This can lead to greater risk exposure. Diversification encourages a disciplined approach to investing, reducing the likelihood of making impulsive decisions based on short-term market trends.

For BKM Wealth Management's financial advisors, thoughtful diversification in portfolio construction helps us to optimize the efficiency of your portfolio. With your input, we can choose to maximize your potential return based on your desired level of risk, or to position for a targeted level of return with the minimal amount of expected risk. Diversification helps us create more resilient and balanced portfolios that are better equipped to handle the ups and downs (volatility) of the market. Lower volatility helps increase the likelihood that you can avoid emotional decision-making, thereby increasing the chance that you will achieve your goals.

These are some of the dynamics that we consider every day when managing your portfolio. Please feel free to contact us at any time to discuss.

## 3) Additional Performance

Everyone wants a portfolio with good returns, so a lot of attention is paid to finding the best performing investments, and rightly so. However, the painful truth is that finding the best performing investments is very difficult. As Yogi Berra once said, "It is difficult to make predictions, especially about the future." That is why it can be important to also consider other, more controllable factors when managing portfolios and planning:<sup>3</sup>

- a) **Minimizing Portfolio Turnover.** Turnover is a measure of how often the positions in a portfolio are changed in a set period. In taxable accounts (non-IRA/retirement accounts) turnover can lead to higher short-term gains which are taxed unfavorably relative to long-term gains. Higher taxes may not show up in a standard measure of portfolio performance, but taxes are a very real cost, and minimizing them can improve real-life performance.
- b) **Proper Asset Location.** Asset location takes into consideration the various account types (IRAs, Roth IRAs, retirement plans, taxable accounts, trust accounts, health savings accounts, 529 college savings plans, etc.) and the differing tax efficiency among investments. For example, a high turnover mutual fund, and income-oriented strategies may be most suitable for tax-deferred accounts which aren't taxed on gains or income, but instead are only taxed on withdrawals. The intelligent and intentional location of assets can improve real-life portfolio performance.

At BKM Wealth Management, we want to ensure that all measures of your portfolio's performance are considered and planned for. Contact us anytime to discuss strategies that might improve your all-in performance.

3) Quote and Concept Source: 7 "Tax Strategies Financial Advisors Need to Understand", Barron's, Jonathan I Shenkman. 8/24/23

#### 4) Finding The Right College

Fall is a time when many high school seniors will apply to college. Helping your student choose the college that is right for them can be daunting. Where should they apply? Which schools are a good fit? How much do they cost? What scholarships are available? BKM Wealth Management can help!

We have tools that can help your student find the right fit. Search for schools by:

- Net Cost
  - Actual cost WITH likely and automatic merit-based scholarships included!
- Geography
  - Both location and/or setting (city, urban, suburban, rural)
- Size & demographics
- Likelihood of acceptance based on the student's:
  - GPA
  - SAT and/or ACT score
- Intended major
- Size of enrollment
- Class sizes and student/faculty ratios
- Athletics
- Rankings (Forbes and U.S. News)
- Private or Public
- And much more!

Parents should also be aware that there are several changes expected to go into effect for the October 1<sup>st</sup>, 2023 Free Application for Federal Student Aid (FAFSA) coming. Among the changes, FAFSA will be shorter, the discount for multiple children in college is eliminated, only the divorced parent that provided the most financial support during the prior 12 months can fill out the FAFSA, and financial support from grandparents and other family members no longer counts towards the expected family contribution (EFC).

Please contact us for assistance in finding your student's best fit.

#### 5) Inherited IRA News

Since new rules went into place in 2020, there has been confusion as to whether distributions from inherited IRAs need to happen on an annual basis. Old rules allowed a beneficiary to "stretch" distributions over the course of their lifetime by taking distributions annually based on their life expectancy. This changed when the Secure Act of 2019 implied that most non-spouse beneficiaries of retirement accounts inherited after the year 2019 would require distributions over a 10-year period.

In July, the IRS issued new guidance on the rules. The new guidance allows most non-spouse beneficiaries to delay distributions in 2023 without penalty. While you may skip a distribution this year if you choose, most IRAs inherited post-2019 will still need to be emptied within 10 years of the original owner's death. This means if you do not take a distribution in 2023, more money will need to be withdrawn in future years to make up the difference.

So, while no distribution may be required this year (see future IRS guidance on this to keep up with the changing landscape) you still may want to consider whether taking a distribution would be advantageous by spreading the distributions over more tax years.

Contact us to discuss your inherited IRA's efficient distribution strategy.

## 6) Technology Changes

If your accounts are held with TradePMR/First Clearing (aka: Wells Fargo) you should see improvements to the log in process on Saturday, September 23<sup>rd</sup>. Wells Fargo is adding Two Factor Authentication (2FA), a more intuitive password creation/change experience, and removing the need for client created security questions.

Two-Factor Authentication is the industry standard for providing additional levels of protection against fraud and cyberattacks on websites and applications that hold important data, like financial, health and other personal information. 2FA can help provide many benefits to both users and businesses, including:

- Increased protection against phishing.
- Reduced risk of account takeover.
- Compliance with industry regulations.
- Enhanced trust with users.

The first time you login to your account after September 23<sup>rd</sup> you will be taken through the 2FA process. Meanwhile, please ensure that an accurate phone numbers and email addresses are listed under "Customer Service" → "Contact Information".

Reminder: BKM Wealth Management has invested in technology that provides most clients with an alternative to the TradePMR/First Clearing access online site. The BKM Client Portal provides a consolidated view of all your accounts, not just those managed by BKM. You can link and view your 401k plans, credit cards, mortgages, bank accounts, etc., with balances automatically updated daily. The portal also allows you to track your financial plan, net worth, and performance. You can even view your account statements, tax documents, BKM Wealth Management newsletters (like this one), estate documents and more.

The new BKM Wealth Management Client Portal and corresponding mobile apps are available now. If you would like access, please contact your advisor to find out if your accounts are eligible.



*Financial advisors whose mission is to positively impact lives.*