MERITAS ADVISORS

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November

World Debt

Cause for Alarm?

Global government debt is growing. Twenty years ago, the estimate for government debt for all countries was estimated to be around $20 trillion. Today, that number has ballooned to $69.3 trillion, and we are now at the highest debt-to-GDP ratio in human history: 81.8%.

You can see from the graphic which countries have the highest debt—and of course, the U.S. leads the way in this dubious statistic, with $21.5 trillion, and a debt-to-GDP ratio (dividing how much the country owes its bondholders by the total amount of economic activity in a recent year) over 100%. The graphic is also color-coded to show the countries that seem to be in a danger zone as far as their ability to repay what they've borrowed. Japan leads the world with a 237.1% debt-to-GDP ratio, but Greece, Venezuela and the Sudan are not far behind. Italy's debt levels are also worrisome; the debt-to-GDP ratio there is 132.2%.

At the other end of the spectrum, you have the Republic of Korea, with just 0.9% of all the world's government debt, and a debt-to-GDP ratio of a comfortable 37.9%, better than Australia (41.4%), China (50.6%) or Mexico (53.6%).

The first thing you think when you see those figures is that the world may be coming to an end. But surprisingly, most global economists are not worried by the growing levels of government debt. When you add the government debt to private debt around the world, the total borrowing reaches $164 trillion, a figure calculated by the International Monetary Fund. But the IMF's most recent warning, in issuing those figures, was that high levels of debt might make it harder for the world economy to climb out of a recession, but that trade wars and protectionism are currently the greatest threat to global growth.

The most likely scenario: higher taxes in the future to pay down what has become a (long-term) unsustainable debt load, not just in the U.S., but in the other high-debt countries as well.

Sources:

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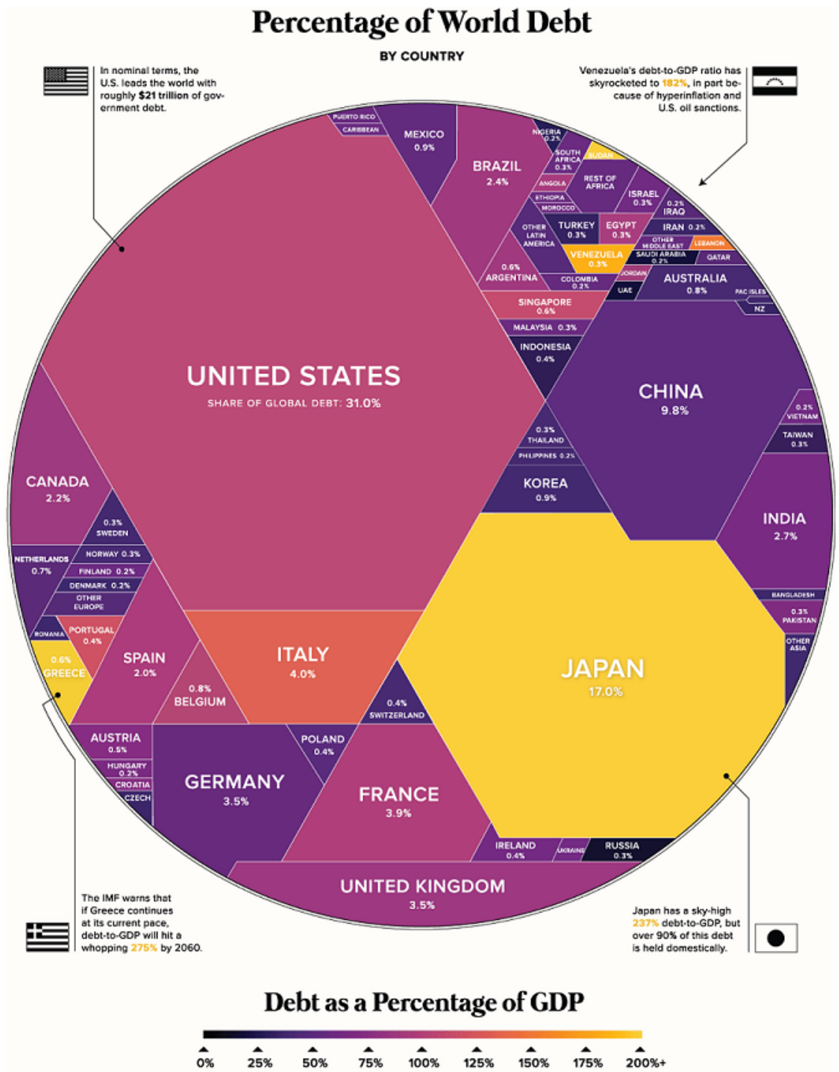


The market at a glance

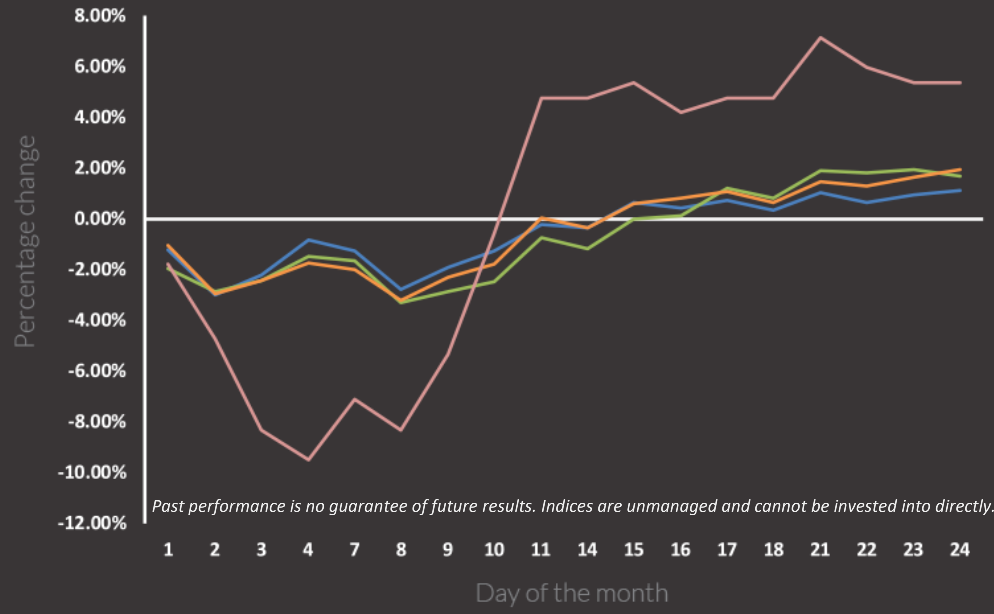
October

U.S. Large Cap
(S&P 500)
3,037.56 (2.04%) ▲

U.S. Mid/Small
(Russell 2000)
1,562.45 (2.57%) ▲

International Large
(NYSE International 100)
5,495.36 (1.79%) ▲

U.S. Treasuries
(U.S. 10-year Treasury yield rate)
1.69 (0.60%) ▲



The market in action

- Electric-car maker Tesla saw shares rise nearly 20 percent following news of a $143 million gain in the third quarter, despite analysts' expectations to post a loss. Tesla reported it delivered 97,000 cars in the quarter and will need to deliver another 105,000 in the fourth quarter to meet its annual forecast.

- Shares of Microsoft rose three percent and reached an all-time high following news that the technology company secured a $10 billion contract from the Pentagon for cloud computing services, beating out rival Amazon for the deal. So far in 2019, Microsoft shares have risen more than 40 percent.

- After posting a strong third quarter where it added 6.8 million subscribers, shares of video streaming service Netflix were trading up nearly 10 percent. Revenue in the quarter grew 31 percent compared to the same period last year as the company continues to expand its international offerings.

- Food delivery service GrubHub saw its shares fall more than 40 percent following disappointing earnings in the third quarter. So far this year, the stock has lost more than half its value, with several analysts downgrading the stock after the news.

Common Estate Planning

Pitfalls

Estate planning is complicated. There are a lot of moving parts to organizing your finances and determine where they will go after your death. And in many cases, people simply sign a stack of documents at their attorney's office and think the job is done.

The result? A lot of mistakes, a lot of people falling into estate planning pitfalls. Here are a few that you should try to avoid.

1) Naming the wrong executor. These are the people who are appointed to take legal control over the assets when you pass away. Executors collect all the assets of the deceased, pay final debts and expenses, and file federal and state estate tax returns (if needed). Unfortunately, it is not uncommon for the named executor, years after the documents have been signed, to be deceased or no longer suited for the position because he/she is too elderly. If a professional is named, is the attorney or CPA still in business? Meanwhile, children who were too young to serve when the documents were signed may now be capable of taking on the executor role.

Solution: periodically check to see who has been named as the executor in the estate documents. Is that still appropriate?

2) Not updating documents to reflect the maturity and financial conditions of the children. Estate planning documents that were created when children were young will have named a guardian, but when the children reach maturity, that would no longer be necessary. The document may leave assets to trusts on behalf of the children, when it makes more sense to distribute them directly to the adults they have become. And in some cases, an unequal distribution of assets might make sense, if one adult child has become financially successful while others are struggling. Finally, when children are minors, they typically don't need health care powers of attorney, living wills or advance health care directives. Once they become adults, they should consider having these documents in their own right.

Solution: check to see the provisions in your will or trusts that relate to the children, and update as necessary.

3) Inappropriate health care directives. Under the Health Insurance Portability and Accountability Act, every individual's medical records and other personal health information is confidential, meaning it cannot be shared with anyone, including family members, without written authorization. Lack of this information and specific directives could impede decision-making by others when you're incapacitated or approaching the end of your life.

Solution: check and update your family's health care powers of attorney, living wills and advanced health care directives.

4) Inappropriate estate tax provisions. In 2019, individuals are legally permitted to transfer assets valued at $11.4 million ($22.8 million for married couples) free of federal estate and gift taxes. But outdated estate documents might include planning that was appropriate for much lower exemption values—for example, forcing a trust for the heirs to be funded up to the applicable exclusion amount, which might impoverish the surviving spouse.

Solution: review the formulas in the estate documents with your attorney and/or tax professional.

5) Estate documents drafted in a state where you no longer reside. Every state has its own estate and income tax laws; some are common law property states while others are drafted with community property laws. There can be significant differences between them when it comes to transferring assets. Moreover, 17 states also impose some form of estate or inheritance tax, with different exemption amounts. Some estates that would not be subject to a federal estate tax might be subject to state estate taxes. If your documents were drafted in a different state from where you currently reside, they could be outdated and misapplied.

Solution: review your estate plan to see if it is still appropriate, with an eye toward reducing state estate taxes and making sure they reflect your current residency.

6) Not utilizing portability. The federal estate rules say that a surviving spouse can take advantage of any unused portion of the spouse's exclusion amount. But that's only true if the estate files a federal estate tax return within nine months of the deceased's passing. (This can go up to 15 months if an extension is granted.) In the normal case where the deceased's estate would not have to pay estate taxes, often nobody realizes that the federal estate tax return (showing zero taxes have to be paid) has to be filed. This can be costly in some larger estates, where the second spouse dies with more than $11.4 million in wealth.

Solution: Some families set up a credit shelter, bypass, family or exemption trust that would be funded with assets from the first spouse's estate. That preserves not only the portability of those assets, but any growth in those assets would not be counted in the estate tax calculation. The surviving spouse could also disclaim part of the deceased's assets, allowing them to pass to the children. Or the executor of the estate can file the federal estate tax return, preserving the portability of $11.4 million of additional estate tax exemption.

7) Failing to plan for capital gains taxes. Most estates will never pay a federal estate tax, which means that the tax planning should be concentrated on income tax planning. One important consideration is the step-up in basis for appreciated assets, which means that, for the heirs, the capital gains tax obligation on the amount of appreciation during the deceased's time of ownership will vanish. This is the closest thing to a free lunch, in the tax world, that you can get.

Solution: Save some highly-appreciated assets like legacy stock positions and shares of the family business from the normal rebalancing and diversification activities, and pass them on to heirs.

-Bob Veres

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