PERSONAL CAPITAL
Survey

Affluent Investor Outlook

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HEAT CHECK

How the Affluent Feel About 2018

Even for those who seem to have everything, the future is still uncertain.

This is according to a Personal Capital survey of America's affluent (defined as those who have total investable assets of $500,000 or more) on how they are thinking about and preparing their financial futures.

With one of the longest bull markets in history now almost a decade old, many affluent investors are wondering what comes next. Will the market continue on its upward trajectory or will it finally come crashing down? What's the best way to structure an investment portfolio to protect against the uncertainty ahead? How will tax policy and the 2018 midterm elections impact investment opportunities?

The answers to these questions varied widely among the mass affluent, with significant differences across generational, income and geographic lines. For example, what's top of mind for a Millennial with young children that will one day require expensive college tuitions is likely very different from what is most important for a Baby Boomer that has an empty nest and a 401(k) that has been building for four decades.

To explore these differences, Personal Capital commissioned a survey in conjunction with ORC International of 1,000 affluent Americans, asking them everything from how they feel about tax reform to what concerns they have about financial planning.

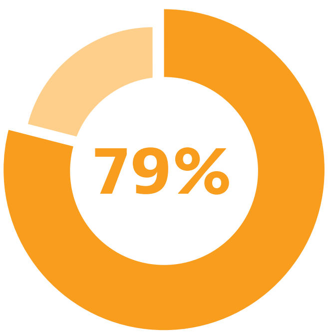
THE BOTTOM LINE: Although the mass affluent are optimistic that markets will continue to climb in 2018, many are nervous that they aren't prepared for a potential market downturn or other financial challenges, and they are divided on the impact that Trump and tax reform will have on their finances.

Faith in the Market, But Fear in the Portfolio

Affluent investors are optimistic about the direction of the market, with nearly half (48%) believing the market will perform better in 2018 than it did in 2017, and nearly one-third (31%) saying it will perform well next year but not as well as in 2017. Only 9% think the market will decline in 2018.

Millennials, many of whom have never invested during a bear market, are especially optimistic, with 67% predicting 2018 will be an even better year than 2017, versus 53% of Gen X, 32% of Baby Boomers and 32% of Silent Generation.

But this enthusiasm is tempered when you look at investors' portfolios.



of affluent investors

think that the bull market will continue into its 10th year in 2018 with an additional 12% predicting the market in 2018 will stay flat.

A shocking 16% of affluent investors—and 25% of Millennials—have most of their net worth invested in cash, a frightening proposition given today's low interest rates. If inflation rises and interest rates remain low, then holding cash in a simple savings account would, in effect, be like manufacturing your own market downturn. While there are many valid reasons to keep cash on hand even during a bull market (saving up to build an emergency fund or buy a home), the data suggests that many people may be missing valuable investment opportunities by not being diversified.

Sixty percent of people—and 87% of Millennials—say they made a financial mistake in 2017, such as not saving enough for retirement, paying too much for luxury items and not having a portfolio that can withstand a market downturn.

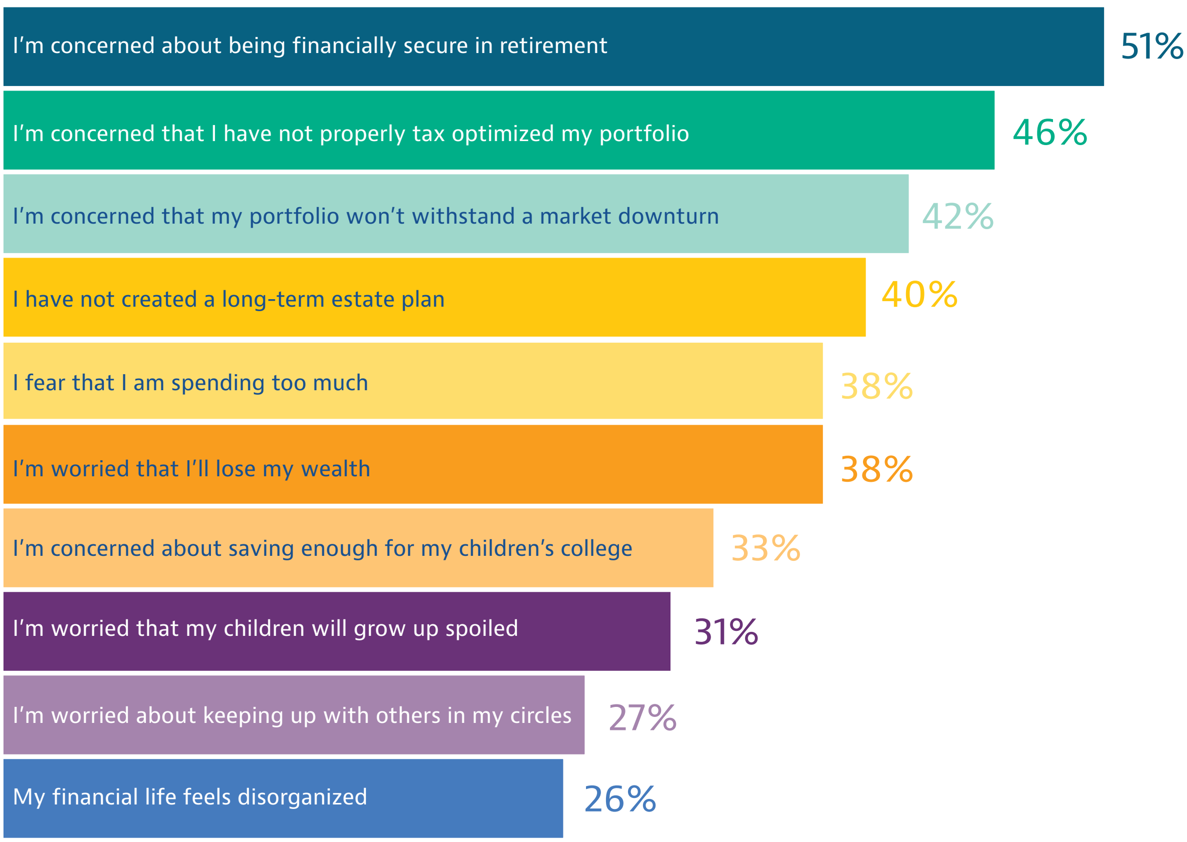
The good news is that mistakes can be fixed.

While no one can predict where the markets will go, recency bias makes it easy to forget that markets are cyclical and that we will eventually see a downturn. A lack of diversification can be like a ticking time bomb in investors' portfolios. The key to protecting against such a scenario is careful and smart financial planning.

What's Keeping the Affluent Up at Night?

The financial lives of the mass affluent are filled with worries, with retirement planning, tax planning and long term portfolio health among the three top things the affluent are losing sleep over.

THE BIGGEST FINANCIAL CONCERNS OF AFFLUENT INVESTORS



54% of affluent Americans said they have most of their net worth invested in stocks, with cash (16%) and U.S. bonds (8%) a distant second and third. However, significantly more Millennials said most of their net worth is invested in cash (25% vs. 17% of Gen X, 8% of Baby Boomers and 6% of Silent), which is the exact opposite of traditional asset allocation models that call for reducing ownership in historically high-risk assets (such as stocks) and reallocating to historically low-risk assets (such as bonds and cash) as an investor ages and prepares for retirement. Personal Capital helps Americans put their money to work, with only 4% of dashboard users with $500,000 or more in investable assets holding more than 50% in cash.

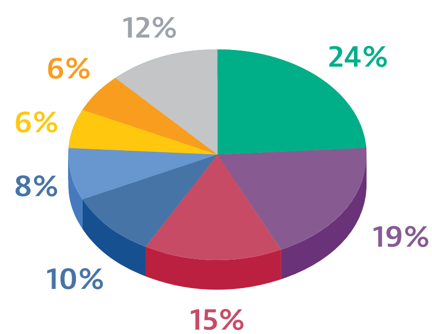
Honesty is a key part of financial success, and acknowledging a pain point can be the first step in fixing a financial problem. 60% of respondents were willing to admit to making at least one financial mistake in 2017, with 87% of Millennials being especially forthcoming about their faults (vs. 66% of Gen X, 40% of Baby Boomers and 30% of Silent Generation).

AFFLUENT INVESTORS REPORT THEIR **BIGGEST FINANCIAL MISTAKES OF 2017**

1. Didn't save enough
2. Paid too much for a luxury item/items
3. Paid too much in fees to investment firms/advisors
4. Made emotional decisions in buying or selling investment(s)
5. Wasn't diversified enough
6. Did not optimize tax strategy

TOP FINANCIAL GOALS OF 2018

- Tax optimizing my investment strategy
- Getting ready for retirement
- Getting a handle on my financial life
- Setting up an estate plan
- Reducing investment fees
- Getting on track to put my child(ren) through college
- Setting up a charitable giving plan
- Other



Meanwhile, the affluent already have their sights set on 2018, with tax optimization and retirement planning coming up as their two biggest financial goals. With Congress expected to pass sweeping tax reforms that will affect 2018 tax returns, tax planning is expected to stay top of mind for many investors.

of those with a budget, will have stuck to it at the end of the year showing the importance of proactive planning. 54% of all affluent investors created a budget in 2017. Millennials were the most budget-oriented of any generation (78% vs. 60% of Gen X, 38% of Baby Boomers and 23% of Silent).

The Trump Effect

The affluent were likely among those most tuned in to the national debate over tax reform. But just like other Americans, wealthy individuals all over the country are divided over everything from what's an appropriate tax rate to whether Trump's policies are a net positive for their investment portfolios. While everyone's exact tax rate will depend on their state of residence and how they generate income, the overall plan is expected to be a net positive for the mass affluent.

But many of our survey respondents indicated they think people making more than $1 million should pay higher taxes, with wealthier and younger respondents more likely to be in favor of a higher tax bracket. We saw geographic differences too, with GOP strongholds in the Midwest and South more likely to favor lower taxes for wealthy individuals compared to the relatively Democratic-friendly regions in the Northeast and West.

All eyes are on the 2018 midterm elections. However, whether a Democrat or Republican-controlled Congress is best for the finances of the mass affluent is a matter of fierce debate.

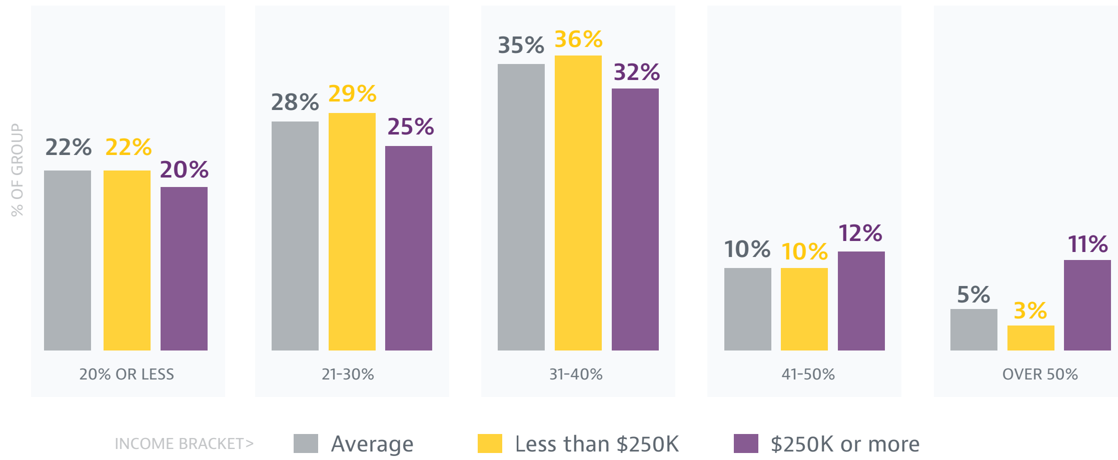
The mass affluent are just as divided as members of Congress when it comes to deciding what's an appropriate tax rate for a wealthy individual or family. While the majority seemed in favor of a tax rate between 21-40%, there were significant differences across income, geographic and generational lines.

When asked, "What's an appropriate federal income tax bracket for someone making more than $1 million per year?" Affluent Americans answer differently by income, region, generation, and gender. (See tables following)

What's an appropiate federal income tax bracket for someone making more than $1 million per year?

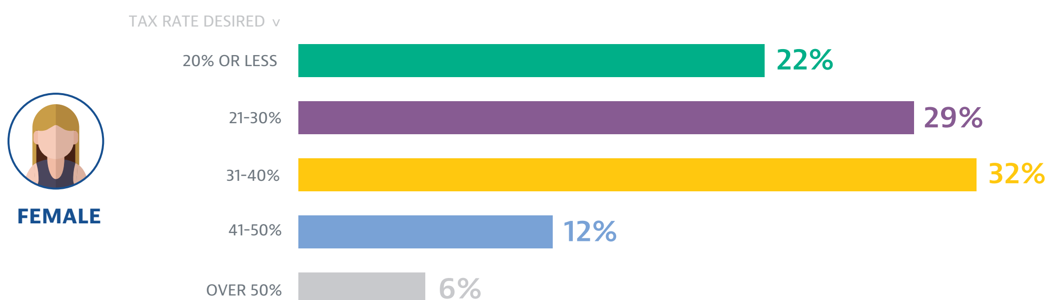
BY INCOME

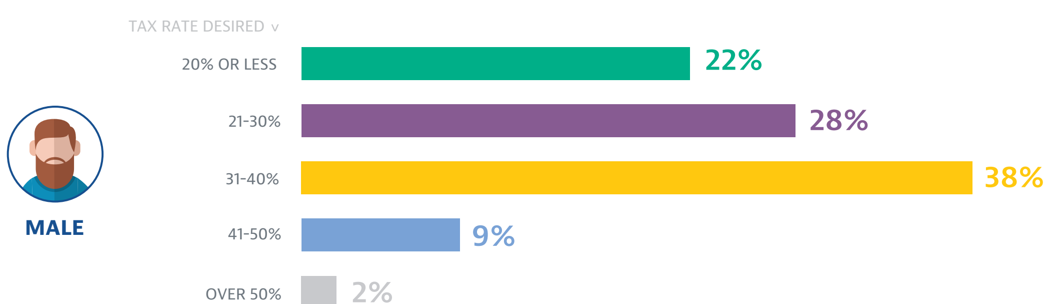
Wealthy individuals making $250,000 or more are more likely to favor higher tax rates, particularly on the higher end of the tax bracket.



BY GENDER

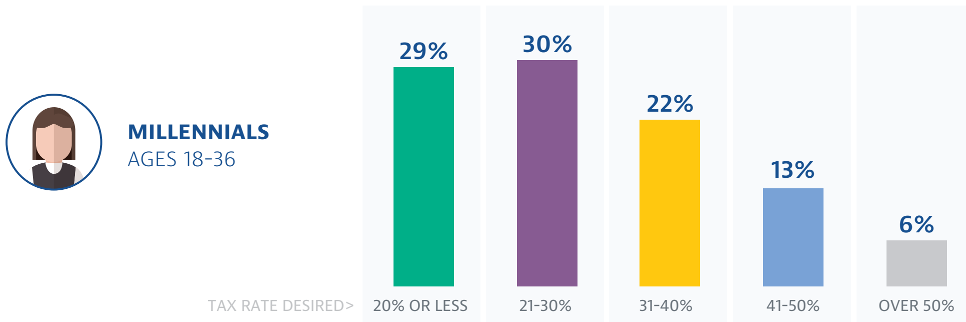
Affluent women tended to favor higher taxes than men, with 18% calling for a tax rate of 40% or higher versus just 12% of men, a 50% difference.

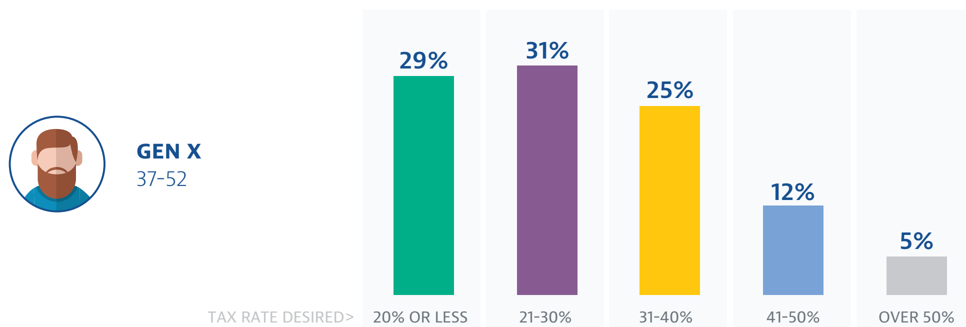


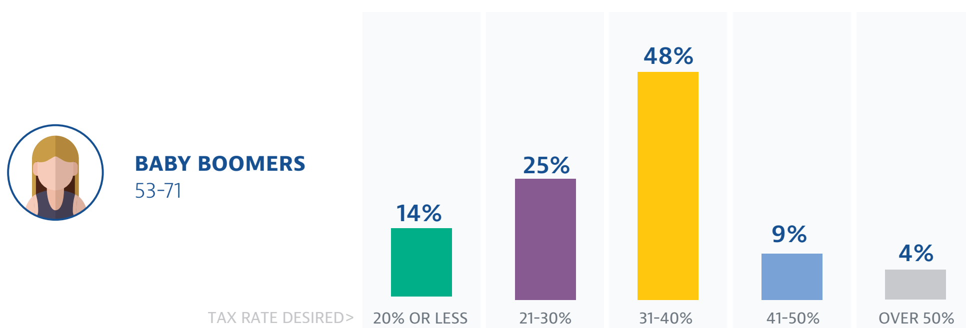


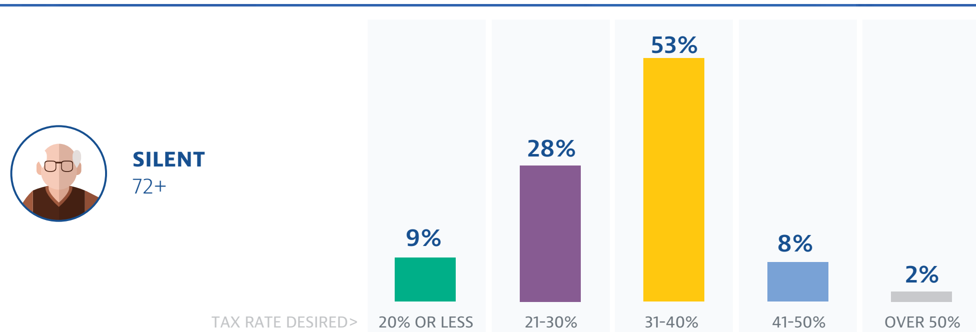
BY GENERATION

Younger generations are more likely to favor higher taxes, while the Silent Generation, many of whom may be used to a lifetime of relatively moderate taxes, would like to see taxes stay in the middle of the spectrum.









Looking Ahead to the Midterm Elections

Affluent Americans are split equally on whether a Democrat- or a Republican-controlled Congress in 2018 would have a more positive impact on their finances. There were, however, some significant differences among specific segments of the survey population, with women (57%) more likely than men (44%) to favor Democrats. Among generations, Millennials (56%) and Gen X'ers (59%), Baby Boomers (43%) and the Silent Generation (38%) say a Democrat-controlled Congress would have a positive impact.

With Trump's approval ratings hovering near an all-time low and several high-profile Republican congressmen expected to retire, the outcome of the midterm elections could have a transformative impact on government policy, and therefore on people's finances.

Would a Democrat- or a Republican-controlled Congress have a more positive impact on your finances?

BY GENERATION		
Millennials	56%	44%
Gen X	59%	41%
Baby Boomers	43%	57%
Silent	38%	62%

of women believe a Democrat-controlled Congress in 2018 would be good for their finances, compared to only 43% of men

CHARITABLE GIVING

'Tis the Season for Generosity, Especially Among Millennials

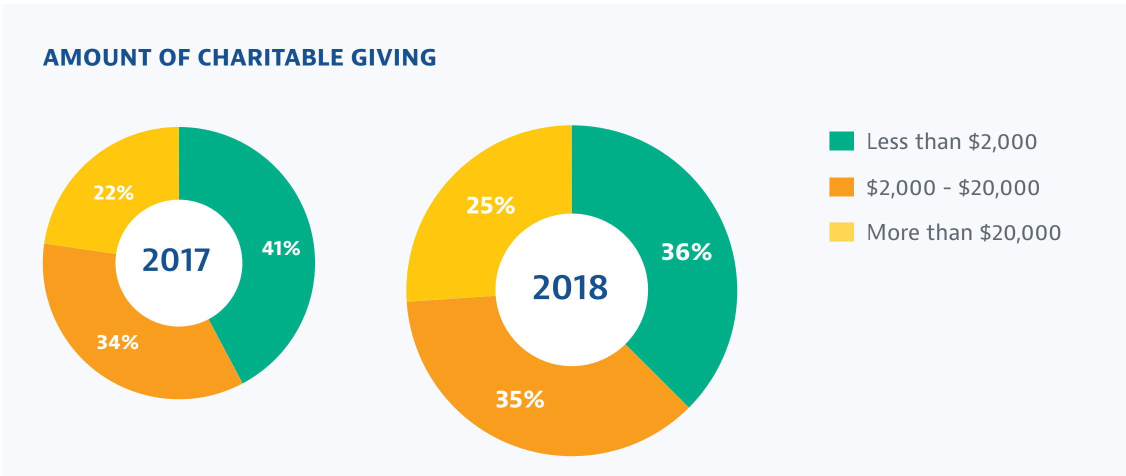
For the mass affluent, financial planning is about more than just protecting and accumulating wealth—it's also about setting aside funds to contribute to charitable causes.

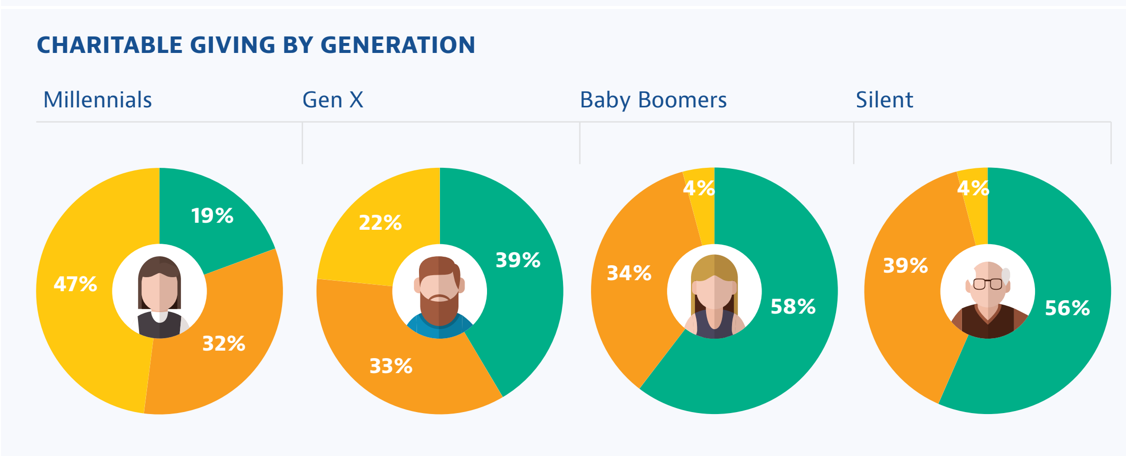
Nearly every affluent American (97%) said they had given something to charity in 2017, with a similar percentage (96%) planning to give in 2018 as well.

And these aren't small donations either. Almost a quarter (22%) of affluent investors will give $20,000 or more, with younger generations (Millennials, 47%) and those with a higher household income ($250,000 or more, 52%) much more likely to write larger checks.

Not to be forgotten, it's also worth noting that charitable donations offer another opportunity for tax optimization, making good deeds even more rewarding.

The mass affluent are not strangers to giving. Nearly everyone we surveyed contributes to a charitable cause. While smaller check sizes of less than $2,000 are more common, many individuals are happy to give $20,000 or more. Millennials are especially generous with 47% saying they've donated more than $20,000 in 2017, despite having less time to accumulate wealth compared to older generations. Check sizes may even increase as we continue towards what will be the greatest wealth transfer in history.



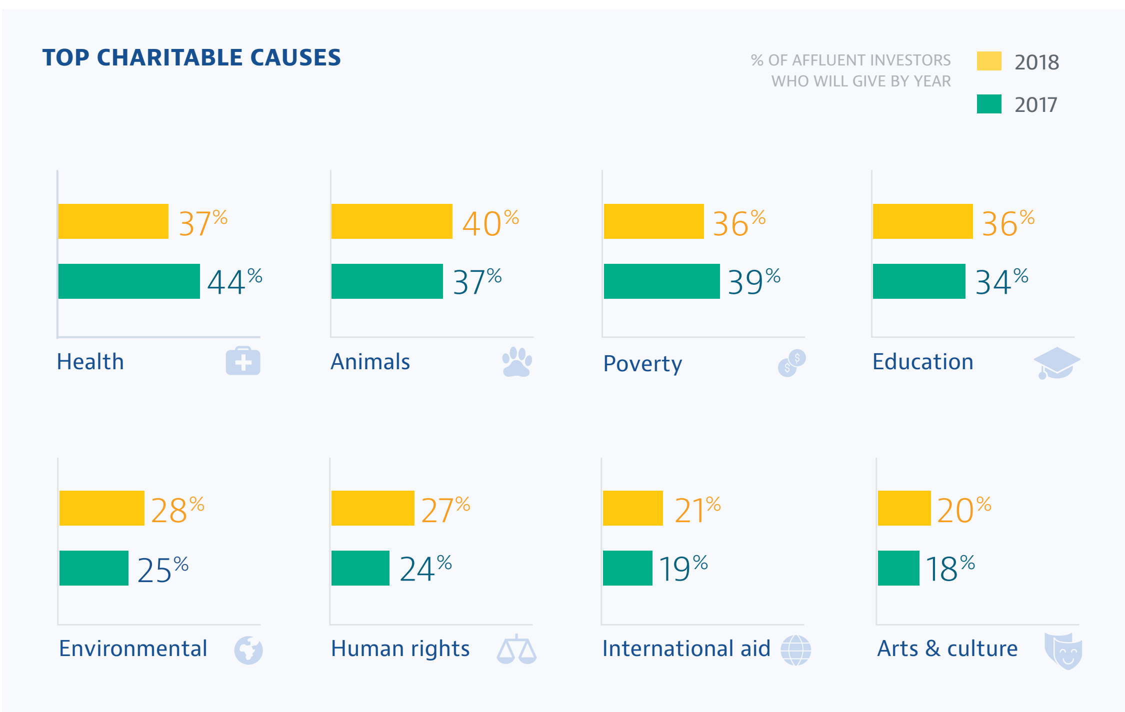


97% affluent americans will have given (or will give) to charity in 2017, with a similar percentage (96%) planning to give in 2018.

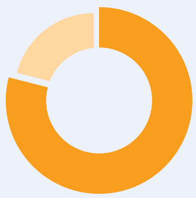
The mass affluent are giving to a wide array of charitable causes, with health, animals, poverty and education related causes attracting the most funding in 2017. However, there are some differences among different segments of the survey population. Women are much more likely than men to give to animal-focused causes (44% vs. 30%), while Millennials are more likely to give to organizations supporting education (48% vs. 33% of Gen X, 23% of Baby Boomers and 27% of Silent) and human rights (37% vs. 28%/11%/19%). Interestingly, respondents based in the Midwest (33%) are less likely to give to health causes than are those living in the West (49%), South (47%) and Northeast (45%).

$30 TRILLION WEALTH TRANSFER

Experts predict that over the next 30-40 years, some $30 trillion in financial and non-financial assets is expected to transfer from Baby Boomers, the wealthiest and one-time largest generation in U.S. history, to their heirs, many of whom are Millennials.

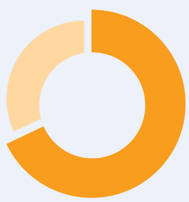


Affluent Americans are optimistic about their financial future, but this optimism comes with a healthy dose of skepticism, doubt and trepidation.



79% expect the market to continue going up

BUT 42% say they are fearful they can't withstand a market downturn and 16% have most of their net worth invested in cash, suggesting a lack of diversification



68% believe Trump's policies will have a positive or no effect on the market in 2018

BUT investors are split 50/50 on whether a Democrat- or a Republican-controlled Congress in 2018 would have a more positive impact on their finances

52% think their overall taxes will go up in 2018,

BUT 46% are concerned that they have not yet properly tax optimized their portfolio

The thrill of the market's recent performance can blunt reality, but what goes up must eventually come down. It's not a question of if, but when, so it's critical for people to be prepared.

By talking to a financial advisor, affluent Americans can navigate an uncertain political and economic environment, plan for the future and still leave room left over for charitable giving.

FINANCIAL PLANNING RESOLUTIONS FOR 2018

1. DON'T BE FOOLED BY FALSE DIVERSIFICATION

> Sit down with your financial advisor and revisit your asset allocation. A diversified portfolio will reduce your risk, steady your returns and help preserve your retirement savings in a downturn.

> Don't rely solely on index funds or mutual funds for portfolio diversification. Broad market indices are typically weighted by individual companies' market capitalizations and therefore provide a false sense of diversification. Most people don't realize that by being top-heavy in the biggest holdings, these ETFs are susceptible to downswings based on the outcome of a few large stocks. Imagine what will happen to your portfolio if one of these stocks turns out to be the next Enron or Lehman Brothers.

> Avoid active mutual funds as much as possible. Mutual funds can cause your portfolio to have too many cooks in the kitchen with overlapping or competing strategies.

> Make sure your holdings are equally distributed across size, sector and style. The alternative is when people get emotionally attached to their winners, especially in such a long-running bull market. Commit to rebalancing your portfolio to avoid these mistakes.

2. LAY OUT A FINANCIAL ROADMAP

> Our survey found that only half of affluent Americans (54%) created a household budget for 2017. Of those who did, more than four in five (84%) will have stuck to it at the end of the year. If you don't have a roadmap, how can you possibly get to your destination?

> There are many free budgeting tools available online that you can use to track your spending, savings and investments, and run what-if scenarios based on decisions like where you send your kids to college or whether to buy a car or a second home.

> While a successful plan begins with a budget, there is much more to it than that. A solid retirement plan should take into account your risk appetite, short- and long-term financial goals, and where you stand on the path to retirement. And the plan should always be accompanied by a diversified portfolio and sound guidance from an advisor that puts your interests first.

> The combination of technology and human insight from an advisor is the best way to meet your retirement goals. Technology can give you a holistic view of your accounts, as well as your spending and saving habits. The advisor can then use this data to work with you to show how you can make smarter financial decisions and stay on track.

3. TAX PLANNING 101

When we talk to clients, we advise them that it's not about the money you make, it's about the money you keep. Investors are thinking about tax cuts, but they often don't think about tax optimization. Things to consider include:

TAX LOCATION

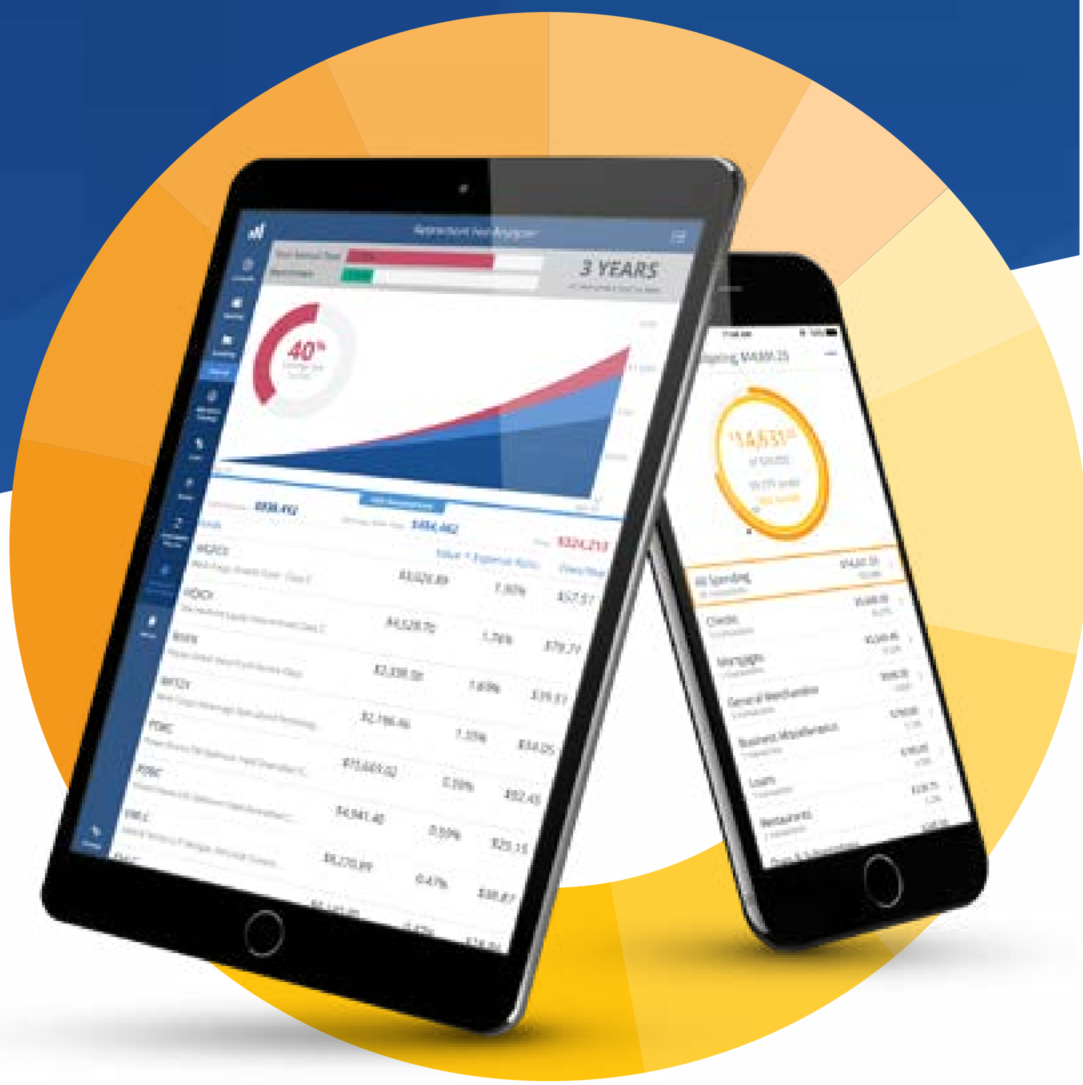
If you have multiple investments, be sure to consider the most appropriate account for each of your assets. Each of your accounts has unique tax characteristics, and if you understand these characteristics, you can place your assets in the most advantageous accounts, thereby minimizing your tax liabilities. *More here

TAX LOSS HARVESTING

This involves selling some of your losses to offset your gains. Typically, tax-loss harvesting works best through portfolios of individual stocks in taxable investment accounts. You sell enough stocks within your portfolio that have lost value to cover the amount of appreciation from the stocks you are selling for a gain. You can offset up to $3,000 in other income if your capital losses exceed your capital gains. Tax loss harvesting can also help you rebalance your stock portfolio and can result in a higher net after-tax return.
*More here

Not all investment vehicles lend themselves to tax loss harvesting, in particular mutual funds and ETFs; ideally you want a portfolio with individual securities to maximize the tax benefits. Similarly, if you use an advisor be sure he/she does this for you or you will need to carefully plan and execute this yourself. This takes a lot of work and we often find our clients did not have time to do this and so they can reap additional savings by having us do this for them on a continual basis employing individual securities.

The smart way to track & manage your financial life.



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PERSONAL CAPITAL

ABOUT THE SURVEY: Respondents for this survey were selected from among those who have volunteered to participate in online surveys and polls. Because the sample is based on those who initially self-selected for participation, no estimates of sampling error can be calculated. All sample surveys and polls may be subject to multiple sources of error, including, but not limited to, sampling error, coverage error, error associated with non-response, error associated with question wording and response options, and post-survey weighting and adjustments.

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