1Q23

The Financial Solutions Advisor

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Economic & Market Perspectives

In 2022, global financial assets experienced near record volatility in a generally hostile environment for investors given that the Fed and other central banks left themselves exposed to a rise in inflation. It was the first year in nearly fifty that stocks and bonds both had negative returns for the first three quarters. Stock market performance was mostly driven by valuation compression as bond yields adjusted sharply higher in response to elevated inflation and monetary policy normalization by the Fed and other central banks.

Sentiment continued to lean risk-off on hawkish takeaways from central bank speeches and increasing growth fears. The path of least resistance was lower for most of 2022 with bounces repeatedly reversed by Fed pushback against occasional easing of financial conditions and expectations (or hopes) of a Fed pivot.

Other observations from 2022 include the outperformance of value over growth and defensive over cyclical stocks. Energy stocks behaved as there was no bear market at all. International stocks eked out outperformance over the U.S., despite China's zero-Covid policy and Russia-Ukraine war. The strong showing of Democrats in the mid-term elections surprised pundits.

The key economic question for 2023 is whether central banks will be able to bring down inflation to acceptable levels without a recession. Beyond the inflation dynamic, we are concerned about potential political and economic shocks that could impact the U.S. and global economy via higher uncertainty and / or tighter financial conditions.

The most significant reason for economic growth to weaken is that the full effects of the substantial monetary tightening over the past ten months have yet to be felt. The main focal points for 2023 will be the Fed (and the recession question) and corporate earnings. We expect the Fed to raise rates to 5% or more and keep the rate at 5% or above for the balance of the year as inflation falls but to still unacceptable levels. The Fed may acquiesce to a 3-4% inflation rate, for the time being, in which a soft landing might be possible. But if the Fed insists on their 2% target, a recession is almost inevitable. In the meantime, what the Fed has already done (raising rates from zero to 4 1/4%) will have a delayed impact on the economy, to be felt in 2023. We expect a mild recession in the U.S. in 2023. Mild due to the cash on corporate balance sheets, a reasonably healthy corporate sector, and a relatively strong banking system.

2022 Returns

S&P 500	*-18.11%*
NASDAQ	*-32.38%*
Russell Small Cap	*-20.44%*
Russell Mid Cap	*-17.32%*
MSCI EAFE	*-14.45%*
MSCI World	*-18.14%*
Barclay US Agg. Bond	*-13.01%*
Barclay Municipal Bond	*-8.53%*

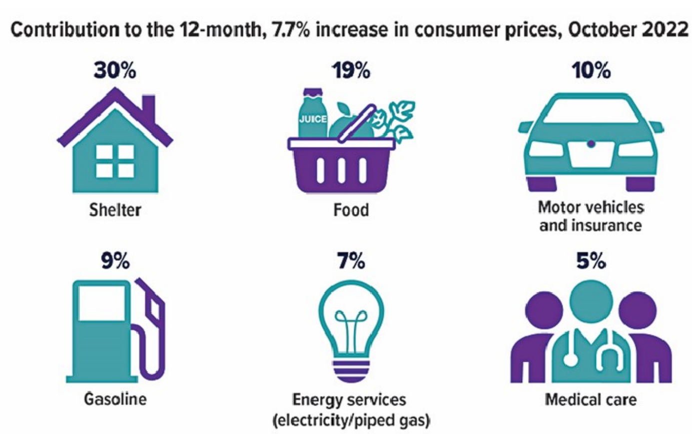
In either scenario, analysts' estimates for earnings are still too high and will need to be reduced. Profit margins are off their peak, but remain elevated by historical standards. As revenue growth slows, negative operating leverage should place further downward pressure on profit margins, creating negative earnings revisions.

For stocks, we expect the lows of last October to be re-tested as growth fears / recession talk increases / earnings estimates are reduced. Bonds should rally during this period. Eventually, the focus will turn towards better economic prospects for 2024. When that occurs, bonds should falter and stocks can rally.

Source: Bob Doll, Crossmark Global Investments

The Top Inflation Drivers of 2022

In June 2022, the 12-month rise in the Consumer Price Index (CPI) peaked at 9.1%, the fastest pace in 40 years, before dropping to 7.7% in October. This bout of inflation has been driven in large part by steep price hikes for essentials, hitting many U.S. households where it hurts the most. In fact, more than three-fourths of the annual increase in the CPI can be attributed to these six categories.



Source: U.S. Bureau of Labor Statistics, 2022

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Busy, cash-strapped parents might welcome all the help they can get when saving for college. Building a college fund, even a small one, can help families feel more in control and less stressed during the college research and admission process. Think of a college fund as a down payment. Then at college time, it can be supplemented by financial aid (grants, scholarships, loans, and work-study), current income, and student funds. A good benchmark is to try and save at least 50% of your child's projected college costs, but any amount is better than nothing.

A 529 savings plan can be instrumental in building a college fund. This individual investment account offers the opportunity for tax-free earnings if the funds are used for college, making every dollar count. (For withdrawals not used for qualified education expenses, earnings may be subject to taxation as ordinary income and a 10% penalty.) You can set up monthly electronic fund transfers from your bank account to put your savings on autopilot. But one-off contributions are allowed, too, and the holidays can be an excellent time for grandparents or other relatives to make a small contribution as a gift. The new year is also a good time to re-double your efforts on building a college fund. Here are some common questions on opening a 529 savings account.

Can I open a 529 savings account in any state's plan?

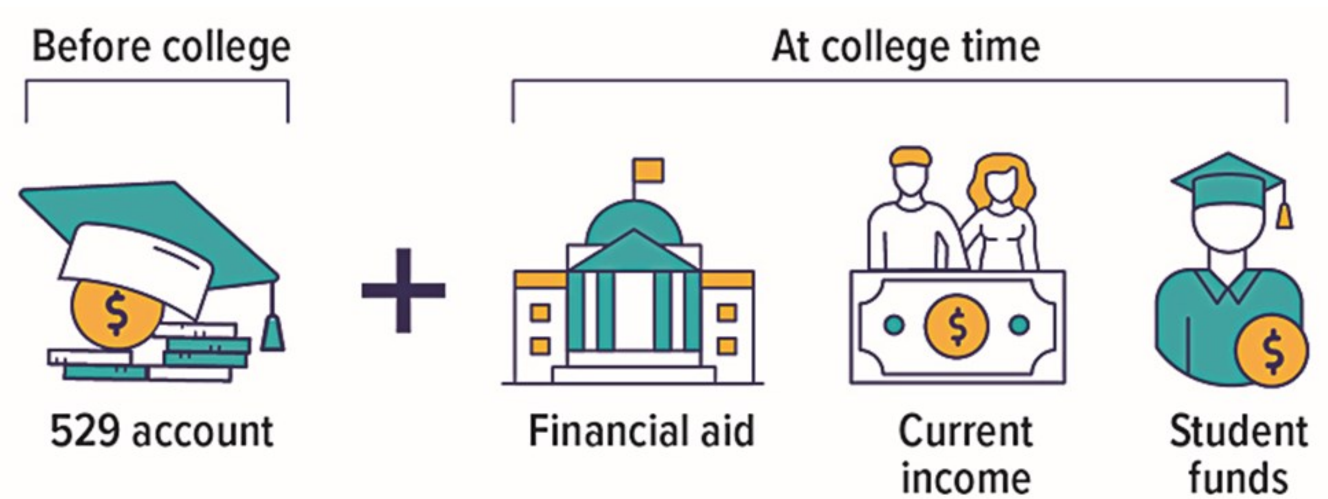
Yes. Currently, all states except Wyoming offer one or more 529 savings plans, and they are generally open to residents of any state. However, it's a good idea to look at your own state's 529 plan first, because some states may restrict any tax benefits (e.g., tax deduction for contributions, tax-free earnings) to residents who participate only in the in-state plan. Why open an account in another state's 529 plan? There could be a number of reasons, including a wider range of investment options, a solid investment track record, an excellent investment manager, or lower management fees. For a list of all 529 plans by state, visit www.savingforcollege.com.

What happens if I open a 529 plan in one state and then move to another state?

Essentially nothing. You can simply leave the account open and keep contributing to it. Alternatively, you can switch to a different 529 plan by rolling over the assets from the original plan to a new 529 plan. You can keep the same beneficiary (under IRS rules, you are allowed one 529 plan same-beneficiary rollover once every 12 months), but check the details of each plan for any potential restrictions. If you decide to stay with your original 529 plan, just remember that your new state might limit any potential 529 plan tax benefits to residents who participate in the in-state plan.

Should I open one 529 account for both of my kids or a separate account for each?

That depends on your personal preferences, but opening separate accounts often makes sense. Two accounts let you contribute different amounts for each child as needed, tailor your investment portfolios to each child's age, and avoid commingling funds. If you choose one account and invest too aggressively, you might incur losses when your older child is close to college. And if you invest too conservatively, your investment returns may not keep pace with college inflation for your younger child. You also run the risk of depleting most or all of the funds for your oldest child.



Does it make sense to open a 529 account if my child is a few years from college?

It might. Even if your child is only a few years from college, you could theoretically save for another four or five years, right up through junior year of college. You could open a 529 account, contribute monthly, and any earnings would be tax-free if the money is used for college. Having a designated college account instead of a general savings account might also lessen the temptation to dip into it for non-college expenses.

As with other investments, there are generally fees and expenses associated with participation in a 529 plan. There is also the risk that the investments may lose money or not perform well enough to cover college costs as anticipated. The tax implications of a 529 plan should be discussed with your legal and/or tax professionals because they can vary significantly from state to state. Most states offering their own 529 plans may provide advantages and benefits exclusively for their residents and taxpayers, which may include financial aid, scholarship funds, and protection from creditors. Before investing in a 529 plan, consider the investment objectives, risks, charges, and expenses, which are available in the issuer's official statement and should be read carefully. The official disclosure statements and applicable prospectuses, which contain this and other information about the investment options, underlying investments, and investment company, can be obtained by contacting your financial professional.

Retirement Investors Get Another Boost from Washington

Amid the 1,650-page, $1.7 trillion omnibus spending legislation passed by Congress last week and expected to be signed by President Biden were several provisions affecting work-sponsored retirement plans and, to a lesser degree, IRAs. Dubbed the SECURE 2.0 Act of 2022 after the similarly sweeping Setting Every Community Up for Retirement Enhancement Act passed in 2019, the legislation is designed to improve the current and future state of retiree income in the United States.

"This important legislation will enhance the retirement security of tens of millions of American workers — and for many of them, give them the opportunity for the first time to begin saving," said Brian Graff CEO of the American Retirement Association.

The following is a brief summary of some of the most notable initiatives. All provisions take effect in 2024 unless otherwise noted.

Later age for required minimum distributions (RMDs).
The 2019 SECURE Act raised the age at which retirement savers must begin taking distributions from their traditional IRAs and most work-based retirement savings plans to 72. SECURE 2.0 raises that age again to 73 beginning in 2023 and 75 in 2033.

Reduction in the RMD excise tax.
Current law requires those who fail to take their full RMD by the deadline to pay a tax of 50% of the balance. The new law reduces that tax amount to 25% in 2023; the tax is further reduced to 10% if account holders take the full required amount and report the tax by the end of the second year after it was due and before the IRS demands payment.

No RMDs from Roth 401(k) accounts. Bringing Roth 401(k)s and similar employer plans in line with Roth IRAs, the legislation eliminates the requirement for savers to take minimum distributions from their work-based plan Roth accounts.

Higher limits and looser restrictions on qualified charitable distributions from IRA accounts.
The amount currently eligible for a qualified charitable distribution from an IRA ($100,000) will be indexed for inflation. In addition, beginning in 2023, investors will be able to make a one-time charitable distribution of up to $50,000 from an IRA to a charitable remainder annuity trust, charitable remainder unitrust, or charitable gift annuity.1

Higher catch-up contributions. The IRA catch-up contribution limit will be indexed annually for inflation, similar to work-sponsored catch-up contributions. Also, starting in 2025, people age 60 to 63 will be able to contribute an additional minimum of $10,000 for 401(k) and similar plans (and at least $5,000 extra for SIMPLE plans) each year to their work-based retirement plans. Moreover, beginning in 2024, all catch-up contributions for those making more than $145,000 will be after-tax (Roth contributions).

Roth matching contributions.
The new law permits employer matches to be made to Roth accounts. Currently, employer matches must go into an employee's pre-tax account. This provision takes effect immediately; however, it may take some time for employers to amend their plans to include this feature.

529 rollovers to Roth IRAs.
People will be able to directly roll over up to a total of $35,000 from 529 plan accounts to Roth IRAs for the same beneficiary, provided the 529 accounts have been held for at least 15 years. Annually, the rollover amounts would be subject to Roth IRA contribution limits.2

New exceptions to the 10% early-withdrawal penalty.
Distributions from retirement savings accounts are generally subject to ordinary income tax. Moreover, distributions prior to age 59½ also may be subject to an early-withdrawal penalty of 10%, unless an exception applies. The law provides for several new exceptions to the early-withdrawal penalty, including an emergency personal expense, terminal illness, domestic abuse, to pay long-term care insurance premiums, and to recover from a federally declared disaster. Amounts, rules, and effective dates differ for each circumstance.

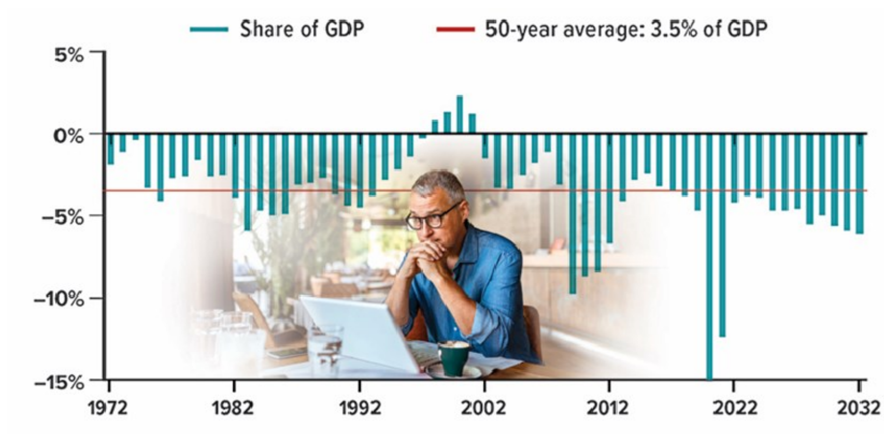
1 Bear in mind that not all charitable organizations are able to use all possible gifts. It is prudent to check first. The type of organization you select can also affect the tax benefits you receive.

2 As with other investments, there are generally fees and expenses associated with participation in a 529 savings plan. There is also the risk that the investments may lose money or not perform well enough to cover college costs as anticipated. Investment earnings accumulate on a tax-deferred basis, and withdrawals are tax-free as long as they are used for qualified education expenses. For withdrawals not used for qualified education expenses, earnings may be subject to taxation as ordinary income and possibly a 10% tax penalty. The tax implications of a 529 savings plan should be discussed with your legal and/or tax professionals because they can vary significantly from state to state. Also be aware that most states offer their own 529 plans, which may provide advantages and benefits exclusively for their residents and taxpayers. These other state benefits may include financial aid, scholarship funds, and protection from creditors. *Before investing in a 529 savings plan, please consider the investment objectives, risks, charges, and expenses carefully.*

U.S. Deficit Lower for Now

After record federal budget deficits of $3.1 trillion in 2020 and $2.8 trillion in 2021, the 2022 deficit is projected to drop to $1.0 trillion, due to increased tax revenue from a stronger economy and the end of government pandemic-relief spending. These deficits are equivalent to 15.0%, 12.4%, and 4.2% of gross domestic product (GDP), respectively. For comparison, the deficit averaged 3.5% of GDP over the last 50 years.

The deficit is expected to drop further in 2023 before rising steadily due to increasing health-care costs for an aging population and higher interest rates on mounting government debt. In 2032, the deficit is projected to be almost $2.3 trillion, equivalent to 6.1% of GDP.



Source: Congressional Budget Office, May 2022. The federal government's fiscal year runs from October 1 to September 30, so FY 2022 began on October 1, 2021, and ended on September 30, 2022. Projections for 2022 and beyond are based on current conditions, are subject to change, and may not come to pass.

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When Should Young Adults Start Investing for Retirement?

As young adults embark on their first real job, get married, or start a family, retirement might be the last thing on their minds. Even so, they might want to make it a financial priority. In preparing for retirement, the best time to start investing is now — for two key reasons: compounding and tax management.

Power of Compound Returns

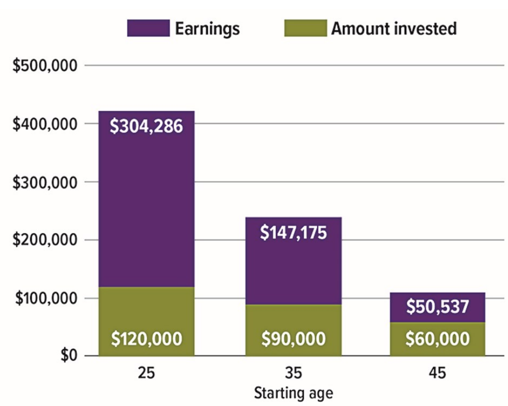
A quick Internet search reveals that Albert Einstein once called compounding "the most powerful force in the universe," "the eighth wonder of the world," or "the greatest invention in human history." Although the validity of these quotes is debatable, Einstein would not have been far off in his assessments.

Compounding happens when returns earned on investments are reinvested in the account and earn returns themselves. Over time, the process can gain significant momentum.

For example, say an investor put $1,000 in an investment that earns 5%, or $50, in year one, which gets reinvested, bringing the total to $1,050. In year two, that money earns another 5%, or $52.50, resulting in a total of $1,102.50. Year three brings another 5%, or $55.13, totaling $1,157.63. Each year, the earnings grow a little bit more. Over the long term, the results can snowball. Consider the examples in the accompanying chart.

A Head Start Can Be a Strong Ally

This chart illustrates how much an investor could accumulate by age 65 by investing $3,000 a year



starting at age 25, 35, and 45 and earning a 6% annual rate of return, compounded annually.

These hypothetical examples of mathematical compounding are used for illustrative purposes only and do not reflect the performance of any specific investments. Fees, expenses, and taxes are not considered and would reduce the performance shown if they were included. Rates of return will vary over time, particularly for long-term investments. Investments offering the potential for higher rates of return also involve a higher degree of investment risk. Actual results will vary.

Tax Management

Another reason to start investing for retirement now is to benefit from tax-advantaged workplace retirement plans and IRAs.

Lower taxes now. Contributions to traditional 401(k)s and similar plans are deducted from a paycheck before taxes, so contributing can result in a lower current tax bill. And depending on a taxpayer's income, filing status, and coverage by a workplace plan, contributions to a traditional IRA may result in an income tax deduction.

Tax-deferred compounding. IRAs and workplace plans like 401(k)s compound on a tax-deferred basis, which means investors don't have to pay taxes on contributions and earnings until they withdraw the money. This helps drive compounding potential through the years.

Future tax-free income. Roth contributions to both workplace accounts and IRAs offer no immediate tax benefit, but earnings grow on a tax-deferred basis, and qualified distributions are tax-free. A qualified distribution is one made after the Roth account has been held for five years and the account holder reaches age 59½, dies, or becomes disabled.

Saver's Credit. In 2022, single taxpayers with adjusted gross incomes of up to $34,000 ($66,000 if married filing jointly) may qualify for an income tax credit of up to $1,000 ($2,000 for married couples) for eligible retirement account contributions. Unlike a deduction — which helps reduce the amount of income subject to taxes — a credit is applied directly to the amount of taxes owed.

Avoiding penalties. Keep in mind that withdrawals from pre-tax retirement accounts prior to age 59½ and nonqualified withdrawals from Roth accounts are subject to a 10% penalty on top of regular income tax.

Additional Fuel for the Fire

Workplace plans that offer employer matching or profit-sharing contributions can further fuel the tax-advantaged compounding potential. Investors would be wise to consider taking full advantage of employer matching contributions, if offered.

Don't Delay

With the power of compounding and the many tax advantages, it may make sense to make retirement investing a high priority at any age.