Wealth Builder

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Advice to Millenials By Mike Berry, CFP®

I was recently asked how I would advise young people just getting started on their financial journey. I really had to think about that one. Would it be any different than how I advised young people 30 years ago?

People in their 20's and 30's today have had a lot thrown at them in their brief time here on earth. Some of which happened in their childhood, but I'm sure they still remember the effect these events had on their parents and family. The terrorist attack on 9/11/2001 and the economic recession that followed; the financial crisis and housing meltdown in 2008 and 2009; the pandemic and now the highest rate of inflation in 40 years. These people were told the only way to get ahead was by getting a college education and to do so many came away with piles of debt and a crowded job market because people were working longer in their lives and that left fewer openings for the millennials to fill. The cost of

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Oh, Inflation By Dan Funderburk, CFP®, CKA®

You can essentially pin the performance of the financial markets in 2022 on one thing: inflation. Sure, things are nuanced, and the various pieces of the markets moved differently for more specific reasons, but eventually inflation was the driving force behind almost all of it.

Let's rewind to the summer of 2021. Inflation was beginning to creep up. This was possibly because of the $5 trillion that the US government printed in 2020 coupled with global supply chain issues. More money in people's pockets + fewer available goods = people being willing to spend more on goods, AKA inflation. **I hope you picked up on my sarcasm – inflation is definitely the result of a crazy amount of money being printed.*

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housing has skyrocketed for these potential first time homebuyers. The disconnect between income and house prices has never been greater. The dream of home ownership is further away for this group than any other in my lifetime. We seem to be entering a second Cold War this time with both Russia and China, which casts some dark clouds over the US economy as our biggest trading partner is China. The federal debt is at $31 trillion and growing. That is pushing close to $100,000 per person. How do I advise someone who is just coming into the beginning of their financial life? Some things hold true regardless of time and circumstance:

Spend less than what you make. Financial success is not rocket science. If you spend less than what you earn especially over a long period of time, you will be financially successful. Live within your means.

Practice "delayed gratification". The generation that grew up during the Great Depression were the best at the discipline of delayed gratification. They never bought anything they didn't have the money to pay for right then. We have become an instant gratification society. Fast food, instant credit instant answers on the internet. Get rid of the "I want it all now" attitude.

"The key is to set goals, keep them in your focus, maintain your patience, and enjoy the ride."

Use credit wisely. Borrowed money commits future earnings to current obligations. Debt is a financial tool, and like any tool, you must know how to use it and use it wisely or it can harm you. Pay off your revolving credit each month.

Pay yourself first. Set aside an amount of money from each paycheck (small as it may be) that is "your pay". It's your money for some future need.

Invest when you have the money. I can't tell you how many times I've been asked over the years if now is a good time to invest. The best time to invest is when you have the money because if you just let it sit around, it will likely get frittered away. Consistently investing money when you have it over a long period of time will produce successful results.

Understand what you are investing in. If you can't explain an investment to someone else so that they understand it, then you shouldn't invest in it. That is my case with crypto. I don't understand it well enough to explain it to someone else, so I don't invest in it.

I guess I would close my millennial advice column by letting them know that these times are not necessarily unique. Each generation has had to work through their own trials and tribulations. The key is to set goals; keep them in your focus; maintain your patience and enjoy the ride.♦

Raise the Roof and Buckle Up By Jeff Funderburk, CFP®

We're again bumping our heads against the debt-ceiling. We hit our heads on this same self-imposed spending limit in 2011 and again in 2013. Those that don't learn from history are doomed to repeat it. Boy, I wish we would learn because *here we go again*.

The debt limit is the total amount of money that the United States government is authorized to borrow to meet its existing legal obligations, including Social Security and Medicare benefits, military salaries, interest on the national debt, tax refunds, and other payments. The debt limit does not authorize new spending. It allows the government to finance existing obligations that the federal government has made in the past.

Back in 2011 and 2013, the Democratic party held the Senate majority, and the White House. The Republican party held the majority in the House. Politics were extremely partisan. Sound familiar? The debt-ceiling again is essentially being used as a bargaining chip by one party to get concessions out of the other when it comes to government spending. Politics aside and ignoring all the debate that could be had over the structure, mechanics, and even the very existence of the debt-ceiling, history has shown that there are very real and tangible risks to not getting it raised.

In 2011 the limit was raised just two days prior to the federal government exceeding it's borrowing authority, but the damage was done. The crisis sparked the most volatile week for financial markets since the 2008 crisis, with the stock market trending significantly downward. Ironically, prices of government bonds rose as investors fled the relative safety of US government bonds (known as a "flight to safety"). The government accountability office (GAO) "estimated that delays in raising the debt limit in 2011 led to an increase in Treasury's borrowing costs of about $1.3 billion in fiscal year 2011." Additionally, the United States government's AAA credit rating was downgraded for the first time in the country's history (although by only 1 out of 3 major credit rating agencies). You can imagine how markets reacted to that news.

Those were the results when the debt-limit wasn't exceeded. But the problem is that the manner in which the ceiling was raised in 2011 was not a permanent fix. We had another crisis with the limit two short years later in 2013. Here we go again 2023.

The treasury department has said that the "extraordinary measures" currently being employed to avert exceeding the limit will be exhausted by June. I expect market volatility to increase more and more as we get close to that deadline. And given the extreme divisiveness in Congress, I would bet that the limit will eventually get raise, but only at the last minute. We've seen that movie before.

Buckle up.♦

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http://www.gao.gov/assets/600/592832.pdf

OH, INFLATION *Continued from p. 1*

The Federal Reserve Board's response to inflation in summer 2021? "It's transitory and will decline once supply chain issues get resolved." This sounds ok on the surface, but it only addressed the shortage of goods. It didn't address the massive influx of free money given to everyone with a pulse in 2020. Because of this, they missed the boat and let inflation continue to jump throughout 2021. It continued its ascent until it hit 9.1% in June of 2022[1]. By then, the Fed had changed it's tune and no longer thought it was "transitory". They pulled a 180° in their policy and began doing everything they could to bring it back down to their target of 2%.

The main inflation-fighting tool the Fed has in its toolbox is manipulating interest rates. The Fed sets the "Fed Funds Rate," which is the short-term rate it charges big banks to borrow money. The banks then in-turn lend to other banks, businesses, and consumers, albeit at a higher rate than what they paid the Fed (this is one of the primary ways banks make money – lend money out at a higher rate than they borrow it). Everything spins off the Fed Funds rate; mortgage rates, small-business loan rates, student loan rates, credit card rates, you name it. As the Fed raises its rate, it makes borrowing more expensive across the board. This slows down economic activity, which is exactly what the Fed was trying to do in 2022.

Now let's distill all of this back to the market performance last year. When I mention the financial markets, I'm specifically referring to the stock and bond markets.

Let's focus on stocks first.

The primary way you make money in stocks is by the company earning higher profits over time. These higher profits will make the company more attractive to investors, which will cause them to buy the stock, which increases it's price on the exchange. If the Fed is doing everything it can to slow down the economy, odds are corporate profits will suffer (i.e., if it costs more to borrow because of higher rates, companies will either absorb the higher expense, therefore lowering profits, or hunker down and not expand, therefore lowering profits). Then you throw the nasty R word out there: Recession. The Fed increasing rates increases the likelihood of a recession, which is bad for stocks. Investors know this, so they were selling stocks in droves last year to get out before a recession happened. The result? The S&P 500 was off 19.44% last year[2].

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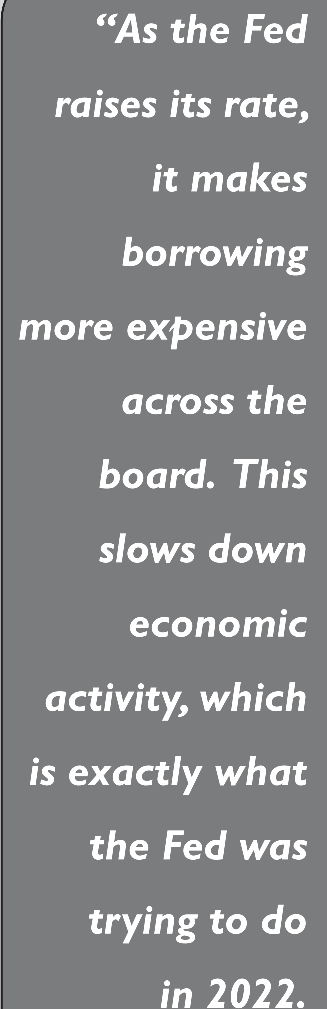
Now let's look at bonds.

During the Certified Financial Planner (CFP®) classes, they drill this financial reality into you: As interest rates rise, bond prices go down. The reason for this is beyond the scope of this article, but if you'd like to know why this is true please ask me next time we speak. I'll be happy to explain in a manner that only slightly glazes your eyes over.

That being said, the above statement actually is true. Look no further than the 10-year treasury in 2022. In a year where the Fed Funds Rate went from 0.08% to 4.33%[3], the 10-year treasury lost 15%[4]. Ouch.



In Summary:

- Stocks fell in 2022 because of higher borrowing costs and recession fears. Why are borrowing costs higher and recession risks elevated? Inflation.
- Bonds fell in 2022 because the Fed raised interest rates at an unprecedented pace. The reason for the increasing rates? Inflation.

We'll continue battling these themes in 2023. Inflation has been declining, but still has a way to go. Until it gets closer to the Fed's 2% target, we'll continue to have higher borrowing costs and a slowing economy. We may or may not experience a recession between here and 2%, but I would argue that a recession has already been priced into the market.

Thankfully, these choppy markets come with some good news as well. Cash is paying about 4% currently, which hasn't been the case since I've been in the industry. Investors who aren't comfortable with risk can now get a decent return in very secure vehicles. New bonds are being issued with higher yields, and existing bonds are much more affordable now given their price drops last year.

If you've read this far, I commend you. Maybe you and I should have that discussion about why movements in interest rates affect bond prices.

Until next time…♦

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[1]https://www.wsj.com/articles/inflation-tracker-cpi-data-prices-11657717467?mod=series_inflation
[2]https://www.morningstar.com/indexes/spi/spx/performance
[3]https://www.macrotrends.net/2015/fed-funds-rate-historical-chart
[4]https://www.barrons.com/articles/bond-prices-2023-outlook-51672939907

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