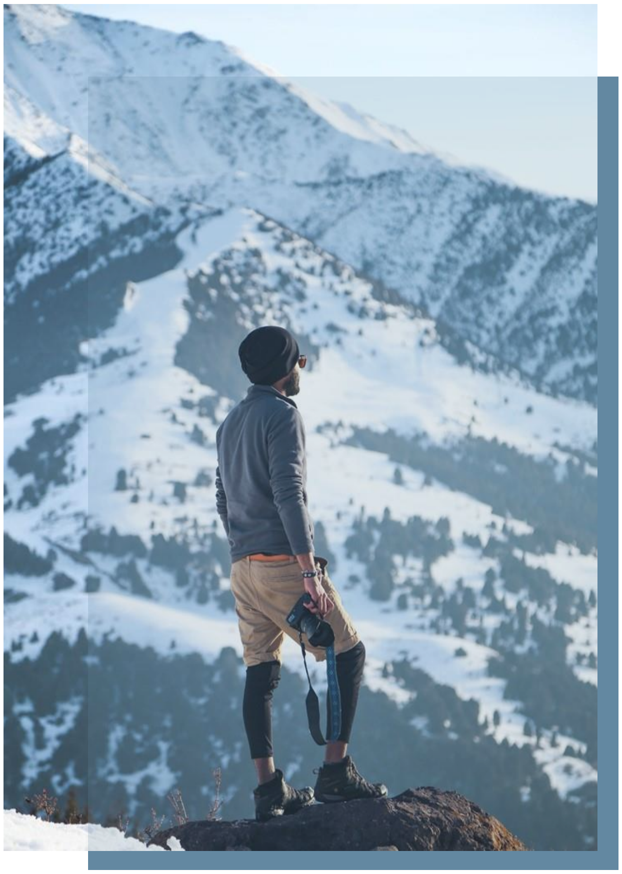
BFS PERSPECTIVES

Benefit Financial Services Group's Newsletter

Quarter Ending June 30, 2022



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Market Recap

Patrick Powers, CFA, CPA/PFP, CFP® (Managing Principal)

The first half of the year was difficult for investors as the Federal Reserve (the "Fed") began raising interest rates to fight inflation, which jumped to 40-year highs. As interest rates rise, the multiple of forward corporate earnings that investors are willing to pay for stocks declines. At the end of last year, before inflation and interest rates shot up, and before the war in Ukraine, investors were willing to pay about 21x the projected next 12 months' earnings[1] of the S&P 500 Index.[2] By the end of the 2nd quarter, that multiple had fallen to just under 16x earnings, resulting in a 20.6% drop in the S&P 500 Index and marking its worst first half of a year since 1970. The growth-oriented Nasdaq Composite[3] fell 29.5%, marking its worst first half on record.

International markets[4] faired just as poorly – down nearly 21%. And not to pour it on – Bitcoin fell 58%! Commodities, as an asset class, generated positive returns as the price of crude oil rose 40.6%. However, that did not make us feel any better at the gas pump!

Unfortunately, bonds values also fall as interest rates increase. If a bond is yiedling 2% and interest rates rise to 3%, you need to discount the price of a bond you want to sell until it yields the 3% the current market is demanding. As a result, the U.S. Aggregate Bond Index[5], had its worst first half on record, falling 10.4%.

This correction in asset prices was expected and it was necessary. Unfortunaltey, it was exacerbated by unforseen circumstances like the war in Ukraine and continued disruptions in supply chains and labor markets. The good news is that the correction has been orderly and reasonable under the circumstances and, as a result of it, the future return outlook for a balanced portfolio has improved, not declined. This setback will be temporary; it always is!

Forecast

Steven Yamshon, Ph.D. (Managing Principal)

I realize that it has been a tough year fo all investors in both the stock and bond markets. I also know it is hard for clients to stay on course in this type of environment. Market psychology turns long-term investors into short-term investors when there is market turmoil such as the one we are having now.

Consider an analogy that I learned from one of my former colleagues at Security Pacific Bank: “You want to go to Chicago and the only means of transportation is a train so you get on board. As the train goes across a hundred year old trestle bridge - the train shakes and shakes. Do you get off? What was your goal in the first place? To get to Chicago! So you say a few prayers and you ride it out and 99.9% of the time the train makes it to Chicago in fine shape.” Every time the market declines, like the decline we are experiencing now, I think of this simple analogy.

What makes me confident and able to sleep at night is that there appears to be no systemic risk to the financial system, unlike the Great Financial Crisis in 2008. So it all boils down to your time horizon. Is your time horizon 1 week or 3-5 years? I think ahead in years and that has been a good path to follow as it has built wealth for the many clients we serve. In the long-term, the bond and stock markets have been a good place to be, in spite of the short-term volatility. We believe that at least this part of history will repeat itself.

Portfolio Management

Michael Allbee, CFP® (Partner/Senior Portfolio Manager)

It could be a while before investors can better assess how the economy and corporate profits will ultimately fare against fast-rising inflation and higher borrowing costs — and the stock market is no fan of uncertainty. This uncertainty along with current geopolitical events was a perfect storm for a balanced portfolio (60% stocks / 40% bonds), impairing the normal diversification of risks in a balanced portfolio. The result was the worst year-to-date performance for a balanced portfolio since the 1960’s.[6]

With the increasing probability of a recession over the next 12 months, the logical tactic is to exercise caution until some of the uncertainty is resolved. While we are exercising caution, we believe the only good reason to sell out of a stock portfolio now is because you learned something about your risk tolerance or your investment goals have changed.

As the late financial historian Peter Bernstein said, “In investing, tortoises tend to win far more often than hares over the turns of the market cycle.” While in the near term, it may not be easy to take troubling headlines in stride, we believe that if you have a sufficiently low-cost, diversified investment strategy, staying invested for the long term puts you in the best position to capture the eventual recovery. In fact, a year after the S&P 500 crossed into bear market territory (a 20% fall from the market’s previous peak), it rebounded by about 20% on average. And after five years, the S&P 500 averaged returns over 70%.[7] And if you continue investing regularly for a long-term goal such as retirement, a down market may be an opportunity to buy more shares at lower prices and lower valuations. And, broadly speaking, lower valuations historically have lead to higher returns going forward. There is some upside to bear markets for long term investors.

Talk With Us!

Paul Horn, CFP®, CPWA® (Senior Financial Planner/Wealth Manager)

Michael Allbee, CFP® (Partner/Senior Portfolio Manager)

Volatility or down markets only become a problem if you’re forced to liquidate at the wrong time. If you have enough cash to get you through, you’re going to come out fine on the other side most of the time. We generally recommend setting aside funds to cover 3-6 months’ (6-12 months’ if retired) worth of non-discretionary living expenses (i.e., housing, taxes, debt service, groceries referred to as needs) as an emergency reserve. This recommendation helps our clients handle short-term problems that are beyond their control (i.e., unemployment, car problems, medical bills, etc.). Without an emergency fund, most people resort to using high-interest rate credit cards to pay their expenses. This conflicts with your long-term goal of saving for retirement and/or necesitates portfolio withdrawals at an inopportune time.

We also recommend matching the time horizon for when you may need the money with the chosen savings product. For example, we recommend keeping some of your emergency reserve in a FDIC-insured savings account at your bank, an online bank, or credit union that offer daily liquidity. What you earn on your emergency reserve is irrelevant and the main goal of this investment is liquidity.One positive of the current increase in yields, is that many of these FDIC-insured savings accounts now offer yields up to 1.20% today. Recently, we have been working with clients to purchase 3-month to 2-year Treasury bills yielding between 2.04% - 3.11% for a portion of their emergency reserves or for other short- and medium-term savings goals, such as a down payment for a house or car purchase. These yields are higher than current Certificate of Deposit (CD) rates and are principal protected if held to maturity.

If you have excess reserves that you won't need for at least 12 months (and preferably 5 years), we have been recommending Series I savings bonds (I Bonds). I Bonds are currently yielding 9.62% and can be bought directly from the Treasury Direct website. Unfortunately, each person is limited to purchasing $10,000 worth of I Bonds a year, and the yields will fluctuate based on inflation. Furthermore, if you cash in your I Bonds within five years of purchasing them, you lose the previous 3 months of interest.

Another consideration is a Roth IRA. The Roth is unique, in that any contributions you make to a Roth can be withdrawn without penalty or taxes. The caveat is that any earnings in the account need to remain for five years, and you must be 59.5 years old or older (unless an exception applies) for it to be considered a qualified distribution to avoid taxes and a 10% penalty. In turn, you are technically saving for retirement and building a nest egg for any short-term unexpected expenses. This option should be looked at as an additional cushion to your emergency reserve and not as a replacement, since the funds in your Roth account should be invested in the markets which will fluctuate in value.

We highly encourage you to Talk With Us if you want to strategize about your emergency reserves or need help building your emergency fund.

Welcome to the Team

Please join us in welcoming Henry VanBuskirk, CFP® to Benefit Financial Services Group. Henry joins BFSG as a Wealth Manager. He will be working with you to help you realize your short and long-term goals by delivering personalized financial plans and retirement analysis. Previously, he worked as an Investment Analyst for an advisor in Woodland Hills, CA. Henry graduated from the University of California, Santa Cruz with a Bachelor's degree in Mathematics and from California Lutheran University with a Master's degree in Business Administration. He is a CERTIFIED FINANCIAL PLANNER™ professional. We are looking forward to the positive impact he is going to make at BFSG and for our clients. Welcome Henry!

In the News

April 16, 2022 – BFSG Named one of Barron's "Top 100 Institutional Consulting Teams" for 2022

The Score Board

	06/30/2022	YTD Change
Dow Jones Industrial Average	31,091.83	-14.44%
S&P 500*	3,785.38	-20.58%
NASDAQ Composite*	11,028.74	-29.50%
MSCI EAFE (USD)*	1,846.28	-20.97%
Bloomberg Commodity Index	117.05	18.03%
U.S. Aggregate Bond Index	2,111.40	-10.35%
10 Yr U.S. Treasury Bond Yield	3.01%	150 bps
30 Yr Fixed Mortgage Rate	5.83%	256 bps
Prime Rate	4.75%	150 bps
Crude Oil ($ / Barrel)	$106.01	40.56%
Gold ($ / Oz.)	$1,807.27	-1.20%
U.S. $ / Euro €	$0.95	8.48%
Core Inflation (excluding food / energy)		6.00%**
Inflation (including food / energy)		8.60%**

**Without Dividends; **Unadjusted 12-Months ended May 2022; bps (1 Basis Point = 1/100%); UNCH (Unchanged)*
Sources for Score Board and quoted statistics: WSJ, US Dept. of Labor, Federal Reserve

Sources:

1. Source: FactSet, as of 6/30/2022. The price-to-earnings ratio is the ratio for valuing a company that measures its current share price relative to its earnings per share (EPS).
2. The S&P 500 Index is designed to be a leading indicator of U.S. equities and is commonly used as a proxy for the U.S. stock market. Price return quoted.
3. The Nasdaq Composite is a stock market index that includes almost all stocks listed on the Nasdaq stock market and is heavily weighted towards companies in the information technology sector. Price return quoted.
4. The MSCI EAFE Index captures large and mid-cap segments in 21 developed markets around the world, excluding the US and Canada. Price return quoted (USD).
5. The U.S. Aggregate Bond Index is a broad-based index used as a proxy for the U.S. bond market.
6. Source: Deutsche Bank, as of 7/4/2022.
7. Source: Ken French website. Returns are calculated for the 1- and 5-year look-ahead periods beginning the day after the respective downturn thresholds of -20% are exceeded. For the 20% threshold, there are 15 observations for 1-year look-ahead and 13 observations for 5-year look-ahead. Peak is a new all-time high prior to a downturn. Fama/French Total US Market Research Index: 1926–present: Fama/French Total US Market Research Factor and One-Month US Treasury Bills. Past performance is no guarantee of future returns. The performance of an index is not an exact representation of any particular investment, as you cannot invest directly in an index.

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