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November 12, 2021

Year-end RMD and Gifting Deadlines – Jeannine Shaffer

As the end of the year approaches, there are several deadlines to be mindful of for tax planning. For those clients 72 and over, who have Traditional IRAs, the Required Minimum Distribution (RMD) must be completed by December 31. Your RMD distribution can be transferred to a taxable account such as a trust or brokerage account to be reinvested or sent to your bank account by ACH if it is linked to your IRA, or a check can be mailed to your address of record for the IRA. Please contact us no later than December 22nd if you have not yet taken your 2021 RMD.

For those clients wanting to make a charitable gift to an organization, you may give securities from a taxable account or make a Qualified Charitable Distribution (QCD) from your IRA, which applies toward your RMD, but is not taxed as income to you or the charity you donate to. There is paperwork required for security transfers and QCDs so please contact us no later than December 10th.

Keeping an Eye on Potential Tax Increases – Bryson Slater, CFP®

There have been many rumblings in Washington about proposed changes to tax laws coming down the pipeline via the Build Back Better (BBB) plan. BBB does not currently have bipartisan support. This is still a very fluid situation that we are keeping a close eye on. One of the main potentially impactful items is Congress implementing new restrictions on IRA contributions and Roth conversions for high earners. They had also initially proposed increases to income and capital gain tax rates for high earners. The tax increase changes have been eliminated from the current version of the bill. However, it is possible for some of these provisions to be reintroduced in future versions.

The bottom line is at this time no one knows what parts of the tax code will be changed. We will keep our finger on the pulse of these issues and will let you know as soon as something definitive is announced. Feel free to contact us with any questions you have.

Capital Gains' Distributions – Jim Stoutenborough, CFP®

It's already that time of year when start to think about year-end mutual fund distributions and the capital gains they might bring. The shift to having a part of the stock portfolio in index funds has helped to reduce some of the year-end tax implications but we do still have some actively managed mutual funds that can throw off gains at the end of the year. This only affects your non-retirement brokerage accounts - Trusts and TOD accounts – not your tax-deferred - IRA's, Roths, Simples, SEP's and 401k's.

We have a couple of funds that distribute twice a year - mid-year and year-end – distribute heavy gains mid-year which concerned us that the year-end distributions may be higher after a couple of years of muted distributions. Alex and Bryson start to review the estimates from the fund companies in early to mid-November to see if doing a step-aside would be beneficial.

In a step-aside, if the capital gain from selling the fund is smaller than taking the distribution – then we sell the fund just before the distribution, take the gain, then buy it back after the price drops after the distribution. Some good news and bad news – good news - since March of last year the gains in the funds have been sizable due to the stock market run-up – the bad news is that there probably won't be a chance to side-step even a sizable year-end distribution, but we will still check to see if there is chance to reduce your taxes.

Is Inflation Here to Stay? – Alex Petrovic, CFP®

First off, what a phenomenal run for stocks so far this year! Corporations continue to report sizable earnings growth for the third quarter. S&P Capital IQ consensus estimates point to earnings growth for the S&P 500 Index companies of about 44% for 2021. That is incredible. However, the massive rebound in earnings is expected to end. The 2022 earnings growth for the S&P 500 Index companies is projected to be around 7%.

Since corporate earnings are the lifeblood of stocks, the massive rebound in earnings has translated into substantial stock appreciation this year. The projected earnings growth for next year is far below this year's growth, but it's still a respectable number. Plus, the U.S. economy is currently forecast to grow about 4 – 5% next year, a very healthy level.

With this said, what is one of the main concerns on investors' and advisors' minds over the past 6 months? **Inflation**. And, yet again we got another report of rising inflation. On November 10, the U.S. Labor Department reported that the consumer-price index (CPI) for October rose to an annual rate of 6.2%, the fastest annual pace since 1990. Inflation also topped 5% for the fifth straight month.

What is Going On?!!?

This recent Wall Street Journal article sums it up well. Below are my curated snippets from the article.

[U.S. Inflation Hit 30-Year High in October as Consumer Prices Jump 6.2%]

> Laura Rosner-Warburton, senior economist at MacroPolicy Perspectives, thinks the U.S. is entering a six-month period of unusually high inflation. "I do think we're moving into a new phase where inflation is broader and where things are going to get a little more intense," she said. "Part of that reflects that [supply-chain] bottlenecks are not resolved going into the holiday season, when a lot of purchases get made, and that the economy is doing really well, so you have strong demand."
>
> Ms. Rosner-Warburton sees a shift under way in which a wider range of factors will push up inflation, as opposed to the previous months' increases, which were driven disproportionately by skyrocketing vehicle prices and the reopening of services after Covid-19 vaccines became available. "Part of [this] still seems likely to be transitory, but maybe not all of it," she said.
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> Companies are struggling to get materials and are delaying orders as elevated demand for goods due to pandemic spending habits has collided with transportation bottlenecks, production disruptions from Covid-19 and labor shortages. The most prominent example is a shortage of semiconductors that has hamstrung auto production. The limited supply of new autos has driven up prices for both new and used vehicles. The chip shortage, which has also affected other industries, has worsened because of shutdowns of factories and ports in Asia in response to Covid-19 outbreaks.

<u>So… should we be worried?</u>

Here's Janet Yellen's current opinion. From: [Yellen Says Fed Wouldn't Allow Repeat of 1970s-Level Inflation]

> Treasury Secretary Janet Yellen, who was chair of the U.S. Federal Reserve from 2014 to 2018, repeated her view that elevated U.S. inflation won't persist beyond next year and said the Federal Reserve will act if needed to prevent a rerun of 1970s-style price rises. "I'd expect price increases to level off, and we'll go back to inflation that's closer to the 2% that we consider normal" as the pandemic fades, Yellen said in an interview that aired Tuesday on National Public Radio's "Marketplace" show. The Treasury chief said that an end to the pandemic would allow more people to return to work, and with consumer demand returning to normal patterns, that will relieve pressure from wages and goods prices.

Here's is what Jerome Powell, current Chairman of the U.S. Federal Reserve, said last week. "We see higher inflation persisting, and we have to be in a position to address that risk should it create a threat of more persistent, longer-term inflation."

<u>Do the financial markets believe them?</u>

Yes… maybe. Historically, there are aspects of inflation that can change quickly, up, or down. And then there are more "sticky" parts of inflation that have more staying power. Economists typically worry about the sticky parts of inflation since they can persist for years.

Gene Podkaminer, Head of Research at Franklin Templeton Investments summed it up… "As an investor and market observer, I need to ask myself what inflation is telling us. Like the difference between good and bad cholesterol—there's also good inflation, led by unexpected demand, and bad inflation, caused by supply constraints."

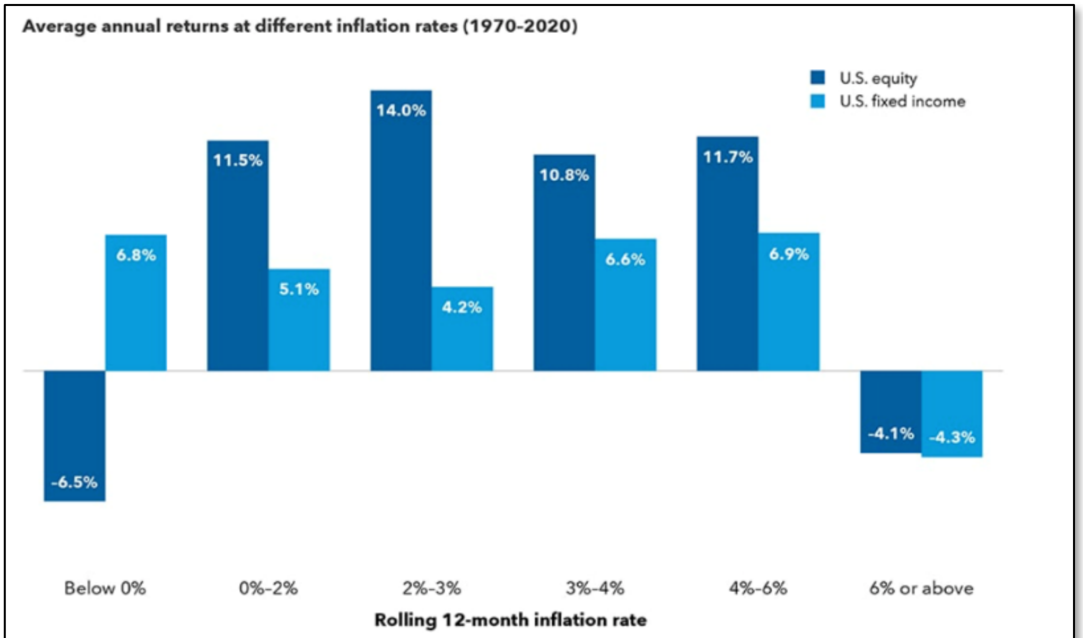
So, Gene is saying that right now the U.S. economy is having a wonder spell of growth due to several factors, but mainly because the U.S. consumer is broadly in very good shape, and people are spending! Debt as a percentage of income is down compared with 10 years ago, and savings are up substantially. However, as life gets back to normal around the world, and growth eventually slows down over the next few years, inflation will most likely come down too. But the wild cards are the supply-chain driven inflation (material and labor shortages), wage increases, rent and housing increases that tend to be more lasting.

With that said, economists at Goldman Sachs presently expect inflation to fall to 2% by early 2023. Most inflation forecasts that I have seen assume that inflation will come down by late 2022. This is longer than anyone would like, but it's not multi-year 1966 – 1982 stagflation (stagnating economy and high inflation). By the way, during that time, inflation (CPI) averaged 6.8% annualized. So far, I have not seen any inflation forecasts that come close to this duration and magnitude. However, inflation (like the future in general) is very difficult to forecast.

<u>How does this impact my investments?</u>

As long as inflation doesn't get out of hand over a period of years and the economy continues to grow (even slow growth is OK), I think stocks will continue to be the better place for investors, assuming one can stomach stock market volatility. As we have discussed in client meetings the past 6 months, the forecast for cash and high-quality bonds over the next 5-10 years doesn't look good… and when you factor in inflation, investors may end up losing money in cash and high-quality bonds. This is already happening right now as inflation is about 6% and cash and high-quality bonds have earned close to zero the last 12 months, before the effects of inflation are considered. So, stocks at least provide the potential to give us positive after-inflation returns.

Why have stocks historically done well during periods of low and moderate inflation (see chart), and why do we think this could be the case this time?



Sources: Capital Group, Bloomberg Index Services Ltd., Morningstar, Standard & Poor's. All returns are inflation-adjusted real returns. U.S. equity returns represented by the Standard & Poor's 500 Composite Index. U.S. fixed income represented by Ibbotson Associates SBBI U.S. Intermediate-Term Government Bond Index from 1/1/1970–12/12/1975, and Bloomberg U.S. Aggregate Bond Index from 1/1/1976–12/31/2020. Inflation rates are defined by the rolling 12-month returns of the Ibbotson Associates SBBI U.S. Inflation Index.

Tony DeSpirito, Blackrock's Chief Investment Officer of U.S. Equities, commented recently, "Companies are feeling they can raise prices… This is partly because consumer income and balance sheets are exceptionally strong and able to endure price increases. Personal savings saw a notable increase during the pandemic while consumer debt declined. Typically, economies see pent-up demand after a recession but an inability on behalf of the consumer to spend. This time, government infusions and reduced expenses during lockdowns helped to pad pocketbooks."

Let's do the numbers - Jim Stoutenborough, CFP®

- After stocks took a pause in September they returned to positive gains in October. For the month, all the major stock indexes were up, Large U.S. companies, the S&P 500 Index, was up 7.0%, the Russell 2000 also gained 4.3% for October and International stocks, the MSCI World ex US, also came in positive at 3.0%. Bonds were flat for Halloween month.

- The good October numbers kept stocks going into the positive for the year. The S&P 500 is up 24% for the year. The Russell 2000 Index (small U.S. companies) is up 17.2%. The international index, the MSCI World ex US, ended October up 12.4% for the year.

- Quality bonds were still off for the year with the U.S. Aggregate Bond Index (quality U.S. corporate and gov't bonds) down (-1.6%) at the end of October. The yield on the 10-year treasury bond went from 0.92% at the beginning of the year to 1.75% at the end of March, back down to 1.30% at the end of August and back up to 1.56% at the end of October.

Asset Class	Index/Category	As of 10/31/21	2020	2019
Cash and cash alternatives	Average 1-yr CD Rate	0.14%**	0.21%**	0.8%**
U.S. Bonds	Barclays US Aggregate Bond Index	-1.6%	8%	9%
U.S. Large Companies	S&P 500 Index	24%	18%	31%
U.S Small Companies	Russell 2000 Index	17%	20%	26%
International Stock Market	MSCI World ex US NR USD	12%	8%	22%

Numbers come from Morningstar, Raymond James and **Bankrate.com

Inside & Outside of PFS

Alex Petrovic - I hope fall has treated you well so far! Since our last newsletter, Ben and Alex had their school photos taken. I tried to get Ben in for a haircut before the photos, but unfortunately, by the time I remembered it was too late! Good job, Dad!

Ben played soccer this fall for the first time through Leawood Parks and Recreation. Two friends of his from preschool also played with him on the same team. Overall, Ben liked playing soccer, but I am not sure he will do it again. On occasion, he was not happy to go to practice or a game. He told me he likes running, but he doesn't like to get sweaty! In his defense, the first few weeks in September were very warm. We haven't decided what he will do in the winter to have some fun (and wear him out a bit). We are considering gymnastics, swimming again, or maybe hip-hop dance classes. Ben loves to dance! Stay tuned…

Little Alex is almost 10 months old and is crawling around the house and pulling up on anything he can find. He enjoys walking, with our help of course. He has 8 teeth and is enjoying trying new foods since we try to feed him something from our dinner plate. At his 9-month doctor's appointment, he came in at around 50th percentile in height, weight and head circumference. This is great progress in our option since he was born only in the 10th percentile. He is a very good eater!! Overall, Alex is a happy baby still, and has a great, toothy smile!

Dasha and I are busy but doing well. Dasha is back in school in the evening working on her MBA through Rockhurst University. She is on track to be done by the end of 2022. It's been a long journey, but she is close! For me, I have been trying to coordinate various home improvements and have been going to physical therapy for tendonitis (AKA tennis elbow) in both of my arms. I am finally at the point where (if I had time!) I could start playing a bit of tennis again. Between the move last year, settling in, and having a baby in January this year, I haven't had much time to play even if I had been healthy.

I hope you and your family enjoy the upcoming holidays and continue to stay healthy!!!

Marsy Gordon - As I write this on a cloudy, cold, and blustery day, it is obvious fall is here and winter will be following soon. This kind of day also reminds me the holidays are just around the proverbial corner. Hopefully we will be able to spend time with family this year over Thanksgiving and Christmas. I certainly missed that last year. You may have noticed the same. Before I get too far ahead of myself, I need to figure out what to do with this cloudy, cold, and blustery day. Maybe I should make a big pot of soup tonight!

Jim Stoutenborough - Probably the big news is that I ran and finished the ½ marathon portion of the Kansas City Marathon – 13.1 miles. It was the culmination of 12 weeks of pretty intense training. The starting (and finish) line was just across the street from my apartment in front of the Nelson Atkins Museum so it couldn't have been easier to get to. Fortunately, the weather was great – a little chilly in the morning – but once the sun came up it got better.

Because of all the roadwork on Main Street the route was a little meandering but enjoyable - starting west, then north and east and then a mix of south and east. I didn't realize how hilly downtown was until I ran it. Running north into downtown was mostly uphill but fortunately running south out of downtown was a little more downhill. About mile 10 at around 18th and Vine was where my hips started to hurt – and then it got progressively worse from there. Most of the pain was the result of the route being 100% road versus when I trained it was usually a mix of road, trail and soft track. The last 3 miles were tough, but I crossed the finish line and that felt good.

At the end I got a finisher's medal and a bottle of water – and being Kansas City, all participants got a free brisket sandwich and a beer. I took the sandwich back to the apartment to my daughter and then came back and got the beer. May have been the best tasting beer I ever had after 13.1 miles.

Jeannine Shaffer - I have discovered internet videos, which all started when I choose to "follow" a couple of people on Facebook. The cooking demonstrations, craft or home repair projects, dance and exercise routines, and music videos that you can scroll through never end making it so hard to stop. I should be reading some good books instead.

Bryson Slater - The past couple of months have been busier than ever! I took a trip to Vegas, celebrated my birthday, went to Columbia to watch a Mizzou game, and played a few rounds of golf to wrap up the 2021 season. I am now preparing to make the journey south of the border for a good friend's wedding. We are going to a resort near Cancun in early November. I am a groomsman in the wedding, so that will make it all the better! It will also be nice to relax on the beach for a few days before the Midwest winter weather arrives.

Marilyn Brohm – First, I'm thankful for the wonderful fall weather, but sure don't like the switch in time last weekend. It's almost dark when I leave from work and sure miss my evening walk with the dog. I'm getting ready to remodel my kitchen – the last, most inconvenient, messy, and expensive project on my house. I dread all the mess and still have not gotten any bids. Not in a big hurry, just want to have it completed by spring.