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The Archvest Advantage Q4 2022 Newsletter

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2022 Recap

2022 was a rough year for asset classes across the board. US equities as measured by the S&P 500 ended the year -18.1% and international equities as measured by MSCI EAFE, did not fare much better -14.5%. Though it is always challenging to be an investor when the market is down, given the range of outcomes and risk level of the market, we would expect this level of negative return approximately once a decade. What surprised investors more was that the US aggregate bonds also declined by double digits, ending at -13.0% for the year, the worst performance in modern times, even worse than the 2008 financial crisis. This was due to the Fed's aggressive action of raising rates to levels unanticipated by the market. Since June, the Federal Reserve (Fed) raised rates by .75% four consecutive times, then ended the year with a .50% rate increase in December. The Fed has demonstrated that it will continue aggressively raising rates to combat inflation if necessary.

Clearly, the dominant theme driving negative performance across asset classes was the uncertainty around the impact of heightened inflation and rising interest rates. Heading into 2023, we expect the Fed to slow the pace of interest rate hikes as inflation slows. The economic signs point to a slowing economy and a possible recession. If fact, depending on the level of unemployment, the Fed will likely need to pause rate increases. We, along with other financial institutions, anticipate continued volatility in 2023 until interest rate increases are predictably slower and, ultimately, paused.

Strategy for 2023

We have been underweight equities in our model portfolios for the last several years because we believe that the market has been overvalued. This downturn has adjusted the market valuations making equity prices more reasonable, but we remain cautious. Throughout the course of 2023, we plan to rebalance the equity allocation to a more moderate stance from the current conservative-leaning models. We are seeing some particularly attractive structured CDs which will give you exposure to the US large caps with no downside if held to maturity. Structured CDs and notes will allow us to add upside potential to your portfolio without drastically increasing risk to the investment allocation.

SECURE Act 2.0

Secure Act 2.0 is now the new law of the land. The legislation increased the age for required minimum distributions (RMD) starting in 2023, decreased the penalty for failing to take RMDs, increased catch-up contributions starting in 2025, and waived the RMD requirement for Roth accounts in employer-based retirement plans. Starting this year, the RMD age increased to age

73 and will further increase to age 75 in 2033. Therefore, if you are under the age of 73 in 2023 and do not need to take withdrawals from your retirement account, we should revisit your retirement account distributions for the year. There is much more in Secure Act 2.0 and we will keep you updated on how it may affect your financial plan.

Difference between Banks, Broker-Dealers, and Crypto Exchanges

In the world of finance, there are primarily banking institutions and brokerage institutions. Over the past several years, we now have had crypto institutions. As we think of the recent headlines, we wanted to step back and consider these different types of institutions and the risk or lack thereof to your money.

When you deposit money at a bank, the money is not held by the bank. As part of banking operations, your money is lent out to borrowers and the bank only retains the required reserves. This acts as a money multiplier in the economy, creating the risk of defaults because the money is not held at the bank. This is where the Federal Deposit Insurance Corporation (FDIC) comes in. FDIC insures deposits up to $250,000 per registrant. In the times that banks have failed, the FDIC ensures that the depositors were unharmed in the event of bank failure. This is why it is important to keep your bank deposits under FDIC limits.

Broker-dealers (BD) such as Charles Schwab & Co. are not banking institutions and operate differently. When you deposit your money, the funds are held in a separate account and not comingled with the company's assets. This is required by law. Additionally, BDs have to be members of the Securities Investor Protection Corporation (SIPC), which ensures that the securities (stocks and bonds) held within your account are not lost. When a broker-dealer fails, your account remains yours and is not subject to the company's creditors. In 2008, when Lehman Brothers failed, the client's assets remained safe and accessible with minimal disruptions. Operationally, BDs operate very differently than banks and your funds are not subject to the same default risk as bank depositors. Therefore, there is no need to spread your assets across multiple BDs as with banks.

Crypto exchanges such as FTX Trading are entirely different. As you may have read, FTX, a major crypto exchange, recently declared bankruptcy. Over 1 million clients may be creditors in bankruptcy proceedings. This is because the company failed to keep the client's assets segregated from the company's assets. It is important to remember that crypto remains relatively unregulated and, therefore, not subject to the same level of protection for clients as banks and BDs.

California Insurance Update

Our insurance contacts have warned us about the state of the property and casualty insurance market in California. Many insurers have pulled out of the market/ stop issuing new policies, and the others remaining are drastically increasing their premiums. Do not be shocked when you receive your insurance renewal bill this year; expect an increase in premiums. For example, most

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insurance carriers have been losing money on their auto lines because the state insurance commissioner has not allowed for rate increases over the past several years coupled with the high values in the used car market. Unfortunately, you, as the consumer, do not have any good options. While we are happy to review your coverages to ensure you have adequate insurance in place, 2023 might not be the year to be shopping for a new policy, the choices available have thinned out. Likely, your best bet will be to stick with the insurance carrier that you already have.

From the Tax Desk

President Biden and Gavin Newsom declared a state of emergency due to the storms. This declaration pushed back both the estimated tax payments as well as the tax filing deadline for the IRS and Franchise Tax Board to May 15, 2023, for the following counties:

> Alameda, Colusa, Contra Costa, El Dorado, Fresno, Glenn, Humboldt, Kings, Lake, Los Angeles, Madera, Marin, Mariposa, Mendocino, Merced, Mono, Monterey, Napa, Orange, Placer, Riverside, Sacramento, San Benito, San Bernardino, San Diego, San Francisco, San Joaquin, San Luis Obispo, San Mateo, Santa Barbara, Santa Clara, Santa Cruz, Solano, Sonoma, Stanislaus, Sutter, Tehama, Tulare, Ventura, Yolo, and Yuba county

For those outside of California, the tax filing deadline remains April 18th. As always, we recommend you speak with your tax professional to confirm your eligibility. Please send us a copy of your tax return when available for our records and review.

Thank You For Putting Your Trust In Us

As always, we greatly appreciate the confidence you have placed in us to work alongside you as you financially prepare for your future. We hope that you're staying healthy and taking good care of yourself.

Starting this year, we are changing the frequency of our newsletter from quarterly to semiannual. As before, we will provide you with market updates as necessary.

If you have any questions or concerns, please contact us and we will be happy to meet with you and review or refresh your overall plan. Follow us on Facebook, LinkedIn, and Twitter, as well as our RSS feed, to stay up to date on what we're reading and thinking. Thank you so much for the opportunity to work alongside you.

THE Archvest Team