



### Current Financial Planning and Investment Themes

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## “Crossing the Bridge”

*It seems our belief that markets would cross the bridge into recovery has become the current situation, but the path forward remains obscure. The calls for recession have grown somewhat quieter, yet still seem like the majority opinion. Our analysis continues to see data that supports the case for avoiding recession but acknowledge multiple factors point toward a period of slower growth. The resiliency of consumers and*



*capital markets is a remarkable phenomenon that continues to show strength despite the current interest-rate environment. That said, being prepared for challenges, yet still forging ahead, is the right mindset for the current conditions...*

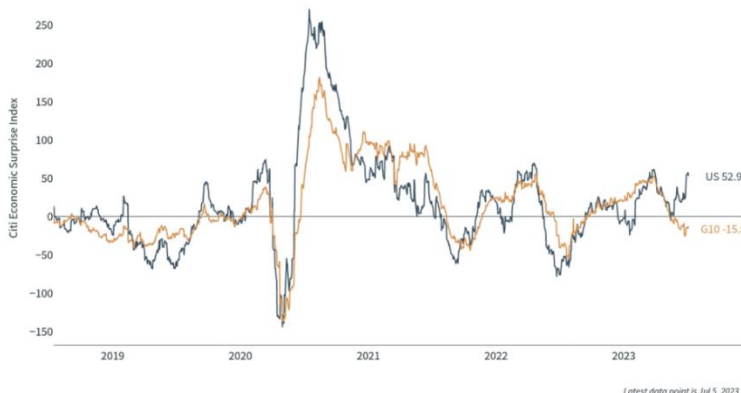
*“Discipline is the bridge between goals and accomplishment.” - Jim Rohn*

## US Economics

Market and Economic Chartbook | July 10, 2023

### Citi Economic Surprise Index

Positive and negative economic surprises for the U.S. and G10 countries  
Past 5 years. Index is calculated daily using a three month window



The economy seems to be crossing the bridge to higher rates without much trouble. The latest Citi Economic Surprise Index read is 52.9, meaning actual economic data is solidly beating expectations. GDP for the 1<sup>st</sup> quarter was revised upward to 2.0% for the final reading, a number firmly not in recession. Likewise, the “preview” of 2<sup>nd</sup> quarter GDP is estimated at a compelling 2.3% according to the Atlanta Fed’s GDPNow. While higher rates are certainly having negative effects, the resiliency of the economy is impressive. There are many economic measures that support our continued thesis of avoiding recession but

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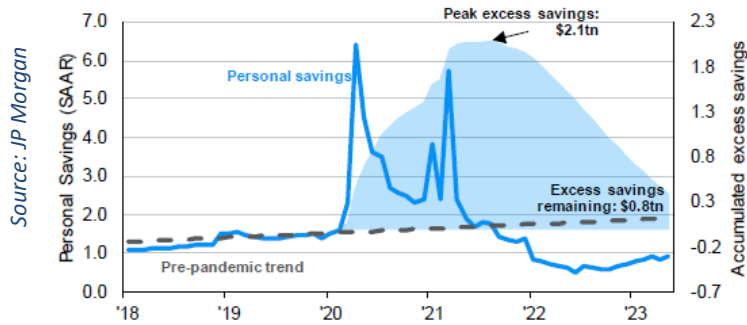
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paddling upstream for a bit. Unemployment remains near 50-year lows with the June U-3 (official) unemployment rate at 3.6%, a slight uptick from March's 3.5%. Additionally, the U-6 (broader definition including part-time) also slightly ticked up to 6.9% in June from the March rate of 6.7%. Notably, both measures are well below their long-term average. Meanwhile, we are still seeing more job openings (9.8M) than jobseekers (6.0M), so 1.63 open jobs for everyone looking. A strong labor market has allowed consumers to maintain healthy spending levels, especially when you combine that with the enduring high levels of household excess savings. Even though higher interest rates and high inflation have reduced excess savings levels from the \$2.1 Trillion dollar peak, there is still an \$800 Billion reserve. We will have to see if interest-rates and inflation revert back to normal before the excess runs out. However, the well-known

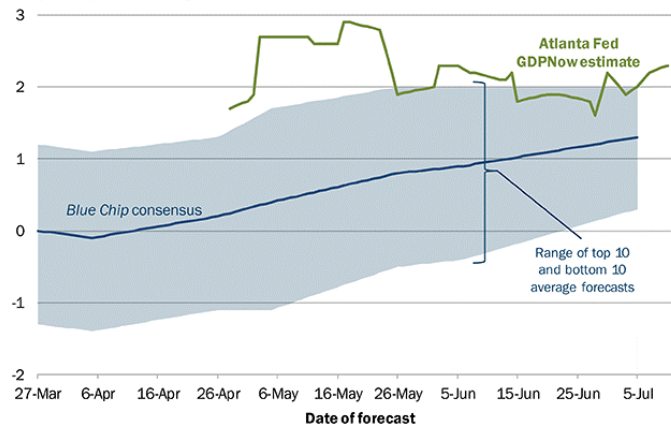
### Household excess savings

Trillions of USD



by far the largest component of GDP growth (68%). We believe that the consumer is the “bridge” over the recession waters...

**Evolution of Atlanta Fed GDPNow real GDP estimate for 2023: Q2**  
Quarterly percent change (SAAR)



Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts

Note: The top (bottom) 10 average forecast is an average of the highest (lowest) 10 forecasts in the Blue Chip survey.

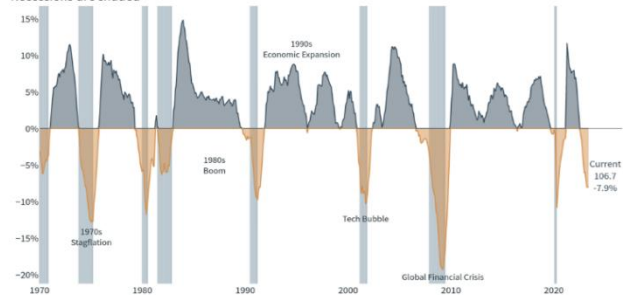
Conference Board Leading Economic Indicators index is still signaling a recession over the next 12 months, although it has been pointing to that for quite a while now. While the index has historically been fairly accurate, critics argue that the index relies too heavily on manufacturing data and doesn't capture “consumption” which makes up 68% of the economy. That's been the story of why we believe the US economy avoids recession, because when consumers don't have to worry about being unemployed, they will keep spending close to current levels, and consumer spending is

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### Leading Economic Indicators

Conference Board LEI year-over-year percent change

Recessions are shaded



Latest data point is May 2023

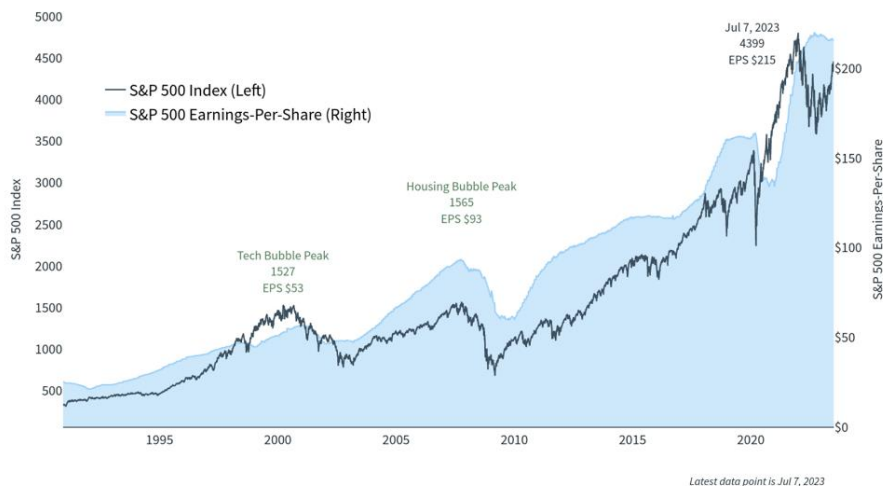


### US Equity Markets

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#### The Stock Market and Earnings

S&P 500 Index price and trailing earnings-per-share since 1990



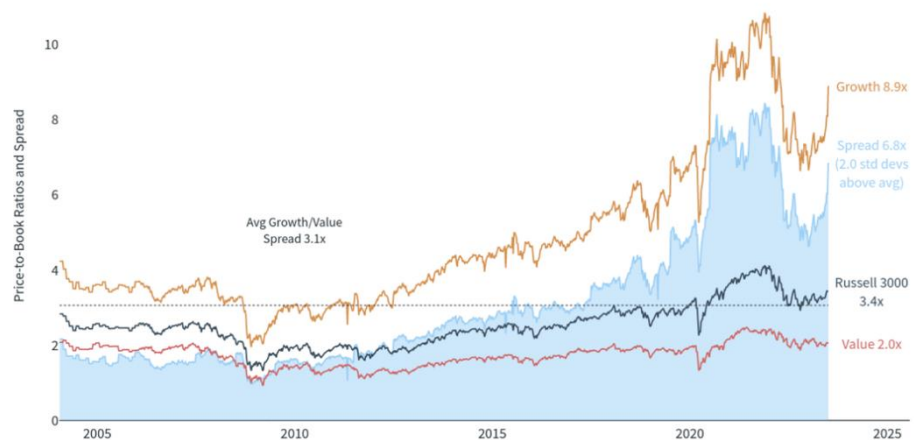
Despite the naysayers, the S&P 500 put up a strong 1<sup>st</sup> half of the year, delivering decent earnings and finishing June at 4450. This is above even our year-end estimate high of 4400 (which some thought was too optimistic). This is a 16.9%+ year-to-date return, very strong considering the average forecast was for a negative year coming into 2023. The Dow Jones, however, was only up 3.8% during the first half. The stand-out though was the NASDAQ gaining 31.7% during the same period. If you zoom out to the trailing 1-year period, however, the dispersion is a bit less pronounced with the

Dow gaining 11.2%, S&P 500 gaining 17.3%, and the NASDAQ gaining 24.7%. Much of what has allowed NASDAQ to break-out, and the Dow to lag behind is the performance of the so-called “MAGNIFICENT 7” stocks that are responsible for ¾ of the market gains this year. The stocks are Apple, Microsoft, Nvidia, Amazon, Meta, Alphabet & Tesla. This staggering concentration has created questions about the sustainability of the rally and a focus on market breadth. That’s not to say that these are the only stocks making gains this year. They just have both significant weightings in indexes as well as significant performance. Growth has historically enjoyed higher valuations than value, but the spread has significantly widened as of late. This makes us think Growth will likely be in a sideways market over the next quarter or two and value should start to participate and grind higher. That said, due to the rapid pace of gains for the S&P 500, the chances of a 5-10% pullback are elevated. For those reasons, we are raising our year-end S&P 500 target to 4400-4600.

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#### U.S. Growth vs Value Valuations

Russell 3000 Growth and Value price-to-book ratios and valuation spread







### US Fixed Income

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#### Fixed Income Performance

Annual bond sector total returns



2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Treasuries 13.7%	High Yield 58.2%	EMD Local 15.4%	TIPS 13.6%	EMD Local 17.5%	High Yield 7.4%	Munis 9.1%	Munis 3.3%	High Yield 17.1%	EMD Local 14.7%	Munis 1.3%	EMD USD 15.0%	TIPS 11.0%	TIPS 6.0%	Munis -8.5%	EMD Local 7.6%
MBS 8.3%	EMD USD 29.8%	High Yield 15.1%	Munis 10.7%	EMD USD 17.4%	MBS -1.4%	Corp 7.5%	MBS 1.5%	EMD USD 10.2%	EMD USD 10.3%	MBS 1.0%	Corp 14.5%	Corp 9.9%	High Yield 5.3%	EMD Local -10.2%	High Yield 5.4%
Agg 5.2%	EMD Local 21.7%	EMD USD 12.2%	Treasuries 9.8%	High Yield 15.8%	Corp -1.5%	EMD USD 7.4%	EMD USD 1.2%	EMD Local 10.0%	High Yield 7.5%	Treasuries 0.9%	High Yield 14.3%	Treasuries 8.0%	Munis 1.5%	High Yield -11.2%	EMD USD 4.1%
TIPS -2.4%	Corp 18.7%	Corp 9.0%	Corp 8.1%	Corp 9.8%	Agg -2.0%	MBS 6.1%	Treasuries 0.8%	Corp 6.1%	Corp 6.4%	Agg 0.0%	EMD Local 10.1%	Agg 7.5%	Corp -1.0%	MBS -11.8%	Corp 3.2%
Munis -2.5%	Munis 12.9%	Agg 6.5%	Agg 7.8%	TIPS 7.0%	Munis -2.6%	Agg 6.0%	Agg 0.5%	TIPS 4.7%	Munis 5.4%	TIPS -1.3%	Agg 8.7%	High Yield 7.1%	MBS -1.0%	TIPS -11.8%	Munis 2.7%
Corp -4.9%	TIPS 11.4%	TIPS 6.3%	EMD USD 7.3%	Munis 6.8%	Treasuries -2.7%	Treasuries 5.1%	Corp -0.7%	Agg 2.6%	Agg 3.5%	High Yield -2.1%	TIPS 8.4%	EMD USD 5.3%	Agg -1.5%	Treasuries -12.5%	Agg 2.1%
EMD Local -5.9%	Agg 5.9%	Treasuries 5.9%	MBS 6.2%	Agg 4.2%	EMD USD -5.3%	TIPS 3.6%	TIPS -1.4%	MBS 1.7%	TIPS 3.0%	Corp -2.5%	Munis 7.5%	Munis 5.2%	EMD USD -1.8%	Agg -13.0%	TIPS 1.9%
EMD USD -12.0%	MBS 5.9%	MBS 5.4%	High Yield 5.0%	MBS 2.6%	EMD Local -8.3%	High Yield 2.5%	High Yield -4.5%	Treasuries 1.0%	MBS 2.5%	EMD USD -4.3%	Treasuries 6.9%	MBS 3.9%	Treasuries -2.3%	Corp -15.8%	MBS 1.9%
High Yield -26.2%	Treasuries -3.6%	Munis 2.4%	EMD Local -2.0%	Treasuries 2.0%	TIPS -8.6%	EMD Local -5.2%	EMD Local -14.3%	Munis 0.2%	Treasuries 2.3%	EMD Local -6.9%	MBS 6.4%	EMD Local 3.5%	EMD Local -9.2%	EMD USD -17.8%	Treasuries 1.6%

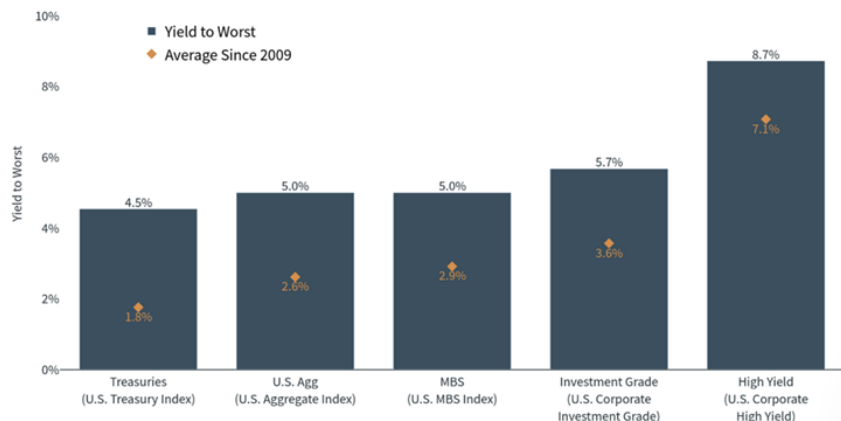
Latest data point is Jun 30, 2023

defaults. A particularly interesting part of what we consider the “fixed income” market is Preferred Stocks. These securities provide fixed payouts typically without a maturity date. Many financial institutions like banks issue these securities, which have suffered in recent months due to banking sector concerns. This has provided attractive discounts with very attractive yields. Keep in mind though that there is still uncertainty about when the Fed will officially stop raising interest rates which is keeping volatility in the Fixed Income market elevated in the short-term. In the medium-term, there remains additional upside price opportunity when rates begin to fall which is likely to be sometime in 2024.

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#### Traditional Sources of Bond Yield

Yield to worst and averages since 2009



Latest data point is Jul 7, 2023



### International Markets

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#### Global Equity Valuations

Forward P/E Ratios for the S&P 500, MSCI EAFE and MSCI EM



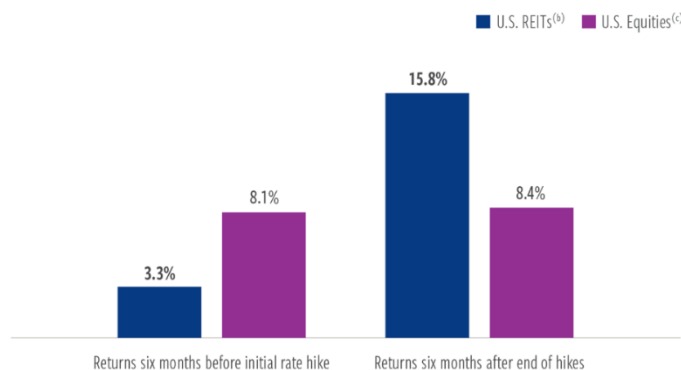
Until recently, international stock markets had been closing the valuation gap somewhat since the extreme divergence in 2022 when looking at P/E (Price/Earnings) ratios. However, US Stocks posted a 16.9% gain through the first half, racing ahead of the MSCI All Country World ex-US index's 9.4% gain. You can see the divergence is partly due to P/E multiple expansion in the U.S. with international counterparts not enjoying the same level of increased confidence. However, valuation still favors the international side as the forward P/E ratios for Developed Markets and for Emerging Markets are 13.0 and 12.2 respectively. Our view is that the second half

of the year slightly favors the international side as US valuations provide limited upside and the US dollar is coming off multi-decade highs. That said, global economic conditions are much less favorable than the US at the time being so there will need to be some relative improvement to unlock any meaningful outperformance. Recovery in international equities should continue regardless of an improvement in economic conditions. It's just the magnitude of gain that is the question...

### Real Estate

On average, listed REITs have historically outperformed broader equities following hikes to the federal funds rate

Average returns during hiking period cycles(a)



At March 31, 2023. Source: Cohen & Steers calculations, Bloomberg, and Federal Reserve.

As we have mentioned in the past, REITs have performed extremely well during the six months that follow the end of Fed rate hikes. It appears that moment is just around the corner if not already here. The recent headlines surrounding commercial office and the stubbornness of the "return-to-office" movement have painted Real Estate in a negative light. However, there are plenty of other types of REITs that are generating very attractive cash-flows such as Data-Centers, Warehouses and Healthcare. Active management here is vastly preferred vs passive indexing. Solid fundamentals along with strong balance sheets should make REITs well positioned at this point.

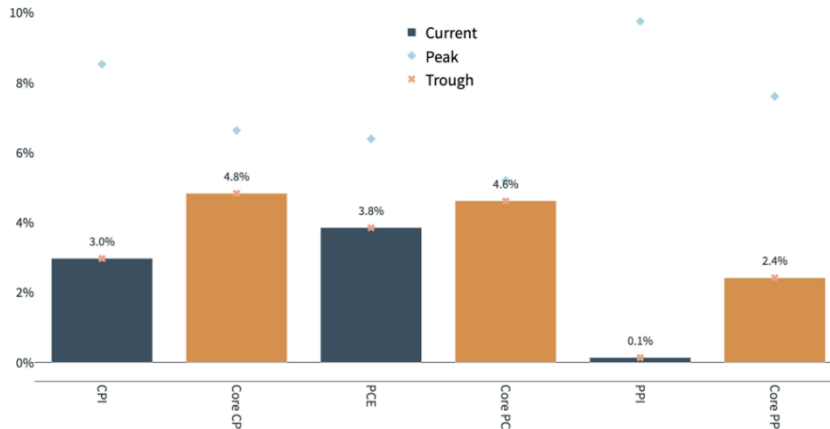


### Inflation, Interest Rates & the Fed

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#### Inflation Measures

Current year-over-year changes and 12-month peaks and troughs



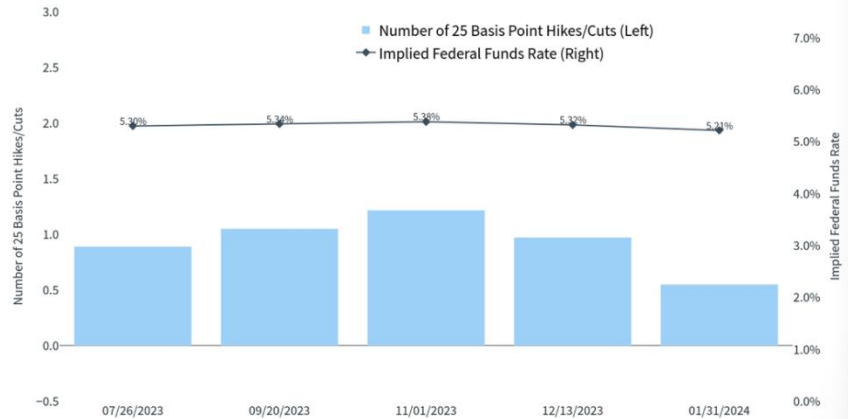
High rates of inflation may soon be considered “water under the bridge” with the June CPI (Consumer Price Index) report showing Headline CPI falling down to 3.0% year-over-year. Furthermore, the June PPI (Producer Price Index) came in at a 0.1% year-over-year increase, which is regarded as a leading indicator for consumer pricing. You can see from the chart to the left, all measures of inflation are at their lowest points in the last 12 months. That said, the Fed’s long-time preferred measure of inflation, Core PCE (Personal Consumption Expenditures) which

excludes food and energy is still lingering above 4%, albeit at its lowest level in a year. Unfortunately, Core PCE has been in the 4.6%-4.7% range since December of last year. This measure seems to be the “stickiest” of the “sticky” inflation. That has caused the Fed to indicate they are planning on adding more rate hikes in the upcoming meetings even though they decided to skip a hike in June. So far, even though they raised rates at the fastest pace in modern history, the economy has not entered a recession (thanks to the consumer). However, they seem to not be able to resist pushing their luck. Recently during testimony to the House Financial Services committee, Chairman Powell indicated that 1-2 more rate hikes this year would be a “good guess”. The latest Fed Funds Futures probabilities shows that the market only believes 1 more rate hike is in store, coming July 26<sup>th</sup>, but that rates will remain steady through the remainder of the year. Previously the market saw rate cuts happening prior to year-end. Markets seem to be OK with what the Fed is doing at this point since, contrary to conventional wisdom, the yield curve, and the Fed’s own prediction of recession, the economy is holding up just fine despite the wild interest rate increases. Our view is that markets will remain calm unless some surprise economic deterioration is discovered and the Fed keeps pushing up to 6%...

Market and Economic Chartbook | July 13, 2023

#### Fed Funds Futures Implied Rates

Implied fed funds rates and number of hikes/cuts at each Fed meeting



### Legislative Affairs

After a rare showing of bipartisanship, the debt ceiling showdown is behind us. Now, lawmakers have resumed discussions about how to amend the Social Security program. Left unchanged, the trust fund is projected to be depleted by the year 2033 and projected payroll taxes would then only cover 77% of benefits. Senate Democrats, led by Sen. Bernie Sanders, are working



on the “Social Security Expansion Act” that promises to *increase* benefits by \$2,400 per year for future recipients. To pay for the increased benefits as well as shore up the system, they propose applying the 12.4% to *all* income above \$250,000+. That is a huge tax increase as current 12.4% FICA tax caps out at \$160,000. The other significant pay for is the bill would raise the Net Investment Income Tax, also known as the Obamacare surcharge, from the current 3.8% to 16.2% for taxpayers whose income is above \$200,000 for single filers and \$250,000 for joint filers. A contrasting strategy from the Republicans, included in the “Protecting America’s Economic Security” budget proposal, calls for gradually raising the FRA (Full Retirement Age) to 69 from 67 as well as reducing some benefits for “high income earners” to fix Social Security. Political experts widely agree that neither proposal is likely to make its way through to becoming law. Nonetheless, it’s good news that Washington has this important issue on its radar! Our view is that a combination of raising the retirement age to coincide with modern-day life-expectancies, a slight raise in the FICA tax, and a modest raise in the taxable income threshold will be key ingredients to any solution.



### **Financial Planning Corner**

## Planning for Long-Term Care Expenses

Planning for expensive healthcare late in life is one of the more daunting parts of retirement planning. What is even more daunting is looking at the nationwide average monthly costs for long-term care services in 2023.

- \$5,148 for a home health aide
- \$1,690 for adult day care
- \$4,500 for assisted living
- \$7,908 for a semi-private room in a skilled nursing facility
- \$9,034 for a private room in a skilled nursing facility



Another cost consideration is that of inflation and the fact that today's costs will likely rise by the time you need it. The annual Genworth cost of care index forecasts the daily cost of care in a private nursing home bed will be \$11,000 per month in five years. At an assisted living facility, they estimate that you will spend \$5500 per month in 5 years. That is an estimated 4.4% annual inflation projection for long-term care costs, which is more than double that of the Federal Reserve's 2% inflation target.

According to recent studies, up to 70% of people will need these services at some point in their lives. However, 90% of people require three or less years of care in a skilled nursing facility. Given the likelihood and potentially prohibitive costs associated with long-term care, we believe that incorporating a plan for these expenses into your retirement plan is critical to your financial well-being.

### What is Long-Term Care?

Long-term care comes into play when assisting people with activities of daily living (ADLs). There are six ADLs, and to qualify for long-term care, you must be unable to perform at least two of them without assistance.

These ADLs include bathing, continence, dressing, eating, transferring from one place to another (like a couch to a bed), and using the bathroom. If you cannot perform these on your own, you will need assistance. How should you plan for this type of scenario? Should you pay for it out of pocket, purchase an insurance policy, or some other alternative?





## General Approaches to Long-Term Care Plans:

### 1) Self-Insurance

With 90% of people requiring 3 years or less of skilled nursing home care, budgeting for 3 years in a nursing home care should help ensure that you will have sufficient money set aside to self-insure your long-term care costs. It is important to note that this is not a guarantee.

At a current annual cost of \$108,408, three years of care would cost \$325,224. For those who need nursing home care, on average they need it starting at age 85. We would highly recommend inputting this scenario in cash-flow analysis software.

Married couples can likely budget the amount for just one person. Often, the first person can be taken care of by the second- person with some professional help.

The money you set aside could be available in an HSA, IRA, 401(k) plan, or taxable investment accounts. For those who have been contributing the maximum to their HSA, they can count those HSA funds towards long-term savings target while taking advantage of its triple tax advantages.

This approach is generally advisable for households with a liquid net worth of at least \$2M.

### 2) Traditional Long-Term Care Insurance

Traditional Long-Term Care Insurance (LTCI) provides insurance coverage in the event of a stay in a nursing home, assisted living facility, and in some cases home health services.

Traditional LTCI is highly customizable to fit the client's specific anticipated needs. Custom options include the benefit period, daily benefit amount, premium structure, and elimination period.

Only Traditional LTCI policies are eligible for a state partnership program. This program is available in most states and benefits the insured in the event they consume all their LTCI benefits. For the policy benefits paid on behalf of the client, that same amount will be exempt for Medicaid, meaning the client can seek Medicaid eligibility, if needed, without adhering to the typical asset limitations.

This approach can be advisable for households with a liquid net worth of \$500k-\$2M. However, it is not always advisable for those with prominent levels of fixed income in retirement (like retirees with pension benefits). Typically, the best time to purchase LTCI is in your late fifties or early sixties.



### **3) Hybrid Long-Term Care Insurance**

Hybrid policies are life insurance policies with a long-term care insurance rider. Typically, people who buy these policies are buying them for the long-term care insurance benefits. These policies offer a

fully guaranteed premium that could never increase and a flexible premium structure, meaning clients can pay it up in a twenty pay, ten pay, or single premium. It can have a lifetime premium cycle that can never increase since the premiums are guaranteed in the contract.

They also have a “live, die, quit” feature, meaning that while the client lives, there is a large long-term care benefit pool that grows at a guaranteed rate of inflation. If they quit, they can surrender and get back some or all their premiums (depending on how they structure the plan). If they pass away, there is an income-tax-free death benefit payable. So, no matter which event happens, they make use of their policy.

These policies do come at a higher initial premium than traditional plans, but the premium is fixed for life and can be paid up in shorter increments.

This approach can be advisable for households with a liquid net worth of \$500k-\$2M. However, it is not always advisable for those with prominent levels of fixed income in retirement (like retirees with pension benefits).

### **4) Medicare/Medicaid Planning**

It is important to keep in mind that Medicare will also pay for certain long-term care services for a limited time. Medicare uses a period of time called a benefit period to keep track of how many days of SNF benefits you use, and how many are still available. A benefit period begins on the day you start getting inpatient hospital or SNF care. You can get up to 100 days of SNF coverage in a benefit period. Once you use those 100 days, your current benefit period must end before you can renew your SNF benefits.

The Medicaid program pays for roughly half of the nation’s total nursing home cost. To qualify for Medicaid, a senior must have a low income and very few assets. If one spouse remains at home while the other lives in a long-term care facility, Medicaid will allow your household to keep more of your assets. In most states, you can make up to 300% of the SSI income limit and still qualify. (In 2023, 300%



of the SSI limit, \$914, is \$2,742 per month). In addition to an income limit, states also impose a limit on the amount of assets you can have while still qualifying for Medicaid. Again, the exact asset limit varies widely by state, but for many states, it is \$2,000 (or \$3,000 for a married couple).

Fortunately, some of your assets are exempt. That means when tallying up your assets, you can leave out the following:

- a car
- household and personal belongings
- one wedding and one engagement ring of any value
- burial plots and pre-paid funeral expenses
- a small whole life insurance policy
- your home, if you intend to return to it or your spouse, minor child, or blind or disabled child live in it.

If you are spending down your assets to qualify for Medicaid, you cannot just give away all your money to your family to qualify for Medicaid faster. Any asset transferred out of your name during the "5-year look-back period" can result in a penalty period during which you are not eligible for Medicaid.

Utilizing an irrevocable asset protection trust to help qualify for Medicaid, or just planning on Medicaid paying for long-term care needs is generally advisable for households with a liquid net worth of under \$500k.

*We're here to help. If you have questions about these or any other topics, don't hesitate to call us at (855) AFS-4545.*