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Financial PERSPECTIVES

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Winning at Investing:

It's a Marathon, Not a Sprint

Who doesn't like to win? Whether its memories of blue ribbons, childhood sports championships or the pickleball match last week, winning is fun. Remember though, when investing, coming in first and winning are not synonymous. Our Importance of Diversification chart that we publish each year adding on the previous year's returns for each asset class is a perfect example of this.

Per this chart, to "win" you would have had your portfolio 100% allocated to real estate in 2021, managed futures in 2022 and large-cap growth stocks in 2023. And, as we know, accurately forecasting to this level of detail—and getting in and out of various asset classes, much less specific stocks—is challenging. If it were easy, we'd all be very rich. As a result, we suggest diversification, so investors have broad market exposure to capture both the winners and "losers" over various time periods. "Losers" is in quotes because many of those still give you a 6-8% return for the year, which is not losing.

In addition to diversification, compounding is the real magic of investing. Compounding is most often thought of in terms of interest or the increasing value of an asset due to the interest earned on both the principal and accumulated interest. The same is obviously true in regard to your entire portfolio. Each year's return added to the increasing base amount. Keeping compounding in mind is an important component to successful investing as it helps shift the focus from, "What is the highest return I can earn this year?" to "How can I invest to sustain the best returns for the long term?"

In the book "Same as Ever," author Morgan Housel wrote, "Investor Howard Marks once talked about an investor whose annual results were never ranked in the top quartile, but over a fourteen-year period he was in the top 4% of all investors. If he keeps those mediocre returns up for another ten years he may be in the top 1% of his peers—one of the greatest of his generation despite being unremarkable in any given year."

Marks' quote and the words of wisdom below remind us that it's critical to stay the course and celebrate the winning of compounding versus letting fear and greed drive us to try to time the market or be frustrated that we didn't have the "winner" in our portfolio this year:

> *The stock market is designed to transfer money from the active to the patient.”*
>
> **WARREN BUFFETT**

> *Stocks are a safe bet, but only if you stay invested long enough to ride out the corrections.”*
>
> **PETER LYNCH**

> *Slow and steady wins the race.”*
>
> **AESOP**

Marathons aren’t easy but your financial advisor, and Edwards as a whole, are here to help you cross the finish line.

The Importance of Diversification:

Annual returns of various asset classes

2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	10 Yr Avg
Small-Cap Stocks 41.3%	Real Estate Securities 27.2%	Large-Cap Growth 5.7%	Small-Cap Stocks 26.6%	Emerging Markets 37.3%	Cash 1.9%	Large-Cap Growth 36.4%	Large-Cap Growth 38.5%	Real Estate Securities 39.9%	Managed Futures 22.1%	Large-Cap Growth 42.7%	Large-Cap Growth 18.6%
Large-Cap Growth 33.5%	Managed Futures 15.8%	Managed Futures 3.6%	Mid-Cap Stocks 20.7%	Large-Cap Growth 30.2%	Govt./Corp. Bonds -0.4%	S&P 500 Index 31.5%	S&P 500 Index 18.4%	S&P 500 Index 28.7%	Cash 1.5%	S&P 500 Index 26.3%	S&P 500 Index 14.9%
Mid-Cap Stocks 33.5%	S&P 500 Index 13.7%	Real Estate Securities 2.3%	Large-Cap Value 17.3%	International Stocks 25.0%	Large-Cap Growth -1.5%	Real Estate Securities 28.1%	Emerging Markets 18.3%	Large-Cap Growth 27.6%	Large-Cap Value -7.5%	International Stocks 18.2%	Small-Cap Stocks 12.5%
Large-Cap Value 32.2%	Large-Cap Value 13.2%	S&P 500 Index 1.4%	S&P 500 Index 12.0%	S&P 500 Index 2.8%	Real Estate Securities -4.1%	Large-Cap Value 26.5%	Mid-Cap Stocks 13.7%	Small-Cap Stocks 26.8%	Equal Weight Blend -12.1%	Mid-Cap Stocks 16.4%	Mid-Cap Stocks 12.3%
S&P 500 Index 32.4%	Large-Cap Growth 13.1%	Govt./Corp. Bonds 0.2%	Emerging Markets 11.2%	Mid-Cap Stocks 16.2%	Managed Futures -4.4%	Mid-Cap Stocks 26.2%	Small-Cap Stocks 11.3%	Large-Cap Value 25.2%	Mid-Cap Stocks -13.1%	Small-Cap Stocks 16.1%	Large-Cap Value 11.2%
International Stocks 22.8%	Mid-Cap Stocks 9.8%	Cash 0.1%	Equal Weight Blend 10.3%	Equal Weight Blend 15.4%	S&P 500 Index -4.4%	Small-Cap Stocks 22.8%	Equal Weight Blend 10.6%	Mid-Cap Stocks 24.8%	Govt./Corp. Bonds -13.6%	Equal Weight Blend 14.4%	Real Estate Securities 8.7%
Equal Weight Blend 18.3%	Equal Weight Blend 8.9%	International Stocks -0.8%	Real Estate Securities 9.3%	Large-Cap Value 13.7%	Equal Weight Blend -6.7%	International Stocks 22.0%	Govt./Corp. Bonds 8.9%	Equal Weight Blend 17.0%	International Stocks -14.5%	Large-Cap Value 11.5%	Equal Weight Blend 8.7%
Managed Futures 7.5%	Govt./Corp. Bonds 6.0%	Equal Weight Blend -1.0%	Large-Cap Growth 7.1%	Small-Cap Stocks 13.2%	Large-Cap Value -8.3%	Equal Weight Blend 19.9%	International Stocks 7.8%	International Stocks 11.3%	Small-Cap Stocks -16.1%	Real Estate Securities 11.5%	International Stocks 6.5%
Real Estate Securities 3.2%	Small-Cap Stocks 5.8%	Small-Cap Stocks -2.0%	Managed Futures 4.2%	Real Estate Securities 9.3%	Small-Cap Stocks -8.5%	Emerging Markets 18.4%	Large-Cap Value 2.8%	Managed Futures 7.5%	S&P 500 Index -18.1%	Emerging Markets 9.8%	Managed Futures 4.4%
Cash 0.1%	Cash 0.0%	Mid-Cap Stocks -2.2%	Govt./Corp. Bonds 3.1%	Govt./Corp. Bonds 4.0%	Mid-Cap Stocks -11.1%	Govt./Corp. Bonds 9.7%	Managed Futures 1.8%	Cash 0.1%	Emerging Markets -20.1%	Govt./Corp. Bonds 5.7%	Emerging Markets 3.3%
Govt./Corp. Bonds -2.4%	Emerging Markets -2.2%	Large-Cap Value -3.8%	International Stocks 1.0%	Cash 0.9%	International Stocks -16.1%	Cash 2.3%	Cash 0.7%	Govt./Corp. Bonds -1.8%	Real Estate Securities -25.1%	Cash 5.0%	Govt./Corp. Bonds 1.8%
Emerging Markets -2.6%	International Stocks -4.9%	Emerging Markets -14.9%	Cash 0.3%	Managed Futures -2.3%	Emerging Markets -16.6%	Managed Futures -4.6%	Real Estate Securities -5.6%	Emerging Markets -2.5%	Large-Cap Growth -29.1%	Managed Futures -2.8%	Cash 1.2%

Source: Conway Investment Research, Morningstar, MSCI, HFRI

Optimize your Retirement Income Strategy

We face many critical financial decisions over the course of our lives. One of the most challenging things is turning lifetime savings into retirement income. The decisions involved are among the most consequential and complex—and often come once we have limited time to make up for any oversights. Taking too much income or selecting the wrong accounts to withdraw from can deplete otherwise sufficient retirement funding.

It's complex. And it's essential. But it's also manageable.

There are ways to manage retirement income to optimize the probability of having the best outcome. The optimal way depends on your income needs, how you have positioned your assets (both from an investment and tax standpoint), and factors beyond your control. Inflation, for instance, is an example of a factor we cannot control.

How Much Income Is the Right Amount for You?

While we can't know what the market and economy will do in the future, we can make reasonable assumptions. It's best to make assumptions conservatively, allowing room for inevitable variations. If you have a well-funded retirement, you may be able to assume capital retention, a concept in which you are not depleting your assets but instead living off the income your assets generate. As long as you live, you can have retirement income coming in. That's an ideal place to be.

If your retirement is not adequately funded, you may be forced to use an assumption of capital depletion, a process in which you will eventually deplete your investment assets.

The most common methods for determining the amount to withdraw are:

- The fixed percent method.
- The four percent rule.
- Interest only.

Fixed-Percent Method

The fixed-percent method involves taking a fixed percentage of your assets each year. The amount is established annually, often using your Dec. 31 balance for calculations for the coming year. If, for example, you were to withdraw 4% annually, you would calculate 4% of your Dec. 31 balance and take one-twelfth of that each month.

The amount of money you receive each month could vary from year to year, depending on investment performance. The downside is that your income is not predictable far in advance; it relies on each year's investment performance.

4% Rule

The 4% rule sounds similar, but it's not. With this rule, you take 4% of your portfolio in the first year. In the second year, you adjust that amount—not based on investment performance but on inflation.

The upside is that your spending level remains constant by adjusting for inflation year over year.

There is always a chance that high inflation could coincide with periods of weak investment performance. This can result in too large distributions relative to your portfolio size.

Interest Only

Taking interest only allows your core investment portfolio to remain intact. Typically, with this method, you're taking all forms of income: interest, dividends and other income generated by the portfolio. With your core portfolio preserved, you're not spending down your principal. However, your income can vary annually and may not keep pace with inflation.

Tax Buckets

Once you determine your spending technique, you can also look to three tax buckets to decide where to pull funds to meet your spending needs:

- **Taxable investments,** such as bank accounts and regular brokerage accounts
- **Tax-deferred investments**, such as 401(k) plans, 403(b) plans and traditional IRAs
- **Tax-free accounts**, such as Roth IRAs or Roth 401(k)s

Taxable investments can be taxed in several ways. Spending cash, such as from a bank account, has no tax implications. Spending investment assets does have tax implications; the gain on the sale of an asset is taxable as either a short-term or long-term capital gain, depending on the holding period. In addition, any earnings on these investments will be taxed as you earn them.

When using tax-deferred investments for income, withdrawals are taxable as ordinary income—there's no favorable treatment. Every dollar distributed is included as income for federal tax purposes, unless you made after-tax contributions to your IRA or workplace retirement plan when saving. In addition to paying income taxes on your withdrawals, a 10% early withdrawal penalty may also apply if you are younger than 59 1/2, although there are some exceptions.

Distributions from tax-free accounts, like Roth IRAs and Roth 401(k)s, are income tax-free, but only if you meet specific requirements; for instance, if you've met the five-year holding period rule and have reached age 59 1/2. If not, income taxes will be due on the earnings, and a 10% early withdrawal penalty may also apply.

Retirement Income Tax Strategy

Your tax rate is a function of your taxable income; you fill up the lowest rate tax brackets first, then pay higher rates as you move up the income ladder. To determine the best strategy for retirement income and

minimize taxes over time, consider the size and account type of each source of funds to optimize your distribution strategy from a tax standpoint.

The key to developing a good retirement tax strategy is understanding how to order withdrawals from your various investment accounts. Knowing when and how to draw on your various assets can significantly impact the taxes you'll owe.

Start with your reliable income. This is the sum of all sources of retirement income. Reliable income may include Social Security, pensions, part-time employment and income from annuities in a given year. Your portfolio assets typically fund the difference between reliable income and your total income needs in retirement.

The Flooring Approach

This popular approach to income planning involves covering the cost of basic retirement living expenses with income from secure sources, creating a baseline (or floor) for income. Secure income sources include all the reliable income sources mentioned above. Any shortages could be supplemented by purchasing annuities, bond ladders, CDs and any other products that don't have direct exposure to the stock market. The primary objective is to reduce volatility for the portion of your portfolio responsible for funding your fixed expenses.

Withdraw Taxable Assets First

These assets can have a tax advantage. Investors must pay taxes on capital gains and dividends. Still, those rates tend to be lower than ordinary income tax rates for the average investor. With the help of your advisor, look for opportunities to take advantage of market fluctuations when deciding which assets to keep or sell to generate income for the year.

Withdraw Tax-Deferred Assets Second

These assets are taxed as ordinary income. Maximize the lower "tax buckets" as you move up the income ladder *(as explained above)* each year to keep your tax bill at an optimal level and reduce future required minimum distributions (RMDs), which begin at age 73 in 2024. Your account balance and life expectancy determine the amount you must take to satisfy your RMD.

Withdraw Roth Assets as Needed

Roth accounts are the best to preserve for you and your heirs. Income tax has already been paid on the core principal amount, so what you've contributed can be distributed tax-free at any time. Earnings on your Roth investments can also be tax-free to you as long as the assets have been held for at least five years and you are over age 59 1/2.

Finally, it's essential to have a cash reserve (emergency fund). Maintaining a stated level of cash holdings during retirement to fund short-term goal expenses will help reduce the impact of liquidating other assets during potential market downturns.

These are complex and variable issues to deal with. Your financial advisor can help plan and optimize your retirement income strategy and help you minimize taxes, increase financial security and extend the life of your assets.

Is That a Fiscal Cliff I See in 2026?

Perhaps you recall the term "fiscal cliff" from 2012? At that time there were several tax laws, spending cuts, debt ceiling limits and other issues that were scheduled to change dramatically—all at the same time—on January 1, 2013. In a last-minute effort, plummeting off the "cliff" was averted with Congress passing the American Taxpayers Relief Act of 2012 .[1]

Well, we have a similar cliff approaching on January 1, 2026, this time with a focus on taxes. The Tax Cuts and Jobs Act of 2017 ("TCJA"), which created the current tax rates and rules we have today, is scheduled to revert to previous tax laws on January 1, 2026—unless Congress acts otherwise. Should the laws revert, there will be notable changes to standard deductions, tax rates, deduction rules and estate exclusions, just to name a few.

Although it is difficult to predict if some or all of the tax provisions will fall off of the proverbial cliff, there are some planning opportunities you can take advantage of between now and then to be better prepared. Here are a few items to consider today in anticipation of the reversion taking place:

Standard Deductions Will Be Halved While Many Itemized Deductions Return

The TCJA doubled the standard deduction, limited state and local tax deductions, eliminated most other deductions, and eliminated the personal exemption. The return of the lower standard deduction, coupled with the availability of renewed itemized deductions, will greatly affect many taxpayers. Work with your tax advisor to determine if you should shift income or delay deductions in preparation of the tax law reversion.

Tax Rates Increase

Tax rates will generally increase for everyone should we tumble off the cliff. The "middle" bracket will increase from 24% to 28%, and the top tax bracket will increase from 37% to 39.6%. Accordingly, consider whether it may be more advantageous to accelerate income or defer deductions to address these tax increases. For example, Roth conversions may be more attractive over the next few years because income tax on the converted amounts would be taxable at the current lower tax rates, while future qualified withdrawals in retirement would be income tax free when tax rates could be higher.

[1] In spite of the Act being dated 2012, the Act actually passed by the House and the Senate on January 1, 2013, and President Obama signed the legislation into law on January 2, 2013, or as the running joke in tax corners became, December 33, 2012.

While Deductions Return, So Too May the AMT

Should tax law reversion occur, limitations on the state and local tax deductions depart as well. Deductions like those for personal casualty losses, or miscellaneous deductions subject to the 2% floor, for example, would return in 2026. However, the Alternative Minimum Tax (AMT) thresholds also revert to their 2017 lower numbers. The AMT was designed to make sure wealthy taxpayers paid their "fair share" of taxes, but the TCJA significantly reduced the number of taxpayers subject to AMT.

If the law changes as planned, individuals with high income, high deductions, stock options or with large capital gains may once again face the AMT. Review whether you can increase income or realize long-term capital gains now and whether such actions may lessen your tax burden. Moreover, controlling or decreasing your AGI going forward may help reduce the chance of facing the AMT in 2026 and beyond.

Estate and Gift Tax Exclusions are Reduced by Half

The current estate and gift tax exclusion is $13.61 million. This elevated estate and gift tax exclusion is also scheduled to be cut to about half of what it will be in 2025. For those who may face a potential estate tax now, or those that may face the tax should the exclusion be reduced in 2026, consider planning to utilize the large exclusions now. Techniques like accelerated gifting, spousal lifetime access trusts, or other wealth transfer strategies may be appropriate to reduce your total transfer tax liability.

While we do not know what Congress may do between now and 2026, we know that some change will occur. Either the laws will revert as written, or Congress will take some action to change this situation. Regardless, change is coming. Work with your financial advisor along with your tax professional to see if you should start taking steps now to prepare for the cliff we see quickly approaching.

Don't Miss Our Tax Tip Tuesdays Blog Series

Our Private Client Services Team will be posting a new tax tip every Tuesday until April 16, so be on the lookout for planning opportunities.

As it has been for the past few years, it's important to note that there are little substantive changes in the rules for tax year 2023. But while tax laws haven't changed much, there are some new provisions becoming effective for tax year 2024 that may require you to modify your planning going forward. Accordingly, our series will focus on issues to address for this year's tax season, but when applicable, items to consider for the 2024 tax year also will be addressed.

To find our Tax Tip Tuesdays series of blogs, go to

benjaminfedwards.com/educational-resources →

A new topic will be added to the list each week, and you can scroll back to catch up on any you may have missed. Also, remember, your financial advisor is happy to work with you and your tax advisor to make filing your taxes as painless as possible.

Happy Tax Season!

MARKET RECAP

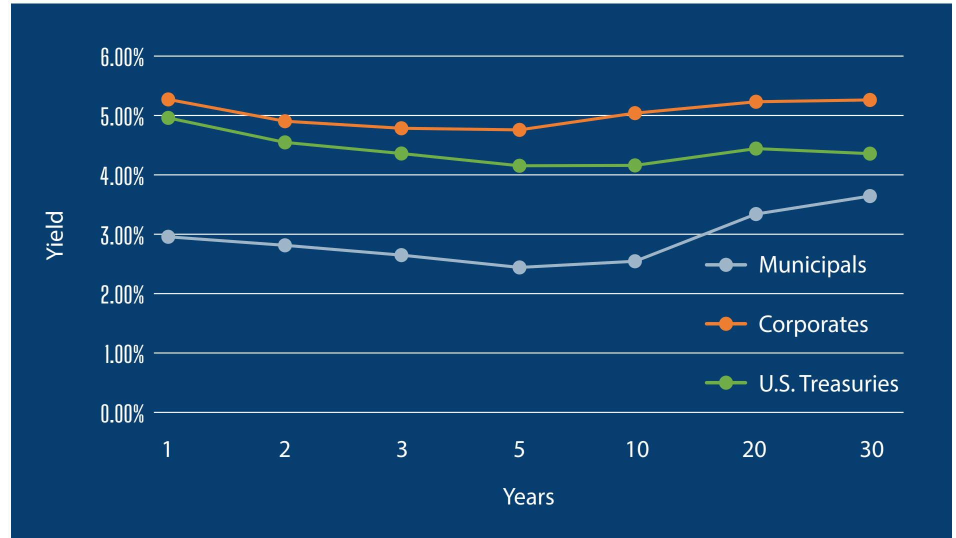
Market Summary

Fixed Income Market Commentary

The U.S. Treasury market remained largely unchanged from the prior quarter, primarily due to the Consumer Price Index and personal consumption expenditures inflation figures pausing the downward trend we had been witnessing for much of 2023. The Federal Open Market Committee (FOMC) has been consistent with its mantra of being data-dependent before starting the moderation of the federal funds rate. The market has adjusted expectations over the last quarter from expecting as many as six cuts to currently pricing in three to four cuts. The FOMC guidance has consistently looked toward two rate decreases by the end of the year.

Fixed Income Yield Curves

As of March 1, 2024



Source: Bloomberg BVAL AAA Curve, Bloomberg US Corporate (A) Fair Value Index, Bloomberg US Treasury Actives Curve

The corporate bond and municipal bond markets have enjoyed significant demand from investors after a couple of tough years for the product types. Investors have been allocating and locking in the higher yields in their portfolio, which is a compelling case given the low rate environment we lived through for the past 10 years. Corporate and municipal bonds are trading at tight credit spreads, signifying the strong demand in the market and the confidence in the U.S. Federal Reserve's ability to engineer a soft landing to a steady economy. This is evidenced by steady inflation and the strong labor market we have been observing.

Equity Market Commentary

- The S&P 500 Index was at an all-time high of nearly 5,100 at the end of February, while the S&P 600 small-cap index remained 11% below its record level.
- Over the past 12 months ending in February, the S&P 500 is up more than 30% with 10 of the 11 equity sectors seeing gains. Tech stocks were up nearly 60% while utilities were down just over a percent.
- The fourth-quarter earnings season finished better than expected with the S&P 500 seeing earnings per share up 4.1% year-over-year. 74% of companies reported earnings better than their consensus estimates.Revenues were also up around 4%, while just 64% of companies beat revenue estimates.
- International equities are positive for the year, but continue to lag the U.S. The MSCI World Ex-US index is up 14% over the last 12 months versus the aforementioned 30% gain for the S&P 500.
- Equity valuations appear stretched relative to consensus earnings expectations for the remainder of 2024. For this reason, we would expect stocks to move sideways with the potential for some volatility through the remainder of the year.

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Past performance is not a guarantee of future results.

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Diversification does not guarantee a profit or protect against loss.

Investing in securities entails certain risks, including the potential loss of all or a portion of the proceeds invested. Individuals should consider their specific financial needs, investment objectives and risk tolerance before making an investment.

Equity investments refer to buying stocks of U.S. companies as well as companies outside of the U.S. The market capitalization of U.S. companies is used to group large, medium (mid) and small companies. The investment return to the owner of stock (shareholder) is in the form of dividends and/or capital appreciation. Shareholders share in both the upside potential and the downside risk. Dividends are not guaranteed and are subject to change or elimination.

Mutual funds and ETFs are sold by prospectus. Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained from your financial advisor and should be read carefully before investing.

There are special risks associated with an investment in real estate, including credit risk, interest rate fluctuations and the impact of varied economic conditions. Distributions from REIT investments are taxed at the owner's tax bracket.

An investment in a 529 plan will fluctuate such that an investor's shares, when redeemed, may be worth more or less than the original investment. Investors should carefully consider a 529 plan's investment objectives, risks, charges and expenses before investing. This and other important information can be found in the 529 plan issuer's official statement, which should be read carefully before investing.

The return of principal for bond funds and funds with significant underlying bond holdings is not guaranteed. Fund shares are subject to the same interest rate, inflation and credit risks associated with the underlying bond holdings. Lower rated bonds are subject to greater fluctuations in value and risk of loss of income and principal than higher rated bonds.

Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline of the value in your investment.

An index is not managed and is unavailable for direct investment. The Dow Jones Industrial Average (DJIA) is an index that shows how 30 large, publicly owned companies based in the United States have traded during a standard trading session in the stock market. The Nasdaq Composite Index measures over 5,000 NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. The Russell 2000 is a stock-market index measuring the performance of 2000 small-capitalization stocks. The S&P 500 Index covers 500 industrial, utility, transportation and financial companies in the U.S. markets. S&P®, Standard & Poor's® and S&P 500® are registered trademarks of the Standard & Poor's Financial Services LLC.

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