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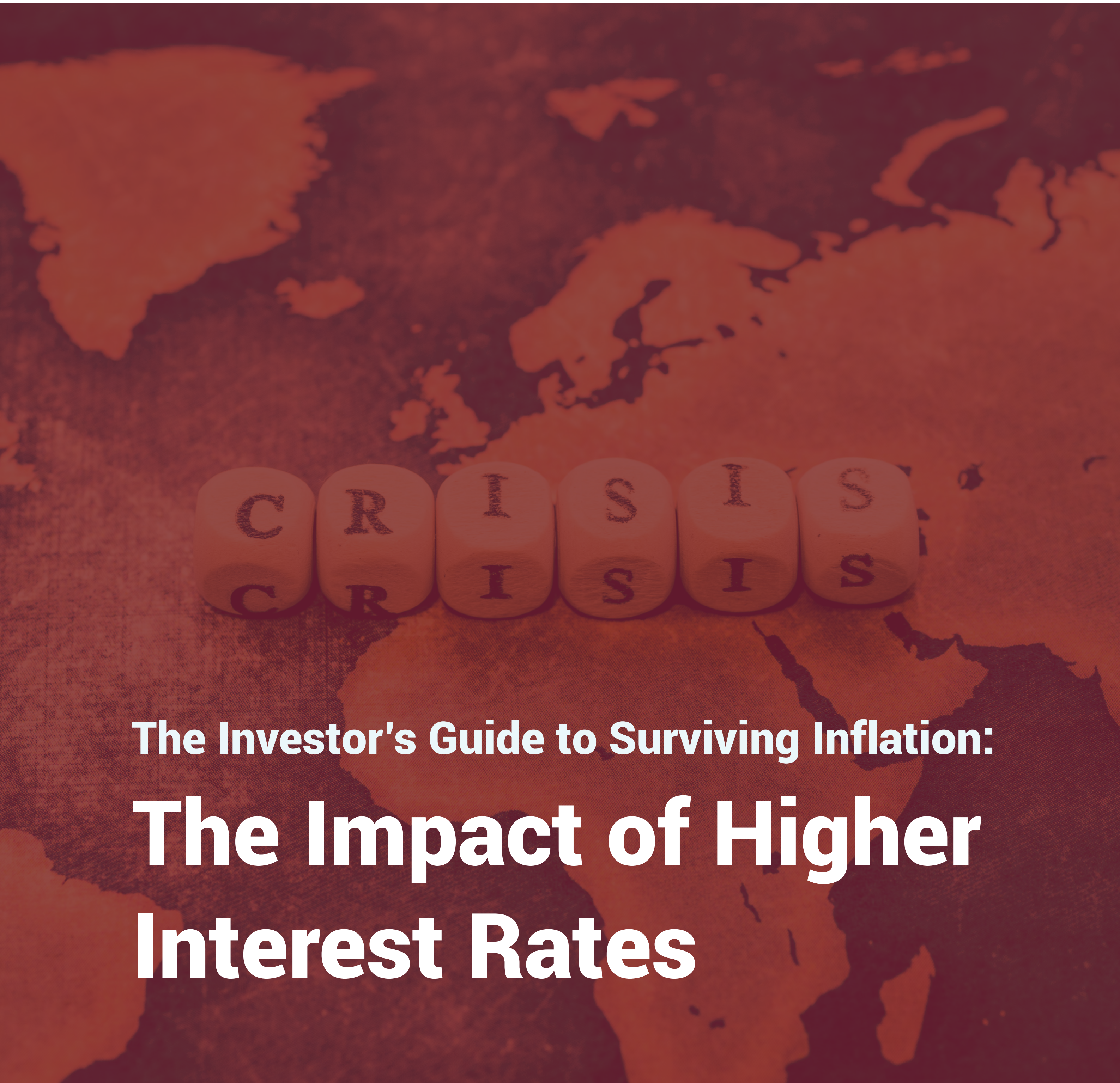


The Investor's Guide to Surviving Inflation:

The Impact of Higher Interest Rates

Introduction:

In our ever-changing state of affairs, crisis efforts are enacted to save us from what's sure to follow. This is why financial advisors are considered "we the people's" most trusted source for guidance.

As substantial inflation continues to blanket the nation and war breaks out in Ukraine, a survival guide can help investors navigate high-interest rates and thick global tension. Just as civilians worry about war, they fear losing investments due to inflation caused by worldwide conflict, pandemics, and natural disasters.

A plethora of headwinds can cause a foggy economic outlook. Questions that investors often ask themselves during volatile times include:

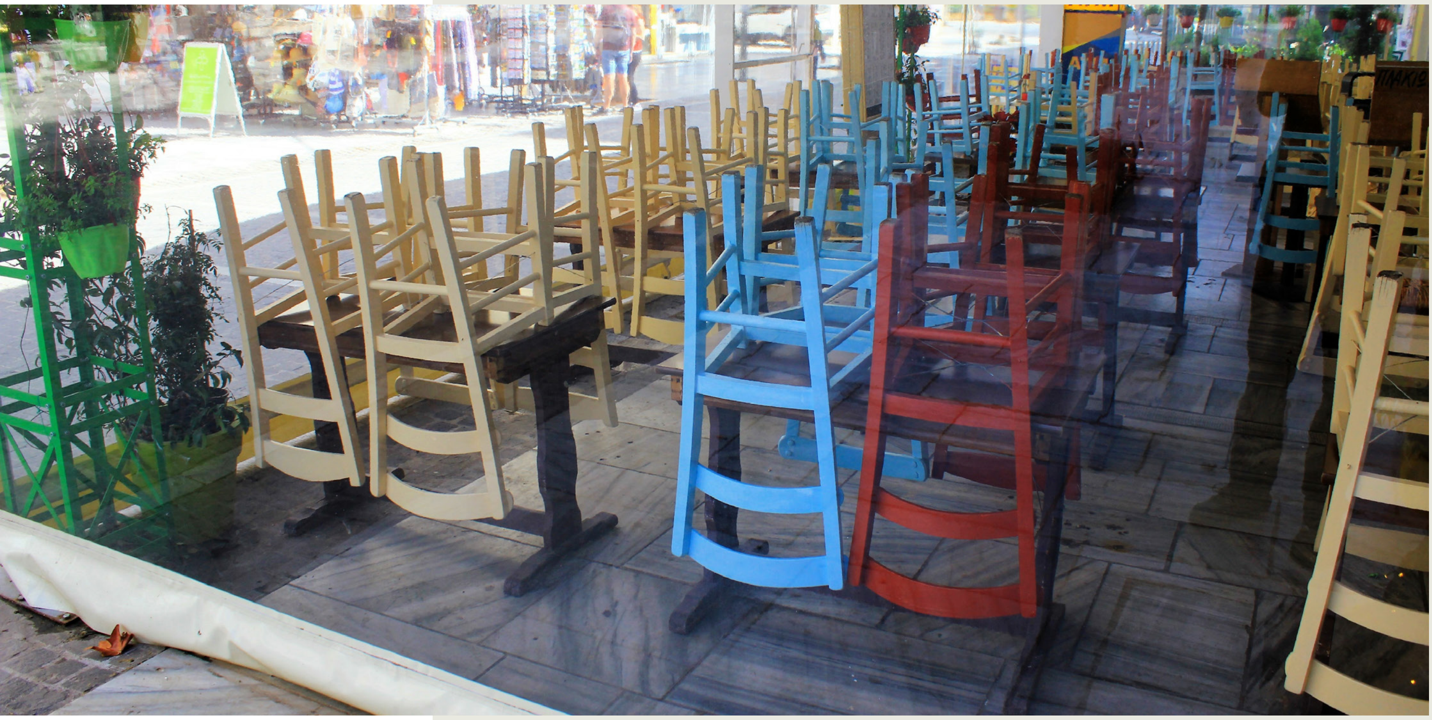
- Will stocks maintain their strong performance?
- Should I be in the market, expecting a move higher?
- Should I move to the sidelines, getting out ahead of the crash?
- Should I rotate from growth to value stocks or vice versa?

Don't throw caution to the wind with investment decisions. Taking mindful preparation steps to equip your portfolio for uncertain events is part of the financial planning process. A study shows the number of Americans working with a financial advisor pre-pandemic was around 29%. A significant jump shows nearly four in ten (38%) are currently benefiting from financial advice.

Their top financial planning priorities over the next year were identified:

- Paying bills/expenses – 48%
- Saving for retirement – 39%
- Paying off debt/loans – 38%
- Taking care of family – 37%
- Investing – 32%

How do your financial priorities fair in comparison?



What is inflation and how did we get here?

Inflation can reduce the value of your savings over time because prices typically increase in the future. This is most apparent with cash. If you're "safekeeping" $20K in an emergency fund at home, that money may not be capable of buying as much a decade from now.

As a macroeconomic reference, inflation (the rate at which prices for goods and services rise) and interest rates (the amount charged by a lender to a borrower) are also linked. When inflation reaches a boiling point, the Federal Reserve System (the central bank of the U.S.) typically raises interest rates to slow the economy and cool inflation.

As seen throughout and in recent economic history, attempts to influence the rate of inflation takes time. This "money supply tool," if you will – influences target employment rates, stable prices, and stable economic growth.

Pandemic

To fight the war against Covid-19, the government enacted heavy restrictions that altered consumer behavior. Not only did human health take a blow – lockdowns, social distancing, mask, and vaccine mandates highly impacted American households and workforces.

The recent pandemic, resulting in market volatility and economic downturn, was a significant factor influencing individuals to seek financial guidance. This trend was most prevalent among younger generations

- 23% of Gen Z
- 23% of Millennials

As younger families take financial action, more business owners, retirees, and professionals are also taking the crucial step towards creating positive financial planning habits to achieve financial security. The pandemic has prompted investors from all backgrounds to revisit their financial plans and seek help.

Job Loss

High inflation is a threat to the achievement of maximum employment. And when the number of Americans looking for work is greater than the number of jobs available, unemployment is ruling the nation. That's why the need to control inflation before it becomes unshakeable is necessary to keep the economy progressing.

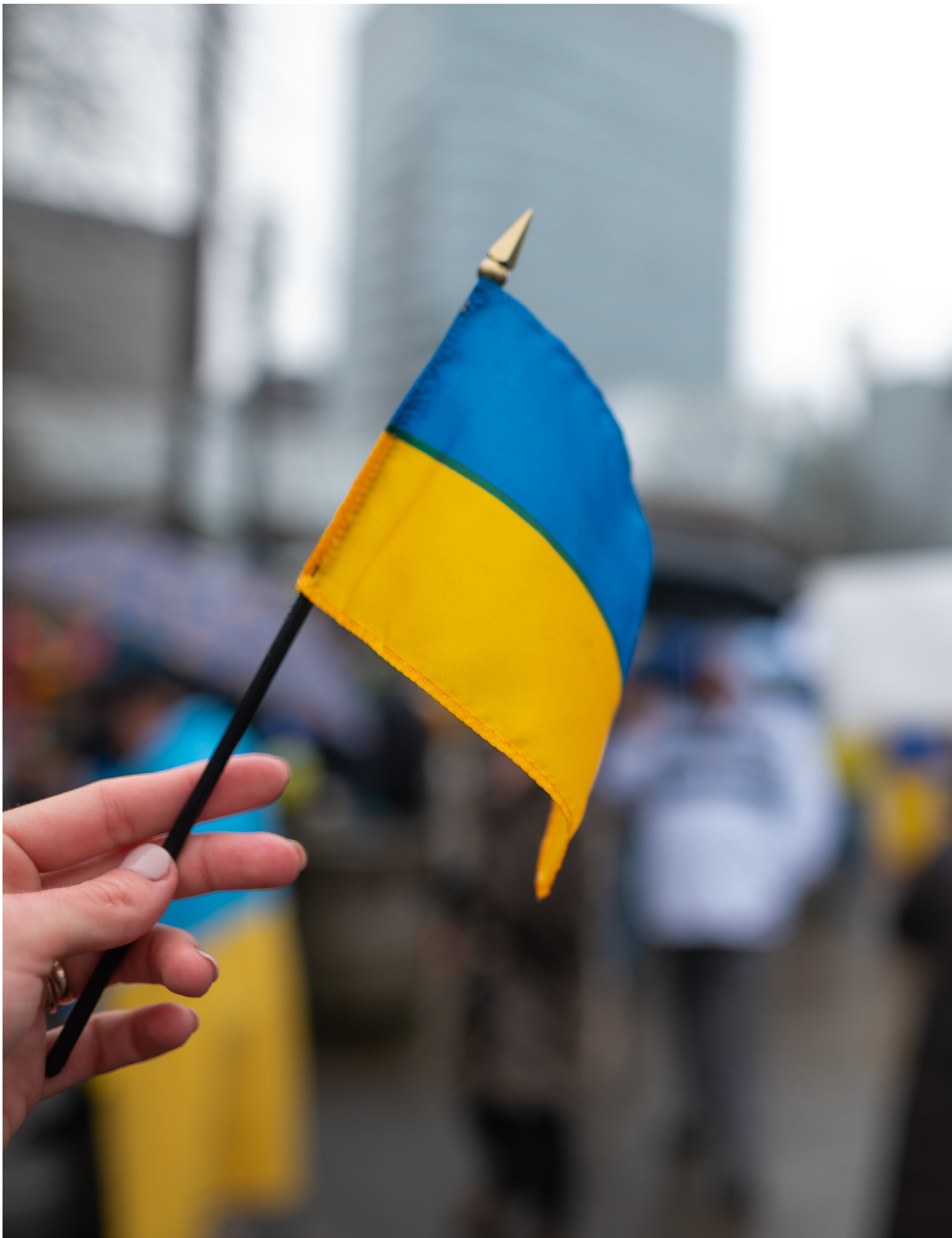
Tens of millions of people lost jobs in the early months of the recent crisis. While employment began to rebound within just a few months, unemployment remained high in 2020. By the end of 2021: ten million households were behind on rent, and 20 million households reported having too little to eat in the past week.

In early 2022, just less than three million were employed than before the pandemic. As recently seen, millions of Americans end up retiring early or avoid jobs because of pandemic-related fears.

The Phillips Curve presents compelling evidence of the inverse relationship between wage inflation and unemployment. No matter the cause - the number of people employed or searching for work is a heavy inflation impact.

Global Tensions:

One of inflation's most significant risks points to geopolitical unrest. A key component in rising inflation is the ongoing turmoil in the global supply chain. Investors make moves when global leaders are butting heads, posing threats, or declaring war, as it naturally prompts fears of rising inflation and high bond yields.



Cost of Living

With citizens' checking accounts squeezed by higher costs for gas, food, rent, vehicles, and basic home upkeep, the Fed is pressured to rein in inflation by raising rates to slow borrowing and spending. This is a typical response to tame inflation. When the economy has recovered enough, the Fed's ultra-low-interest rate policies are no longer needed.

Decline in Purchasing Power

As inflation soars, supply chain problems present financial problems for consumers and investors. Inflation reduces the value of any currency's purchasing power, affecting an increase in prices. Therefore, your hard-earned American dollar is not worth what it was previously.

To measure purchasing power, you can compare the price of a good or service against a price index like the Consumer Price Index (CPI). Because inflation tends to erode a currency's purchasing power over time, central banks try to keep prices stable by maintaining the currency's purchasing power by setting mechanisms such as interest rates.

Price of Gas:

Since the early pandemic lows, the oil demand has poured, and production has not kept up. With world crisis events such as Russia invading Ukraine, gas prices grow wildly erratic. Russia is one of the world's largest producers of oil and natural gas, accounting for 17% of its natural gas and 12% of its oil. Some Wall Street analysts are eyeing the possibility of oil hitting as high as $100 – $150 per barrel.

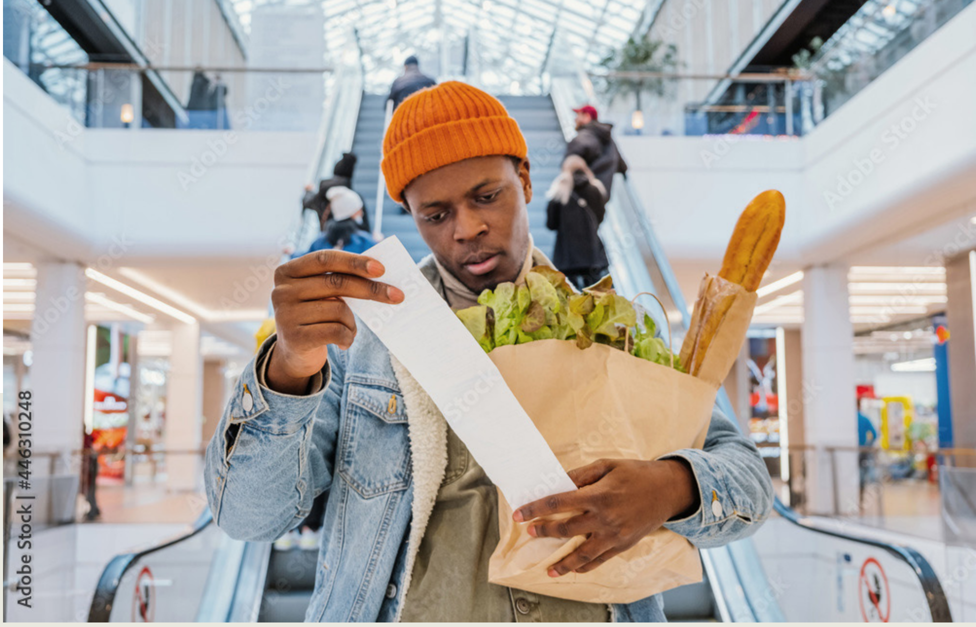
Let's take a quick glimpse at Brent crude prices per barrel:

- 2020 = averaged less than $42 (extraordinarily low)
- 2021 = averaged just under $71
- February of 2022 = trading in the low $90s
- Even if tensions in Ukraine de-escalate as a "best-case scenario," oil probably would not fall below $84

As you can see, a combination of factors, including the coronavirus pandemic response, created this extreme volatility. Because gas/oil is a significant input on global and national levels – used in almost every household and industry, it is linked to inflation. High gas prices are primarily due to high crude oil prices:

- Oil costs account for 43% of the price of regular gasoline
- 57% comes from distribution and marketing, refining, and taxes

If input costs rise, so should the cost of end products. There appears to be a greater link between oil and the Producer Price Index (PPI), which measures the price of goods at the wholesale level.



Grocery Shopping:

Significantly reduces a large portion of Americans' disposable income during inflammatory conditions. Since the beginning of the recent pandemic, food and supply prices rocketed – when it was hard to find necessities like bottled water and toilet paper. Rationing was in order to supply the demand fairly.

Almost two years later, "U.S. households were spending more than 12% of their disposable income on food purchases, according to data from the Bureau of Economic Analysis. That's up from 10.8% at the end of 2020 — and it marked the highest share of food spending in more than two decades."

Compared to a year prior, as of January 2022

- Cost of beef/veal up 16%
- Pork up 14.1%
- Eggs up 13.1%
- Fish/seafood up 12.7%
- Chicken up 10.3%

Basic staples such as cooking oils and flour are up by double-digits year-over-year. Overall, according to the latest Consumer Price Index, inflation reached a four-decade high of 7.5% in January.

Cars and Building Materials:

Car dealer lots are half full – and the remaining sales staff call upon owners asking to buy their vehicles at higher prices. Why? Because they need inventory. After 2020, automakers found themselves unable to meet demand because of semiconductor chip shortages and supply chain problems. Prices for both new and used cars rocketed.

Overall, consumer inflation soared 7% in 2021, the biggest increase in nearly 40 years. Used car and truck prices shot up 37% last year. The average used vehicle is now costing around $29,000.

Building materials such as lumber, steel, and aluminum also skyrocket during inflationary times. Contractors can get in line for needed materials to support their businesses. The Associated General Contractors of America reports that the overall pricing of construction materials jumped nearly 20% in 2021. The Producer Price Index for steel mill products rose 0.2 % in December and 127.2% over the last 12 months.

Student Loans:

Will be unpaused; borrowers will face surmounting pressure come spring when a federal moratorium on their debt payments expires. Tens of millions of students/ graduates are bracing to resume student loan payments since March of 2020.

Rising Interest Rates

How do interests rates work? When interest rates rise more than 2% to 3% a year, the Federal Reserve will raise the funds rate to control the rising prices. Higher interest rates create higher borrowing costs. The result: people will eventually spend less.

Will interest rates rise in 2022? According to a research report from the bank, the Fed is expected to raise interest rates six times in 2022 for a total of 150 basis points – faster than previously predicted. After hotter inflation data pressured the Fed to combat soaring prices, major investment banks anticipate an increasingly strong run of interest rate hikes for 2022.

The Fed is likely to hike rates by 25 basis points by the end of the March policy meeting, 25 basis point hikes in May, June, July, September, and December.

Impact of interest rate hikes on investments: Rising interest rates result in lower stock prices. That's because people commonly pull out of the market when times are uncertain. Finding a better return usually becomes the hunt. Certain stock market sectors do outperform others as interest rates rise. This is where it pays to have financial advisor guidance.

Interest rate hikes cause the price of existing bonds to fall immediately since the prices are inversely related. They are equivalent in face value. Newer bond offerings have higher coupon rates (ratio between interest the bond pays and its price), resulting in higher payments to reflect the rate rise. Current bonds will fall in price so that their coupon rate aligns with newer bonds.

Fed tightening can impact investors whose portfolios are more exposed to bonds, like those nearing retirement. Speak with your financial advisor to map out the best way to navigate the risks posed by rising interest rates.

Inflation-Proof Investing

Assets that have historically done well during periods of high inflation include:

- Commodities: includes grain, precious metals, electricity, oil, beef,
- orange juice, and natural gas, as well as foreign currencies, emissions, and specific other financial instruments
- A 60/40 stock/bond portfolio: traditional mix of stocks and bonds in a conservative portfolio
- S&P 500: high concentration of technology businesses and
- communication services (accounting for a 35% stake in the Index)
- Real estate income: earned from renting out property
- The Bloomberg Aggregate Bond Index: government, corporate, taxable, and municipal bonds
- Treasury inflation-protected securities (TIPS) type of U.S. Treasury bond: indexed to inflation to explicitly protect investors from inflation (TIPS payout at a fixed rate twice annually)

Discovering the Best Investments for Inflation for YOU will be better accomplished with a financial advisor.

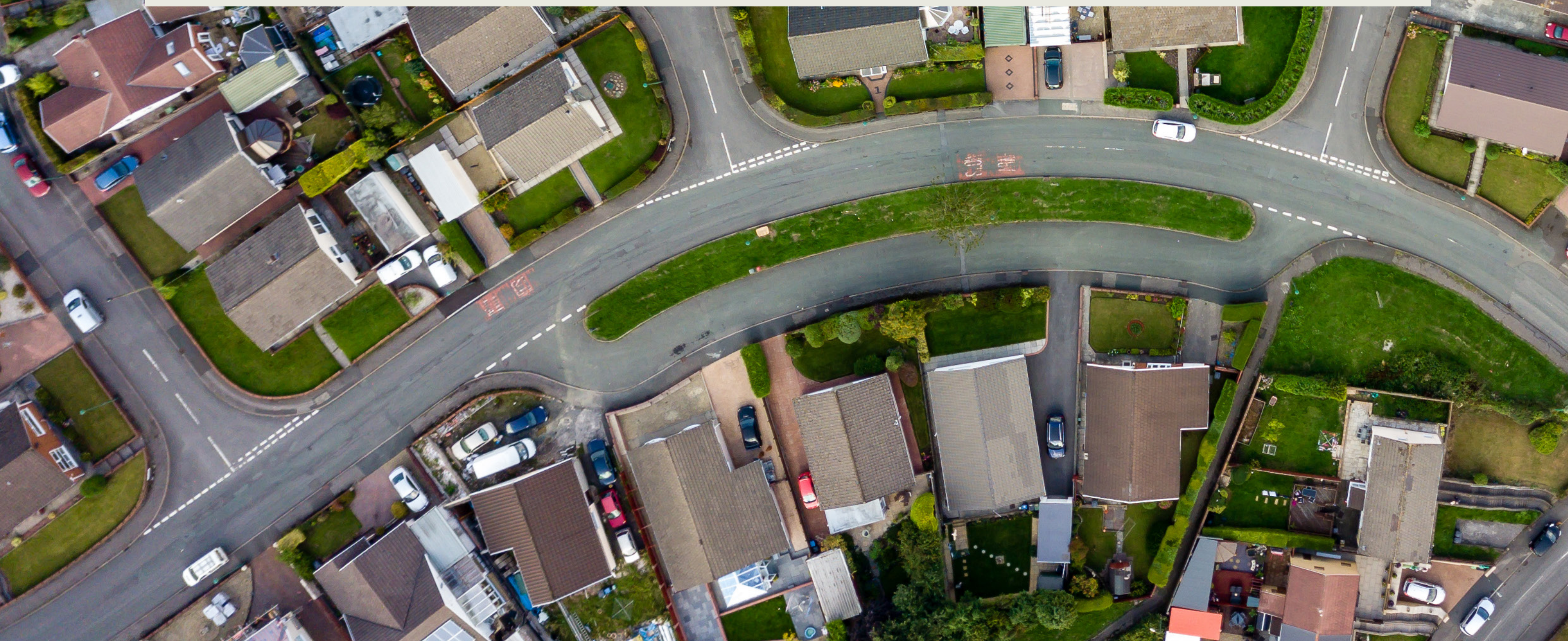
Stocks: One of the hedges against inflation is an asset class in which you're likely well-versed. Stocks have consistently provided returns above the pace of inflation for several decades now and remain one of the best sources of purchasing power protection for capital. Consider sectors where demand is inelastic despite rising prices, like consumer staples or large retailers.

Real Estate

A common inflation defense is owning a home with a fixed-rate mortgage. Since your obligation remains the same despite purchasing power loss, this secure mortgage is a good debt to have during times of high inflation. A fixed interest rate is a life-saver in this case.

Owning a tangible asset will increase in value over time. Homeownership as part of the American dream provides safety, security, and peace – especially during high inflationary periods; there's no place like an affordable home.

Real estate is a popular choice for investors because it can create value amid inflation while generating increased rental income. Investors can purchase real estate directly or invest in it through shares in a specialized fund.



Retirement Investments

Are you solely dependent on one form of retirement savings? It helps to craft a retirement plan that plans for inflation, as it will continue to erode the purchasing power of your retirement nest egg. The cost of food, transportation, and healthcare will cost more than they do today – so plan for it. The same is to be said for enjoying retirement when it comes. The cost of your future plans will require more savings or investments that can afford you more.

Social Security Cost-of-living adjustments (COLA): As a significant source of income for most retirees, there is something to know about the annual cost-of-living adjustment. Although COLA was designed to improve the ability of Social Security benefits to keep up with inflation, it lacks in calculation.

This is mainly due to underweighing sectors such as healthcare, which have had price increases much greater than the overall inflation rate. Because healthcare is a cost that supports our longevity, retirees might find out that the Social Security COLA does not keep up with inflation well.

Limiting Contributions on Retirement Plans: Remember, the Internal Revenue Service (IRS) limits contributions to a traditional IRA, Roth IRA, 401(k), and other retirement savings plans. Why are they capped? Limits vary by plan but are commonly capped so that high-income earners will not benefit more than the average worker.

Business Impacts

The painful impact of rising prices on all businesses is a "particularly ironic" punishment for bad businesses. Warren Buffett compares this to a realistic daydream: "Inflation takes us through the looking glass into the upside-down world of Alice in Wonderland." A bad business "must retain every nickel that it can."

The less prosperous the company, the more significant the proportion of available sustenance claimed by inflation. Asset-heavy businesses with meager returns on equity have no leftovers to spend on growing, paying down debt, issuing dividends, or making acquisitions. Spending cash in those areas could mean sacrificing long-term competitive position, sales volumes, or financial strength.

The kinds of businesses that weather inflation best are those with valuable intangible assets and little need for tangible assets. Companies can handle rising prices by hiking prices without sacrificing material market share or unit volumes and adjusting to significant dollar-volume increases in business without investing much additional capital.

On the Bright Side

Relief in wage increases: Inflation is cited as the main reason that U.S. businesses plan to raise wages by an average of 3.9% this year and offer higher pay for new hires. (From a report by the Conference Board)

Inflation can reduce the value of debt if your earnings keep up with inflation. It's entirely possible to have inflation with no increase in income, and if this is the case, it is more challenging to pay off your debt. Spending more on goods for day-to-day living leaves less disposable income to pay your debt.

Quality of life and priorities: As Covid certainly created extra space to rethink what's most important, many people from various backgrounds decided to hire a professional advisor to reprioritize life and invest smarter. Because most people don't plan and forecast dreaded events, seeking this support is helpful before it demands attention.

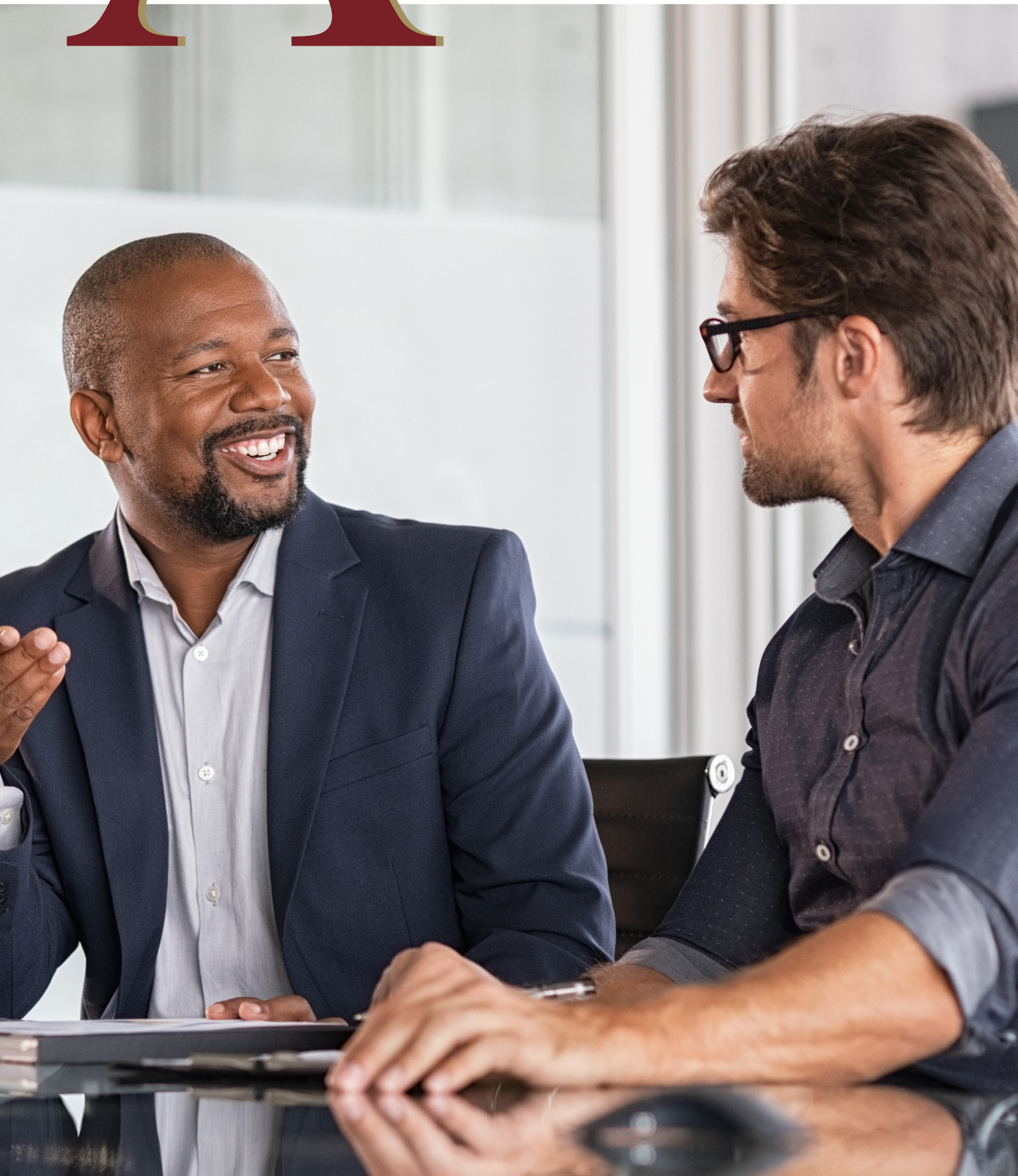
Homeowners benefit: As mentioned, being a homeowner can guarantee your monthly living expense with a fixed mortgage. And, an inflation hedge strategy is to invest in real estate, especially when mortgage rates are low. Plus, if you decide to rent out your property for a season, you have the option to make extra income.

Investing: Where there is money to be made: this effort could use the guidance of a trusted professional financial planner. Inflation is not a curse for the country; smart investors know what asset classes can benefit them, especially during or following a crisis.

The Takeaway

With today's volatile stock market and changing tax laws, more people seek a second opinion to make sure they are on track to achieving financial goals. Consider where you stand and what financial support you need to get ahead – even in the thick of inflation.

As some preemptive financial advice, don't follow the herd and make fear-based moves. A dedicated professional can be your best ally. If you're not confident in picking investments, consider some guidance based on your risk tolerance and return objectives to help you build a diversified portfolio to match your needs.



Prepare your portfolio for anything knowing that volatility is part of the game. An informed investor welcomes volatility, and an erratic market means that low prices will periodically be attached to solid businesses.

Focus on quality and value; invest in promising companies when they're available on the cheap. Create a watchlist of stable companies with reputable brands that you can run by your financial advisor in Phoenix, Flagstaff, or Mesa.

You don't have to be a billionaire to make these strategies work for you, but they can increase your wealth while saving you the most valuable assets – time and peace of mind. Plan for crisis ahead of time and ask for help to navigate the global turmoil. Your financial health does not have to waiver with change – instead, you can use it to your advantage.

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