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FINANCIAL OUTLOOK

WINTER 2023

BONDS FOR EVERY STAGE OF LIFE

Many think bonds are for the very conservative investor. In actuality, bonds are an important component to a well-balanced portfolio throughout every stage of an investor's life.

They can provide stability during volatile markets, provide an income stream, help with tax liability, and provide higher rates of return for capital growth. Regardless of your life stage, you should consider having bonds in your investment portfolio.

AT THE BEGINNING

As a beginning investor in your 20s or 30s, you have a long time to maximize capital and you are probably in the best position to assume risks for larger returns. Even at this early stage of investing, you should develop a portfolio that also balances risk and market volatility. While higher-yield investments are important, you will still want to balance them with some lower-risk investments, including bonds. At this stage, you can:

- **GROW CAPITAL** with bonds that offer higher yields if you assume higher risk. Although higher-risk bond investments have potential for loss because of interest rate and credit risk, they are typically still a safer investment than equities. You should make sure you understand the terms and conditions, including the bond's rating, call features, and if it is insured.
- **PROTECT YOUR SAVINGS** for a large purchase, such as a car, a wedding, or a house. Lower-risk bonds can be a better investment than a traditional savings account to save for large purchases. Bonds will pay a higher interest rate and offer a safe way to protect your savings. You may want to consider Treasury or corporate bonds with maturity dates that align with the time frame in which you will need the money to ensure that you don't encounter a loss in investment value.
- **DIVERSIFY YOUR EMPLOYER-SPONSORED RETIREMENT PLAN,** such as a 401(k) plan. Your plan most likely offers a variety of mutual funds, and bond funds are a good way to diversify your

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CHALLENGES TO RETIREMENT

We all know saving for retirement is becoming more and more challenging. Longer life expectancies, fewer traditional pensions, and lower investment portfolios are the most obvious challenges. But there are other threats to your retirement:

- **EVEN IF YOU HAVE A TRADITIONAL PENSION PLAN, THOSE BENEFITS CAN CHANGE.** Your employer can't take away benefits you've already earned, but benefits going forward can be reduced.
- **SWITCHING JOBS CAN AFFECT YOUR RETIREMENT BENEFITS.** If you have a traditional pension plan, don't change jobs without considering your pension benefits. The same applies to 401(k) plans with matching employer contributions.
- **DON'T FORGET ABOUT PENSION BENEFITS AT PREVIOUS EMPLOYERS.** Many employees leave a company without realizing they are entitled to pension benefits. Before changing jobs, check with your employer to find out what benefits you are entitled to.

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Bonds

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portfolio and spread your risk within your plan. The stock and bond markets do not typically move in the same direction, so bonds can stabilize and help with your overall returns.

In the Middle

Your mid-30s to late 40s should be a time of accumulating wealth and investing for retirement and other long-term goals. At this point in your life, you should rebalance your portfolio on a regular basis to ensure your allocation is keeping pace with your goals and is still appropriate for those goals.

Many experts agree that at this point you should consider more medium-risk investments in combination with your higher-risk investments.

Bonds should become a larger portion of your asset allocation than when you were younger, because they will offer more predictable income and continue to balance higher-risk equities.

Following are some bonds to consider at this stage in your investment life:

- **Tax-advantaged bond investing** is a good way to help offset taxes if you're in a higher tax bracket. Municipal bonds, which are issued by state and local governments, are an attractive investment in your income-earning years because they are exempt from federal income taxes. And, if you live in the same state as the issuer, they are free from state and local taxes as well. In most cases, you should not include this type of investment in a tax-deferred retirement or college savings account because you would be wasting the tax exemption feature.
- **Zero-coupon bonds can be a good cost-effective investment for specific goals,** such as paying for college or investments for retirement. They are sold at a steep discount from their face value, and when they mature, the face value will include both the principal and the accumulated interest earned. These bonds also work well in a tax-deferred account because the interest is taxable when it is credited to the bond, but you can't spend it until it matures.

Approaching Retirement

Now that you're getting closer to retirement, you will want to take fewer chances of losing a large portion of your portfolio.

Many experts recommend that at this point you should begin increasing the bond portion of your portfolio to 50% or more to lower your risk.

Some issues to consider when evaluating bonds for your portfolio:

- **Managing interest rate risk** is important because when interest rates rise, bond prices fall, and vice versa. One way to manage this risk is with a bond ladder. This strategy allows you to invest in a portfolio of bonds with different maturity time frames to help your investments do well in any interest rate environment. When rates rise, you will have short-term bonds that mature so you can then invest the principal at higher rates. And when rates fall, you will have the longer-term bonds paying higher returns.
- **Tax-advantaged bond investing** will continue to be a good way to manage income taxes, especially if you're in a higher tax bracket. Again, municipal bonds can be a good investment because they are exempt from federal income taxes, and, if you live in the same state or city as the issuer, they are free from state and local taxes as well.

In Retirement

Now your main goal becomes protecting and maximizing your income for the remainder of your life.

Social Security will most likely only replace a portion of your income during retirement, so your portfolio and retirement benefits will need to make up the rest.

Bonds can be a valuable portion of your retirement portfolio, since they will help you generate retirement income while preserving your principal.

Things to consider:

- **Guarding against inflation** because you are now living on a fixed income. Treasury Inflation Protection Securities (TIPS) or Treasury Inflation Indexed Securities will help you guard against inflation. TIPS have a fixed coupon rate, but their principal amount is adjusted every six months according to changes in the Consumer Price Index. When TIPS mature, you will get the higher of the original face value or the inflation-adjusted amount. You may also want to keep a small portion of your portfolio in stock for growth potential.
- **Spend from taxable accounts first.** When you take money from tax-deferred accounts, you will pay income tax on your distributions. By spending the tax-deferred accounts last, your portfolio will continue growing tax deferred while you are in retirement. In the long term, this can save a significant amount of taxes.

Please call if you'd like to discuss bonds and their role in your investment portfolio in more detail. ❍❍❍

Retirement

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- **Early retirement can significantly reduce your retirement benefits.** Don't just look at how much you'll receive when you retire early. Also consider what you would receive if you wait until normal retirement age. Retiring early can dramatically lower your monthly pension benefit for several reasons — you don't have as many years of service, salary increases you would have earned aren't considered, and those extra years of benefits cause a large actuarial deduction in benefit calculations.
- **You may not be able to count on health insurance benefits after retirement.** Due to rapidly increasing costs for health insurance, many companies are either phasing out health insurance benefits for retirees or increasing retirees' share of the cost. While Medicare is still available once you turn age 65, those benefits don't cover all medical costs.
- **Social Security benefits are changing.** Normal retirement age is gradually increasing from age 65 to age 67, a change affecting anyone born in 1938 or later. You can still receive reduced benefits at age 62, but the permanent reduction in benefits is increasing from 20% to 30%, depending on your year of birth. These changes are meant to encourage you to retire at a later date.
- **Decide carefully before taking a lump-sum distribution.** Some traditional pension plans allow lump-sum distributions instead of monthly pension benefits. Use that option with care. While the amount of money might seem large, are you sure you can invest it and earn more than the monthly pension option?

There are many challenges to saving for retirement. If you'd like to discuss your retirement plans in more detail, please call. ❍❍❍

How Inflation Affects Bonds

Inflation has a direct impact on all of us in some way. For investors, the degree of impact varies depending on their asset allocation. For example, the effects of inflation on stocks are sometimes deemed negligible, since stock prices often rise in correlation with the price of goods and services. Inflation's effects on bonds, on the other hand, are more tangible.

When you purchase bonds, you're essentially lending money to either the government or a corporation, with a promissory note in the form of a stipulated interest rate (coupon) and the maturity date when your principal will be returned. Because any given bond transaction occurs in today's dollars, there's always the likelihood that the principal you lend through purchasing bonds simply won't hold the same purchasing power by the bond's maturity date, particularly since many bonds have a 5-10 year life span, therefore increasing the probability of inflation. The relationship between inflation and bonds is an inverted one: the higher inflation rises, the less valuable bonds become. In fairness, this phenomenon is true of any type of fixed-income investment, which is why it's important that the interest offered within the specified investment window outweighs the costs of inflation.

When we consider a bond's cash flow from purchase to maturity, the effects of inflation become a bit more complicated, particularly because over the course of a bond's lifetime, its coupon and the current interest rates don't always align. While this can certainly work to your favor when interest rates are low, it can be problematic during times of inflation, when the Fed typically raises the interest rates in an attempt to slow inflation's pace. Remember: most bonds are similar to stocks in the sense that's they're traded on the market. Even the slightest rise in interest rates affects their market price because they must now be traded at a discount lower than their face value. Therefore, in spite of the par value you've paid for a bond, it might sell for less or more than that value, depending on market interest rates. Bonds with a coupon lower than the current interest rate must sell at a discount to offset the interest rate hike.

If you own individual bonds, assuming you hold them to maturity, their par value is generally secure, less the call or default risk. Likewise, your bond's interest payments will continue at the originally promised rate. Sell prior to maturity, however, and you'll incur the loss in face value. For this reason, many individual bondholders avoid selling.

Much of the impact of inflation on your individual bonds, too, depends on the term and even type of bond. Short-term bonds hold less risk when it comes to inflation for a few key reasons: a) there's less chance of inflation within a shorter investment period; b) the rate at which inflation occurs is likely to be less; and c) there's a greater chance you'll hold the bond to maturity. This comes at a price of course, since short-term bond coupons are typically much less attractive than those of long-term bonds. Your bonds' exposure to inflation also depends on the category of bonds you invest in. TIPS, for example, are designed to rise in value with inflation.

Any fluctuation in the economy, regardless of the direction, can affect bonds and stocks alike, albeit in different ways. To discuss the relationship between your investment plans and changing interest rates, please call. ❍❍❍

FINANCIAL DATA

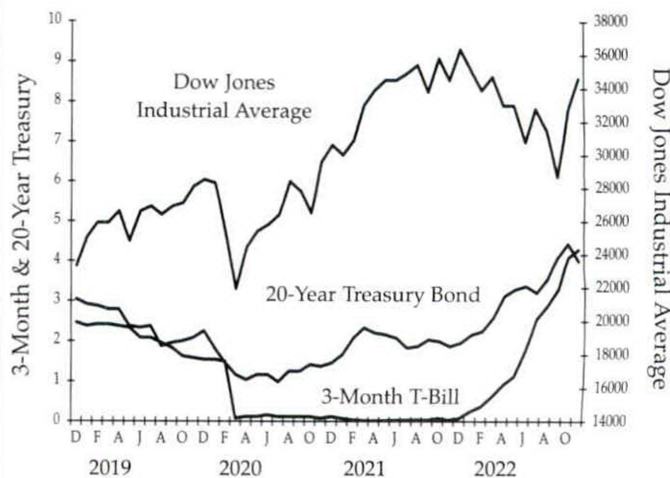
Indicator	Sep-22	Oct-22	Nov-22	Dec-21	Nov-21
	Month-end				
Prime rate	6.25	6.25	7.00	3.25	3.25
Money market rate	0.20	0.24	0.31	0.07	0.07
3-month T-bill yield	3.27	4.07	4.29	0.08	0.05
10-year T-bond yield	3.83	4.10	3.68	1.52	1.43
20-year T-bond yield	4.08	4.44	4.00	1.94	1.85
Dow Jones Corp.	5.76	5.93	5.46	2.48	2.54
30-year fixed mortgage	6.92	7.16	6.84	2.63	2.64
GDP (adj. annual rate)#	-1.60	-0.60	+2.90	+6.90	+2.30

Indicator	Sep-22	Oct-22	Nov-22	YTD	12 Mon
	Month-end			% Change	
Dow Jones Industrials	28725.51	32732.95	34589.77	-4.8%	0.3%
Standard & Poor's 500	3585.62	3871.98	4080.11	-14.4%	-10.7%
Nasdaq Composite	10575.62	10988.15	11468.00	-26.7%	-26.2%
Gold	1671.75	1639.00	1753.50	-2.9%	-2.8%
Consumer price index@	296.17	296.81	298.01	7.2%	7.7%
Unemployment rate@	3.70	3.50	3.70	-11.9%	-19.6%

— 1st, 2nd, 3rd quarter @ — Aug, Sep, Oct Sources: *Barron's, Wall Street Journal*

4-YEAR SUMMARY OF DOW JONES INDUSTRIAL AVERAGE, 3-MONTH T-BILL & 20-YEAR TREASURY BOND YIELD

DECEMBER 2018 TO NOVEMBER 2022



It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

FROM THE DESK OF: TOBIN HOM

ALLOCATING YOUR BOND INVESTMENTS

How you allocate your investments depends on considerations such as what you're saving for, how much you've accumulated in your portfolio, how much more you plan to invest, how long before you plan to make withdrawals, how much you need to withdraw, and your tolerance for risk.

What you are saving for is one of the most important considerations. If you're 35 years old and saving for retirement, your bond allocation will be very different than if you're 55 years old. If you're saving for your daughter's wedding and she's already engaged, your allocation will be very different than if you're saving for your 5-year-old's college education. For very near-term expenditures, short-term bonds or cash equivalents are typically your best alternative.

One of the most significant risks long-term investors face is that their investment portfolio won't keep pace with inflation. Before even considering withdrawals, you need a rate of return at least equal to inflation for your funds to maintain their value in real terms over time. If you expect your portfolio to grow in value in real terms, you need returns that are higher than inflation.

THE RISK/RETURN TRADEOFF

Stocks are inherently riskier than bonds, but they also offer the potential for greater returns. If you can keep your money invested for the long term, then you can ride out market fluctuations, like stock market ups and downs. But when it comes time to withdraw money for items like a new house, your child's college education, your daughter's wedding, or for annual retirement expenses, you may want investments that are less risky.

Please call if you'd like help determining what mix of each asset class makes sense for your investment goals. ❍❍❍

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As a Financial Advisor of Raymond James & Associates, I am not qualified to render advice on tax or legal matters. As federal and state tax rules are subject to frequent changes, you should consult with a qualified tax advisor prior to making any investment decision.