July – August 2023

Money Moxie®

The World Currency Leader

Part 2

SMEDLEY FINANCIAL SERVICES, INC.®

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The Future of Retirement

The world's population is getting old, really old. In the United States, about 10,000 people turn 65 each day. Americans of retirement age will outnumber people 18 and younger by 2035. This has never happened in U.S. history, and it is a phenomenon happening worldwide. This is both astounding and concerning for many reasons.

Historically, when an individual reaches retirement age, 65 to 67, they say goodbye to a long career and move on to enjoy their senior years. This trend is changing. For Americans, reaching retirement age is no longer as pivotal as it once was, and they may continue to work for many years.

Medical breakthroughs have helped seniors to live longer, more active lives. Some seniors enjoy the mental and social benefits they get while remaining engaged. As we have said ad nauseam, people need something to retire to. After working for 30 to 40 years, it is hard to wake up each day wondering what you will do. For this reason, some people may want to continue in their careers, working fewer hours with flexible schedules.

This "gray tsunami" can be a great advantage to businesses. They need these workers and embrace senior employees. Senior employees have many positive qualities – institutional know-how, a willingness to share their experience, complex problem-solving skills, emotional stability, and a strong work ethic, to name a few.

Unfortunately, too many Americans continue to work because they are not financially prepared. Research conducted by Empower, a retirement plan provider, in September 2021 paints an alarming picture. It ranked the average retirement account balance by state. Connecticut came in first at $545,754. Utah came in dead last at $315,160, yes, 51st place (for those saying, "Wait, there are only 50 states," the research includes the District of Columbia). Many factors play into these numbers; for instance, Connecticut has more millionaires per capita than any other state, so that you would expect higher balances. Different states have favorable tax laws allowing employees to sock away a greater share of the paycheck.

A better indicator of financial preparedness may be the median balance by generation – Boomers: $587,943, Gen X: $303,663, Millennials: $75,745, and Gen Z: $12,016. No matter how you dice it, Americans need to save more.

The good news is that most employers sponsor retirement savings plans, such as 401(k)s, so employees can save for their senior years. Americans can prevent a savings crisis by increasing the percentage of income they save periodically as they receive pay increases, always saving enough to receive the full employer's match if available.

Financial preparedness is more than just a number. It's based on lifestyle, income needs, inflation, longevity, and investments. It can only be addressed through financial and income planning, something we are experts at providing. Call us today to talk about your goals and review your financial plan.

Sharla

Sharla J. Jessop, CFP®
President

Upcoming Podcasts

SFS releases new Power Up Wealth podcasts on timely and timeless financial principles. In the coming weeks, we will be doing a deep dive into each article written in this newsletter. Subscribe wherever you get your podcasts or listen at SmedleyFinancial.com.

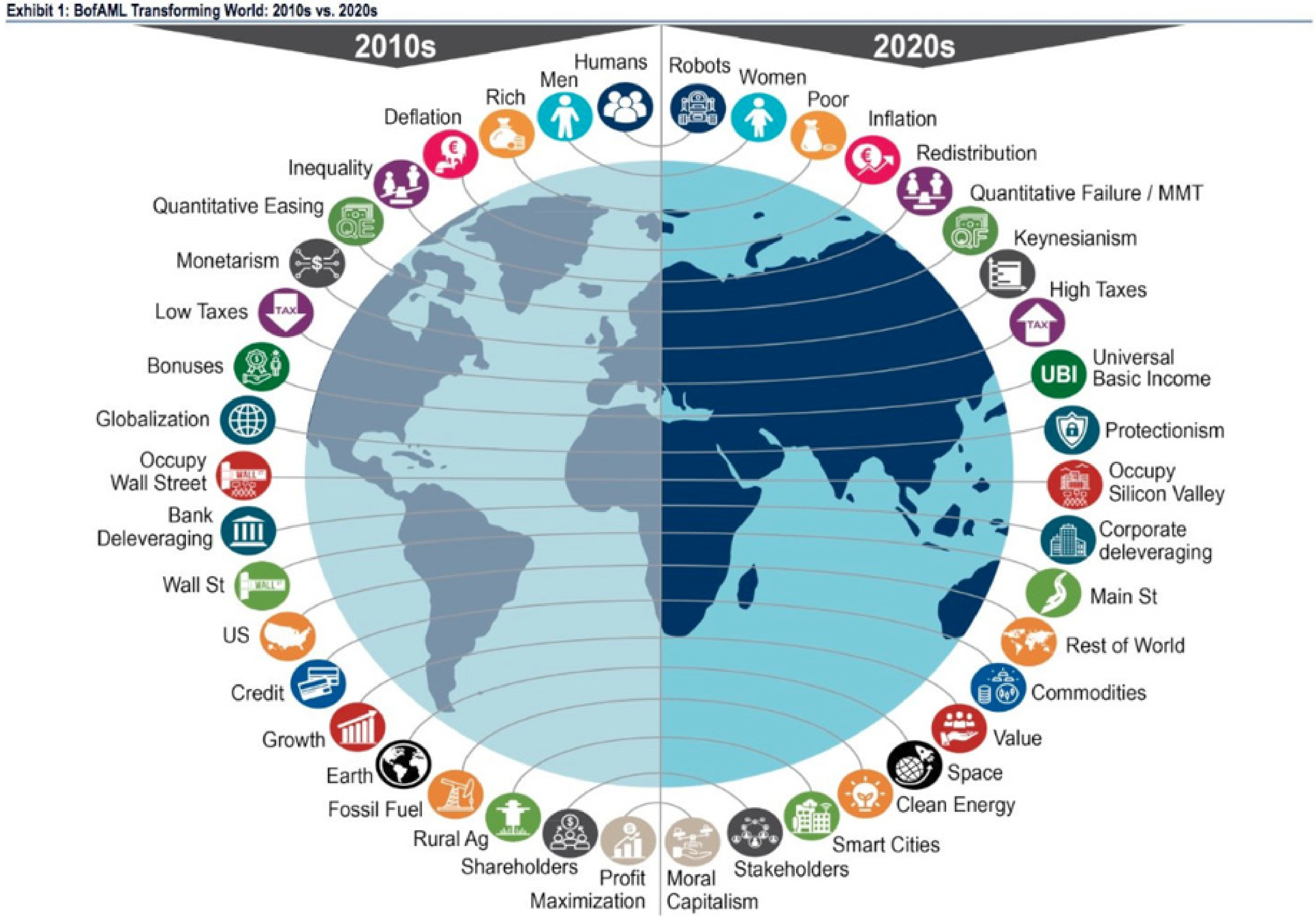
Economic Cycles Can Teach Us A Lot About the Future

By James R. Derrick Jr., CFA®

Three years ago, gasoline was around $2 per gallon. The government was giving away money, like deficits did not matter. And the Federal Reserve had been stoking financial markets for over a decade with what it called Quantitative Easing. All of these fit nicely into a popular philosophy known as Modern Monetary Theory. What have we learned? A lot.

New paradigms of the 2020s

Exhibit 1: BofAML Transforming World: 2010s vs. 2020s



Source: BofAML Global Research

On January 16, 2020, I shared the graphic above in a presentation I gave to peers in Atlanta, GA. The premise was that we would reach an inflection point with many changes.

It has only been a few years, and many of these are already coming to pass. Some are known by different names. Some are happening more slowly. A few have disappeared, for now.

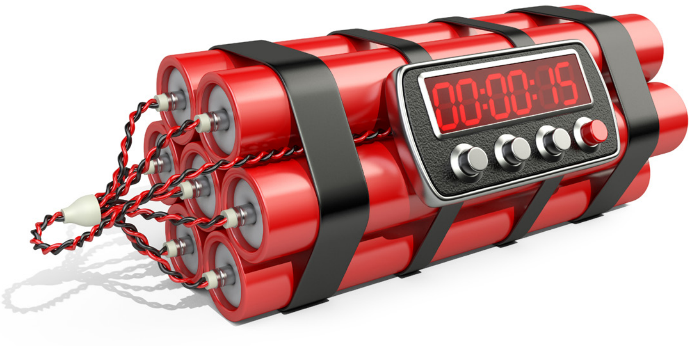
Globalization is deglobalizing now that nations and corporations prioritize security and resilient supply chains. Quantitative Easing has turned to Quantitative Tightening.

Just as an idea takes hold, and when we think we have the world figured out, things change. What has not changed? Economic cycles and progress. Stimulus led to inflation. Inflation led to higher rates. Interest rates will eventually have an impact on slowing growth.

These financial cycles encourage progress from electricity to artificial intelligence. They inspire and reward innovation. They also teach vital lessons–including the hard times. Our current cycle will do the same as it progresses.

Is Your Retirement Account a Tax Bomb?

By Mikal B. Aune, CFP®



Conventional wisdom has said to put as much away as possible into tax-deferred retirement vehicles, like an IRA or 401(k) because you will be in a lower tax bracket when you take out your money. The reality is that most people are in the same tax bracket, and some are even in a higher tax bracket. Compound that with the fact that taxes will likely go up because of our enormous national debt, and the tax picture looks even worse. If you have IRAs and 401(k)s worth more than a combined $1M, then you have a real tax time bomb waiting to explode on you and your heirs.

If you have been a diligent saver, you have built a large nest egg to see you through retirement and make sure you don't become a burden on anyone else. You have had the benefit of not paying taxes on the money you put into your pre-tax IRA or 401(k). Now that you are close to or in retirement, taxes are staring you in the face. Every time you take a distribution to supplement your retirement income, a big chunk is withheld just to pay the taxes. **Not surprisingly, "taxes" are the biggest complaint many retirees have.**

If you have a few hundred thousand dollars in IRAs or 401(k)s, you can usually spread the distributions over a number of years, do small Roth conversions, and/or donate some to charity. This can help ease the tax burden. However, suppose you have over $1M in IRAs or 401(k)s. In that case, your distributions can create major tax headaches, especially after you turn 73 and must start taking Required Minimum Distributions (RMDs).

For example, if your IRA were $5M, you would be required to take a distribution of $200,000 per year on top of your Social Security and other income. This already pushes you into a higher bracket, and there is an additional tax on Medicare. If you had two children, they stand to inherit $5M ($2.5M each). When they inherit the money, they would be required to take it out over a maximum of 10 years, meaning they would each need to take out at least $250,000 per year. This would be taxed on top of their existing income. Talk about unintended tax consequences!

There are some tax planning strategies that can make a large difference for you and your heirs.

First, if you are charitably inclined, each year, you can donate a portion or all of your RMD (up to $100k) directly from your IRA to a charity, and the donation is tax-free. **This Qualified Charitable Distribution (QCD) is the most tax-efficient way to get money out of your IRA since the tax rate is 0%.**

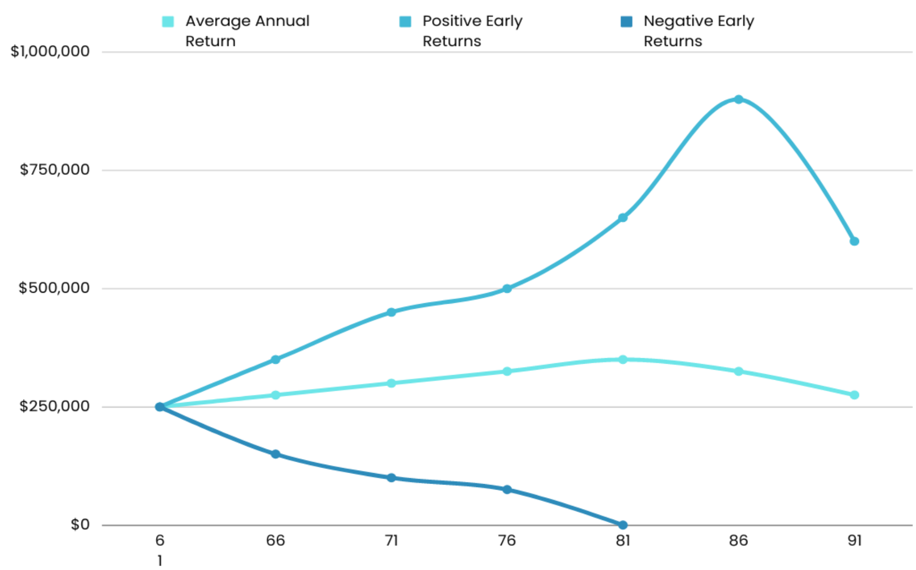
Second, you can do a Roth conversion and "fill up" your tax bracket. If you are in the 24% tax bracket and have another $100,000 in income before going into the 32% tax bracket, you can choose to pay 24% tax on the $100,000 and "convert" it into a Roth. We typically withhold the taxes of $29,000 from the distribution (24% fed tax, 5% state tax), and the remaining $71,000 goes into the Roth to grow tax-free for the future. Keep in mind there will also be a small additional tax on Medicare.

Let's look at one case for a client with $5M in an IRA/401k. Following conventional wisdom, they would leave their heirs $4.5M after taxes and distributions. However, only $1.6M of that has already been taxed. The heirs would still need to pay tax on $2.9M! In contrast, filling up the 24% bracket would convert roughly $100k annually into the Roth. At the end of the plan, they would pass on more money ($4.7M), with only $0.1M being subject to tax. The remaining $4.6M would be tax-free!

Conventional wisdom will only get you so far and shouldn't be followed blindly. If you have a large IRA/401(k), consult with one of our private wealth managers or a qualified tax professional to see if there are strategies that can diffuse your tax time bomb.

Am I Going to Be Okay?
Part 1

By Parker Thompson



One of the most common questions I get asked by retirees is, "Am I going to be okay?" Whether it is the first or last question, it is the most important. People want to know, "Will my retirement last?"

Risks to retirees are significant, and some have always been around while others are becoming more and more relevant.

The effects of bear markets, consequential portfolio losses, and inflation have always been something we combat. In addition, the sequence of return risk and the timing of retirement are more critical than ever.

There are ways to measure and tactics to help mitigate all of these risks.

Bear Markets

Most people describe a bear market as greater than 20% from the most recent high or simply the prolonged decline in prices and struggle of the market or economy. It can also coincide with investor fear and pessimism. The worst thing about a bear market is not necessarily the drop in prices but how long it can last.

A few studies looking back to the late 1800s and early 1900s have shown that the average duration of a bull market is 11 years. Once a bear market begins, it takes 19 years to go down and come back up to the previous high. Since 1929, investors have lost an average of 39.1% during bear markets. Some of the worst ones include the 80% loss of the Great Depression and the approximate 50% losses of the Dot Com Bubble and the Great Recession. The way markets cycle up and down; we are bound to have several during our retirement.

Sequence of Returns

Another risk you have probably heard of by now is the sequence of returns risk. This is best described as the consecutive returns one gets while taking distributions in retirement. Specifically, it is the potential for big losses in the early years of retirement. Having significant, negative losses in those formidable years can drastically affect how long your money lasts. Look at the graphs that depict the different scenarios above.

This assumes the same $250,000 and the same average 7% annual return over the retiree's life. You can see that if the same dollar amount is subject to early negative years in the market, you can run out of money sooner than you would like.

More risks like these lead us to create strategies to combat downside risk and volatility. We do everything we do here at Smedley Financial to ensure you do not run out of money by creating portfolios that do not sway as much with the market, implementing Lifetime Income Planning, and actively managing investments. Please watch the following newsletter as we will explore additional risks for retirees and the science behind how to overcome them.

The Global Reserve Currency and De-dollarization

Part 2

By Jordan R. Hadfield, CFP®

Since 1944, the United States dollar has become the world's reserve currency. With the recent weaponization of the dollar, the rise of inflation, and our government's ever-growing national debt, some believe the world economy will crown a new global currency. Is de-dollarization indeed a threat, or is it merely fear-driven speculation?

What is the gold standard?

The gold standard is a monetary system that links the currency of a country directly to the gold it possesses. Countries hold precious metals in central banks and print paper currency for trade in the marketplace. Central banks agree to buy and sell gold to anyone at a fixed price. This provides the credibility required for paper money to function as a basis of trade. Under the gold standard, governments are unable to print money without first obtaining the gold to back it.

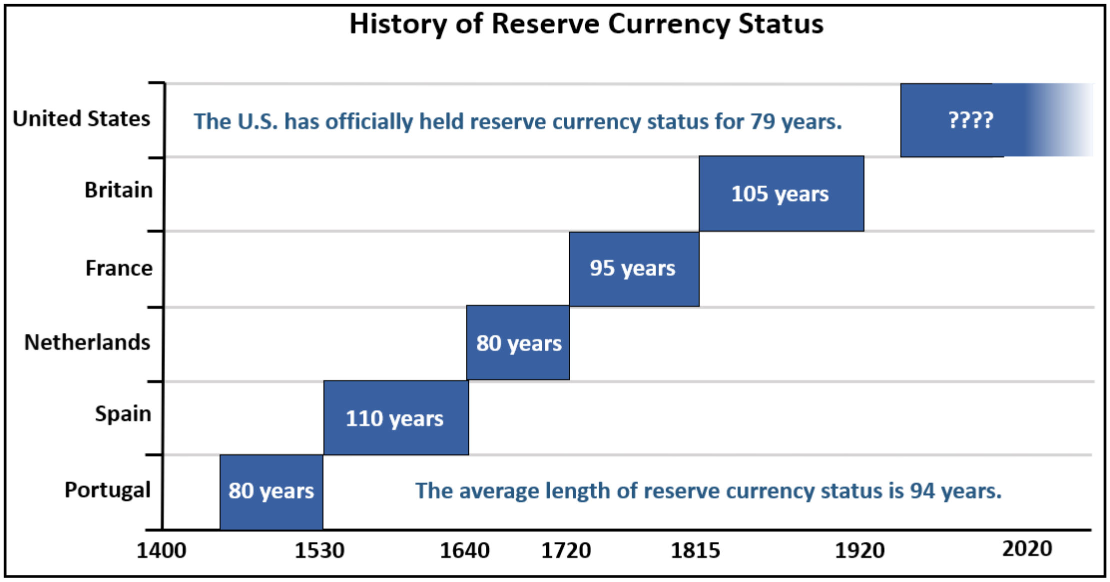
Although there are pros to the gold standard, it can create deflation and significantly prevent economic growth. As an economy grows, the money supply should grow with it. Where there are more goods and services, there needs to be more money for those goods and services. Think of the gold standard as training wheels on a bike - they can provide safety and security, but no one will ever win the Tour de France with training wheels.

The global economy has become so large that there is not enough gold in the world to back any one currency, making the gold standard impractical today.

Who held the reserve currency before the United States, and how did they lose it?

Since 1450 AD, there have been six world currencies. Great Britain was the last country to lose reserve currency status. In the 19th and early 20th centuries, most international trade was denominated in pounds sterling under the gold standard.

As we entered the First World War, Britain faced a struggling economy. Because of the fixed exchange rate of the gold standard, Britain was hamstrung and couldn't engage in expansionary policies to provide stability during this economic crisis. In 1914, Britain had no choice but to break from the gold standard and increase the money supply to stimulate its economy. This caused a severe weakening of the pound. By 1920, the pound had dropped by 35%.



At the same time, the United States was exporting large amounts of weapons to ally nations in exchange for gold. This allowed the US to stay on the gold standard, strengthening the dollar. By 1947, the United States owned 70% of the world's gold supply.

In 1925, Britain returned to the gold standard in hopes of solidifying the pound as the world currency. But its economic struggles only continued, and countries began trading outside of Britain in larger quantities. Britain was again forced to abandon the gold standard in 1931, never to return.

The Bretton Woods Agreement

Because the United States had accumulated so much of the world's gold by the end of World War II, many foreign governments lacked the gold necessary to back their currencies. This created currency risk and trade problems. **The world needed a new economic order.**

In 1944, 44 countries agreed to peg their currency to the value of the U.S. dollar. The dollar was pegged to gold, thus indirectly backing the other currencies with gold. Although unavailable to common citizens, the U.S. granted any foreign nation the ability to exchange dollars for gold. This is known as the Bretton Woods Agreement, which officially crowned the U.S. dollar as the world's currency.

The Nixon Shock

In the 1960s, the U.S. governments finances came under stress as the government increased spending to fund the Vietnam War and social programs. The Federal Reserve printed money without increasing the gold supply in order to cover deficits. With more dollars in the world, the international market began to worry the U.S. lacked the gold required to back its currency. Countries began to exchange their dollar reserves for gold.

President Richard Nixon feared a global run on U.S. gold. In 1971, Nixon suspended the convertibility of the dollar into gold in hopes of keeping the Bretton Wood system alive and eventually eliminated the gold standard entirely. This fueled international fears, and the dollar declined in value. Countries unpegged their currencies from the dollar in favor of floating exchange rates, and the Bretton Woods system fully collapsed in 1973.

Many expected these events would end the dollar as the world currency. They could not have been more wrong. The U.S. financial markets continued growing to become the largest in the world, and the economic gap between the United States and other advanced economies widened significantly.

Please look for part 3 and a conclusion of this discussion in our next issue of Money Moxie.

Your SFS Team

Smedley Financial Services, Inc.® is an independent registered investment advisory firm. We work for our clients. Our wealth managers have the flexibility to implement our financial plans, retirement plans, and income distribution plans using strategies that work toward each client's needs and goals. We work with individuals, businesses, and family estates. We provide financial solutions for your life.

Wealth Accumulation
- Managed Accounts
- Indexed Investing
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- Exchange Traded Funds (ETFs)
- Stocks and Bonds
- Alternative Investments

Family Protection
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- Whole Life Insurance
- Universal Life Insurance
- Variable Universal Life Insurance

Retirement
- Social Security Maximization Strategies
- Medicare Supplement
- Guaranteed Income (Annuities)
- Lifetime Income Planning

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- Long-Term Disability Insurance

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- Long-Term Care Insurance
- Hybrid LTC

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- Health Insurance
- 401(k) Plans

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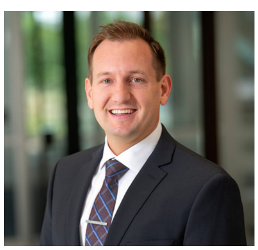

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