May – June 2023

Money Moxie®

World Currency Leader

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A Brief History of Dollar Doubts and Dominance

If you ever worry about the future of the U.S. dollar, you are not alone. Fear over the dollar dates to its beginning. Alexander Hamilton, the first U.S. Secretary of the Treasury, created a national bank that would strive to build confidence in the U.S. government and its currency. Failure to do so would result in higher interest rates and the eventual collapse of the nation. He had no precedent to follow. He was creating it with every agreement and every paper dollar his department printed.

The 7th president of the United States, Andrew Jackson, hated paper money. He thought it was not real–even when it could be exchanged for gold or silver at a branch of the national bank. President Jackson abolished that national bank, opening the door to our regional system consisting of private banks. On January 1, 1835, his administration paid off all federal, interest-bearing debt. He is the only president to have done so. That sudden cut in government spending shocked the economy. By year's end, a severe recession began. Those new private banks could not afford to exchange paper for gold and silver. Over 600 banks failed nationwide.

Paper money could be exchanged for gold or silver until the early 1890s. Americans could take advantage as the dollar was worth a fixed amount of silver and gold, even though the metals fluctuated independently. The famous story Wizard of Oz was originally a book written in outrage over dropping silver as a reserve for the U.S. dollar. The yellow brick road, which had no silver, led to a wizard who had duped everyone. The math didn't make sense. The country never went back to silver.

In 1971, our country dropped the gold standard—something still hotly debated today. It was necessary as there was not enough gold in the world to support the demand for the U.S. dollar. We knew because we had so much of it. The British gave us gold during WWI and WWII in exchange for oil, food, and weapons. That was the end of the British pound as the world currency.

Approximately 90% of all foreign exchange is done with the U.S. dollar (Global Trade Magazine). That is nearly everyone trading currencies. Apple's dominant iPhone only has a 53% market share (Mac Daily News). What about the global trade of goods? It is still approximately 50%. Dollars are preferred, and they are THE global reserve currency.

In times of uncertainty, dollar demand rises. This is an incredible advantage. It allows our government to borrow money when it needs it most—often at low-interest rates. The best example is the debt ceiling debate of 2011. The fear was that the government would miss a payment on its debt. Stocks began to crash about a week ahead of that date, and investors fled to safety. Ironically, they were buying U.S. debt.

Who wouldn't prefer dollars? Perhaps Russia, and maybe China. Even those are open for debate.

James

James R. Derrick, CFA®
Chief Investment Strategist

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.

Managing a Mountain of Risk

By Sharla J. Jessop, CFP®

Going up the mountain, a climber has a good perspective of where to place each foot or where to find handholds. They can see the terrain and determine the best approach. Conversely, an experienced climber will tell you the descent may be the most challenging part of the climb, and it is hard to see where to take the next step or even the best route to get you down the mountain safely.

Likewise, the same volatile markets that benefit investors saving for retirement can ravage a retiree's nest egg.

Dollar Cost Averaging
Young investors are trekking up the mountain. They have a portion of every paycheck going into a 401(k) or other retirement saving plan and are dollar-cost-averaging into the market. This practice of making consistent investments, regardless of what the market is doing, has an enormous payoff. Market dips allow the systematic investor to buy at a discount – when things are on sale. Then by remaining invested, they take advantage of long-term appreciation.

Diversifying investments over a range of market sectors can help 401(k) investors manage risk and the emotional side of investing. No one knows what area of the market will do well at any given time. While diversification does not guarantee investors will not experience a loss, it does help reduce the risk that investors will experience an unrecoverable loss.

Spreading investments across many market sectors, investors will have a portion of their account that may experience growth and another sector that may experience a loss during the same time. If done correctly, the combination of diversified investments can help smooth out the ups and downs in the investors' accounts.

Declining Balances in Retirement
Like a climber descending a mountain, dollar-cost-averaging out of the market can have a devastating effect on retirees. Why? If a retiree takes money from an investment that is dropping in value, they remove the potential of riding the market back up. The investment has been sold, possibly at a low point, and the shares cannot recover. This is known as the sequence of return risk.

Experiencing negative market returns in the early years of retirement can prematurely reduce a nest egg. This is a serious problem because retirees are living longer than ever before. Traditional diversification may not deliver the protection one might expect when taking withdrawals. These obstacles require a strategy to properly allocate risk and distribute money at the right time and from the right account – Not easy to do.

Lifetime income planning takes a different approach to risk allocation. It is designed to protect the retiree's income source from market volatility while at the same time remaining invested for long-term appreciation. Using lower risk investment strategies to support income needs allows investments with greater risk to remain invested to navigate volatility.

If you are nearing retirement, let us show you the benefits a Lifetime Income Plan can provide you.

Is the Bank the Safest Place?

By Mikal B. Aune, CFP®

At times, I have had clients tell me they keep so much money in the bank because they feel it is "safe." However, any place you put your money has risks. You can bury cash in the backyard and a flood, earthquake, or faulty memory could wipe it out. You can stash some money all over the house, but it can go up in smoke. Just because you think a place is "safe "doesn't mean it is.

A savings account at the bank can still be wiped out, especially from fraud. I recently had a client lose over $100,000 from their checking account. How did this happen? Wasn't the bank safe?

I've had too many clients impacted by scams like this, so I want to keep raising the warning bell: Watch out for fraud!

In this instance, a warning notice popped up on their computer that there was an issue. The client was instructed to call a phone number that looked legitimate. Since somebody wasn't calling them from Timbuktu, they felt more secure. The person who answered the phone assured them everything was OK but asked them for personal information and computer sign-in information. With that information, the perpetrator was able to gain access to their computer and lock it down. Then they were able to find banking information. They logged into the bank and wired money to an offshore account. Wires are hard to recover. Even though the bank made efforts to recover the money, they could not get it back.

We have to be even more vigilant in our world. Fraudsters are everywhere: emails, computer hacks, text messages, and phone calls. Even if an email looks legitimate, only click the link or open the attachment if you are expecting the email or you have called the person who sent it to verify. Refrain from trusting the phone number or website link in an email or pop-up window. Do your research to find the actual phone number or website instead. If you get a phone call from your "nephew" who is in jail in Mexico and needs money wired to them, hang up.

Be smart and protect yourself by using a password manager so you can use a unique complex password for every login. If one password is compromised, the tricksters won't have access to all your information.

At Smedley Financial, we already have security systems and protocols to help protect your investments from fraud.

- We follow client verification procedures, including personal information and signatures.
- We have a policy not to accept requests via email.
- We use additional verification procedures for high-risk transactions like wire transfers.

We will continue to work hard to protect your hard-earned assets from fraud. If we all do our part, we can prevent fraudsters from tricking another victim.

Buying Big Ticket Items

By Parker Thompson

Big purchases and expenses are inevitable in life. We save up, prepare, and try to anticipate when they may happen. Some are more stressful and anxiety-inducing than others, like paying for a new roof, replacing a totaled car, or figuring out how to finance college or weddings. These situations force us to think more about our financial situation because they tend to be more expensive.

Adding to the stress are the rising interest rates in our current economic environment. Even the monthly payments on loans start to look scarier. Currently, average auto loan rates start at 6-8% and go higher. The average monthly payment for a new car has reached $716, assuming a loan term of almost 70 months. Used vehicles are not much better, as their prices remain high. Whether it's a large monthly payment or having a loan for that length of time, it's natural to feel concerned.

Mortgage rates are hovering around 7% for a 30-year loan. Buy now, pay later services are becoming more common, even for small purchases. Credit card rates average between 20% and 30%. Personal loans and payday loans come with even higher rates.

Considering these numbers can be worrying, especially when planning a significant purchase in the near future. However, if we adhere to sound financial principles, we can make better decisions.

First, we need to analyze whether it's a need or a want. Can we do without it for a little longer? Those who exercise delayed gratification might find themselves in a better position when prices decrease and interest rates stabilize.

Second, we must assess affordability. We should evaluate our cash flow and monthly income to determine if we can handle a lump sum payment or the required installments. Do we have enough cash on hand to pay for it outright? Will we still have our emergency fund and enough cash for future large expenses? If the answer is yes, then we can afford it. However, if we don't have enough money at the moment or only have partial funds, we need to consider our debt-to-income ratios for financing the purchase.

Welcome to Personal Finance 101. Your monthly housing debt payments should not exceed 28% of your gross income. Your total debt, including housing, should not exceed 36% of your gross income. Some individuals prefer to calculate these ratios based on net income instead of gross pay, taking a safer and more conservative approach. For instance, let's assume a yearly income of $60,000 for simplicity. If your monthly gross income is $5,000, your upper limit for mortgage or rent should be $1,400. Suppose you have student loans, a car payment, or other debts. In that case, your upper limit, including those expenses with your housing costs, should be no more than $1,800. There's not much room left for a $700 car payment in this scenario.

Staying under these ideal ratios allows you to afford other unexpected expenses that arise in life. If your ratios are much higher, say in the 40%-50% range, it may be challenging to maintain the desired lifestyle in the long term, and unexpected purchases can significantly disrupt your financial stability. These guidelines help us avoid overextending ourselves and staying within our means.

In this environment of high prices and interest rates, it's crucial to monitor your spending, manage debt, and stay informed about current rates. Avoid high-interest debt, understand your ratios, and assess whether you can genuinely afford your purchases. If you're not in the financial position you desire for milestone purchases or where you need to be in the future, remember that we're here to help you plan your path forward.

The Global Reserve Currency and De-dollarization

Part 1

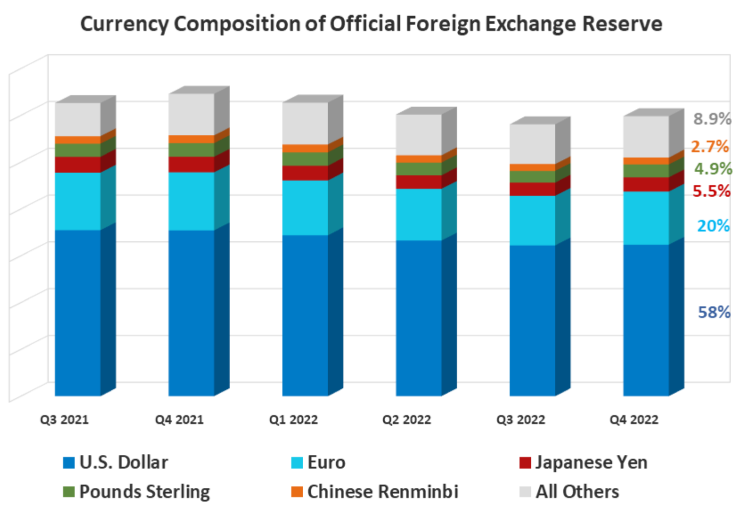
By Jordan R. Hadfield, CFP®

Since 1944, the United States dollar has officially been 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 a reserve currency?
Every country has its own currency, and the values of these currencies fluctuate relative to each other. If a company in South Korea wishes to import widgets from the U.K., they would otherwise negotiate a price in pounds sterling. From the time negotiations settle to when the invoice is paid, the exchange rate of the S.K. won may drop compared to the U.K. pound. This would result in the S.K. company paying more for the widgets than expected. This is called exchange rate risk.

The easiest way to reduce exchange rate risk is for governments and institutions to agree to trade in one currency. Hence, a global reserve currency. Central banks and financial institutions throughout the world hold large amounts of the reserve currency to help facilitate international transactions, including investments and debt obligations.

As of September 2022, about half of all international trade was invoiced in dollars, and about half of all international loans and global debt securities were denominated in dollars. In foreign exchange markets, dollars were involved in nearly 90% of all transactions. Central banks currently hold 59% of foreign currencies in U.S. dollars—a healthy percentage.



Advantages of the reserve currency
Currencies trade on the open market like other assets. The global reserve currency has a significantly higher demand than other currencies, which creates many advantages.

(1) The larger the demand for a currency, the lower the borrowing costs for the issuer of that currency. If the issuing country can borrow money at a lower interest rate, that country will have more capital and can pay a lower amount of interest on that debt.

Continued on next page

(2) Businesses and citizens of that country will also have greater access to cheaper money.

(3) Taxes are often lower as government debt is less expensive, and demand is increased as there is more cash in the system.

(4) All of this stimulates growth, creates wealth, and stabilizes the economy during times of crisis.

(5) There is also political power in having reserve currency status. Because international trade uses the reserve currency, all countries rely on the financial system of the issuing country. The U.S. has leveraged this to enforce rule-based international order, establish justice, punish fraud, and ensure the world's security. The dollar's status has given Washington leverage over its political adversaries.

Disadvantages of the reserve currency
A strong currency is expensive, creating a paradox for the issuing country.

On the one hand, the country enjoys low-interest loans and the ability to raise capital quickly through issuing reserve currency-denominated bonds. On the other hand, the country wants to use capital and monetary policy to ensure that domestic industries are competitive in the world market and that the domestic economy is healthy and not running large trade deficits.

At times, these objectives can be mutually exclusive. This is called the Triffin Dilemma, and Americans have experienced it for decades, first with Japan and then with China.

Because the reserve currency status increases the demand for dollars, the price of the dollar is increased compared to other currencies. This results in U.S. exports becoming more expensive, reducing demand for U.S. goods.

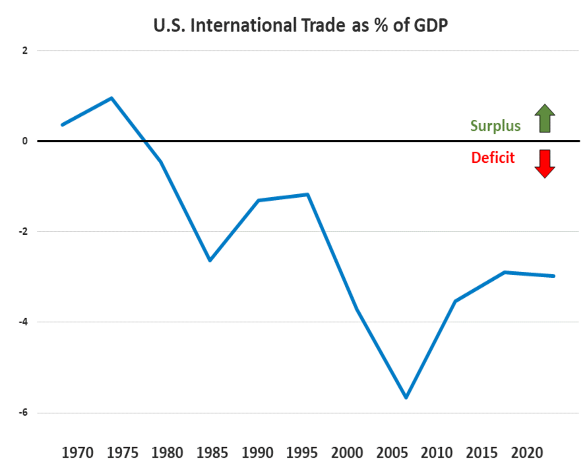
A more expensive dollar also makes foreign goods less expensive. This leads to greater imports and larger trade deficits. As foreign demand for the dollar pushes its value higher, reduced demand for U.S. goods can result in fewer jobs and higher unemployment. The only way for the U.S. to remedy this is to expand borrowing and increase debt.

Issuing the reserve currency makes monetary policy an international issue as opposed to strictly a domestic one. The government must balance the desire to keep unemployment low and economic growth steady with its responsibility to make monetary decisions that will benefit other countries. In this way, issuing the reserve currency can become a threat to national sovereignty.

Do trade deficits harm the economy?
A trade deficit occurs when a country imports more goods than it exports, thus transferring cash out of the country in exchange for goods into the country. On the surface, this sounds negative; however, the intricacies of economic trade are nuanced. Balanced international trade often results in a win-win scenario for the citizens of the two countries.

America loves to consume. Because foreign products are often cheaper, importing leads to more consumption. If U.S. trade deficits do not reach excessive levels, a deficit is not harmful to the U.S. economy. The United States has run a trade deficit nearly every year since the end of WWII and has remained the strongest economy in the world. Other countries have had continuous trade surpluses, and their economies have seen little growth.

However, large deficits are dangerous. Cash flowing out of the country strengthens the economies of those who receive it. Those countries often reinvest those dollars in the U.S. government by purchasing treasuries—increasing U.S. debt and leading to foreign nations subsidizing American consumption. As dividends and interest are paid on debt and American investments, more cash flows out of the U.S. and into foreign nations.



In this way, being the reserve currency is itself a threat to maintaining the reserve currency. Having reserve currency status can ultimately lead to a weaker economy and stronger foreign nations. The question becomes, how much of a deficit can the U.S. economy handle?

Please look for part 2 and a continuation 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.

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- Alternative Investments

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- Universal Life Insurance
- Variable Universal Life Insurance

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- Medicare Supplement
- Guaranteed Income (Annuities)
- Lifetime Income Planning

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- Short-Term Disability Insurance
- Long-Term Disability Insurance

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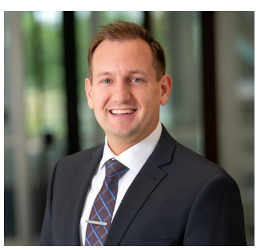

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