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Money Moxie®

SMEDLEY FINANCIAL SERVICES, INC.®

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How Do You Measure Your Financial Success?

How do you measure your financial success? The U.S. government grades its economy based on Gross Domestic Product (GDP). This is similar to looking at how much money is spent in this country. There are no adjustments for happiness, security, or savings. As American consumers spend, spend, spend, they send GDP up, up, up. So, where does all the money come from?

Just as the fundamental rule in accounting is debits equal credits, our spending must balance. Most is paid for with income if you are working (from savings if retired). We could also make some adjustments for taxes and debt. I came up with this equation: **Spending = Income – taxes – savings change + debt change.**

Now, imagine this equation for all Americans. Does our national income match our total spending? There is a measurement for this as well. It is called Gross Domestic Income (GDI), and it is rarely discussed. My college professor brushed over it like this: *GDI is equal to GDP, so we will focus on GDP*.

It comes as no surprise that the nation and its consumers have both been tapping into savings and increasing debt over the last 12 months. Spending and income have not been this different since 2007. Americans are currently spending around 3% more compared to last year. That is on top of inflation. National income is up only 0.4% over the same time. GDI has been slowing for 8 quarters in a row while GDP has risen.

We should pay more attention to our spending. Federal debt may not be an emergency, but interest payments are becoming a major burden. Personal credit card debt is at all-time highs, and rates average over 24% (LendingTree.com). The U.S. government has ways of extending the status quo for much longer than one would think possible. It can also print money, literally. We do not have this luxury.

Our personal financial health is not measured by how much we spend. That would be crazy. What do we look at? Perhaps it is how well we live within our means. Whether we track it in a budget or not, we should all have some idea of how much we are spending. Set financial goals. Identify priorities. Create a rainy-day fund. Be intentional about saving and spending.

We may not be able to control everything in our national circumstances, but we can control our personal finances. When we do, we have a better chance at achieving those things money cannot buy, like happiness and security.

James

James R. Derrick, CFA®
Chief Investment Strategist

POWER UP
WEALTH

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.

Stepping Off the Edge into Retirement

By Sharla J. Jessop, CFP®

A lifetime of work culminating with a single trigger – or so it seems. Even though you have spent years preparing, setting an actual retirement date can be terrifying. It doesn't need to be. Retirement is more than just a financial decision; it is also an emotional one. The best way to conquer this fear is understanding the risks you may face and having a plan to help manage them. I will focus on two concerns that top the list for many of us.

Replacing your paycheck is generally the top concern. Retirement is not free. You will need a certain amount of money to live on, which increases over time to keep up with inflation. The exact amount will fluctuate based on changing needs. Think of retirement years in stages.

You will likely spend more money in the early years of retirement – known as the "Go-Go years." While still in good health, you will be eager to do the things you have dreamed of for years: traveling, attending concerts, taking classes, and starting a new hobby. These extras are in addition to your regular monthly living expenses.

Once you reach mid-retirement, during the ***"Slow-Go years,"*** you may reduce spending on the extras. You may not travel as much or do as many extra activities.

As retirement progresses, your needs change. You may experience an increase in health care needs, or need someone to help mow the lawn or clean the house. This period is known as the ***"No-Go years."*** Getting out and about is harder than it used to be.

Planning for these stages and your changing income needs will help as you transition to retirement.

Having proper medical coverage is another concern retirees face. According to *Fidelity Retiree Health Care Cost Estimate,* a single person age 65 in 2023 may need approximately $157,500 saved to cover health care expenses in retirement. A married couple may need $315,000.

If you retire at 65 or older, the decision becomes which type of Medicare coverage you will choose. Will you go with traditional Medicare and get a Medigap policy to provide supplement coverage? Or will you go with a Medicare Advantage plan that will incorporate most of your needs under one policy? You may also need to purchase coverage for prescription drugs separately.

If you retire before age 65, you need coverage on an individual basis. Some employer plans have a cobra provision – allowing you to extend coverage for a specified period under the former employer's plan. The premium is no longer subsidized by your employer. When the cobra period ends, you turn to the open market.

If you retire early, regardless of which option you choose, make sure your coverage is creditable. This will avoid any hiccups when you are ready to switch to Medicare. You also need to understand the trigger points for starting Medicare coverage – the windows for signing up are very specific. If you miss a window, you may find yourself without coverage or may incur costly penalties you will pay every year going forward.

You can feel confident as you transition to retirement by having a plan that you can rely on. Let our wealth management team help you create that plan, preparing for this life change and the challenges that may arise. It's never too early to plan for a successful future!

The Paradox of Wealth

By Mikal B. Aune, CFP®

We usually think of wealth generation in a linear fashion, like traveling down a path or going up steps. It has the following levels: dependence, survival, stability, security, independence, freedom, and abundance.[1] Many people progress along this path, but it seems like some are trapped in the dependence/survival levels, and some are perpetually in the freedom/abundance levels. Hence the saying, the rich get richer, and the poor get poorer. However, something entirely different is happening. This is the paradox of wealth.

This wealth cycle seems straightforward. You can probably relate to the different levels of wealth: dependence, survival, stability, security, independence, freedom, and abundance. In your formative years, you were dependent on your parents. Then you got your first job, car, house, and bills and were in survival mode. You got a little further into your career, finances were not so tight, and you were able to save a little, creating stability. Once you have been able to save more and finally pay off most of your debt, you find security.

Paying off all your debt and having a good nest egg gives you independence. Then you have the freedom to do what you want when you want. Finally, you feel like you have more than you will need, which is the final phase of abundance. You may see your own progress somewhere along this line.

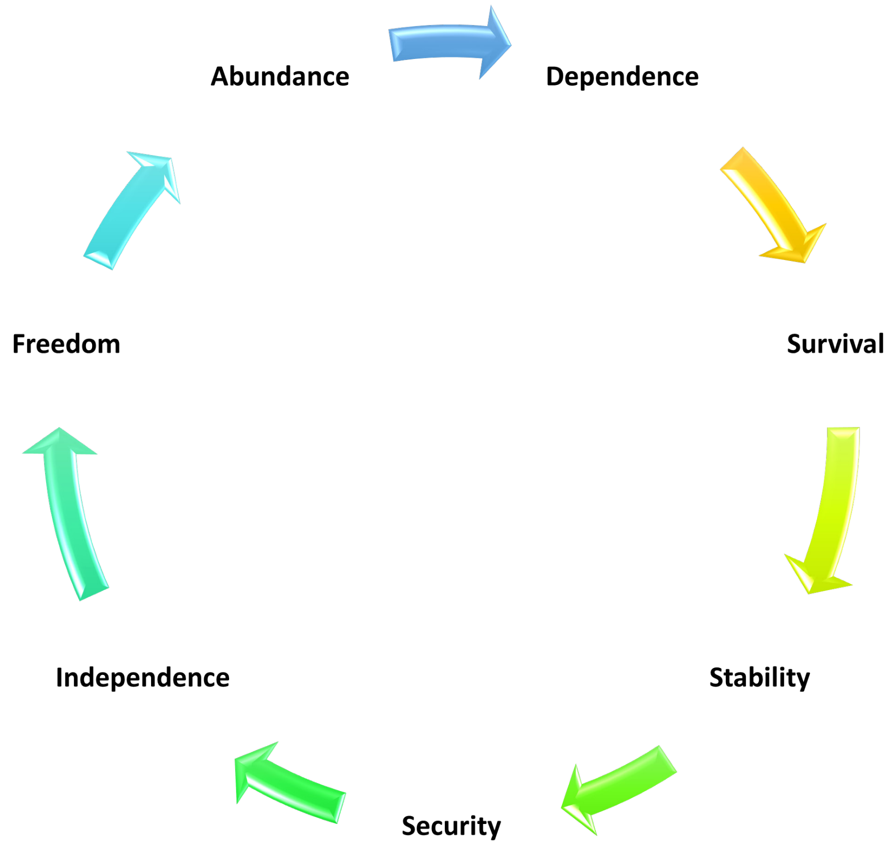
In our minds, we picture this as a straight line going up to the right. We imagine families just picking up from where the patriarchs left off and continuing the upward march to ever better levels. Hence, the rich get richer, and the poor get poorer.

However, not everyone attains all the levels of wealth. There is a whole segment of society that is trapped in poverty. Relatively few seem to break the cycle to find stability and security. We do see people starting in middle-class security and progressing to where they move to freedom and independence. We see entrepreneurs who create businesses that sell for millions (or billions) of dollars, catapulting them into the abundance category. We often think that once they get to abundance, their family is set. They have reached the pinnacle, and they are never going back.

The paradox of wealth is that for 80% of "rich" families, the wealth will be destroyed within two generations. That means the family "riches" are squandered and the third generation must start all over again. This perpetuates the wealth lifecycle, which paradoxically means the rich get poorer and the poor get richer. Extend it out one more generation to the third generation, and 90% of "rich" families will lose their wealth. Only 10% of families maintain their wealth beyond three generations.

This doesn't just apply to those in the abundance phase. This also applies to those in the security, independence, and freedom phases. Many times, we see clients that have worked hard their whole lives to build a nest egg of security, only to see it consumed when it gets to the next generation.

What is counterintuitive is that we shouldn't picture wealth generation in a linear fashion. We need to picture it as a circle that goes around. (See graph) Sometimes, there is a progression from one level to another level. Sometimes, there is a regression back a level or two. Paradoxically, the next step from abundance is dependence, which occurs when a family comes full circle, destroying the wealth that was so carefully cultivated and protected.



In the U.S., this phenomenon of families losing their wealth is referred to as shirtsleeves to shirtsleeves in three generations. However, it isn't unique to the U.S. In Ireland, it is called clogs to clogs in three generations. In China, it is called rice patty to rice patty in three generations.[2]

So, if this phenomenon is worldwide, why does it still feel like the rich get richer and the poor get poorer? While this seems counterintuitive, research proves that "The vast majority of affluent clients are New Money, not Old Money. Approximately 80% of...individuals have come to their wealth during their lifetime, not having been born and raised with wealth."[3]

Wealth is being generated, but it isn't from just the rich. Some of the rich stay rich, and some of the poor stay poor. But conversely, some of the rich become poor, and some of the poor become rich.

If you are starting out along the path and are just struggling to make it from survival to security, keep your spirits up. We live in the United States, where the American dream is still alive. You can progress around the circle of wealth and find more security, independence, freedom, and even abundance.

If you have already found independence, freedom, and/or abundance, and you are worried about the next generation, take heart. There are ways to follow the path of the 10% of families that maintain wealth beyond three generations.

The keys to maintaining wealth are found in communication, education, and a change in mindset.

The paradox of wealth is that the rich get poorer, and the poor get richer. It doesn't need to be that way. If the right principles are implemented, we can help lift the poor out of poverty and also help family wealth be maintained and grow over time.

1. *https://www.caminofcu.org/understanding-the-7-stages-of-financial-independence/*
2. *Wealth: Keeping it in the Family.*
3. *US Trust Survey of Affluent Americans, 2007; Phoenix Wealth Survey Executive Summary, 2007; Capgemini/Merrill Lynch World Wealth Report, 2009.*

Am I Going To Be Okay?

Part III

By Parker L. Thompson

For those following along, this is the third installment answering the question, "Will my retirement last?" We have discussed risks that retirees face in retirement, like bear markets, the sequence of return risk, retirement timing, losses, and inflation. Here, we will go over how to plan to combat these risks.

All the risks we have laid out come into play during retirement. The fact that we are living longer as humans means that we must plan so that we do not run out of money too soon. How do we balance all these risks? How can we look at our plan and know that we are going to be okay?

We have solutions at Smedley Financial. Some are fundamentals that anyone can deploy, and others are strategies that we use to combat these things so that retirees live the lifestyle they want during retirement.

Mitigating Standard Deviation

The primary tactic that many ignore is mitigating standard deviation. If that sentence went over your head, that is fine. We are going to explain.

Standard deviation is the fluctuation of your money. In other words, it is volatility. It is one way investors measure risk. The standard deviation for the stock market is large, whereas the standard deviation for bonds, especially short-term bonds, is lower.

Let's see why standard deviation plays such a big role. Take two portfolios, the Hare portfolio and the Tortoise portfolio, during a 10-year period. Each starts at $100,000. The Hare represents the S&P 500 performance, and the Tortoise would simply be that same performance but cut in half. The results will surprise you.

	HARE PORTFOLIO	INVESTMENT	TORTOISE PORTFOLIO	INVESTMENT
Year 1	26.46%	$126,460	13.23%	$113,230
Year 2	-37.00%	$79,670	-18.50%	$92,282
Year 3	5.49%	$84,044	2.75%	$94,816
Year 4	15.79%	$97,314	7.90%	$102,301
Year 5	4.91%	$102,092	2.46%	$104,813
Year 6	10.88%	$113,200	5.44%	$110,515
Year 7	28.68%	$145,666	14.34%	$126,362
Year 8	-22.10%	$113,474	-11.05%	$112,399
Year 9	-11.89%	$99,982	-5.95%	$105,717
Year 10	-9.10%	$90,883	-4.55%	$100,907

The Hare portfolio represents S&P 500 performance 2000-2009.
The Tortoise portfolio is the same annual performance cut in half.

By the end of 10 years, the Tortoise wound up with more money. It did not have near the gains in the market as the Hare did, but it did not have near the losses either. Losses are powerful.

You can mitigate standard deviation in a few ways.

Basket of Holdings

One could comprise a list of holdings in a portfolio of funds that do not deviate as much as the market but continue to grow. This is how most do it, and even here at Smedley Financial, we use this to analyze the investments we select.

Lifetime Income Plan Buckets

Another tool we use is the Lifetime Income Plan. We split assets up into different accounts. Some of those accounts may have higher than desired standard deviation, and some may be too low. Overall, they create the desired standard deviation. This is a strategy that we use in conjunction with others.

Active Management

We can also proactively trade based on opportunities and risk in the markets. Using a host of indicators and information, we can make judgment calls that can potentially help reduce market risk.

The overall goal is to protect not only the accounts but the lifestyles of those retirees who own them. By deploying these efforts, we are better able to weather the storms of retirement timing, sequence of returns risk, and the power of losses, making it through the barrage of bear markets and inflation. We do this so we can look across the table at our clients and say, "Yes, you are going to be okay." We are happy to partner with you and ensure your retirement will last.

Investing involves risk, including the potential loss of principal. The S&P 500 index is widely considered to represent the overall U.S. stock market. One cannot invest directly in an index. Past performance does not guarantee future results. The opinions and forecasts expressed are those of the author and may not actually come to pass. Diversification does not guarantee results, nor does active trading. This is not a recommendation to purchase any type of investment.

The Shortsighted Investor

By Jordan R. Hadfield, CFP®

Steven is shortsighted. He's been that way his whole life. Steven mostly spends what he makes. He doesn't save a lot. He doesn't plan for the future. Steven lives in the now.

Although Steven claims to be satisfied with where he is in life, he recognizes that he hasn't met his full potential. He often follows the crowd. He tends to jump at his first opportunities, which aren't usually his best opportunities. But Steven isn't concerned too much about that.

When it comes to finances, Steven gets caught up in the news of the day. Because of his shortsightedness, he often makes the wrong money decisions and at the wrong time. Wise investors try not to be like Steven. However, even a broken clock is right twice a day.

There are 3 things shortsighted Steven is doing right today and 3 he is doing wrong.

Steven has noticed that high-yield savings accounts and CDs are paying more than they have in many years. He also sees that his checking and savings accounts at the bank aren't paying him diddly. Steven is smart to move some of his extra cash and emergency funds into these short-term accounts.

However, Steven fails to recognize that when short-term interest rates move up, other investment options move up as well. Steven puts too much money into these short-term vehicles and ends up missing out on bigger opportunities. Steven feels good about his new CD, but by putting too much there, Steven is stepping over dollars to pick up dimes.

With the news of a possible recession on the horizon, Steven decides to cut back on spending and save a little extra. This is a wise decision. But Steven fails to notice that the interest rate on his credit card has moved up considerably. Steven is now borrowing from his future self at a much higher rate. Paying off all high-interest debt is what his future self wishes Steven would do now.

Steven sees the volatility in the markets and hears it could get worse. Steven knows that investing in volatile times can greatly work in his favor. Steven decides to contribute a little more to his retirement account. Good job, Steven.

However, Steven also knows that volatility can lead to losses in the short term. Because of this, he changes his investments in all long-term accounts to be conservative. If Steven fails to reallocate his investments at the right time, he could leave a lot of money on the table. This is a risky move Steven, and one we don't recommend.

My best advice to Steven, and everyone else thinking about how best to financially handle the short-term, is to speak with a financial professional. We are here to help ensure you don't miss great long-term opportunities due to shortsightedness. SFS

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
- Mutual Funds
- Exchange Traded Funds (ETFs)
- Stocks and Bonds
- Alternative Investments

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

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

Disability (Injury)
- Short-Term Disability Insurance
- Long-Term Disability Insurance

Elder Care
- Long-Term Care Insurance
- Hybrid LTC

Employers and Self Employed
- Health Insurance
- 401(k) Plans

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