July – August 2022

Money Moxie®

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The Final Dash

I recently read the results of a study by Ramsey Solutions with 10,000 millionaire participants. The study revealed that these millionaires did not receive any inheritance from parents or family members, and they had mainstream jobs like teachers, engineers, accountants, attorneys, or management. A large portion of them, 8 out of 10, invested in their company's 401(k) plan.

Maximizing your company's retirement plan is an excellent way to save, invest, and build wealth. For one thing, it's easy! Money goes directly into your account before you receive your paycheck. This places saving for the future at the top of your financial to-do list. Most plans offer diversified options that coincide with an anticipated retirement date. They even allow you to make up for missed time if you are 50 or older through increased contribution limits.

For too many investors nearing retirement, this isn't enough. They are making a final dash. They want and need to save more than the 401(k) plan will allow. Or, they may wish to have access to their money without the restrictions found in qualified retirement accounts.

This can be accomplished by investing in a non-retirement account. In other words, the account is titled in an individual name, joint name, or the name of a trust. The benefit is that you have complete control over how much you invest, when you invest, when you withdraw money, and even how you will pay taxes.

These accounts qualify for capital gains treatment, which opens a world of possibility. For example, you can apply tax-loss harvesting, where the sale of appreciated assets is offset by selling an asset with a loss, eliminating or reducing taxes.

You can donate appreciated assets to a qualifying charity and claim the gift on your itemized tax return, avoiding capital gains taxes altogether.

You can even gift the asset with a low tax basis to a family member who may be in a lower tax bracket and would not lose as much to taxes when they sell the asset.

In short, preparing for retirement is more than just putting money into your retirement account. Non-qualified accounts increase flexibility and put you in the driver's seat.

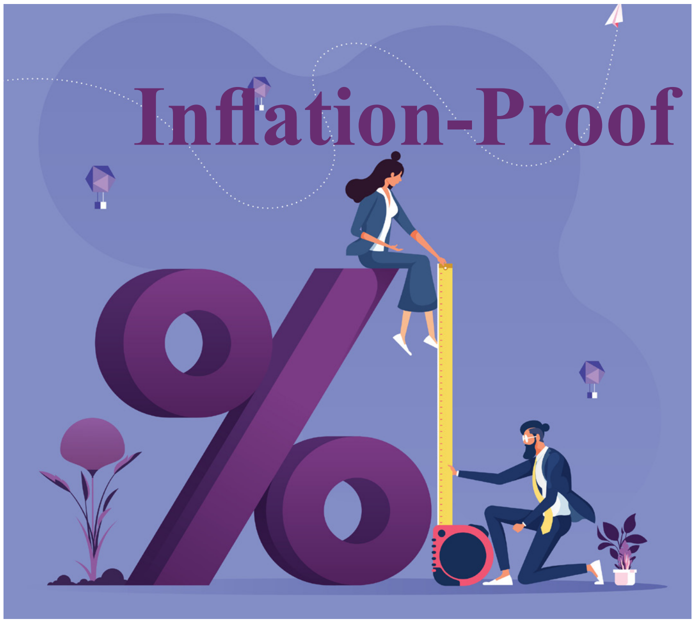
Sharla J. Jessop, CFP®
President

Sharla

Upcoming Webinar and Podcasts

SFS will be hosting our quarterly market update webinar on August 11th. We plan to discuss the possibility of entering a recession with high employment and what it might look like for consumers and investors. Watch your email for more detail.

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



Inflation-Proof Spending Habits

By Parker Thompson

We're living in expensive times right now. Inflation is rampant throughout the country, and a potential recession is knocking on the door if we are not already in it. Rising prices are hitting us where it hurts. It may seem impossible to stick to your budget now or in the future. Here are a few tips for managing your spending and being budget-wise during these times.

Track Your Spending
Let's start out by establishing that if you're not on a budget yet, you should be. At a minimum, tracking your spending to know where your money is going would be wise. Plenty of banking apps will support this already. Popular apps and websites like Mint, You Need A Budget, and Every Dollar will do it automatically for free for you. You could always open a spreadsheet if you are feeling savvy, and we have one we can email you to get you started.

Research, Research, Research
Take advantage of the resources we have in our hands. The internet is a wonderful thing, especially when it comes to researching your purchases. Researching an item or service you plan to buy can save you hundreds, sometimes thousands of dollars. The more time you spend researching, the more you will know the range you can expect to pay. You can usually find the best deal through aggregate search sites. For example, GasBuddy.com can show you where to find the cheapest gas in your area. Speaking of gas, that brings up the next tip.

Join Rewards Memberships
Many grocery stores and gas stations are offering you the option to enroll in memberships or reward cards. Some of them are free, and others have you pay a small fee. On the low end, you can save 10 cents a gallon, up to 20-30 cents per gallon of gas. That can add up over time. If you do this coincided with a grocery chain, you can double up the savings with grocery discounts too. Otherwise, it might be time to temporarily give up the avocado toast for breakfast.

Grocery Shop with a List
Shopping with a list can help you be more efficient at the grocery store and save you a lot of money. When shoppers go in without a list, they grab what looks good, impulse buy, and put things in the cart they may not need. Make yourself a list, and you will only get those things you need. Better yet, if you have a complete meal plan and a checklist to go with it, you can curb inflation and hunger.

Negotiate Bills
Here's something we don't always think we can control or change. Negotiate your utility bills, subscriptions, and interest rates. Negotiating your rent could save you hundreds of dollars, and many find this an effective way to put more money in their pocket each month.

Buy Secondhand
Why buy something at full price if you can find it lightly used for a fraction of the cost? This is usually the case with furniture that's so expensive to buy. Secondhand sites like Facebook Marketplace or a local classifieds site can be a gold mine for things you need and cheap, and you can find virtually anything you need there.

Delayed Gratification
To be honest, things are just plain expensive right now. Supply chains are still out of whack. It may be worth it to wait for the home renovation or that new car. If you don't absolutely need it right now, consider waiting until things calm down. When inflation does come back down to regular levels, you may just wish you waited to purchase that airline ticket to Bora Bora.

Higher Inflation or a Recession

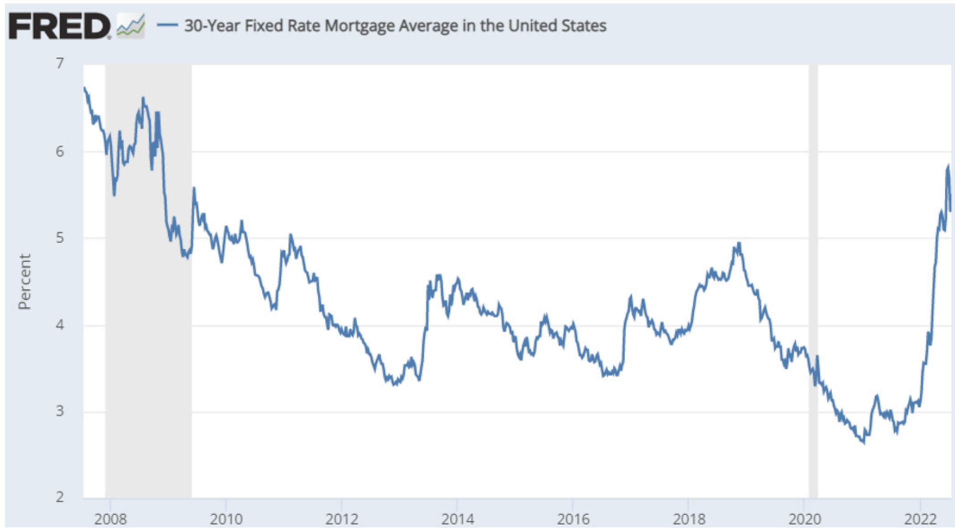
Only One Could Lead to Long-term Economic Prosperity

By James R. Derrick Jr., CFA®

There is a saying in economics that the solution to high prices is high prices. This works in two ways that overlap: supply and demand.

Supply: As prices rise, producers want more products to sell in order to make more money. The increase in supply creates extra. Then prices come down to entice buyers.

Demand: As prices rise, consumers may choose not to buy, which encourages sellers to lower their prices.



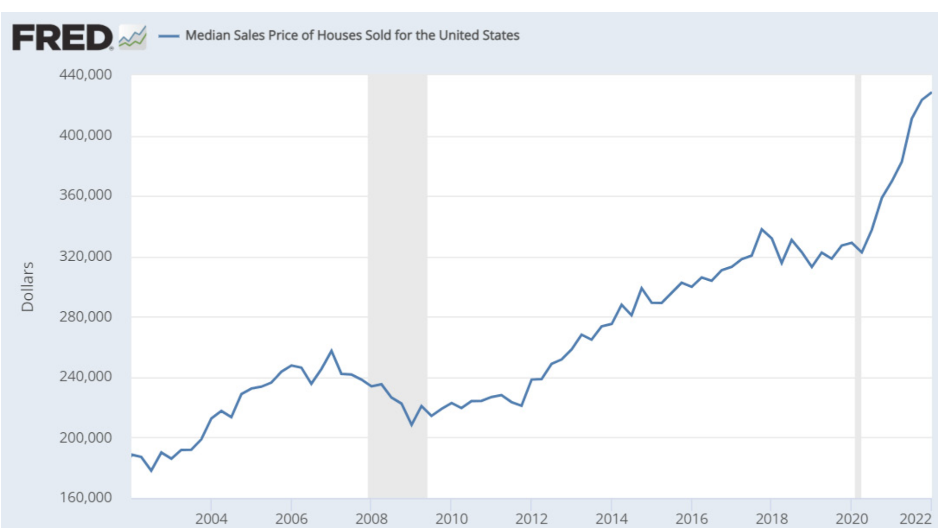
If prices come down eventually on their own, why does the Federal Reserve (Fed) raise and lower interest rates? Because once an upward (or downward) movement gets started, historically, they have been incredibly painful. If the Fed gets things right, it smoothes out the cycles.

In 2020 and 2021, when the government was doing its best to stimulate economic growth, the Fed believed that high prices were temporary and would solve themselves, and they have not, and the Fed is nervous.

Now, the Fed is determined to stop inflation. It has all the tools it needs. By increasing rates, the Fed will increase the cost to borrow and bring down spending, especially in areas sensitive to borrowing (housing).

The 30-year fixed rate is still low compared to October 1981, when it was over 18%. However, low rates in recent years have increased affordability, which has allowed home values to move higher. Now, affordability has never been worse.

A mortgage payment is based on the borrowed amount, the time horizon, and the interest rate. If the rate goes up and the time horizon doesn't increase, the borrowed amount must come down. This is where we are likely headed: If inflation doesn't come down soon, we may see home values decline substantially.



I believe we have already reached that tipping point where people are beginning to change their behavior. The Fed needs to make sure and will continue raising rates.

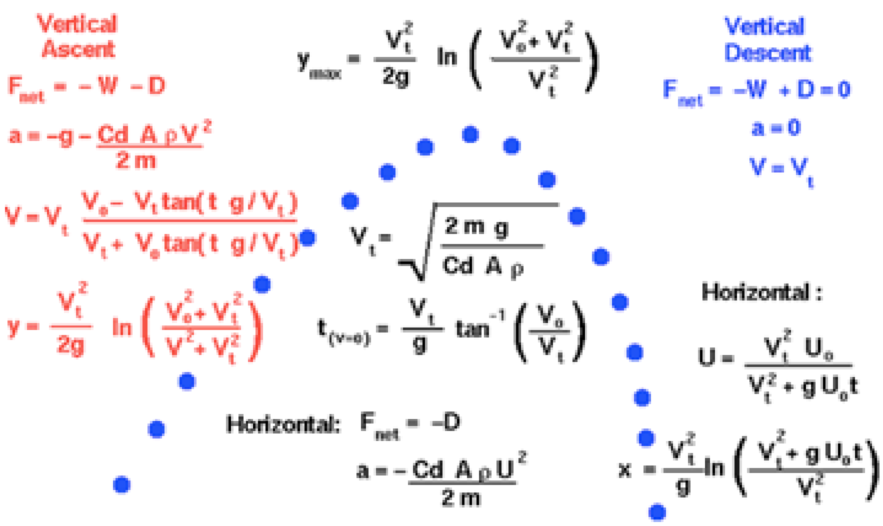
It is all part of a cycle we have seen many times before. Ultimately, we really want a balance of supply and demand. Even if it causes some short-term pain, the economy will grow better with low inflation.

Winning Reactions

By Jordan R. Hadfield, CFP®

First base was my position. I quit playing baseball in high school to pursue other opportunities, but a piece of my heart remains at first base even today. Knowing how to catch is probably the most important of the many skills required to play the sport.

To position yourself correctly to catch a pop fly, you must consider several variables, such as the speed of the ball, its height, and wind resistance. The formula required to calculate where the ball will land looks like this:



I have completed the process of catching pop flies thousands of times. Yet not once did I ever solve this complex equation. My coaches never taught quadratic functions at practice, and I have never purchased an algebra book at a sporting goods store.

Through experience and some common sense, catching pop flies becomes routine. One instinctively reacts to the situation in the way that gives them the best chance to succeed.

Recessions and bear markets are like pop flies in some important ways. They are inseparable elements in their respective worlds, and reacting properly is paramount to success.

Here are five winning reactions to recessions and bear markets. Like reacting to pop flies, these behaviors should be procedural. Excessive deliberation at each encounter would be similar to doing math on the ball field.

Reduce Excess Spending
A struggling economy can create problems on an individual level. Reducing excess and unnecessary spending is an important step to fortifying yourself financially. Review your budget and allocate funds to places that better serve you.

Minimize High-Interest Rate Debt
High-interest debt, such as credit cards, can chip away at your financial structure. Although there is never a good time to carry high-interest debt, heading into a market downturn could be the worst time. Minimize and pay off bad debt.

Evaluate your Emergency Fund
A distressed economy leads to higher unemployment. An emergency fund is designed to get you through those kinds of tough periods. Make sure you have a healthy emergency fund of 3-6 months of expenses; more if you feel necessary.

Continue to Invest
With great volatility comes great opportunity. More money is made after a down market than at any other time. Don't stop investing! A down market means a market on sale. It may be the best time to invest if you have extra cash, even though it's emotionally difficult.

Focus on the Big Picture
Don't get caught up in the bad investment news of the day. Markets have always had periods of volatility, and they have always recovered. New market highs are continually around the corner. Be patient and keep a long-term perspective.

Company stock down big?

By Mikal B. Aune, CFP®

If you have company stock inside your 401(k), you may have heard of Net Unrealized Appreciation (NUA). But, have you heard of Net Unrealized Depreciation (NUD)? At the end of the day, NUD and NUA could save you a lot in taxes. It is a great time to consider NUD since many stocks are down. To understand NUD, you first need to understand NUA.

NUA: The point of NUA is getting company stock out of your 401(k) at a lower tax rate. It works with stocks that are highly appreciated. Normally, any pre-tax money distributed from your 401(k) is taxed at an ordinary income rate, which could be as high as 37%. If you get part of that money treated as a long-term capital gain, the tax is only up to 20%, greatly reducing your taxes.

To get NUA treatment, you must hold company stock from your current employer inside your 401(k) or profit-sharing plan. You must have a qualifying event like separation from service, turning age 59 1/2, disability, or death. The stock must be distributed in-kind to a brokerage account. The other holdings in the 401(k) must be disbursed in the year of the NUA transaction. You can roll over the remainder of the holdings to an IRA to avoid taxation on that portion. At the end of the year, the 401(k) balance must be zero. Typically, the distribution happens after age 59 1/2 to avoid the 10% early withdrawal penalty on the basis.

The strategy will increase your current year's tax liability as you will have to pay tax on the basis (Basis = the price at which you bought the stock). To avoid selling stock, you must have cash on hand to pay the taxes when you file your tax return the following year. However, the growth, or Net Unrealized Appreciation, won't be taxed until you sell the company stock from your brokerage account. The good news is, "The net unrealized appreciation will always be taxed at long-term capital gains rates, regardless of the actual holding period of the stock inside the plan."*

NUA Example: Let's say your company stock has really grown in value. You purchased 10,000 shares of stock inside the 401(k) at $1. The stock is now worth $100 per share or $1M total value. If you take out the $1M, you will have to pay ordinary income tax rates of up to 37% or $370,000. If you transfer the shares to a brokerage account as an NUA transaction, you will need to pay taxes immediately on the basis of $10,000, or about $3,700. In the year you sell the stock, you will owe long-term capital gains taxes. Your remaining $990,000 would be taxed at 20%, or $198,000. The total tax would be $201,700, saving about $168,300 in taxes!

NUD: However, what happens if your company stock is down significantly from its high? You wouldn't seek NUA treatment because your basis is higher than the current value. You would just take it out and pay ordinary income tax rates.

Enter Net Unrealized Depreciation. If your company stock has suffered recently, like many stocks, now is a great time to choose to lower your cost basis on your company stock. This seems counterintuitive since outside of a 401(k), you want the highest basis possible as you have already paid taxes on the basis. However, inside of a 401(k), you haven't paid tax on the basis. If you can lower your basis, then you can potentially lower your future tax burden.

NUD Example: Let's say your company stock was worth $100, and you forked out $1M to buy 10,000 shares. Now the stock has tanked and is only worth $1 per share. (Ouch!) If you were over 59 1/2 and took out the $10,000, you would pull that out and pay ordinary income taxes. However, if you aren't over 59 1/2 or retiring soon, you can really benefit. You can log into your 401(k) portal, sell your company stock, and then buy it back the next day. This will reset the basis. Outside of a 401(k), buying back the same stock the next day is not allowed as it is considered a "wash

Continued on next page

*Source: www.kitces.com/blog/net-unrealized-appreciation-irs-rules-nua-from-401k-and-esop-plans/

sale." But inside the 401(k), it is allowed and does not cause a taxable event. Before selling stock, confirm your provider allows you to trade daily and doesn't lock you out for 15 days or limit stock purchases.

The purpose of NUD is to set up a future NUA. Keep in mind that investing involves risk, and there is no guarantee your company stock will increase in value. Also, note that it can only be stock for the company where you work. You can't just buy an individual stock, like Qualtrics (XM) or Domo (DOMO), and then do NUD or NUA unless you actually work for Qualtrics or Domo, respectively.

This is a complex financial transaction with caveats and considerations. It is best to consult with a qualified financial advisor and accountant. If done correctly, you could potentially save yourself a ton in taxes, keeping more of your hard-earned money. If this is something you think will work for you, call us today to talk it through.

Economic Cycles & Personal Finance

By Lori B. Taylor, CFP®

In the first chapter of the Personal Finance textbook currently used at the University of Utah, we are introduced to a macro-economic concept known as the Business or Economic Cycle. The textbook claims that success in personal finance depends in part on how well we understand the economic environment. Certainly, it is comforting to recognize a regularly repeating pattern.

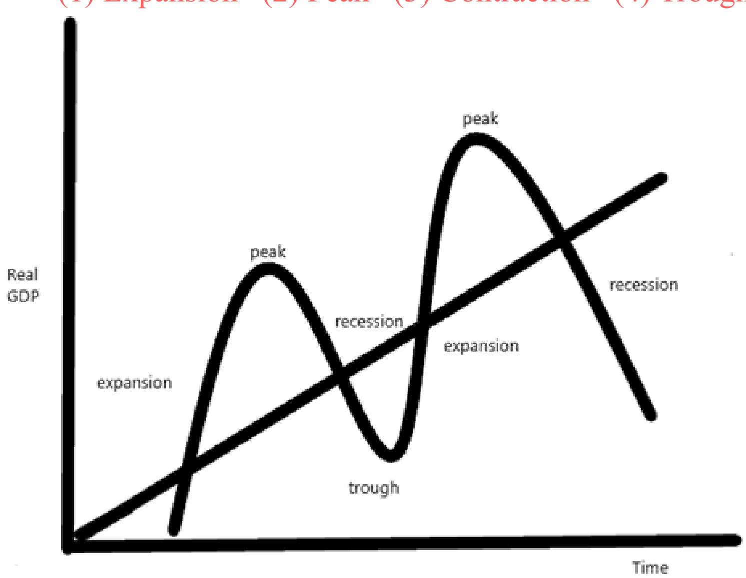
The current situation will not last forever, whether contraction or expansion. If we are paying attention to the trend, we are better focused on saving during expansion times to protect ourselves during approaching downturns. We can also position ourselves to take maximum advantage of expansions. If we are investors, we recognize that this latest shock is not a surprise but part of a cycle that will work itself out and start again on recovery and expansion. The best thing an investor can do is keep their long-term goals in mind, stay invested, and wait for the next expansion. Most expansions last far longer than contractions so that economic growth trends upward.

Phases of an Economic Cycle

(1) Expansion (2) Peak (3) Contraction (4) Trough

Average Cycle
5.5
Years

Average Expansion
4.7
Years



Longest Expansion
12
Years
2009-2020

Longest Contraction
18
Months
2007-2009

Determining Factors
GDP, Interest Rates, Employment, Consumer Spending

Internal Pressures
Supply & Demand, Money Supply, Macro-Economic Policy

External Pressures
Wars, Natural Factors (Pandemic), Population Growth, Shocks

Source: National Bureau of Economic Research. "US Business Cycle Expansions and Contractions." Accessed Feb. 3, 2022

Your SFS Team

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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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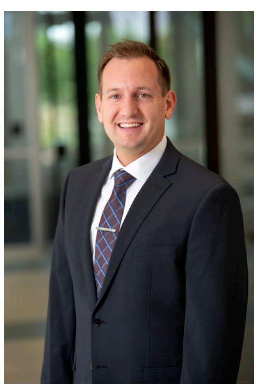
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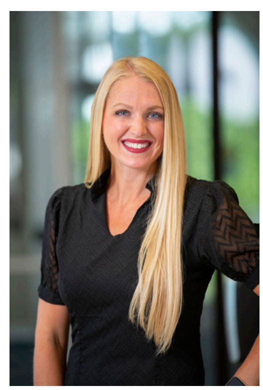
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