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Life. Investing. And Everything in Between

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A Crisis of Confidence

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Have you ever reflected on the foundation of the financial system? What comes to mind? Banks, investors, the stock market, the bond market, or the credit markets? That's partially true.

They are the underpinnings of this system, but the foundation or the bedrock of the financial system is confidence. Without confidence, we are left in a very precarious situation.

Of course, we want to have full confidence that when we withdraw cash from a bank account or money market fund, or for that matter, close out an account, we will have immediate access to those funds.

But bank vaults aren't filled with cash that can be easily repatriated to depositors if, by an incredible long shot, everyone shows up one day to close their account. Our deposits are invested in high-quality bonds, Treasury bills, and loans.

What happened at Silicon Valley Bank last month was simply an old-fashioned bank run. Why? Confidence quickly evaporated.

But the root cause of its demise had many regulators, investors, and Fed officials scratching their heads because nearly everyone was caught off guard. Which I find surprising, however hindsight is 20/20.

A far cry from 2008…but, what happened?

OK, this is NOT 2008. Then major banks were saddled with bad real estate loans. This time, a regional bank in California, Silicon Valle Bank (SVB), invested heavily in a portfolio of high-quality, longer-term Treasury bonds. From a credit standpoint, these are super-safe investments. What could go wrong?

Well, nothing if the bonds were held to maturity or if interest rates had remained stable.

Bond prices and bond yields move in the opposite direction. When yields rose, the bonds fell in value, creating a paper loss.

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But SVB's customer base was unlike the majority of other regional banks in our country. Their customers were venture capital investors who had been drawing down on their deposits as more traditional sources of funding were drying up.

With deposits being drawn down, SVB was forced to sell [$21 billion in bonds], and the bank took a nearly $2.0 billion loss. SVB's hastily announced plan to raise capital was quickly scuttled when it stock tumbled, and depositors quickly began to withdraw cash, since a large majority of the bank's deposits were above the FDIC limit.

Less than two days after the bank revealed its loss on the sale of Treasuries, regulators were forced to shut the bank.

Time to failure: less than 48 hours from a late March 8th announcement of its plans to raise capital and a morning shuttering on March 10th.

Moreover, Signature Bank, which was heavily into the cryptocurrency space, was closed on Sunday, March 12th.

SVB and Signature were the second and third largest bank failures in U.S. history, respectively.

Regulators did not have the time to line up buyers, and the FDIC moved to guarantee all bank deposits of these two failed banks.

As controversial as it was, Treasury and Fed officials fretted over the potential of massive bank runs when markets opened on Monday.

It's difficult to estimate the carnage we might have seen on Monday morning, but the plan to ring-fence the banks with deposit guarantees and a new lending facility from the Federal Reserve helped contain the crisis and prevent contagion.

The new lending program called Bank Term Funding Program enables banks with high-quality bonds to borrow against the full value (par value, not current value) of their bonds, using the bonds as collateral. In theory, there is no need to sell the bonds.

As the month came to a close, worries began to subside, and it was reflected in most of the major market indexes.

Table 1: Key Index Returns

	MTD %	YTD %
Dow Jones Industrial Average	1.9	0.4
NASDAQ Composite	6.7	16.8
S&P 500 Index	3.5	7.0
Russell 2000 Index	-5.0	2.3
MSCI World ex-USA**	1.7	7.2
MSCI Emerging Markets**	2.7	3.6
Bloomberg US Agg Total Return	2.5	3.0

Source: Wall Street Journal, MSCI.com, Bloomberg
MTD returns: February 28, 2023 – March 31, 2023
YTD returns: December 30, 2022 – March 31, 2023
**in US dollars

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The Fed broke something.

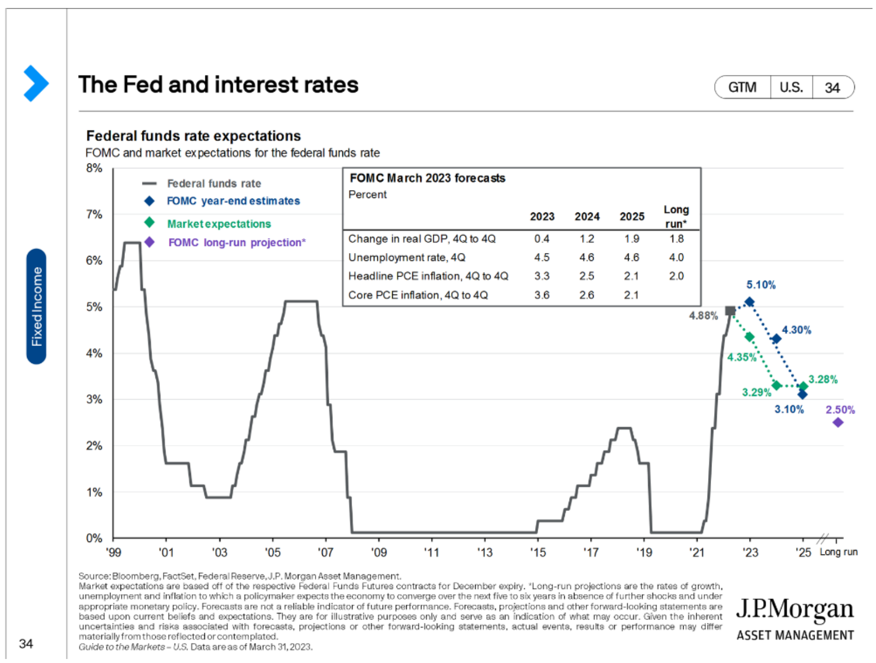
While way back in 2008, the financial crisis started with subprime lending. Fast forward to today and a perfect storm of banks' mismanagement of assets like loans and bonds paired with rate hikes from The Federal Reserve has made for some serious financial turbulence.

Banks such as SVB piled into high-quality, long-term bonds but didn't hedge against the possibility of a rapid rise in interest rates. Rising interest rates exposed a fatal flaw in its portfolio. Hedging against interest rates probably would have offset the change in their bond portfolio's value. Again, hindsight is always 20/20, right?

So, what happens next? Regulators will need to dive into the details for a more thorough understanding of what happened, but the finger-pointing has already begun.

Nonetheless, the impact may be felt for quite some time.

Prior to SVB's shenanigans, The Fed was probably on track to boost the fed funds rate by 50 basis points (bp, 1 bp =0.01%) to 5.00%- 5.25% at its March meeting.



As I am writing this newsletter, inflation remains stubbornly high, but the Fed wisely chose to defer to banking stability, and opted for a cosmetic hike of 25 bp.

It gives the appearance that inflation remains a priority, while focusing on the banking system.

It also puts the Fed in a difficult position, as it hopes to tackle two conflicting goals: fighting inflation with rate hikes, which would put added stress on banks, or concentrating on financial stability.

The crisis might do the Fed's job for it, as tighter lending standards slow economic growth. In fact, this week, I spoke to a client and friend who works for a local regional bank. He confirmed that since these events occurred, lending has indeed become more difficult. Bankers are paying attention.

How much can tighter lending standards slow economic growth? No one knows.

Inflation hasn't been squashed, but problems with SVB has not spread to other banks. The crisis eased as the month came to a close, and most of the assets of the failed banks were purchased.

In recent days, sentiment has shifted on rates, but sentiment is ever shifting. How the Fed reacts this year will depend on economic performance.

As March came to a close, fears waned, helping the market to rally, allowing March to end on a favorable note.

Managing your Social Security

Social Security has always been one of my favorite things to help our clients understand.

First, a little background …On January 31, 1940, the first monthly Social Security check was issued to Ida May Fuller of Ludlow, Vermont. Miss Ida, known around Ludlow as "Aunt Ida", worked for three years under the Social Security Program. The accumulated taxes on her salary during those years was a total of $24.75. She received $22.54. Before passing away in 1975, she collected $22,888.92 in Social Security benefits.

Interesting trivia aside, many younger folks have little faith that Social Security will be there for them when they retire. According to Northwestern Mutual's 2020 Planning and Progress Study, nearly 75% of Gen Z (born after 1996) believe it's somewhat likely or not likely at all that they will receive benefits.

The program that began nearly 100 years ago is heading toward insolvency. However, that does not mean monthly checks will disappear. Instead, benefits would be reduced by about 21% if no action is taken. This reduction would balance the inflow of taxes with the outflow of payments.

The Social Security trust fund for retirees will run out of funds in about 10 years if Congress does nothing. I find it hard to believe that Congress will not act. Currently there is legislation that would expand benefits and ensure Social Security is fully funded for the next 75 years. But legislation is legislation and politics is … well, you know… politics.

That being said, we can't control how Congress addresses a funding shortfall. We advise you to control what you can control, and preparing for benefits is of paramount importance.

Social Security wasn't designed to replace all of your income, but coupled with retirement savings, it will provide you with additional support.

Besides, you've paid into the program your entire working life. When the appropriate time comes to receive benefits, you deserve your monthly check.

Types of Social Security

1. **Retirement benefits**. These are the benefits most of us are familiar with. The earliest you may receive a monthly payment is age 62. The full retirement age is between 66 and 67. It's rising to 67 for those who were born in 1960 and after.

   So, when should you grab your benefit? There's no hard and fast rule, but the best guideline is to wait as long as you can. The longer you wait, the greater the benefit, up to 70.

   For example, if you are born in 1960, you'd receive 70% of the full retirement benefit at 62. That amount rises to 75% at 63, 80% at 64, 86.67% at 65, 93.33% at 66, and 100% at 67. Continuing on, 108%, 116%, and 124% from 68 to 70.

   That higher or lower benefit lasts for the rest of your life and increases with annual cost-of-living adjustments based on the rate of inflation.

   Simple math tells us that someone who receives a 5% cost-of-living adjustment on a $1,500 per month payment will receive a smaller increase than someone with a $2,000 payment. Those annual increases (assuming inflation is above zero) compound for a lifetime.

   If you are married, you have other items to consider. At full retirement age, you can take either 100% of your own retirement benefits or 50% of your spouse's, whichever is higher.

   If you are divorced and you were married for 10 years or more, you can receive benefits based on your ex-spouse's Social Security record (up to 50% of their full retirement benefits). This won't affect your current spouse's benefit if you have re-married.

   If you're widowed, you can receive either your own retirement benefit or up to 100% of your spouse's benefits, whichever is higher.

These are guidelines and are designed to provide you with a broad understanding of Social Security basics. We are happy to work with you and refine your approach.

So, let me give you an example of how we recently helped one of the families we work with.

Bob, who is 63, and Linda who is 57 asked me when they should start taking their social security. Bob is going to retire this July 2023 and will have a pension from his employer. Linda is still working and intends to retire when she turns 62.

We have a terrific Social Security Planning Tool that helped us run Social Security Income scenarios so our clients can make an informed decision about the strategy that fits their needs the best. Here are the details of each scenario:

Scenarios

1. Both Claim Early

The goal of this scenario is for each spouse to claim at age 62 or as early as possible afterwards.

Strategy:
Apr 2023: Bob claims on own record at **age 63** starting at **$2,750**.
Oct 2027: Linda claims on own record at **age 62** starting at **$2,161**.
Dec 2047: Linda claims survivor benefits at **age 82** starting at **$4,423**.

Lifetime **nominal** benefit : **$2,222,388**

2. Both Claim at FRA

The goal of this scenario is for each spouse to claim at full retirement age (FRA) or as early as possible afterwards.

Strategy:
Mar 2026: Bob claims on own record at **FRA (66 + 10 mo.)** starting at **$3,623**.
Sep 2032: Linda claims on own record at **FRA (67)** starting at **$3,369**.
Dec 2047: Linda claims survivor benefits at **age 82** starting at **$5,491**.

Lifetime **nominal** benefit : **$2,559,212**

3. Both Claim Later

The goal of this scenario is for each spouse to claim at age 70 or as late as possible.

Strategy:
May 2029: Bob claims on own record at **age 70** starting at **$4,819**.
Oct 2035: Linda claims on own record at **age 70** starting at **$4,458**.
Dec 2047: Linda claims survivor benefits at **age 82** starting at **$6,882**.

Lifetime **nominal** benefit : **$2,864,885**

4. Linda Claims Early, Bob Claims Later

The goal of this hybrid scenario is for the lower-benefit spouse to claim as early as possible and the higher-benefit spouse claim as late as possible.

Strategy:
Oct 2027: Linda claims on own record at **age 62** starting at **$2,161**.
May 2029: Bob claims on own record at **age 70** starting at **$4,819**.
Dec 2047: Linda claims survivor benefits at **age 82** starting at **$6,882**.

Lifetime **nominal** benefit : **$2,769,013**

5. Maximum Lifetime Nominal Benefit

The goal of this scenario is to search all possible filing strategies and find the one that yields the maximum combined lifetime benefits.

Strategy:
May 2029: Bob claims on own record at **age 70** starting at **$4,819**.
Dec 2034: Linda claims on own record at **age 69** starting at **$4,136**.
Dec 2047: Linda claims survivor benefits at **age 82** starting at **$6,882**.

Lifetime **nominal** benefit : **$2,867,224**

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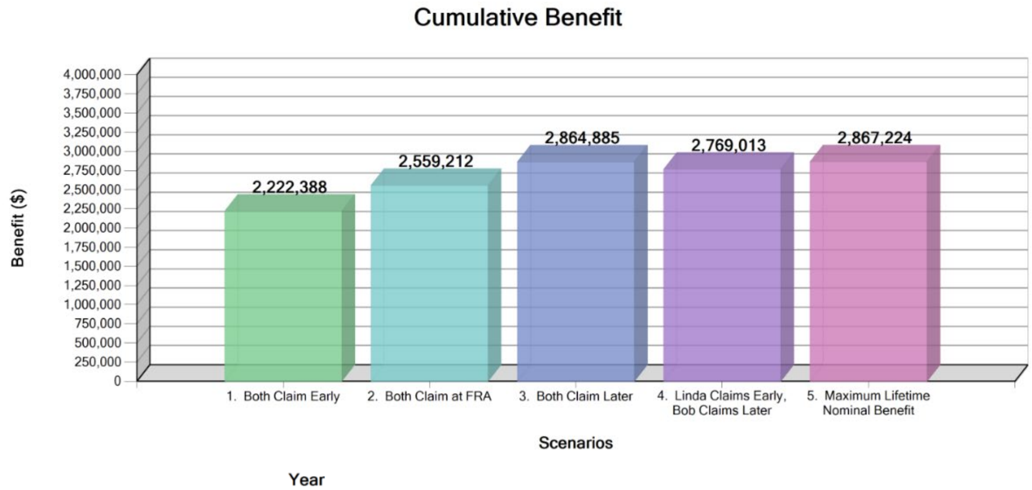
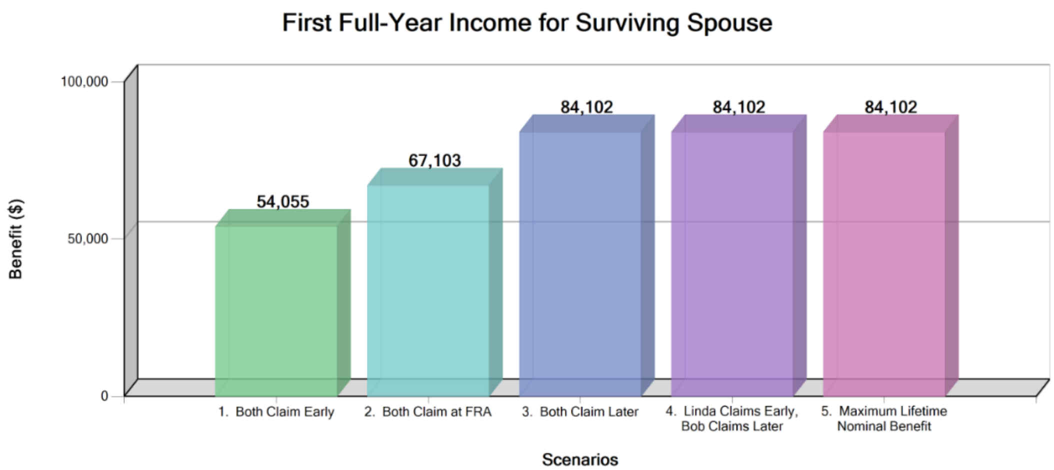
Here is what they can expect depending on which scenario they decide to go with:



Here is what they can expect after the first Full-Year of Income for the surviving spouse:



Wow! I love working with this planning tool. It has helped so many of our families make educated Social Security Income decisions!

And FYI - **I will be hosting a webinar in April called "Savvy Social Security Planning: What Baby Boomers Need to Know About Their Retirement Income".** Keep your eyes open for the invitation in a couple of weeks so that you can register if you want to know more about this topic.

Ok, a brief mention of other benefits. The Social Security has a terrific glossary of terms related to your benefits.

2. If you meet the requirement, usually work experience between five and ten years, **Social Security Disability** may be available to you if you have a severe medical impairment (physical or mental) that's expected to prevent you from doing "substantial" work for a year or more or have a condition that is expected to result in death.

3. **Dependent benefits** may be available to your spouse or dependent. Minor children may also qualify for benefits, depending on the worker's income.

4. If you are the surviving spouse of a worker who qualified for Social Security retirement or disability benefits, you and your minor or disabled children can be entitled to **survivor benefits** based on your deceased spouse's earnings record. As a widow or widower, you may begin to collect benefits once you reach age 60, or age 50 if you have a disability that prevents you from working.

   Children qualify if they are unmarried and under age 18, under 19 but still in school, or 18 or older but they were disabled before age 22.

Final thoughts

It's important to check your earnings history. Your benefit is calculated using the highest 35 years of earnings, so it is **VERY** important that your earnings record is accurate.

You can verify your earnings history, its accuracy and much more through a personal My Social Security Account: https://www.ssa.gov/myaccount/ And it's simple to set up. If you find a discrepancy in your earnings history, you can get it changed. If you do find a discrepancy, here is a link to help.

We understand that Social Security may be complicated. There are various paths you can take to maximize your benefits, and we are here to guide you through the maze.

Let me know if you have any questions or would like to discuss your personal situation.

I am sure you can tell that I love this stuff! I want these monthly letters to leave you a little more educated and comfortable with current events and important retirement topics.

As always, if you are a client, Thank you! I recognize that you have many advisors to choose to work with. That you have chosen our firm, we are honored and humbled for the opportunity to serve as your financial advisor. If you are not one of our client and would like to chat about our unique client experience, I would be very happy to meet with you!

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All the best,

Kelly