2023 2nd Quarter Financial & Investment Management General Commentary

A look at the Market

Where are we today?

Let's begin with a historic view as it relates to current market conditions.

Conventional wisdom on the history of the stock market would tell you the longest bull market in history was 1982 to 1999. What people miss who express this opinion is that in 1987 the stock market fell over 25% before it rallied back to be up for the year. So, the actual longest bull market in history is from 2009 to 2021, 13 years. The annualized return of the S&P 500 index was 16%. The stock market ended 2022 down 18% but was down over 25% earlier in the year. During this bull market run the composite data compiled by our research partner of our dividend strategy reflected a compounded annual return of 10.9%. This is certainly lower than the index, but this was still well ahead of all of our client's financial plan needs. Additionally, this was accomplished with less volatility and without hitting the lows that the indexes reached when they were down. For this reason, we like the slow and steady approach rather than overreaching for returns and suffering the swings of the market.

Although the quarter and 1-year returns are positive, given the historical view, it is important to look at longer term returns and take volatility into consideration. Short term returns can vary from any index viewed, but the ultimate goal is to meet long term targets. Portfolios are set up for a reasonable return with a reasonable risk. This means not chasing returns and holding a diversified portfolio. Looking at a single index like the S&P 500 gives a false sense of how an overall market is performing given the variety of asset classes available and many of those are built into our portfolio models.

Looking ahead

Perhaps the best indicator at any point in time on the future return of the stock market is relative price. When stocks are cheap, you can get great future returns, but when stocks are expensive, future returns are low. The price to sales ratio is the best indicator of whether stock prices are cheap or expensive. Now it is true that most people like to use price to earnings ratios, but we believe earnings can be manipulated more easily than sales. We have 120 years of price to sales data, and with the help of our research partner, we compared the price to sales ratio at year end last year to the history we have. What this showed was that the price to sales ratio of the S&P 500 as of 12/31/2022 was in the top 5% of price to sales ratios over this 120-year history, expensive by anyone's standard. We wondered if perhaps our data was actually for too long a period. Perhaps an odd thing to consider, but remember 120 years ago was 1903 and a lot has changed since then. So, we took out the bottom half of price to sales data whenever it occurred. What this left us with was 60 years of price to sales data but spread out over 120 years. The result did not change, the price to sales ratio in this methodology was still in the top 5% of the 10-year history.

On any measure, one does not want to be aggressively investing when we are in the top 5% category, regardless of how one calculates the top 5%. So, that is where we are, stocks are expensive. While this is clearly a time for caution, it is not a time for burying your head in the sand. Our dividend strategies will provide reasonable returns over the next decade just like they did in the 2000s even if the index is flat.

ST. JOHN & ASSOCIATES
INTEGRATED FINANCIAL SERVICES

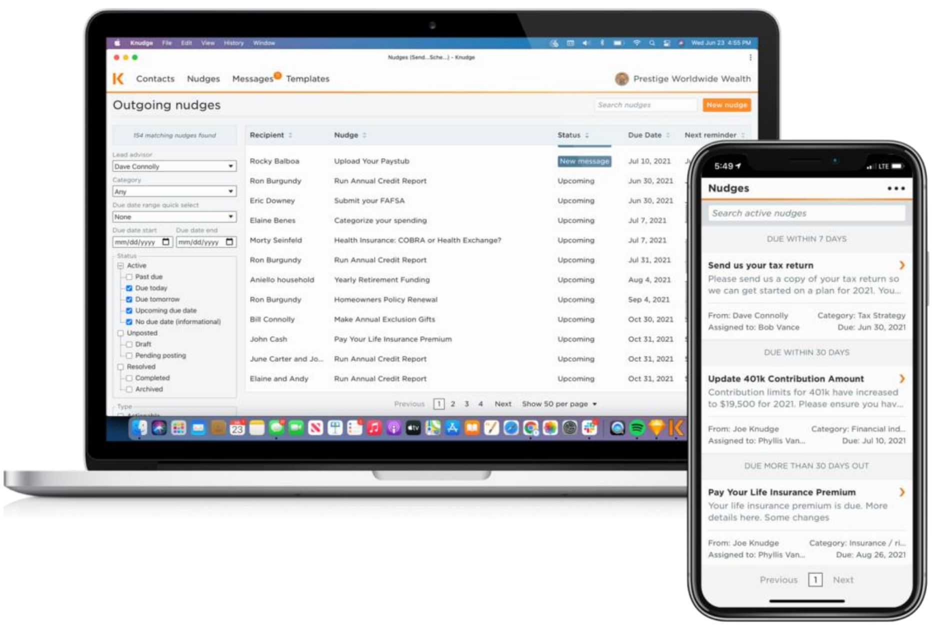
FINANCIAL SERVICES

Introducing a new client service

We wanted to find a way to help our clients take part more easily and effectively in the financial planning and investment planning process. We need to have documents signed, there are deadlines for required actions, tax returns need to be forward to us, financial planning goals need to be updated, and more…much more. Clients need an easy way to keep up with it all in order to optimize our service to you. The answer? **Knudge**.

Knudge is an email and/or text messaging system that allows us to program in to-do and open items and then share them with you. It helps all of us get stuff done. Knudge sends reminders to you at optimal times to increase the likelihood of an action being taken on time and keeps a record of our progress. We will be rolling out Knudge over the course of this year beginning with those full-service clients with the most needs. We will send you an invitation to join so you don't have anything you need to do at this time.

You can learn more by following this link then clicking on *Unsure What Knudge Is?*



Recent Updates of Our Website

Our website has been completely revised and we ask you to take a moment and have a look.

Through the services of Street Studio Creative and Kalaila Spearman we have made the site more interactive, easier to navigate and contains a refresh of the entire content. We would like to bring your attention to the Blogs, Newsletter and Prior Quarterly Commentary it contains as Sarah Crawford posts new materials periodically under the INSIGHTS tab. A great place to revisit periodically.

FINANCIAL PLANNING

Proposed legislation would apply Social Security tax to all income

Will Social Security benefits really fall in 2034? As the projected year of the OASDI Trust Fund exhaustion draws nearer, interest is growing in how this math problem will be solved. One is testimony by SSA Chief Actuary Steven Goss to the Senate Budget Committee. Another is a bill by Sheldon Whitehouse and Brendan Boyle called the "Medicare and Social Security Fair Share Act." And a third is a revision to John Larson's "Social Security 2100 Act," which extends the sunset date of its provisions to 2034 from 2027, extending solvency to 2066.

Read more:

- Steven Goss Testimony
- Social Security 2100 Act
- Medicare and Social Security Fair Share Act

Estate planning 101

While many prefer not to think about it, creating a legally binding plan to distribute your assets after your death provides you with peace of mind. You can rest easy knowing that your wishes will be carried out as you have requested.

While we encourage you to sit down with a legal professional, we also want to provide some general guidelines you can think through independently. Estate planning is a complex field, but a general outline can clear up some of the mystery.

What do you want to accomplish? Will you be providing for children under 18? Or to your beneficiaries' young adults, older adults, relatives, or charities? Exactly how might you provide for your children?

Options you may consider include a trust and/or a will.

What is a trust? Trusts provide control over the distribution of assets, provide privacy, and have potential tax advantages. A trust is a fiduciary arrangement that allows a trustee to hold assets on behalf of a beneficiary or beneficiaries. Trusts can be arranged in many ways, specifying exactly how and when the assets pass to the heirs.

Are you concerned that a young adult might fritter away his or her inheritance? A **spendthrift trust** might be the answer. Instead of an account that allows immediate access to the assets, the trustee of a spendthrift trust dispenses the assets over time.

Is there a need to minimize taxes? An **irrevocable trust** might fit into your plan. By placing assets into an irrevocable trust, the estate's value is reduced regarding estate taxes. Besides tax considerations, irrevocable trusts also help protect assets in lawsuits.

You may also decide to create a **living trust**, which transfers your assets to your beneficiaries and avoids probate.

Other trusts that you may find advantageous include charitable trusts, special needs trusts, generation-skipping trusts, and bypass trusts. The latter two offer ways to reduce the estate tax.

You should also consider a will. A will is a legal document that takes effect upon your death. It outlines your wishes, including provisions for guardianship of your minor children.

Have you taken stock of your possessions? It's important to create an inventory of your assets, such as bank accounts, insurance policies, investment accounts, and personal belongings.

Don't avoid the difficult conversation. If you were to pass away suddenly, do your loved ones have access to important documents, financial statements, etc.? It is important to inform your loved ones about the location of your will and the legal professionals who will handle the process.

Choose the right executor or trustee. Select a trustworthy individual or institution to act on your behalf. You need someone dependable, trustworthy, organized, fair, and financially savvy. Identifying the best candidate can be made easier if you focus on these important attributes.

Be sure to designate and regularly update your beneficiaries. It's common to list a beneficiary or beneficiaries for IRAs and life insurance policies.

Prepare for medical decisions. Estate planning isn't complete unless you prepare legal documents such as a durable power of attorney for financial matters and a medical power of attorney for medical decisions. It is crucial in the event you are incapacitated.

Update your estate plan regularly. Life is full of unexpected turns. Milestone events such as marriage, divorce, births, and deaths can significantly impact your wishes and create gaps in your plan.

Latest College Net Prices

When looking at college prices, what matters is the net price a family pays. You can derive the net price of a college for your family by subtracting any grants and/or scholarships in an award package from the cost of attendance.

You can see average net prices at hundreds of private and public colleges and universities with a new downloadable spreadsheet that The HEA Group produced after analyzing the latest U.S. Department of Education cost figures. FYI, the founder of The HEA Group was previously in charge of the federal government's College Scorecard, which aims to bring transparency to the higher-ed industry.

College majors and future salaries

The HEA Group also used the most recent U.S. Department of Education numbers to create a spreadsheet that shows the median salaries of alumni four years after graduating at nearly 37,000 academic programs at individual colleges.

The good news is that most graduates are earning more than $40,000 a year. Out of 36,096 programs with earnings data available, nearly two-thirds show the majority of their graduates earning at least $40,000 four years later.

Nearly 5,000 college programs, however, show the majority of graduates earning less than $30,000. And alarmingly, alumni of 1,010 of programs are earning less than $20,000.

The gulf between the haves and have nots is glaring. At or near the top of the median earnings heap are computer science majors at Harvard, MIT, Carnegie Mellon and the University of Pennsylvania, who are earning close to or exceeding $250,000 a year.

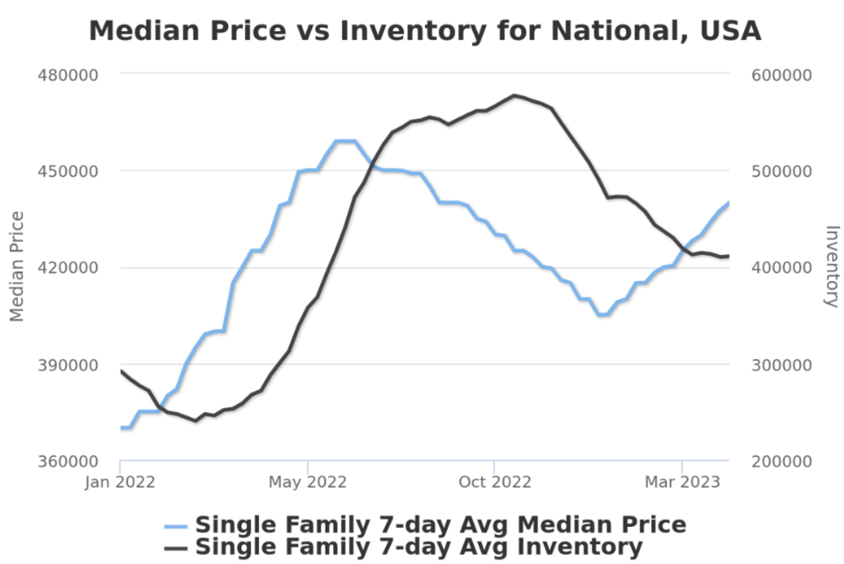
Near the bottom of the earnings ladder are music majors at New York University and Johns Hopkins University, who are eking out a median salary of $18,600 a year! And the cost of attendance at these two institutions is $81,000 or higher!

Too many parents and teenagers assume that if you get into a well-regarded university, a good or even great salary will follow. That is absolutely not true. What matters, regardless of the school chosen, is the ultimate major.

If you download the spreadsheet, you will see endless examples of this reality. For instance, at Penn State University, civil engineers and electrical engineers earn salaries of $74,766 and $83,362 respectively, but experimental psychology majors and rhetoric/composition majors earn just $37,289 and $21,323 respectively.

It’s important that families understand this reality when looking at potential schools and majors.

Housing Market Tracker



The nation's housing industry has entered a new normal in which the dynamics of the market appear perplexing - marked by high mortgage rates and high home prices, along with shrinking mortgage originations.

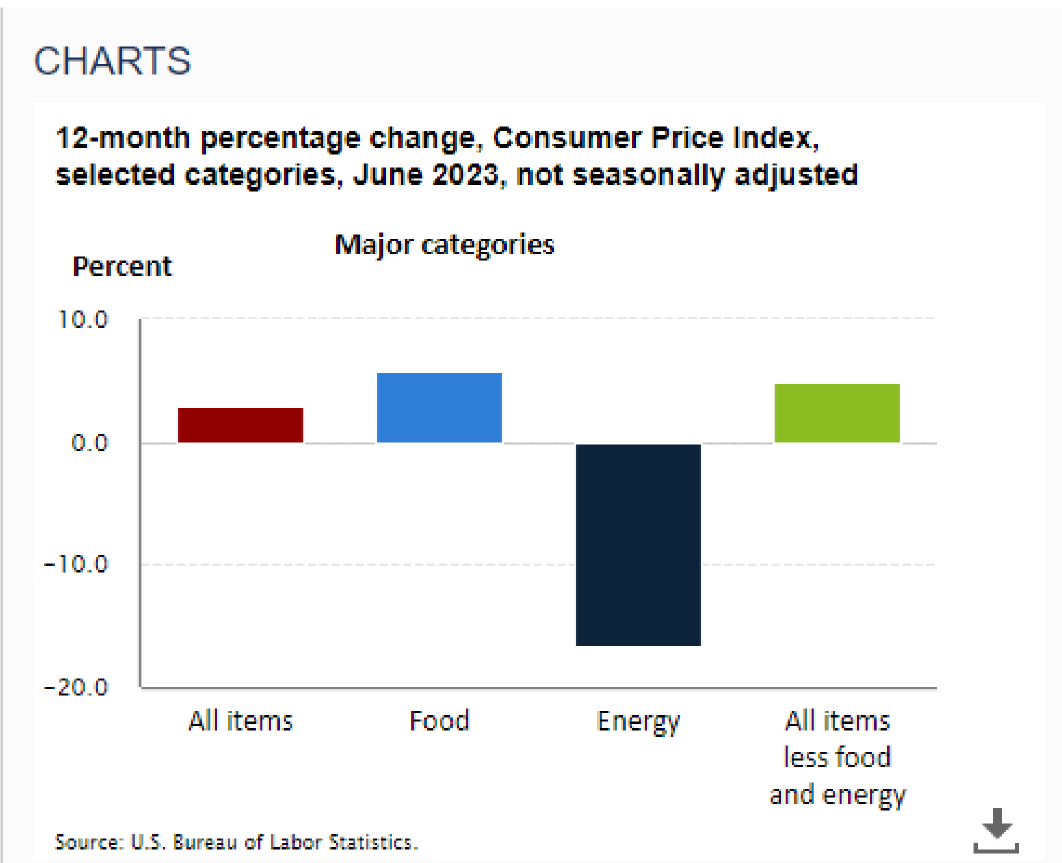
The perplexing part: Why are home prices not declining in this environment? It boils down to two factors, a lack of housing inventory or supply; and high demand for that limited housing stock which also is fueling a jump in new-home sales.

This is a trend that has prevailed throughout the first half of the year, and without a significant uptick in for-sale inventory, or another massive shift in the market, is likely to continue.

FINANCIAL MARKETS

CPI

In June, the Consumer Price Index for All Urban Consumers increased 0.2 percent, seasonally adjusted, and rose 3.0 percent over the last 12 months, not seasonally adjusted. The index for all items less food and energy increased 0.2 percent in June (SA); up 4.8 percent over the year (NSA).



While inflation has slowed down in the past couple of months, the reality is that we have already had consumer price increases. The fact that the growth rate is beginning to flatten does not take away the increases we have had over the past 2 years. Those price increases seem here to stay.

The Fed has been raising interest rates in order to stem the growth of inflation, not reverse it, but this comes with a price as it is actually a negative to the economy. It not only incentivizes consumers to spend less, but the extreme rise of interest rates has created problems for major purchases like cars and homes. Except to the larger companies that are flush with cash, rising interest rates are stifling business expansion removing the availability of capital or making capital so expensive, it is cost prohibitive to borrow money.

This cost of borrowing mixed with the increased costs to produce good, caused from inflation and the consumer being forced to spend less will eventually have a negative effect of corporate earnings. We have already seen companies trying to cut costs through hiring freezes and layoffs.

Inverted yield still pointing to a recession

An inverted yield curve shows that short-term interest rates are higher than long-term interest rates.

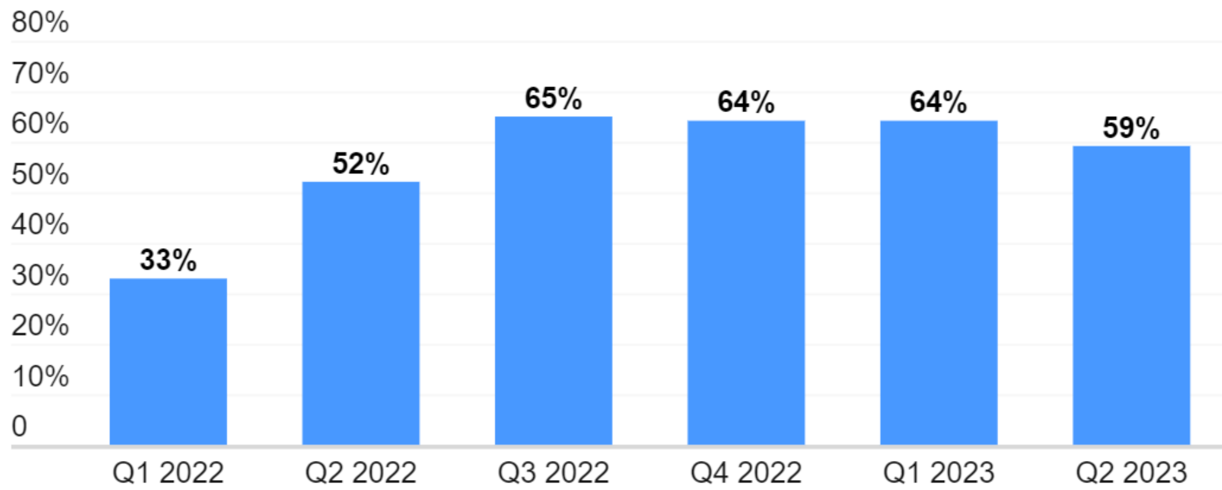
In an article by Reuters dated July 7, 2023, it states that: "Expectations of another rate hike by the Federal Reserve to tame stubbornly high inflation helped push a closely watched part of the U.S. Treasury yield curve to its deepest inversion since 1981 on Monday, once again putting a spotlight on what many investors consider a time-honored recession signal."

This phenomenon is closely watched as an indicator as it has preceded past recessions.

There is still an expectation that the Fed will be raising rates 1 to 2 times more this year pushing short term rates higher.

Should I be worried about a recession?

The yield curve remains inverted which has historically been an indicator of a recession and economists say a recession is more likely than not; however, a resilient economy has pushed those forecasts out further into the horizon, while the odds of downturn have retreated slightly. This is illustrated by the chart below showing responses from expert economists regarding percent chances the economy will contract within the next 12 to 18 months. It is down slightly.



Note: Figures reflect average forecast among respondents.
Source: Bankrate Second-Quarter Economic Indicatory survey, July 2023

Ultimately. we are not out of the woods regarding a recession and this will come down to the results from the existing tightening that has been done so far.

Correction vs. bear market vs. recession

A bear market is a decline of 20% or more in stock prices usually over a sustained period of time, typically two months or more, but there is no hard number.

A correction, on the other hand, is a shorter-term market downturn, usually over a timeframe of less than two months. It is a drop of less than 20% in major stock indices.

Although U.S. stocks are in bear market territory, this is not the same as an economic recession. To clarify, an economic recession is typically defined as two consecutive quarters of declines in quarterly real (inflation adjusted) gross domestic product (GDP). Technically we are in a recession based on the GDP alone, but the argument of high employment has given controversy as to if we are actually in a recession yet. As we discussed above, in times of high inflation and low earnings, employment issues will eventually be seen.

Employment is a key indicator of the strength of the economy. An anomaly has formed that unemployment is still considered high, but has been slowly decreasing as we see more and more mass layoffs every day. This is giving a mixed signal and some have wondered if the reduction in unemployment numbers are a result of some people having to take multiple jobs to make ends meet. These numbers are inherently skewed as well due to the fact that people who have given up trying to find a job are not included in the survey.

Asset Class Performance / Investment Markets

Some History

When 1998 closed and we entered 1999, we did an analysis of how the S&P 500 achieved the return of 28% in 1998. We had the suspicion that the largest stocks contributed significantly to the total return of 28%. What we found was more dramatic than we expected, the top 11 stocks contributed more than the total return of the index. What this meant was that the top S&P 11 was up 29% and the bottom S&P 489 was down 1% as weighted in the index. We had certainly seen periods of concentration, but not like this. So, when we looked back to reporting from Q1 1999 Year End newsletter we talked about what had happened in 1998 and we never again thought we would see a market where so few stocks provided more than the total return of the index. Were we ever wrong! In 1999 the top 6 stocks contributed more than the total return of the index which was up 21%. In addition, over this two-year period those top 6 stocks, which were part of the top 11 in 1998, provided the total return of the S&P 500 index which was up 55% over the two-year period. We had seen concentration before, but this redefined it.

This was a period of new technology stocks leading the market and seemingly leading the economy with tools that would improve the lives of businesses and individuals. The thought was that these new tools would change our lives for the better and they deserved very high valuations. What the market got right was the part about changing our lives but what the market got wrong was valuations. Change is hard and often slower than we would like. The leading stock over the two-year period in the 90's was Microsoft. Microsoft was then and is today a great company that is making our lives better, the problem was investors had driven the price too high. It took Microsoft 13 years and 9 months to get back to the high price it achieved in 1999. That is almost 14 years with no return. Along the way Microsoft did start paying a dividend, so investors did get income for some of the time. That said, this redefined a dry spell.

What happened after 1999? Exactly what you think would happen after two years of severe concentration, the stock market fell dramatically. The S&P 500 declined in 2000 by 9%, in 2001 by 12% and in 2002 by 22%. $1 invested in the S&P 500 index on the first day of 2000 was worth 58 cents at the end of 2002.

Welcome to 2023! The same phenomenon exists today. For the first 6 months of 2023 the S&P 500 is up 16.9%. The chart below shows the contribution of the 7 top 10 stocks to that return.

		Weight		
		12/31/2023	6/30/2023	YTD
S&P 500				16.89
Apple Inc	AAPL	7.53	7.67	49.72
Microsoft Corp	MSFT	6.98	6.87	42.66
Alphabet Inc Class A + C	GOOGL	4.18	3.60	35.67
Amazon.com Inc	AMZN	3.07	3.10	55.19
NVIDIA Corp	NVDA	2.66	2.82	189.54
Tesla Inc	TSLA	1.57	2.02	112.51
Meta Platforms Inc Class A	META	1.68	1.75	138.47
		27.68	27.82	

So, let's see if we can make some sense of this.

NVIDIA is a stock of the Metaverse, which will certainly change our world for the better. The problem with technology changing ideas is the price of their stocks get way ahead of the impact of the technology. Today NVIDIA trades at 220 times earnings, which means it better change our world very quickly. The most likely outcome is the price of the stock has gotten ahead of the contributions it will make on society. History is full of these stories; Microsoft went over 13 years from its 1999 high before it hit a new high. Ark is one of our managers that is in some of our client portfolio models. Ark invests in companies they believe can achieve annualized return of 15% per year over the next 5 years, and Ark had owned NVIDIA for the entire time they have managed portfolios for us. They sold NVIDIA this year because they believe the stock price is too high to achieve that 15% annualized return. Good company? Absolutely! Problem is the price is just too high.

META is a company that had big designs on products that the consumer did not rate highly. They talked about investing the Metaverse and invented products they thought the public would love. It turned out their product launch failed, they had to lay off workers and the stock fell precipitously from $379 in August of 2021 to $93 in October of 2022, just 14 months with a 75% decline. Meta trading at $93 was the same price it traded for in August of 2015, almost 8 years ago. META moved up to $148 by the end of last year, the same price it was in June of 2017. Now we are all familiar with the fact that 30% of the workforce at Meta was laid off and all hiring stopped. So, this was a nice bounce off the bottom but far from a price move based on great news.

Tesla is by anyone's standards a volatile stock. It trades today at $261.77 (6/30/2023) which is up from its price of $123.18 at the start of the year but still far off its high of $409.97 on 11/4/2021. Now Tesla is a great company. The business most people know it for is the car business but it is much more than that. You likely saw that Tesla is allowing Toyota and Ford to use its charging stations which are the largest group of chargers in the country. By allowing this, the Tesla charging system has become the standard for our country. This does not generate much revenue for Tesla today, but it will be a revenue source when charging an electric car comes at a cost everywhere, which it assuredly will. The third business of Tesla is a self-driving taxi business. The headlines today suggest that is a long way out into the future, but there are some developments which might suggest otherwise. Today Arizona is allowing self-driving taxis, not from Tesla but from Waymo. This started in 2022 when people could choose a driver or driverless taxi. Today Waymo has a fleet of driverless taxis in Arizona that are thriving. The people we follow suggest that there will be driverless cars nationally within two years. We will see if that is right, but it will come someday, and Tesla will have the largest driverless taxi fleet in our country. So, like Meta, the price movement of Tesla today is still down from its high of $410, today trading at $262 (6/30/2023).

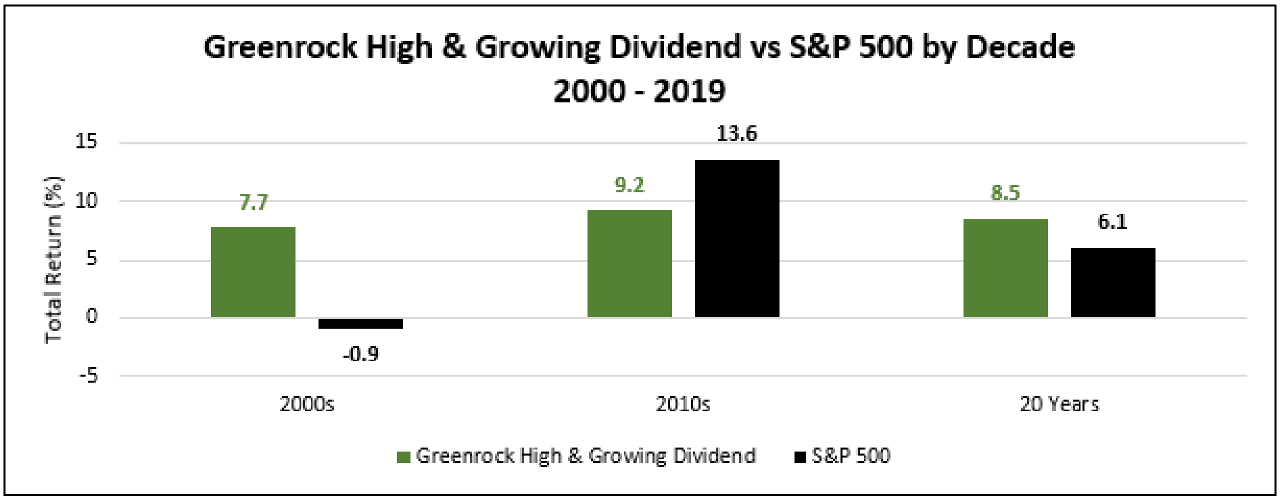
Apple, Microsoft, Alphabet and Amazon are all companies that are up between 36% and 46%. Yes, they are all great companies and yes, they are volatile but those returns are difficult to explain and would suggest caution not jumping on the bandwagon.

What Happens Now

All of these companies will be around five years from now and likely all of their stock prices will be higher. The real question is will they be good investments. History suggests caution. The easy answer is the companies that will be higher are those whose who achieve high earnings growth but with reasonable price relative to that growth will be the winners. So, our view on all of these stocks is that

NVIDIA is likely to have the best growth rate from here, but the question for them today is what price relative level will be used to value the company in 5 years. It is unlikely it will be 222 times earnings. Meta, Apple, Microsoft, Alphabet and Amazon will all be more mature companies 5 years from now, so their P/Es are likely to be lower. That said, any of them could add products or services that could change their direction. You may have seen that Tesla delivered 83% more cars in Q2 of this year than they did in the same quarter of last year. It is hard to believe we will see that same growth 3 or 4 years from now, so Tesla's future is dependent on the timing of self-driving and the revenues from owning the charging network, not just selling cars. Perhaps the biggest future revenue source for Tesla will be self-driving taxis.

That is what we see for the small group of stocks moving the market today. What we see for our dividend portfolios is another story. Let's start with a look at history. The chart below shows the performance of our dividend strategy and the S&P 500 during the decades of the 2000s and the 2010s.



Returns are based on historical models from our research company who helped build our current models

The dilemma we face as investment managers is it is not prudent to invest in only a handful of stocks that are currently the driving force of the S&P 500. Additionally, it is not prudent to chase stocks that are, for now, the driving force of the index due to the issues revealed above that these stocks may not continue to produce a reasonable return long term. For this reason, we tend to default to a diversified income driven portfolio which tends to be slow, steady growth over the long term. The benefits of this is we have found this strategy to keep up with the broad market indexes long term with less volatility.

<u>Alternative Assets</u>

The bond market continues to face challenges and interest rates remain in flux. Short term rates continue to rise emanating from the FED's decision to fight inflation. Longer term rates are being pulled in multiple directions creating the yield curve issues we discussed earlier. Lenders make money on lending and as rates increase, it is more difficult to find borrowers. The housing market continues to be slow and people want to hang on to lower mortgages and homeowners have reconsidered moving. Corporate debt has slowed as companies dealing with inflation have seen earnings drop making it harder to service loans and there is less motivation to expand if a loan to do so is needed. Most would presume that with rates rising, that the returns of bonds would also rise, but this is actually backwards and the reason we have held off purchasing a long-term bond portfolio. The Bloomberg US Aggregate bond index, a broad market index for bonds, was down for the last year -0.94%.

There are challenges that present themselves in both the equity and fixed income markets; therefore, we continue to constantly research and vet various alternative investments that have little correlation to other sectors of the market, such as stocks and bonds.

Overall, the objective of this portion of the portfolio is to achieve:

- High current income, yield, and solid risk-adjusted returns for investors seeking safety, security, and reliable cash flows;
- Risk management with a focus on capital preservation and down-side protection;
- Alternative returns that are diversified and uncorrelated to broader financial markets;
- Senior position loans that provide investment safety and security across market cycles;

Investment Markets

Portfolio management

As a result of struggling markets, it is best to restrict withdrawals from portfolios as they are allowed to recover; however, we do take proactive action to mitigate this challenge. Our dividend portfolios are structured to generate continued income in the form of a dividend. Although stock prices may fluctuate, it is important to note that the number of shares owned will remain constant and be allowed to recover in the future as long as dividend income is the only source of income spent. In addition, a tactical (or actively managed) portfolio allows for proactive responses to market changes to minimize returns while seeking upside potential. Lastly the alternative asset class previously mentioned is designed to support a steady income stream as well. The combination of the management of these portfolios is intended to support the potential of an ongoing income stream as markets respond to various factors.

The Bottom Line

Inflation is the root of the problems relating to the market right now. Corporate earnings, wages, consumer spending, product pricing and transportation costs are all components of market drivers and inflation sensitivity.

At this point, we are at the mercy of the FED's decisions related to interest rates with the next one being at the end of July of 2023. In simplest terms, the FED is raising interest rates to eventually stem inflation. Should the FED raise rates too far or too fast it could stall the economy driving it into a recession. It is difficult to get it exactly right and the chances of a soft landing get worse with every increase.

Ultimately, it will come down to the path inflation takes and how the FED responds to this information through interest rate targets and other tools.

Below are the returns for index categories making up the broader markets. Morningstar sourced these index returns. Returns beyond one year are annualized.

	2nd Qtr. 2023	**1 Year Average**	**5 Year Average Return**	**10 Year Average**
S&P 500 Growth	10.59	18.28	13.01	14.49
S&P 500 Value	6.64	19.99	10.58	10.51
S&P Midcap 400 Growth	5.14	19.22	7.16	10.11
S&P Midcap 400 Value	4.53	15.97	8.00	9.96
S&P SmallCap 600 Growth	4.78	10.62	5.22	10.26
S&P SmallCap 600 Value	1.95	8.88	4.96	9.19
DJIA	3.97	14.23	9.59	11.26
S&P 500	8.74	19.59	12.31	1286
S&P 500 Equal Weighted	3.99	13.76	10.21	11.48
S&P Mid-Cap 400	4.85	17.61	7.79	10.21
S&P Small Cap 600	3.38	9.75	5.22	9.81
Russell 1000	8.58	19.36	11.92	12.64
Russell 2000	5.21	12.31	4.20	8.26
Russell 3000	8.39	18.95	11.39	12.34
MSCI EAFE	2.95	18.77	4.39	5.14
MSCI EAFE Large Growth	3.21	21.70	6.71	6.84
MSCI EAFE Large Value	3.91	18.91	3.44	4.10
MSCI Emerging Mkt	0.90	1.75	0.93	2.95
MSCI World	6.83	18.51	9.07	9.5
MSCI US IMI Gold	-12.39	-20.66	5.41	6.07
DJ Real Estate	2.43	-2.65	4.57	6.57
Bloomberg Commodities	-2.56	-9.61	4.73	-0.99
Bloomberg Agg US Bond	-0.84	-0.94	0.83	1.33
Bloomberg Agg US Interim	-0.75	0.6	0.83	1.33
Fidelity Money Market	1.18	3.65	1.42	0.91