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Financial planner

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Summer 2022 Newsletter Topics



What the Fed's Interest-Rate Increase Means for You

The Federal Reserve raised its short-term benchmark rate by a half-percentage point on Wednesday, May 4th, the sharpest increase since 2000. Though widely expected, the move will ripple through the economy and Americans' financial lives.

Intended to combat the highest inflation in four decades, the higher rates will make it more expensive to buy a home or a car, or carry a credit-card balance. The Fed began increasing rates in March by one quarter of a percentage point after lowering them to near-zero levels during the pandemic. Wednesday's increase will accelerate the impact on American wallets from gradual to more sudden.

Over the past decade, rate increases and rate cuts were smaller and happened more slowly, said Yiming Ma, assistant professor in the finance division at Columbia Business School. This faster pace makes it more important for consumers to pay closer attention.

Here is how the latest Fed rate change will affect your money and what to look out for as more interest-rate increases are expected this year.

Mortgage Rates

Over the last two years, low rates and low housing inventory ignited a fiercely competitive housing market. House hunters encountered higher prices and bidding wars. As of March 2022, the median sales price of a single-family home reached $375,500, up 15% year-over-year, according to the National Association of Realtors.

Mortgage rates are based largely on the yield of the 10-year U.S. Treasury bond. This rate is used as a benchmark for many types of loans, including mortgages.

When the Fed raises rates, this pushes the yield on the Treasury note higher, which will then push mortgage rates higher. As the Fed signaled higher rates earlier this year, the 10-year yield moved higher. With it rose the average rate on a 30-year fixed-rate mortgage, which was 5.1% as of the week of April 28, according to Freddie Mac. Just a year ago, the same rate was 2.98%.

Anxious house hunters should look at the broader historical context, said Charlotte Geletka, managing partner of Silver Penny Financial, a financial-services firm in Brookhaven, Ga. Though it might come as little consolation to buyers who have grown used to years of ultralow rates, compared with decades past, a 5% mortgage rate is still considered low, she said.

"Yes, mortgage rates are higher than they were a year ago, but if you've done the work and saved the money and it makes sense in your financial plan, 100 basis points in a mortgage rate shouldn't necessarily prevent you," she said. "You might have to be cautious in how much house you're getting, so make sure you have a really good handle on your monthly payments."

Savings Accounts and Certificates of Deposit

While less happy for home-buyers, rising rates could mean good things for savers long saddled with minuscule rates of return on savings accounts and certificates of deposit.

Interest rates offered on many CDs and savings accounts often move with the federal-funds rate. Americans hit the highest personal savings rate in generations during the pandemic, despite getting little return from banks.

As of February 2022, the average annual percentage yield on a one-year CD is 0.14%, according to the FDIC. Online banks like Ally are also offering 0.50% for their high-yield savings products, and Goldman Sachs Group Inc.'s Marcus account is now offering 0.6%.

All of these should move slightly higher as rates go up, but as these rates won't move immediately, you have more time to wait. Given the broad trend in people socking money away, banks have had little incentive to raise interest on savings accounts. Some banks might be slower to raise interest rates than others, so this could be a good time to shop around, Ms. Ma said.

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"Historically, banks have not been very good with transmitting these rate increases to the borrowers," Ms. Ma said. "They have all the incentive to not offer as much, so it's definitely good to shop around for different types of deposits offered by different institutions."

Credit Cards

Higher interest rates often mean credit cards will get a higher annual percentage rate, or APR, so keep a close eye on your balance and rate being charged by your credit-card company. According to WalletHub's May report on more than 1,500 credit-card offers, the average annual percentage rate for those with good credit was 18.84%, which could potentially go up given the rate increase.

"It's good to think about ways in which debt could potentially be reduced or consolidated or paid back, so the affected amount one owes on cards could be as low as possible as we go into this rate hike," Ms. Ma said.

Wall Street Journal reporting has found that some credit-card rates are going up regardless of interest rates. As rewards and points programs become more popular with cardholders, perks are costing banks more, leading many to raise rates to pay for them.

Auto Loans

The rate hike shouldn't bring any surprises for those who have already secured a fixed rate for their auto loans. These loans typically have a fixed interest rate pegged to Treasury yields. But those car shopping might see higher costs during the purchasing process.

Individual car dealers and lenders can charge different amounts for your new car loan. As of the week of April 27, the average rate on a five-year new-car loan was 4.47%, according to Bankrate.com, compared with 4.12% a year ago.

The car market remains hot, so be sure to do your math before purchasing a vehicle.

Student Loans

For those with federal student loans, interest rates have already been set for the 2021-2022 school year, so this increase won't affect borrowers. The rate for direct subsidized and unsubsidized undergraduate loans is 3.73% until June 2022, according to the U.S. Department of Education.

The student-loan pause that went into effect in March 2020 halted interest accrual and gave some borrowers a break from their regular monthly payments (and, for some, a chance to eliminate their debt altogether). The pause has been extended to August 2022.

The interest rate for federal student loans is set every May according to the 10-year Treasury note auction. These rates are fixed for the life of the loan. Next year, however, the rise in rates could impact loans distributed for the following academic year.

Private student loans, however, either charge fixed rates, which stay consistent, or variable rates, which can increase or decrease depending on the institution you borrow from or your individual financial circumstances. These could be affected by The Fed's decision, leading to those borrowers facing higher interest rates.

Caring for Elderly Parents

With people living longer, adult children are often asked to act as coordinators and managers of an elderly parent's care. Although physical care should be the primary concern, managing and protecting finances is a close second. An outdated estate plan, a successor trustee verging on incapacity — these are potential missteps when it comes to elder financial care. And any one of them could lead to family strife.

One common issue involves children doing all they can to arrange 24-hour nursing care for an ailing parent, yet failing to secure their own financial well-being in the same way. Then there are the scenarios in which the hired caregiver becomes a confidant, and the parent amends an estate plan to name the caregiver as agent, fiduciary and beneficiary in the estate plan documents. After the parent dies, the caregiver and child become locked in an expensive dispute over the validity of the documents. A well-constructed estate plan can help prevent these types of surprises.

Does the Elderly Parent have Capacity?

There are two main types of capacity:

Testamentary capacity: the ability to make a will or trust.

Contractual capacity: the ability to enter into contracts.

Each state has its own interpretation of capacity and the distinction between the two. In general, the mental capacity required to enter into contracts is higher than the mental capacity required to make a will or trust.

The practical consequence of testamentary incapacity is that an individual can no longer make or modify a will or trust. For contractual incapacity, the consequence is the inability to enter into contracts. In other words, if an individual enters into a contract while she is incapacitated, her rights and obligations under the contract may not be enforceable.

Most individuals do not recognize when they themselves reach the point of incapacity. This can lead to a whole host of financial problems, ranging from not paying bills on time to becoming a target for bad actors or undue influence. Accordingly, it's up to an individual's family members to recognize the signs of incapacity, and to take the appropriate actions to have the declaration of incapacity made official and a conservator or guardian appointed by the court. Contact an estate planning or elder law attorney in the state where the parent resides if your parent could be incapacitated.

Is There a Plan for Incapacity?

There are several steps that can be taken to help ensure the safety of the parents and the security of their financial affairs through incapacity.

Have a durable financial power of attorney and health care directive in place and up to date. In these documents, an individual appoints an agent to make decisions on her behalf if she is incapacitated. Under a financial power of attorney, the agent has the authority to make certain financial decisions on behalf of the individual; under the health care

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directive, the agent has the authority to make health care decisions on behalf of the individual. For the financial power of attorney to remain effective through incapacity, it must be a "durable" power of attorney. In addition to naming an agent for health care matters, the health care directive should include a living will, in which the individual makes known her end-of-life wishes.

Integrate a revocable trust into the estate plan. The beauty of a properly funded and structured revocable trust is that it can accomplish the transition of control upon incapacity without any judicial proceeding, change of ownership or even the use of a financial power of attorney. Upon the incapacity of a grantor of a revocable trust (assuming the grantor is also serving as trustee), the person named as successor trustee will automatically assume control of the trust and all of the assets held within the trust.

Review successor fiduciary/agent appointments in all estate planning documents. This is essential if parents are close in age, and if they have named each other as fiduciaries/agents in their wills, living trusts and powers of attorney. There may be a circumstance where both parents die or become incapacitated around the same time, so it is important for the continuity of control that successor fiduciaries and agents are appointed in the estate planning documents. It may even make sense for the parent to resign now, while he still has capacity, and have the successor trustee take over the administration and management of the trust.

Does the Estate Plan Reflect the Elderly Parent's Current Wishes?

If a significant amount of time has passed since the last review of estate planning documents, a lot may have changed from a family and financial perspective. Take the time to review beneficiaries, fiduciary succession and the terms of any continuing trusts. Furthermore, in certain circumstances, it may also make sense for the parents to consider certain gifting strategies, with the intent of depleting the parents' taxable estate.

Any gift planning requires the advice of an estate planning attorney or other professional advisor, but if time is of the essence (as it can be when dealing with elderly individuals), there are some easy gifting strategies to implement:

Annual exclusion gifts. Depending on how many children, grandchildren and other potential beneficiaries the parents may have, this technique can have a serious impact. Each year, an individual can give $15,000 each to as many people as he likes, without cutting into his lifetime exemption (this means married couples can give $30,000 each year). If the parents have three children (including the client), and each of these children has a spouse and three children, two years of annual exclusion gifts to all of these individuals will remove $900,000 from the parents' taxable estate.

Paying tuition and medical expenses directly. The payment of tuition and medical expenses directly to a school or medical provider — as long as certain very strict requirements are met — is not considered a taxable gift. With the cost of private school education and college today, this can be an impactful way to benefit younger generations. One way to supercharge this technique is to prepay future tuition to certain institutions where beneficiaries will be attending school for several years. To qualify, these prepayments cannot be refundable under any circumstances.

Should the Parents Be Replaced as Current Trustees?

Even if the parents are still firmly in the realm of capacity, it may make sense to replace the parents as trustee of their revocable trust at the current time. As described earlier, the trustee has authority over all of the assets held in the trust, so even if the parents become incapacitated, the trustee's authority over the assets will not be affected.

Does the Estate Plan Need to Account for the Parents?

If you have been paying for any portion of your parents' care or living expenses, or if you envision a circumstance where that may become the case, review the estate planning documents to ensure that these arrangements will continue in a situation where you predecease your parents.

Can measures be taken to help the parents qualify for federal or state benefits?

Depending on the parents' financial situation, they may qualify for state or federal benefits like Medicaid. Support given to your parents should be structured so as not to disqualify them from these benefits. This is often achieved through the use of special needs trusts or Medicaid-qualifying trusts. It may also make sense to restructure the parents' assets (through gifting or trust structures) to strike a balance between continuing qualification for benefits and preserving lifestyle and legacy. An attorney that specializes in elder law is the expert of choice for these types of inquiries.

Is Now the Right Time to Invest?

Each time a lottery jackpot skyrockets, ticket sales spike. Even those who aren't regular lottery players don't want to be left wondering if they've missed their big chance.

Investing, on the other hand, is less trivial. When it's your retirement on the line rather than a $2 lotto ticket, you may question whether it's the right time to be in the market. Have stocks peaked and we're in for a downturn? Will this bear market ever end?

However, it's impossible to know whether the market is entering a bear or bull market until after the fact. That's why, historically, investors have been better served by simply being invested rather than waiting for a "better" time to invest.

Seeing the Forest for the Trees We looked at the most recent bear markets in the S&P 500 Index (defined as a 20% drop from the most recent market peak). Since 1990, the market has experienced five of them.

As Figure 1 shows, even if you had the worst possible timing—meaning you invested $10,000 on each of the five peak days immediately before a bear market began—your investments would have lost value initially but recovered in an average of 2.7 years. Your hypothetical investment of $50,000 would have grown

to $229,405 as of December 31, 2021.

In other words, even if you managed to repeatedly invest at the worst-possible times, the amount you invested still would have more than tripled. While past performance doesn't guarantee future results, it's encouraging to see that, historically, the market has eventually rebounded from its deepest selloffs.

FIGURE 1

Time in the Market Has Outweighed the Timing of Your Initial Investment

"Worst" Times to Invest in the S&P 500 Index

Date of Market Peak	Negative Market Event That Ended Bull Market	Portfolio Value on Peak Day	Bottom Before Recovery	Time to Recover Investment
9/1/2000	Dot-com Bubble Burst	$10,000	$6,433	6.1 years
3/19/2002	Accounting Scandals	$17,850	$11,957	1.8 years
10/9/2007	Sub-Prime Mortgage Crisis	$36,386	$17,933	4.5 years
1/6/2009	Global Financial Crisis	$32,362	$23,564	0.3 years
9/1/2000	COVID-19 Pandemic	$158,190	$104,737	0.5 years
			Average	2.7 years
				Total investment: $50,000 Balance as of 12/31/21: **$229,405**

Data Sources: Ned Davis Research and Hartford Funds, 2/21. Assumes a $10,000 investment on each date in column 1. The portfolio values in column 3 are cumulative.

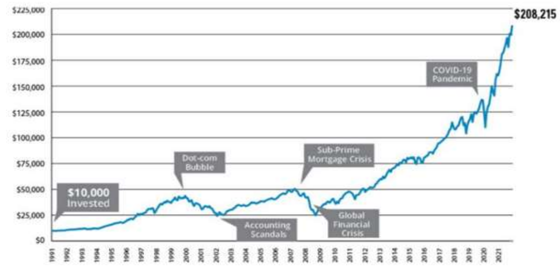
Another reason not to stress about timing: Despite bumps and stumbles along the way, stocks have historically grown over the long run, as **FIGURE 2** shows. And 78% of the market's best days have occurred during a bear market or during the first two months of a bull market when it was difficult to tell whether a bull market had even begun. This means sitting out could mean significantly missing out.

In short, for long-term investors who have the time horizon to weather ups and downs, the length of time you're in the market matters far more than what the market is doing when you invest.

FIGURE 2

Stocks Have Grown Over the Long Term Despite Bear Markets

Growth of $10,000 invested in the S&P 500 Index 1991–2021



Past performance does not guarantee future results. Indices are unmanaged and not available for direct investment. Source: Morningstar Direct, 2/22.

How to Get in – and Stay in Part of weathering the market's ups and downs is making sure you're working with a financial professional to build a customized portfolio that aligns with your goals and risk tolerance. Having an intentionally designed portfolio can help you feel more confident during difficult market environments, which in turn can help you stay invested long term.

Consider setting a predetermined amount to invest on a regular schedule. This can help reduce that internal "is this a good time?" debate and help you stick to your plan, regardless of the market environment.

Content courtesy of

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