BKMWM Newsletter April 2023

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BKM WEALTH MANAGEMENT

1) How Am I Protected?

Silicon Valley Bank, Silvergate Capital, Signature Bank, Credit Suisse and First Republic Bank have all made news recently as the stability of the banking system has come into question. It may have you wondering, as an investor, how am I protected?

Brokerage accounts like those held with First Clearing (a trade name used by Wells Fargo Clearing Services, LLC) have two sources of protection from firm insolvency. The first is SIPC coverage, which insures each client up to a maximum of $500,000 (including up to $250,000 for claims for cash)[1].

First Clearing maintains a program of additional protection provided through London Underwriters, led by Lloyd's of London Syndicates, ("Lloyd's").[2] For clients who have received the full SIPC payout limit, First Clearing's policy with Lloyd's provides additional coverage above the SIPC limits for any missing securities and cash in client brokerage accounts up to a clearing firm aggregate limit of $1 billion (including up to $1.9 million for cash per client). Please note that coverage provided by SIPC and Lloyd's does not protect against the loss of market value of securities, nor do they insure the quality of investments or protect against losses from fluctuating market value. All coverage is subject to the specific policy terms and conditions.

FDIC Insurance plays a role in protecting the cash and "cash sweep" portion of enrolled TradePMR/First Clearing accounts. Balances in the Cash Sweep Program, uninvested cash (principal and interest) in each eligible account is automatically deposited into one or more sweep vehicles. The program consists of three distinct options. The Standard Bank Deposit Sweep consists of interest-bearing deposit accounts at two or more Program Banks affiliated with WFCS, LLC ("Affiliated Banks"). Cash sweep deposits are FDIC insured for up to $500,000 per single depositor (or $1 million for joint ownership accounts with two or more owners). The Expanded Bank Deposit Sweep consists of interest-bearing deposits at up to five banks including affiliated and unaffiliated banks. Cash sweep deposits are FDIC insured for up to $1.25 million per single depositor (or $2.5 million for joint ownership accounts with two or more owners).[3]

For accounts held with TradePMR and First Clearing please refer to their customer/client agreements for additional details and contact us with further questions on how your assets are protected.

1) *SIPC coverage is not the same as, nor is it a substitute for FDIC deposit insurance. Securities investments purchased through TradePMR are not FDIC insured and may lose value. For more information visit www.sipc.com.*
2) *For More information about Lloyd's, visit www.lloyds.com.*
3) *More information on FDIC coverage is available at www.fdic.gov.*

2) Headwinds: Interest Rates, Inflation & War

Our May 2022 newsletter had the same headline. Nearly a year later, those same issues persist.

- Short-term interest rates were roughly 0.50% percent a year ago. Now they are about 4.75% and could climb past five percent soon.
- Inflation may have peaked and could be headed lower, yet year over year the Consumer Price Index (CPI) was still up six percent as of March.
- The Ukraine War continues with ever more requests for military aid from the United States and others.

Higher interest rates typically slow economic growth. Which should mean lower corporate profits as sales slow and borrowing costs rise. Lower profits often lead to fewer and smaller dividend increases. Couple this with the now much higher interest rates available on more conservative investments, and the weakness in stocks seems quite understandable. Investors have been pouring money into bank CDs, U.S. Government Treasury bills and money market funds, as well as corporate bonds and higher dividend paying stocks.

Wars increase government spending. They are contributors to inflation and can erode investor confidence.

An additional headwind not mentioned in last year's newsletter is the aging population across much of the world. Fewer workers to replace retiring workers may help keep wages higher. A reduction in world trade as some offshore work is moved home may also help keep wages, inflation, and interest rates moving higher for longer than investors would like.

There is some good news for investors. Stock valuations in general are much cheaper than they were a year ago. The S&P 500 traded at about 25 times trailing earnings last spring. It is now about 20.6 times. That is in line with long term median valuations at about 20.34 times.[4]

Many short-term bonds and CDs are yielding over 5%. Cash is no longer trash! Real estate values have stopped increasing and have moved modestly lower in many markets. Those not needing big mortgage loans more pricing power and options than they had a year ago.

Given the headwinds we continue facing, we've been staying relatively defensive. We've been investing in more interest paying investments by building "ladders" of bonds and bank CDs from six months to five years for many clients. Ladders may help reduce the effects of further large swings in interest rates.

We will not abandon stock exposure. The volatility that comes with stock ownership is the price you historically pay for their ability to outpace inflation over longer periods.

As always, call us to discuss ways to earn more interest on your cash and to review your risk tolerance.

4) Source: https://www.gurufocus.com/economic_indicators/57/pe-ratio-ttm-for-the-sp-500

3) Why Interest Rates May Be Nearing the Peak

The past year or so of interest rate hikes, both domestically and abroad, have rewritten the playbook for companies, consumers and investors alike. The Federal Reserve has sharply raised rates in an effort to curb inflation, but these enhanced interest rates are unlikely to stay inflated indefinitely.

In recent months we have seen the first signs that price increases for consumers may be meaningfully easing, leaving many economists to believe that the peak of inflation is behind us. The Federal Reserve has been charged with the difficult task of using interest rates to combat inflation while also not sending a vulnerable economy into deep recession. The superficial purpose for raising interest rates is to deter spending by corporations and consumers, bringing pricing down with it, but this happens at the cost of forcibly cooling off the economy, meaning the Fed must carefully balance opposing interests. Although Fed Chair Jerome Powell has been outspoken that they will learn from history and not make the mistake of easing rates too early[5], as had been done in the era of stagflation in the 1970s, lower inflation will ultimately herald an end to interest rate hikes.

While inflation may be on a return trajectory to Earth, the recent stumbling of Silicon Valley Bank, and concerns elsewhere in the financial sector, may tilt the scales towards the Fed erring on the side of protecting a teetering economy rather than tamping down inflation. Consensus estimates suggest that the potential of a 50 basis point (0.5%) rate hike[6] at next week's Federal Open Market Committee meeting has all but been taken off the table. Additionally, while the economy as a whole has stayed stronger for longer than many anticipated, last month's data release suggests that businesses and individuals are finally starting to reduce their spending – a key element to curbing inflation. Meanwhile, certain important pricing elements, like energy, residential rents, and certain foods, appear firmly on the decline.

It is not expected to be a smooth transition. We have already seen several short-term reversals in inflation data, including whiplash in the past two data releases, which has catalyzed sharp interest rate spikes and dips. And while indications are that the worst of inflation is in the rearview mirror, inflation may persist for longer than many expected, and the Fed's commitment to see things through – economic strength permitting – likely ensures that the interest rate peak will occur sometime after the summit for inflation.

5) Source: Federal Reserve Chair Jerome Powell. Senate Banking Committee address, 7 March 2023, Capital Hill.
6) Source: Reuters poll of economists, 17 March 2023.

4) 529 Plan to Roth IRA Rollovers

When Congress passed the Secure 2.0 Act last year one of the more buzzworthy topics amongst financial advisors was the new ability to roll unused 529 plan assets into a Roth IRA. Now that the dust has settled and the details are becoming clearer, the strategy is still worth discussing, but less of a slam dunk win than previously thought.

529 college savings plans allow your college savings to grow tax-deferred and be withdrawn tax-free and penalty-free if used for qualified higher education expenses. They can also be used to pay for up to $10,000 per year of K-12 tuition and/or up to $10,000 lifetime of student loan payments. In many states the contributions can be deducted from State income taxes up to a limit. In Wisconsin, that limit is $3,860/year per beneficiary in 2023.

The new law allows a lifetime maximum of $35,000 to be rolled from a 529 plan to a Roth IRA. This sounds like a great benefit, and it is. However, there are a lot of caveats.

- Rollovers cannot start until 2024.
- The 529 account must have been in existence for at least 15 years.
- 529 contributions made less than five years from the rollover date are not eligible to roll.
- The annual rollover amount is limited to the amount the beneficiary would be eligible to contribute to a Roth IRA in that year. If the beneficiary has no earned income, or too much earned income they may not be eligible.
- The amount rolled over in a given year counts against the beneficiary's IRA contribution limit for that year. For example, they cannot rollover $6,500 and contribute $6,500 in the same year.

All of these rollover rules and limitations should not dissuade you from considering a 529 plan for your child or grandchild. 529 plans can be a tax-smart way to save and the Secure 2.0 Act makes them even more flexible. Just be sure to understand all the rules before making large contributions and rollovers.

5) Check Your Spam/Junk Folder

Last month BKM Wealth Management updated the background technology sending our emails. This change may have caused some email programs to filter our emails into the junk/spam folder. Please look at your junk folder and add our emails to your list of safe senders.

Reminder: Online account access is now on the First Clearing side of Wells Fargo's technology platform. To access your accounts online please visit https://tradepmr.fccaccessonline.com/.

6) 2023 Contribution Limits

2022 IRA contributions can still be made up until April 18th. If your account is held with TradePMR/First clearing your checks should be made payable to First Clearing. Below is information on 2023's contribution limits.

Traditional IRAs

Maximum annual contribution

- Lesser of compensation or $6,500
- Up to $6,500 contribution can also be made for nonworking spouse
- Catch-up contributions (age 50 and over): $1,000

Traditional IRA deductibility table

Filing status	Covered by employer's retirement plan	Modified AGI 2023	Modified AGI 2022	Deductibility
Single	No	Any amount	Any amount	Full
	Yes	$73,000 or less	$68,000 or less	Full
	Yes	$73,001–$82,999	$68,001–$77,999	Partial
	Yes	$83,000 or more	$78,000 or more	None
Married/ Jointly	Neither spouse covered	Any amount	Any amount	Full
Married/ Jointly	Both spouses covered	$116,000 or less	$109,000 or less	Full
		$116,001–$135,999	$109,001–$128,999	Partial
		$136,000 or more	$129,000 or more	None
Married/ Jointly	Yes, but spouse is not covered	$116,000 or less	$109,000 or less	Full
		$116,001–$135,999	$109,001–$128,999	Partial
		$136,000 or more	$129,000 or more	None
Married/ Jointly	No, but spouse is covered	$218,000 or less	$204,000 or less	Full
		$218,001–$227,999	$204,001–$213,999	Partial
		$228,000 or more	$214,000 or more	None

Employer retirement plans

Maximum elective deferral to retirement plans, e.g., 401(k), 403(b)	$22,500
Catch-up contribution limit for 401(k), 403(b), and certain 457 plans	$7,500
Maximum elective deferral to SIMPLE plans	$15,500
Catch-up contribution limit for SIMPLE plans	$3,500
Maximum elective deferral to 457 plans of government and tax-exempt employers	$22,500
Limit on annual additions to defined contribution plans	$66,000
Annual compensation threshold requiring SEP contribution	$750
Limit on annual additions to SEP plans	$66,000
Maximum annual compensation taken into account for contributions	$330,000
Annual benefit limit under defined benefit plans	$265,000
Limitation used in definition of highly compensated employee	$150,000
Health flexible spending account maximum salary reduction contribution	$3,050

Sources: IRS and Social Security Administration updates 2023.

Roth IRAs

Maximum annual contribution

- Lesser of compensation or $6,500
- Up to $6,500 contribution can also be made for nonworking spouse
- Catch-up contributions (age 50 and over): $1,000

Contribution eligibility

Modified AGI is less than $138,000 (single) or $218,000 (married/filing jointly); phaseouts apply if modified AGI is $138,000–$152,999 (single) or $218,000–$227,999 (married/filing jointly).

Deductibility

Contributions to Roth IRAs are not deductible.

Conversion eligibility

There is no income restriction on eligibility for a Roth IRA conversion.

Base amount of modified AGI causing Social Security benefits to be taxable

	Up to 50% taxable	Up to 85% taxable
Married/Filing jointly	$32,001–$44,000	> $44,000
Single	$25,001–$34,000	> $34,000

Maximum earnings before Social Security benefits are reduced

Under full retirement age ($1 withheld for every $2 above limit)	$21,240
Full retirement age and over	No limit*

* Interim annual limit of $56,520 applies for whole months prior to attaining full retirement age during year individual reaches full retirement age ($1 withheld for every $3 above limit).

Health savings accounts contribution limits

Individual	$3,850
Family	$7,750

Catch-up contribution: Taxpayers who are 55 or older in 2023 may contribute an additional $1,000, or a total of $4,850 for individuals and $8,750 for families.