Comprehensive Investment Management, LLC
Fee Only Personal Financial Planning
Winter 2023

A Review of the Financial Markets at December 31, 2022

On the very first business day of 2022 the S&P 500 index hit its all time high of 4,797. For the next nine months it was downhill. The index was in bear market territory by June and bottomed out in October at -25%. In describing the behavior of the 2022 financial markets, 35 year veteran Rick Reider of Blackrock settled on the word "extraordinary." He focused on how in March the federal funds rate was 0% and the Federal Reserve was still practicing quantitative easing (QE), the practice since 2008 of buying large amounts of bonds to make borrowing cheaper. By the end of the year, the funds rate had been raised to 4.5% and QE was no more.

Recent market and economic activity is newsworthy. However most of it can be dismissed as "noise" and not indicative of a trend. Investment performance over longer periods, while not predictive, is significantly more meaningful.

Concerning the United Kingdom's Royal Air Force, Winston Churchill famously declared: "Never was so much owed by so many to so few". In 2022, investors can declare about the Federal Reserve Board members: "Never has so much blame been owed to so few." Certainly, it was obvious after Covid, that a return to economic 'normalcy' was not going to be easy. Massive government outlays and low interest rates flooded the market with free money. It was inevitable that inflation would follow. The Federal Reserve should have been ready to act, but it failed to take the required initial steps. Instead even into March it described price increases as transitory, that is, brief and ok to ignore. Throughout the rest of 2022 the markets became fixated on the Reserve, over reacting to its latest action, no-action, the minutes of its meetings and public comments by Chairman Powell and other Board members. The markets sold off on good economic news, because it meant the Reserve would probably respond by raising

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Average Annual Returns of CIM Select Mutual Funds

At December 31, 2022	QTR	YTD	1 Year	3 Years	5 Years	10 Years	15 Years
Large Cap Stocks	11.8	-11.5	-11.5	7.4	8.7	13..3	10.7
Mid Cap Stocks	8.7	-20.1	-20.1	5.3	6.6	13.0	9.8
Small Cap Stocks	5.1	-25.0	-25.0	2.3	5.6	11.0	9.0
Healthcare Stocks	10.3	-6.6	-6.6	8.8	10.4	14.9	12.4
Foreign Stocks	12.1	-26.5	-26.5	.8	1.9	5.8	4.8
Short Term Bonds	1.4	-5.7	-5.7	-.7	.9	1.1	2.0
Intermediate Bonds	2.1	-13.1	-13.1	-1.7	.7	1.2	3.1
High-Yield Bonds	4.9	-9.1	-9.1	-.3	2.2	3.7	5.3
Wellesley Fund 65/35 bonds/stocks	6.7	-9.0	-9.0	2.3	4.0	5.7	6.0*
Wellington Fund 35/65 bonds/stocks	7.4	-14.3	-14.3	4.1	5.9	8.5	7.0*

*On a deposit of $100,000, after 15 years, Wellington's balance of $284,895 exceeds Wellesley by $39,500.

interest rates. Bad news was seen as good news. In August the typical market inclination toward optimism got the best of it. Rumors spread that the Reserve was going to soon stop raising rates for fear of causing a recession. By September that proved not to be the case and the S&P moved back into a bear market, staying there for the rest of the year. The Reserve did what it had to do, but had waited too long. Because of the delay it had to take more steps more quickly than markets could absorb.

You didn't hear much about it, but the fourth quarter was good for investors, especially compared to the first three. Although expectations for higher rates, slower economic growth and low profits continued to plague the bigger tech companies, less economically sensitive companies and those trading at lower valuations outperformed as there was a shift towards defensive sectors. International markets outperformed the US as China finally abandoned its Zero Covid policy and the UK reversed the spending and tax plan put forward by Prime Minister Liz Truss whose term in office lasted only seven weeks, a record.

Also under the radar, bonds finally showed life as investors reacted to US economic resilience. Both high yield and investment grade bonds posted positive returns as investors reacted to lower monthly increases in the Consumer Price Index, which has steadily fallen from 9.1% in June.

> *"There are two kinds of forecasters: those who don't know, and those who don't know they don't know." (John Kenneth Galbraith) Hmmm. Which one should we pay attention to?*

LOOKING AHEAD

The market appears to be approaching a potentially important transition period that could see recent headwinds ease in the months ahead. First, inflation has shown definitive signs of declining. At six percent, we have quite a way to go, but the Fed hiking cycle is likely to slow. And while both economic growth and corporate earnings are expected to decline in 2023, those negative expectations have been pretty much priced in. Note that the S&P 500 hasn't registered two consecutive negative years since 2002. Bonds have never experienced two consecutive down years. Finally, market declines of the magnitude of 2022 are generally followed by strong recoveries.

There are undoubtedly challenges ahead in 2023, particularly for stocks. Despite the US Gross Domestic Product declining in the first six months of 2022, the economy did not fall into recession. We may not be so lucky in 2023. On the positive side, unemployment is low, consumer balance sheets are in good shape and wages are on the rise. So, it's still possible that a strong consumer may spend their way past a recession. However, there are some troubling factors, for example housing. Home sales are down 30% from a year ago and prices continue to decline. Mortgage rates are three times what they were a year ago. (Now that's extraordinary). Housing drives a large percentage of economic activity, so when it's struggling the economy is struggling.

For bond investors the swift double digit drop in prices, at times matching that of stocks, was the real surprise in 2022. We expect bonds to go up when stocks go down. Interest rates had to go up at some point. With thirty year fixed mortgages going for 2.35%, there was no room for them to go lower. Continued historic low rates can be a distorting contributor to the economy, discouraging normal savings (encouraging spending was, after all, the idea) and a drag on financial institutions, and certainly our bank savings accounts and certificates of deposit.

The outlook for bonds has greatly improved. A bond fund's yield is a good predictor of what it will return and they are up significantly. Funds that were yielding less than 2% at the start of 2022 are now at 5% and climbing. Suddenly cash is king, with money market funds yielding over 4% after years of returns less than a quarter of one percent. It's nice to finally earn some income on cash holdings. It may be a good idea to move money from a bank account that is still paying next to nothing. But don't raise cash by giving up on long term winners just because they are now under water after what many pundits called an extraordinary year.

The White House has announced it will begin taking "extraordinary" measures to prevent the US government from the catastrophe of breaching the debt ceiling this summer. There's that word again.

Tax Credit Mayhem for Electric Vehicles

A lot of folks are considering switching to an electric vehicle (EV). Their popularity is on the upswing. They require little maintenance. They run so quietly, that for pedestrian safety, manufacturers added a noise when it's moving below 20 miles per hour. So far they have opted for a whining noise and not a recording of "watch the car please."

Under the Inflation Reduction Act, you may get a tax credit of up to $7,500. For used EVs, the credit is 30% of the sale price up to a $4,000 credit. While the credit is an incentive, its provisions are complex and limiting. You are not going to want it to dominate your purchase decision. Consider all the usual factors in your purchasing decision, such as safety, reliability, overall cost, passenger room, cargo space and comfort features. And specifically for EVs the distance range before you need a battery recharge.

Hyundai Ionic 5

To get a credit the vehicle has to be on an eligibility list. The MSRP of a new EV cannot exceed $80,000 for vans, sports utility vehicles, and trucks and $55,000 for all others. For used, the price must be less than $25,000. EVs are not cheap, so the price limits will leave you with choosing among the least equipped models. Kelly Blue Book puts the average new EV at $66,000, so you can see the problem. The 2023 Motor Trend SUV of the year is the Hyundai Ionic 5. Its MSRP starts at $41,450. Hyundai says it's a SUV and Motor Trend obviously agrees. Alas, the government does not and limits the model to $55,000. Not to worry, it didn't make the list anyway. Hyundai and 11 other companies don't have any models on the list including Mercedes, Toyota and Subaru.

Credit eligibility comes with many limitations and conditions. Some rules are so complex the IRS is still working on them and is not expected to issue complete regulations until sometime in the Spring. There are restrictions on foreign vehicles. President Biden is getting more than an earful from some of our biggest allies. There may need to be some concessions in that regard.

There are limits on the modified adjusted gross income of the purchaser. For new, the limits are $300,000 for joint filers and $150,000 for single. For used, limits $150,000 for joint filers and $75,000 for single filers. The credit is nonrefundable, so you can't get back more for the credit than your tax liability.

Additional factors to qualify for the credit include the vehicle's battery capacity, manufacturer and assembly location. At the time of sale the seller must report required information to you and the IRS. In addition, you need a written and binding sales contract to substantiate your claim for the EV tax credit. The vehicle has to be assembled in North America which will be indicated by a VIN Decoder tool.

On the internet you will find the IRS list of *Manufacturers and Models for New Qualified Clean Vehicles Purchased in 2023 or After.* Listed is a Ford Escape Plug-In Hybrid. Maybe that's an idea. Tesla just announced a big sale and it has 8 models listed. You are advised to check back for additions to the list. Again, being on the list is just step one.

EVs have and are going to continue to play a significant role in the future of the automotive industry. California has banned the sale of new gas-engine cars by 2035, and our neighbor Delaware has announced plans to do the same. Several states are considering similar plans. Of course, aggressiveness of any plan is subject to change in either direction.

In the US auto makers sold over 800,000 EVs moving to 5.8% of all sales from 3.2% a year before. Tesla dominated with Ford in second place. For sure, manufacturers, in their own best interest, will lobby to make the credit easier to get in the future.

In the meantime, if you are considering an electric vehicle and are otherwise eligible for and interested in the credit, you should probably wait until the rules are finalized this spring. Then, if all the factors align, and there are many, you may be rewarded with a tax credit.

Comprehensive Investment Management, LLC

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Control risk yet outperform the market by using well managed, no commission, low cost mutual funds. Maintain appropriate asset allocation and diversification. Minimize taxes.

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WE GOT MAIL

Q. A friend asked me for a recommendation for a financial advisory firm and, of course, I referred her to CIM. She asked would she better off with a big firm. I said I doubt it. Was I right?

A. The PA Department of Banking and Securities oversees 200,000 broker dealers and investment advisers. Of the advisers, 80% have two or fewer employees. There are a number of reasons small advisory firms continue to thrive. To paraphrase Kermit, it's not easy being big. How do you like the service from your cable or phone company? Or your bank, your health insurance company? Vanguard's customer service was good back when it was at a few billion, but at over seven trillion, not so good. Scientific studies have found a direct correlation between the size of a company and the longer your time on hold. Despite what the recording says, your call is not important to them. For many firms, efforts at adding scale (growth) and the monetization of their services, are the quickest and surest way to increase profitability. But those goals are hardly associated with providing quality service.

Large firms build their own technology and then they are stuck with it as it ages. It's why we don't use our car's GPS. Big firms are laden with processes, rules, procedures and constraints. They not only have to keep customers in line, but their own staff as well. Wells Fargo has paid out billions due to regulators findings of serious "system failures." In 2016 it was discovered that over several years more than a thousand employees, in order to meet unrealistic sales quotas, opened millions of fake accounts.

Small firms may lack certain in-house resources, but there are legions of firms available to provide them with information, technology and operational support. Serving small business is big business.

CIM, not surprisingly, thinks it's better for an investor to swim in a smaller pond than a bigger one. A valid question is: how much money do you need to have to receive first class service from a bigger firm? There is no clear answer. For the most part, big firms are just not capable of providing consistent, excellent, personalized service. They're just too, how should we say, big.