www.firestonecapital.com

QtrNotes

Qtr 1 January 2022

Volume 30 No. 1

Quotes

Finding good partners is the key to success in anything: in business, in marriage and, especially, in investing.
Robert Kiyosaki

Investing is a business where you can look very silly for a long period of time before you are proven right.
Bill Ackman

While enthusiasm may be necessary for great accomplishments elsewhere, on Wall Street it almost invariably leads to disaster.
Benjamin Graham

By the time any view becomes a majority view, it is no longer the best view: somebody will already have advanced beyond the point which the majority have reached.
Friedrich Hayek

Be fearful when others are greedy and greedy when others are fearful.
Warren Buffett

Giving should be entered into in just the same way as investing. Giving *is* investing.
John D. Rockefeller

Economy, Employment, and Markets Robust Despite COVID

2021 ended on a positive note for investors, although the pandemic continues with no conclusive end in sight.

Despite new COVID variants, the economy marched forward in 2021. Employers added six million jobs to their payrolls, and the unemployment rate dropped to 4.2%. Incomes also rose, and consumer spending increased nearly 15% for goods and services. On the corporate side, companies increased retail prices to offset cost pressures, boosting revenues and leading to a year of extremely strong earnings growth.

Looking ahead to 2022, US stocks still look relatively attractive. Despite big stock price increases, valuations improved this past year, and stocks currently trade at lower P/E (Price-to-Earnings) levels today than they did at the start of 2021. If corporate earnings can keep rising in 2022, stock prices should too.

Analysts are optimistic, given a number of factors. The economy appears poised to keep growing, unemployment is expected to keep falling, and government policies are anticipated to remain supportive. Stock market returns are unlikely to do as well in 2022 as they did in 2021, but history shows the market often has consecutive years of good returns.

US stocks could extend their dominance for a third year into 2022, but international markets still present opportunity. Even though the economies of many foreign countries grew faster than the US economy in 2021, heightened risks and volatile currency movements put a damper on foreign stock markets. International stock prices now look favorable relative to the US, while still providing diversification benefits to portfolios. We plan to maintain exposure to foreign stocks, while focusing mostly on US markets to reduce unknown risks.

Index	*12/31/2021*	*YTD*
Dow Industrials	**36,338.30**	**18.7%**
S&P 500	**4,766.18**	**26.9%**
S&P Small-Cap	**1401.71**	**25.3%**
MSCI EAFE	**2,336.07**	**8.8%**
Bloomberg US Bond	**2,355.14**	**-1.5%**
US Treas 10-yr yld	**1.5%**	

Interest rates and monetary policy have played a large role in supporting financial markets, and investors wonder what changes may be in store for 2022. Bond yields remain near historic lows, and the outlook for fixed income remains stable but muted.

The primary role for bonds in portfolios today is as a source of ballast: insurance against recession, unexpected crises, or reversing tides in the stock market. Investors should keep holding bonds in an amount sufficient to support short-to-intermediate cash funding goals, but long-term funds should be mostly invested in assets with better growth prospects.

Lastly, cryptocurrencies are a growing presence in financial markets, although they remain highly speculative and volatile. We are paying more attention to this investment category, and having thoughtful discussions with clients who are interested.

Inflation: Transitory or Not?

The resurgence of inflation has been one of the big stories of 2021. As the economy expanded, inflation accelerated and asset prices heated up. Strong consumer demand, supply chain disruptions, and government policy forces combined to push inflation to an alarming 6.8% for the year, a 40-year high. This has been something of a shock following two decades when the long-term rate has remained close to 2%.

(cont'd next page)

1501 Venera Ave., Suite 310
Coral Gables, Florida 33146
305.669.2119
www.firestonecapital.com

jack@firestonecapital.com
carol@firestonecapital.com
carlos@firestonecapital.com
anthony@firestonecapital.com

FIRESTONE CAPITAL MANAGEMENT

New IRA Distribution Tables for 2022

There have been many recent changes to the rules for required minimum distributions (RMD). The SECURE Act, signed into law at the end of 2019, increased the beginning age from 70½ to 72, and completely changed the manner in which inherited IRA asset distributions are managed. RMDs were waived entirely in 2020, as part of the response to the economic crisis of lockdowns.

For 2022, another update goes into effect, a sweeping change impacting all distributions from IRAs and qualified retirement plans. Required withdrawals are decreasing. The Uniform Table, the life expectancy table used to calculate RMDs, has been updated for the first time in almost twenty years.

RMD calculations are made based on the account balance at each year-end, divided by a factor according to the account holder's age. These factors have been recalculated to produce lower figures, with the intention of extending the life expectancy of retirement accounts to match the longer life expectancy of retirees.

The changes to the life expectancy tables mean that less money can be taken out in any given year, allowing account assets to last longer – not to mention lowering taxes for the IRA holder.

Inflation Concerns

(cont'd from page 1)

Through most of the year, Federal Reserve chairman Jerome Powell thought that the rapid rise in inflation was transitory. However, he has recently acknowledged that we could have above-normal inflation for some time. The Federal Reserve now agrees that the time has come for them to take their foot off the gas, but they are also intent on not stepping on the brake.

To reduce surging inflation and accomplish a smooth monetary cooldown, the Fed has already started to reduce the amount of new bonds it buys each month (reversing the quantitative easing called QE). This should tamp down on rising prices by withdrawing some of the excess liquidity in the economy.

The Federal Reserve continues to keep interest rates at zero, but may start to slowly raise rates later in the year. Current estimates are for three increases of a quarter of a point each in 2022. The economy and markets are reliant on interest rates to stay fairly low, and the Fed will be quick to step in should rates rise faster than expected.

The Fed is endeavoring to achieve its dual mandate of stable prices and full employment with moderate interest rates, but other factors come into play as well. Too much demand chasing too little supply forces prices and wages up. Home prices are at an all-time high, consumer debt service is at a 40-year low, hourly earnings are finally increasing after decades of stagnation, and the Federal government has instituted anti-poverty programs, which are certain to boost spending.

As investors, we can look to areas that historically do well in inflationary times: commodities, US stocks (especially large-value, small cap, and dividend payers), international stocks, and inflation protected and variable rate bonds.

Why We Don't Try to Time the Markets

The last two years have given us outsized market gains. Some analysts feel the market has become overpriced and "frothy", and is due for a correction or even, heaven forbid, a crash. Does this mean you should sell? Selling all your stocks and going to cash to avoid a market crash can be just as costly as the crash itself, if not more so.

In a perfect world, investors with perfect foresight would sell at the top of the market, wait, and buy back at the very bottom. Sounds like a plan, but it doesn't work in real life. You must make two calls correctly: when to sell and when to get back in. For different reasons, it's almost impossible to make either call successfully.

Psychology comes into play, with the "greed and fear cycle." At market highs, investors tend to be overconfident, even greedy: nobody knows when the fall might come, and everyone hopes it won't come yet. When markets fall, fear is rampant, and the urge is to sell, not buy.

In the crash in 2008, prescient investors might have sold at the right time and avoided a 50% market decline; but few had the stomach to buy at all as markets bottomed in March of 2009. When the tide turned after that, far too many remained in cash, and missed one of the greatest bull market runs of all time. Anyone who stayed in cash for the next decade were far worse off than if they had just stayed the course, or lightened up on stocks and used the cash to rebalance into a more diversified portfolio. Most clients who already had a diversified portfolio suffered only half the drawdown temporarily, and were back on track within three years or less.

The problem of being in cash is that it becomes very difficult to pull the trigger, to get back to investing again. Even when the markets recover, there are always reasons for not getting back in. "The markets have run up too much"; "If I buy now the markets will crash;" "I've already missed too much – I'll wait and buy after the next crash." We have interviewed prospects who have lost a decade deluding themselves with these reasons.

There is a better way: rebalancing. When stocks values rise, sell some to return to your target portfolio allocation. When stocks fall, rebalancing forces investors to buy – to follow the market axiom of buying low and selling high. A diversified portfolio will include a minimum allocation to stocks, below which the holdings will never go.

While we can't be investors without assuming some risk of temporary loss, we can be prudent and manage the risks we choose to take.