



Qtr Notes

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Bear Markets by the numbers:

The S&P 500 has suffered 10 separate bear markets between 1950 and 2021. Each time, the markets recovered and eventually achieved a new all-time closing high. The length of time from the bear market low to the new closing high has ranged from just 3 months (in 1982) to nearly 6 years (1974-1980). The average time required has been just over two years.

Firestone's Privacy Policy and Form CRS:

Every year, Firestone includes a copy of our Privacy Policy in your quarterly report packet. This month, you will also find an updated copy of our Customer Relationship Summary (Form CRS).

This document provides clear and detailed information about our service offerings, fees, compensation, disciplinary history, and potential conflicts of interest. Most of this information is also covered in our other disclosure documents, but the Form CRS gives a more prominent position to the most important points.

Form CRS also includes suggestions for starting points for questions to ask your advisor. Please feel free to contact us at any time with these or any other questions.

Confronting Inflation, Fears of Recession

It's ugly out there. Inflation is at multi-decade highs, war rages in Ukraine, and recession fears mount. With all asset classes under pressure, even diversified portfolios are experiencing heightened losses, associated with rare periods of extreme stress. It's no wonder that consumer confidence is in the pits. But long-term investors understand this part of the economic cycle clears the dead wood, setting the stage for healthier, more stable markets ahead.

The burning question is now: are we in or entering a recession? For the first half of 2022, the S&P turned in its worst midyear performance in half a century, while bonds fared only slightly better. The economy grew over 6% in the first quarter, but inflation topped 8% for the same period, and the second-quarter figures are still being crunched. The consensus is that recession is likely, but there is no agreement on the timing or severity. Recessions are impossible to time accurately, especially given that economic data is backward-looking. One important and consistent fact applies to all recessions: they are temporary and will pass.

Of central importance to most consumers is the burden of inflation, especially the skyrocketing cost of energy. Diesel cost spikes and supply shortages have pushed up transportation costs for all goods, while soaring gas prices eat into consumers' disposable income, leaving less for buying other goods. There is very little the US can do in isolation to reduce the price of oil, which is priced as a global commodity; the jump in oil prices has been driven in part by reduced output (a hangover from the pandemic) and by Russia's brutal war in Ukraine.

On the home front, fighting inflation is the new top priority of the Federal Reserve. But it has been late to the game with its approach, which combines rate hikes and reductions to its bond portfolio. Mortgage rates have doubled in the past year, and some commodity prices for copper,

Index	6/30/2022	YTD
Dow Industrials	30,775.43	-15.3%
S&P 500	3,785.38	-20.6%
S&P Small-Cap	1,127.97	-19.5%
MSCI EAFE	1,846.98	-20.9%
Bloomberg US Bond	2,111.40	-10.3%
US Treas 10-yr yld	3.0%	

lumber, and used cars are now falling. Bond yields have risen steadily throughout the quarter, triggering painful short-term losses, but longer-term higher bond yields will ultimately reward savers.

In addition to ongoing supply chain problems, there's an imbalance in supply and demand in the labor market. Companies that slashed their payrolls during the pandemic are now finding it difficult to replace workers. Retirement within the baby-boom generation and limitations to immigration will likely keep the supply-demand balance disrupted for some time.

When investors become anxious, the natural reaction is to sell. But history shows that trying to time markets in this way is a huge mistake. Investing after markets have corrected and when consumer sentiment is low yields significantly better outcomes than investing when consumer sentiment is high.

Resisting Capitulation

Inevitably, when the markets get choppy, the common question asked is "What do I do now?" That question is driven by the effect of human instincts to react – a reflex to immediately seek shelter, to duck and cover. Those feel like the right impulses at the moment, because we fear that things could always get worse – which is always possible. But a better question to ask is "How have we planned to get through this?"

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Our Role As Fiduciaries

At Firestone, you will often hear us use the word “fiduciary”: in our contracts and formal documents, in conversation and discussion. But just what does the word mean? And why do we keep emphasizing it?

The word comes from the Latin word “*fidere*,” which means “trust.” It’s the same root that you’ll see in “*bona fide*,” “*fideli*,” and the Marine Corps’ slogan, *Semper Fidele* (“always faithful”). A fiduciary is one who is committed to act in good faith and in the best interests of their clients.

It’s more than just a word for us. Every recommendation we make, every piece of advice we give you, and every action we take on your behalf must be, first and foremost, in your best interests. If there is a conflict of interest, it must be resolved to your benefit – and, moreover, we will disclose and discuss the conflict with you.

Resisting Capitulation

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As clients of Firestone, chances are you have already planned to make it through, and planned well. Because of this, with regard to your investment policy, very little changes even in the face of a crisis, because life goals rarely change overnight. We are long-term, goal-focused, plan-driven investors. We own diversified portfolios of established companies; these companies have demonstrated the ability to increase earnings (and in most cases dividends) over time, thus supporting increases in their value. We own equity positions for growth, fixed-income positions for predictability, alternative positions for differentiation, and cash to support recurring distributions.

We act continuously on our financial and investment plans; we try hard not to react to current events, no matter how distressing they may be. More often than not, holding steady through tough times has produced the best outcomes for investors. Staying put is also one of the more difficult decisions to make.

After 30 months of chaos – the pandemic in all its variants, the election that would not resolve, roaring inflation (most painfully in stupefying gas price increases), the supply chain mess, war in Europe, and so on – we’re all understandably exhausted. That’s when the impulse to capitulate – to get to the illusory “safety” of cash – becomes strongest. So that’s when the impulse must be resisted most strongly. And that’s our job.

This, too, shall pass. We have helped clients get through tough times before, and we will continue to help. We are here to talk all this through with you at any time. Thank you for putting your trust in us. It is a privilege to serve you.

Better News for Cash

As the Fed moves to raise interest rates, there’s good news for savers, who are beginning to earn decent returns on cash again. High-yield savings accounts are starting to approach 1%, money market funds are at 1.3%, and 1-year Treasuries are yielding close to 3%, a rate we haven’t seen in over a decade.

Short-term individual treasury bonds are another of the more attractive cash reserve options today. These bonds can be purchased in your

existing Schwab account. Bonds can be laddered (purchased with staggered maturity dates), so your cash isn’t all locked up for the same period. Interest income on federal bonds is exempt from state taxes.

Another popular cash alternative, the US government’s Series I Savings Bond, has gained considerable attention recently. It has a variable rate, tied to inflation; with inflation so high, these bonds are currently earning 9.6% for the current six months. There are benefits and caveats to these bonds:

- Each person may only purchase \$10,000-\$15,000 in these bonds annually.
- The bonds must be purchased directly through the US Treasury website, which is an old, user-unfriendly platform.
- Your money is entirely locked up for 1 year. For the next 4 years, you can cash out the bond at will, but you will forfeit 3 months of interest.
- You cannot purchase these bonds in a trust account, and you need to designate a joint owner or beneficiary for each bond.
- Inflation will go back down at some point, and the bond’s interest rate will decrease. However, this type of bond can serve as an inflation-indexed cash reserve account.
- The interest accrues until you cash it in, or until the bond matures in 30 years. Federal taxes on the income are due after you cash in the bond.
- The bond’s principal is guaranteed by the government and does not lose value.
- The variable rate for the bonds resets every 6 months and cannot go negative.

Since we don’t know how long inflation will remain high or how fast it will subside, it’s hard to determine how long this bond will remain attractive. Each investor should determine whether the additional effort is worth the reward.

If you have ample cash in reserves, now is a good time to revisit your financial goals and make sure you are taking advantage of current opportunities. We are here to help you evaluate and consider all your options.