ALBION FINANCIAL GROUP

Guiding Clients To A Lifetime of Good Decisions

APRIL 2024

IN THIS ISSUE

From John Bird's Desk **Economy & Markets** **Planners Corner** **Albion Community**

INTRODUCTION

Welcome to spring and the second quarter of 2024. Thank you for reading Albion's quarterly letter, which features updates and insights from our leadership, investment team, and advisory team.

Our CEO and Co-Founder, John Bird, discusses some significant new reporting requirements that apply to smaller businesses. Then, CIO and Chief Economist Jason Ware discusses the state of the economy and the markets. Finally, Senior Wealth Advisor Patrick Lundergan assesses the financial planning landscape in 2024, highlighting current challenges and common withdrawal strategies.

We hope you find this information useful, and please contact us if you have any questions or concerns.

FROM JOHN BIRD'S DESK

Thanks to all of you who were able to join us at our annual Albion ski day. As most of you know our roots as a firm are in Alta, Utah. We began our investment management and financial advising journey in the basement of the Alta Lodge in 1982 and through the rest of the 1980's officed up at the end of Little Cottonwood Canyon. While we've long since moved down into the Salt Lake valley our hearts are still attached to that mountain oasis. On to this quarters' musings.

Money Laundering. Shell games. Hiding the true owner of assets for nefarious purposes. These are a handful of reasons behind one of Washingtons' efforts; the Corporate Transparency Act ("CTA"), a part of the

As of January 1, 2024, millions of startups and small businesses must file a Beneficial Ownership Information (BOI) Report with the U.S. Department of Treasury's Financial Crimes Enforcement Network (FinCEN).

Money Laundering Act of 2020. Turns out rule makers believe our current system of LLC's, Partnerships, and Corporations allow the actual humans who own these entities to hide behind a nearly impenetrable wall of structures to mask their ownership. And perhaps through these opaque structures engage in illegal activities with very little risk of being discovered. The purpose of this law is to pierce that veil.

Unfortunately this will apply to many of our clients. Those with closely held businesses, family partnerships and/or limited liability companies, and closely held entities will find themselves subject to the reporting requirements.

The provided information is not public. Rather, the gathering entity – the Financial Crimes Enforcement Network ("FinCEN") is authorized to disclose information to U.S. federal law enforcement agencies, with court approval to certain other agencies, to non-US law enforcement agencies upon request of a US federal law enforcement agency, and with consent of the reporting company to financial institutions and their regulators.

Prior to this act the burden of collecting beneficial ownership information fell on financial institutions. This shifts the burden to the entities themselves.

None of us are happy about additional reporting requirements and what feels like further intrusion of the federal government into our affairs. We could wax philosophic for paragraphs on the topic, but we'll spare you such a soliloquy. Instead, let's focus on who this applies to and what you must do to comply. To be clear we are not attorneys and nothing here should be considered legal advice. We encourage every reader to consult with counsel to determine if they have a reporting requirement under the act and if so to ensure reports are filed in a timely manner.

There are twenty-three exempt entities which can be

summarized in a few categories. First are financial institutions; for example banks, securities issuers, credit unions, bank holding companies, broker-dealers, money services businesses, securities exchanges and clearing companies, investment companies and investment advisors, venture capital fund advisers, insurance companies, state licensed insurance producers, entities registered with commodity exchanges, accounting firms, and pooled investment vehicles. These entities already have stringent reporting requirements.

The next significant category is made up of governmental entities. This includes federal, state and tribal entities and includes political subdivisions which means counties, cities, towns and school districts.

The final category are “large” operating companies. For this law “large” is considered to be companies with over twenty employees, over $5,000,000 in gross receipts from US customers, and with an operating presence at a physical office within the United States.

Know that the entities as outlined above are but an approximate summary of exempt organizations. It’s essential to dive into the details and if there is any question to retain counsel to determine whether or not your entity is exempt. Fines for non-compliance are punitive and run up to $500 per day which can accumulate up to $10,000. None of us want to get this wrong.

So what types of entities will be subject to the reporting requirements? Unfortunately many of the small family partnerships, LLC’s, trusts, and corporations we and our clients work with on a daily basis are subject to this law.

The information required with the reporting includes the legal name, any trade names, DBA’s or trading as names, the current street address and principal place of business, the jurisdiction of formation or registration, and the tax ID number. Beneficial owners must report their name, date of birth, residential address, an ID from an acceptable document (passport, US driver’s license), and the name of state or jurisdiction issuing the document. An image of the document must be provided and it cannot be expired.

Businesses in existence prior to January 1, 2024 must file by January 1, 2025. Businesses formed during calendar year 2024 must report within 90 days of creation of the entity and businesses formed after January 1, 2025 must file within 30 days of creation of the entity.

More information can be found through your legal counsel and online at fincen.gov/boi.

This quarterly note differs from the usual fare. However, given the circumstances, we believe it’s important to be front and center with all of you regarding this new requirement as year end (and the risk of non-compliance) will be here in the blink of an eye.

ECONOMY & MARKETS by Jason Ware

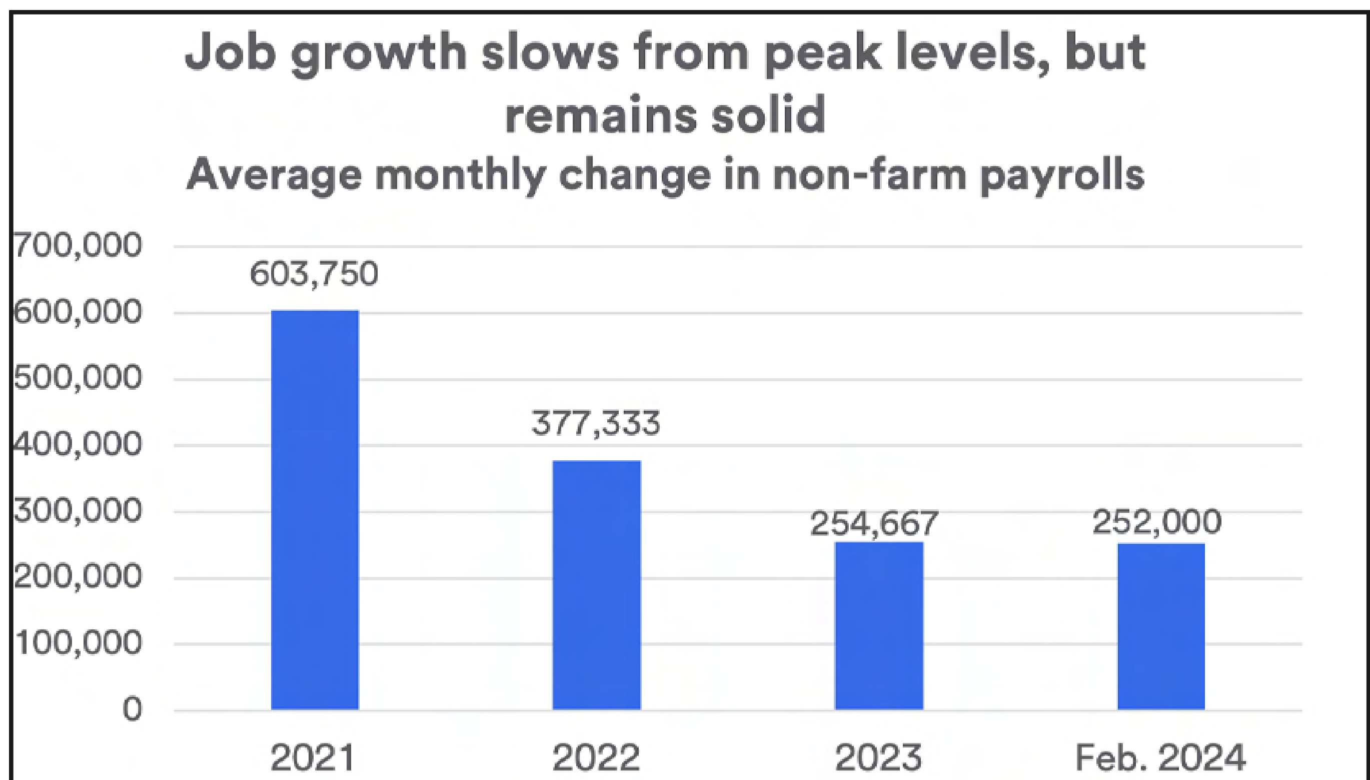
If something cannot go on forever, it will stop. Economist Herbert Stein articulated this principle nearly forty years ago when discussing growing trade deficits with lawmakers. This humble insight can be applied to many situations. These days it feels as though post-pandemic economic strength will go on forever. Yet, we know that it won’t. It can’t. Our central theme of “normalization” is evident over the past eighteen months, and eventually the business cycle will overcorrect causing recession (not to be feared *entirely* as contractions cleanse the system). But that day isn’t today. Indeed, as we exit the first quarter the US economy is doing fine. Better than fine really, it’s

quite robust. Consumer spending is resilient, jobs are plentiful, businesses are investing, and government budgets are expansionary. Real GDP grew by +2.5% in 2023, accelerating from the previous year, and estimates for Q1 sit around +2%. While these are backward-looking figures, more current information – like spending data from credit and debit card companies, retail sales, services PMIs, jobless claims, and even (recently) improving consumer confidence – suggests that momentum has carried into 2024.

But why the potency? The simple truth is economic strength is closely tied to jobs, which remains solid. And because the economy is strong that keeps the labor market strong as business profits support employment and wages. It's a virtuous loop. And while signs of normalization (there's that word again) in the labor are present, like softer demand for workers and increased supply, layoffs are low and hiring is steady. This balance is beneficial nurturing a more secure foundation. Until this situation changes, economic expansion should continue. The critical question now is, can we successfully move from too tight to well-adjusted in the jobs market *without* the pendulum swinging negative? Time will tell.

Inflation's stride has also cooled over the past 20 months, from over 9% to roughly 3%. While much progress has been made, Jerome Powell asserts more work and greater confidence in the trend is needed to declare victory. We agree. The Fed's target is ~2% and the "last mile" won't be easy. Still, our long-held view endures – the contemporary war against inflation will be won.

Speaking of the Fed, last July we opined that the central bank was done hiking interest rates. Be it lucky or good, that view proved correct. We continue to reason that the Fed won't need to raise rates further. We've gone from 0% to ~5.5%, a ton of credit tightening, and without a jump in unemployment. Job well done. The new Wall Street parlor game centers on how long the Fed will maintain its current stance before lowering rates. The answer hinges on the trajectory of



Source: U.S. Bureau of Labor Statistics as of February 29, 2024

the economy, employment, and inflation. Our best guess is the first cut will occur in the second half of this year.

All told, "soft landing" odds have increased compared to a year ago, a time when our preferred forward indicators signaled maximum caution. Several indicators have improved, meaning there's been considerable diminution of risk over the past year. At this point we see recession odds at about a coin toss (down from over 80%). Historically, in any given year it's ~15%.

In bonds, the action will likely be on the front end of the yield curve as big moves further out have mostly occurred. While things can move cyclically based on data and mood, structurally speaking longer duration securities appear sensibly priced for the current environment.

Meanwhile, firms are in good shape with profits holding steady in 2023. Despite “no growth”, revenues were higher last year due to an advancing economy and increasing prices. But so too were costs, in many cases more than revenues, resulting in compressed operating margins and inert profits. Looking ahead, analysts predict energetic earnings growth of +11% in 2024 and +13% for 2025, driven by a healthy economy and margin re-expansion. Those are high bars. From our perch, margins may have indeed bottomed *if* we can avoid a downturn. Thus the near-term direction of profits will largely hinge on the macroeconomy. Regardless, our primary attention is the longer-term outlook. Especially for those investments we own on your behalf. And here, we are optimistic for the years ahead.

For its part, the stock market has continued its momentum, driven by expectations of no recession and Fed rate cuts. Despite unease over the looming election, investor attitudes are (unsurprisingly) cheerful on the back of impressive recent performance.

Moreover, the inflation problem is under control and geopolitics, while tense, sit more at a simmer than a boil. Yet risks remain if fundamentals, including lofty earnings expectations, fail to deliver.

On valuation, there's some level of enthusiasm to be sure, particularly in areas like AI. However, at this juncture, this verve is probably more rational than irrational (paging Alan Greenspan and Bob Shiller!). As declared, the economy is sound, inflation is falling, the 10-year Treasury yield is off its peak, the Fed has finished raising rates, corporate earnings are ample, and technology is bliss. Given this backdrop, although the stock market is not exactly cheap, it is also not overly expensive when you consider where key factors like inflation, interest rates, and profits are expected to be in the coming years. Moreover, there is still approximately $6 trillion in cash "on the sidelines," mainly in money market funds, a portion of which (not all, but some) will likely seek higher returns when the Fed eventually begins to ease.

Bottom line: while short-term estimates vary, our longer run outlook for US equities remains wildly bullish.

As always, there is perpetual motion in economics and financial markets, so it's vital to make decisions based on the available information. We find great joy in this important vocation. Which I suppose leads us back to where we began, with Mr. Stein's observation … but with a twist. What happens if something, like the work of a steadfast financial advisor, *can* go on forever? Thanks for your unrelenting trust.

PLANNERS CORNER by Patrick Lundergan

Retirement planning in America is constantly transforming. The widely accepted concept that everyone can retire is only a few generations old. In such a rapidly changing world, how we achieve such a feat will also continue to evolve, which means that traditional approaches to securing retirement income need to be revised. Longevity is on the rise, traditional pensions (defined benefit plans) are becoming relics of the past, and the onus of retirement planning now squarely rests on the individual.

Given the statistical likelihood of living well into our 90s, especially for non-smokers and those of higher socioeconomic status, the necessity for robust and foolproof retirement planning strategies has never been more apparent. This reality drives us to rethink and innovate in how we protect your financial future.

When creating comprehensive retirement plans for clients, it is important to identify and address some of the potential hurdles future retirees face. I often return to a list that author Larry Swedroe coined as the *"Five Horsemen of the Retirement Apocalypse."* One of these five included "historically low bond yields," which is no longer as relevant today, but I still find this list useful when trying to understand how to best plan for our clients' futures. So, the following *Four Horsemen* remain top of mind for retirement planning in 2024:

- **Historically High Equity Valuations**: With the U.S. stock market's long bull run, it is wise to adjust expectations and prepare for potential downturns in equity investments.
- **Increased Longevity**: As life expectancy rises, retirement planning must account for potentially longer retirement periods, necessitating a portfolio that can last 30+ years.
- **Long-Term Care Costs**: With the likelihood of needing long-term care increasing with age, planning for these costs is essential to avoid financial burden and ensure quality of life.
- **Social Security and Medicare Benefits**: There's a chance that benefits could be reduced or taxes might go up to support these programs. We need to plan for multiple outcomes.

All we have to do is look at annuity sales in 2023 to see that consumers and advisors alike are turning to insurance contracts for peace of mind in the face of these headwinds. In ways, it's unfortunate to see a record 25% increase in year-over-year annuity sales, as often, it's primarily the agents who benefit from these products. Most annuity sales tactics use the same general concerns discussed above to incite fear and force quick action at the client's own peril. My general thought process for insurance and annuities is straightforward: insurance is a great risk transfer tool but an expensive way to invest. If an annuity contract cannot be clearly explained, including all fees and market-based outcomes, I'm not interested.

A critical, yet often missed, step in sound financial planning is customizing withdrawal strategies to suit individual needs. This should usually be the first move in crafting a tailored retirement income strategy. When done in concert with a comprehensive financial plan, customized retirement withdrawal strategies can provide greater financial security because they allow for flexibility. None of us know what the future holds and unlike an annuity contract that locks you into a particular set of terms with possible penalties for making changes, customized income strategies allow you to make adjustments at the margins or pivot when necessary as your retirement years unfold.

As we consider the often jarring transition from saving to spending, it is essential to understand the various withdrawal strategies for portfolio assets available in

retirement, which broadly fall into four categories:

- **Constant-Dollar Withdrawal:** Start with a fixed percentage, then adjust annually for inflation. It can suit those needing a consistent income to cover fixed expenses.
- **Constant-Percentage Withdrawal**: Withdraw a consistent percentage of your portfolio each year. Nice for those with flexible spending needs and lower fixed costs.
- **Variable-Percentage Withdrawal**: The withdrawal percentage adjusts based on your portfolio's annual value. Suitable for flexible spenders without the aim to leave a significant inheritance.
- **Spend Only the Income**: This approach only spends dividends and interest, preserving the principal. It suits individuals with low expenses compared to their portfolio size or those wishing to use their current asset base for legacy planning.

Note that *none* of these strategies are a set-it-and-forget-it approach. They are part of a *constant* discussion about how we can help you most efficiently and comfortably spend the money you have worked so hard to earn.

Morgan Housel's *"The Psychology of Money"* emphasizes the personal nature of financial decisions, reminding us of the wide variance in how people view and manage money. This diversity points to the absence of a one-size-fits-all approach to retirement planning. The goal is to find a strategy that aligns with your needs, ensures stability, and adapts to life's uncertainties.

As your financial planners, we're dedicated to navigating the complex landscape of retirement planning with you. If you have friends or family who require sound advice and a comprehensive review of retirement income planning options, please reach out and refer them to our team. Our goal is to ensure that our client's retirement strategies are not only robust and tailored to their needs but also flexible and ready to adjust to the constantly evolving financial world.

ALBION COMMUNITY UPDATE

As we conclude the first quarter of 2024, we look back a few weeks to celebrate a cherished tradition: our seventh annual client ski day. The event is an opportunity for the Albion team, clients, and guests to spend time together, conversing on the lifts, carving down the slopes, and savoring a meal in the warm comfort of the lodge, along with informative commentary from our leadership team. If you were able to join us this year, thank you for attending. We look forward to carrying this tradition on for years to come and we hope everyone can join us, even if not to ski, but to enjoy the comradery of fellow clients and your Albion team.

ALBION FINANCIAL GROUP