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I. Secure Act 2.0 Broadens 529 College Savings Plans:

While most of us were on holiday around the end of 2022 (or licking our wounds from both stock and bond investment losses in 2022), the Secure Act 2.0 was passed. The law makes dozens of changes which affect saving for retirement, etc. I'd like to highlight one of the provisions:

In an article from *Forbes*, found on *Apple News* on my I phone, there is news of interest to parents and grandparents who are assisting relatives/children with saving for college. Section 529 plans have been around for a long time, and each state sponsors a plan. I do not directly manage investments within such plans but I recommend that parents/grandparents use whatever state plan is administered by Vanguard because it is bound to be the lowest cost plan.

In a 529 plan there are contributions to an account in the name of a beneficiary to assist the beneficiary with education expenses. Education is not limited to college costs, but this is the emphasis for most savers. Here is discussion of the change to the plans from the *Forbes* article, entitled (in a bit of an overstatement): "How a 529 Plan to Child IRA Conversion Can Turn Your Teen into a Middle-Class Millionaire."

> "There's been a problem with 529 plans from their very beginning. They've always been a gamble. You gambled your child would actually go to college. You gambled your child would not earn a scholarship. You gambled you would put too much money into the 529 plan.
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> Why is the 529 plan a gamble?
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> When you put money into a 529 plan, you lock it up forever. You can only use that money to pay for qualified education expenses. Keep in mind not all education expenses are qualified.
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> Secure 2.0 has changed that. Beginning in 2024, excess funds in 529 plans can be converted to Roth IRA savings for your child. This change addresses the reluctance of many to use the 529 plan as a savings tool.
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> Patricia Roberts, COO at Gift of College, Inc… says 'Grandparents may find comfort in knowing that if the funds they invest on a particular grandchild's behalf are not ultimately utilized for higher education pursuits, they can be rolled into an account that can benefit that grandchild later in life (in their retirement years) and may even be used toward a first-time home purchase (since Roth IRAs allow for this under specific circumstances).'
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> But there are restrictions you need to pay attention to.

An Illinois wealth adviser states, 'There's a $35,000 lifetime cap on transfers to a Roth. Rollovers are subject to the annual Roth contribution limit. (The limit is $6,500 is 2023.) The rollover can only be made to the beneficiary's Roth IRA—not that of the account owner. A bigger issue is that the 529 account must have been open for at least 15 years, and the accountholders can't roll contributions, or even earnings on those contributions, made in the last five years. This may make the process a bit trickier.'

…"If you have a current 529 plan, the age at which you can convert it into a Child IRA for your child will depend on how old your child was when you established the 529 plan. According to Morningstar, on average, parents start 529 plans when a child is seven years old. Because of this, Morningstar says the child will miss out on $30,000, by not establishing the 529 plan when the child was born (this assumes parents save $50,000 spread equally throughout the life of the 529 plan). If you start the 529 plan when the child is 7, you won't be able to begin the conversion process until 15 years later, when the child is 22. If you start the 529 plan when the child is a newborn, the conversion process begins at 16. How much money does the 7-year old lose versus the newborn? Again, assuming an 8% long-term return (vs. an 11% historical average), the 7-year old's Child IRA will grow to $1.3 million when retiring at age 70. The newborn Child IRA, on the other hand, grows to $2.1 million at age 70. That's a difference of more than $750,000."

Smartt comment:

The figures in the preceding paragraph contain a lot of "blue sky." A good bit of multi-year planning and significant front-end investment may be required. And $1.3 million to $2.1 million will buy a lot fewer loaves of bread in 65 years in the future than it does now.

If you have an interest, I'd be pleased to email/mail a copy of the article to you.

II. What are YOUR and MY Asset Allocations?

Each of us has a different ability to live with uncertainty (risk) and so our investments will be different:

As of December 31, 2022	Clients	John Smartt
Money Market Funds	1.4%	0.3%
Bond Funds	27.4	18.4
Stock Funds	71.2	81.3
Totals	100.0%	100.0%

Remember each of us has different goals and needs, and our asset allocation should fit us and our family.

If you have questions about your asset allocation, or your retirement plan investments, I'd be pleased to assist.

III. Vanguard Rates of Return (through Latest Quarter End)

Performance percentages are per ***Morningstar.*** Amounts in parentheses are percentile rankings. (1= best and 100= worst) within category.

Periods ended December 31, 2022	Yr.-to-date	5 Years	10 Years

Total Stock Market Index Admiral	**-19.5%**	(75)	**8.7%**	(50)	**12.1%**	(35)
Tax-Managed Capital Appreciation Admiral	**-19.1%**	(68)	**9.2%**	(33)	**12.5%**	(13)
Tax-Managed Small Capitalization	**-16.1%**	(46)	**5.9%**	(26)	**10.8%**	(6)
REIT Index Admiral	**-26.2%**	(61)	**3.7%**	(50)	**6.4%**	(34)
Total Int'l Stock Index Admiral	**-16.0%**	(57)	**1.1%**	(56)	**4.1%**	(60)
Balanced Index Admiral	**-16.9%**	(79)	**5.5%**	(22)	**7.8%**	(18)
Total Bond Market Index Admiral	**-13.2%**	(41)	**0.0%**	(33)	**1.0%**	(38)
Int.-Term Invstmt.-Grade Bond Admiral	**-13.8%**	(18)	**0.7%**	(30)	**1.8%**	(61)
High–Yield Corporate Bond	**-9.1%**	(28)	**2.2%**	(30)	**3.6%**	(28)

For comparison, here are several stock and bond benchmarks:

Periods ended December 31, 2022	Yr.-to-date	5 Years	10 Years
S & P 500 (large stocks)	**-18.1%**	**9.4%**	**12.6%**
Russell 2000 (small stocks)	**-20.4%**	**4.1%**	**9.0%**
MSCI World Index	**-18.1%**	**6.1%**	**8.9%**
Bloomberg US Aggregate Bond Index	**-13.0%**	**0.0%**	**1.1%**
ICE BofA US High Yield Master TR (bond index)	**-11.2%**	**2.1%**	**3.9%**

Vanguard mutual funds and ETFs (exchange-traded funds) continue to perform as expected. I expect each Vanguard fund or ETF, for each ten-year period to be in the top 1/3 before taxes based on low cost, and they ought to be in the top 1/4 (stock funds) after income taxes.

The Vanguard High Yield Corporate Bond fund takes significantly less risk than the average "high yield" (also known as "junk bond") fund. The Vanguard fund, which takes less risk, continues to rank highly in the rankings over the last ten-year period. Over the last ten years the Vanguard fund has captured most of the excess of junk bond returns over good quality bond returns—meeting my expectation. I continue to believe that, for tax deferred accounts, this fund is a reasonable, additional diversification, and it comprises some of my personal bond holdings.

If you have questions about your investment asset allocation, please contact me.

IV. Rainy With Sunny Breaks:

From the World Ahead 2023 edition of *The Economist Magazine*, released in December, 2022, subtitled "The American Economy is Set for a Downturn, Not a Crisis:"

> "Start with the bad news, America is heading for a recession in 2023. Over the past half-century, whenever inflation has reached an annual pace of more than 5%, it has always taken a recession to wring it out of the economy…The current episode of inflation will be no different. Only when growth truly goes negative will America be able to contain its rampant price pressures.
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> A churl would point out that American growth was already negative in the first half of 2022. That technical decline coincided, however, with a remarkably robust labour market such that the boffins at the National Bureau of Economic Research, whose job it is officially to identify recessions, demurred

from declaring one. In the coming year [2023] they will not be so reticent. As growth softens, the unemployment rate will climb, leaving little doubt that America's economy is in fact contracting.

The proximate cause of the recession will be the Federal Reserve, which is set to continue tightening monetary policy in 2023. In September, 2022 the median forecast of Fed officials was that they would raise interest rates to a floor of 4.6% in 2023, up from 3% now [December, 2022]. But inflation will still be frustratingly persistent in the new year, so they will probably go beyond that, taking rates up to about 5%. Financial markets, already under stress from all the rate rises in 2022, will face fresh worries as indebted companies and spendthrift households struggle to cover their elevated interest costs.

But it will not be all gloom. There is reason to think that the coming recession will be mild. Throughout the past year the number of open jobs has far outstripped the number of available workers. The implication is that even if a growth contraction leads companies to pare back their hiring plans, they are likely to refrain from large scale lay-offs. The unemployment rate will inch up from the lows of 2022, but it will not rocket up, as has typically been the case in previous recessions.

America has plenty of additional buffers that will help cushion the impact of a downturn. That is thanks in large part to the long half-life of pandemic era stimulus programmes. At the end of 2021 state governments were sitting on cash reserves of more than $250 billion, roughly twice as much as in 2019. Households have about $1.5 trillion in excess savings compared with before covid. Businesses have also build up solid rainy day funds. All of these reserves will be whittled down by a recession but they should be sufficient to forestall giant spending cuts, even if growth slows.

The picture of the American economy will change markedly over the course of 2023. Disinflation will eventually take hold, turning into outright month-on-month deflation when the recession strikes. That ought to spell the end of the Fed's rate increase cycle by the middle of the year, with the focus instead shifting to when it might start to loosen policy. The Fed will be in no haste to make big rate cuts, having fought so hard to rein in prices. But the combination of a recession and fast-diminishing inflation will head it to trim rates before the end of 2023, in an attempt to ease the downward pressures.

…The bloom may come off the big-spending rose. Even as growth slows, it will be hard to find the workers needed to deliver big [infrastructure and environmental] projects, which will drive up their costs. There will also be growing criticism of the government's ambitious investments as wasteful, especially in semiconductors, as that industry swings from global undersupply to oversupply.

By the end of 2023 the American economy will be climbing out of its mild recession, with inflation in retreat. Instead the concern will be whether America's costly plans to re-engineer its industrial landscape, guided heavily by the government, amount to a clever strategy or a hubristic mistake."

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