GLOBAL WEALTH ADVISORS LLC
Registered Investment Advisor

INSIGHTS

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Why I'll Always Be Optimistic About the Market

Dimensional Fund Advisors LP
Dec 14, 2021

It's hard to believe we're approaching the end of the second year of this global pandemic. Despite the pain and loss endured by so many all over the world, I hope some positive changes have come from the shock we've all been forced to experience. As we look forward to 2022, despite continued uncertainty, I'm feeling a sense of educated optimism that's stronger than ever before. Why? Because over the past two years, my beliefs have been tested more than ever. And they've held up.

At the start of 2020, before we knew the extent of the global pandemic we were headed toward, I reminded investors that the market has no memory and encouraged them to avoid making forecasts and timing markets based on predictions of the future.

A few months later, I thought that human ingenuity would lead our way through the crisis. It has. I didn't know when a vaccine would be available or who would make it, but I never doubted the power of so many great minds focusing on one huge problem.

When we were in the midst of March 2020 and the S&P 500 was down 20%, it was scary.[1] I wrote then that we can't control crises, but we can control our response to them. Those who could stay in the market were rewarded. Over the next 12 months, the S&P went up 56%.[2]

When you're entrusted with investors' hard-earned money, as we are at Dimensional, it's gratifying to see that the choices you make can lead to good outcomes.

So now we find ourselves at the doorstep of 2022, and we've just seen the S&P 500 hit record highs—again. But not all investors perceive this as good news. Record highs make many people nervous, because they think that what goes up must come down. When markets are working as they should, reaching record highs with some frequency is exactly the outcome we would expect. That makes intuitive sense, because if stocks didn't have a positive expected return, no one would invest in them.

This brings me to why I'm always optimistic about the power of markets, and why I always bet with them rather than against them: Markets represent people coming together. We can't predict the nature or timing of a crisis, but we can

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A Personal Note From Global Wealth Advisors

The US stock market Indicies are having another strong year with returns in the double digits. We are also experiencing some of the highest inflation rates going back almost four decades. To help combat this, the Fed recently announced that it will more quickly reduce and end its bond purchase programs this year. This program is what helped drive down interest rates for things like mortgages and consumer loans, in an effort to help stimulate the economy.

Gross Domestic Product (GDP) for 2022 is projected to be lower at around 3.0%. However, consumers are still spending money and as the supply chain catches up, purchases of big ticket items like cars and home furnishings should increase as well. Therefore, the economy should continue to grow even without the Fed QE program and the possibility of increases in interest rates.

Lastly, the 800 pound Gorilla in the room is the new Omicron variant of COVID. Modern medicine has allowed us to protect against and treat the effects of the virus much better than we could in the beginning. Hopefully, this will continue to be the case as we continue to adapt and migrate through the two plus years of this "new normal". We say stay invested and fasten your seat belts, as we may experience some investor turbulence.

Jim Knaus Mike Krencicki

How TIPS Can Boost Retirement Readiness

Dimensional Fund Advisors LP
October 21, 2021

The recent surge in inflation shows how the cost of goods and services can increase quickly and unexpectedly. To help plan participants maintain a stable standard of living in retirement, plan sponsors can provide an investment solution designed to accumulate a stream of inflation-protected income using Treasury Inflation-Protected Securities (TIPS). As recent Dimensional research confirms, TIPS are the most appropriate asset to provide protection against unexpected inflation. That protection makes TIPS an ideal asset class for plan participants seeking inflation-protected income in retirement.

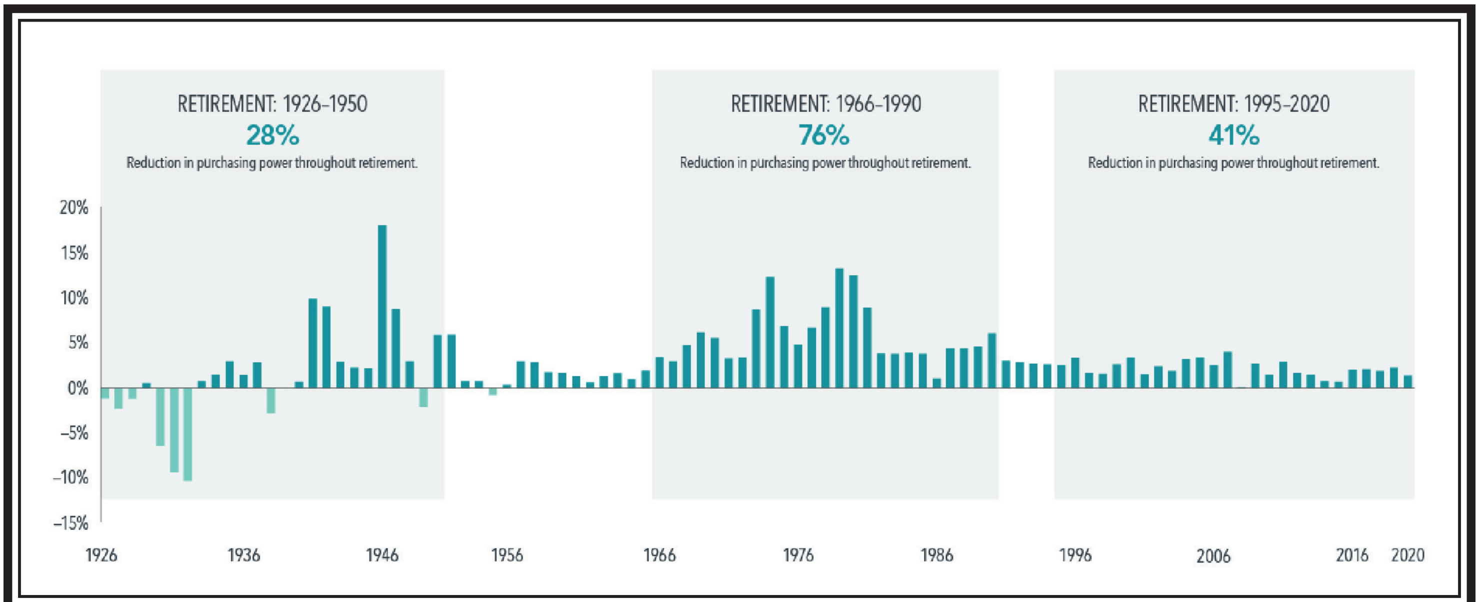
Let's examine how TIPS work and why they were created in the first place.

The goal of a retirement plan (when combined with Social Security) should be to enable retirees to maintain the standard of living they enjoyed in the years before retirement. Social Security itself offers inflation protection because benefits rise when the Consumer Price Index (CPI) increases, providing an income stream that is "constant" in terms of units of income. When the US Treasury Department designed and issued TIPS in January 1997, the purpose was to provide households with an asset class fully protected against inflation. Accordingly, the Treasury issued TIPS, which are bonds whose principal and interest payments are linked to the CPI.[1]

Exhibit 1 shows that investors who retired in 1926, 1966, or 1995—and spent 25 years in retirement—experienced a significant loss of purchasing power due to inflation. TIPS may provide a hedge against unexpected inflation because their principal is adjusted up (down) based on the actual inflation rate over the life of the securities. When TIPS mature, the investor receives the greater of the original principal amount or the inflation adjusted principal. Therefore, TIPS can be the building blocks that provide real retirement income to supplement Social Security benefits.

Plan participants should hold a portfolio of TIPS designed to provide a stream of real (inflation-adjusted)

Exhibit 1 - Annual Changes In Inflation and Loss of Purchasing Power



A 25-year retirement is assumed in calculating the reduction in purchasing power. Inflation is measured by annual changes in Consumer Price Index. Data from Stocks, Bonds, Bills, and Inflation Yearbook, Ibbotson Associates, Chicago. Roger Ibbotson is an Independent Director of Dimensional's US mutual fund board.

income in retirement. A participant's consumption in retirement could be thought of as an annual series of cash flows (liabilities). We define the term "retirement liability" as the present value of that stream of retirement income. To eliminate interest rate risk associated with retirement income, what's needed is a strategy of hedging (or matching) that liability using a plan participant's investment portfolio. That strategy is known as duration matching.[2] As real (inflation-adjusted) interest rates increase, the present value (cost) of those future liabilities will decrease based on their duration and the rise in real rates. Conversely, as real interest rates decrease, the present value (cost) of those liabilities will increase based on their duration and the fall in rates. To adequately fund those future liabilities, the duration of the TIPS portfolio should match the duration of the liabilities.

As such, the value of the participant's liabilities and assets should move in tandem with changes in interest rates. As participants approach retirement and reduce their allocation to growth assets (which are generally equities), they should be systematically shifting to a portfolio of TIPS with a duration equal to the series of cash flows needed in retirement.

DIMENSIONAL'S TIPS STRATEGY

Dimensional Fund Advisors created a series of Target Date Retirement Income Funds that apply lifecycle research from the field of financial economics. A key principle is that people have two sources for funding retirement: financial capital (current savings) and human capital (expected future earnings). The balance of these change over time, with young plan participants having more human capital than financial capital and participants closer to retirement having more financial capital than human capital.

Through time, as human capital is converted into financial capital, it is important to try and balance the risk between growth and income assets. In a participant's early working years, Dimensional's funds focus on income-growth assets (a diversified portfolio of stocks and global bonds). Over time, as human capital depletes and financial capital grows, growth assets are gradually invested in a TIPS strategy. The TIPS investments seek to minimize the impact of interest rates and inflation on retirement consumption by matching the duration of the TIPS with the duration of the participant's consumption in retirement.

Once a participant reaches retirement, the focus of the allocation is on providing clarity and confidence about how much consumption the savings can support, so the majority of the assets in the funds are invested in an income risk management strategy that includes TIPS. Following this approach helps investors transition from their working life into retirement. ●

1. See Michelle L. Barnes, Zvi Bodie, Robert K. Triest, and J. Christina Wang, "A TIPS Scorecard: Are They Accomplishing Their Objectives?" Financial Analysts Journal, 66:5 (2018): 68–84.
2. Duration measures the sensitivity of an asset or liability to changes in yields. Duration matching is a common approach for managing a liability-driven investment strategy.

Why I'll Always Be Optimistic About the Market

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bank on human ingenuity finding a path through it. Markets are forward-looking and reflect this optimism—an optimism that I believe is innate to humanity. And your optimism only increases when you begin to understand how markets work.

How we deal with uncertainty is the central challenge of human existence. We are defined by the choices we make, but we never have all the information we want. So what do we do?

It pays to have a philosophy to guide our choices, in investing, and in life. In conversations with investors over the years, I've explained my philosophy about markets in different ways, but what all these descriptions have in common is choosing to side with human ingenuity rather than against it. Betting against the market is exhausting, and we believe that it doesn't pay.

So at the end of every year, we look back and forward. What do we think the next year will bring? I don't know. No one does. Think about it: No one does. After these last two years, this lesson should be obvious to all of us.

But for the past 50 years, I have held a long-term faith in the power of markets. When they go up or down, I see them simply responding to new information. The market always wants buyers and sellers to make a deal. Transactions only happen if people agree on a price that seems fair to both sides.

In 2022, new challenges await. New businesses will grow. Old ones will adapt. Some will fail, while others flourish. Rather than having to guess what will happen to whom and when, I choose a different path. I invest in the market. It is a unique human invention. From it flows our modern life. Most of us live in a world where we go to the store or pick up our phones and see choices I could not have imagined as a boy. So, of course, I am optimistic. And, of course, there is more work to be done. The problems we face as humans are daunting. That has always been true. I was born at the end of World War II and before a vaccine for polio. I wake up every morning believing the market will go up a little but prepared for if it drops. And you should too. Markets will go up and down, but you should expect them to be positive, and that is what history has also shown. If you can hold this in your heart, you can be optimistic and resilient, you can manage the central challenge of human existence. It's hard to do. But it's worth it. ●

1. S&P data © 2021 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.
   Indices are not available for direct investment. Index returns are not representative of actual portfolios and do not reflect costs and fees associated with an actual investment. Decrease of 19.6% was from Jan. 1, 2020–March 31, 2020. Increase of 56.35% was from March 31, 2020–March 31, 2021.
2. Past performance is no guarantee of future results.

Happy

NEW YEAR

2022

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