APPLETON PARTNERS, INC.

Fortifying Financial Decision-Making

An Approaching Demographic Sea Change

Generation X households are likely to inherit a staggering $30 trillion in wealth over the next 25 years and overtake the Baby Boomers as America's wealthiest generation.[1] The magnitude of this dynamic has caught the attention of wealth management professionals, and what is unfolding in an aging America is also likely to have a profound effect on individual relationships with money.

Looking forward, we see a need for many of our clients to find a way to draw younger family members into their estate and overall financial planning process. Doing so can be integral to helping the next generations not only more successfully manage potential future inheritances, but also navigate their own financial lives in a society that has rapidly pushed responsibility onto the individual. These two challenges are quite different in certain respects but similar in terms of the need to understand financial concepts and ultimately make good decisions. How prepared are your children and grandchildren to tackle a lifetime of investment and related economic matters?

Ensuring Intergenerational Success

The importance of engaging family members in personal financial matters has been amplified by a profound change in the relationship between employment and retirement over recent decades. Our once paternalistic system of pension plans complemented by Social Security has clearly receded with only 15% of private-sector workers currently having access to a Defined Benefit plan.[2] The demise of private sector pensions has placed a burden on individuals, many of whom are entering the work force or moving through their peak earning years without sufficient financial background or guidance.

As advisors, we often find that clients measure the ultimate success of their wealth management plans at least partially through the extent to which their legacy and family objectives are realized. Ensuring loved ones have adequate financial know how as they navigate their careers and personal lives is a key ingredient in successful multi-generational wealth management. What might facilitate future success in this regard and how can Appleton help?

It Starts with Financial Literacy

Establishing a baseline level of knowledge and experience can help your loved ones understand and carry out your wealth transfer and legacy wishes, while also bolstering their ability to make wise economic and investment decisions in other aspects of their lives. Whether it relates to establishing and adhering to a long-term asset allocation strategy, building retirement savings, funding education and other future liabilities, mortgage financing and debt management, constructive involvement with you and your portfolio team can be beneficial.

As a practical example of the challenges many face, consider that a 2022 TIAA Institute study revealed that US adults could only answer 50% of basic financial literacy questions correctly and a mere 36% relating to investment risk (defined by the uncertainty of investment outcomes).[3] Furthermore, while education and income were found to be positively correlated with financial literacy, those earning $50,000-99,999 and greater than $100,000 annually fared only marginally better, answering 51% and 60% correctly.

Absent adequate financial knowledge, managing an inheritance, navigating turbulent market cycles such as we are currently experiencing, or simply taking the right steps to build long-term retirement savings can be more difficult. As a society, we have not prioritized financial literacy, yet resources are available, one option being through The National Endowment for Financial Education.

Take Proactive Action Steps

So, how does Appleton fit into the equation? Above all, we encourage clients to think about where they see planning and educational gaps within their families. No one approach works for everyone, although we suggest leveraging our resources to help subsequent generations become more conversant and comfortable with wealth management and your specific plans.

Our Private Client Services team prioritizes offering practical, easily digestible guidance concerning multi-generational planning issues. We recognize the magnitude of the challenge and are trying to help in part by providing information that can be easily shared with other family members. Our financial planning webinar series tackles topics such as "Financial Consequences of Adulthood," "Equity Analysis Concepts," and "Women and Financial Planning," among others. We also emphasize short written briefs that cover matters such as social security distributions or college planning. Our goal is to raise awareness and share actionable advice. We encourage you and your family members to visit our website to access a variety of content of this nature.

Personal finance hardly needs to become one's hobby. What matters is ensuring your loved ones possess a sufficient level of knowledge and understanding of the core concepts that will ultimately impact their ability to manage often complex financial lives, a process that may also one day involve an inheritance. Drawing family members into your planning process can be a good way to start. Your Appleton portfolio management team is here to help, and we encourage your input into what might work best for your family.

1. Cerulli Associates
2. March 2021 National Compensation Survey from the Bureau of Labor Statistics
3. 2022 TIAA Institute-GFLEC Personal Finance Index (P-Fin Index) — an annual survey measuring US adults' financial literacy levels across eight functional areas.

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MARKET OBSERVATIONS & IMPLICATIONS

Tax-Exempt Investment Grade Municipals

- Yields marched higher in Q2, albeit not on a straight-line basis, as the 10-year AAA hit an intra-quarter high of 2.99% only to grind lower to 2.43% by early June before ending Q2 at 2.72%.
- The municipal curve also steepened, raising the 2s to 10s spread to 77 bps.

	3/31/22	6/30/22	QTD change
2-yr AAA Muni	1.76%	1.95%	+19 bps
10-yr AAA Muni	2.18%	2.72%	+54 bps
30-yr AAA Muni	2.53%	3.18%	+65 bps

- We have used yield curve steepening as an opportunity to target exposure in the 3 to 12-year maturity range.
- After a 75-bps increase at the June meeting the Fed Funds rate is now 1.50% - 1.75%. The Fed is expected to hike another 75 bps in July and 50 bps in September. Two more 25 bps increases in Q4 would bring Fed Funds to 3.25%- 3.50% by year-end.
- We believe that the municipal curve has largely priced in these rate hikes. The curve could steepen a bit further though as front-end yields trade lower, particularly if the Fed begins to pause later in 2022 and into 2023.
- Municipals look attractive relative to USTs with the 10-year ratio ending Q2 at over 90% vs. a 52-week moving average of 78%.
- Retail fund flows remain negative with aggregate net YTD outflows of $76B marking the largest outflow cycle since 1992. More than 52% came out of long maturity funds, with intermediate and high yield accounting for 27% and 17% respectively.
- Selling pressure has pushed credit spreads wider. The 10-year AAA – A spread of 47 bps is up from 22 bps on 12/31/21, while AAA-AA spreads of 27 bps exceed the 10-year average of 19 bps. We are finding value in certain A rated bond issues.
- Municipal issuance has slowed considerably in 2022 after two record years, a dynamic that may have limited the impact of the market sell-off. June issuance was down 46% YoY, and YTD is lagging by 15%.
- Seasonality should be a positive technical factor and JPM expects net negative issuance of $33B over June, July, and August.
- Credit has underperformed in a weak performance environment with the "BBB" rated segment of the municipal market returning -11.33% YTD while the "AAA" rated segment returned -8.51%.

Investment Grade Corporates & Treasuries

- IG Corporates spreads widened during Q2 as recession fears grew. The Bloomberg Barclays US Corporate Bond Index saw OAS reach 155 bps by the end of June, the highest level since June 2020. Our upper investment grade focus should be well positioned in this environment.
- Credit fundamentals remain strong though and we see favorable technicals having an offsetting positive influence on the direction of OAS.
- IG Corporate supply is down 9% YoY and issuers remain cautious about coming to market in an unsettled environment.
- Weak economic data and growing recessionary fears drove down UST yields to close Q2. The curve declined by roughly 12 bps during June with the 10Yr ending at 2.88% after reaching a 2022 high of 3.48% on 6/14.
- Our UST trading range over the remainder of 2022 is 2.75 – 3.40%. With consumer demand and sentiment lagging, we do not anticipate a significantly higher UST yield move from here. Treasury supply is also slowing considerably.

Equities

- The S&P 500 fell -16.1% in Q2 to bring its YTD return to -19.9%. Q2 was the weakest since the height of the pandemic and the first 6 months of 2022 marked the worst start since 1970. The tech-heavy Nasdaq fared even worse, closing at -29.2%.
- All 11 sectors finished Q2 in the red with outperformance from Consumer Staples, Utilities, and Healthcare. Growthier sectors such as Consumer Discretion, Communication Services, and Technology stocks led declines. LC Growth trailed LC Value by 8.7% (-20.9% vs -12.2%) in Q2 to bring the YTD gap to a whopping 15.6%.
- Inflation remained a big drag on risk appetite with May's CPI of 8.6% representing the largest annual increase since 1981. The Fed's commitment to tame inflation led to a more aggressive pace of rate hikes and balance sheet runoff. Tighter financial conditions appear to be having the desired effect of slowing the economy, raising hopes for a pause later in 2022.
- Valuation contraction has driven down equity prices with the S&P 500 forward multiple falling from over 21x to 15.8x on a YTD basis. Q2 earnings are now top-of-mind and failure to post nominal YoY growth could prompt further pressure on equities. Consensus estimates have moderated and now call for +4% growth for the quarter and +10% for all of 2022.
- The path of least resistance has been to the downside, although sentiment is washed out and several technical indicators point to the market being oversold. Ultimately, a dovish Fed pivot might be the catalyst the stock market needs to find a floor.

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