AUGUST 2023 ISSUE 7

THE LEGACY INSIDER

THE OFFICIAL NEWSLETTER OF THE LEGACY FINANCIAL GROUP

BRENT SCHUTTE, CFA | JUN 19, 2023

Declining Inflation and a Pause by the Fed Sends Markets Higher

Brent Schutte, CFA, is chief investment officer of the Northwestern Mutual Wealth Management Company.

Equities continued their recent march higher last week with the S&P 500 notching a fifth consecutive week of gains and hitting highs last seen in April 2022. The Federal Reserve's decision to hold rates steady, along with inflation data that showed prices rising at the slowest pace in more than two years, sparked a wave of buying even as the Fed indicated it may raise rates two more times by year end.

Progress in the deflationary process was evident in the latest Consumer Price Index (CPI) release, which shows that headline inflation grew at a scant 0.1 percent in May, down from April's rate of 0.4 percent. On a year-over-year basis, prices rose 4 percent, marking the slowest 12-month increase since March 2021.

GREETINGS FROM PHOEBE & JOSH

Welcome Friends & Family!

We hope you've been enjoying your summer so far and had a great 4th of July holiday.

We are excited to announce we have a new intern. Kaia Story, arriving one week early. Phoebe and Matt welcomed baby Kaia on May 23rd to the Legacy Family , pictures on page 8.

In this issue of the Insider we've included commentary on the recent and current market conditions, as well as information on life insurance. Specifically, how it can be utilized in your retirement.

As always, let us be a resource to you. If you have any questions or would like to schedule a call please don't hesitate to reach out.

Be safe and enjoy your summer!
Cheers,
Phoebe and Josh

Both the monthly and year-over-year increases were lower than Wall Street expectations. Shelter was once again a driving force of the increase in headline readings, with an increase of 0.6 percent for the month. On a year-over-year basis that category was up 8 percent in May, a decrease of 0.1 percent from the prior reading. As a reminder, shelter has a large and lagging effect on inflation readings in services (it accounts for 34 percent of the total CPI measure and has around a 12-month lag).

As we've noted in previous commentaries, given the lagging nature of the shelter reading, we believe it is useful to evaluate price pressures after stripping out this backward-looking measure. Doing so highlights the significant progress made in bringing inflationary pressures down. Since the surge in CPI readings that took place in May and June of 2022, prices excluding the shelter number are up just 2.1 percent annualized on a non-seasonally adjusted basis and up 0.4 percent when adjusting for seasonality. Put simply, when excluding the lagging shelter reading, all-in inflation is running at a level consistent with the Fed's stated target. We highlight the rate following the June peak to show why we believe year-over-year CPI readings are set to tumble in the coming months as the extreme increases from May and June roll off the twelve-month total.

Core CPI, which excludes volatile food and gas prices, rose 0.4 percent in May, unchanged from April's reading. On a year-over-year basis, the core reading came in at 5.3 percent, down from April's rate of 5.5 percent. Although still elevated, it's important to note that the latest year-over-year reading is the slowest 12-month increase since November 2021. Once again, if shelter is taken out of the equation, core CPI drops to 3.4 percent year over year and stands at just 2.8 percent annualized during the past nine months.

Dissecting the data further reveals that food and shelter combined have been significant drivers of high year-over-year readings. When those two categories are removed, all-in inflation is up a meager 1.1 percent, below the Fed's long-term target of 2 percent. It's worth noting that the latest report showed food prices have moderated and were up just 0.2 percent month over month.

Further evidence that inflation pressures have largely retreated save for a few pockets can be found in the latest data from the Atlanta Federal Reserve Bank's so-called Sticky CPI-Ex Shelter measure, which shows that core "sticky" inflation, excluding lagging shelter, is running at an annualized pace of 1.59 percent in June, down from a three-month annualized rate of 2.5 percent. On a year-over-year basis, the measure is up 3.9 percent.

Similarly, the Cleveland Federal Reserve calculates an inflation reading called the 16 Percent Trimmed Mean CPI that excludes abnormally high and low categories. The last three monthly readings of this indicator show price increase percentages of 0.22, 0.33 and 0.22, respectively. This highlights that inflation pressures in most categories are at or approaching the Fed's stated target.

The purpose of this deep dive into various inflation measures is to underscore why we believe the battle against rising prices is well on its way to being won. However, given the fact that the Fed's forecasts for the remainder of the year call for two additional 25-basis-point hikes, we believe some members of the Fed may not be willing to rest until the seemingly resilient job market weakens and results in a recession. While wage pressures have retreated in recent months and wage expectations remain muted, the threat of a resurgence in wages that could be used to pay ever-higher prices appears to continue to haunt some members of the Fed. As such, we continue to believe there is risk the Fed will overshoot to the upside on rates, and the economy will slip into a shallow, mild recession.

Wall Street Wrap

Here are some of the other items that caught our attention in a week of light data.

Input costs recede further: Producer input final demand dropped in May, coming in at -0.3 percent, according to the latest Producer Price Index (PPI) from the Bureau of Labor Statistics. The latest reading marks the second in the past three monthly reports in which prices fell. On a year-over-year basis, the headline PPI is up 1.1 percent, down from May's reading of 2.3 percent, which was below market expectations and at the lowest level since December 2020. Core PPI, which strips out volatile food and energy, was unchanged in May and was up 2.8 percent on a year-over-year basis, which was the lowest 12-month reading since January 2021. The PPI measures price increases for finished goods leaving the factory; it is generally a forward-looking measure of where prices for consumers are headed. As the costs producers face for finished goods continue to ease, we expect to see further price relief for consumers at the retail level.

Jobless claims jump: Weekly jobless claims were unchanged from last week's upwardly revised 262,000 new claims, the highest level since October 2021. While weekly filings can be volatile, the four-week rolling average of new jobless claims rose to 246,750, an increase of 9,250 from the previous week and the highest reading since November 2021. We pay particular attention to the four-week rolling average because it smooths out some of the volatility seen in the weekly claims. Continuing claims (those people remaining on unemployment benefits) remain elevated at 1.775 million.

Wage expectations muted: The latest consumer sentiment survey released by the University of Michigan shows consumers on average expect their wages to grow just 1.7 percent in the coming year. For context, the reading reached 6.5 percent in 1980, when inflation was embedded in the economy.

Inflation expectations also remained anchored, with respondents expecting prices to rise 3.3 percent in the coming year. That figure is down from 4.2 percent in May and the lowest level since April 2021. Long-term inflation expectations remained stable at 3 percent, inside the range of 2.9 to 3.1 percent recorded during the past 23 months.
Overall, the consumer sentiment index improved to 63.9, up from last month's reading of 59.2. While the jump is encouraging, the level is still consistent with levels registered during previous recessions.

Small businesses remain relatively cautious: The latest data from the National Federation of Independent Business shows optimism among small business owners inched higher to 89.4, up 0.4 points from April. However, the reading remains well off from its 49-year average of 98. According to commentary detailing the results of the survey, "Overall, small business owners are clearly in a recession mood, expressing great concern for future business conditions. But until customers stop coming in, owners (especially in services) will continue to try to hire workers, increasing compensation to attract applicants and retain their current workforce."

Retail sales tread water: The latest retail sales numbers out from the U.S. Census Bureau came in above Wall Street expectations. The report shows overall retail sales in May were up 0.3 percent month over month, compared to Wall Street expectations of a decline of 0.2 percent. It is important to note that the retail numbers are not adjusted for inflation. When accounting for price increases during the month, sales were essentially flat. Sales were up 1.6 percent on a year-over-year basis, modestly above the 1.2 percent year-over-year increase recorded in April, which marked the smallest 12-month rise since May 2020. Motor vehicle and auto parts sales were a driving force for both the monthly and year-over-year increases.

The week ahead

Monday: A week heavy on housing reports kicks off mid-morning with the Home Builders Index from the National Association of Home Builders.

Tuesday: We will get May housing starts and building permits from the U.S. Census Bureau. This data, along with the Homebuilders Index released on Monday, will provide insights on whether consumers can expect greater housing inventory in the months ahead.

Wednesday: Fed Chair Jerome Powell heads to Capitol Hill to present his semi-annual monetary policy report. We will be listening to his comments for indications of how he views the balance of risks between controlling inflation and economic damage and a rise in unemployment that may result from additional rate hikes.

Thursday: Initial and continuing jobless claims will be announced before the market opens. Initial filings were up last week, and we will be watching to see if recent signs of some softening in the job market have taken root.

We'll get a look at existing home sales mid-morning by the National Association of Realtors. This report, along with the new homes data released earlier in the week, should provide a clearer picture of whether the real estate market continues to stabilize.

The Conference Board's latest Leading Economic Index survey for May will be released shortly after the market opens. For the past several months, the report has suggested the economy is on the cusp of or in a recession. We will be scrutinizing the data for any indications of a change in the pace of softening.

Friday: We'll get an update on the health of manufacturing and services in the U.S. when S&P Global releases its Flash Purchasing Manufacturers Index reports for June. Activity for manufacturing continues to show weakness, and growth on the services side has shown some signs of slowing. We will be watching for signs that growth on the services side continues to cool

JON BYMAN | JUN 22, 2023

Life Insurance in Retirement

Once the kids move out and the house is paid off, it may seem like you don't really have a need for life insurance anymore - after all, some of the main things you would want a death benefit for are now behind you (phew!). But as you approach retirement, life insurance - specifically permanent life insurance - can still fulfill many different roles in your financial plan.

How to use permanent life insurance in your retirement planning

With its guaranteed death benefit that won't expire and tax-advantaged cash value that you can access at any time for any reason, permanent life insurance can help you with a number of major financial goals in retirement. Here's how to use permanent life insurance in retirement.

Using life insurance to weather down markets in retirement

Market-based investments are an important part of a retirement plan because they help you grow your wealth and can protect you from inflation over time. If prices rise, typically your investments will also increase in value. But market declines are also a reality of investing. If you're forced to sell investments to continue to create income when the market falls, you may end up taking a larger chunk out of your retirement nest egg than you want.

That's where permanent life insurance can play a major role in your retirement planning. With whole life insurance (one of the types of permanent life insurance), your cash value is guaranteed never to go down. Since it's not tied to the market, it can allow you to hang onto those market-based investments when the markets fall. Instead, you could either take cash value out of your policy (which will permanently reduce the death benefit) or simply borrow against it (which will temporarily reduce the death benefit until you pay back the loan once your investments regain value).

Using life insurance for tax efficiency in Retirement

Because of our progressive tax system, the more you earn in a given year, the larger the percentage of your additional earnings you will have to send to the IRS. This remains the case during retirement because when you withdraw from your traditional 401(k) or IRA, you'll owe income tax on those funds.

Let's say you have higher-than-expected costs in a given year in retirement—like an added expense you didn't anticipate—and you have to withdraw more from your retirement accounts to cover them. The larger withdrawals may put you into a higher tax bracket, and when that happens, you'll have to withdraw more money to also cover the increased tax liability.

For that reason, it's helpful to have a mix of taxable and non-taxable sources that you can pull from in retirement. With permanent life insurance, you can withdraw the basis that you pay into the policy tax-free. After that, you can borrow against your cash value without owing any tax as long as the policy stays in place. That means in any given year, if you need to withdraw more than you expected, you can use your life insurance cash value (instead of selling market-based investments) to avoid crossing into a higher tax bracket.

Life insurance can help you create guaranteed income in retirement

If you want guaranteed income in retirement and don't have a need for your life insurance anymore, you can do something known as a 1035 exchange for an annuity. A 1035 exchange allows you to trade one insurance policy for another without owing tax at the time you make the exchange.
Say you have $200,000 in cash value. You could exchange some or all of that value for an annuity that will send you regular payments for as long as you live.

Life insurance can help ease concerns over spending down your other assets in retirement

Perhaps you want to leave something behind for your family. Or maybe you're in a position where you need to fund care as your spouse's health deteriorates. When you're concerned about spending down your assets, you can find yourself making difficult choices.

Permanent life insurance can free you to spend down your assets on what's most important to you while you're alive—the death benefit can replenish assets for your spouse to generate income, fund your legacy or both. It's a flexible asset to use as you need to.

Can I use term life insurance to plan for retirement?

Term life insurance differs from permanent life insurance in that it only provides a death benefit if you die within a specified timeframe (say, 10 or 20 years, or until you reach a certain age), and it does not have a cash value component. So while the death benefit could help you leave something behind for your family, its lack of cash value doesn't provide any living benefits for you in retirement.

Building a retirement plan that works for you

Building a diversified retirement plan will give you flexibility down the road to continue working toward your goals in retirement while adapting to whatever life throws at you. Permanent life insurance can be a flexible addition to your retirement plan, thanks to the potential its cash value offers. If you're unsure how permanent life insurance might fit into your retirement plan, you can always connect with a financial advisor to learn more and talk through options.

Utilizing the accumulated value through policy loans, surrenders, or cash withdrawals will reduce the death benefit; and may necessitate greater outlay than anticipated and/or result in an unexpected taxable event.
CAUTION: Loans taken against a life insurance policy can have adverse effects if not managed properly. Policy loans and automatic premium loans, including any accrued interest, must be repaid in cash or from policy values upon surrender, lapse or the death of the insured. Repayment of loans from accumulated values upon surrender or lapse can trigger a potentially significant tax liability and there may be little or no cash value remaining in the policy to pay the tax. The policy will lapse if loans become equal to the cash value while the policy is in force and additional cash payments are not made.
This publication is not intended as legal or tax advice. Financial Representatives do not render tax advice. Consult with a tax professional for tax advice that is specific to your situation.

Check Us Out

Welcome Kaia Louise Story

Born May 23rd
6lbs 15oz

ARTICLE 1 | PAGE 1
DECLINING INFLATION AND A PAUSE BY THE FED SENDS MARKETS HIGHER | NORTHWESTERN MUTUAL
ARTICLE 2 | PAGE 5
LIFE INSURANCE IN YOUR RETIREMENT PLANNING | NORTHWESTERN MUTUAL

"Our mission is to help businesses and individuals create financial security for generations to come. We thrive on building meaningful relationships that last a lifetime."