TILIA NEWS

INVESTMENT MANAGEMENT | FIDUCIARY ADVICE | RETIREMENT PLANNING

Series "I" Savings Bonds

The current investment backdrop is tricky for bond investors. Yields are low on prospective fixed-interest investments while inflation is running high.

One tool that can help investors protect themselves against the negative forces of inflation on idle cash is Series I Savings Bonds. I Bonds pay interest equal to the rate of increase in the consumer price index (CPI) and are backed by the "full faith and credit" of the federal government. The current annualized Series I Bond interest rate is 7.12%, though the bonds adjust to the current CPI level every 6 months.

What's the catch? You can't cash them in within the first year, and if you cash them in before the 5 year mark, you forfeit the last quarter's interest payment. You are also limited to directly buying a maximum of $10,000 per person, per calendar year.

Rising Interest Rates & Stock Performance

January started in violent fashion for the stocks of high-growth, high-valuation companies. After notable weakness in Q4 2021, the growth-stock-heavy Nasdaq 100 index posted its worst start to the year since January of 2008. The S&P 500 index fared slightly better, but still posted its worst month since the spring of 2020.

Inflation, and more specifically, the Federal Reserve's anticipated response to inflation, are the primary worries on investors' minds at the moment. The Federal Reserve's weapon in the fight against inflation is a tightening of monetary policy. This occurs in two ways: 1) Gradually increasing the Federal Funds Rate & 2) Shrinking the Federal Reserve's balance sheet by selling U.S. Treasury bonds & mortgage-backed securities owned by the Fed. Both of these tools are designed to cool economic demand by raising the costs of borrowing money. At the same time, you have manufacturers rushing to increase supply in everything from windows, to lumber, to oil & gas, etc. These two forces of raising supply & softening demand are bound to intersect and have a steadying impact on the price of goods.

How will this monetary tightening impact the price of stocks? Taking a look at the last two tightening cycles ('04-'06) and ('15-'18), the market continued to perform well during the span of the Fed's action. In the '04 - '06 cycle, the S&P 500 continued to climb at an annual growth rate of +7.43% a year. During the '15 - '18 cycle, the S&P 500 compounded at +8.56% a year. Underneath the surface, there was quite a bit more dispersion. In the '04 - '06 cycle, value stocks handily outperformed growth stocks (+12.87% compound annual growth vs. growth's +3.80%). During the '15 - '18 cycle, growth

For clients with large tax refunds, an additional $5,000 in Series I Bonds can be purchased using their refund proceeds. Series I Bonds are available for purchase directly from the U.S. Treasury at TreasuryDirect.gov. While we can't buy them on your behalf, we're happy to coach you through the process.

Don't want to do it yourself? Talk to us about investing in U.S. Treasury Inflation Protected Securities (TIPS). TIPS offer similar inflation protection and are more liquid. The trade-off for that daily liquidity of market-traded TIPS is price volatility.

TIPS have been a part of our bond strategy for many years, so if you owns bonds with us, you likely already have exposure to them.

stocks outpaced value stocks (+10.13% compound annual growth vs. value's +6.42%). With the recent outperformance of value stocks, the market seems to bet that this cycle will more closely resemble the '04 - '06 cycle, where the Fed aggressively raised interest rates from 1.00% to 5.25% over 2 years.

This time around, Chairman Jerome Powell has stressed that the Federal Open Market Committee will keep their options open during this period of monetary tightening. That's a good position to take, as the market has already done some of the work for the committee, with demand for bonds falling and rates for 10 year U.S. Treasury bonds rising from 1.25% to over 2.00% over the last 6 months. Year-over-year inflation comparables may become more favorable in June, as we lap the high inflation period of last Spring. Easier comparables, coupled with higher rates, could give the Fed cover to take a more measured approach to rate increases than the market is currently anticipating.

Uncertainty abounds, which is an apt description for most investment periods. Inflation worries, an ongoing Russia/Ukraine conflict, and upcoming mid-term elections will continue to make headlines in the coming months. More than ever, we believe that patient investors with prudent investment plans will be rewarded, while markets will frustrate the short-term oriented investor.

Sources: bls.gov, "The Treasury Has a Bond Bargain for You" wsj.com, federalreserve.gov/monetarypolicy/openmarket, treasurydirect.gov, koyfin.com