GREENLEAF TRUST

Perspectives

A Greenleaf Trust Newsletter

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William D. Johnston
Chairman, Greenleaf Trust

Economic Commentary

The New York Fed revised their May 19 Weekly Economic Indicator reading upward to 4.29%; however, their May 26 initial reading declined to 3.52%, reflecting the trend in place. Simultaneously, the Conference Board, as well as University of Michigan consumer surveys, also mirrored a small, but consistent, decline in consumer sentiment and confidence in short term economic prospects. The Conference Board Consumer Sentiment Index declined to 106.4, down from April's reading of 108.6. It is not the degree of change that matters, but rather the confirmation of the trend in place. However, the current reading was significantly better than the composite of analysts' expectations of a 103.6% projection.

Food and energy prices weighed heavily on consumers' minds as savings declined and credit card debt expanded during the period. Specifically, consumers put on hold decisions to purchase autos, homes and appliances. We will look to durable goods sales data later this month to confirm those survey responses by consumers. The University of Michigan Consumer Sentiment Index declined across all three categories of sentiment, current conditions and the forward six-month expectation results. Again, the declines were relatively small, but consistent with the now four-month trend in place. Composite Leading Indicators (CLI), Business Confidence Index (BCI), as well as the composite Consumer Confidence Index (CCI) all validate the declining trend in place in overall consumer confidence. We will look for the latest jobs report Friday, June 3 to see if consumers are more concerned about employment than prices. Anecdotal responses within the surveys suggest pricing is weighing heavier than employment, which certainly makes sense. Analysts focusing on payroll surveys are forecasting an additional 352,000 jobs added to the payroll in May, bringing us to an unemployment rate of 3.52%.

It is estimated by several banking associations that about 40% of Americans have a savings account, and that a majority of Americans would not have enough savings to cover an emergency requiring one thousand dollars. Should those statements be accurate, it is easy to see why the current 31% increase year-over-year in at-the-pump fuel prices would cause behavioral changes in many consumers. Transportation of goods

Economic Commentary, continued

and services resulting in fuel surcharges only amplifies the erosion of the purchasing power of people trying to work and feed families.

Economists have long argued the theory that replacement choice decisions tend to mute the impact on inflationary pressures. Their assumption is that vendors and retailers are not simply free to pass on wholesale price increases, as customers will substitute behaviors and purchasing choices to combat the increasing cost of goods. The replacement choice theory makes sense when there are options available, but seem unlikely when price increases are broad and include all components necessary for shelter, food and transportation. We have spent a good deal of time in this column on the inflationary pressures of supply chain interruption, which created too much money chasing too few goods, and now we have amplified that condition by making the transportation of those goods more costly.

Conservative economists would argue that our eleven-year recovery from the financial crisis in 2008 through 2019 and the global COVID-19 pandemic in 2020-2021 is responsible for our current inflationary cycle. They maintain that there was too much central bank intervention in injecting liquidity into the banking system, and that we artificially lowered the cost of debt, causing inflated real estate and investment values. Further, they suggest that if we allowed market forces to work as they should, banks that deserved to fail during the financial crisis would have done so and, in the long run, stability would have returned to markets based upon market force fundamentals. Of course, they don't spend much time explaining away the personal human tragedies that would have taken place with this scorched earth approach to a global financial crisis. Similarly, they spend minimal time suggesting the alternative to keeping people employed during a global pandemic. It is true that all of the stimulus packages passed by Congress allowed most consumers to remain, by and large, financially healthy during the pandemic, and that consumer demand remained uniquely strong during the depths of the disease spread. Did that increase the demand for goods beyond what could be produced for a period of time? There is little argument that it did. It also reduced a staggering unemployment rate of 14% within a relatively short period of time. Prices of consumer goods, prior to the pandemic and Russia's invasion of Ukraine, suggest that an appropriate equilibrium between consumer demand and production supply existed. Unemployment was at historically low levels while wages were increasing moderately and were particularly benefiting the lowest quintile of earners.

> "The cure to supply chain inflationary pressures must be the return to normalization between demand and production…"

The pandemic immediately changed the equilibrium between supply and demand, much as it did in the financial crisis of 2008. The pandemic, as well as the financial crisis, was global and not country specific. Our supply chain, as we have written previously, is global and not specific to one country. The cure to supply chain inflationary pressures must be the return to normalization between demand and production, and can best be accomplished in a few years, not months or certainly weeks. The price of fuel at the pump, prior to the Russian invasion of Ukraine, was equivalent to $0.65 per gallon in 1978, on an inflation-adjusted basis. The current thirty percent increase in the at-the-pump fuel prices has everything to do with global distribution interruption and, again, will not be cured in weeks or days, but rather by the duration of time that the supply is interrupted during this international conflict.

Some might argue that we can lower our fuel prices in the United States by becoming more energy independent. Doing so would be to restrict United States producers and refiners of energy products from distribution, exploration and refining in the global marketplace, as they are part of global corporations that create, refine and supply energy to the entire bandwidth of global need. To assume that American domiciled energy producers only explore, produce, refine and distribute within our country's sovereign boundaries is to ignore the reality of the global energy sector. Time will be our friend in the restoration of the global supply chain as well as the restoration of the global energy supply. In the conversation about energy prices, we must come to recognize that on a longer term inflation-adjusted calculation, our energy prices are very low and, in fact, much lower than almost every other country.

COVID remains with us and seems to be morphing into what many pandemic researchers had forecasted more than eighteen months ago. Infections will continue and new strains will be diagnosed. Those who have been vaccinated and boosted will not be immune, but will face significantly better outcomes when and if infected. Global inoculations continue to increase and suffering, hospitalizations and deaths continue to decline. Research will discover new variants and research will modify vaccinations and boosters. I am prone to repeat that, as Americans, we do not need to be hungry to eat or thirsty to drink. We want to know who is to blame and what the solution is. We don't want it messy, though we make a lot of messes. We want COVID over. Turns out it isn't over now and won't be for a very long time, and chances are it will be replaced by something we don't presently know of. It will be like many other maladies that we, as humans, each have the opportunity to fall victim to. We can prepare, prevent, take appropriate remedies and precautions, and live with it and through it or not. The evidence continues to suggest that those that do are faring better than those that don't.

"In the conversation about energy prices, we must come to recognize that, on a longer term inflation-adjusted calculation, our energy prices are... in fact, much lower than almost every other country."

Michael F. Odar, CFA®
President and
Chief Executive Officer

Next Level Leadership

The development of our talent is critical to our growth. As we continue to find and hire new teammates we need to make sure they are properly supported. We do this by making sure every teammate in our organization has a coach. The coach's primary responsibility is to support and develop those they lead along a growth path that is aligned with their aspirations and talents. They meet formally one-on-one four times throughout the year to discuss the teammate's goals, needs, performance, and any pathing plans. Since the relationships are very personal, we try and keep coaching responsibilities to a manageable number, usually seven or fewer. With an average of over 20 new teammates per year, we need to make sure the next level of leadership is being developed as well.

In conjunction with our overall succession planning efforts, that is exactly what we are doing. Through thoughtful conversations during their coaching sessions we can mutually identify those teammates who, as part of their growth at Greenleaf Trust, would like to include leading people. It is important that they have both the desire and talent to lead. To enable this continued growth, we created a Next Level Leadership program several years ago. Karen Baldwin, Director of Human Resources at Greenleaf Trust, and I lead monthly meetings with these future leaders. By bringing this group together we can create a cohort of leaders learning together to obtain a foundation to build on as well as management tools and a new peer group to draw strength from. Our meetings also involve interactive discussions with other organizational leaders to learn from their experiences. And, we help them understand that managing people is not necessarily always a promotion. It's a career path.

"To enable… continued growth, we created a Next Level Leadership program several years ago."

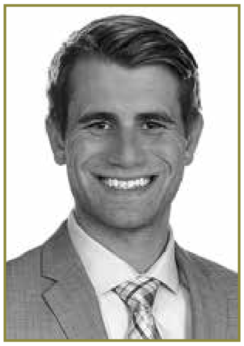
We started our meetings this year by reading the book *Switch: How to Change Things When Change is Hard* by Dan and Chip Heath. The authors bring decades of counterintuitive research in psychology and sociology to shed new light on how people can affect transformative change. Their thesis is that our minds are ruled by two different systems - the rational mind and the emotional mind – that compete for control. The rational mind wants to change something at work; the emotional mind loves the comfort of the existing routine. Relieving the tension between the two can make change easier. In a book club format, we take the lessons from the book and relate them back to their experiences at Greenleaf Trust and their new roles leading people.

Karen and her team have also begun meeting regularly with our Emerging Leaders. These are our new mentors that are just beginning their leadership journey at Greenleaf Trust. Similarly, their discussions focus on talent, coaching, management tools, interviewing and selection, critical conversations, and policies and procedures. Mentors at Greenleaf Trust provide informal advice and help to our newer teammates and interns. They have expressed an initial desire to grow in this manner and being a mentor provides them with a glimpse on how it feels to actually lead people.

We are excited about our future leaders and work hard to make sure they are supported and equipped with the tools they need to be successful. Our investments here ensure that our entire team is supported with a meaningful and caring coaching relationship focused on them.

Liquid Alternatives

A CASE STUDY ON PORTFOLIO DIVERSIFICATION



Jacob A. Barker, CFA®, CFP®
Senior Manager Selection Analyst

Many of you are familiar with the phrase popularized by Nobel Prize winning economist Milton Friedman, "there's no such thing as a free lunch." This rudimentary economic principal tends to hold true within the realm of economic theory; however, this idea was put to task by Harry Markowitz in 1952 when he published his research paper on what is known as Modern Portfolio Theory. This eventually secured his spot alongside Dr. Friedman as a Nobel Prize winning economist. What Dr. Markowitz's empirical research demonstrated is that within the context of investment portfolio management there exists an exception to the no free lunch principle. As he put it, "diversification is the only free lunch," where allocating to a variety of assets with differing return profiles can result in a significant increase in a portfolio's expected risk-adjusted return.

Today, the idea that portfolio diversification is beneficial to long-term investment performance is taken for granted. What is still debated, however, is which assets or strategies provide the best diversification benefits and how to best obtain access to these sources of diversification. We hope that this article will provide readers with a better understanding of how Greenleaf Trust employs a variety of exposures within a portfolio to best capture the benefits of portfolio diversification.

"… we also believe that portfolio risk-adjusted returns can often be enhanced by allocating a portion of a portfolio to non-traditional investments."

WHAT ARE ALTERNATIVES?

Investment management practitioners and finance academics alike have long advocated for the use of stocks, bonds, and cash as the fundamental building blocks for private client investment portfolios. While we use these traditional asset classes as the primary allocations for client portfolios, we also believe that portfolio risk-adjusted returns can often be enhanced by allocating a portion of a portfolio to non-traditional investments.

Liquid Alternatives, continued

Non-traditional investments, otherwise known as alternative investments, are generally defined as being any investment that is not accessible via the public markets or that uses complex investment and trading strategies. Common examples include Private Equity, Hedge Funds, Private Real Estate, and Private Credit.

Amongst these strategies, there are a wide variety of substrategies with widely varying return targets and risk exposures. They range from strategies targeting returns in excess of equities to strategies targeting lower returns, but greater diversification benefits. Additionally, many alternative investment strategies are offered in private investment vehicles that have limited liquidity and transparency as well as greater tax complexity and higher investment management fees relative to mutual funds. However, there exists a subcategory of funds, commonly known as liquid alternatives, that provides investors access to alternative investments in more liquid formats, including mutual fund and ETF structures. As you might imagine, some private investment strategies lend themselves to being offered in a liquid format more easily than others – liquid alternatives that replicate certain hedge fund strategies are most common.

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At Greenleaf Trust, we appreciate liquidity and transparency when selecting investment strategies. Through our research, we identified Managed Futures and Merger Arbitrage as two of the more compelling liquid alternative approaches given the present market environment, their expected role within client portfolios, and their availability in liquid and transparent fund structures. A brief overview of these investment approaches is provided below.

Managed Futures

Managed Futures strategies seek to generate returns that are uncorrelated to the broad stock or bond markets by implementing long or short positions in the global futures markets spanning equities, bonds, currencies, and commodities. In essence, the approach uses computer models to identify market price trends across the globe and enter into trades that will benefit from the fall or rise in asset prices, a strategy known as trend following.

The purpose of this allocation is to provide diversification with an emphasis on downside protection during equity market sell-offs. To illustrate what this looks like, consider our recent market experience: global commodity prices rapidly increased while global equity and bond prices rapidly decreased. For investors that limit portfolios to only holding publicly traded stocks and bonds, there were few places to hide. This is where Managed Futures take center stage. During the market disruption, Managed Futures funds had the ability to take long positions in energy futures while at the same time enter short positions in equity and bond futures, thus benefiting from the rise in commodity prices as well as the fall in stocks and bonds. This allocation has provided diversification and compelling returns in the first four months of 2022.

Merger Arbitrage

Merger Arbitrage is a strategy that seeks to generate a "riskless" profit by exploiting market inefficiencies that occur during mergers and acquisitions. Here is how it works: when a public company announces its intent to purchase another company, there is a price discrepancy between the current price of the stock of the company being acquired and the price offered by the acquiring company. This difference in price vanishes once the deal is closed and so there is, in theory, a riskless profit to be made by simultaneously purchasing the stock of the company being acquired and shorting the stock of the company making the acquisition.

The purpose of this allocation is to reduce portfolio volatility and generate consistent returns in excess of those provided by core fixed income. While this strategy is certainly not riskless in practice – failed deals and imperfect hedging are common – it historically has generated low-to-mid single-digit returns with relatively low volatility and little correlation to equity and bond markets.

INCORPORATING ALTERNATIVE ASSETS INTO A PORTFOLIO

In the preceding sections, we identified an opportunity to increase portfolio risk-adjusted returns through diversification into liquid alternatives and recognized Managed Futures and Merger Arbitrage as two investment approaches that appear up to the task. After identifying the strategies, our next task is to determine the appropriate size of the allocation. We do this through a risk-aware process of modelling historical and expected future risk and return.

In 2021, Greenleaf Trust's year-end capital market assumptions projected core fixed income returns below 2% over the next decade, with the majority of this return coming in the second half of the period. Based on our observations and expectations, we believed there was an opportunity to improve some portfolios' risk-adjusted returns by tactically increasing the alternatives allocation, directing assets away from fixed income and into liquid alternatives.

Our objectives when increasing this allocation were to (1) improve expected risk-adjusted returns for portfolios, (2) maintain a reasonable level of overall portfolio volatility, and (3) control downside risk in stressed equity markets. Our preferred combination of alternative asset strategies facilitated these objectives because of their low correlation to traditional stock and bond markets. As illustrated in following table, the Managed Futures strategy we enlist has maintained a negative correlation to both stocks and bonds over the trailing three-year period ending April 30, 2022. Our preferred Merger Arbitrage strategy has generated positive returns, but low levels of correlation to stock and bond markets, with limited volatility.

"The purpose of [a Merger Arbitrage] allocation is to reduce portfolio volatility and generate consistent returns in excess of those provided by core fixed income."

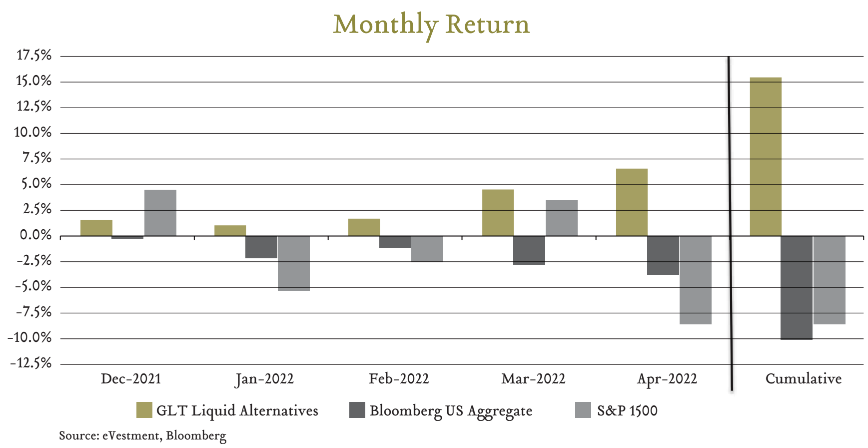
Liquid Alternatives, continued

	GLT Liquid Alternatives	Merger Arbitrage	Managed Futures	Bloomberg US Aggregate	S&P 1500
GLT Liquid Alternatives	1.00				
Merger Arbitrage	0.27	1.00			
Managed Futures	0.86	-0.23	1.00		
Bloomberg US Aggregate	-0.27	0.22	-0.35	1.00	
S&P 1500	0.08	0.43	-0.09	0.24	1.00

Source: eVestment

At this point you may be wondering how the liquid alternatives allocation has performed relative to stocks and bonds over the five-month period since the change was enacted. The below graph shows the monthly return from the liquid alternatives allocation as well as the return from the S&P 1500 index and the Bloomberg US Aggregate index. These indices are commonly used as proxies for the US equity and fixed income markets respectively. As shown, the allocation generated positive returns in each of the five months, handily outperforming both stocks and bonds. While we know there will be periods when the alternative asset allocation will underperform in the future, the recent results are encouraging and validating of our investment research process.

"While we know there will be periods when the alternative asset allocation will underperform in the future, the recent results are encouraging"



It goes without saying that helping our clients achieve their financial goals is a top priority at Greenleaf Trust. Constantly working to ensure that the best available tools and methods are being employed in client portfolios is just one of the ways in which we work to meet this overarching goal. While future portfolio repositionings may not reap the same rewards as the one we discussed here today, we believe that proper portfolio diversification, the closest thing there is to a free lunch, along with steady stewardship and a long-term investment perspective, give our clients the best probability of achieving their financial goals.

Making Gifts to Individuals

Regina Jaeger, CTFA
Vice President
Senior Trust Relationship Officer

As we work with clients to fulfill their goals and objectives, one of the most common strategies that we discuss is gifting. Making gifts to achieve goals and objectives, which are often generational in nature, requires a great amount of analysis and detailed execution to attain the desired outcome. Gifting strategies vary widely depending on the purpose (enhance lifestyle or reduce future estate tax), the type (present or future interest), the value (above or below the annual exclusion and lifetime exemption), the form (majority or minority interest), and the source (liquid or illiquid). In addition, the considerations often diverge when making gifts to individuals and making gifts to charitable organizations. This article focuses on making personal gifts to individuals.

In Michigan, three elements are necessary to constitute a valid gift: (1) the donor (person making the gift) must intend to gratuitously pass title/ownership of the property to the donee (recipient); (2) actual or constructive delivery of the property must be made; and (3) the donee must accept the gift.

The Internal Revenue Service defines a gift as "any transfer to an individual, either directly or indirectly, where full consideration (measured in money or money's worth) is not received in return." In other words, a gift is a transfer of money or assets (including intangible interests) to another person, and nothing of comparable value is given in return. A gift may be either a taxable or a non-taxable gift depending on how much is given, who it is given to, and how the gift is used.

"... a gift is a transfer of money or assets (including intangible interests) to another person, and nothing of comparable value is given in return."

In general, any gift made to an individual is a taxable gift. Meaning that the gift should be reported on IRS Form 709 to reduce your lifetime gift tax exemption or pay any gift taxes due. However, there are a few exceptions to this rule. Generally, the following gifts are not taxable or reportable gifts.

1) Gifts that are not more than the annual gift tax exclusion for the calendar year to any one individual ($16,000 for 2022)
2) Tuition or medical expenses you pay directly for someone
3) Gifts to your spouse
4) Gifts to a political organization for its use

In addition to the annual gift tax exclusion, every individual has a lifetime gift tax exemption. In 2022, that amount is $12,060,000 and is adjusted annually. Married couples enjoy an exemption of twice that amount because the lifetime exemption is available to each individual. Any gifts that exceed the lifetime exemption are taxable and reportable on IRS Form 709, Gift (and Generation-Skipping Transfer) Tax Return, unless a specific exclusion applies. Any single gift or cumulative gifts that exceed the lifetime gift tax exemption is taxed at the current Federal Gift Tax rate

Making Gifts to Individuals, continued

of 40%. It is important to note that in 2026 the lifetime gift tax exemption is scheduled to reset back to $5,000,000 (adjusted for inflation), unless Congress makes changes between now and 2026. This current period of a relatively high lifetime gift tax exemption creates a significant planning opportunity for high net worth individuals who want to reduce taxes upon their death.

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Annual exclusion gifts are the most common type of giving. As already mentioned, each person is allowed to give up to $16,000 per calendar year to as many individuals as they would like, and the gift is exempt from gift tax. A married couple can combine their annual exclusion amount and give up to $32,000 to any one person in a calendar year.

Example: In a calendar year, wife wants to give her 4 nieces and her neighbor the maximum annual exclusion ($16,000 x 5 = $80,000 total giving). Husband wants to give wife's 4 nieces and his 5 nephews the maximum annual exclusion ($16,000 x 9 = $144,000 total giving). Husband and wife have just given away $224,000 ($80,000 + $144,000) in a calendar year gift-tax free because each individual gift did not exceed the annual gift tax exclusion of $16,000.

Beyond the personal satisfaction of making these gifts, husband and wife also realize the benefit of removing $224,000 (and any future appreciation) from their taxable estate for Federal Estate Tax purposes upon death. For those individuals who have taxable estates, annual exclusion gifting is a powerful tool used to reduce future federal estate taxes.

The amount of tuition and medical expenses (as defined by the IRS) that you make directly on behalf of someone else is treated as a non-taxable gift and is unlimited. However, an important detail is that when you are paying tuition or medical expenses for another person, you need to pay those expenses directly to the educational institution or the medical provider. You cannot give your 20-year non-dependent daughter $24,000 for deposit to her checking account with the understanding that she will use the money to pay her tuition bill and have the gift qualify as an exception. In order to qualify for the unlimited non-taxable gift exemption for tuition, you must write the check directly to the educational institution. The same applies for direct payments of medical expenses.

If you do make a gift that does not qualify for one of the IRS taxable gift exceptions, the gift is reportable on IRS Form 709 tax return and any taxes due are from the person who actually made the gift, not the person who received it. The person receiving the gift does not report the gift as income or as any other taxable event in the year of receipt. Items you may need to include with your Form 709 return include a copy of a qualified appraisal, a copy of relevant documents with regard to the gift, and documentation of any unusual items shown on the return like partially-gifted assets such as

50% interest in real estate. Gifts reportable on Form 709 are required to be reported at fair market value, meaning the price at which the property or asset would change hands between a willing buyer and a willing seller (i.e., an appraisal for real estate or a business interest).

We often advise clients on how to most efficiently carry out the transfer of a business interest to their heirs with the goal of effective succession planning and/or reducing gift and estate taxes upon death. The rules available for valuation discounts can be immensely beneficial when gifting these types of assets. In its simplest form, when reporting the market value of a gift of a business interest on Form 709, the value of the gift can sometimes be discounted for items like lack of marketability, lack of control, minority share and future interest discounts. These discounts can range from 10% to 45%, meaning you are able to give away an asset that has a market value of $1,000,000 that potentially could be discounted for a taxable gift value of $550,000, resulting in using less of your available lifetime gift tax exemption than you would if the gift had to be reported at full market value. While a tax savings on 45% of the value of an asset seems like an easy outcome to shoot for, enormous care should be taken when contemplating using valuation discounts, as all valuation discounts must be substantiated by a qualified appraiser. If the IRS disallows the discount, significant underpayment of taxes and penalties could be due. It is also noteworthy to observe that there is currently serious discussion in Congress surrounding proposed legislation that would disallow all valuation discounts.

There are also a handful of irrevocable trusts that can take advantage of the current rules and regulations relating to gifts to individuals that can help reduce taxes upon death. We have discussed many of these in detail in previous *Perspectives* articles, and each of them warrants its own time and attention because of the complexity of the strategies. For the purpose of this article let it be sufficient to name a few of those irrevocable trusts and allow you to reference our website (www.greenleaftrust.com) for details from previous articles: Spousal Lifetime Access Trust (SLAT), Qualified Personal Residence Trust (QPRT), and Grantor Retained Annuity Trust (GRAT).

Although making gifts to individuals is a common occurrence by the clients we advise, it is an action that requires much thought and understanding of the rules associated with those gifts to assure your goals are met and all available strategies are considered. You will want to review your giving goals annually to ensure that laws have not changed and that the reason for the gifts are still relevant in the context of your estate plan. Take the time to talk with your Greenleaf Trust team before you make a gift (to an individual or charity) to ensure your gift is well thought out and properly implemented.

"… making gifts to individuals… is an action that requires much thought and understanding of the rules"

Jeff T. Pauza, CFA®, CFP®
Senior Wealth Management Advisor

Spring Harvesting

The year 2022 has been challenging across financial markets, to say the least. While it is best to stay disciplined during times of uncertainty to achieve long-term goals, that does not mean we avoid making changes. Tax-loss harvesting is a strategy that we consistently use for clients regardless of economic conditions. Given the challenging market environment today, where stocks and bonds have sold off simultaneously, we believe the time is ripe to harvest.

Tax-loss harvesting allows you to sell investments that are below their cost basis, immediately replace them with reasonably similar investments, and then offset realized capital gains with capital losses. The end result is that less of your money goes to taxes and more will stay in your pocket. If there was a year where you did not have any realized capital gains, losses can then be used to offset $3,000 of ordinary income for a joint tax return. Unused capital losses can also be carried forward indefinitely, allowing investors to build a reserve of losses today to be used against any future gains. The end result does not show up on an investment performance report but on your tax return through lower income taxes.

"Tax loss harvesting allows you to sell investments that are below your cost basis, immediately replace them with reasonably similar investments, and then offset realized capital gains with capital losses."

With market volatility that feels like a roller coaster, it doesn't mean that the only thing you can do is close your eyes and hang on until the ride is over. Volatility can actually provide additional opportunities for agile trading strategies that can use market movements to their advantage.

We offer a personalized strategy to clients that want to take advantage of capturing stock market index returns while also accumulating capital losses to be used to offset future capital gains. The strategy, known as direct indexing with a tax alpha overlay, works by first purchasing a large subset of the individual securities that make up a particular index that we want to match. For example, instead of purchasing a mutual fund or exchange-traded fund to invest in the S&P 1500, clients of this particular strategy directly own many of the individual stocks that make up the index. Since our clients own the individual securities, it allows us to actively trade on a position level rather than buying or selling entire funds. If our strategy held a position in Coca-Cola shares and they were trading at a loss in any particular month, we could sell the shares and immediately purchase a similar stock like Pepsi. This would allow our client to remain fully invested and ride the following recovery, while also accumulating a capital loss to be used to offset future capital gains. We do this across a large portion of the individual stocks that make up an index and the strategy is perpetually searching for trading opportunities. This approach creates "tax alpha" or an extra rate of return that is earned beyond the index. Historical results have demonstrated that this strategy can add 1-2% of tax alpha outperformance beyond the rate of return for the index.

We have included a hypothetical example of how the tax loss harvesting process generates capital losses while continuing to keep a portfolio invested. Remaining invested is essential because a pillar of our investment philosophy is that maintaining discipline throughout all market cycles will lead to improved investment outcomes. The tax benefit generated by this strategy provides a reward for your discipline.

Tax-loss harvesting opportunities are substantially greater when the underlying investments in a portfolio have higher volatility. Market corrections in December 2018 and March 2020 are terrific examples of the added benefit that our tax alpha strategy has created for clients. During each of these corrections, markets suffered quick drops and followed with a rapid recovery. Investors that were not utilizing a nimble, active, tax-loss harvesting approach likely missed out on capturing losses with the pace of the recovery.

We believe this strategy can be effective and is well suited for clients of all different backgrounds. If you own a business and are contemplating a sale in the future, this can be an ideal strategy to build losses today in order to avoid future taxes on the sale. Our clients that own real estate and are therefore subject to capital gains on the future sale of property have benefitted tremendously from accumulating losses today. The tax alpha strategy has demonstrated that we can produce capital losses equal to about 33% of the initial portfolio value within the first five years, while still capturing the full return of the index.

To determine if this strategy makes sense in your particular circumstance, please reach out to a member of your client centric team.

"We believe this strategy can be effective and is well suited for clients of all different backgrounds."

Rosalice C. Hall, CRPS®
Senior Relationship Specialist

Reprioritizing Retirement Plan Design

Over the past few years, our world and many workplaces have shifted dramatically as we endured a global pandemic. While employers focused on workforce reductions and remote work, setting priorities for their 401(k)/403(b) plans was often low on the priority list. However, as life begins to normalize, we are beginning to see a renewed interest in retirement plan design.

Employers are realizing they are more likely to retain employees who feel valued and adequately compensated for the work they are doing. Understanding what is important to your employees goes a long way in structuring a compensation package they will appreciate. "Reinventing Retirement. Defined Contribution Plans 2021," by the international consulting firm Mercer, revealed the "critical importance of focusing on employees and what they need, want, and expect." Mercer suggests starting by reviewing participant demographics and key behaviors across the benefit programs, with an eye toward the financial pressures experienced during the pandemic. Using the information gathered, it may be easier to understand subsets of employees and what they value and need from their employer.

"Employers are realizing they are more likely to retain employees who feel valued and adequately compensated…"

SEVERAL KEY AREAS OF PLAN DESIGN REVIEW

Eligibility: Employee attraction and retention is vital during this strong labor market with low unemployment and vast job openings. New employees are often dismayed to learn they must wait up to a year before beginning employee deferrals into their new employer's retirement plan. Reducing the waiting period for entering the plan can be a quick, easy win. However, determining the eligibility period can be a balancing act, especially for companies with high turnover. In situations of high turnover, requiring at least 90 days of employment can help to weed out short-term employees, without triggering the administrative work necessary to allow their participation in the plan.

Payment of 401(k) expenses: The decision to pay for retirement plan expenses from company assets or plan assets is a topic that many plan sponsors debate. From a fiduciary standpoint, there is no risk of excessive fees being charged to participant accounts if the company is covering the bill. Besides the fiduciary liability benefit, paying the fees from company assets can be advantageous because they are tax-deductible and may result in tax savings. Additionally, it can improve transparency to participants, which may contribute positively to employee relations.

Roth 401(k)s: As of April 2022, approximately 75% of 401(k) retirement plans offer a Roth deferral option. This number has increased drastically over the last five years. Younger savers are starting to take advantage of the Roth 401(k) tax benefits, which includes the money growing tax-free and tax-free withdrawals at retirement. The Roth deferral option does not meaningfully impact plan sponsors, as any employer match is applicable to both pre-tax and Roth deferrals. Yet, Roth 401(k)s provide participants the benefit of future tax-free withdrawals.

Distribution Options: Plan sponsors can provide a buoy to participants by ensuring the plan allows for hardship distributions and/or loans, so that if a disaster strikes, the participant will be able to access the balance of their retirement plan account. For participants closer to retirement age, there is a desire for the plan to allow regular monthly distributions, similar to a pension plan. Additionally, it has become painfully obvious during the pandemic that having an emergency savings is a luxury for many. As a result, retirement plans with flexible distribution options are appreciated by participants.

Employer Contributions: The decision to offer a match and/or profit share can be a difficult subject for many business owners. Employees often desire cash compensation in place of other job-related perks. However, many business owners take a paternalistic approach when making decisions on behalf of their employees and their future retirement potential. Providing a match option requires that participants have some 'skin in the game' in order to receive the additional employer dollars. While others feel that a match lacks compassion for those without the discretionary income to contribute to the plan.

Automatic Enrollment: When considering ways to boost participation, auto enrollment and auto escalation are quickly becoming best practice. Research in behavioral economics shows that when it comes to complex choices such as whether to save and when to retire, people's decisions are often influenced by social norms and the presentation of their options. In terms of retirement plans, auto enrollment and auto escalation are widely accepted by employees and they tend not to opt-out, if the deferral rate stays below 10%.

Retirement plans are designed to be a long-term savings vehicle; they should be structured to positively impact participants and improve their retirement readiness. Ensuring the plan design is up-to-date with today's standards can go a long way in attracting, retaining, and engaging employees. The Retirement Plan Division of Greenleaf Trust appreciates the work all of our plan sponsors do every day to benefit their employees and our retirement plan participants. As always, our team is ready and willing to assist with your retirement plan needs.

"Ensuring the plan design is up-to-date with today's standards can go a long way in attracting, retaining, and engaging employees."

Stock Market Pulse

Index	5/31/2022	Total Return Since 12/31/2021
S&P 1500	943.39	-12.63%
Dow Jones Industrials	32,990.12	-8.43%
NASDAQ	12,081.39	-22.52%
S&P 500	4,132.15	-12.76%
S&P 400	2,514.80	-11.01%
S&P 600	1,235.61	-11.39%
NYSE Composite	15,827.05	-6.84%
Dow Jones Utilities	1,023.05	5.79%
Barclays Aggregate Bond	2,145.05	-8.92%

P/E Multiples	5/31/2022
S&P 1500	20.1x
Dow Jones Industrials	17.8x
NASDAQ	39.6x
S&P 500	20.6x
S&P 400	15.6x
S&P 600	15.4x

Key Rates

Fed Funds Rate	0.75% to 1.00%
T Bill 90 Days	1.06%
T Bond 30 Yr	3.05%
Prime Rate	4.00%

Current Valuations

Index	Aggregate	P/E	Div. Yield
S&P 1500	943.39	20.1x	1.54%
S&P 500	4,132.15	20.6x	1.53%
Dow Jones Industrials	32,990.12	17.8x	1.99%
Dow Jones Utilities	1,023.05	19.3x	3.16%

Spread Between 30 Year Government Yields and Market Dividend Yields: 1.51%

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