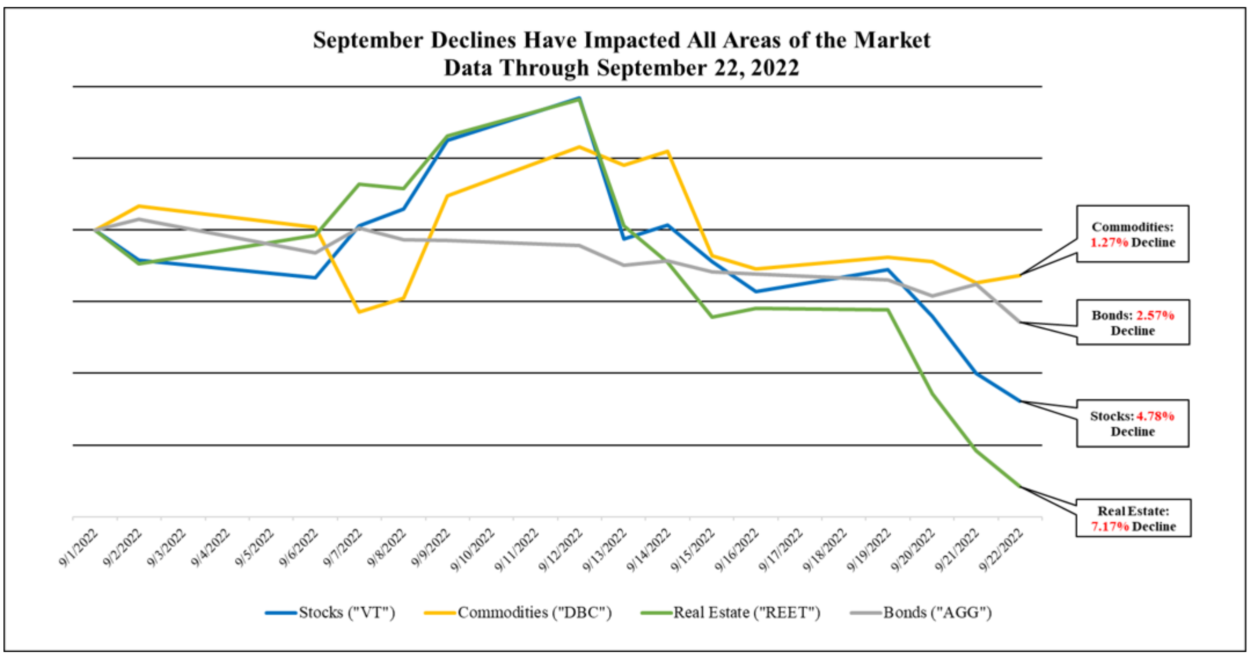
Hello:

Our plan was to do a more thorough market update shortly after 9/30/2022. However, given the unusually poor performance in stocks, commodities, bonds, and real estate this month (see chart below), and more broadly this year, we didn't want to wait to share some of our thoughts with you. If you would like to go over your portfolio, don't hesitate to schedule time on our calendars using the links below. If the link doesn't work due to certain security tools in your email, you should be able to copy/paste the text of the links below into your web browser to reach our scheduler tools. If you prefer to call in to make an appointment, please phone Jacquie Rowe @ 208-957-6922 extension 4.

Trevor - https://calendly.com/trevorscottocpa
Richard - https://calendly.com/richarddaveycpacfp
Tom - https://calendly.com/tvogelheim



Things could get worse in stocks but we should be humble in our attempts to predict FUTURE short-term price movements and FED policy. The market reaction to the rapid rise in interest rates is not a surprise. As rates rise, the math around stock valuations based on discounted future cash flows becomes more challenging. With higher rates, we transition from a world where stocks and real estate investments are the only game town, to one where income-oriented investments like bonds become attractive alternatives, particularly on a risk-adjusted basis. But since the market is forward-looking, it had already priced in the 75 basis point increase in rates that was announced last Wednesday before the announcement was actually made. It was the aggressive posture of the FED in the post-announcement comments that led to further declines in the market. The FED was rather direct that they will continue down this path of tight monetary policy until inflation is tamed.

Common Question: So, can't we just assume that things will get worse due to FED tightening and incorporate that assumption fully into our asset allocation decisions? *Our answer here is very clear… "no", at least not in any* *absolute fashion.* In recent years, the FED has a track record of reversing course with monetary policy when "real" market pain sets in. Just look at Q4'2018 to Q1'2019. The S&P 500 hit a 20% decline near Christmas Eve. The FED was bent on increasing yields and shrinking their balance sheet (aka "Quantitative tightening") to finally unwind the 2008 stimulus packages. The 10-year treasury eclipsed 3.15% and we saw what became known as "the taper tantrum". Economic weakness set in, and rather abruptly, the FED caved on their tightening path which resulted in a very quick reversal in stock prices to the upside where the S&P 500 saw a ~40% return peaking in Feb'2020. Had we taken the FED at their word in late 2018 and sold out of stocks, the results would have been devastating locking in losses and missing out on one of history's most robust 14-month bull markets.

Again, beginning in Feb'2020, stocks sold off as COVID-19 panic set in. The S&P 500 was down ~35% in ~1 month as businesses shuddered and widespread corporate defaults looked all-but certain. Without a clear appreciation of the uncertainty of near-term stock market movements and FED reactionary policy, we likely would have sold all our stocks here. There was no news but bad news. Then, the FED did something it had never done in history. It bought junk bond ETFs. Again, the market experienced an insane 18-month bull-run that almost no one predicted on the back of unprecedented FED policy. The S&P 500 returned >100% in just 20 months! Hopefully a recap of these events provides some context. <u>Hindsight is 20-20, but if we are honest with ourselves, trying to implement and execute a strategy these last few years incorporating major swings in our stock weightings in client portfolios would have been reckless. But is it just us? Can't the "big guys" time the market?</u> *The Short answer here (again) is a big fat "no" based on ALL the data about hedge fund manager and mutual fund manager performance that is available.* Per Morningstar's Mutual Fund Landscape studies, we repeatedly see that these institutions, which are staffed up with the largest and most sophisticated economic forecasting teams in the world, fail to outsmart the market also. They have armies of CFAs, CPAs, PhD economists, algorithmic trading specialists, Washington DC policy insiders, etc. and yet less than 20% of these active fund managers beat their benchmarks over 15+ year periods.

<u>**Another Common Question:** So why don't we just pick the 20% of active investment managers that DO outperform?</u> *Well, unfortunately this same Morningstar Mutual Fund study indicates that trying to select the top 20% of active mutual fund managers in any given period is equally unpredictable. Many statisticians, with an intimate understanding of the data, would suggest that being a 20% top performer in a given period is actually random.*

The investment markets are forward looking. Current prices reflect both the current state of affairs as well as future projected earnings. We cannot predict if the FED will successfully guide us to a soft landing or if they will even follow through on additional rate hikes. Further it is impossible to predict the low point of the market. Typically, this occurs not when things <u>actually</u> start to get better but more when the investment community concludes that things will start to get better in the *near* future. What we can say is that as markets drop in price (be it stocks, bonds, or real estate), the prospects for FUTURE returns in those markets generally improve. Here's some data to illustrate this point. We looked at subsequent 1-, 2-, and 3-year annualized returns in the S&P 500 in all 20% or larger selloffs since 1980. In all but one of these instances, forward 3-year annualized returns were > 5% with the average 3-year return being 14% annualized. For some context, it only takes ~5 years for money to double at a 14% rate of return!

20% Or Bigger Declines Since 1980 and Subsequent Returns				
		Annualized Rate of Return from Bottom		
Trough Date	Decline	1 Year After	2 Years After	3 Years After
9/25/1981	-20%	9%	23%	14%
10/19/1987	-33%	23%	24%	12%
10/11/1990	-20%	30%	17%	16%
4/4/2001	-27%	2%	-11%	1%
9/21/2001	-26%	-12%	4%	5%
7/23/2002	-32%	24%	17%	16%
10/10/2008	-37%	19%	14%	10%
11/20/2008	-25%	45%	26%	17%
3/9/2009	-28%	69%	40%	27%
12/24/2018	-20%	37%	26%	26%
9/22/2022	-24%		?	
AVERAGE	**-27%**	**25%**	**18%**	**14%**
BEST	**N/A**	**69%**	**40%**	**27%**
WORST	**N/A**	**-12%**	**-11%**	**1%**

The news is dismal in European and Asian markets, but should these foreign-domiciled companies be free? At what point is the juice worth the squeeze? The data supports we are there. Certain developed markets, like South Korea and Germany are trading at fire-sale prices. As we already stated above related to US stocks, we can't, nor will we try to time the market bottom in foreign equities. Having said that, these indexes below, contain many of the world's largest multi-national corporations that generate revenues all over the globe. At present, these markets all trade at enormous discounts to the US stock market and at more reasonable prices based on historical measures.

Index	Price to Sales Ratio	Discount to S&P 500	% of 52 Week High
S&P 500	2.1	N/A	23.4%
iShares Germany Index Fund ("EWG")	0.7	67%	42.2%
iShares United Kingdom Index Fund ("EWU")	1.2	43%	25.2%
iShares Japan Index F und ("EWJ")	0.9	57%	31.2%
iShares South Korea Index Fund ("EWY")	0.6	71%	39.3%
iShares MSCI China Index Fund ("MCHI")	1.1	48%	40.7%
iShares MSCI Emerging Markets ex China Index Fund ("EMXC")	1.2	43%	27.4%

With continued geo-political uncertainty, investing in these stocks will involve risk. However, we feel there is also tremendous upside here for investors with a longer time horizon (5+ years) who can ride out the near-term volatility. We believe most if not all the bad news is priced into the European and Asian equity markets. The result is that valuations are simply too cheap to ignore and there are several potential positive events (such as those listed in bullet points below) that could drive rapid recoveries in these markets.

- *Peace in Europe.* If fighting in Ukraine stops, which could happen under several different scenarios, we feel that European equities could rebound 30-40%+ in a short period of time.

- *New aggressive monetary and/or fiscal stimulus in Europe and Asia.* If the post-2008 era has taught us anything, it's that tough times generally bring easy central bank policy not only in the US, but in Japan and Europe. The FED is exhibiting extreme hawkishness right now, but as stated above, they have done 180º turns before. The UK recently increased rates in Europe, but if extreme recession sets in, it's hard to believe additional stimulus will not be implemented which would present a tailwind for European stocks.

- *Chinese ADR Delisting Risks Materially Subsiding Over Ongoing Progress in Negotiations between China Securities Regulatory Commission and US Public Company Accounting Oversight Board.* Over the last couple years, Chinese "ADRs" (Chinese companies listed on US exchanges) have widely plummeted in value as the US has threatened delisting these stocks without increased inspection access over audit workpapers. Tencent (↓65%), Ali Baba (↓75%), Baidu (↓65%), Meituan (↓65%), and Nio (↓70%) have lost ~$700B+ collectively in market capitalization since 2020. While China is unpredictable, it's hard to imagine follow-through on policies that would result in permanent loss for foreign investors buying shares of Chinese companies. Like the US, China needs outside capital from foreigners to enhance the strength of its economy. As noted by Goldman Sachs on 8/28, delisting risks have been halved in recent months due to increased cooperation between these two countries. Additional progress made here presents enormous upside opportunities for the largest Chinese companies in the world's 2nd largest economy.

- *Dollar Strength Subsiding:* Emerging market stock performance has been materially / adversely impacted by the strongest dollar in decades. Predicting currency movement is another example of a fruitless investing endeavor, but it's generally safe to say that emerging market economies see outsized damage from a strong dollar as they must convert their local currencies to USD to repay borrowed money. Paying back debt in a strong USD is horrible for their economic health. If we see the dollar "cool off", emerging markets should also be the biggest winners. Legendary investor Jeffrey Gundlach of DoubleLine Capital (infamously called "The Bond King") sited on September 19th, 2022, that if USD strength subsides, "you want to be in big" (on emerging markets stocks) as they are "really really cheap".

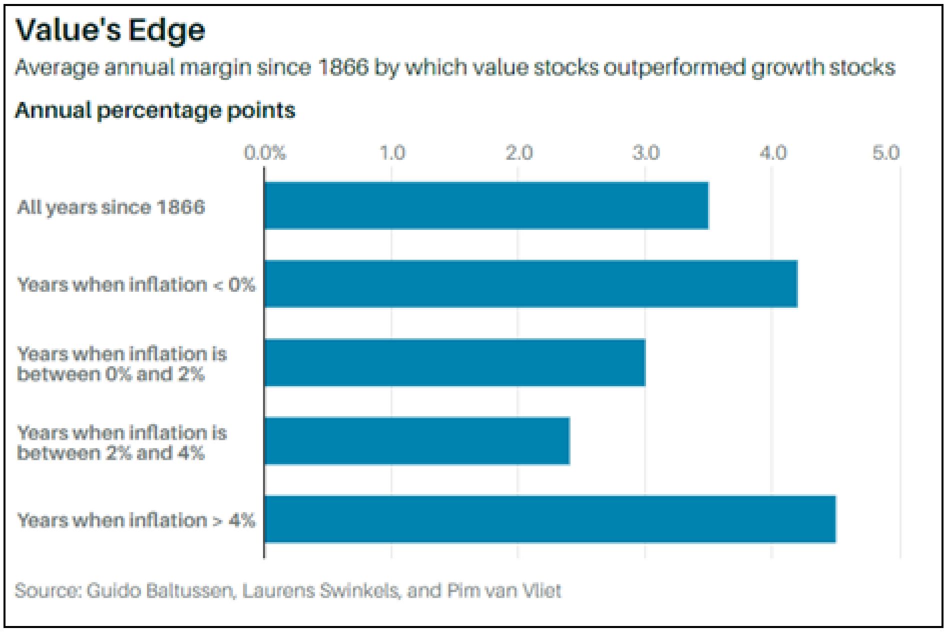
Some basic valuation math to consider when thinking about foreign stocks (see table below). Everyone knows that Germany faces enormous energy challenges due to the war in Ukraine and their dependence on Russian oil. So, just for sanity's sake, let's do a stress test. Let's assume that EWG's (Germany Stock ETF) companies experience an enormous drop in sales of 50% this coming year all while US companies in the S&P 500 retain a level year-over-year amount of sales (highly unlikely). Under this assumption, the price-to-sales ratio from this level (EWG trades at ~$20/sh) would be 1.4x sales. This would still be a 32% discount on price-to-sales to our home country S&P 500! <u>We hope this example, albeit oversimplified, illustrates what we mean by "bad news being priced in already".</u>

Description	Current	50% Germany Sales Decline Stress Test
EWG Price Per Share	$ 20.00	$ 20.00
EWG 12 Month Revenue / Share	$ 28.50	$ 14.25
Price-to-Sales	0.70	1.40
Price-to-Sales S&P 500	2.07	2.07
Germany Index Discount	66%	32%

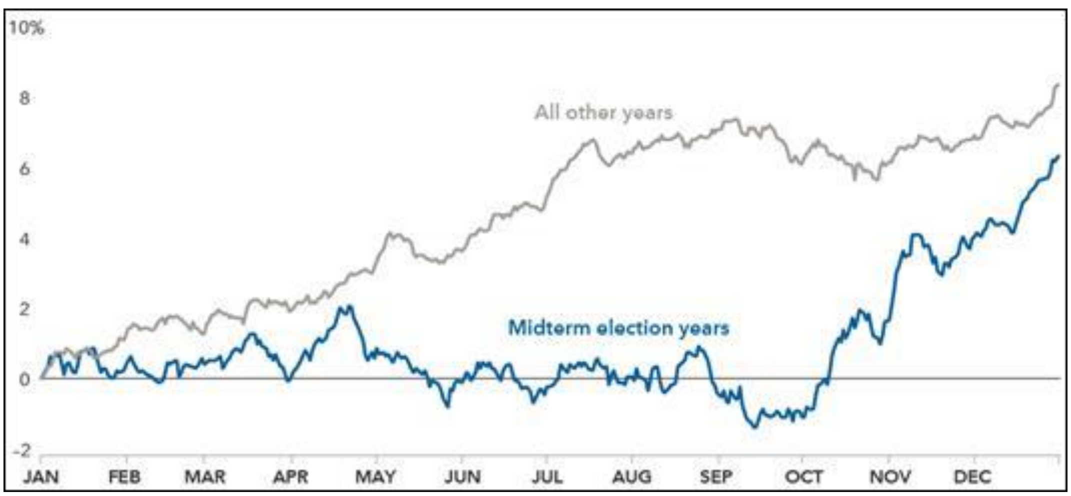
EWG Dividend Yield	S&P 500 Dividend Yield	Dividend Yield Premium on Germany Index
4.92%	1.52%	224%

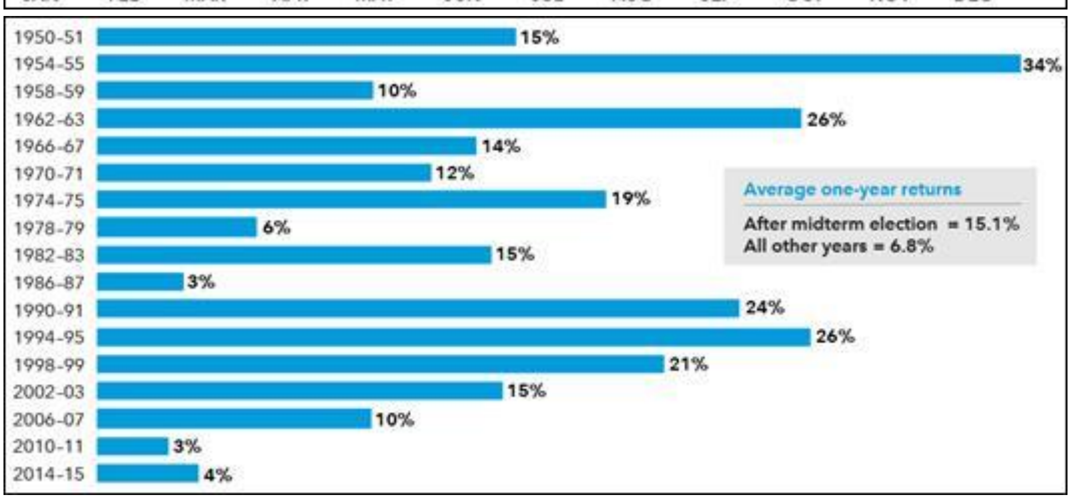
Despite dismal relative performance vs. growth stocks from 2008-2021, value stocks have outperformed over ~95 years of recorded history with a high degree of reliability for investors with a 5+ year holding period. The incremental return in value stocks vs. growth stocks has increased as inflation increased (see 1st chart below). With unexpectedly high inflation in 2022, value stocks have outperformed by a wide margin (both in the US and International stocks).

At FFG, we tend to favor value stocks both in our selection of index fund products and in our own individual stock portfolios. The result has generally been that our US equity allocations have outperformed broad benchmarks in 2022 after lagging in 2020 and 2021. This is a theme we intend to consistently apply over time. Despite significant outperformance of value stocks in 2022, value stocks remain inexpensive (if history is our guide) relative to growth stocks (2nd and 3rd charts below). As such, we will maintain our bias to these types of stocks looking ahead.



While we place <u>less weight</u> on politics as investors, mid-term election years have historically been tough and better times might lie beyond Nov'2022 elections.





Bond losses in 2022 are unprecedented. We avoided most of the pain, and now see more opportunity in slightly longer-term bonds. *From Forbes: "Looking back to 1977 using the Bloomberg US Aggregate Index, you can see that 2022 is the worst year for bonds. In 45 years, bonds have fallen in value only five times, and the most significant decline was 2.9% in 1994. In 2022, the bond index is currently down by more than 11%." [↓14.2% as of 9/22].*

At FFG, we made a concerted effort to keep exposure to "interest rate risk" (measured by the average maturity length of bonds in a portfolio) to a minimum as rates hit all-time lows at the close of 2021. The lion's share of our clients' bonds are down in the low-to-mid single digits so far this year. As prices on bond indexes have dropped much more significantly *(↓14.2%* for the Barclays Agg Bond Index), the potential returns expressed as yield-to-maturities have significantly increased. For example, the yield on the 5-year treasury now rests at 4.02% up from a meager 1.26% at 12/31/2021. *Bank accounts for anything but very short-term money now seem like an **unattractive** location for your reserve funds. Treasury bills present far better prospects, particularly after the tax advantages are considered.*

Taking on Credit Risk in bonds still seems premature considering recession risks where corporate defaults tend to spike. In March of 2020, junk bond yields skyrocketed to 11.38% against what were sub 1% 10-year treasury yields. In other words, a ~10% premium yield could be earned for taking on credit risk lending money to less creditworthy companies instead of the US gov't during the height of COVID-19 lockdowns. In today's market, yields on junk bonds have gone up again due to recession risks (8.84% as we write this note), but offer only ~5% incremental income against what is now a 3.7% yield on the 10-year US treasury bond. We do not feel that a 5% premium justifies junk bond investing at the moment with recession risks where they are.

Market Date	10 Year Treasury Yield	Ice BofAML Junk Bond Index Effective Yield	Spread
March 23th, 2020	0.76%	11.38%	10.62%
September 22nd, 2022	3.71%	8.84%	5.13%

Cash Flow Planning should still be the (primary) driver for your investment plan and only longer-term money should be allocated into stocks. If you are unclear as to what an appropriate "cash/bond allocation" should be for you based on your circumstances, please schedule time with us immediately to review your plan.

We appreciate your trust and acknowledge that this is a very tough time for our clients, like it is for all investors, to stay disciplined. Rest-assured, we follow these same disciplines with our own investments. Let's all hope for better times ahead!

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