Private Wealth *perspectives*

VERSION 23.3

INVESTMENT MANAGEMENT • FINANCIAL AND ESTATE PLANNING • PRIVATE BANKING • FIDUCIARY ADMINISTRATION • RETIREMENT PLAN SERVICES

Legendary investor Warren Buffett famously said, "The true investor welcomes volatility" and while we agree, a little respite would be welcome! Headline news brings the volatility of the world into sharper view each day with stories of global unrest, political tension and stalemate at home and the challenges created by rapidly rising interest rates and stubbornly sticky inflation. But sometimes it's a step back from the day-to-day that helps create the clarity needed to navigate these seemingly unstable times. In this edition of Perspectives our team seeks to educate on a few fundamental tenets of building a successful plan and a recap of the remarkable first half of 2023. If volatility is simply a short-term mask for long-term opportunity as Mr. Buffett states, then appropriately our focus is to ensure our clients are positioned for the long-term and not knocked off course by short-term volatility. Thank you for taking time to engage with the thoughts of our team and to benefit from our perspective.

Stay Healthy. Stay Safe. Stay Positive.

Michael Joyce
President, Private Wealth Advisors

> "**Volatility** actually is the opposite of risk. It's opportunity. But you need to think through and fight some basic human weaknesses."
>
> JEFF UBBEN

> "**Volatility** is the price of admission. The prize inside are superior long-term returns. You have to pay the price to get the returns."
>
> MORGAN HOUSEL

RETIREMENT PLAN SERVICES

Secure 2.0

We keep hearing about Secure 2.0 (Setting Every Community Up for Retirement Enhancement Act 2019). It brings many changes as well as many questions. It is intended to improve retirement outcomes. Congress and the IRS are still working on the specifics and how plans will incorporate these features. While there are many features, we will focus on a few that are important to our plan participants and sponsors.

1. CATCH UP CONTRIBUTIONS – Beginning in 2024, for participants that earned more than $145,000 in the prior calendar year, all catch-up contributions at age 50 or older will need to be made to a Roth source (in after-tax dollars). Participants who earn $145,000 or less, will be exempt from the Roth requirement.

   Beginning January 1, 2025, participants ages 60 – 63 years of age will be able to make catch up contributions up to $10,000 to their qualified workplace retirement plan. (The catch-up limit for participants 50 and older for 2023 is $7,500)

2. AGE INCREASES FOR RMD's – Beginning January 1, 2023 the age requirement for taking your RMD is age 73. The age increases to 75 in 2033. If you turned 72 in 2022 or earlier, you need to continue taking RMDs as scheduled. If you will be turning 72 in 2023 and have already scheduled your withdrawal, you may wish to update your schedule for withdrawals.

   - Starting in 2023, the penalty for not taking your RMD will decrease from 50% to 25% of the RMD amount not taken.
   - Beginning in 2024, Roth accounts in qualified employer plans will be exempt from the RMD requirements.

3. AUTOMATIC ENROLLMENT – Beginning in 2025, new 401(k) and 403(b) plans will require eligible employees to be automatically enrolled at a rate of at least 3%.

4. STUDENT LOAN DEBT – Beginning in 2024, employers will have an option to "match" employee student loan payments with matching payments to a retirement account. This will be an incentive for participants to save while paying off student loan debt.

5. EMERGENCY SAVINGS – Beginning in 2024, plans will have the option to add an emergency savings account that is a designated Roth account. This will only be permitted for non-highly compensated employees. Contributions will be limited to $2,500 annually (or lower if the employer determines). Participants will be permitted to take the first 4 withdrawals in a year, tax and penalty free. This is intended to encourage more saving since participants will be able to access their funds in the event of an emergency without being penalized.

These enhancements will help participants to more easily prepare for a comfortable retirement. Should you have any questions you may reach out to your Retirement Plan Advisor listed below.

John McMahon
Retirement Plan Advisor

John McMahon

If you have any questions or would like to talk to one of our retirement plan team members, the Retirement Specialists at First Merchants Private Wealth Advisors are here to help:

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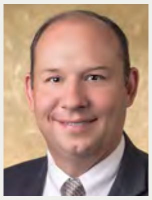
INVESTMENT MANAGEMENT



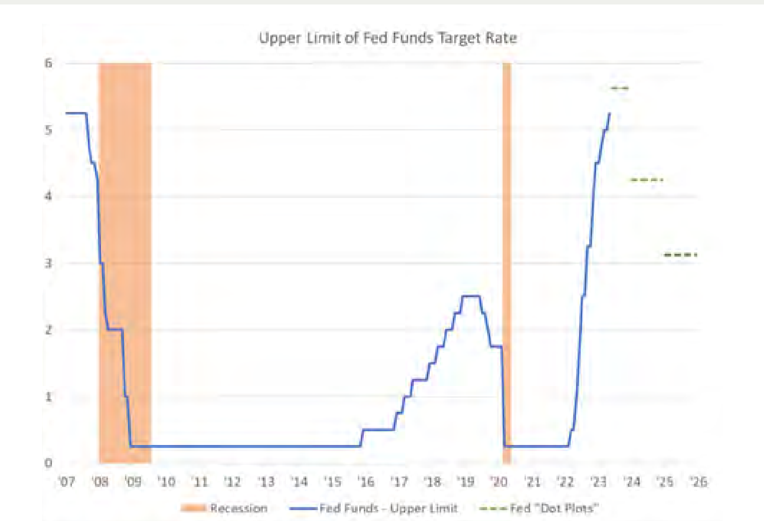
First Half Recap & Second Half Outlook

Pessimism turned to optimism in the U.S. financial markets as the calendar turned from 2022 to 2023. After enduring inflation levels at 40-year highs, seven rate hikes from the Federal Reserve, equity market returns of -20% and bond market returns of -13%, investors were eager to leave 2022 behind. As inflation began to show signs of slowing, equity markets moved upward early in the year amid hopes that the Federal Reserve's rate hike cycle was nearing an end. The recovery was firmly underway until early March when cryptocurrency-focused Silvergate Bank announced it was closing down operations due to losses suffered in its loan portfolio. Two days later, on March 10, a bank run at San Francisco based Silicon Valley Bank caused it to collapse and be seized by regulators later that day. On March 12, regulators closed Signature Bank, a New York based bank that also focused on the cryptocurrency industry. The bank failures put significant pressure on the financial system as concern spread among investors over the safety of the U.S. banking system, and regional banks in particular. Depositors began withdrawing cash from some regional banks, with San Francisco-based First Republic Bank losing $100 billion in deposits by the end of March. Despite a $30 billion lifeline from a group of major U.S. banks and $70 billion in financing from JPMorgan Chase, First Republic Bank was closed by California regulators on May 1 and its assets were sold to JPMorgan Chase. The collapses of First Republic Bank, Silicon Valley Bank and Signature Bank were the second, third and fourth largest bank failures in the history of the United States, eclipsed in size only by the failure of Washington Mutual during the 2007-2008 financial crisis. We agree with RBC Wealth Management's Atul Bhatia, who wrote in April that "A crisis for a few banks is not a banking crisis". This is not a systemic problem encompassing the entire financial system as with the 2008-2009 financial crisis, but rather a contained event involving a limited number of banks with similar elevated risk profiles.

Thanks to a quick response from the Federal Reserve to put some special liquidity instruments in place to limit the fallout across the banking sector, market concerns began to fade and the focus turned to the looming debt ceiling deadline. The country had actually hit its debt ceiling on January 19, 2023, and had been acting under "extraordinary measures" since that time. Treasury Secretary Janet Yellen warned that these measures could be exhausted as early as June 1st. Markets remained cautious as the date loomed closer with no agreement reached between President Biden and House Speaker Kevin McCarthy. Finally on May 27, Biden and McCarthy struck a deal to increase the debt ceiling but cap federal spending. The deal resulted in the bill known as the Fiscal Responsibility Act of 2023 which passed the House on May 31, the Senate on June 1, and was signed into law by President Biden on June 3, bringing the crisis to an end. Some of the provisions in the bill include: The suspension of the debt limit until January 1, 2025, discretionary spending capped for fiscal years 2024 and 2025, rescind all unused funds appropriated during the COVID-19 pandemic, rescind 25% of the $80 billion in additional funding for the IRS provided for in the Inflation Reduction Act of 2022, and the student loan payment moratorium enacted in 2020 is to end on September 1, 2023.

With the banking system and debt ceiling uncertainties resolved, markets looked to end the first half of the year on an upswing. At their June meeting, the Federal Reserve elected to hold rates steady, after raising the Federal Funds Rate at each of the prior ten meetings. A broad stock market recovery seemed underway, with the S&P 500 rising nearly 9% on the year through May. In reality, the breadth of the market resurgence was actually very narrow. While seven Mega-Cap technology related names (Apple, Amazon, Microsoft, Google, Meta, Nvidia, Tesla) had a cumulative market cap growth of nearly 50% through May, the other 493 stocks in the S&P 500 had a cumulative market cap growth of -1.1% over that time. In other words, without the performance of those seven stocks, the return of the S&P 500 would have actually be flat to slightly negative. There is also a disconnect between the market capitalization of the largest stocks in the S&P 500 vs. the amount of earnings they produce. Currently the ten largest stocks in the S&P 500 represent 32% of the value of the index but produce only 21.6% of its earnings. This differential is significantly larger than even that of the "dot com bubble" years of 1999 – 2000. The narrow bull market leadership will be one trend we'll be watching in the second half of 2023.

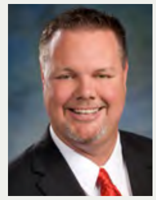
While exuberance over the rising popularity of Artificial Intelligence (AI) drove the outsized returns among a select few technology stocks in the first half of the year, we remain cautious about the staying power of the resulting elevated valuations. As the novelty of the "AI Takeover" wears off, we expect valuations for AI related names to return to more reasonable levels in the months ahead. Cautiousness also prevails in our attitude surrounding the immediate path forward for the Federal Reserve. While earlier forecasts indicated the June Fed meeting to be the peak of the rate hike cycle, current projections are signaling more rate hikes ahead. The Fed's "dot plot," a graphic showing the future path of the expected Federal Funds Rate, with each dot representing the rate expectation of a Federal Open Market Committee member, now shows two more hikes ahead. In Fed Chairman Jerome Powell's June press conference, he was quick to point out that "not a single person on the committee wrote down a rate cut this year, nor do I think it is at all likely to be appropriate." Powell went on to say he doesn't see a rate cut coming until inflation comes down meaningfully and significantly, to which he added, "we're talking about a couple of years out." Although one half of the Fed's dual mandate, price stability (low inflation), has garnered most of the headlines, the other half of the mandate, maximum sustainable employment, remains worth watching going forward. Since the current unemployment rate remains well below the Noncyclical Rate of Unemployment trend line, there is nothing signaling the need for a rate cut on the unemployment front at this time. With both sides of the Fed's mandate signaling continued tightening of monetary policy, it creates the potential to become an obstacle for stocks. Given the types of stocks that have rallied the most, persistently high rates could work like a vise tightening on the economy and weighing on growth. Based on history, the Fed typically tightens until something breaks. In this case, it could be the consumer. Given that consumer spending drives roughly two thirds of our nation's GDP, it's an important indicator. Metrics show consumer spending is cooling but not yet falling off a cliff. Cracks are beginning to show, however, as excess consumer savings from the Covid pandemic have dried up and credit card usage and payment delinquencies have ramped up. Total U.S. consumer credit card balances outstanding have now passed $1.2 trillion for the first time ever. Persistently higher interest rates will make the desired economic "soft landing" considerably harder for the Federal Reserve to achieve.



As we consider how to position investments for the remainder of the year, we have already taken a step to de-risk portfolios by significantly reducing our exposure to high yield bonds. The additional risk of owning high yield bonds in a slowing economic environment outweighs the potential rewards. In addition, we will also be looking at equity market valuations and asset allocations that could potentially provide higher expected returns going forward. Based on current equity market valuations versus long-term historical trends, international developed and emerging market equities appear to be attractively valued relative to U.S. large cap stocks. Bonds have found a renewed role in portfolios as well, with yields rising to levels last seen some 15 years ago. With short-term Treasury Bills yielding over 5% and investment grade corporate bonds providing yields over 6%, there are finally sensible alternatives in the fixed income space after years of ultra-low interest rates. We thank you for your continued confidence in First Merchants Private Wealth Advisors. As always, please reach out to a member of your First Merchants PWA team with any comments or questions. We look forward to a sustained partnership with you throughout the remainder of 2023 and beyond!

Travis McEowen
Portfolio Manager

WEALTH MANAGEMENT



Sequence of Returns

As you may have heard 2022 was an unprecedented year for investors. The equity markets saw a significant decline that coincided with one of the worst bond markets in recorded history. A year like 2022 coupled with the first few years of withdrawals during retirement can jeopardize the success of a retirement plan. The sequence of returns in retirement is often times overlooked in the planning process.

The sequence of returns refers to the order in which investment returns are experienced over a specific period. When you're drawing down retirement savings, the sequence of returns becomes crucial because it can significantly impact the longevity of your portfolio and your ability to sustain a desired standard of living throughout retirement.

2023

The sequence of returns matters for several reasons:

Portfolio Performance: The performance of your investments in the early years of retirement can have a lasting impact. If you experience poor returns or significant losses early on, it can deplete your portfolio more quickly and reduce the overall value of your investments.

Withdrawal Rate: The sequence of returns affects the sustainability of your chosen withdrawal rate. A withdrawal rate is the percentage of your portfolio that you withdraw annually to cover expenses. If poor returns occur early in retirement when you're withdrawing funds, it can lead to a higher depletion rate, forcing you to withdraw a larger percentage of your portfolio to maintain your standard of living. This increased withdrawal rate may put your portfolio at risk of running out of money prematurely.

Loss Aversion: Humans tend to be loss-averse, meaning we feel the pain of losses more than the pleasure of equivalent gains. If you experience significant investment losses early in retirement, you may be more inclined to make emotional decisions like selling investments at a low point, which can further erode your portfolio's value.

> "
>
> If your portfolio loses 20% in a year what will your return need to be in year number 2 to return to your original value?
>
> (ANSWER AT THE END)

To mitigate the impact of unfavorable sequence of returns, you can consider the following strategies:

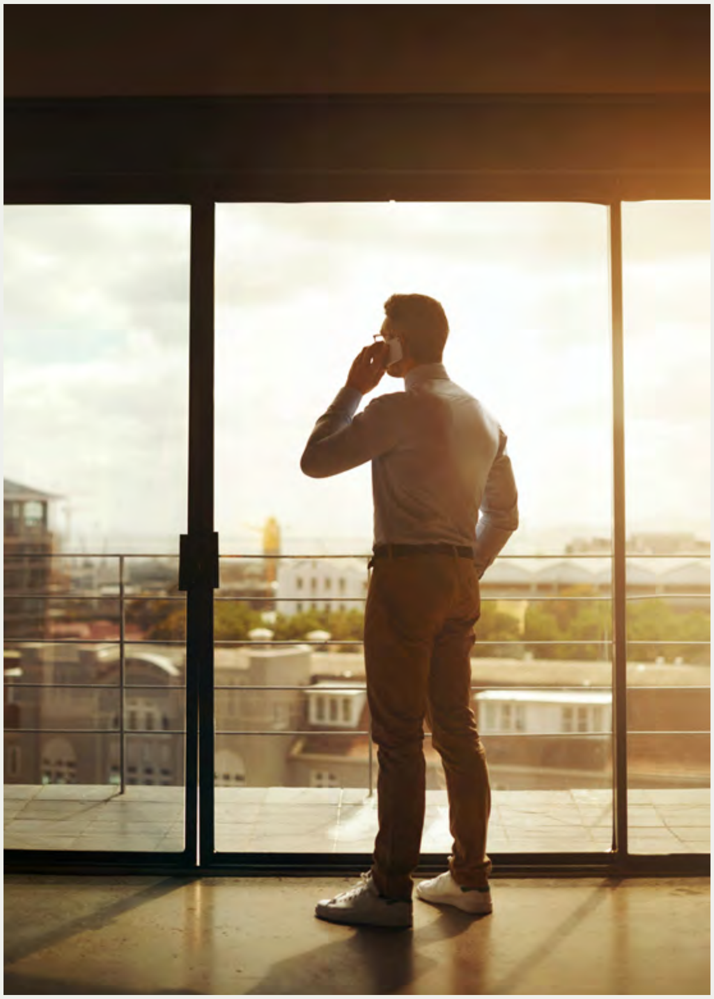
Diversification: Maintain a diversified investment portfolio to spread risk across different asset classes. This can help reduce the impact of poor performance in a single investment.
Asset Allocation: Allocate your investments based on your risk tolerance and time horizon. Balancing assets that offer growth potential with those that provide stability can help manage volatility.

Flexibility in Withdrawals: Be prepared to adjust your withdrawal rate and spending habits based on market conditions. During periods of poor returns, consider reducing your withdrawals to protect the longevity of your portfolio.

Professional Guidance: Seek advice from a qualified financial planner or investment advisor who can help you create a retirement plan that considers the potential impact of the sequence of returns.

By understanding and accounting for the sequence of returns, you can make informed decisions to help safeguard your retirement savings and maintain financial security throughout your retirement years.

Michael Tomaw
Wealth Manager



> "
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> The answer is 25%"

WEALTH MANAGEMENT

To Trust or Not to Trust

If you read any of the "retirement" type publications (basically those aimed at seniors like me), you likely have seen the terms "living trust", "revocable trust", "grantor trust", etc. These terms are pretty much interchangeable and refer to the same type of entity. These are heavily touted as estate planning tools primarily to help individuals shield their estates from probate costs. Ok, so what exactly is this entity, you might ask? That is the precise question we hope to briefly explore. Further, and perhaps more importantly, should everyone have a living trust as part of their life and estate planning? We'll also delve into that issue.

First, let's start with the basics. In so doing, our discussion here will be limited in scope to the living trust. There are MANY other type trusts. However, the extent and specifics of other types could fill volumes of pages—way too far into the weeds for now.

DEFINITION OF A LIVING TRUST

A living trust is a legal entity that allows for a person or persons to place assets into the name of the trust, with said assets to be managed for the purposes outlined in the TRUST AGREEMENT. The trust agreement is a legal document that (1) outlines the purposes of the trust, (2) governs how the contributed assets are to be managed, and (3) specifies how the trust assets are to be used or expended. The trust agreement also identifies the trustee(s) and successor trustee(s).

REASONS FOR CREATION OF A LIVING TRUST

Such trusts can be set up for a number of reasons. Typically those reasons fall into the following general categories:

1. Avoidance of probate costs at death-trust agreements can be effectively drafted such that, at the death of the grantors (the persons establishing the trust), the trust assets held can pass to the beneficiaries named in the trust agreement OUTSIDE the probate estate of the grantors.
2. This can greatly simply and reduce the costs related to the final affairs of the grantors. Life planning-living trusts typically transfer the burden of managing trust assets to the trustees. The grantors can specify in the trust agreement what is expected of the trustee—while the grantors are still alive and after they have passed. Such management directives, for example, could include (a) paying the bills/expenses of the grantors, (b) overseeing the preparation and payment of the grantors income taxes, (c) maintenance of any homes or real estate owned by trust, etc.
3. Estate planning-a living trust can be a useful tool in planning for how the grantors' assets are to be used or distributed after the grantors are deceased. The trust agreement can address special family situations. Among the more typical might be (a) provisions for a handicapped family member, (b) provisions for a minor child or (c) special provisions for children of a first marriage if the grantors are from multiple marriages.

SELECTION OF A TRUSTEE AND SUCCESSOR TRUSTEE

If it is decided that a living trust fits the needs of the grantors, one of the major issues becomes the selection of the trustee and the successor trustee. Typically, if the grantors are capable, they name themselves as initial trustees. This makes sense in many cases. They have probably managed their own affairs for years. They can certainly continue as their own trustees.

Ah, but what if one or both trustees are unable to handle their affairs? This is where the naming of the successor trustee becomes critical. At some stage, the grantors/initial trustees may want an entity or person to step in and take over. This becomes the job of the successor trustee. The successor trustee is the person or entity the grantors designate in the trust agreement to manage the trust in a later phase.

In choosing a successor trustee (or any trustee), the grantors should consider some of the following factors:

1. Continuity/stability-these should weigh heavily in any decision related to the choice of a trustee. The trust's term may extend over many years and beyond the lives of the grantors. If an individual is chosen, consideration should be given to the health and potential lifespan of that person. It is important that any trustee is around and can capably serve in that capacity for many years.
2. Investment and other specialized skills-a trustee must be capable of investing the trust assets productively and prudently. Trustees should have the skills to (a) make investment decisions within a planned investment strategy, (b) account for the trust's cash and investment activity, (c) address tax issues, and (d) conscientiously follow the

instructions provided in the trust agreement. A non-professional trustee may have limited experience in knowing what is required to fulfill the trustee's duties. Additionally, an individual may lack the investment, accounting, and tax skills needed to insure issue-free administration. Further, a non-professional trustee may not have the time needed to manage the assets and attend to the needs of the grantors properly.

3. Objectivity-the trustee may be called upon to make careful decisions in the best interests of the grantors. A professional trustee can make decisions objectively and can avoid being influenced by persons with a stake in the trust or by emotions of others involved.
4. Individual trustee vs professional trustee-depending on the complexity of the situation, the family dynamic, the needs of the grantors, and the make up of the trust assets, consideration may want to be given to the designation of a professional (like First Merchants) to serve as trustee or successor trustee. In a successor trustee role, the professional can assume responsibility for the management of the trust at such time as the initial trustees deem appropriate. There may be fees associated with the engagement of a professional. However a professional trustee can provide a high degree of efficient administration and such engagement can be well worth the costs.

SHOULD EVERYONE ESTABLISH A LIVING TRUST?

The simple answer to this question is no. Living trusts are useful tools. Family situations exist that warrant consideration of such a trust. However, the establishment of a living trust comes at a price. The trust agreement, as stated earlier, is a legal document. It must be drafted by an attorney. Drafting such agreement, depending on complexity, can run from $1,000 to more than $10,000.

Before one jumps into trust mode, there are also other items to consider. If probate avoidance is the primary concern, potential grantors should critically review the value and composition of their assets. Not all assets would normally be considered part of a person probate estate. For instance, IRAs, other retirement plans, and life insurance typically have beneficiary designations which bypass the probate estate. Also, assets held in joint ownership with rights of survivorship and those with transfer on death designations normally avoid the probate process. After grantors "strip away" these type asset holdings, the grantors may find that the probate assets of their estate occupy a reasonably small value. If this is the case, most states have what is referred to as a small estate statute. In short, depending on your state of residence, if the value of your total probate estate assets are below a set threshold, no probate estate administration is required to be opened.

IF ON THE FENCE, ASK!

The folks at First Merchants would be happy to review and "talk through" with you the specifics of your situation. Our goal is always to provide accurate information and help people meet their needs.

Neal Barnum
Regional Manager, Wealth Management