UBS Financial Services Inc.
One Broad St Plaza Fl. 2
Glens Falls NY 12801

Tel. 518-743-2073
Fax 855-848-5007
Toll Free 800-526-3763

Pearsall Wealth Management

Adam E. Pearsall, CFP®
Senior Vice President – Wealth Management
Senior Portfolio Manager

Melissa T. Battiste, CRPC®
Senior Wealth Strategy Associate

Tara Johnson
Client Service Associate

October 2023 Pearsall Wealth Management Newsletter

Index[1]	3rd Quarter 2023	Year to Date 2023
S&P 500	-3.27%	13.07%
Dow Jones Industrial Average	-2.10%	2.73%
Russell 2000	-5.13%	2.54%
MSCI EAFE	-4.05%	7.59%
Barclays Aggregate Bond	-3.23%	-1.21%
US Treasury Bill – 3 month	1.34%	3.71%

Thomson Reuters performance data as of 9/30/2023

Market volatility returned this past quarter with most asset classes ending the quarter lower than they began in July[1]. Thankfully year to date most remain higher than where they started the year. One important caveat is the returns have been narrow, for example within the S&P 500 (500 largest publicly traded companies within the US) the majority of returns have come from 7 stocks this year[2], namely mega-cap growth oriented companies viewed as leaders in artificial intelligence.

Where do interest rates go from here? In our view they are likely to move lower from here. We've enclosed a short informative report from UBS Chief Investment Office from October 10th (*UBS House View Daily, Yields do part of the Fed's tightening task*) which goes into more detail on the market fundamentals and mechanics of why rates may soon move lower.

Why not just stay in cash? Though many of the year to date returns above exceed that of cash, there is market risk and volatility involved, and it can be tempting to sit on the sidelines with cash right now. The risk you retain, as discussed back in our July newsletter, is the reinvestment risk – as noted above rates are likely to move lower, and whether you are in savings accounts, money markets, or even CD's when you go to reinvest the yields are likely to already have adjusted in other asset classes, with those who are invested already receiving the benefits of higher yields and / or price appreciation. Though the market tends to rhyme rather than repeat itself and past history is no guarantee of what we will experience the next few years, we've enclosed an informative piece from MFS that looks at overall returns of various fixed income classes when interest rates are peaking. UBS particularly likes investment grade fixed income at this time given the current yields[3]. It has been said that fixed income is the "self-healing" asset class; if a bond is trading at a discount the price will rise as it approaches maturity (bonds mature at par (typically 100)), in addition to the interest received. Given the dislocation in fixed income markets the past two years the total return (change in price plus the yield) is currently more attractive than it has been in some time.

Shifting gears if you are curious about "Artificial Intelligence" and have not watched the video series that Melissa sent out a link to last month I encourage you to do so. Though each are interesting, the last video "AI in action: use cases" which aired September 6th, may be the most interesting for those who are curious about how generative AI is being used today and how it may transform certain positions within the next few years. The videos are available at: https://www.ubs.com/global/en/wealth-management/insights/summer-of-artificial-intelligence.html

Please give us a call if you'd like to review your portfolio, update your financial plan, discuss any of the items above, or catch up in general.

From Melissa-

Cyber Security- October is Cyber Security Awareness month and is now in its 20th year. The Department of Homeland Security and the Federal Bureau of Investigation (FBI) collaborate each year with their top tips and they include[4]:

- Keep all systems and software up to date and using a good antivirus program.
- Scrutinize email addresses and URL addresses. Sometimes scammers use slight variations in spelling.
- Never respond to an email or text requesting you to update, check or verify any kind of account information. It's best to separately go to the website (not using any link provided) and login using credentials you usually use.
- Scrutinize any electronic requests for payment or transfer of funds.
- Be extra weary of "urgent" requests.
- Always confirm payments or wire transfers in person or over the phone with all parties involved.

One of my favorite ways to keep on top of my identity and making sure everything is the way it should be is regularly checking my credit reports for free. I feel comfortable doing it online but should you not, the top three credit reporting agencies have ways to request them by phone and by mail. I spread them out throughout the year and I always make sure I don't pay for anything when completing the report request.

Decluttering- For many, spring is the time of the year for decluttering and cleaning projects, but for me it's fall. The thought of the approaching Halloween, Thanksgiving, and Christmas holidays spurs the decluttering motivation in me. One item that is the easiest to go through for me is paperwork (toys and clothes not so much). While I have my own UBS statements on E-delivery I know many do not. Financial institutions like ours are legally required to send out regular statements, prospectuses, fund updates, and disclosures.

If you feel like decluttering and think you might want to give E-delivery a try please reach out to myself and Tara. We can either show you how to do it on UBS Online Services over the phone, via Zoom or many of our clients bring their phones, laptops and tablets into the office and we can help you in person. As we have mentioned to many of you before, you can securely shred your old UBS statements no longer needed by stopping in to see us or bringing them to a regularly scheduled appointment.

Benefits Enrollment- Mid October through the end of the year is typically medical healthcare plan enrollments for many types of enrollees- Medicare, Medicaid, State Marketplace and Employer sponsored plans. Whether choosing workplace benefits or retirement healthcare benefits UBS Advanced Planning Group suggests following a four point checklist:

1. *Choose Health Insurance Plan*- Review the premiums, deductible, coinsurance, copays, and out-of-pocket maximum terms for each plan, and use these to evaluate the total costs you may be exposed to over the coverage period. Review costs from previous year to get an idea of what your out of pocket costs may look like and be sure to set aside those funds in a flexible spending account (FSA) or health savings account (HSA) if you are eligible.

2. *Protect your human capital*- calculate your disability and life insurance need, review current coverage and determine if there is a gap. If there is gap, review what is available at work and/or if you are retired or nearing retirement please talk to us to see if can price out potential coverage for you.

3. *Save for retirement*- determine how much you can afford to save by comparing your spending and your income. Review your employer's retirement savings plan (limits, matches, retirement contributions). Invest in yourself by increasing with any subsequent pay raises after year end.

4. *Make the most of equity awards*- Gather the details of your equity compensation plan and share them with us. One thing that is very important that many people overlook is to monitor the amount of your wealth that is held in your company's stock. It's important to manage the risks associated with holding a concentrated stock in your portfolio.

Learn more by checking out the full report (physical copy available upon request), video explanations, and podcasts on the Advanced Planning page.

From Tara-

Year End Planning

Required Minimum Distribution: RMD's are the minimum amount that you must withdraw annually from your IRA when you turn a certain age. Beginning in 2023, the SECURE 2.0 Act raised the age that you must begin taking RMDs[5].

- If you were born between July 1, 1949 and before 1951 your required minimum age is 72.
- If you were born between 1951-1959, your required minimum age is 73.
- If you were born 1960 or later your required minimum age is 75.

You must take your first required minimum distribution for the year in which you reach your required minimum age by April 1st of that next year. Just be aware if you do this you would be doubling up in one tax year. If you have any questions about how much you have left of your RMD please give me a call and I would be happy to help you.

Gifting: If you are considering gifting this year please let us know by the beginning of December if you will be giving gifts of stock or setting up 529 plans for your kids, grandkids or great grandkids. In addition, for those over 70 ½ by year end if you have any charitable giving you would like to do as a Qualified Charitable Distribution from your IRA just let us know so we have plenty of time to process paperwork.

Fees: Annual RMA, IRA and Qualified Plan account fees are coming up. If you would like to pay ahead you are welcome to do that, otherwise it will come out automatically on December 6th.

Best wishes for a great Fall,

Adam E Pearsall, CFP®
Senior Vice President-
Wealth Management
Senior Portfolio Manager

Melissa Battiste, CRPC®
Senior Wealth Strategy Associate

Tara Johnson
Client Service Associate

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529 plans are sold with program descriptions that contain details of the risks, fees and charges associated with the particular investment, which you should read carefully before investing. Even though individuals are not required to invest in their in-state plan, some states do provide tax or other advantages exclusively to residents who invest in their own state's plan. For example, many states offer a state income tax deduction for contributions and/or state income tax exemption for qualified withdrawals. States may impose state tax liability on withdrawals and/or earnings from out-of-state 529 plans. In addition, some states offer prepaid tuition plans. Investors should be aware that the markets have risks and the value of their investments may change from day to day. Therefore, an investment's return and principal value will fluctuate so that an investor's shares, when redeemed or sold, may be worth more or less than their original cost
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[1] *Thomson Reuters via UBS Portfolio Management Report performance data as of 09/30/2023*
[2] CIO GWM Investment Research Blog Same old song and dance 8/9/2023
[3] UBS House View Monthly Extended – October 23 Intra-month update 10/4/2023
[4] *https://www.fbi.gov/contact-us/field-offices/norfolk/news/fbi-highlights-online-safety-tips-during-cybersecurity-awareness-month*
[5] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-required-minimum-distributions-rmds

Yields do part of the Fed's tightening task

UBS House View - Daily US

Solita Marcelli, GWM Chief Investment Officer Americas, UBS Financial Services Inc. (UBS FS)
Mark Haefele, Global Wealth Management Chief Investment Officer, UBS AG
Vincent Heaney, Strategist, UBS AG London Branch
Christopher Swann, Strategist, UBS Switzerland AG
Matthew Carter, Strategist, UBS AG London Branch
Alison Parums, Strategist, UBS Switzerland AG

Thought of the day

After a relentless rise over recent weeks, the yield on 10-year US Treasuries fell on Tuesday. Having hit an intraday peak of 4.88% on Friday, a fresh 16-year high, it fell to 4.66%. The decline appeared partly due to a broader rally in safe-haven assets, following the Hamas attack on Israel over the weekend and the threat that this could escalate into a broader regional conflict and disrupt oil prices.

Considerable uncertainty remains over several underlying forces guiding the Treasury market, including the outlook for government bond issuance, the economically neutral level of fed funds rates, and the term premium—the rate of compensation demanded by investors for holding longer-term over shorter-term bonds.

But, in our view, the recent upward momentum in yields has been spurred largely by technical factors and should be reversed:

Top Federal Reserve officials have hinted that the tightening of financial conditions resulting from rising yields may reduce the need for further rate hikes. Even after Tuesday's decline, the 10-year yield is still around 50 basis points higher than at the start of September. This restricts credit conditions and has contributed to a rise in the Goldman Sachs US Financial Conditions index to the highest level since last November, one that indicates a net drag on the economy.

This point was underlined by Dallas Fed President Lorie Logan, who said on Monday that "if long-term interest rates remain elevated because of higher term premiums, there may be less need to raise the fed funds rate." The comments were more impactful since President Logan has been among the more hawkish policymakers in advocating the need for continued tightening. Fed Vice Chair Philip Jefferson said the central bank could "proceed carefully" with any further hikes, and also suggested higher bond yields were doing part of the central bank's job for them. Following the comments, markets roughly halved the probability of a rate increase at the Fed's November policy meeting to around 14%, based on the CME Group's FedWatch estimate, and also scaled back the chances of a hike at the December meeting.

What to watch: 11 October 2023

- Minutes of the Fed's September policy meeting
- ECB Consumer Expectations Survey

The threat of higher rates for longer could also be receding, as higher yields restrain growth. The September dot plot, which charts the rate expectations of top Fed officials, pointed to just 50 basis points of easing for 2024, down from a 100 basis points in the prior June release. That added to concern that the Fed would feel it was necessary to keep rates elevated well into 2024 to curb inflation. Recently, the fed funds futures market has moved to price in faster easing in 2024, with four 25-basis-point cuts during the year, up from three at the time of the Fed's last meeting.

Inflation worries remain anchored, which bodes well for high-quality bonds. Much of the momentum behind the recent rise in bond yields has come from technical factors, including quantitative tightening from the Fed and the high level of bond issuance by the US Treasury, in our view. We have not seen an increase in inflation expectations—which would be a more sustainable driver of higher yields—and the 10-year breakeven rate of inflation has remains relatively steady. It currently stands at 2.31%, consistent with the Fed hitting its 2% target.

The next focus for investors will be the release of the September Consumer Price index on Wednesday. Another top Fed official, Michael Barr, expressed optimism that the central bank had made "significant progress" on "bringing inflation toward the direction we want." Despite data on Friday showing double the pace of employment growth economists had expected for September, Barr said that supply and demand factors were coming "into better balance."

So, recent developments support our view that yields should move lower over the coming 6–12 months. Against this backdrop, we are most preferred on fixed income. We recommend investors consider buying high-quality bonds in the 5–10-year maturity range. We foresee further cooling in inflation and slower global growth. Our 12-month forecast for the 10-year US Treasury yield is 3.5% in a base case, 4% in an upside scenario, and 2.75% in a downside scenario, which includes a US recession.

Caught our attention

Potential offshore default in China's property sector. China's largest private property developer, Country Garden, warned on 10 October that it may not meet a number of upcoming payments on offshore debt. Citing its highest operational priority as speeding up the completion of unfinished apartments, the news reflects the wider challenges for China's property sector. Developers face liquidity challenges, as property sales have yet to recover following several property easing announcements. Property fixed asset investment fell 8.8% year-over-year in August, suggesting it remains a drag on Chinese growth. And while measures like reduced downpayments, easing of purchase restrictions on tier-1 cities, and permitting mortgage refinancing should eventually stabilize the sector's activity, Beijing's selective stance reflects a desire to support homeowners rather than prop up developers with weaker balance sheets or operating models.

Our view: Without taking a view on individual companies, we remain very selective on Asian high yield debt, as China's property sector developments suggest lengthy restructuring processes and ongoing negative sentiment—even if Chinese property accounts for only 5% of the index (JPMorgan JACI). Beyond the property sector, we retain a most preferred view on Chinese equities in our Asia strategy. Announced and anticipated policy easing should boost consumption in particular, stabilizing China's overall economic activity and setting the stage for brighter earnings prospects through year-end. We favor a barbell strategy of cyclical growth beneficiaries in the internet, consumer, materials, and industrials sectors, and exposure to defensive sectors, high dividend yields, and resilient cash flows for protection against the current market volatility. We stay most preferred on emerging market equities in our global strategy. For investors looking beyond China, we like EM Asian markets, particularly India and Indonesia.

Key market data

10.10.2023	Current (*)	1D	5D	1M	YTD
		Percent change. For volatility indices, net change in points. For yields, net change in bps			
VIX Index	17.7	-0	-2	+4	-4
MOVE Index	127	-4	-1	+22	+5
S&P 500	4336	+0.6%	+1.1%	-2.7%	+12.9%
Euro Stoxx 600	450	+1.3%	+2.0%	-1.1%	+5.8%
Shanghai Composite	3075	-0.7%	-1.3%	-1.3%	-0.5%
US 10-year Treasury	4.67	-13	-12	+41	+80
US 2-year Treasury	4.99	-9	-16	+0	+57
Germany's 10-year Bund	2.78	+1	-18	+17	+22
Germany's 2-year Bund	3.06	+3	-14	-1	+32
EURUSD	1.057	-0.0%	+0.9%	-1.7%	-1.3%
EURCHF	0.957	+0.1%	-0.7%	-0.1%	-3.2%
Brent crude, USD/bbl	88	-0.5%	-3.6%	-3.3%	+2.1%
Gold, USD/oz	1856	+0.3%	+1.7%	-3.6%	+1.6%

(*) or last close if not available

Source: Bloomberg, UBS, as of 10 October 2023.

Appendix

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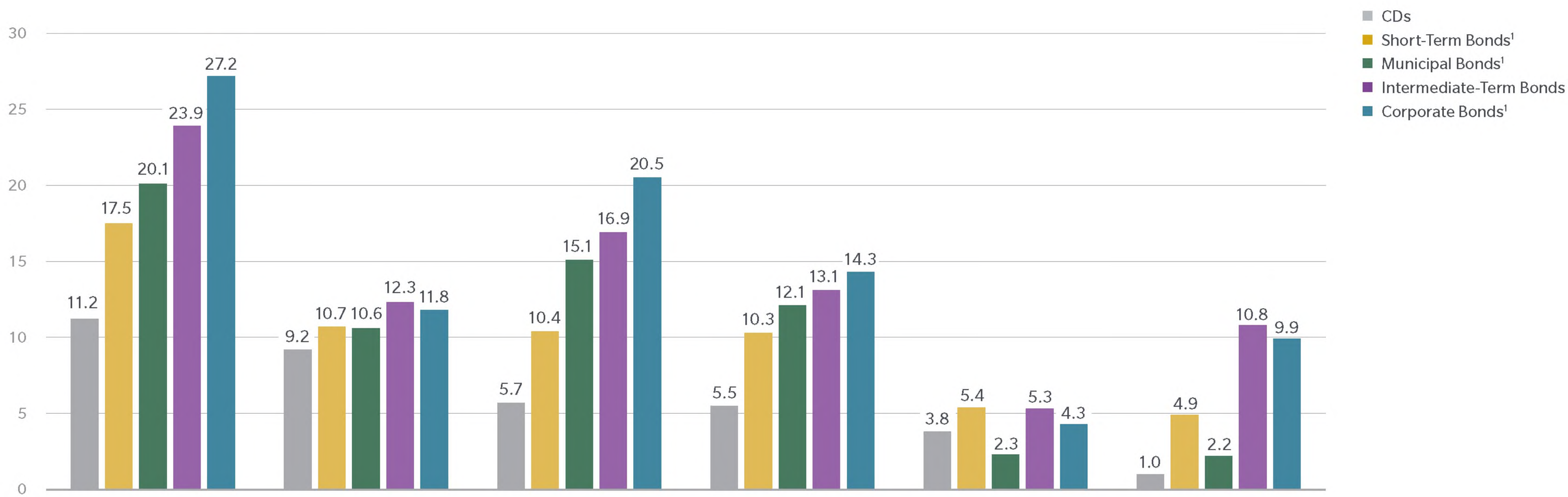
MARKET SNAPSHOT

CDs: Opportunity or Potential Opportunity Lost?

As the US Federal Reserve began raising interest rates, many investors began investing in certificates of deposit (CDs) due to the higher relative yields being offered and also due to heightened concerns about the volatility in the bond markets. With the Fed close to ending their interest rate tightening cycle we believe it may benefit investors to add exposure to bond funds. Over the last 40 years, CD rates peaked near or at the end of the last six Fed tightening cycles. Historically, in the twelve months after CD rates peaked (dates shown below), indexes representing a diversified mix of short-term bonds, municipal bonds, a diversified mix of intermediate-term bonds and corporate bonds have generally generated stronger total returns than CDs. While bond market volatility may continue, the end of the Fed hiking cycle may provide a backdrop to start allocating maturing CD balances into bond funds exposed to to areas of opportunity within fixed income markets.

Generally, investing in CDs at peak rates has left money on the table

One-year subsequent total return from peak CD rate (%)



1984	1989	1995	2000	2007	2019	Peak Year
11.24%	9.21%	5.69%	5.52%	3.79%	1.00%	**CD Peak Rate**
8/01/84 – 7/31/85	4/1/89–3/31/90	2/1/95–1/31/96	6/1/00–5/31/01	9/1/06–8/31/07	5/1/19–4/30/20	**One-year period after peak CD rate**

It may be time to consider adding credit and duration exposure to help drive long-term value.

[1] Short-Term Bonds, Municipal Bonds, Intermediate-Term Bonds, and Corporate Bonds are represented by the Bloomberg 1-3 Year U.S. Government/Credit Bond Index, the Bloomberg Municipal Bond Index, the Bloomberg US Aggregate Bond Index and the Bloomberg US Corporate Bond Index, respectively. See the reverse side for additional information.

Source: CD rates from Bankrate.com. CD rate dates are from month that 1-year national average CD rates peaked. For CD return, money was invested at the peak 1-year CD rate for that period. Please see the back page for index definitions.

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Opportunity Costs

While CDs generally have offered more stability, that stability may come with a cost. As demonstrated in the chart below, bond funds have generally delivered more growth (green boxes) than CDs during the periods highlighted below. Moreover, very few investors can successfully time the market, and waiting for the right time has historically meant missing the best days of a market rebound. The opportunity cost can be substantial over time.

Growth Opportunity with initial $100,000 investment[2] when investing at peak CD rates

outperformed CDs   underperformed CDs

CDs	$ 111,240	$ 109,210	$ 105,690	$ 105,520	$103,790	$ 101,000
Short-Term Bonds	$117,502	$110,663	$110,394	$110,314	$105,418	$104,944
Municipal Bonds	$120,083	$110,552	$115,053	$112,143	$102,298	$102,162
Intermediate-Term Bonds	$123,913	$112,339	$116,945	$113,115	$105,261	$110,842
Corporate Bond	$127,248	$111,753	$120,480	$114,293	$104,321	$109,884
Performance Dates	8/1/84–7/31/85	4/1/89-3/31/90	2/1/95–1/31/96	6/1/00–5/31/01	9/1/06–8/31/07	5/1/19–4/30/20

Source: CD rates from Bankrate.com. CD rate dates are from same month that 1-year national average CD rates peaked. For CD return, money was invested at the peak 1-year CD rate for that period. All other data from Morningstar Direct.

[2] Growth Opportunity represents the index total returns, reinvesting all income and capital gains distributions. Green boxes in table depict time periods where the category outperformed the CD total return and red boxes depict underperformance.

 CDs are FDIC insured and have principal and interest guarantees but offer no opportunity for growth of capital or income. The principal value and return of an investment in mutual funds will fluctuate with changes in market conditions. Bonds generally offer higher income than either CDs or money market funds.

Index Definitions: Short-term Bonds: Bloomberg 1-3 Year U.S. Government/Credit Bond Index - measures the performance of the short-term (1 to 3 years) investment-grade corporate and U.S. government bond markets. **Municipal Bonds:** Bloomberg Municipal Bond Index - measures the performance of the tax-exempt bond market. **Intermediate-Term Bonds:** Bloomberg U.S. Aggregate Bond Index - measures the performance of the U.S. investment grade, fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities with at least one year to final maturity. **Corporate Bonds:** Bloomberg US Corporate Bond Index - measures the investment grade, fixed-rate, taxable corporate bond market.

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Important Risk Considerations: Investments in debt instruments may decline in value as the result of, or perception of, declines in the credit quality of the issuer, borrower, counterparty, or other entity responsible for payment, underlying collateral, or changes in economic, political, issuer-specific, or other conditions. Certain types of debt instruments can be more sensitive to these factors and therefore more volatile. In addition, debt instruments entail interest rate risk (as interest rates rise, prices usually fall). Therefore, the portfolio's value may decline during rising rates. Portfolios that consist of debt instruments with longer durations are generally more sensitive to a rise in interest rates than those with shorter durations. At times, and particularly during periods of market turmoil, all or a large portion of segments of the market may not have an active trading market. As a result, it may be difficult to value these investments and it may not be possible to sell a particular investment or type of investment at any particular time or at an acceptable price. The price of an instrument trading at a negative interest rate responds to interest rate changes like other debt instruments; however, an instrument purchased at a negative interest rate is expected to produce a negative return if held to maturity.

Keep in mind that all investments, including mutual funds, carry a certain amount of risk including the possible loss of the principal amount invested.

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