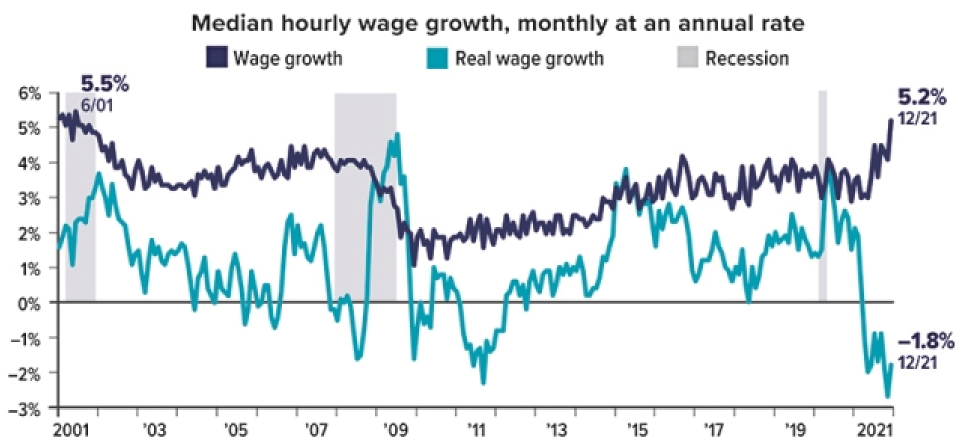
Farmers Trust Company

John D. Stewart, CFA
Chief Investment Officer
Farmers Trust Company
42 McClurg Rd
Boardman, OH 44512
330-743-7000
stewartj@Farmerstrustco.com
farmerstrustco.com

Be sure to read John Stewart's article, "Commodities Go Wild On Russian Escalation" below.

Inflation Cuts into Wage Gains

Driven by labor shortages, median hourly wages increased at an annual rate of 5.2% in December 2021, the highest level since June 2001. However, inflation cuts into buying power, and *real wages* — adjusted for inflation — actually dropped as inflation spiked in 2021. By contrast, negative inflation (deflation) during the Great Recession sent real wages skyrocketing temporarily even as non-adjusted wage growth declined.



Sources: Federal Reserve Bank of Atlanta, 2022, and U.S. Bureau of Labor Statistics, 2022, data 1/2001 to 12/2021. (Wage growth is calculated by comparing the median percentage change in wages reported by individuals 12 months apart; real wage growth is calculated by subtracting CPI-U inflation from wage growth.)

Commodities Go Wild

Last month, Russian posturing was keeping stocks on edge while sending energy prices higher. In the past couple of weeks we've seen the Russian invasion of Ukraine send those same dynamics into overdrive. In two-and-a-half weeks, oil soared roughly 40%, briefly touching $130/barrel, a level not seen since 2008, before it eased back toward $100 on hopes of more supply coming from OPEC nations as well as increased efforts to bring forward domestic supplies. Many other commodities have also risen dramatically in price. Gold recaptured $2,000/ounce for the first time since 2020, and nickel prices soared 90% in just one day earlier this month. Despite, or perhaps because of, the obvious inflationary pressures, wage growth has stalled and surveys of business activity have shown a cooling of demand and economic growth.

Looking ahead, the most important question to answer is whether the Federal Reserve will allow higher prices for longer in order to protect growth, or if they will be more aggressive in combating inflation at the expense of growth, which will have implications for the future path of commodity prices in addition to all financial markets. We'll get some color on the answer to that question this week when the Fed meets. It seems that we're always looking ahead to find out what the Fed is going to do or say. Perhaps that's because they've engrained themselves so deeply into the functioning of financial markets. Like it or not, that's the world we live in. Given that we are currently seeing evidence of stagflation (rising inflation and slowing growth), the Fed will need to thread the needle to convince the market it can handle the inflation problem without undermining the economy and risking further damage to the stock market.

When buying financial assets, most people think only of the return they expect to achieve by holding the investment for a certain period of time. Some people take the next step and try to quantify the potential risk of the investment. Fewer still actually have a plan for how they will exit an investment if things don't go according to plan. When we make decisions, we have to ask ourselves how reversible they are. "If I am wrong, how easily can I get out of it?" Some investors may have decided to take a shot and purchase shares in one of several publicly traded Russian stock index funds. That obviously wasn't prudent given the massive price drop in Russian stocks due to sanctions placed on the Russian economy. To add insult to injury, those funds have now stopped trading completely, and investors have no ability to exit those positions at any price and with no expectation of when, if ever, they may be able to unwind those investments. This is obviously an extreme example; unprecedented in many ways. Nevertheless, there are a lot of investments lurking around out there that have certain liquidity constraints, making it difficult for investors to get out when they want to get their money back, regardless of whether the investment is at a profit or a loss. Do your homework, and understand how easy it is to liquidate an investment before you jump in.

Key Retirement and Tax Numbers for 2022

Every year, the Internal Revenue Service announces cost-of-living adjustments that affect contribution limits for retirement plans and various tax deduction, exclusion, exemption, and threshold amounts. Here are a few of the key adjustments for 2022.

Estate, Gift, and Generation-Skipping Transfer Tax

- The annual gift tax exclusion (and annual generation-skipping transfer tax exclusion) for 2022 is $16,000, up from $15,000 in 2021.
- The gift and estate tax basic exclusion amount (and generation-skipping transfer tax exemption) for 2022 is $12,060,000, up from $11,700,000 in 2021.

Standard Deduction

Taxpayers can generally choose to itemize certain deductions or claim a standard deduction on their federal income tax returns. In 2022, the standard deduction is:

- $12,950 (up from $12,550 in 2021) for single filers or married individuals filing separate returns
- $25,900 (up from $25,100 in 2021) for married joint filers
- $19,400 (up from $18,800 in 2021) for heads of household

The additional standard deduction amount for the blind and those age 65 or older in 2022 is:

- $1,750 (up from $1,700 in 2021) for single filers and heads of household
- $1,400 (up from $1,350 in 2021) for all other filing statuses

Special rules apply for those who can be claimed as a dependent by another taxpayer.

IRAs

The combined annual limit on contributions to traditional and Roth IRAs is $6,000 in 2022 (the same as in 2021), with individuals age 50 or older able to contribute an additional $1,000. The limit on contributions to a Roth IRA phases out for certain modified adjusted gross income (MAGI) ranges *(see chart).* For individuals who are covered by a workplace retirement plan, the deduction for contributions to a traditional IRA also phases out for certain MAGI ranges *(see chart).* The limit on nondeductible contributions to a traditional IRA is not subject to phaseout based on MAGI.

MAGI Ranges: Contributions to a Roth IRA

	2021	2022
Single/Head of household	$125,000–$140,000	$129,000–$144,000
Married filing jointly	$198,000–$208,000	$204,000–$214,000
Married filing separately	$0–$10,000	$0–$10,000

MAGI Ranges: Deductible Contributions to a Traditional IRA

	2021	2022
Single/Head of household	$66,000–$76,000	$68,000–$78,000
Married filing jointly	$105,000–$125,000	$109,000–$129,000

Note: *The 2022 phaseout range is $204,000–$214,000 (up from $198,000–$208,000 in 2021) when the individual making the IRA contribution is not covered by a workplace retirement plan but is filing jointly with a spouse who is covered. The phaseout range is $0–$10,000 when the individual is married filing separately and either spouse is covered by a workplace plan.*

Employer Retirement Plans

- Employees who participate in 401(k), 403(b), and most 457 plans can defer up to $20,500 in compensation in 2022 (up from $19,500 in 2021); employees age 50 or older can defer up to an additional $6,500 in 2022 (the same as in 2021).
- Employees participating in a SIMPLE retirement plan can defer up to $14,000 in 2022 (up from $13,500 in 2021), and employees age 50 or older can defer up to an additional $3,000 in 2022 (the same as in 2021).

Kiddie Tax: Child's Unearned Income

Under the kiddie tax, a child's unearned income above $2,300 in 2022 (up from $2,200 in 2021) is taxed using the parents' tax rates.

Splurge or Save? Making the Most of Your Income Tax Refund

The IRS issued more than 128 million income tax refunds for the 2020 filing season, putting $355.3 billion into the hands of U.S. consumers.[1] For most recipients, such a sudden influx of cash prompts an important question: What's the best way to use the money?

Last year, 27% of consumers said they planned to spend their refund on everyday expenses, whereas equal numbers (8%) planned to either "splurge" or take a vacation.[2] But what about your other options?

Debt Decisions

Though spending your tax refund is tempting, most people surveyed said they planned to save their tax refund and/or pay down debt.[3] While reducing debt can be the cornerstone of an effective financial strategy, it's essential to avoid making choices that could set you back in the long run. For example, a home mortgage is often the largest debt taxpayers carry, and making extra mortgage payments can reduce your principal balance and shorten the term of the loan, allowing you to accumulate equity faster.

However, using a refund to cut down mortgage debt ahead of schedule could have counterproductive consequences, including losing the ability to claim the home mortgage interest deduction when filing your income taxes. In addition, the reduction in your overall liquidity may limit your ability to make new purchases or investments that you hadn't anticipated.

With that in mind, it may be better to pay off higher-interest, nondeductible debt first, such as credit-card bills and car loans. Although that strategy may still limit your potential to pursue additional financial opportunities in the short term, your long-term savings may be significant.

Retirement Readiness

Using your refund to potentially bring retirement goals closer to reality might be prudent. IRA contributions (up to $6,000 in 2022; $7,000 if age 50 or older) may be deductible, depending on your income and the type of IRA you choose. The 2022 cap on contributions to 401(k) and 403(b) workplace retirement plans is $20,500 ($27,000 if age 50 or older). If you aren't yet contributing the maximum, using this year's refund to finance some routine household expenses could help you allocate more of your income to a workplace retirement account. As an added potential benefit, the amount of any matching employer contributions may increase as a result.

Of course, you might want to use this year's refund for another purpose. Be sure to speak with your financial professional for guidance about the best way to proceed. There is no assurance that working with a financial professional will improve investment results.

1) Internal Revenue Service, 2021

2-3) National Retail Federation, 2021