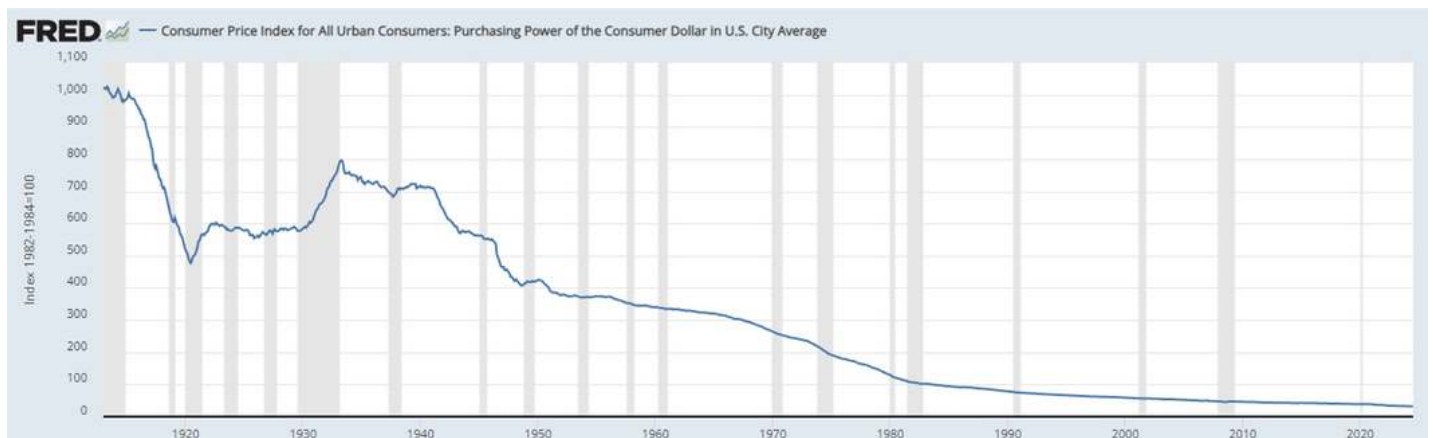


How Inflation Affects Your Stock Market Returns

“Someone is sitting in the shade of a tree today because someone planted a tree a long time ago.” -Warren Buffet

A Look at Recent Inflation Data



It is no question that Americans have seen consistent erosion in their purchasing power over the past 4 years. The Consumer Price Index is designed to track households' out-of-pocket expenses to form a basis for cost-of-living adjustments. Since February 2020, The Consumer Price Index has increased 20.9%, with even higher increases in specific sectors. For example, food and energy are up 25.2% and 30.4%, respectively. The below chart shows how drastically inflation has eroded the value of the dollar.

Thankfully, inflation has been increasing at a slower rate. In July 2024, the Bureau of Labor Statistics reported that inflation rose 2.9% on an annual basis. That is lower than the 3% yearly price increase recorded in June, and the slowest pace of inflation recorded since March 2021.

Stock Market Performance During Inflationary Times

A popular opinion is that high inflation equals poor stock market performance. However, when you look back over the past 74 years the data does not reflect that opinion. As you see in the chart below, the 10 best annual returns and the 10 worst annual returns have similar inflation rates. There has been a lot of research done on what type of stocks perform better in periods of high inflation. To keep it simple, let's focus on growth vs value stocks. Value stocks have strong current cash flows and are more likely to grow slowly or diminish over time, while growth stocks represent

fast-growing companies that may not be profitable at the current moment. We could use the discounted cash flow formula to see that growth stocks perform worse in periods of higher interest rates (rising interest rates are typically associated with higher inflation).

NORTHWESTERN MUTUAL WEALTH MANAGEMENT COMPANY

INFLATION AND STOCK MARKET RETURNS

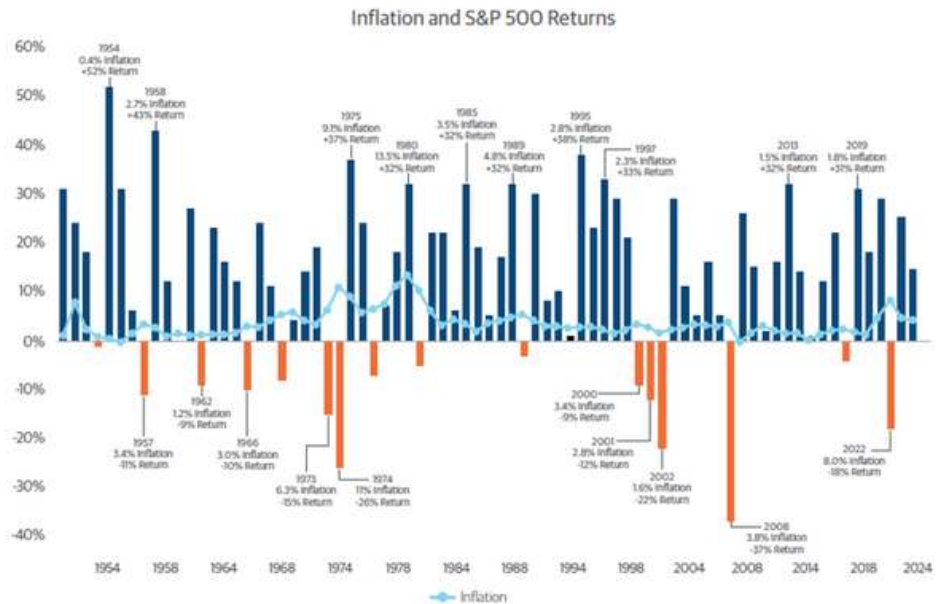
A common misconception is that inflation leads to lower stock market returns.

INFLATION PERCEPTIONS

Since 1950, the average inflation rate has been 3.5%. While periods of rising inflation can lead to lower stock market returns, when looking at stock market performance, the 10 best- and worst-performing stock market years had an almost identical inflation rate.

Average Inflation and 10 Best and Worst S&P 500 Returns Since 1950

10 Best Annual Returns	36%
Inflation	4.2%
10 Worst Annual Returns	-1.7%
Average Inflation	4.4%

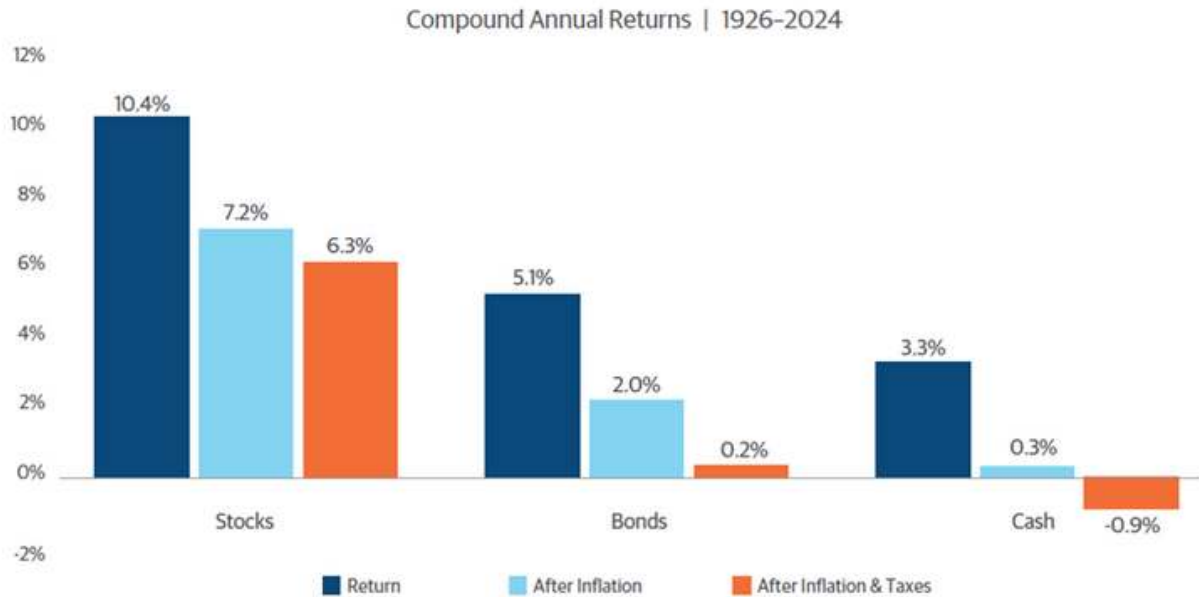


S&P 500 Total Return data is from Morningstar Direct. CPI data is from the Federal Reserve. Data is from 1950 - 6/30/24. The chart is for illustrative purposes only and not intended as a recommendation. Past performance is not a guarantee of future results. All investments carry risk, including potential loss of principal, and no investment strategy can guarantee a profit or completely protect against loss. Indexes are unmanaged and cannot be invested in directly.

When you look at annual portfolio returns after inflation and taxes the numbers show that stocks are the best solution for the typical investor. Of course, there are years when equities may not be the best solution, but when investing over the long-term stocks are difficult to beat.

INFLATION AND TAXES REDUCE RETURNS

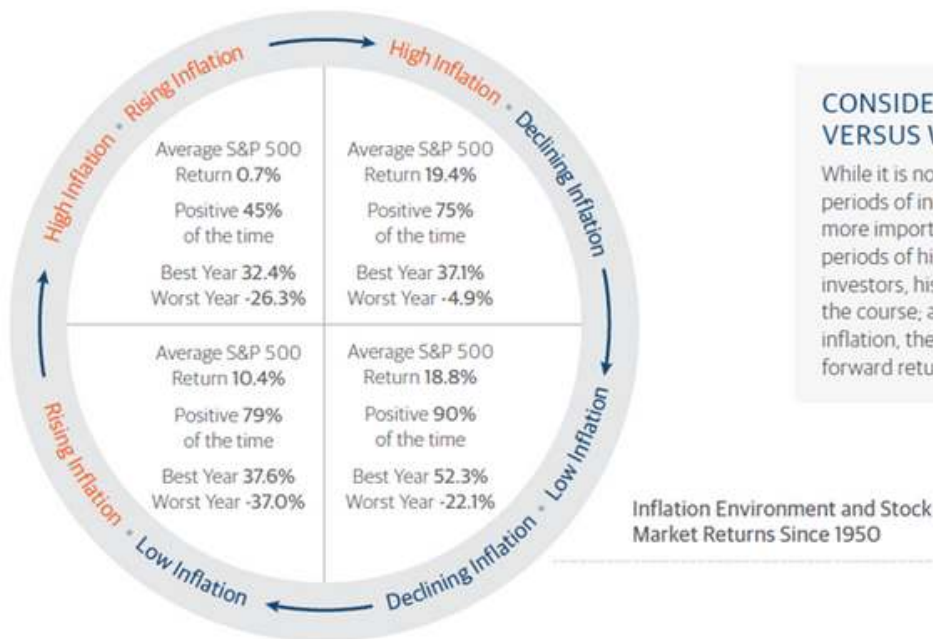
Pairing a diversified portfolio with a comprehensive financial plan can help minimize the adverse effects of inflation and taxes on your future goals.



Stocks are represented by the Ibbotson® Large Company Stock Index. Government bonds are represented by the 20-year U.S. government bond, cash by the 30-day U.S. Treasury bill, and inflation by the Consumer Price Index. The data assumes reinvestment of income and does not account for transaction costs. Federal income tax is calculated using the midpoint between the highest and lowest marginal income tax rates for each tax year since 1926, a 36.2% tax rate. Dividend tax rate is the average dividend tax rate since 1926, a 24.6% tax rate. For stocks it is assumed that all income is dividend income and is taxed as qualified dividends at the dividend tax rate. All income from bonds and cash is taxed at federal income tax rates. All data from Morningstar Direct. Data through 5/31/2024.

Phases of Inflation

When you look at annual portfolio returns after inflation and taxes the numbers show that stocks are the best solution for the typical investor. Of course, there are years when equities may not be the best solution, but when investing over the long-term stocks are difficult to beat.



CONSIDER WHERE WE ARE GOING VERSUS WHERE WE ARE

While it is not unusual for volatility to accompany periods of inflation, often where inflation is headed is more important than where it currently stands. While periods of high, rising inflation can be challenging for investors, history shows that it's important to stay the course; as rising inflation gives way to declining inflation, the stock market often has seen attractive forward returns.

Inflation Environment and Stock Market Returns Since 1950

High inflation is defined as 5% or greater annual CPI. Rising inflation is defined as the annual CPI rate being higher than the previous calendar year. Declining inflation is defined as the annual CPI rate being lower than the previous calendar year. The chart is for illustrative purposes only and not intended as a recommendation. Past performance is not a guarantee of future results. All investments carry risk, including potential loss of principal, and no investment strategy can guarantee a profit or completely protect against loss. Indexes are unmanaged and cannot be invested in directly.

In Summary

Navigating the relationship between inflation and stock market returns requires a nuanced understanding of economic cycles and market behavior. Despite common beliefs, high inflation does not always correlate with poor stock performance. Historical data shows that while inflation impacts various sectors differently, certain stocks and sectors can thrive even in elevated inflation environments.

Investors should be aware that the overall performance of stocks relative to inflation remains robust over the long term. As inflation rates fluctuate, investors must stay disciplined, patient, and understand their time horizon. A recent-college graduate can be less worried about how inflation will affect their annual portfolio returns, however someone approaching retirement will want to be more risk averse as they near the distribution phase of their life. At Patterson Andrews, we manage our client's risk by correlating the amount of dollars they have in fixed income with their projected annual retirement expenses. We have found this is a great way to set our clients up for success in retirement.

The opinions expressed are those of Patterson Andrews Wealth Management as of the date stated on this commentary and are subject to change. There is no guarantee that any forecasts made will come to pass. This material does not constitute investment advice and is not intended as an endorsement of any specific investment or security. Please remember that all investments carry some level of risk, including the potential loss of principal invested. Indexes and/or benchmarks are unmanaged and cannot be invested in directly. Returns represent past performance, are not a guarantee of future performance and are not indicative of any specific investment. Diversification and strategic asset allocation do not assure profit or protect against loss. Charles R Andrews, David B Miller and Wesley J Patterson, use Patterson Andrews Wealth Management as a marketing name for doing business as representatives of Northwestern Mutual. Northwestern Mutual Private Client Group is a select group of NM advisors and representatives. Patterson Andrews Wealth Management and Northwestern Mutual Private Client Group are not a registered investment adviser, broker-dealer, insurance agency, federal savings bank or other legal entity. Northwestern Mutual is the marketing name for The Northwestern Mutual Life Insurance Company, Milwaukee, WI (NM) and its subsidiaries. Investment advisory services as Advisors of Northwestern Mutual Wealth Management Company® (NMWMC), Milwaukee, WI, a subsidiary of NM and federal savings bank. Insurance Agents of NM and Northwestern Long Term Care Insurance Company, Milwaukee, WI. Investment brokerage services as Registered Representatives of **Northwestern Mutual Investment Services**, LLC (NMIS), a subsidiary of NM, registered investment adviser, broker-dealer and member FINRA (finra.org) and SIPC (sipc.org).