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SECOND QUARTER | 2022

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Current Outlook & Portfolio Strategy

Ian N. Breusch, CFA
Chief Operating Officer

Much has transpired across the world during the first few months of the new year. Just as global economies were moving toward normalcy as the Omicron variant began to fade, geopolitics took center stage. Russia invaded Ukraine on Feb. 24, creating a humanitarian crisis on a scale not seen in Europe since World War II. The war has caused several hundred global corporations to withdraw from Russia. NATO members have imposed significant economic sanctions against Russia, exacerbating inflationary concerns, particularly across energy and grain markets where Russia is a key contributor. This turmoil has certainly impacted volatility across capital markets, which is likely to continue until a peaceful solution is established.

Geopolitics aside, we entered 2022 with other economic concerns already at the fore. Year-over-year inflation readings were at a 40-year high before the Russia/Ukraine conflict began. To combat inflationary pressure, the Federal Reserve Board has been tapering its bond purchases for several months, while signaling that interest-rate increases would follow. On March 16, the Fed raised the Federal Funds rate for the first time since the beginning of the COVID-19 pandemic. Additionally, much of the fiscal stimulus discussed by Congress last year has been sidelined due to inflationary concerns expressed by both political parties. More restrictive (less accommodative) monetary and fiscal policies are designed to reduce the pace of price increases and the corresponding erosion of purchasing power. To be clear, most economists believe inflation of approximately 2% per year is both sustainable and healthy for our economy. However, most economists also believe that our current level of inflation (7%-8%) is damaging – particularly to lower-income consumers.

The Fed certainly has the tools to curb inflation. A steady increase in the Federal Funds rate is one such tool. Following the most recent Fed meeting, we expect another six rate increases between this year and next. Interestingly, the rest of the Treasury yield curve began adjusting to the likelihood of higher rates months ago. Longer-term interest rates have already risen substantially, and corresponding bond prices have fallen. If the Fed decides to be even more aggressive, it can sell fixed-income assets from its own balance sheet, which would also depress bond prices, increase yields, and dampen lending markets and inflationary pressures. A successful tightening cycle will be characterized by higher interest rates, lower inflation, and sustained consumer spending and economic growth. The correct mix, scale, and timing of Fed policy decisions is key to this success and is a hotly debated topic among economists for good reason.

Despite the above-mentioned risks, there is much to be optimistic about. Although stock markets tend to be more volatile when interest rate policy is changing, stocks tend to perform rather well when interest rates are rising, as investors initially view rising rates as symptoms of a healthy economy. However, valuation certainly matters more when rates are rising, which is why it's important to be a discriminate investor. Despite the near-term risks presented by inflation and geopolitical conflict, our economy remains healthy overall. While we continue to believe that value/dividend-paying companies offer slightly better forward return prospects than many of their growth counterparts, a mix of both is important in a well-rounded portfolio. For clients desiring fixed income (bonds) to reduce risk, we continue to favor high-quality shorter maturity bonds as interest rates move higher. As always, our focus will remain on sourcing and managing high-quality investments for our clients, with valuation being at the forefront of investment decision making.

Gold's Role as a Hedge Still Stands

Edwin C. Ciskowski, CPA
Senior Portfolio Manager

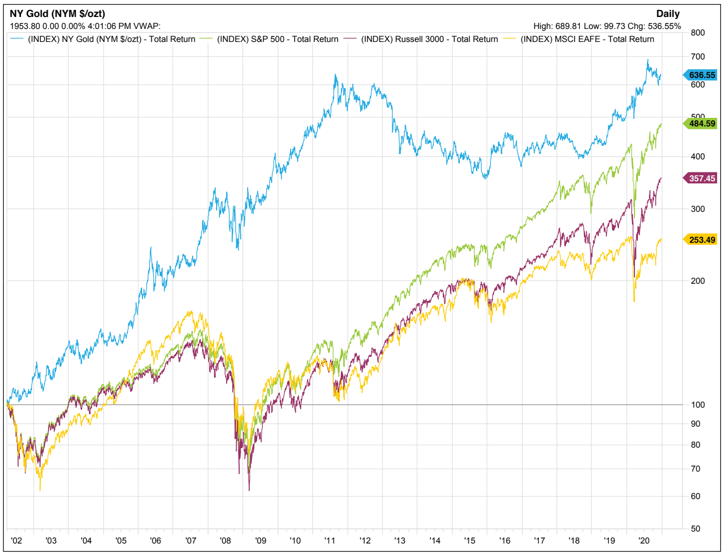
"Gold is money, everything else is credit," legendary banker and financier John Pierpont Morgan is reported to have said in 1912 when asked about the difference between paper money and the metal. In a mere seven words, J.P. Morgan captured the essence of money. Since that time, gold's function has morphed into an investible asset class with respectable long-term performance. As the following chart shows, gold's value has risen faster than prominent stock indices the past 20 years.

In fact, since 1971, when the gold standard effectively ended, gold has appreciated approximately 8.3% per year. A 2019 Willis Towers Watson pension study found that on a risk-adjusted basis, owning gold slightly adds alpha to any portfolio.

So, gold is money, it generates long-term returns, it improves portfolio performance, it's generally negatively correlated to stocks during times of stress, it's a hedge against inflation and depreciating currencies and it provides liquidity on a global basis with no credit risk. This makes gold a unique "asset." How? Why? Principally, it's a function of scarcity. Unlike fiat currencies, gold can't be printed in unlimited quantities. Whatever is in the ground is the total available market (TAM). In the last 20 years, production has increased about 1.5% per year, and all the gold known to exist would fill approximately two-and-a-half Olympic-sized swimming pools. Based on recent above-ground estimates, about 47% of known gold is held as jewelry, 20% is bars and coins, 17% is held by central banks, and the remaining 15% is held by ETFs, or others.

Gold is a hedge against depreciating currencies. We don't advocate buying gold to try to outperform stocks. Rather, it should be owned if you think currencies will continue to decline in value due to the printing of money and inflation. When we note gold has appreciated 8.3% per year, that's another way of saying how much currencies have been debased.

So, what's the downside to owning gold? There's an adage in the metals markets that says, "if you don't hold gold, you don't own gold." Hold is an operative word. We can own gold several ways, but do we hold



it? Many investors buy gold ETFs to "own" their gold, but in reading the fine print of the prospectus, it makes clear some of the ETFs own futures contracts on gold or have borrowed the gold from large owners of bullion and must keep proper daily accounting of the amounts borrowed and repaid. The investor in those ETFs has no claim on actual gold. Here, the ETFs serve more as a trading vehicle than a depository.

Second, you could buy specifically allocated amounts of gold and hold it at mints (e.g., U.S., Canada, Australia). While this is an improved form of ownership (specifically allocated serial numbers of gold bars), you are depending on the mints to hold your *gold under all circumstances.* Lastly, you could own gold physically.

Bottom line, gold is money and a unique asset. Like many unique assets (e.g., cryptocurrencies), it's something best owned outside your Trust Company account due to the limitations associated with holding it. The same basic notions apply to silver, platinum, copper, etc.

Housing: Can the Boom Continue?

Craig J. Holston
Senior Portfolio Manager

2021 was an incredible year for the U.S. housing market by many measures. The National Association of Realtors (NAR) reported that sales of existing homes increased 8.5% to a 15-year high of 6.12 million. Low interest rates and widespread remote work were major factors driving last year's sales streak. Housing prices hit an all-time record with existing homes selling for a median price of $346,900 in 2021.

As we look at the current state of the housing market, lack of supply is the major factor that has led to a slowdown in sales so far in 2022. In February, existing home sales fell to an annual rate of 6.02 million, which was down 7.2% from January and 2.4% from one year ago. Because the current inventory of unsold homes is equivalent to only 1.7 months' supply, it is no surprise that home prices continue to rise. The NAR also recently reported that year-over-year prices have increased for 120 consecutive months, which is the longest-running streak on record.

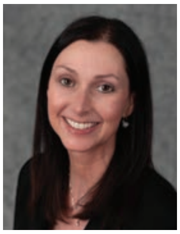
When we hear these astonishing housing statistics, it would be reasonable to ask if these are signs of another housing and lending bubble like we experienced 12 years ago? Our short answer is no, we don't think so. The data is pretty clear to us that housing is experiencing the same supply and demand imbalances that are pushing up costs for goods like gasoline, meat, wheat, butter, lumber, coffee beans, and copper. Too many buyers have been chasing too few homes on the market. But, in the case of housing, it looks to us like those imbalances are correcting, and price increases are starting to revert to normal.

The chart above shows the amount of new homebuilding that occurred since the late 1950s. As you can see, the level of new building has peaked and troughed many times in the past. But fix your eyes toward the right side of the chart, to the period between 2006 and 2011. Builders were erecting more than 2.2 million homes a year at the peak, which was far more than our population growth could support back then. That oversupply eventually drove down home prices, which we all know started a chain-reaction of financial failures.

In the aftermath of 2008, home builders went into hiding, and construction levels dropped by 80% in the following years. This created a shortage of homes, since our population kept increasing. Keep in mind, builders need to erect probably 1.2 - 1.4 million new homes a year just to keep up with population growth. They didn't hit that figure for six years in a row, causing rising shortages. That fed the first wave of house price increases this past decade. We should also point out that since the housing crisis passed, mortgage lending has remained very conservative by historical standards. Prices are not escalating today due to loose lending. No longer are banks financing second and third properties with less than 5% down payment as they did prior to the Great Recession, and the market for buying and selling packages of mortgages has since been much more regulated.

Despite slightly higher mortgage rates, underlying conditions remain very favorable for housing, and that tells us there seems to be no bubble on the horizon.

The Importance of Managing Valuable Digital Assets



Megan M. Marquardt, CFP®, CTFA
Wealth Services

Earlier in my career, I encountered a woman named "Jane" who passed away suddenly. Her trust company ran into numerous complications that could have been avoided with proper and simple planning. The home where she was living was owned by an Irrevocable Trust and the trust company was serving as trustee. Their first challenge was disarming the ADT security system. You see, the ADT account was in her deceased father's name, and they did not have a pin number or password. After attempts to enter the home, and multiple visits by the Sheriff's Department, they finally were able to properly arm and disarm the property. The problems continued as they tried to cancel Amazon orders of perishable foods that continued to be delivered to the home. Family and friends requested photos that were on Jane's Shutterfly account. Also, Jane had not executed a valid will, so there were delays in determining who had legal rights to access these accounts and many other digital assets.

'Digital assets' can include social media, digital photos and videos, smart phone applications and data stored on those applications, cryptocurrency, domain names for a website, bank accounts and investment accounts. Although you may not care what happens to these assets after you pass, there are numerous problems that can arise if not properly transferred to your heirs.

Privacy issues can also arise. Most websites have strict rules against disclosing personal information to third parties and may require a court order before they will provide a password. This can be extremely frustrating if you are the executor trying to track these assets down. You may now be paying all your bills online, including newspaper and magazine subscriptions, a car loan, or utility bills. Your executor will need access to those websites and passwords to manage and shut off the payments.

To avoid some of these problems, here are a few steps to take:

Make a list of important passwords and online accounts, including email and social media. Keep this list in a safe location and be sure to let family members and your estate planning attorney know how to access the list. If you keep your list in a safe deposit box, be sure to update it on a regular basis. You may consider utilizing a password management app which would allow you to store these passwords in an encrypted database that would be locked by a master password.

Avoid Cybersecurity risks. Some social media platforms will automatically mark a deceased user's profile as 'memorialized,' which alerts cybercriminals to begin scanning the deceased's online accounts for information. Sometimes these assets have substantial monetary value. You might have thousands of dollars of cryptocurrency, or a PayPal balance, or a large library of music that you have paid to download. This can lead to lost music and unclaimed money for your heirs.

Don't rely on the cloud for backup. Download your data to a computer on a regular basis so that your family members or fiduciaries have easy access.

Utilize online tools to designate an individual to access your account after a certain period of inactivity, your incapacity, or your death. Facebook, for example, allows users to designate a Legacy Contact to manage their account after death. The Legacy Contact can post on the user's profile, update cover photos, and request the removal of the account.

Finally, work with your estate planning attorney to include language in your documents that would provide consent to family members and fiduciaries to access this information from providers. This power can be granted via a will, trust or power of attorney per Florida's statue called the Florida Fiduciary Access to Digital Assets Act (FFADAA).

Since most people today manage their lives on a computer or smart phone, it is important to think about these 'assets' when planning.

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