State Farm®

WINTER 2018

mutual funds INVESTOR

As Rates Rise, Bonds Still Pay

Bonds can be a keystone investment, even in a rising-interest-rate environment.

THE FEDERAL RESERVE (FED) RAISED ITS KEY SHORT-TERM INTEREST RATE MULTIPLE TIMES IN 2018, INCLUDING TO 2.5 PERCENT IN DECEMBER, ITS HIGHEST LEVEL IN MORE THAN A DECADE .[1] Most members of the central bank's interest-rate-setting committee expect to raise rates several times in 2019 and 2020.[2] Higher interest rates aren't necessarily bad for fixed-income investors. In fact, with a little planning, investors can benefit from interest rate hikes.

As rates rise, prices fall

Commonly, rising interest rates are viewed as bad for fixed-income investments because of the relationship between interest rates and bond prices: As interest rates rise, the value of existing bonds falls. This is because new bonds issued during a period of higher interest rates offer investors higher yields than do comparable bonds issued when rates were lower. As a result, investors looking to resell their bonds usually have

[1]Federal Reserve Bank of St. Louis Economic Research
https://fred.stlouisfed.org/graph/?g=k4sS

[2]Federal Reserve Economic Projections, June 2018
https://www.federalreserve.gov/monetarypolicy/files/fomcprojtabl20180613.pdf

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How to Contact Us:

VISIT YOUR REGISTERED STATE FARM® AGENT

VISIT STATEFARM.COM® TO:
- View your personal portfolio.
- Obtain current values.
- View transaction history.

Investing involves risk, including potential for loss.

Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained by visiting the prospectus page on statefarm.com (www.statefarm.com/IPS/prospectus). Read it carefully. AP2018/08/0956

Bonds are subject to interest rate risk and may decline in value due to an increase in interest rates.

Not FDIC Insured	No Bank Guarantee
	May Lose Value

to settle for a lower price to help make them attractive enough to compete with the newer, higher-yielding bonds.

But this dynamic doesn't mean investors should forgo bonds entirely. Bonds are an essential component of a well-balanced portfolio because of the steady income they provide and their capability to offset some of the volatility created by a stock portfolio. What's more, interim fluctuations in price don't matter as much if you plan on holding your bond until it matures—you still get the income promised and a return of the principal, barring a default by the issuer. Meanwhile, higher rates generally mean higher yields on new bonds. You will have an opportunity to generate more income from your new investments in bonds.

When interest rates spike

It's possible that rates may rise more quickly than anticipated, particularly if inflation increases rapidly or the economy starts overheating. In those cases, the Fed may need to be more aggressive with its rate increases. This could mean the negative effects from falling prices may be larger than the benefits from higher yields.

If you are worried this might happen, there are strategies to help protect your portfolio. One of them is increasing your exposure to shorter-duration bonds. Generally, short-term bonds are less sensitive to interest-rate changes than bonds with longer durations. This is because investors can reinvest their principal more frequently to help take advantage of higher yields.

Also, investing in bond funds rather than individual bonds may provide flexibility for investors worried about the effects of rising rates. Bond funds offer greater diversification than individual bonds and are easier to sell if you need to withdraw your money on short notice. Typically, for investment-grade corporate bonds, bond funds distribute income monthly rather than every six months, allowing you to more regularly reinvest income into higher-yielding securities if interest rates spike.

Treasury Inflation-Protected Securities (TIPS) are another option to consider. The face value of TIPS adjusts in line with inflation, which helps protect the bond's value in a rising rate environment. The higher principal value maintains attractive interest payments, even in the face of higher yields offered on newly issued bonds.

Also, maintaining a significant share of your portfolio invested in bonds and other fixed-income instruments may be a boon when the market enters the next recession. For instance, during the market downturn that accompanied the 2008 financial crisis, large-cap stocks fell 37 percent, while intermediate-term government bonds gained 13 percent.[3] That kind of strong performance in the face of a declining stock market is part of what makes bonds valuable in any investor's portfolio.

If you have questions, contact a registered State Farm agent.

[3]2015 Ibbotson SBBI Classic Yearbook (Large-cap stock returns based on the S&P 500 Index.)

HOW COMPOUND INTEREST AFFECTS DEBT

As of early 2018, Americans held more than $13 trillion in total debt—a record.[1] If you have multiple balances to whittle down, understanding **the long-term impact of compound interest** can help you put **the best repayment plan** in place.

HOUSEHOLD DEBT	2013–2018 % INCREASE
HOUSING	11%
STUDENT	40%
AUTO	50%
CREDIT CARD	14%
OTHER	33%

OVER THE PAST FIVE YEARS, AMERICAN HOUSEHOLD DEBT HAS RISEN.

Debt figures from the New York Federal Reserve[1]

Over time, the interest you owe on the debt you hold generates interest of its own, called **compound interest.** This increases the cost of your debt. **Making extra principal payments, if possible, can improve your bottom line.**

What you might owe depends on two factors:

1. LOAN DURATION
2. INTEREST RATE

The longer you carry the balance, the **more interest costs** you have to pay, and the **more expensive that debt is.**

For debt with **HIGHER INTEREST RATES,** the impact can be **EVEN LARGER.**

PAYING OFF MORTGAGE DEBT

COST OF INTEREST on a $100,000 fixed-rate mortgage at 5%...[2]

15-YEAR LOAN	$42,300
30-YEAR LOAN	$93,300

PAYING AN EXTRA $1,000 on day 1 of a ...

15-YEAR 5% home mortgage HELPS SAVE: $1,097 in interest costs over the life of the loan

30-YEAR 5% home mortgage HELPS SAVE: $3,383 in interest costs over the life of the loan

PAYING OFF CREDIT CARD DEBT

PAYING AN EXTRA $1,000 on a credit card balance that charges **12% INTEREST**

CAN SAVE...

$241 in interest payments

Pays off the balance **3 MONTHS FASTER**

Assumes a $500 per month repayment plan of 23 months, no annual fee, a starting balance of $10,000 and no new charges.[3]

GET STARTED TODAY:

FIRST, TARGET YOUR EXTRA PAYMENTS TOWARD YOUR HIGH-INTEREST-RATE DEBT to maximize your potential savings on the cost of interest. **You can use the State Farm® Debt Payment Calculator** to plan out how much an extra payment can save you.[3]

1 Federal Reserve of New York https://www.newyorkfed.org/microeconomics/hhdc.html

2 All mortgage calculations based on Bankrate.com mortgage calculator. https://www.bankrate.com/calculators/mortgages/mortgage-calculator.aspx

3 State Farm Debt Payment Calculator https://www.statefarm.com/simple-insights/planning/make-a-plan-to-tackle-your-debt-with-this-calculator

Choose the Right Investments

How to narrow down the options without being overwhelmed.

DIPPING YOUR TOES INTO THE INVESTMENT WATERS CAN BE THRILLING—AND TERRIFYING. Through a registered State Farm® agent, you have more than 140 mutual funds to choose from. And while having so many choices means you might discover some opportunities, it also can leave you feeling overwhelmed. **Here are some tips for handling tough investment decisions:**

DETERMINE YOUR INVESTMENT GOALS.

Before you choose, clarify what you want to achieve. Is it creating a source of retirement income? Starting a business? Financing your children's education? Make a list of your financial goals and define the time range for each. Having a clear picture of what you want to accomplish, in the short term and the long term, can help guide your investment decisions.

KNOW YOUR RISK TOLERANCE.

The degree of risk you can endure depends greatly on your timeline. If you're a younger investor with many years ahead, you may be able to invest more heavily in stocks and cope with greater volatility than if you are a retired investor living on a fixed income. To help clarify your risk tolerance, figure out your time horizon and when you plan to start withdrawing funds.

UNDERSTAND HOW EMOTIONS INFLUENCE YOU.

Even when humans know better, we are notoriously swayed by our emotions, especially in the face of fear or excitement. Unfortunately, the impulsive decisions investors make in the heat of the moment can backfire. Many factors fuel emotional decision-making: stress at work, worries at home, concerns over something happening in the news. It's important to recognize how your emotions influence your thinking so you can avoid making investment choices based on how you feel.

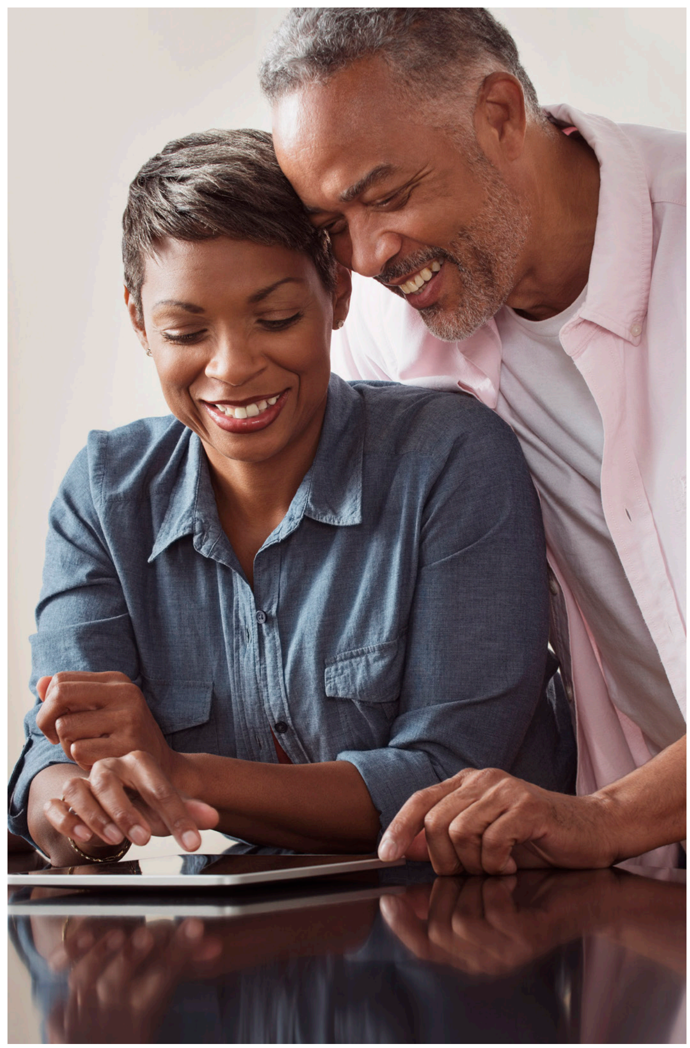
CONSULT OUTSIDE HELP.

A registered State Farm agent can be an excellent resource for setting up an investment portfolio that's right for your goals, timeline and risk tolerance. An advisor can answer your questions, help you narrow your choices and keep you focused if the process begins to overwhelm.

MANAGE YOUR EXPECTATIONS.

There's probably no single best investment, so look for the options that match your goals and risk tolerance. Research how those investments are likely to perform, so you know what to expect. Be realistic about the potential for losses. After you've chosen, resist the temptation to revisit your decision or agonize over the options you could have chosen. Stick to your plan and let strategy guide your next moves.

The investment world is full of options. Don't let the vast array of choices deter you from diving in. The best way to start is to define your goals and narrow your choices accordingly.

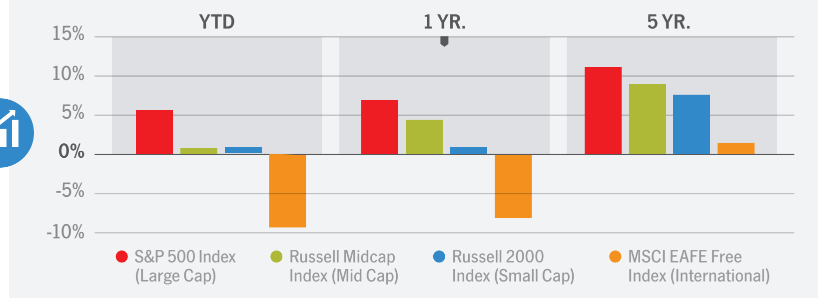


STATE FARM MARKET RECAP As of November 30, 2018

EQUITIES RECAP

- After October's sharp declines, global equity markets recovered modestly in November, helped by positive corporate earnings and signs of progress on trade issues between the U.S. and China.
- In the U.S., equities moved back into positive territory in November. For the month, the benchmark S&P 500® Index posted a 2.0% total return. Mid- and small-cap stocks, as measured by the Russell MidCap® Index and Russell 2000® Index, also advanced for the month, gaining 2.1% and 1.4% respectively.

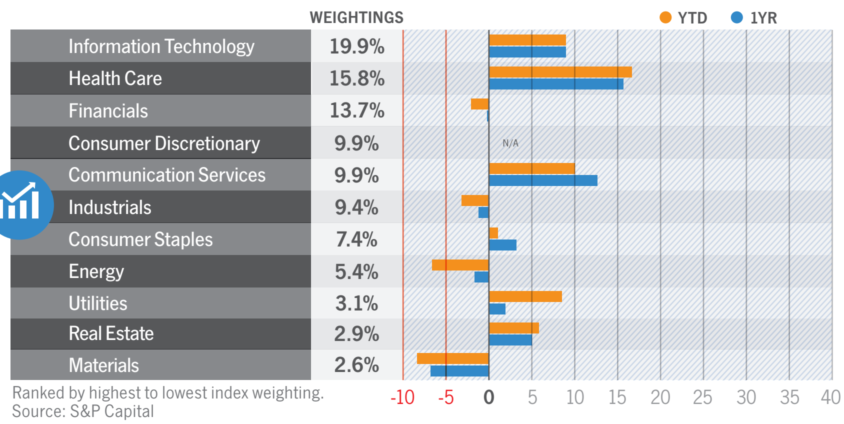
EQUITIES MARKET PERFORMANCE Total Returns for Periods Ended November 30, 2018



U.S. EQUITIES

- U.S. equities posted modest gains in November, with the benchmark S&P 500 Index closing out the month posting its best week of 2018, rising close to 5%. The markets, however, remained volatile during the month, with eight days experiencing price moves of 1% or more. Through 11 months of the year, the stock market experienced 54 moves of 1% or greater (30 up and 24 down) compared with eight for all of 2017. Year-to-date (YTD) through November, U.S. equities, as measured by the S&P 500 Index, recorded a 5.1% total return.

PERFORMANCE OF S&P 500 INDEX Total Returns for Periods Ended November 30, 2018

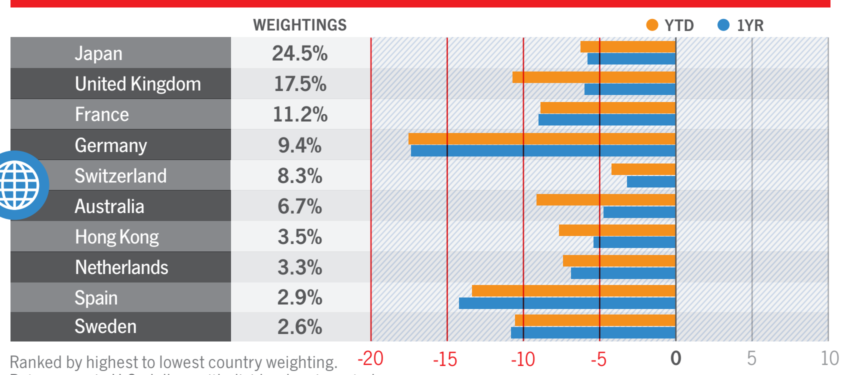


Ranked by highest to lowest index weighting.
Source: S&P Capital

GLOBAL EQUITIES

- In November, Emerging Market equities rallied on the prospect of a more moderate outlook for U.S. monetary policy, while a sharp decline in crude oil prices was supportive of those emerging markets that are net importers of oil. YTD, the MSCI Emerging Market Index (not shown) returned -12.2%, in U.S. dollar terms. Meanwhile, international developed markets closed lower for the month, hampered by concerns about slowing global growth, ongoing trade tensions and tightening monetary policies. YTD, the MSCI EAFE Index returned -9.4%, in U.S. dollar terms.

PERFORMANCE OF MSCI EAFE INDEX Total Returns for Periods Ended November 30, 2018

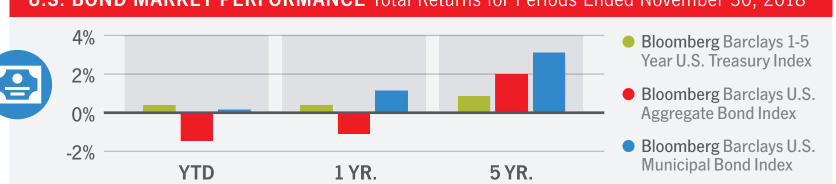


Ranked by highest to lowest country weighting.
Returns are in U.S. dollars with dividends reinvested.
Weightings as of 9/30/2018.

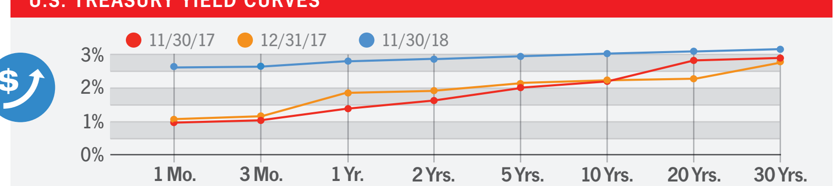
FIXED INCOME RECAP

- The U.S. fixed income markets posted modest gains in November, as hopes remained high that the U.S. and China could reach an agreement on trade tariffs. For the month, the Bloomberg Barclays U.S. Aggregate Bond Index posted a 0.6% total return. Over the longer one- and five-year time periods, investment grade bonds recorded annualized total returns of -1.3% and 2.0%, respectively.
- U.S. municipal bonds rallied in November, as investor demand outpaced supply. For the month, the Bloomberg Barclays Municipal Bond Index posted a 1.1% total return. Over the longer one- and five-year time periods, municipal bonds recorded annualized total returns of 1.1% and 3.5%, respectively.

U.S. BOND MARKET PERFORMANCE Total Returns for Periods Ended November 30, 2018



U.S. TREASURY YIELD CURVES



MARKET COMMENTARY

Are the U.S. Midterm Election Results a Big Deal for Investors?

The 2018 congressional midterms are now in the rearview mirror. Many investors are trying to gauge what impact the results will have on the U.S. economy and financial markets.

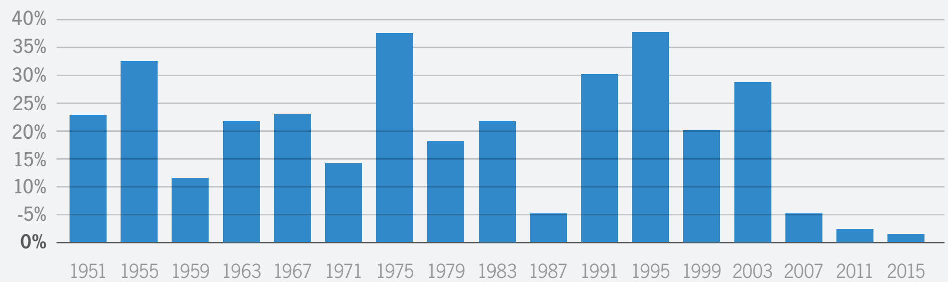
In 2019, America will have a divided Congress, with Republicans retaining the Senate majority and Democrats taking control of the House. What does a divided Congress, and the potential legislative gridlock in Washington over the next two years, mean for investors?

Historically, midterm elections have not had major impacts on financial markets. In fact, looking back, the financial markets have performed relatively well in the aftermath of midterm elections. For instance, since 1950, the stock market has not declined in any one-year period following a midterm election. And the average gain for the S&P 500® Index has been 19.9 percent on a total-return basis.

For investors, the results of the midterm elections may be far less important than some of the major issues currently impacting the financial markets. Trends in global growth, interest rates, inflation and oil prices, along with trade tariffs and geopolitical tensions, are among the developments outweighing the recent changes in Congress. Consequently, investors should be cautious about making emotional investment decisions based on the election results. Instead, they should stay focused on the fundamental issues that typically determine market performance while always maintaining an eye on investment goals and time horizon. State Farm is here to help you with these and other financial and insurance needs you may have.

STOCK MARKET PERFORMANCE IN YEARS AFTER MIDTERM ELECTIONS
S&P 500® Index Total Return: 1951–2015

Data shows the one-year total return of the S&P 500 Index following midterm elections since 1950. **Past performance is no guarantee of future results.**



Source: S&P Capital

- **Securities, insurance, and annuity products are not FDIC insured, are not bank guaranteed and are subject to investment risk, including possible loss of principal.**
- Past performance is no guarantee of future results.
- It is not possible to invest directly in an index.
- Diversification, Automatic Investment Plans, and Asset Allocation do not assure a profit or protect against loss.
- Investing involves risk, including potential for loss. Current and future portfolio holdings are also subject to risk.
- Bonds are subject to interest rate risk and may decline in value due to an increase in interest rates.
- The stocks of small companies are more volatile than the stocks of larger, more established companies.
- Foreign investments involve greater risks than U.S. investments, including political and economic risks and the risk of currency fluctuations.
- Emerging markets involve greater risks than U.S. investments due to lower trading volume, political and economic instability, and other governmental limitations on foreign investment policy.
- The S&P 500® Index tracks the common stock performance of 500 large U.S. companies.
- Standard & Poor's, S&P, and S&P 500 are registered trademarks of Standard & Poor's Financial Services LLC, a subsidiary of The McGraw-Hill Companies.
- The Standard & Poor's Growth Index is comprised of the growth companies within the S&P 500 Index.
- The Russell Midcap® Index measures the performance of the mid-cap segment of the U.S. equity universe and is a subset of the Russell 1000 Index.
- The Russell 2000® Index tracks the common stock performance of the 2,000 smallest U.S. companies in the Russell 3000 Index.
- Russell Investments is the owner of trademarks, service marks, and copyrights related to its respective indexes.
- The Morgan Stanley Capital International Europe, Australasia and Far East (MSCI EAFE) Index captures large- and mid-cap representation across Developed Markets countries around the world, excluding the U.S. and Canada.
- The MSCI EM (Emerging Markets) Index is a capitalization-weighted index of stocks from 26 emerging markets that only includes issues that may be traded by foreign investors.
- The MSCI Japan Index is designed to measure the performance of the large- and mid-cap segments of the Japanese stock market.
- The Bloomberg Barclays 1–5 Year U.S. Treasury Index measures the performance of short-term U.S. Treasury Securities maturing within one to five years.
- The Bloomberg Barclays U.S. Aggregate Bond Index represents debt securities in the U.S. investment-grade fixed-rate bond market.
- The Bloomberg Barclays Municipal Bond Index is an unmanaged index representative of the tax-exempt bond market.
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