Financial Advisory Service, Inc.

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FAS Monthly Economic and Market Update

December 2019

As of November 29, 2019

Contents

Economic Conditions.....3

Market Conditions..... 4

Education.....5

Disclosures & Index Definitions.....8

Economic Conditions

U.S. GDP growth in the third quarter of 2019 was adjusted upward to 2.1% according to the second estimate released by the Department of Commerce – a slight uptick from the 1.9% growth stated in the estimate released in late October. Revisions to private inventory investment, nonresidential fixed investment and personal consumption contributed to the upward adjustment for Q3 GDP. Consumption continues to be the force driving the economy, offsetting the decline in business investment.

The Fed announced in mid-December it would not cut rates further citing current rates being at appropriate levels for keeping the expansion going. With federal budget deficits projected to reach $1.2T per year for the next ten years the Treasury Department is expected to continue to issue record amounts of debt and that could have adverse affects on the "repo" market, which is a mechanism for institutions to borrow short-term money – often overnight – to have cash on their books per certain regulatory requirements. These overnight loans are backed by government debt, which is essentially viewed as cash. However, when too much collateral ends up chasing not enough cash, we see a situation like we witnessed in September when overnight rates spiked and cash became abnormally expensive. The Fed was forced to intervene to mitigate the spike in rates and could be forced to face that scenario yet again.

Market Conditions

Index Returns	Dec '19	YTD
S&P 500	3.4%	25.30%
DJIA	3.72%	20.25
NASDAQ	4.50%	30.60%
MSCI EAFE	0.97%	14.80%
Barclays Aggregate	(0.05%)	8.79%

Just as the U.S. major market indices began November with all-time highs they also closed out November near all-time highs. All three indices recorded ten record highs in the month of November before pulling back slightly on the last trading day of the month. The S&P 500 and Dow returned 3.4% and 3.72%, respectively while the NASDAQ returned 4.5%. All three indices are up at least 20% year-to-date. The S&P and NASDAQ are both up double digits over the trailing one year, which includes the 15% drop we experienced last December. The Dow is up just under 10% over the same time frame.

Trade once again drove short-term movement in the markets as the U.S.-China trade talks looked to be headed in the right direction. Top officials from both countries agreed on a preliminary phase one deal, which was finalized (for what seems like the second or third time) in early December. Part of the agreement was for the U.S. to scale back some of its tariffs and in exchange China would purchase more farm products and increase intellectual property protections. On the surface this is not a huge breakthrough (especially considering China was going to purchase more agriculture products from the U.S. to begin with), although it does provide a level of positivity moving forward for markets.

The Secure Act

The "Setting Every Community Up for Retirement" (SECURE) Act was passed by the House in May earlier this year. It has since been held up by lawmakers in the Senate but was tied to the spending bill earlier this week which was passed by the House and is likely to be passed by the Senate as well. Once this bill is approved by the president we will likely see sweeping changes in retirement planning which include allowing people to contribute to their IRAs after age 70 ½, increasing the age for required minimum distributions, 401(k) access for part-time workers and eliminating the "stretch IRA." Below is a summary of some changes we will see and what they mean to you.

Traditional IRA Contributions After age 70 ½

Currently when an individual hits the age of 70 ½ they are prohibited from making contributions to their traditional IRAs, regardless of whether or not they still have earned income. Due to increased life expectancies and individuals working for longer, the bill will allow for traditional IRA contributions just as the current law allows for 401(k) and Roth IRA contributions. The current contribution limit is $6,000, plus an additional $1,000 catch up contribution for individuals age 50 and over.

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The Secure Act

Increased Age for Required Minimum Distributions

Under the current law, investors are required to begin taking required minimum distributions (RMDs) from their traditional IRAs in the year they turn 70 ½. Again, due to increased life expectancies the new bill would increase this age to 72. The only caveat is that it will only apply to those who have yet to reach age 72 by the end of 2019. Anyone who is between the ages of 70 ½ and 72 and are currently taking RMDs will still be required to do so even if they are not yet 72.

Elimination of the Stretch IRA

This is quite possibly the biggest change with the new bill. As the law is currently written, any non-spouse beneficiaries of IRAs have the option of using the life expectancy table to take required minimum distributions annually from that inherited IRA. For example, for individuals as young as 40 or 50 those distribution rates range from 2.3% to 2.9% and slightly increase annually. Alternatively, beneficiaries have the option of taking a lump sum or withdrawing all funds within five years. Most choose to stretch distributions out in order to lower their tax burden and allow the assets to continue to grow tax-deferred for years, if not decades. Under the Secure Act, this option would go away in order to

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The Secure Act

recoup the tax revenue which would be going away/getting deferred to later dates. The Secure Act would require all assets in inherited IRAs to be withdrawn completely within ten years. Using the example from earlier, this would mean the distribution rate for those younger beneficiaries would go from the 2% range up to 10% annually, on average. A 50 year old non-spouse beneficiary who inherits $500,000 from a parent's IRA today would be required to distribute approximately $14,620 in the year following the grantor's death. That amount would gradually increase each year, however the majority of those assets would continue to grow tax deferred. Under the new law that beneficiary would be required to distribute, on average, $50,000/year to ensure the IRA has been fully distributed after ten years. That means more than $35,000 more earned income for the beneficiary under the new law versus the law today.

There are ways to plan for this new rule change so please reach out to your adviser with any questions regarding how these changes may affect you or to discuss generational planning strategies.

Disclosures & Index Definitions

Under style performance boxes, indexes referenced in the equities section for large, mid and small reference the Russell 1000, Russell MidCap and Russell 2000 stock indices, respectively. The Barclays US Government, Barclays Credit and Barclays High Yield fixed income indices refer to Gov't, Corp, and HY, respectively. Short, Intermediate and Long refer to the time frame of the investments and their positions on the yield curve.

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All dates are as of November 29, 2019 unless stated otherwise.

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Index Definitions

The **S&P 500 Index** is based on the market capitalizations of 500 large companies whose stocks are listed on the NYSE and NASDAQ. This is widely regarded as the single best gauge of large cap US Equities.

The **Dow Jones Industrial Average** is a price-weighted average of 30 actively traded blue-chip stocks, primarily industrials. It is used as a barometer of how shares if the largest US companies are performing.

The **NASDAQ** is a market capitalization weighted index of the more than 3000 common equities listed on the NASDAQ Stock Exchange. These securities include American Depository Receipts, common stocks, real estate investment trusts, and tracking stocks.

The **MSCI EAFE (Europe, Australasia, Far East) Net Index** is recognized as the pre-eminent benchmark in the US to measure international equity performance. It comprises the MSCI country indices that represent developed markets outside of North America, Europe, Australia, and the Far East.

The **MSCI Emerging Markets Index** captures large and mid cap representation across 23 Emerging Markets (EM) countries. With 822 countries, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

The **Barclays US Aggregate Index** is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS, ABS, and CMBS.

All index information has been gathered from public sources who are assumed to be reliable, although we cannot guarantee the accuracy or completeness of those public sources.