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MONTHLY ECONOMIC UPDATE

THIS MONTH'S HIGHLIGHT IS SOCIAL SECURITY

Social Security benefits can be a critical part of your retirement income. It's important to understand how it works and consider carefully when to claim your benefits. The following articles are designed to help you start thinking about Social Security

June 2018

THE MONTH IN BRIEF

In May, investors were left to interpret mixed geopolitical and financial signals. The historic U.S.-North Korea summit was on, then off, then possibly on again. An apparent truce emerged in the U.S.-China tariffs battle, but it did not last. Oil rallied, but then prices fell. Federal Reserve policy meeting minutes indicated central bank officials would accept above-target inflation for a while. Other economic signals were clear: new and existing home sales were down, consumer confidence was back up, and consumer spending was strong. In the end, the markets took all this in stride – the S&P 500 rose 2.16% for the month.

DOMESTIC ECONOMIC HEALTH

On May 19, Secretary of the Treasury Steven Mnuchin told the media that the U.S.-China trade war was "on hold." Both nations agreed to refrain from imposing new import tariffs, and China announced plans to lower taxes on imported cars and trucks from 25% to 15%. Ten days later, the U.S. surprised economists, journalists, and investors by electing to proceed with the 25% tariffs on $50 billion of Chinese imports it had proposed in April. The Chinese government indicated it was ready to institute tariffs in response. On May 31, the Trump administration said that it would move forward with its planned steel and aluminum tariffs against Mexico, Canada, and the European Union, as well as extend short-term exemptions no further. Mexico and the E.U. quickly announced retaliatory taxes for U.S. imports.

What did the Federal Reserve mean when it used the word "symmetric" in the minutes of its May meeting? The text referred to its "symmetric inflation objective," and that obscure adjective (meaning "showing symmetry") was used nine times. Market participants did learn that Fed policymakers were willing to let inflation briefly top the central bank's 2% target rate. The Fed held interest rates steady last month, but a June rate hike seemed a distinct possibility: "Most participants judged that if incoming information broadly confirmed their current economic outlook, it would likely soon be appropriate [to] take another step in removing policy accommodation."

Looking at inflation gauges and other core economic indicators kept by federal government departments, the positives seemed to outnumber the negatives. Consumer prices were up 2.5% annually through April, just 0.1% above the March reading, and yearly wholesale inflation fell to 2.6% from the 3.0% advance measured in the third month of the year. The Core PCE Price Index showed 2.3% year-over-year inflation through April, as opposed to 2.5% through March. Hard goods orders were down 1.7% in April, but rose 0.9% minus defense industry orders. Retail sales improved another 0.3% for April, and that gain held up even with auto sales removed. Another report showed consumer spending advancing 0.6% in April, consumer incomes 0.3%. Gross domestic product in the first quarter was evaluated at 2.2%.

Unemployment dropped to 3.9% in April and 3.8% in May, according to the Department of Labor. That was a low unseen since 2000. Wages grew 0.1% in April and 0.3% a month later; net job creation was at 159,000 in April and 223,000 in May. The U-6 rate, tracking both unemployed and underemployed workers, fell to 7.6% in May; it was 0.2% higher a month before.

The Institute for Supply Management's purchasing manager indices showed slightly slower industry growth in April than in March; both benchmarks lost 2.0 points. The manufacturing PMI was at 57.3; the non-manufacturing PMI, at 56.8.

Lastly, the Conference Board's consumer confidence index rose 2.4 points in May, reaching a lofty 128.0. The University of Michigan's consumer sentiment index declined 0.8 points from its initial May mark to 98.0.

GLOBAL ECONOMIC HEALTH

Political turmoil in Southern Europe made investors uneasy as May concluded. Italian President Sergio Mattarella effectively prevented the formation of a coalition government in late May. Populist parties managed to establish a new government as May ended, but investors and economists worried that the populists could try to push Italy out of the European Union. Spanish Prime Minister Mariano Rajoy was ousted by a parliamentary vote and replaced by new Prime Minister Pedro Sanchez, who headed a coalition including Catalan separatists.

An analysis by Bloomberg pointed to a moderate deceleration in the Chinese economy. Bloomberg Economics concluded in late May that the P.R.C. was indeed on pace for 6.5% growth in 2018, parallel with official estimates. That would represent a drop from the nation's 6.9% GDP in 2017. Meanwhile, new data showed the Japanese economy contracting 0.6% the first quarter, displaying its first negative GDP reading in more than two years. In its May economic report, Japan's Cabinet Office maintained that the world's third-largest economy was "gradually recovering."

WORLD MARKETS

Away from America, the TSX Composite achieved the standout gain of the month, rising 2.91%. Nearly matching Canada's leading stock benchmark, the United Kingdom's FTSE 100 advanced 2.25%. Taiwan's TSE 50 improved 1.09%. There were other, minor index improvements: the Shanghai Composite rose 0.43%; the Sensex, 0.46%; the MSCI World, 0.31%.

Losses were widespread in a month with much geopolitical and trade uncertainty. The West saw two of the biggest drops: a 7.64% slump for Mexico's Bolsa and a 10.87% fall for Brazil's Bovespa. Political tension in Spain drove the IBEX 35 5.16% lower. Singapore's Straits Times index slipped 5.14%, and Malaysia's Kuala Lumpur Composite took a 6.94% fall. France's CAC 40 lost 2.21%; the Nikkei 225, 1.45%; the Hang Seng, 1.10%. The MSCI Emerging Markets index retreated 3.75%.

COMMODITIES MARKETS

In the middle of May, light sweet crude seemed poised for a major monthly gain. Although the NYMEX price surpassed $72 at one point, things reversed: oil ended up losing 2.09% on the month, settling at $67.15 on May 31. Natural gas was the leader among major energy futures, up 6.62%. Heating oil rose 2.22%, while unleaded gasoline gained 1.94%. Crops were led by cotton, which jumped 11.10%, and sugar, which surged 11.02%. Coffee futures advanced 2.74% in May; wheat, 1.79%; corn, 0.32%. Soybeans retreated 1.93%, and cocoa dropped 13.60%.

Ending May at a COMEX close of $1,298.00, gold was down 1.17% for the month. Other key metals advanced: silver gained 1.14%; platinum, 1.25%; copper, 0.30%. (Silver futures closed out the month at $16.45.) The U.S. Dollar Index stood at 94.07 at the close on May 31, having added 2.43% for the month.

REAL ESTATE

Mortgage rates may have soared in April, but they stabilized in May. On May 31, Freddie Mac's Primary Mortgage Market Survey found the mean interest rate for a conventional home loan at 4.56%, which was 0.02% lower than on April 26. (At the end of May 2017, the average interest rate on a 30-year ARM was 3.95%.) The average rate for the refinancer's favorite, the 15-year FRM, rose 0.04% to 4.06% between April 26 and May 31; the average rate for the 5/1-year ARM increased 0.06% to 3.80%.

Home buying fell off in April. According to National Association of Realtors research, there was a 2.5% retreat in the pace of existing home sales. What homes did sell spent an average of 26 days on the market. The median sale price ($257,900) was up 5.4% in April from the start of 2018. Census Bureau data showed new home sales slowing 1.5% in the fourth month of the year, and while the median sales price for a new residence declined 7.9% during April, that median price ($312,400) was not exactly in starter-home territory in many parts of the country.

The March S&P CoreLogic Case-Shiller home price index arrived, displaying a 6.8% overall annualized improvement for housing values across 20 metro areas; the increase matched that seen in the February edition. The NAR's pending home sales index declined 1.3% for March. Builders went to work on 3.7% fewer projects in April than they had in March. Mirroring the decline in starts, the Census Bureau also recorded a 1.8% dip in building permits.

LOOKING BACK…LOOKING FORWARD

What really attracted equity investors in May? Tech and small-cap shares. Both the Nasdaq Composite and Russell 2000 had a great month. The Nasdaq surged 5.32%; the Russell, 5.95%. (The Russell, incidentally, ended May at +6.39% YTD.) The S&P 500 posted a fine 2.16% gain, while the Dow Jones Industrial Average rose a respectable 1.05%. The CBOE VIX lost 3.14% for the month. When the closing bell rang on May 31, the Dow settled at 24,415.84; the Nasdaq, 7,442.12; the S&P, 2,705.27; the Russell, 1,633.61; the VIX, 15.43.

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	-1.23	+16.22	+12.31	+9.32
NASDAQ	+7.80	+20.06	+23.07	+19.50
S&P 500	+1.18	+12.17	+13.18	+9.32
REAL YIELD	5/31 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.76%	0.40%	-0.05%	1.58%

Sources: wsj.com, bigcharts.com, treasury.gov – 5/31/18[1,20,21,22]
Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly. These returns do not include dividends. 10-year TIPS real yield = projected return at maturity given expected inflation.

Tariffs are now being levied on imported steel and aluminum, and the trading partners affected by these taxes are responding or planning to respond with tariffs of their own on U.S. goods. Could stocks stall out because of this? An impeded flow of international trade would certainly impact the GDP of the world's major economies and exert a drag on corporate earnings. The uneasiness about the brewing trade war gives some investors pause; the potential scope of it seems too large to price in. It is hard to imagine any kind of summer rally if the measures and countermeasures taken by various countries escalate. Not all investors appear to be worried, though – witness what happened in May even as the distinct possibility of trade wars emerged. The blue chips were hurt, but the tech sector and the small caps held up. Do these shares have further room to advance, and will investors retain their bullishness about them? June presents significant questions for investors worldwide, and we may see equities tested as threatened tariffs become reality.

Retirement Planning Weak Spots

They are all too common.

Many households think they are planning carefully for retirement. In many case, they are not. Weak spots in their retirement planning and saving may go unnoticed.

Couples should recognize that they may face major medical expenses. Each year, Fidelity Investments estimates how much a pair of newly retired 65-year-olds will spend on health care throughout the rest of their lives. Fidelity says that on average, retiring men will need $133,000 to fund health care in retirement; retiring women, $147,000. Even baby boomers in outstanding health should accept the possibility that serious health conditions could increase their out-of-pocket hospital, prescription drug, and eldercare costs.

Retirement savers will want to diversify their invested assets. An analysis from StreetAuthority, a financial research and publishing company, demonstrates how dramatic the shift has been for some investors. A hypothetical portfolio split evenly between equities and fixed-income investments at the end of February 2009 would have been weighted 74/26 in favor of equities exactly nine years later. If a bear market arrives, that lack of diversification could spell trouble. Another weak spot: some investors just fall in love with two or three companies. If they only buy shares in those companies, their retirement prospects will become tied up with the future of those firms, which could lead to problems.

The usefulness of dollar cost averaging. Recurring, automatic monthly contributions to retirement accounts allow a pre-retiree to save consistently for them. Contrast that with pre-retirees who never arrange monthly salary deferrals into their retirement accounts; they hunt for investment money each month, and it becomes an item on their to-do list. Who knows whether it will be crossed off regularly or not?

Big debts can put a drag on a retirement saving strategy. Some financial professionals urge their clients to retire debt free or with as little debt as possible; others think carrying a mortgage in retirement can work out. This difference of opinion aside, the less debt a pre-retiree has, the more cash he or she can free up for investment or put into savings.

The biggest weakness is not having a plan at all. How many households save for retirement with a number in mind – the dollar figure their retirement fund needs to meet? How many approach their retirements with an idea of the income they will require? A conversation with a financial professional may help to clear up any ambiguities – and lead to a strategy that puts new focus into retirement planning.

Are Your Beneficiary Designations Up to Date?

Who should inherit your IRA or 401(k)? See that they do.

Here's a simple financial question: who is the beneficiary of your IRA? How about your 401(k) or annuity? You may be saying, "I'm not sure." It is smart to periodically review your beneficiary designations.

Your choices may need to change with the times. When did you open your first IRA? When did you buy your life insurance policy? Was it back in the Nineties? Are you still living in the same home and working at the same job as you did back then? Have your priorities changed?

While your beneficiary choices may seem obvious and rock-solid when you initially make them, time has a way of altering things. In a stretch of five or ten years, some major changes can occur in your life and may warrant changes in your beneficiary decisions.

In fact, you might want to review them annually. Here's why: companies frequently change custodians when it comes to retirement plans and insurance policies. When a new custodian comes on board, a beneficiary designation can get lost in the paper shuffle. (It has happened.) If you don't have a designated beneficiary on your retirement accounts, those assets may go to the "default" beneficiaries when you pass away, which might throw a wrench in your estate planning. An example: under ERISA, your spouse receives your 401(k) assets if you pass away. You spouse must waive that privilege in writing for those assets to go to your children instead.

How your choices affect your loved ones. The beneficiary of your IRA, annuity, 401(k), or life insurance policy may be your spouse, your child, maybe another loved one, or maybe even an institution. Naming a beneficiary helps to keep these assets out of probate when you pass away.

Many people do not realize that beneficiary designations take priority over bequests made in a will or living trust. For example, if you long ago named a son or daughter who is now estranged from you as the beneficiary of your life insurance policy, he or she will receive the death benefit when you die, regardless of what your will states.

You may have even chosen the "smartest financial mind" in your family as your beneficiary, thinking that he or she has the knowledge to carry out your financial wishes in the event of your death. But what if this person passes away before you do? What if you change your mind about the way you want your assets distributed and are unable to communicate your intentions in time? And what if he or she inherits tax problems as a result of receiving your assets?

How you choices affect your estate. If you are naming your spouse as your beneficiary, the tax consequences are less thorny. Assets you inherit from your spouse aren't subject to estate tax, as long as you are a U.S. citizen.

When the beneficiary isn't your spouse, things get a little more complicated – for your estate and for your beneficiary's estate. If you name, for example, your son or

your sister as the beneficiary of your retirement plan assets, the amount of those assets will be included in the value of your taxable estate. (This might mean a higher estate tax bill for your heirs.) And the problem will persist: when your non-spouse beneficiary inherits those retirement plan assets, those assets become part of their taxable estate, and their heirs might face higher estate taxes. Your non-spouse heir might also have to take required income distributions from that retirement plan someday and pay the required taxes on that income.
If you properly designate a charity or other 501(c)(3) non-profit organization as a beneficiary of your retirement account assets, the assets can pass to the charity without your estate being taxed, and the gift will be deductible for estate tax purposes.

How Retirement Spending Changes With Time

Once away from work, your cost of living may rise before it falls.

New retirees sometimes worry that they are spending too much, too soon. Should they scale back? Are they at risk of outliving their money?

This concern is legitimate. Many households "live it up" and spend more than they anticipate as retirement starts to unfold. In ten or twenty years, though, they may not spend nearly as much.

The initial stage of retirement can be expensive. Looking at mere data, it may not seem that way. The most recent Bureau of Labor Statistics figures show average spending of $60,076 per year for households headed by Americans age 55-64 and mean spending of just $45,221 for households headed by people age 65 and older.

Affluent retirees, however, are often "above average" in regard to retirement savings and retirement ambitions. Sixty-five is now late-middle age, and today's well-to-do 65-year-olds are ready, willing, and able to travel and have adventures. Since they no longer work full time, they may no longer contribute to workplace retirement plans. Their commuting costs are gone, and perhaps they are in a lower tax bracket as well. They may be tempted to direct some of the money they would otherwise spend into leisure and hobby pursuits. It may shock them to find that they have withdrawn 6-7% of their savings in the first year of retirement rather than 3-4%.

When retirees are well into their seventies, spending decreases. In fact, Government Accountability Office data shows that people age 75-79 spend 41% less on average than people in their peak spending years (which usually occur in the late 40s). Sudden medical expenses aside, household spending usually levels out because the cost of living does not significantly increase from year to year. Late-middle age has ended and retirees are often a bit less physically active than they once were. It becomes easier to meet the goal of living on 4% of savings a year (or less), plus Social Security.

Later in life, spending may decline further. Once many retirees are into their eighties, they have traveled and pursued their goals to a great degree. Staying home and spending quality time around kids and grandkids, rather than spending money, may become the focus.

One study finds that medical costs burden retirees mostly at the end of life. Some economists and retirement planners feel that retirement spending is best depicted by a U-shaped graph; it falls, then rises as elders face large medical expenses. Research from investment giant BlackRock contradicts this. BlackRock's 2017 study on retiree spending patterns found simply a gradual reduction in retiree outflows as retirements progressed. Medical expenses only spiked for most retirees in the last two years of their lives.

Retirees in their sixties should realize that their spending will likely decline as they age. As they try to avoid spending down their assets too quickly, they can take some comfort in knowing that in future years, they could possibly spend much less.

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