MARKET & LEGAL UPDATE
JUNE 2018 REVIEW

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"Trade War Fears Weigh on the Markets"

Domestic stock markets were rocky in June but closed out the second quarter with positive returns. Headlines were dominated by trade war talk and inflation fears during the month, overriding favorable economic data. In addition, a rising interest rate environment, coupled with a strengthening U.S. dollar, produced vulnerability in both developed and emerging international markets.

Trade war headlines dominated the news in June, leaving investors uncertain about the potential impact of the recently imposed tariffs on China and Europe and the retaliatory tariffs on U.S. exports. Although the magnitude of tariffs is currently small, only accounting for 2% of all U.S. imports and 0.3% of our GDP, further escalation threatens to restrict global free trade and hurt economic progress. Determining the impact of tariffs on the economy can be difficult and it is even harder trying to understand the indirect impact on consumer confidence. Despite looming trade concerns, the three major domestic indices all finished the month in positive territory. The tech heavy NASDAQ led the way, marking its eighth consecutive quarter in the black, gaining 0.9% in June. During the first half of 2018, the index advanced 8.8%. The S&P 500, which was down in the first quarter, finished the second quarter on a positive note as well. The index added 0.6% in June and has gained 2.7% year to date. The Dow remains negative year to date at -0.7% but posted a 0.5% gain for the month.

The European economy, which seemed to be on the road to recovery for several years, has recently experienced a slowdown. Political uncertainty in Italy and Spain, combined with a decline in economic activity in Germany, has driven down the value of the Euro. Additionally, the EU has been pushing for regulatory policies which are perceived by investors as anti-growth. As a result, the MSCI EAFE Index was down 1.2% in June and has lost 2.8% for the quarter while emerging markets took the biggest hit during the month, losing4.2%.

Trade uncertainty has also become a concern for Fed Chair Powell, who is warning that it may "cause us to question the economic outlook". However, this did not stop the FOMC from voting to increase interest rates another 0.25% at the June meeting. As a result, the yield curve continues to narrow and it is flatter than it has been in over a decade. The spread between the 10-year and 2-year treasury yields has flattened to less than 35 basis points, which is close to an inversion. Historically, an inverted yield curve has been an indicator of an impending recession. As a result, fixed income results were mixed in June. The Barclays Aggregate Bond index was down 0.1% while the Barclays U.S. High Yield Index shrugged off inflation concerns and gained 0.4%.

	June 2018	YTD
DJIA	0.49%	-0.73%
S&P 500	0.62%	2.65%
NASDAQ	0.92%	8.79%
MSCI EAFE	-1.22%	-2.75%
MSCI Emerging Markets	-4.15%	-6.66%
Barclays Aggregate	-0.12%	-1.62%
Barclays Corp High Yield	0.40%	0.16%
	6/30/2018	5/31/2018
US 10-Year Treasury	2.85%	2.83%

Overall, the first half of 2018 has been extremely volatile with swings in both directions on a near daily basis. The market will likely continue to follow news on trade for the rest of the year, which may continue to be a source of volatility. Trade tensions, coupled with a flat yield curve, a slowdown in Europe, and a stronger dollar will likely continue to weigh on the markets going forward.

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LEGAL UPDATE | Restatement Periods for 403(b) Plans and Pre-Approved Defined Benefit Retirement Plans

IRS restatement periods are currently underway for both 403(b) plans and Pre-Approved Defined Benefit Plans. Here is some important information pertaining to these restatement periods.

Q: What is the IRS 403(b) plan document restatement process and why is it required?

A: Although the plan document requirement and restatement process has been ongoing for other qualified retirement plans (such as 401(k), profit sharing, defined benefit) for quite some time, 403(b) plans were historically relieved of this process. In fact, prior to 2009, 403(b) plans were not even required to have a written plan document. This changed with passage of the final 403(b) regulations, which required 403(b) plans to have the written plan document in place by December 31, 2009. However, despite the written plan document requirement, there was no process under which a 403(b) plan sponsor could get assurance from the IRS that the plan met the legal requirements until now. With the establishment of the preapproved 403(b) plan document program, plan sponsors will now have such assurance, as these preapproved 403(b) plan documents have received advisory or opinion letters from the IRS indicating that the documents contain all the required provisions and legally comply with the tax code requirements. Plan sponsors technically have until March 31, 2020 to convert or restate their 403(b) plans to the new pre-approved plan.

Q: Why do pre-approved defined benefit plans have to be restated?

A: Pre-approved defined benefit plans were last restated sometime between May 1, 2010 and April 30, 2012. The IRS has established a cyclical system where pre-approved defined benefit plans are required to be restated once every six years. The current restatement period recently opened on May 1, 2018 and will close on April 30, 2020. There are definite advantages to maintaining defined benefit plans on a pre-approved plan document. A pre-approved plan incorporates all the recent law changes, and has received an opinion letter from the IRS confirming that the document contains all the required provisions and legally complies with the tax code requirements.

Current USI Consulting Group clients will be contacted about this important plan restatement process. However, if we have not drafted your documents in the past, or if you are interested in converting your defined benefit to a new pre-approved plan, please contact your USI Consulting Group plan representative.

For previous market commentaries please click here.

An index is a measure of value changes in a representative grouping of stocks, bonds, or other securities. Indexes are used primarily for comparative performance measurement and as a gauge of movements in financial markets. You can not invest directly in an index and, for comparative purposes; they do not reflect the effect of the various fees inherent in actual investment vehicles.

The S&P 500 Index is a market value weighted index showing the change in the aggregate market value of 500 U.S. stocks. It is a commonly used measure of stock market total return performance.

The Dow Jones Industrial Average is a price weighted index comprised of 30 actively traded blue chip stocks; primarily industrial companies, but including some service oriented firms.

The NASDAQ Composite Index is a market-value weighted index that measures all domestic and non-U.S. based securities listed on the NASDAQ Stock Market.

Gross Domestic Product (GDP) is the market value of the goods and services produced by labor and property in the U.S. It is comprised of consumer and government purchases, net exports of goods and services, and private domestic investments. The Commerce Department releases figures for GDP on a quarterly basis. Inflation adjusted GDP (or real GDP) is used to measure growth of the U.S. economy.

The MSCI Europe and Australasia, Far East Equity Index (EAFE) is a market capitalization weighted unmanaged index developed by Morgan Stanley Capital International to measure approximately 1,100 securities in 21 major overseas stock markets. It is a commonly used measure for foreign stock market performance.

The Barclays Capital U.S. Aggregate Index covers the U.S. Dollar denominated investment grade, fixed-rate, taxable bond market of SEC-registered securities.

The Barclays Capital U.S. Corporate High Yield Index covers the U.S. Dollar denominated, non-investment grade, fixed income, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's Fitch, and S&P is Ba1/BB+/BB+ or below.

The MSCI Emerging Markets Index (EM) is a free-float-adjusted market-capitalization index developed by Morgan Stanley Capital International. It is designed to measure the equity market performance of 26 emerging market countries.

The 10 Year Treasury Yield is the interest rate the U.S. government pays to borrow money for a 10-year period. In addition to influencing how much the government pays to borrow over this timeframe, the 10-year Treasury Yields also determines how much investors earn by investing in this debt and it is a good indicator of investor sentiment. The higher the yield, the better the economic outlook.

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