SilverStar Insights

for your wealth

SILVERSTAR
WEALTH MANAGEMENT
Plan • Invest • Guide

By Tim Hudson, CFP®, CLU, ChFC, CRPS® April 2019

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We have moved! We are now located within the Cy-Fair Federal Credit Union location at Skinner Road (near Highway 290) 13525 Skinner Road, Cypress, TX 77429.

In this expanded issue, we will define a recession and discuss today's current market environment to address the media coverage on this hot topic.

We will also discuss why an in-service distribution from a company retirement plan may make sense, by rolling over a portion to an IRA that can provide you more investment options to consider to help reduce investment risk for those approaching their retirement years.

Please review our upcoming workshops covering a wide variety of important topics. The *Savvy Tax Planning: How Tax Planning Changes Through Four Stages of Retirement* workshop is one of our newest and has been very well-received, so please RSVP today!

Market View

2019 Year-to-Date Performance of Capital Markets	
S&P 500 - The S&P 500 (Standard & Poor's Index) is a stock market index containing the stocks of 500 American corporations with large market capitalization that are considered to be widely held.	**13.65%**
Barclays U.S. Aggregate Bond – The Barclays U.S. Aggregate Bond Index is an index of U.S. dollar-denominated, investment-grade U.S. corporate, government and mortgage-backed securities.	**2.94%**
MSCI EAFE – The MSCI EAFE serves as a benchmark of the performance in major international equity markets as represented by 21 major MSCI indexes from Europe, Australia, and Southeast Asia.	**9.98%**

Source: Morningstar (Performance from 1/1/19 to 03/31/19)

The word "recession" gets tossed around liberally in the financial media these days, a boogeyman lurking and ready to strike at any moment. But is danger really that imminent?

Henry Wadsworth Longfellow's poem, "The Midnight Ride of Paul Revere," retells the story of a patriot who shouts a harrowing warning to his fellow colonists, "A recession is coming! A recession is coming!"

Well, that's not quite the story, but given the seemingly non-ending talk about a recession, you might think that economists are reacting Paul Revere's midnight ride.

Yes, a recession is eventually inevitable, but is it imminent?

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The long-running expansions of the 1960s, 1980s, and 1990s gave rise to talk that a combination of fiscal and monetary policy may have ended the risk of a recession. Such talk was premature.

Today, the pendulum has swung in the opposite direction. Analysts and short-term traders have become hypersensitive to any signs a recession may be looming.

Stock market volatility and the steep correction late last year, the recent slowdown in U.S. economic activity, and an inverted yield curve (more details to follow) have contributed to worries about an economic downturn.

Plus, the economic expansion is fast approaching its 10-year anniversary. If the economy is still expanding in July, and odds suggest it may be, the current expansion will become the longest on record, exceeding the expansion of the 1990s, which lasted exactly 10 years.

Recessions are a part of the business cycle in a free market economy. But we should remind ourselves that expansions do not die of old age, expansions come to an end when economic and financial imbalances arise, such as a stock or housing bubble, or when the Fed aggressively hikes rates in response to a spike in inflation.

That brings us to the question.

What is a recession?

Contrary to the more traditional definition, a recession is not defined as two consecutive quarters of negative real (inflation-adjusted) GDP.

The National Bureau of Economic Research (NBER), a private economic research organization, defines an economic **recession** as: "a significant decline in economic activity spread across the economy, lasting more than a few months, affecting real GDP, real income, employment, industrial production, and wholesale-retail sales."[1]

These are very broad categories. They are not tied to one or two sectors, which might be experiencing weakness at any given time.

For example, during a recession, we'd expect to see declining retail and business sales. This would lead to a decline in industrial production and a rise in the unemployment rate.

It's not as if the NBER confirms a recession has begun shortly after it begins. It took nearly a year for the NBER to confirm the last recession. By then, it was a forgone conclusion. A similar delay occurs when the economy begins to recover, and the NBER is tasked with calling the end of the recession.

Why do we care about recessions?

There are plenty of reasons. For most Americans, job insecurity increases, layoffs rise, and it becomes much more difficult to find work.

For investors, it's a time of heavy uncertainty. Bear markets—a 20% or greater decline in the S&P 500 Index—are typically tied to recessions, as corporate profits decline and companies warn about the future.

The canary in the coal mine

Economists have always had trouble forecasting an upcoming recession. A few might get it right; most miss it.

But it's not as if we lack warning signs.

The Conference Board compiles what is called the Leading Economic Index®, or LEI as illustrated in Figure 1. It's akin to Paul Revere's midnight ride. It has historically warned of an impending recession, but the timing is in question.

There are 10 components of the LEI. These are leading predictors of economic activity:

1. Average weekly initial claims for unemployment insurance
2. Building permits for homes
3. 500 common stocks
4. 10-year Treasury bond less federal fund rate (yield curve—more on this in a moment)
5. Average weekly hours for manufacturing,
6. New orders for consumer goods and materials
7. The ISM® Index of New Orders
8. New orders for nondefense capital goods ex-aircraft
9. Average consumer expectations for business conditions
10. Leading Credit Index™

The list may seem a little overwhelming and some categories are less familiar than others.

1 nber.org/cycles

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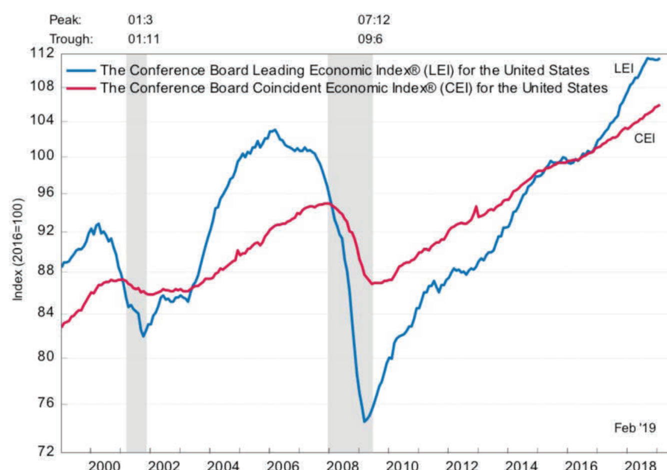
That said, the Conference Board plugs each months' numbers into a formula and reports on the LEI every month.

Why do we call them leading indicators? Simply because they tend to foreshadow future economic activity as illustrated.

Why 10? One or two might send out false signals. That's less likely with a compilation.

How do leading indicators work? Take first-time claims for unemployment insurance. When economic activity slows, we'd expect layoffs to tick higher. We might also expect stock prices to decline. And falling building permits would likely signal upcoming weakness in housing.

Figure 1. U.S. index of Leading Economic Indicators



The Conference Board Leading Economic Index® (LEI) components: 1) average weekly hours worked, manufacturing; 2) average weekly initial unemployment claims; 3) manufacturers' new orders – consumer goods and materials; 4) ISM index of new orders; 5) manufacturers' new orders, nondefense capital goods; 6) building permits – new private housing units; 7) stock prices, S&P 500; 8) Leading Credit Index™; 9) interest rate spread; 10-year Treasury less fed funds; 10) index of consumer expectations.,

Source: ©The Conference Board. Data through February 2019, released March 21, 2019.

Given the LEI, why is it so difficult to forecast a recession? Looking back at the last seven recessions (back to the 1969-70 recession), the lead time given by the LEI has ranged from 7-20 months.[2] That's quite a range.

Furthermore, there have been times when the LEI has given false recessionary signals, including the mid-1960s, the mid-1990s, the late 1990s, and during the recent expansion.

These "false positives" were temporary downticks. Nonetheless, the short-term declines could have been construed as a recessionary signal.

A cautiously upbeat signal

According to the Conference Board, the LEI has essentially been flat since October. It has correctly signaled a slowdown in the economy, but it has not signaled a recession.

In fact, in the Conference Board article title, "Fading Domestic Headwinds Will Keep Growth Above Trend," is cautiously encouraging.[3]

A shift in the atmosphere and a pivot by the Fed

During the third quarter of 2018, the economy was firing on all cylinders. At the September meeting of the Federal Reserve, policymakers were projecting three rate hikes in 2019–all 0.25 percentage point increases.

The Fed cut its forecast to two rate increases at the December meeting amid stock market uncertainty and signs U.S. growth was moderating.

At the conclusion of the March meeting, the Fed said it sees no rate hikes this year.

Furthermore, Fed Chief Jerome Powell was forced to push back on talk of a possible rate cut this year, arguing at his press conference that he expects "the economy will grow at a solid pace in 2019."

The pivot is complete.

The kink in the interest rate curve–inversion

Normally, the yield curve is upward sloping. As the maturity of bonds lengthen, the investor receives a higher yield. Think of it like this: you expect to receive a higher interest rate on a two-year CD than a six-month CD.

But there are times when the yield curve inverts—shorter-dated bonds yield more than longer-dated bonds.

2 Advisorperspective.com
3 Conference-Board.org

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On March 22, the yield on the three-month T-bill exceeded that on the 10-year Treasury by 0.02 percentage points.[4] That hasn't happened since 2006.

Based on data from the NBER and St. Louis Federal Reserve, the last seven recessions going back to the 1969-70 recessions have all been preceded by an inversion of the yield curve. We must go back to 1966, when a brief inversion was followed by a steep slowdown in growth and not a recession.

On average, a recession ensued 11 months later.

An inverted curve is signaling that investors believe short-term rates will eventually come down in response to a weaker economy. It may also hamper lending by banks.

John Kelly, Chief Strategist with JP Morgan believes an inverted curve may be a "broken barometer." He stated, "the yield curve itself has been distorted by unprecedented central bank buying of long-term bonds."[5]

But, is it different this time? "It's different this time," a four-word phrase that should always set off alarm bells. Usually it isn't. But are we getting confirmation from other signals?

1. Another strong recession predictor is an inversion of the 10-year/2-year Treasury. That has not occurred, as the 2-year yield has been falling along with the 10-year.
2. The Conference Board's Leading Index has been flat since October, signaling the slowdown in U.S. growth. But it has not declined.
3. In addition, weakness in Europe has pushed yields down sharply overseas, which may be encouraging some global investors to park money into higher-yielding U.S. bonds.
4. The Fed is no longer eyeing rate hikes, and financial conditions have eased during the first quarter.

Recessions have typically been preceded by major economic imbalances, such as a stock market bubble or housing bubble. Or, a sharp rise in inflation forces the Fed to aggressively respond with rate hikes.

For the most part, neither conditions are currently present, lessening odds a near-term recession is lurking.

Further, recent market action has been impressive. It's not as if we haven't seen some volatility, but year-to-date performance isn't signaling an economic contraction is imminent. Employment is still strong, inflation is in check, and stocks are not overvalued by historical measures, but there are signs of structural risk. As stated by Christopher Riggs of Alphalytics Research, there are "concerns about the trend on capital goods and construction," with the current numbers on new completions and home sales being down.[6]

No one can predict recessions with accuracy, but good planning dictates it is always wise to be proactive and re-examine risk attributes of investment portfolios and retirement income plans, especially for those approaching or in retirement. Contact us if you want to re-examine your portfolio and overall wealth plan, or if would like to discuss risk mitigation options.

The Value of In-Service Distributions

More companies today are allowing employees who at least age 59 ½, and nearing retirement age, to do in-service distributions by rolling over a portion of their retirement plan to an IRA from their retirement plans—401(k)s, 403(b)s, 457(b)s—at work while they are still employed. Many employees are unaware that their retirement plan may offer in-service distributions and do not take advantage of them.

According to a survey by the Profit Sharing Council of America, more than 70% of 401(k) plans do allow in-service distributions.

Many retirement plan providers today want to allow their employees that are nearing or in retirement the flexibility of having a broader option when it comes to investing for their retirement years. This non-taxable option allows

4 Treasury.gov
5 David Kelly, "Economic and Market Update," *JP Morgan Market Insights*, (March 31, 2019).
6 Christopher Riggs, "Policy at The Forefront: Aligning with Macro Themes & Asset Class Opportunities in 2019" Webcast, *Alphalytics Research*, (April 10, 2019).

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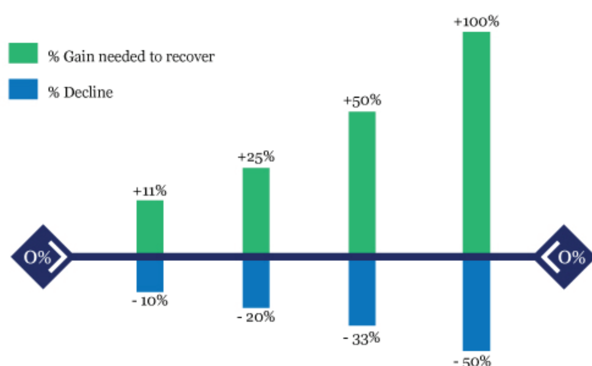
employees to rollover a portion or all their plan assets to an IRA rollover where they can explore numerous investment options outside of their company retirement plan.

Some options may allow for lower investment risk strategies and/or annuities that can provide secure retirement income. According to a survey by the Profit Sharing Council of America, more than 70% of 401(k) plans do allow in-service distributions.[7]

Since retirement plans usually represent a large portion of an employee's net worth, it is important to manage our investment portfolios for risk, as well as growth, due to significant losses being very difficult to overcome, especially for those nearing or in retirement. For example, a 50% portfolio loss would require a 100% gain to just get back even as illustrated in Figure 2. This can be especially painful for people depending on income derived from investment portfolios.

Figure 2. Losses and Gains



For example, if someone took a widely accepted safe withdrawal rate of 4% from a $1,000,000 investment portfolio, the income would be $40,000 per year. But, if that portfolio experienced a 20% loss down to $800,000, then the percentage of withdrawal based on the same $40,000 withdrawal per year would rise to 5% ($40,000 / $800,000), thereby, increasing the chances of depleting the portfolio, and income.

Employees approaching retirement should explore in-service distributions in the context of their overall investment, retirement, and wealth planning when they are available.

Upcoming Wealth Planning Workshops

We hope you can join us for these workshops and feel free to invite a friend.

Seating Limited—Must RSVP by:

1. **Visiting www.SilverStarWealth.com**
2. **Emailing staff@SilverStarWealth.com**
3. **Calling 281-477-3847**

Savvy Social Security Planning: What Baby Boomers Need to Know to Maximize Retirement Income

When: Wednesday, May 22nd at 6:00 – 7:15 pm
Where: Lone Star College-CyFair Library, Rm. 131
9191 Barker-Cypress Road, Cypress, TX 77433

Dinner provided

The Social Security decisions you and your spouse make when you are in your 60s will determine the amount of total income you will receive over your lifetime – including the lifetime of the spouse who lives the longest. Come learn about some little-known rules that can help married couples get more out of the Social Security system.

Learn:

- How your benefit will be affected by the age at which you apply
- How spousal benefits work
- How survivor benefits work
- How divorced-spouse benefits work
- How working affects benefits
- How benefits affect taxes
- 5 factors to consider when deciding to apply for benefits
- When it makes sense to delay benefits—and when it does not
- Innovative strategies for coordinating benefits with your spouse
- How to coordinate Social Security with your other forms of retirement income

7 Plan Sponsor Council of America, *59th Annual Survey*, 2016

In-service 401k distributions cannot be taken until age 59 ½. Taking an in-service distribution may affect your ability to make future contributions to your 401k plan. While 401k assets have broad federal creditor protection, IRAs may not. Fees related to having your own IRA could be more costly than the investment option fees inside your 401k. If you hold highly appreciated company stock your 401k, rolling that stock to an IRA eliminates any ability you may have to take advantage of the Net Unrealized Appreciation Tax treatment. Investors should discuss their specific circumstances and all implications of an in-service rollover qualified advisor before making a rollover decision.

Savvy Tax Planning: How Tax Planning Changes Through Four Stages of Retirement

When: Wednesday, June 5th at 6:00 – 7:15 pm
Where: Juergen's Hall Community Center
26026 Hempstead Rd, Cypress, TX 77429

Dinner provided

In retirement, your tax rate may vary widely over the years based on the timing and order in which you use different sources of money to pay for your living expenses. You want to apply the tax code in an organized and efficient way.

You need a retirement tax strategy that will:

- Identify the types of taxes you will face at various stages
- Address how taxes impact Social Security and Medicare
- Plan when to tap different accounts so you don't overpay taxes

Learn:

- The critical tax question you must answer BEFORE retirement
- The surprises that often make retirement more expensive
- What the Social Security "tax trap" is and how you can avoid it
- Why tapping assets in the wrong order can trigger higher Medicare premiums
- Why you need to manage taxes even before you retire
- The four stages of retirement and important tax actions in each stage, including tricky IRA challenges
- Mistakes to avoid when it comes to your investment portfolio, health care, and estate

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How to Create Sustainable Income in Retirement

When: Tuesday, July 9th at 6:00 – 7:15 pm
Where: Juergen's Hall Community Center
26026 Hempstead Rd, Cypress, TX 77429

Dinner provided

Creating monthly income that lasts throughout your retirement is tricky. A wrong decision could subject you to unnecessary taxes, penalties, and inflation.

In this interactive workshop, you'll learn the strategies that can help you preserve & sustain your retirement income.

Learn:

- Why a retirement income plan is crucial
- How to estimate your retirement income needs
- Where to look for retirement income (6 sources)
- How taxes could affect you in retirement
- The pros & cons of the 4 most popular withdrawal methods
- How to manage retirement withdrawals
- Action plan for building a sustainable retirement income stream

Savvy Caregiving: 4 Keys to Making a Difference in a Family Caregiving

When: Thursday, July 25th at 6:00 – 7:15 pm
Where: Juergen's Hall Community Center
26026 Hempstead Rd, Cypress, TX 77429

Dinner provided

A caregiving plan ultimately impacts all generations of your family. It's never too late to start.

Families need to ask:

- What happens when an elderly parent needs caregiving?
- What's the best way to guarantee our loved ones get the best care possible?
- Do we know who will oversee our parents' care?
- Has anyone discussed how caregiving expenses will be covered?
- Do we have a clear understanding of the personal, residential, medical, legal, and financial issues involved with caregiving?

Learn:

- What every family's number one priority is when creating a caregiving plan
- The most overlooked aspect of family caregiving planning
- Best ways to start the caregiving discussion in your family
- Why now is the best time to start the process
- The critical legal issues that must be addressed quickly
- What caregivers need to know to ensure they can help their family as much as possible
- The key topics covered in a good caregiving plan
- Why no one person can effectively do everything related to a caregiving plan
- The key roles professionals play in helping families respond to caregiving challenges

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Humor Matters

A guy goes in for a job interview and sits down with the boss.
The boss asks him, "What do you think is your worst quality?"
The man says, "I'm probably too honest."
The boss says, "That's not a bad thing, I think being honest is a good quality."
The man replies, "I don't care what you think!"

I am great at multitasking. I can waste time, be unproductive, and procrastinate all at once.

There is a new trend in our office; everyone is putting names on their food. I saw it today, while I was eating a sandwich named Kevin.

A bus station is where a bus stops. A train station is where a train stops. On my desk, I have a work station…

To err is human, to blame it on someone else shows management potential.

I don't mind going to work, it's the 8-hour wait to go home I can't stand.

Source: humorthatworks.com

Please send us your favorite joke and if we use it, we will send you a gift certificate to your favorite restaurant.

Words of Wisdom

"Always plan ahead. It wasn't raining when Noah built the ark." — Richard Cushing, American Prelate of the Roman Catholic Church

If you would like to meet before your next scheduled wealth planning meeting, please contact our office to arrange.

We appreciate the opportunity we have in serving you!

The SilverStar Team—Tim, Andrea, Erica, and Angela

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This material is intended for informational purposes only and is not intended to be a substitute for specific individualized tax or legal advice, as individual situations may vary.
Investing involves risk including the potential loss of principal. No investment strategy, including diversification, asset allocation and rebalancing, can guarantee a profit or protect against loss.
Although the information has been gathered from sources believed to be reliable, it cannot be guaranteed. Federal tax laws are complex and subject to change. Neither SagePoint Financial, Inc., nor its registered representatives, offer tax or legal advice. As with all matters of a tax or legal nature, you should consult with your tax or legal counsel for advice.
This material may contain forward looking statements and projections. There are no guarantees that these results will be achieved. It is our goal to help investors by identifying changing market conditions, however, investors should be aware that no investment advisor can accurately predict all of the changes that may occur in the economy or the stock market.

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See Pages 5-7 for Upcoming Workshops

*Visit **SilverStarWealth.com** for more Details and to RSVP*