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Putting the Smiley Face on a Worried World

As this issue goes to "press," the Group of 20 leading nations have concluded their annual show of diplomatic cool and conviviality in Buenos Aires. Photo ops featured bright smiles, hearty handshakes, and warm embraces. The closing communiqué proffered lofty goals, shared interests, and calls for high-level cooperation. Investors might be forgiven a bit of skepticism.

Perhaps more than at any time in at least a quarter century, the world order feels increasingly *disordered*, and not in a fun way. The United States still throws the greatest economic and military weight, as those factors are traditionally measured. Most recently, the U.S. economy has been a global bright spot. Its workforce continues to grow; wage increases have been more broadly inclusive; incentives for entrepreneurs and innovators are manifest; and an open society continues to draw the creative and aspirational.

But will those attributes continue to carry the force and influence that largely defined and defended the international order in the decades after World War II? The image of the U.S. as a military colossus astride the globe has probably been outdated for years. Projecting power is much more complex in a world of multiple strategic competitors, asymmetric threats, proliferation of destructive technological capabilities, and the interplay of state and non-state actors.

Short of large-scale, existential warfare, today's projections of power tend to be more diffuse, exercised within the confines and peculiarities of a specific region or sphere of influence. Competitors look to meld political, economic, and military influence to their best advantage.

Salient examples include Russia's preoccupation with the eastern European republics it once controlled, as well as China's "Belt and Road" initiative and efforts to expand the reach of its territorial waters in the South China Sea. Then there's the Middle East's tangle of alliances and assailants trying to gain an upper hand in the region. Even the U.S. faces backyard challenges stemming from corrosive disorder in Central America and Venezuela, once one of the hemisphere's richest nations on a per capita basis.

In short, it's an untidy, confusing landscape. Major players offer distinctive, competing brands of political, economic, and social policy. Since the end of the Cold War, the reigning hope has been that a rapidly integrating global economy would smooth rather than sharpen the edges of those differences.

That hope may have been naïve, but it springs eternal. The thrust of business, cultural, and technological networking seems bound to persist (see "Is the World Getting Better" on page 3). And at least today's headlines are dominated by trade disputes rather than armed conflict. It can all be a little unsettling, but markets certainly have weathered more trying circumstances. ■

The New "Global" Looks "Multi-Local"

Given the geopolitical and trade tensions noted in the accompanying article, investors might wonder about the prospects for multi-national corporations that have ridden the globalization wave. Much of the concern over tariffs has focused on the extensive, integrated supply chains that involve component parts as well as finished products crossing multiple national boundaries. The Fall *Client Quarterly* focused on the cross-border sourcing of components and revenue across the U.S., Canada, and Mexico.

Business management is all about adaptation. Capital Group portfolio manager, Jody Jonsson, notes that in the face of trade tensions, evolving market characteristics, and technological enhancements, multi-national companies are increasingly thinking *multi-local*. The idea is to get closer to consumers and buying trends that can vary markedly across different countries and even individual communities.

Bringing production closer to distinct customer populations may be more important as companies try to reduce delivery times and tailor production to contrasting sales trends and product preferences. Advanced data management has become more critical, supporting smart customization of inventory levels, product selection, and promotional initiatives on a more granular, localized basis. Of course, varying customer preferences are not the only factor. Business and financial regulation also vary by national, state, or provincial jurisdiction.

Beyond the current noise of competing trade complaints, multinationals based in highly developed countries may face a rising challenge from aspiring multi-nationals and locally focused competitors being cultivated in major emerging nations such as China, India, and Brazil. The strengths and advantages of established leaders based in the de-

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Is "Goldilocks" Settling In or Restless?

Early indications are that consumers will fund a rousing holiday shopping season on the heels of robust third-quarter economic numbers. Gross domestic product expanded at a 3.5% annual rate, while unemployment has dropped to levels not seen since the late 1960s.

In a November 28th speech on financial system stability, Federal Reserve Chairman Jerome Powell took a little victory lap around those numbers. After all, in terms of the Fed's dual mandate to promote price stability and "maximum" employment, we may be as close to simultaneous success (the proverbial "Goldilocks economy") as at any time in the Fed's long history.

Most observers expect the Federal Reserve Open Market Committee to nudge rates higher again at its December meeting. However, with inflation holding around the Fed's 2% target rate, and with growth *outside* the U.S. looking crimped, rate hikes in 2019 appear less certain.

Investors with longer memories may still see today's rate environment as pretty benign, but a long period of low rates has prompted households to rebuild record levels of total debt. Recent rate increases on mortgage loans and consumer credit are boosting debt servicing costs faster than household disposable income. This is a common feature of late-stage economic expansions, as is the slowing trend in housing and autos, two of the economy's most rate-sensitive sectors.

Corporate debt levels are also high, but it is hardly surprising that companies used a decade of ultra-low rates to move their capital structures in the direction of debt versus equity. Nevertheless, there has been some softening in corporate capital spending, whether due to higher rates, slower growth overseas, trade concerns, or a tight labor market.

This fall has seen stock market volatility driven by day-to-day head-lines, comments from the Fed, quar-terly earnings reports, and presiden-tial tweets. Time will tell whether the current idyll of low infl ation and high employment is merely a mo-ment in time, soon to be shattered by events that can't be perfectly predicted. But for now, there's clear comfort in the numbers. ■

Investment Performance Review	**TOTAL RETURN *** (dividends and capital gains reinvested)			
Selected Mutual Fund Categories *	**--- Annualized through Dec. 6, 2018 ---**			
	1 yr.	***3 yr.***	***5 yr.***	***10 yr.***
Large-Cap Stocks (Blend)	2.4 %	9.3 %	8.7 %	13.3 %
Mid-Cap Stocks (Blend)	- 2.0	7.2	6.3	13.6
Small-Cap Stocks (Blend) †	- 4.5	7.5	5.9	14.0
Foreign Stocks (Large Blend) †	- 9.6	3.0	1.4	7.4
Diversified Emerging Markets †	-10.3	6.7	1.0	8.9
Specialty Natural Resources †	- 8.9	6.4	- 1.3	7.9
Specialty Real Estate †	4.7	6.3	9.1	13.8
Cons. Allocation (30-50% Equity)	- 1.7	4.0	3.3	7.4
Long-Term Bond	- 3.8	3.6	5.0	6.5
World Bond †	- 2.1	2.4	0.9	4.0
High Yield Taxable Bond †	- 0.6	5.4	3.2	10.1
Long-Term Municipal Bond	0.2	2.1	4.0	5.4

* Source: Morningstar. **Past performance is NOT indicative of future results.**

† Small-cap stocks, high-yield (lower rated) bonds, and sector-specific funds may exhibit greater price volatility than the stocks of larger, established companies and/or more broadly diversified funds. Securities of companies based outside the U.S. may be affected by currency fluctuation and/or greater political or social instability.

More Head Room for Retirement Plan Contributions

They don't happen every year, so we want to note *2019*'s increases in the limits for contributions to Individual Retirement Accounts and other tax-advantaged retirement plans. The annual limit for IRA contributions jumps from $5,500 to $6,000, its first increase since 2013. Those over 50 can add another $1,000 under "catch-up" provisions.

For participants in 401(k), 403(b), and most 457 plans, the maximum elective salary deferral amount bumps from $18,500 to $19,000. Catch-up for those over 50 adds $6,000 to that limit. The overall cap on the combined (employee + employer) contribution to these plans rises from $55,000 to $56,000. For defined *benefit* plans, the maximum target benefit rises from $220,000 to $225,000.

The IRS also is adjusting the income ranges that determine how much can be contributed to a Roth IRA. For 2019 that phase-out range shifts up to $122,000-$137,000 of adjusted gross income (AGI) for singles and heads of household, or $193,000-$203,000 for joint filers.

For those who participate in an employer-sponsored plan but might also be able to deduct an IRA contribution, those phase-out ranges ratchet up to the following: $64,000-$74,000 of AGI for singles or $103,000-$123,000 joint. If only one spouse is covered by an employer plan, the other spouse's ability to deduct an IRA contribution doesn't phase out until AGI hits the $193,000-$203,000 range.

One last item: The income caps to qualify for the Saver's Credit are increasing as follows: $64,000 for married couples filing jointly, $48,000 for heads of household, and $32,000 for singles and married individuals filing separately. For those who are just getting started on the long road to retirement, the tax deduction plus the Saver's Credit can provide a nice boost. And here it is, almost Christmas. ■

Building Equity with Your Employer? All in Good Measure

In the formative years of the 401(k) retirement plan revolution, publicly held companies often contributed their own stock to their employees' plan accounts. In some cases, employees also were encouraged to invest their salary deferral contributions into more of that employer's stock.

As 401(k) plans became a more pivotal component of retirement planning, most advisors cautioned clients not to rely so heavily on the prospects of a single company. After all, a key goal of retirement savings is to build financial wherewithal that is *independent* of an employer. Nevertheless, America's equity culture is alive and well. A stake in one's employer can add meaning and motivation to the workday.

Schwab Stock Plan Services recently surveyed 1,000 individuals who receive stock options or restricted stock awards and/or participate in employee stock purchase plans. Equity-based compensation accounted for an average of nearly 30% of those individuals' net worth. Nearly 40% of survey respondents, including 60% of Millennials, listed such compensation as one of their jobs' key attractions.

Those who fall into that Millennial cohort reported that an average of 42% of their net worth is derived from equity-based compensation, compared to 24% and 19% respectively for their Gen-X and Baby Boomer colleagues. Of course, younger workers are still early in the process of wealth building that often spans at least three decades of systematic investing in the public markets and paying down debt. Employer stock awards may tend to take the lead earlier in the game.

The survey also found that about three out of four of those employees also own company stock outside of their equity compensation plans. Their 401(k) retirement accounts represented the largest repository of those holdings.

Nearly two decades ago, a fast-growing company called Enron became a case study in the dangers of over reliance on an employer's stock. Memories of Enron have faded, but the lesson appears to have sunk in. A broader study by the Employee Benefit Research Institute (EBRI) and the Investment Company Institute (ICI) showed only 6% of 401(k) assets invested in company stock as of the end of 2016. That's one of the lowest percentages recorded in the study's database.

For those who may still be tempted to load up on employer stock, the more recent object lesson is probably General Electric, a storied icon of corporate America that has lost nearly 70% of its value in just five years, and more than 80% since late 2007. Broad diversification is still the antidote to those kinds of risks for investors intent on retiring, comfortably and confidently, one of these days. ■

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The New "Global" Looks "Multi-Local"

veloped world have helped pave the way to rapid growth and modernization across emerging markets. But new, nimble competitors steeped in their own culture and tradition could prove to be formidable competitors.

In recent years, large multinationals have seen a distinct trend toward consolidation. Many industries in the MSCI All Country World Index are now dominated by just a few big companies. In the U.S. alone, a 2016 study found that more than 75% of industries had become increasingly concentrated, as measured by antitrust regulators.

Nevertheless, beneath the rarified air of those behemoths, there's a rich, dynamic ecosystem of enterprises capitalizing on the talents and energy of remarkable people *everywhere*. Investors can look to broad diversification and astute management to sweat the details and profit from whichever trends prevail. ■

Is the World Getting Better? One Firm's Data-Driven View

It may not always feel like it, but according to Vanguard Funds chief economist, Joe Davis, the world *is* getting better. He claims that a wealth of data supports that assessment.

Davis' team at Vanguard observed that throughout history, ideas widely shared have triggered more ideas at an accelerating pace. They set out to find a formula – an "ideas multiplier" – that would appear to drive innovation and human creativity. They digested hundreds of books and presentations from the past 20 years and crunched "billions of data points" to derive that leading indicator of the rate of innovation.

That work indicates that the "ideas multiplier" rose from a ratio of about 40:1 in 1980 to 200:1 by 2000, but probably stagnated some since then. Now the global idea exchange appears to be accelerating again, including between the U.S. and China. Davis sees the multiplier approaching *400:1*, suggesting an innovation wave that he believes will be most impactful in the areas of telecommunications, polymers and materials, agriculture and plant science, oncology, and genetics.

Globalization is cited as a prime driver, not just in terms of traded goods and services, but in the flow of ideas and knowledge across firms, societies, and cultures. Globalization has taken its political lumps lately, yet total U.S. trade flows have hit record highs this year. The flow of knowledge and ideas may be more fluid than ever.

Politicians often extoll the virtues of innovation while trying to corral it for the exclusive benefit of their own constituents. According to one large investment firm, the multiplier effect of innovation is all about the sharing. ■

Focusing on Your Best Use of Benefits

In a recent survey by the American Institute of Certified Public Accountants (AICPA), respondents expressed a four-to-one preference for a job with benefits over the same job offering 30% more salary but *no* benefits. Among those holding a job, a 401(k) match and health insurance were rated the most important benefits, followed by paid time off, a pension, and flexible work hours.

No big surprise there, but the survey did show some generational differences. More than half of Baby Boomers cited pension benefits as critical, versus just 16% of Millennials who rated time off, flexible hours, and student loan help more highly. Obviously, each group focuses on its more immediate concerns. Boomers are nearing retirement, while Millennials face work-life balance issues, childcare costs, high student loan balances, new mortgages, etc.

Nevertheless, individuals need to weigh *both* long-term objectives and near-term pressures. The Bureau of Labor Statistics says that employee benefits represent nearly 32% of average worker compensation. Failing to make truly effective use of such a large share of one's compensation would be unfortunate indeed.

Tax treatment is a good starting point. Any benefit that delivers real dollar value *without being counted as taxable income* can help manage expenses *and* build financial security. With a comprehensive picture of *your* benefits, your tax and financial advisors can help sort it all out. ■

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A 2019 Raise for Retirees, and Some Small Offsets

Starting in January, the past year's uptick in general inflation will prompt a boost in Social Security and Supplemental Security Income (SSI) benefits for more than 67 million Americans. A 2.8% cost-of-living adjustment (COLA) should add about $41 monthly to the *average* retiree's Social Security check, $69 for the average couple who are both receiving benefits, and as much as $80 monthly for individuals drawing the maximum benefit.

Most recipients have Medicare Part B premiums automatically deducted from their Social Security benefits, so it was also good news that Part B premiums will rise by just $1.50, to $135.50 per month in 2019. The same *percentage* increase applies to upper income retirees who pay higher Part B premiums. For 2019, the per-person monthly premium is $433.40 for individuals with income in the $160,000-$500,000 range ($320,000-$750,000 for couples) and $460.50 for those whose income exceeds those applicable ranges.

Medicare's annual Part B *deductible* is also edging up 1.1% to $185. But all in all, retirees should still see a *net* pick-up from 2019's COLA which is the largest in eight years. ■

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