FINANCIAL
Insights

MERITAS ADVISORS

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Managing
inversion

The inversion of the so-called yield curve, where short-term government bond returns are higher than long-term ones, has gotten some attention lately, since it has in the past been such a good predictor of recessions. In March of this year, the two-year Treasury yield briefly touched above the yield on 10-year Treasuries, triggering headlines across the financial marketplace.

Inverted yield curves are not ideal for economic growth. They can discourage banks from longer-term lending, and they discourage investors from committing their capital to lending longer-term. (Why accept lower rates on riskier long-term investments when you can get a higher rate on a less-risky short-term one?) And this current yield curve inversion may be telling us what we already know: that a recession is coming, sooner or later. In the past, the U.S. economy has experienced a recession around one in every five years; the current 9-year economic expansion is already overdue to end.

The one entity that can put back some steepness in the yield curve is the Federal Reserve Board, which has expressed concern about the situation already, and which acted by cutting the Fed Funds Rate by 0.25%. That action, and at least one other rate cut expected this year, would bring down the yield of short-term bonds and end the inversion. It would also encourage corporations to borrow to finance long-term projects, giving the economy a bit of a boost—and (though this is not guaranteed) reduce the depth of the inevitable next recession.

-Bob Veres

Source:

https://www.forbes.com/sites/simonmoore/2019/08/12/the-feds-struggle-to-end-yield-curve-inversion/#6b2b6de97b34

The market at a glance

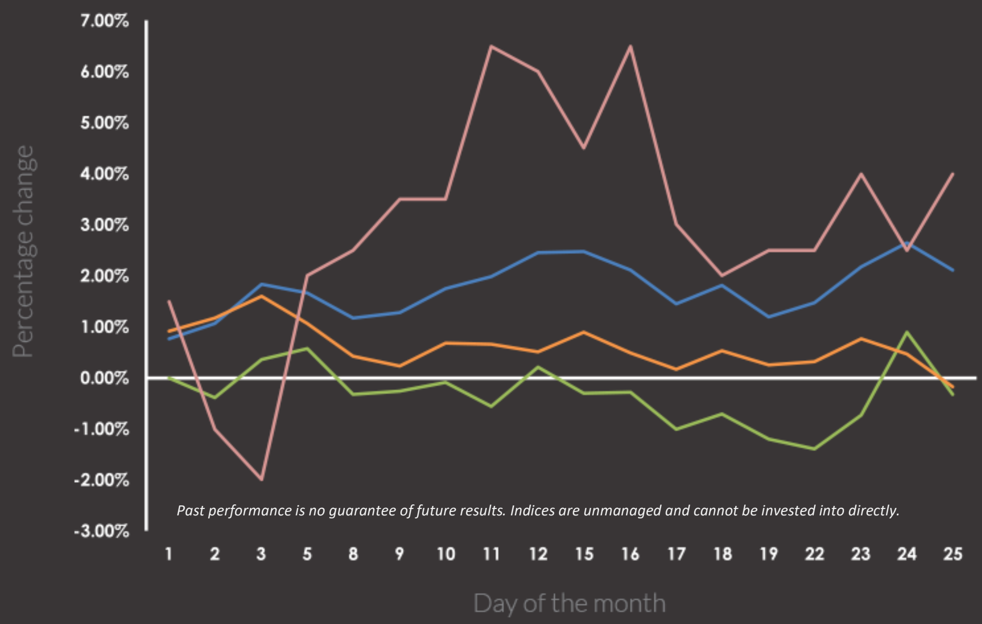
July

U.S. Large Cap
(S&P 500)
2,980.38 (1.31%) ▲

U.S. Mid/Small
(Russell 2000)
1,574.61 (0.51%) ▲

International Large
(NYSE International 100)
5,431.26 (-1.39%) ▼

U.S. Treasuries
(U.S. 10-year Treasury yield rate)
2.02 (1.00%) ▲



Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly.

The market in action

- The Department of Justice has formally agreed on a $26 billion merger between telecommunications companies T-Mobile and Sprint, who are currently the third and fourth-largest U.S. wireless providers, respectively. Shares of both T-Mobile and Sprint reached all-time highs following the news.

- Capital One Financial Corp announced that personal information of nearly 100 million U.S. individuals was obtained in a successful hacking attempt. Information obtained includes close to 140,000 Social Security numbers and 80,000 bank account numbers. Shares of Capital One fell four percent following news of the incident, which is expected to cost between $100 million and $150 million to manage.

- The Federal Trade Commission (FTC) approved a roughly $5 billion settlement with social media company Facebook regarding the company's privacy scandal with political consulting firm Cambridge Analytica. The FTC investigation found that Facebook improperly allowed access to personal data from tens of millions of Facebook users around the time of 2016 U.S. elections. The fine is the largest ever imposed by the FTC on a tech company, beating the previous $22.5 million imposed on Google in 2012.

- American Airlines and United Airlines have extended their grounding periods for the Boeing 737 Max airplane into early November amid concerns that the troubled plane will not be recertified in the near future. Following the October 2018 crash of a 737 Max airplane that killed 157 passengers, Boeing has lost more than $8 billion and seen its shares drop more than 16 percent.

Four options for your 401(k) when changing jobs

Changing jobs is one of the biggest life decisions you can make and doing so presents an important financial decision: What should you do with your former employer's 401(k) plan? There are four options you have and understanding the pros and cons of each will be crucial to find the best fit for your situation.

Keep the funds in the old employer's plan

While this option certainly requires the least amount of effort, not all investors are eligible to leave funds in their former employer's plan. If your vested 401(k) funds amount to less than $5,000, your former employer has the right to require you to remove the money in some fashion. That $5,000 balance can include all of your contributions, all vested employer contributions, and all investment earnings on those funds. Additionally, your former employer may require that you withdraw your funds once you reach the plan's average retirement age.

Outside of being low-effort, keeping funds in your former employer's plan can be beneficial if you need more time to research alternative options, if your new employer's plan requires employees to reach a certain length of employment to enroll, or if you had access to exceptionally good investment options.

Before deciding to let the funds stay put, make sure there are no additional fees associated with the plan for non-current employees and that your investment options remain the same.

Roll the funds into your new employer's plan

It has become far more commonplace for 401(k) plans to accept rollovers from past employers without penalty but there are considerations to make before doing so. First, be sure that you are satisfied with your new job and that you will be there for a reasonable amount of time. Should you decide the new position is not for you, it can be a headache transferring funds around. Second, compare the investment options in your new employer's plan to your old one. Once you have transferred the funds out of the old plan, there is no going back to your previous options.

If you decide to roll over into your new employer's plan, ensure that the transfer is made directly into the new plan – also known as a trustee-to-trustee transfer. This allows your funds to remain tax deferred and avoids the temporary 20 percent penalty that would be applied if you were to cash-out your retirement savings and then deposit them manually into your new employer's plan. Now, you would get that 20 percent back once filing your tax return at the end of the year however, there is no need or benefit to putting up the money in this scenario. To avoid that penalty, make sure that rollover checks are written out directly to the new plan or plan administrator, not yourself. It would be wise to contact your company's plan administrator for details on this process.

The biggest perk of rolling your retirement funds into your new employer's plan is for simplicity's sake. Often, investors can lose focus on the performance of their investments with a former employer. As long as your investment options are comparable at your new position, rolling over into one main account is a good practice.

Transfer the funds into an Individual Retirement Account (IRA)

Coming from a former employer's plan can lead many investors to overlook the option of transferring their funds into an Individual Retirement Account (IRA). An IRA can be set up through nearly any bank or other financial institution and allows a greater range of investment options than the ones chosen by most employer 401(k) plans. While the differences between a 401(k) and an IRA are numerous, the main advantage to your employer's 401(k) is the matching of contributions up to a certain percentage.

It is important to note that you will not receive a match on the funds you transfer from a previous employer, only on the funds you contribute once enrolled in the new plan. Because of this, there is no real reward on choosing to transfer into your employer's plan over an IRA unless the plan's investment options are more attractive. With an IRA, you are in the driver's seat to choose which funds, stocks, or bonds you invest in and there will be more effort required as a result. On the other hand, you may encounter some savings depending on what plan fees are associated with your employer's plan.

Just like rolling over into your new employer's 401(k), you will want to execute a trustee-to-trustee transfer if choose the IRA option. The same fees will apply if you withdraw funds before transferring to your IRA.

Cash out the funds

Lastly, cashing out your funds from your former employer's plan is the option that nearly every financial professional would advise against. The same penalties discussed above that apply to an early withdrawal cannot be made up in your tax return as they can with a 401(k) or IRA transfer and will be a pure loss. Despite the losses, 2013 research from Boston Research Technologies found that just over 30 percent of workers changing jobs will elect to cash-out their retirement funds.

The only two instances where cashing out should become an option is if you are over the age of 55 or need the money for an immediate purpose. If you terminate your employment in or after the calendar year in which you turn 55, you will no longer be subject to an early-withdrawal penalty for that employer's plan. In the case of a former employer's plan that you left before age 55, those funds will still be subject to this penalty. The potential workaround is if these funds were transferred into a post-55 employer's plan.

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