Yanni & Associates
Investment Advisors, LLC

2017 CELEBRATED OUR TENTH YEAR IN BUSINESS!

FOURTH QUARTER – 2017 CLIENT NEWSLETTER

REVIEW OF THE MARKETS:

Index:	4Q17	2017
S&P 500	6.64%	21.83%
S&P Mid-Cap	6.25%	16.24%
S&P Small Cap	3.96%	13.23%
Morgan Stanley's EAFE (International Stocks)	4.23%	25.03%
Barclay's US Aggregate (Bonds)	0.39%	3.54%

ECONOMY & MARKETS:

Overall, the economy continues to remain very strong. The final estimate for third quarter GDP came in at a healthy 3.2%. While the December unemployment report had only 148,000 jobs created, which was well below 190,000 consensus, the actual unemployment rate remained at 4.1%. Overall, the unemployment trend remains low and is another sign of a healthy economy. Wage growth picked up slightly to 2.5%. Further, economic projections have picked up slightly due to the tax cuts.

The Fed increased interest rates again in December for the third time last year. Economists and traders are mixed with their expectations arriving somewhere between 2-3 hikes for 2018. We will also have a new Fed chair, Jerome Powell, starting in February. The early news on Mr. Powell is that he will attempt to maintain a fairly accommodative approach. As stated in the past newsletter, the Fed is "shrinking its balance sheet" by permitting its bond holdings to mature. Beginning in October 2017, the Fed started allowing up to $10 billion of securities to mature each month, which is expected to rise to $20 billion starting in January. While this "balance sheet reduction" was the main headline for weeks, it's more of an after-thought at this point.

As for the stock market, 2017 was a spectacular year. While 2018 has started out on the same path, we continue to attempt to keep client expectations realistic of long-term historical averages. Further, we are in the longest period of S&P 500 history without a greater than 3% correction, with no move of that size since November 4, 2016. It is likely we will see a stock market correction in 2018, but unlikely it will be a steep bear market. Valuations for the year have already started on the high side. Further, the positive market was not limited to the United States in 2017. For the first time in history, global stocks (using the MSCI AC World Index) were up every single month in 2017. Risks for 2018 include higher volatility, higher inflation, and more central bank tightening than expected.

YAIA Firm Update: We recently hired a new Investment Analyst – **Komal Motwani**. She passed the CFP exam in March, 2015 and last worked as a Financial Associate at another Investment Firm in Pittsburgh. She and her husband are originally from India. She has also obtained her Bachelor's Degree and Masters of Science in Banking & Finance. She will be providing internal support for the investment analytics and may attend client meetings with me as well.

PA Department of Banking & Securities update: First, Matt attended the all-day, on-site Compliance Seminar in Harrisburg in late October. It was an excellent opportunity to talk with the regulators on a variety of compliance issues and to solidify contacts at the State for when questions arise. Overall, there are no major topics to convey to clients. But, we did end up slightly modifying a few of our own internal policies to ensure they continue to remain compliant with regulations. Second and coincidently, the State also conducted another routine on-site audit of our Company. There were about 5-10 minor items to which the Examiner asked us to change (and of course, we handled them immediately). But, once again no major deficiencies were found in what was now our second routine audit. It is normal for the regulators to audit investment firms.

New Tax Cut Rules: While this new tax cut brings about many new changes, we wanted to outline one that has direct impact on our business. This new tax cut now permits 529 plan withdrawals to be used in a new way whereby up to $10,000 per child per year towards a public, private or religious elementary or secondary school. Previously and what still remains is that 529 plan withdrawals can be used in an unlimited disbursement amount towards "higher education".

Common Tax Forms to expect to receive after year end:

Each year, we receive questions for the explanation of the individual tax forms, why forms are sometimes revised, the timing of receiving them, and what taxable items are not included on the forms. We are dedicating this page to "Tax forms" and will divide it into two sections: outlining the most common tax forms & answering the most common tax-form related questions.

Most common tax forms:

1. **1099** – A 1099 is the most common tax form and is produced on non-retirement accounts (individual accounts, joint accounts, most Trusts, and Transfer-on-Death Accounts). The 1099 will summarize the prior calendar year's dividends (1099-DIV), interest (1099-INT), capital gains (see below), and others. The other reportable items may include foreign taxes paid, margin interest charged, and others.
    a. Most commonly dividends can be categorized into Ordinary Dividends and Qualified Dividends. Qualified dividends are held over a year and possibly taxed at a lower rate.
    b. Interest can sometimes be taxable at the federal level, the state level, neither, or both.
    c. Capital gains can be reported as a "realized gain" or a "distribution". "Realized gains" are the active buying and selling what YAIA does for clients throughout the year. Normally, we actually attempt to realize losses in an effort to reduce gains or enable clients to use excess losses to offset other areas of their taxes. Consequently, capital gain "distributions" are generated by the mutual fund companies and often reported on a single date in the fourth quarter (often termed "pass-through gains"). We commonly get questions **on days mutual funds pay distributions** as share prices often fall on one day, then the reinvested shares show up on the second day (it's very misleading). Both types of capital gains are internally thoroughly tracked. To make matters more confusing, capital gains ("realized gains" and "distributions") can also be considered short-term or long-term. Further, the tax rates may be different if the gain is generated as a "realized" short-term, "realized" long-term, short-term "distribution", or long-term "distribution".

2. **1099R** – The 1099R simply shows distributions from retirement accounts (mainly Traditional IRAs, Roth IRAs, and Inherited IRAs). This simplified form is typically one page and will also outline any federal or state taxes withheld. Further, "Box 7" shows a distribution code that categorizes the distribution in a certain manner for the IRS.

3. **Year-end Gain / Loss Report** – This is another form generated by retirement accounts. In most instances, it is meaningless and thus, not worth attempting to explain. However, it still should be given to your Accountant.

4. **5498** – This tax form outlines IRA contributions made for the prior year. Technically, you are able to contribute up until April 15th of the following year to make a contribution to an IRA for the prior year. Thus, the tax form 5498 is not generated by custodians **until the following May** (most likely, after you have filed your taxes in April). Don't be confused or concerned if you get a tax form 5498; just give it to your Accountant.

Most common tax-form related questions:

1. *Which forms should I give to my Accountant?* – ALL OF THEM!

2. *Why are tax forms sometimes revised?* - Tax form revisions, most commonly on the 1099, are mainly due to the mutual fund companies changing their data. For example, if a mutual fund company slightly changes its capital gains "distribution" amount, that updated information is sent to Schwab, whereby a revised 1099 is now required.

3. *When should we file our taxes?* – Due to potential revisions to 1099s, I guide clients to meet with their Accountants early in the tax season, but not to actually have their Accountant to file their taxes until the middle of March.

4. *What items are not included on the forms that we need to give to our Accountant?*
    a. IRA contributions – As stated above, the 5498 form is not generated until May and thus, you will not have this form to give to your Accountant if you file your taxes prior to April 15th.
    b. 529 plan contributions – Custodians for 529 plans are not required to provide documentation for contributions, only for withdrawals. Further, we advise to keep all education expenses and invoices that can be matched up against 529 plan withdrawals (in the event you are audited).

Please note that these are all general definitions to some, but not all tax forms and a variety of related questions. For further clarification, please discuss these matters with your Accountant. In addition, when signing up for E-delivery at Schwab, we do recommend maintaining the tax forms as the only category that still comes via the mail; having only the tax forms come by mail make it a lot easier to recognize the importance of these documents.