MARKET & LEGAL UPDATE

March 2022 REVIEW

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"Despite War, Record High Inflation and Rising Rates, Markets Advance"

Global stock markets finished down for the quarter, but posted the first positive month of 2022, despite the war inflicted by Putin, record high inflation, lingering COVID cases and supply chain issues, and the first rate increase since 2018 by the Federal Reserve. The Federal Reserve Bank raised rates by 0.25% during the month and the markets have priced in 6 more separate rate hikes, including one or more of 0.50% increase for the remainder of 2022. At the end of last year expectations were for 3 rate hikes this year. The planned rate hikes would mark the most aggressive path in 40 years. The S&P 500 Index was up 3.4% for the month, but down -4.6% for the quarter, marking the first time in two years the index was down for a quarter. Bond yields have risen sharply in 2022 (e.g., 10-year Treasury Yield rose to 2.3% from 1.5% at the end of 2021, and as rates rise, bond prices fall, with the Bloomberg U.S. Aggregate Bond Index down -5.9% for the quarter.

The unprecedented sanctions by allied countries in response to Russia's aggression for its baseless war against Ukraine have further exacerbated strained supply chains and caused energy prices to sharply rise. According to a NATO estimate on March 30th, between 7,000 to 15,000 Russian troops have died and Russia has about 40,000 total losses, which includes captures and troops that have deserted the military. Ukraine troop losses are in the thousands as well and, in addition, more than 4 million Ukrainian citizens have been forced to flee the country according to the United Nations. The exodus is the largest movement of people in Europe since World War II. The Office of the United Nations High Commissioner for Human Rights verified a total of 1,189 civilian deaths as of March 29th, including 108 children. Diplomatic talks were held on March 29th in Istanbul, Turkey with negotiators for both countries present. During negotiations, Ukraine proposed a neutral status between NATO and Russia, but requested a security guarantee by the U.S., U.K., France, Turkey, Germany, Canada, Poland, and Israel which would ask the countries to respond to a violation of its sovereignty. Russia was to deescalate around Kyiv during the talks, but instead continued to strike targets in the capital.

Market Return Indexes	March 2022	YTD 2022
Dow Jones Industrial Average	2.5%	-4.1%
S&P 500	3.7%	-4.6%
NASDAQ (price change)	3.4%	-9.1%
MSCI Eur. Australasia Far East (EAFE)	0.6%	-5.9%
MSCI Emerging Markets	-2.3%	-7.0%
Bloomberg High Yield	-1.2%	-4.8 %
Bloomberg U.S. Aggregate Bond	-2.8%	-5.9%
Yield Data	**March 2022**	**February 2022**
U.S. 10-Year Treasury Yield	2.32%	1.83%

In addition to energy prices spiking due to the invasion, wheat and fertilizer prices have doubled and increased by 75%, respectively. Russia and Ukraine account for 30% of global wheat exports and over 25% of fertilizer exports. Agriculture is the largest part of Ukraine's economy, accounting for 14% of its GDP in the third quarter of 2021. As such, Ukraine is often referred to the breadbasket of Europe. It is inspiring that many of the farmers in Ukraine continue to work in the face of adversity and war. Prices for uranium, a critical fuel for nuclear-powered plants, have also spiked as Russian uranium enrichment accounts for about 35% of the global market according to UxC and nuclear power provides 20% of U.S. electricity generation and 10% of the global amount The disruption in supply chains and sharp increase in commodities prices could continue to push inflation higher.

The consumer price index (CPI) measured 7.9% in February, the highest level in 40 years and core Personal Consumption Expenditures (PCE) prices came in at 5.4% (slightly below 5.5% economic forecasts). The Federal Reserve sets interest rate policy through two key measures of inflation and unemployment levels. Unemployment fell to 3.6% with 431,000 jobs added in March, indicating the economy remains strong. Federal Reserve Chairman Powell has a delicate balancing act to raise rates to curb inflation, but not cause economic activity to slow too much to trigger a recession. According to Neil Shearing, chief economist at Capital Economics, out of 16 times since the late 1970s when Central Banks in the U.S., U.K., and Eurozone raised rates, 13 ended in recession. The Bank of England raised rates for the third time in three months in March and provided guidance that it plans to continue raising rates. The European Central Bank is expected to raise rates in 2023. The yield curve briefly inverted during the month with 2-year U.S. Treasury yields higher than 10-year Treasuries. In the past, a yield curve inversion preceded many recessions. The yield curve last inverted in 2019 and a recession briefly occurred in 2020, however that was due in large part to COVID.

Due to the war and lingering effects of Omicron, global economic growth forecasts for 2022 were revised downward. The U.S. was expected to grow by 3.7% and Europe by 4.3% before the invasion, but those measures were revised downward by 0.9% and 1.4%, respectively. In addition, in late March, China imposed a strict lockdown of its largest city, Shanghai, a city of 25 million citizens. Logistics companies including Geodis and Maersk have warned of further delays and rising costs amid the two-stage planned COVID-19 lockdown by Shanghai, which is expected to last for less than two weeks.

Despite numerous headwinds, the markets provided some signals during March that economic growth, the job market, and corporate earnings could remain robust for 2022. Higher inflation certainly reduces consumer spending and corporate earnings, particularly if companies are unable to pass the added cost onto consumers. However, one catalyst to offset some of the headwinds in increased productivity in both the manufacturing and service sectors. Private nonresidential business investment grew by 7.4% in 2021, the fastest pace since 2012. Manufacturing firms are expected to raise capital expenditures by 7.7% and service companies by 10.3% in 2022, according to the Institute for Supply Management. The expenditures could raise productivity and create a more productive economy that produces more goods and services with the same level of workers, thus mitigating some inflationary pressures. Additionally, corporate earnings remain positive and S&P 500 companies' earnings growth are expected to be a modest 5-6% during the first quarter of 2022. Companies start reporting earnings in mid-April which will provide some insight into market performance for the second quarter of 2022. Of course, peace in Ukraine would be welcomed by the markets, but more importantly, for its citizens and affected families.

LEGAL UPDATE | IRS ISSUES NEW PROPOSED REGULATIONS FOR REQUIRED MINIMUM DISTRIBUTIONS

On February 24, 2022, the IRS issued proposed regulations under Code Section 401(a)(9), which reflect the changes made by the Setting Every Community Up for Retirement Enhancement Act of 2019 ("SECURE Act"). These regulations impact the calculation of required minimum distributions ("RMDs") from qualified plans and IRAs.

Changes Affecting All Plans and IRAs

- The proposed regulations are effective for distributions for calendar years beginning on and after January 1, 2022.
- The SECURE Act changed the definition of the "required beginning date" (RBD) age from 70½ to 72 for participants born on or after July 1, 1949, and is now reflected in the proposed regulations.
- These regulations do not extend the deadline for plan amendments to reflect these changes. For most plans, amendments are due by the end of the 2022 plan year.

Changes Affecting Defined Contribution Plans

For defined contribution plans, the guidance includes new rules applicable to beneficiaries and timing of payments. RMD rules continue to vary depending on whether the participant dies before or after his or her RBD.

New Rules Regarding RMD Payment Timing. When a participant dies before his or her RBD, the timing of the RMD payments depends on the beneficiary classification:

Eligible Designated Beneficiary (EDB)

- An "EDB" is the surviving spouse, the participant's child who has not reached the age of majority (at the time of the participant's death), a disabled or chronically ill beneficiary, or a beneficiary who is not more than 10 years younger than the participant.
- At the EDB's election, payment of the distributable amount can be made (a) beginning in the year after the participant's death over the beneficiary's lifetime, or (b) by the end of the calendar year including the 10th anniversary of the participant's death.

Designated Beneficiary

- A "designated beneficiary" must be an individual.
- The designated beneficiary must receive the entire distributable amount by the end of the calendar year including the 10th anniversary of the participant's death.

Nondesignated Beneficiary

- If the participant has a beneficiary that is not an individual, such as a trust that is not a "see-through" trust, the beneficiary is a "nondesignated beneficiary."
- The nondesignated beneficiary must receive the entire distributable amount by the end of the calendar year including the 5th anniversary of the participant's death.

When a participant dies after his or her RBD, the timing of the RMD payments again depend on the beneficiary classification but the timing is complicated by the addition of the "at least as rapidly" rule. RMDs must continue to be paid based on the longer of the participant's life expectancy or the designated beneficiary's life expectancy. EDBs generally may continue to receive the RMDs based on the applicable life expectancy, however, in some cases the entire benefit of the participant must be paid out as follows:

- If an EDB dies, then the beneficiary of the EDB must receive all remaining benefit amounts by end of the calendar year including the 10th anniversary of the EDB's death.
- If the EDB was older than the participant, the entire amount of the benefit must be paid out by the calendar year when the EDB's remaining life expectancy is less than or equal to one.
- If the EDB is a minor child, the entire amount of the benefit must be paid out by the 10th calendar year following the year the child reaches age 21.

Changes Affecting Defined Benefit Plans

The proposed regulations make the following changes to the existing rules for defined benefit plans:

- Although the new required beginning date is now age 72, the proposed regulations do not change when actuarial increases must apply. Actuarial increases continue to apply at age 70½. The proposed regulations clarify that this adjustment does not apply to a 5% owner.
- Plan sponsors are still permitted to use a uniform RBD based only on age (that is, not dependent on retirement status), regardless of 5% owner status.
- New rules expand the exceptions to the "non-increasing annuity payment" rule for resumption of benefits following certain suspensions of benefits.
- New rules modify the exceptions under which annuity contract payments from insurance companies are permitted to increase (a) by providing that the total value is calculated as of the date on which the contract is annuitized as opposed to the date annuity payments commence, and (b) by providing three more examples of permissible increases: (i) for a final payment upon death that does not exceed the excess of the total value being annuitized over the total payments before the participant's death,(ii) a short-term acceleration of payments of up to one year, and (iii) acceleration to meet these new RMD rules.
- New rules require that the annuity contract must be issued by an insurance company licensed in the jurisdiction where the annuity is sold.
- New rules also provide some relief from RMD compliance where the RMD beneficiary payments are restricted from materially underfunded plans under Code Section 436.

What Plan Sponsors Should Do

Plan amendments to reflect the new RMD rules under the SECURE Act must be adopted on or before the last day of the 2022 plan year. Compliance with these rules will impact communications, systems and plan documentation. Plan sponsors are encouraged to discuss the administrative process of RMDs with their recordkeepers to make sure the plan's administration is consistent with the plan document.

If you have any questions regarding the new RMD rules, the proposed regulations or necessary plan amendments, please contact your USI Consulting Group representative.

How USI Consulting Group Can Help

The USI Consulting Group (USICG) team is happy to assist plan sponsors with all retirement plan compliance matters and changes in the market, including those discussed here, to help you mitigate risk and financial impact to your organization. Questions? Contact your USICG representative, visit our Contact Us page or reach out to us directly at information@usicg.com.

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