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## 4th Quarter 2009

### Weigh Your Retirement Options and Plan

One casualty of the recent bear markets has been many people's faith in their ability to retire. Retirement plans based on what once seemed a reasonable 10% annual rate of appreciation have instead seen 10 years of minimal, if any, real appreciation in their equity investments. The question now is what should you do with respect to planning for retirement?

**The first step is simply to spend less and save as much as you can.**

If the market experiences an average return of 5.5% (which looks quite rosy at this point), building a nest egg of \$1 million will take either hefty investments now, or a longer period until retirement. Each year you delay saving, the more you will need to set aside.

Years to Fund	Planned Payment (Per Year)	Total Payments	Total Earnings @ 5.5%	Accumulated Value
5	\$169,835.48	\$849,177.42	\$150,822.58	\$1 million
10	\$73,618.74	\$736,187.38	\$263,812.62	\$1 million
15	\$42,299.14	\$634,487.17	\$365,512.83	\$1 million
20	\$27,184.20	\$543,683.98	\$456,316.02	\$1 million
25	\$18,530.19	\$463,254.81	\$536,745.19	\$1 million
30	\$13,085.68	\$392,570.32	\$607,429.68	\$1 million
35	\$9,454.91	\$330,921.74	\$669,078.26	\$1 million
40	\$6,938.71	\$277,548.56	\$722,451.44	\$1 million

Source: [www.72.net/CostOfWaiting](http://www.72.net/CostOfWaiting)

**Remember that risk is very real when you invest your savings.**

Before working with a financial adviser or money manager, ask what they will do to protect your savings in the event of another market downturn, because there will be one. If they don't have a plan that you can buy into, don't invest.

**Consider alternative retirement goals.**

- Work longer, which will increase your Social Security payments and give your retirement investments more time to grow. IRS regulations allow participants in a 401(k) and other workplace retirement plans to delay their minimum distributions well beyond 70.5 as long as they continue to work.
- Phase in your retirement. Gradually reduce your work hours until you can afford to fully retire.
- Plan to work part-time in retirement. But be careful because this will impact the amount you receive from Social Security if you opt for early retirement.

**Hit reset on your lifestyle.**

A smaller house, renting a vacation home instead of owning, cutting back on club memberships... these are all ways to free up funds that you can use for retirement. Look for ways to minimize monthly expenses such as property maintenance, loan payments etc. Even when expenses seem small individually, added together they become real money. If you are assisting younger members of your family with their expenses, this may be the time to cut the strings.

Retirement is not beyond your reach. In fact, it may be much more feasible than you think. The important thing is to not wait until the last minute to start planning. The earlier you put a plan in place the greater your chances of succeeding. For help with achieving your retirement goals, let's talk.

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*“fund managers who invest based on macroeconomic trends — and are willing to adjust their portfolios as those trends change — are the managers most likely to add value for investors.”*

## Benefits of Active Management Acknowledged

The last few months have seen the publication of several studies that are restoring a bit of sanity to what passes for investing knowledge. For years, investors have been told that they can't beat the market so there is no use in trying. *The “right” investment is an index based mutual fund with the lowest expense ratios* maintained many investment “authorities.”

To many of us, this seemed equivalent to saying all education/cars/etc. are the same, so there's no reason to purchase anything but the very cheapest. Now recognition is beginning to filter out that perhaps there is a difference in the results of the truly good investors.

From the New York University Stern School of Business comes a study released in November 2009 finding that “fund managers who invest based on macroeconomic trends — and are willing to adjust their portfolios as those trends change — are the managers most likely to add value for investors.”

The study identified the top 25% of actively managed equity mutual funds by analyzing data from January 1980 through December 2008. This group showed proficiency in their ability to select stocks during expansionary economic periods as well as recessions.

D. Bruce Johnsen, a professor of law at George Mason University in Arlington, Va., has published a recent study, *Myths About Mutual Fund Fees: Economic Insights on Jones v. Harris* in which he concludes: “Lower advisory fees don't necessarily benefit investors.” What matters is not how much the fees are, but how the fund performs.

A study conducted by Robert Isbitts, chief investment officer with Emerald Asset Advisors, of 34 categories of mutual funds found that the ten best performers were also among the most expensive. The results of the study are summarized below:

1. *Of the 34 mutual fund categories studied, the 10 that produced the highest 10-year alpha had an average expense ratio rank of 28, placing them among the most expensive.*
2. *The top 10 alpha rankings (alpha is a measurement of the value added by the manager beyond the gains of the market) were dominated by small and midcap fund categories. These managers in general were able to maneuver better than their large-cap competitors, who could not distinguish themselves from investing in an index.*
3. *World allocation funds ranked eighth in alpha (and 29th in cost). This is likely due to a combination of manager skill in this area and the long slide in the U.S. dollar, which has lifted non-U.S. investments.*
4. *The long-short category of mutual funds ranked seventh in alpha, despite being the highest-cost fund group by a wide margin.*

“If you want skill, don't be afraid to pay for it,” concludes Isbitts.

<sup>1</sup> “Market timing trumps buy-and-hold strategies during market swings, says NYU study” by David Hoffman, [InvestmentNews](#), November 10, 2009

<sup>2</sup> “Mutual fund fees fight may be much ado about nothing,” Sheryl Nance-Nash, [Daily Finance](#), an AOL money and investing site. Nov 5, 2009. <http://www.dailyfinance.com/2009/11/05/mutual-fund-fees-fight-may-be-much-ado-about-nothing/>

<sup>3</sup> “Dispel the low-cost mutual fund mixup,” [Boomer Market Adviser](#), Published 11/1/2008, <http://www.boomermarketadviser.com/Issues/2008/11/Pages/Dispel-the-low-cost-mutual-fund-mixup.aspx>

## Request Annual Free Credit Report

The Fair Credit Reporting Act guarantees individuals access to a free credit report from each of the three nationwide reporting agencies — Experian, Equifax, and TransUnion — every 12 months. Make a practice of ordering a free report each year. You want to make certain no accounts have been opened in your name that you haven't authorized. And, you want to make certain information on the report is accurate.



The U.S. Federal Trade Commission authorized source to request your free report is **Annual-CreditReport.com**, or call **1-877-322-8228**, or fill out the **Annual Credit Report Request** form and mail it to Annual Credit Report Request Service, P.O. Box 105281, Atlanta, GA 30348-5281. You can request all three reports at once or order one report at a time. By requesting the reports separately, you can monitor your credit more frequently throughout the year.

*Request Annual Free Credit Report continued*

Be wary of ordering free reports from other sources. Because you are supplying your social security number and personal data with the request you don't want to take chances. You also don't want to end up with charges for services or information. The credit reports must be provided FREE from the major reporting agencies. That doesn't mean they won't try to sell you on credit monitoring services, credit scores, etc., but you don't need to pay anything to access your reports once a year.

You are also entitled to a free report if you are refused credit, are currently unemployed and looking for a job, or are a victim of identity theft.

### **Investing in Gold ... Taxes and Other Cautions**

With gold prices exceeding \$1,200 per ounce in December, many investors are looking for ways to add exposure to gold to their portfolios. But investing in gold comes with its share of hazards, from taxes to volatility, that investors need to be aware of before, not after, they invest.

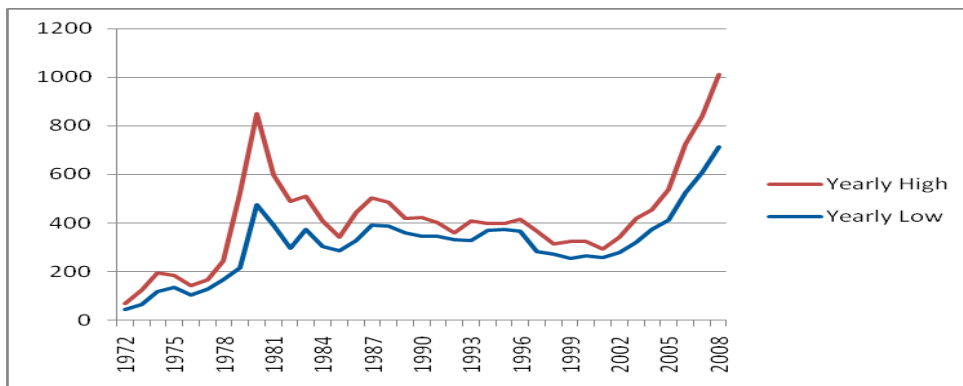
With respect to taxes, gold is considered a collectable and gains on gold held for over one year are currently taxed at 28% versus 10% and 15% for equities (in 2011, capital gains rates will revert to pre-2003 rates, generally 20%). Short-term gains from buying and selling gold, like short-term gains on equities, are taxed at the individual's personal income tax level.

Collectible gold includes gold coins and bullion **as well as ETFs and other investments** that hold actual gold in their portfolios. Buy gold directly or indirectly and it becomes a collectible. If you choose to hold your own gold, you have additional issues of storage and security.

One way to get around the collectible issue is to buy stock in companies that mine gold or provide services to gold mining companies. But this adds new variables to the value of the investment including management abilities, quality of reserves, extraction costs, etc.

Volatility is another consideration. Gold is gold. It does not generate income or increase in value because of the growth of the underlying asset. Its value reflects the emotions of the market, with its rise generally signaling very nervous markets and at the worst the potential for a major market crash. As a result, gold is more volatile when the price is rallying. With equities the reverse is typically true. This volatility is reflected in the spread between high and low prices each year in the chart below.

**Historical London Spot Gold Prices**



If you had invested in gold at its last high in 1980, 25 years would have gone by before it came back to its earlier high. This is why professional traders consider gold a short-term investment. With that said, adding gold to a portfolio needs to be done as an active investment strategy with the awareness that gold will have to outperform other assets to make up for its high tax rate.



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It's been an unbelievable year in the financial world. We saw the S&P plunge to 667 in March, and then rise over 60% from that low as the economy moved away from the precipice and started to recover. Tried-and-true lessons were brought to light yet again, including knowing your risk tolerance, understanding what "long term" really means, and the ongoing benefits of active asset management and diversification.

Heading into 2010, we see an improving economic environment and remain optimistic on the market, although risks remain. Weakness in labor markets has continued around the globe, but there have been some signs of stabilization in U.S. weekly job claims. Further signs of improvement in the housing market also emerged. However, orders for durable goods weakened again, causing economists to debate the depth of the recovery in manufacturing. Third quarter U.S. gross domestic product figures were revised downward by 70 basis points.

Oil prices were roughly flat over the month, with WTI Cushing crude oil prices ending around \$77 per barrel, despite gains in other commodity markets. A rebound in the dollar against some currencies during the month helped suppress oil prices (a higher dollar would tend to reduce demand for oil, which is denominated in dollars, by making it more expensive in other currency terms). Corporate bonds and high-yield debt are still attractive versus U.S. Treasuries, although yields have fallen to levels that prevailed before the fall of Lehman Brothers.

The U.S. economy has bounced well off the bottom and continues to improve, although not in a straight line. The growing questions are whether growth can be sustained when external fiscal and monetary stimulus is scaled back, and how much of a factor will inflation be in the future. Needless to say, we'll be keeping a close eye on things in 2010!



### 2010 Window Opens for Roth IRA Conversions

To convert existing IRA funds to a Roth IRA, taxes must be paid on any pre-tax IRA contributions, but there's another benefit to converting in 2010. For funds converted in 2010, the tax liability can be paid one half in tax year 2011 and half in tax year 2012. Convert in 2011, and taxes will be due on the full conversion amount for tax year 2011.

Before you opt to convert to a Roth, however, you need to run the numbers. Although all earnings from a Roth IRA are exempt from federal income taxes, by paying taxes on all contributions in advance you lose the earning power of those funds. You may also be paying taxes at a higher rate than you might if you held your IRA into retirement when your tax rate might be less.

Typically, a Roth conversion will make the most sense for individuals with years to go before they retire.

The closer you are to retirement, the less value a Roth might have unless your goal is to pass on the IRA to your heirs. There are no distributions required from a Roth IRA during your lifetime and by converting to a Roth and paying the necessary taxes, you will shrink your taxable estate. That could mean bequeathing a pool of income-tax-free money to your heirs.

If you have an IRA in which after-tax contributions have been made, you only need to pay taxes on accumulated earnings to convert to a Roth IRA.

## Watch Out for this Advice!

The fallout from the investment scandals of the past two years usually takes the form of a list of guidelines for investors such as the following:

**Do your homework when picking a financial adviser.**

**Ask tough questions to identify potential conflicts of interests.**

**Ask tough questions about risk factors, too.**

**Check whether the fund manager's interests are aligned with yours.**

**Check whether the fund firm's interests are aligned with yours.**

Before you take these statements to heart, you need to face one very important fact. **Crooks lie. The better the crook, typically the better the lies.** Asking the questions above does you no good unless you have a means of verifying whether or not the answers are true.

In place of the advice above, we offer the following:

- Never write an investment check to an individual unless you are purchasing real property, such as real estate or gold coins and even then use a financial intermediary to assure that you receive legal possession of the asset.
- Financial investment checks should be written only to legal entities, i.e. brokerage firms, trust companies, investment companies, etc. that are legally organized under the laws of the state. If you have any questions, verify with the state of record.
- Have your assets held/custodied at an independent custodian (brokerage firm, trust company, mutual fund company, annuity issuer) where the investment manager or adviser has the ability to direct how your funds are invested but does not have access to those funds.
- Receive and review monthly statements from the custodian, not just your financial adviser. Ideally have online access to your account so you can verify where your assets are invested at any time.
- If you are investing directly with a hedge fund, limited partnership or pooled investment structure, your risks increase. You need to understand that you have given up regulatory oversight. The compliance burden is on you.
- You need to have some means of verifying that statements from the company are true and that verification needs to be more than once a year. Who is the auditor? What is their relationship to the firm? How often are portfolios reviewed? Request a copy of the latest audit.

How are assets held within the portfolio legally titled? Verify with the state of record that the assets are indeed held under that entity. It's a matter of public record. How are the investors' assets protected in the event of a lawsuit. If there a means of checking the manager's statements consider it a red flag. It's not like asking if their interests align with yours. It's saying "prove it."

A good crook is a good liar. Check the facts. Know where your money is.



## **4th Quarter Newsletter**

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