Financial Briefs

Guidance For Every Stage of Life

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Hi Everyone,

The articles in this issue address a variety of topics -- from the Federal Reserve's actions, to reducing debt and beyond.

They're all designed to prompt you to think about your finances. Remember that good plans shape good decisions.

Give us a call if we can help with your planning issues.

Warm regards,
Deidra

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The Fed's Great Unwind and Your Portfolio

After more than five years of unprecedented support for the economy, the Federal Reserve Board has begun to reduce its purchases of bonds. And though the Fed has said interest rates may stay low even after unemployment has fallen to 6.5%, higher rates increasingly seem to be a question of timing. Both of those actions can affect your portfolio.

Bond purchases: the tale of the taper

In the wake of the 2008 credit crisis, the Fed's purchases of Treasury and mortgage-backed bonds helped keep the bond market afloat, supplying demand for debt instruments when other buyers were hesitant. Fewer purchases by one of the bond markets' biggest customers in recent years could mean lower total overall demand for debt instruments. Since reduced demand for anything often leads to lower prices, that could hurt the value of your bond holdings.

On the other hand, retiring baby boomers will need to start generating more income from their portfolios, and they're unlikely to abandon income-producing investments completely. Those boomers could help replace some of the lost demand from the Fed. Also, the Fed's planned retreat from the bond-buying business has roiled overseas markets in recent months; when that kind of uncertainty hits, global investors often seek refuge in U.S. debt.

Rising interest rates

When interest rates begin to rise, investors will face falling bond prices, and longer-term bonds typically feel the impact the most. Bond buyers become reluctant to tie up their money for longer periods because they foresee higher yields in the future. The later a bond's maturity date, the greater the risk that its yield will eventually be superseded by that of newer bonds. As demand drops and yields increase to attract purchasers, prices fall.

There are various ways to manage that impact. You can hold individual bonds to maturity; you would suffer no loss of principal unless the borrower defaults. Bond investments also can be laddered. This involves buying a portfolio of bonds with varying maturities; for example, a five-bond portfolio might be structured so that one of the five matures each year for the next five years. As each bond matures, it can be reinvested in an instrument that carries a higher yield.

If you own a bond fund, you can check the average maturity of the fund's holdings, or the fund's average duration, which takes into account the value of interest payments and will generally be shorter than the average maturity. The longer a fund's duration, the more sensitive it may be to interest rate changes. ***Note:*** *All investing involves risk, including the loss of principal, and your shares may be worth more or less than you paid for them when you sell. Before investing in a mutual fund, carefully consider its investment objective, risks, fees, and expenses, which are outlined in the prospectus available from the fund. Read it carefully before investing.*

For those who've been diligent about saving, or who have kept a substantial portion of their investments in cash equivalents such as savings accounts or certificates of deposit, higher interest rates could be a boon, as rising rates would increase their potential income. The downside, of course, is that if higher rates are accompanied by inflation, such cash alternatives might not keep pace with rising prices.

Balancing competing risks

Bonds may be affected most directly by Fed action, but equities aren't necessarily immune to the impact of rate increases. Companies that didn't take advantage of low rates by issuing bonds may see their borrowing costs increase, and even companies that squirreled away cash could be hit when they return to the bond markets. Also, if interest rates become competitive with the return on stocks, that could reduce demand for equities. On the other hand, declining bond values could send many investors into equities that offer both growth potential and a healthy dividend.

Figuring out how future Fed decisions may affect your portfolio and how to anticipate and respond to them isn't an easy challenge. Don't hesitate to get expert help.

See disclaimer on final page

Spring Cleaning Your Debt

Making more than the required minimum payment is especially important when it comes to credit card debt. If you only make the minimum payment on a credit card, you'll continue to carry the bulk of your credit card balance forward for many years without actually reducing your overall balance.

It's springtime--time for you to take stock of your surroundings and get rid of the dirt and clutter that you've accumulated during this past year.

In addition to typical spring cleaning tasks, you may want to take this time to focus on your finances. In particular, now may be as good a time as ever to evaluate your debt situation and try to reduce and/or eliminate any debt obligations you may have. The following are some tips to get you started.

Determine whether it makes sense to refinance

If you currently have consumer loans, such as a mortgage or an auto loan, take a look at your interest rates. If you find that you are paying higher-than-average interest rates, you may want to consider refinancing. Refinancing to a lower interest rate can result in lower monthly payments on a loan and potentially less interest paid over the loan's term.

Keep in mind that refinancing often involves its own costs (e.g., points and closing costs for mortgage loans), and you should factor them into your calculations of how much refinancing might save you.

Consider loan consolidation

Loan consolidation involves rolling small individual loans into one larger loan, allowing you to make only one monthly payment instead of many.

Consolidating your loans into one single loan has several advantages, including making it easier to focus on paying down your debt. In addition, you may be able to get a lower interest rate or extend the loan term on a consolidated loan. Keep in mind, however, that if you do extend the repayment term on a consolidated loan, it could take you longer to get out of debt and ultimately you may end up paying more in interest charges over the life of the loan.

Look into taking out a home equity loan

If you own a home and have enough equity, you may be able to use a home equity loan to pay off your debt. The interest on home equity loans is often lower compared to other types of loans (e.g., credit cards) and is usually tax deductible.

Home equity loans can be an effective way to pay off debt. However, there are some disadvantages to consider. If you end up having an available line of credit with a home equity loan, you'll need to be careful not to incur any new debt. In addition, when you take out a home equity loan, your home is potentially at risk since it serves as collateral for the loan.

Evaluate whether you should invest your money or pay off your debt

Another effective way to reduce your debt load is to take cash that you normally would put toward certain investment vehicles and use it to pay down your debt. In order to determine whether this is a good option, you'll have to compare the current and anticipated rate of return on your investments with interest you would pay on your debt. In general, if you would earn less on your investments than you would pay in interest on your debts, using your extra cash to pay off your debt may be the smarter choice.

For example, assume that you have $1,000 in a savings account that earns an annual rate of return of 3%. Meanwhile, you have a credit card balance of $1,000 that incurs annual interest at a rate of 19%. Over the course of a year, your savings account earns $30 interest while your credit card costs you $190 in interest. In this case, it might be best to use your extra cash to pay down your high-interest credit card debt.

Come up with a payment strategy to eliminate credit card debt

If you have a significant amount of credit card debt, you'll need to come up with a payment strategy in order to help eliminate it. Some options include:

- Making lump-sum payments using available funds such as an inheritance or employment bonus
- Prioritizing repayments toward cards with the highest interest rates
- Utilizing balance transfers

Whenever possible, make additional payments

Making payments in addition to your regular loan payments or the minimum payment due can reduce the length of the loan and the total interest paid over the life of a loan. Additional payments can be made periodically and at a time of your choosing (e.g., monthly, quarterly, or annually).

Making more than the required minimum payment is especially important when it comes to credit card debt. If you only make the minimum payment on a credit card, you'll continue to carry the bulk of your balance forward for many years without actually reducing your overall balance.

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Saving through Your Retirement Plan at Work? Don't Let These Five Risks Derail Your Progress

Keep in mind that no investment strategy can guarantee success. All investing involves risk, including the possible loss of your contribution dollars.

As a participant in your work-sponsored retirement savings plan, you've made a very important commitment to yourself and your family: to prepare for your future. Congratulations! Making that commitment is an important first step in your pursuit of a successful retirement. Now it's important to stay focused--and be aware of a few key risks that could derail your progress along the way.

1. Beginning with no end in mind

Setting out on a new journey without knowing your destination can be a welcome adventure, but when planning for retirement, it's generally best to know where you're going. According to the Employee Benefit Research Institute (EBRI), an independent research organization, workers who have calculated a savings goal tend to be more confident in their retirement prospects than those who have not. Unfortunately, EBRI also found that less than half of workers surveyed had actually crunched the numbers to determine their need (Source: 2013 Retirement Confidence Survey, March 2013).

Your savings goal will depend on a number of factors--your desired lifestyle, preretirement income, health, Social Security benefits, any traditional pension benefits you or your spouse may be entitled to, and others. By examining your personal situation both now and in the future, you can determine how much you may need to accumulate to provide the income you'll need during retirement.

Luckily, you don't have to do it alone. Your employer-sponsored plan likely offers tools to help you set a savings goal. In addition, a financial professional can help you further refine your target, breaking it down to answer the all-important question, "How much should I contribute each pay period?"

2. Investing too conservatively...

Another key to determining how much you may need to save on a regular basis is targeting an appropriate rate of return, or how much your contribution dollars may earn on an ongoing basis. Afraid of losing money, some retirement investors choose only the most conservative investments, hoping to preserve their hard-earned assets. However, investing too conservatively can be risky, too. If your contribution dollars do not earn enough, you may end up with a far different retirement lifestyle than you had originally planned.

3. ...Or aggressively

On the other hand, retirement investors striving for the highest possible returns might select investments that are too risky for their overall situation. Although it's a generally accepted principle to invest at least some of your money in more aggressive investments to pursue your goals and help protect against inflation, the amount you invest should be based on a number of factors.

The best investments for your retirement savings mix are those that take into consideration your total savings goal, your time horizon (or how much time you have until retirement), and your ability to withstand changes in your account's value. Again, your employer's plan likely offers tools to help you choose wisely. And a financial professional can also provide an objective, third-party view.

4. Giving in to temptation

Many retirement savings plans permit plan participants to borrow from their own accounts. If you need a sizable amount of cash quickly, this option may sound appealing at first; after all, you're typically borrowing from yourself and paying yourself back, usually with interest. However, consider these points:

- Any dollars you borrow will no longer be working for your future
- The amount of interest you'll be required to pay yourself could potentially be less than what you might earn should you leave the money untouched
- If you leave your job for whatever reason, any unpaid balance may be treated as a taxable distribution

For these reasons, it's best to carefully consider all of your options before choosing to borrow from your retirement savings plan.

5. Cashing out too soon

If you leave your current job or retire, you will need to make a decision about your retirement savings plan money. You may have several options, including leaving the money where it is, rolling it over into another employer-sponsored plan or an individual retirement account, or taking a cash distribution. Although receiving a potential windfall may sound appealing, you may want to think carefully before taking the cash. In addition to the fact that your retirement money will no longer be working for you, you will have to pay taxes on any pretax contributions, vested employer contributions, and earnings on both. And if you're under age 55, you will be subject to a 10% penalty tax as well. When it's all added up, the amount left in your pocket after Uncle Sam claims his share could be a lot less than you expected.

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This newsletter strives to provide factual and up-to-date information on the topics discussed, but it should not be regarded as a complete discussion of these issues. The reader is advised to engage the services of a competent professional before taking action on any subject matter discussed.

My teenage daughter just got her driver's license. Will my auto insurance rates go up?

The short answer is: yes. Anytime you add an extra driver to your policy, your rates will increase. However, you may end up paying even more when you add your daughter to your policy, since teenage drivers are some of the highest-risk drivers on the road. According to the most recent statistics from the National Transportation Safety Board, teen drivers have represented less than 7% of the driving population but have accounted for more than 13% of drivers involved in all deadly crashes. (Source: National Transportation Safety Board, October 2013)

Fortunately, there are some steps you can take to help make insuring your teen a bit more affordable.

- **Take advantage of policy discounts:** Your first step should be to ask your insurer if your teen qualifies for any policy discounts that are specifically designed for teens. For example, many insurance companies offer discounts (usually around 10% to 15% off of premiums) for teens who complete a driver's education course, obtain a certain grade point average, or participate in a safe driver program.
- **Consider the type of car your teen will be driving:** Typically, new cars are more expensive to insure than older ones. As a result, you may want to consider purchasing an older, less expensive car for your daughter to drive. You may even be able to save more money by forgoing collision coverage on an older vehicle.
- **Consider whether an individual policy makes sense:** In the future, circumstances may arise where it may be more affordable to insure a teen under his or her own individual policy as opposed to listing him or her as an insured on your policy (e.g., he or she gets into an accident or has numerous motor vehicle infractions). When the time comes, ask your insurance agent to help you run the numbers to see which option is more affordable.
- **Be sure to shop around:** You'll want to take the time to compare the rates offered by different insurers. Insurance company rates vary widely, so it often pays off in the end to do your homework.

Is there anything I can do to lower my auto insurance bill?

Yes. Insurance companies base auto insurance rates on a variety of criteria, such as your age, driving record, residence, and even the type of car that you drive (though factors vary from state to state). If you find that you're paying more than you think you should for auto insurance, there are ways you can lower your premiums.

- **Shop around:** Auto insurance rates vary from company to company, sometimes significantly. As a result, a good way to save money is to look into whether another insurer offers the same coverage at a lower rate.
- **Consider raising your deductible:** For the most part, the higher your deductible, the lower your premiums. Before you raise your deductible, though, you'll want to be sure you can cover the out-of-pocket expense should an accident occur.
- **Eliminate unnecessary coverages:** For example, if you have an older car, it may make sense to drop your collision and comprehensive coverage since a claim paid by your insurance company may be minimal and might not exceed what you'd pay in premiums and deductibles. Or, maybe you are paying your insurer for roadside assistance coverage that you already have through a separate road and travel club membership.
- **Consider changing the type of car you drive:** The type of car that you drive directly impacts what you pay for insurance. Typically, newer, higher-priced cars and sport/high-performance vehicles cost more to insure than used/lower-end models.
- **Check for discounts with your insurer:** Depending on your circumstances, you may be eligible for one or more auto insurance discounts. For example, your insurer might provide discounts to those with a safe driving record or to those who insure more than one car with them.

One final note: don't be tempted to save money on your auto insurance by lowering your liability coverage limits (although state minimums do apply). Having less than adequate amounts of liability coverage can expose you personally to claims for other people's losses--which in the case of a serious accident, can be significant.

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