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Financial Briefs

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Focus on the Basics

It's easy to become overwhelmed when faced with all the decisions that need to be made to ensure you select appropriate investments to help pursue your long-term investment goals. How do you choose the right combination of investments to help you work toward a goal that may be decades away? The answer is to focus on the basics. Make sure you are getting these fundamentals right:

- **Don't wait — invest now.** To put the power of compounding to work for you, start investing now. It's easy to put off investing, thinking you'll have more money or more time at some point in the future. Typically, however, you'll be better off saving less now than waiting and saving more later. Consider the savings habits of a 20-year-old couple. The wife starts contributing $2,000 per year to a tax-deferred investment, such as a 401(k) plan, when she is 20. After 10 years, she decides to stop investing and let her money grow until retirement. She has invested a total of $20,000. Her husband starts investing when she stops, investing $2,000 per year from the time he is 30 until he retires at age 65. Thus, he saves every year for 35 years, making a total contribution of $70,000 — $50,000 more than his wife. If they both earn 8% compounded annually, who will have the larger potential balance at age 65? Time and compounding of earnings favor the wife. Before paying any taxes, her balance would equal $462,649, while her husband's balance would be $372,204. *(This example is provided for illustrative purposes only and is not intended to project the performance of a specific investment.)*
- **Live below your means so you can invest more.** It's a basic fact that most people have trouble coming to grips with — the amount of money you have left over for investing is a direct result of your lifestyle. Don't have any money left over for investing? Ruthlessly cut your living expenses — dine out less often, stay home rather than going away for vacation, rent a movie rather than going to the theater, cut out morning stops for coffee. Redirect all those reductions to investments. This should help significantly with your retirement. First, you'll be saving much more for that goal. Second, you'll be living on less than you're earning, so you'll need less for retirement.
- **Maintain reasonable return expectations.** When developing your financial goals, you'll typically decide how much you need, when you'll need the money, and

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Assessing Your Risk Tolerance

While investors want the highest returns possible, returns compensate you for the risks you take — higher risks are generally rewarded with higher returns. Thus, you need to assess how much risk you are willing to take to obtain potentially higher returns. However, this can be a difficult task. It is one thing to theoretically answer questions about how you would react in different circumstances and quite another to actually watch your investments drop in value. What you are trying to assess is your emotional tolerance for risk, or how much price volatility you are comfortable with. Some questions that can help you gauge your risk tolerance include:

- **What long-term annual rate of return do you expect to earn on your investments?** Your answer

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Focus on the Basics

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how much you'll earn on those savings. Those factors will determine how much you need to save on an annual basis to reach your goals. The higher your expected return on your investments, the less you need to save every year. However, if your assumed rate of return is significantly higher than your actual rate of return, you won't reach your goals. Thus, it's important to come up with reasonable return expectations. While past returns aren't a guarantee of future returns, you'll want to start by reviewing historical rates of return for investments you're interested in. You can then adjust those returns based on your expectations for the future. Assessing your progress every year will allow you to make adjustments along the way. If your return is lower than expected, you may need to increase savings or change investment allocations.

- **Understand that risk can't be totally avoided.** All investments are subject to different types of risk, which can affect the investment's return. Cash is primarily affected by purchasing-power risk, or the risk that its purchasing power will decrease due to inflation. Bonds are subject to interest-rate risk, or the risk that interest rates will rise and cause the bond's value to decrease, and default risk, or the risk that the issuer will not repay the bond. Stocks are primarily subject to nonmarket risk, or the risk that events specific to a company or its industry will adversely affect a stock's price, and market risk, or the risk that a stock will be affected by overall stock market movements. These risks make some investments more suitable for longer investment periods and others more suitable for shorter investment periods.
- **Diversify your portfolio.** When stocks had above-average returns for an extended period, diversification acted as a drag on total return. By definition, allocating anything other than all of your portfolio to the best-performing asset lowers your return. But when stocks decline substantially, the disadvantage of investing only in one asset class becomes apparent. Typically, you do not know which asset class will perform best on a year-to-year basis. Diversification is a defensive strategy — it helps protect your portfolio during market downturns and reduce your portfolio's volatility. Diversify your investment portfolio among a variety of investment categories, such as stocks, bonds, cash, real estate, and others. Also diversify within investment categories.
- **Only invest in the stock market for the long term.** Stocks should only be considered by investors with an investment time frame of at least five years. Remaining in the market over the long term reduces the risk of receiving a lower return than you expected.
- **Don't try to time the market.** Timing the market is a difficult strategy to accomplish successfully since so many factors affect it. Remember that most people, including professionals, have difficulty timing the market with any degree of accuracy. Significant market gains can occur in a matter of days, making it risky to be out of the market for any length of time. Instead of timing the market, concentrate on setting an investment program that works in all market environments and you can stick with in good and bad times.
- **Pay attention to taxes.** Taxes are probably your portfolio's largest expense. Using strategies that defer income for as long as possible can make a substantial difference in the ultimate size of your portfolio. Some strategies to consider include utilizing tax-deferred investment vehicles (such as 401(k) plans and individual retirement accounts), minimizing portfolio turnover, selling investments with losses to offset gains, and placing assets generating ordinary income or that you want to trade frequently in your tax-deferred accounts.

Focusing on the fundamentals can help ensure you work toward your financial goals. If you need help with investing, please call.

Overdiversification

Diversify. Diversify. Diversify. While this investment advice seems to be continually discussed, it is possible to overdiversify, which can lead to lackluster returns. Thus, it is important to know the difference between healthy diversification and excess diversification.

The primary benefit of diversification for your portfolio is to spread market risk over different stocks in a way that will decrease the impact any one stock will have on your total return. With an appropriate level of diversification, your overall return will not be significantly impacted if one or even a few investments do not perform as expected.

Thus, it is not just the number of investments you hold that impacts your return, but how they interact with one another. If you keep adding investments that react to the market in the same way, you are not really diversifying. You are just adding similar investments to your portfolio.

Adding too many investments to your portfolio also makes them more difficult to monitor. With too many investments to keep track of, it is more likely that you will miss important information.

Please call if you'd like to review the level of diversification in your portfolio.

Risk Tolerance

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will help determine the types of investments you need to choose to meet that target. Review historical rates of return as well as variations in those returns over a long time period to see if your estimates are reasonable. Expecting a high rate of return may mean you'll have to invest in asset classes you aren't comfortable with or that you may be frequently tempted to sell. A better alternative may be to lower your expectations and invest in assets you are comfortable owning.

- **What length of time are you investing for?** Some investments such as stocks should only be purchased for long time horizons. Using them for short-term purposes may increase the risk in your portfolio, since you may be forced to sell during a market downturn.
- **How long are you willing to sustain a loss before selling?** The market volatility of the past several years will give you some indication of how comfortable you are holding investments with losses.
- **What types of investment do you own now and how comfortable are you with those investments?** Make sure you understand the basics of any investments you own, including the historical rate of return, the largest one-year loss, and the risks the investment is subject to. If you don't understand an investment or are not comfortable owning it, you may be tempted to sell at an inopportune time. Over time, your comfort level with risk should increase as you better understand how risk impacts different investments.
- **Have you reassessed your financial goals recently?** Periodically, your financial plan may need to be revamped. Otherwise, you may find you won't have sufficient resources in the future to meet your goals. Based on your current investment values, determine what needs to be done to meet your financial goals. You may need to save more, change or eliminate some goals, or delay your retirement date.
- **Do you understand ways to reduce the risk in your portfolio?** While all investments are subject to risk, there are some risk reduction strategies you should consider for your portfolio. These strategies include diversifying your portfolio, staying in the market through different market cycles, and investing consistently.

Please call if you'd like help assessing your risk tolerance.

Why Have an Asset Allocation Strategy?

Your asset allocation strategy represents your personal decisions about how much of your portfolio to allocate to various investment categories, such as stocks, bonds, cash, and others. When stock market returns were above average for an extended period, investors did not have much interest in asset allocation. Then, the best strategy seemed to be only owning stocks. But investors are again focusing on asset allocation. Some of the advantages of an asset allocation strategy include:

- **Providing a disciplined approach to diversification.** An asset allocation strategy is another name for diversification, an important strategy for reducing portfolio risk. Since different investments are affected differently by economic events and market factors, owning various types of investments helps reduce the chance that your portfolio will be adversely affected by a particular risk type.
- **Encouraging long-term investing.** An asset allocation strategy is designed to control your portfolio's long-term makeup. It should not change based on economic conditions or market fluctuations.
- **Eliminating the need to time investment decisions.** Market timing is a difficult concept to implement. Not only do investment professionals have a difficult time accurately predicting the market's movements, but waiting for the perfect time to invest keeps many investors on the sidelines. With an asset allocation strategy, you don't have to worry about timing the market; you just have to ensure your investments stay within the proper percentages.
- **Reducing the risk in your portfolio.** Investments with higher returns typically have higher risk and more volatility in year-to-year returns. Asset allocation combines more aggressive investments with less aggressive ones. This combination can help reduce your portfolio's overall risk.
- **Adjusting your portfolio's risk over time.** Your portfolio's risk can be adjusted by changing allocations for the different investments you hold. By anticipating changes in your personal situation, you can make those changes gradually.
- **Focusing on the big picture.** Staying focused on your asset allocation strategy will help prevent you from investing in assets that won't help accomplish your goals. Rather than investing in a haphazard manner, it gives you a framework for making investment decisions.

Your asset allocation strategy will depend on a variety of factors unique to your situation, including your risk tolerance, return expectations, investment period, and investment preferences. Please call if you'd like to discuss asset allocation in more detail.

News and Announcements

From the Flinton Household

With all that the previous twelve months brought, one of my favorite memories from the year was the play my two daughters put together. Dance is their passion at this moment in time, so they worked tirelessly for countless days perfecting their own rendition of The Christmas Story. I didn't count, but they probably spent 30 hours putting everything together. They researched the perfect set list to ensure that the story was clearly told through the dance and music. They painted a backdrop on cardboard to set the scene alongside the manger. There was a refreshment table with drinks and candy to purchase, and handmade programs for the performance. Obviously there were tickets produced and needed for entrance, as this wasn't a free entry either. They put up a ladder and covered it with a sheet, because an angel can't just stand on the ground! They even had our German shepherd play the role of the donkey in the evening showing.

In its entirety it was a choreographed ballet/dance mix with thirteen songs (yes, 13 songs!), over a dozen wardrobe changes (on a frigid December 25th in the garage mind you), and approximately 30 minutes in length. Not counting me and my wife, only two other people got to see the play, and not even at the same time. It. Was. Great. The best part was a wonderful memory for life that two young sisters will recall and laugh about for the rest of their lives.

To making memories,

Andrew Flinton, CFP®

From the Alexander Household

As we plan for 2021, I am intrigued by the Tibetan phrase that expresses the process of waking up or enlightenment as "a clearing away and a bringing forth."

This translation brings to mind the book "What Got You Here Won't Take You There" by Marshall Goldsmith. For me, this concept is a reminder that the habits that contributed to success at one stage of life aren't always the ones I need now. That's where the "clearing away" comes in. And through "bringing forth," I discover new approaches.

I find this concept helpful in the process of forming new habits. I've been contemplating ways to bring greater joy to the process of change. Seeing the project as an aspiration rather than a demand, inviting a friend along for the journey, and seeing it as a way to gain greater awareness can be helpful. My annual review to determine what to keep or clear includes three questions. 1. What worked? What went well this year? 2. What didn't? 3. What must I do differently to get where I want to be? What is the one thing I can do, such that by doing it everything else will be easier or unnecessary?

Isn't clearing away and bringing forth a great way to approach any habit you want to establish or reprogram and your goals as we welcome a new year?

Carol Ringrose Alexander,

CFP®, AIF®, CEPS, CDFA™

From the Bolander Household

Happy New Year — 2021 is here! Nothing quite says happiness like a newborn litter of puppies. Just before Christmas, our daughter's sweet dog Luna welcomed nine soft and cuddly pups. Luna is mostly Border collie and her puppies have the classic white socks and tips on their tails though some markings are more noticeable than others. The runt gets extra feedings from a bottle, which the grandkids think is the coolest thing ever. They simply adore all the pups, but mom says they can only keep one. So, they have selected their favorite and named her Buttons for her black eyes and nose. The rest will be ready to adopt just in time for Valentine's Day!

"Dogs are good for your heart," according to the American Kennel Club, and it is one of ten science-based benefits of having a dog. Benefit number two states, "Studies suggest that dog owners have lower blood pressure levels and … reduced stress, which is a major cause of cardiovascular problems." Number six says, "Dogs make you more attractive — even virtually. A dog's presence [even in a picture] may make people appear more likeable and attractive." In summary, owning a dog makes us healthier and happier. So, if someone you know needs a puppy, send them my way!

Have a great month.

Brenda C. Bolander,

CFP®, CPA/PFS