Investor Insights & Outlook

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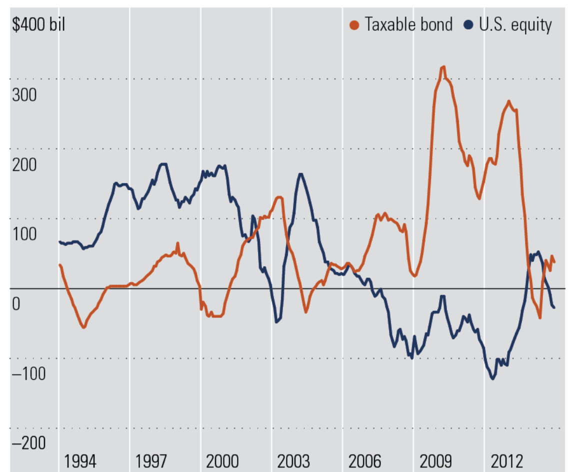
Bond Versus Equity Fund Flows

Fund-flow data can be a useful for analyzing where investor money is going and how fund-flow trends are correlated with asset-class performance. Between 1994 and 2001, equity flows were higher than bond flows, but all that changed after the dot-com crash when investors started losing confidence in stocks.

The 2007–2009 crisis on the graph illustrates how investor behavior is tied to market performance, even though the timing may not always be right. In 2009, as the stock market hit bottom, investors should have been buying cheap stocks, but instead bond flows increased. In 2012, stock inflows started to climb again. The upswing was short-lived, however, and stock flows have once again been on the decline since April 2014.

Rolling 12-Month Fund Flows



Source: Morningstar Direct. Funds analyzed include U.S. open-end mutual funds. Data as of December 31, 2014.

The investment return and principal value of mutual funds will fluctuate and shares, when sold, may be worth more or less than their original cost. *Mutual funds are sold by prospectus, which can be obtained from your financial professional or the company and which contains complete information, including investment objectives, risks, charges and expenses. Investors should be read the prospectus and consider this information carefully before investing or sending money.*

Returns and principal invested in stocks are not guaranteed, and stocks have been more volatile than bonds.

Contour Financial INCORPORATED

MORNINGSTAR

Advisor Corner

Cindy Menker

cindy@contourfinancial.com
(708) 460-3800
ContourFinancial.com

Cindy Menker, CFP™, CPA, MBA is President of Contour Financial, Inc. The firm, located in Orland Park IL, specializes in retirement planning and investment management. Tax planning, including tax preparation, is also offered.

Cindy is a member of the National Association of Personal Financial Advisors (NAPFA), the financial industry's leading organization.

One requirement for membership is that Contour Financial be "Fee Only", meaning that all fees be fully disclosed to the client.

For archived newsletters and interviews visit the "Current Clients" tab found at ContourFinancial.com. Cindy has been interviewed by local and national publications including Money Magazine, Elite Magazine, and the Chicago Tribune.

Feel free to forward this newsletter to your friends and family. Provide us with their email addresses so that they do not miss out on any future issues.

Success Factors for Retirement, Part 1

OK, folks, here's what we're asking you to do. First, save as much money as you can while you're working, despite ongoing expenses. Next, figure out how to invest the money and, once you've gained critical mass on your savings, determine if it's going to be enough. Is it any wonder so many pre-retirees are overwhelmed by retirement planning?

However, there is good news, as well. Some of the key success factors that have the power to make or break a retirement plan can be simple if understood correctly. While investors don't need to hit the mark on every last one of them, handling the majority of them correctly increases the chances of a successful retirement plan.

Success Factor 1: A Flexible Retirement Date. For investors who analyzed the numbers on their retirement plans and found that their nest egg could come up short, one option to consider is working longer. Doing so can be advantageous on a few different levels. Investors will have more years to save and fewer years to draw from their portfolios. They may also be able to defer Social Security, which can be profitable, especially for people with a longer-than-average life expectancy. Another option to consider is a hybrid strategy, shifting into a lower-paid, but more rewarding and/or less stressful, career. Alternatively, investors could stay put in their current positions but spend (rather than bank) additional retirement-plan contributions. Such a strategy could allow some people to pay for retirement dreams, such as exotic travel, while still working. Additional retirement-plan contributions in your 60s benefit less from tax-deferred compounding than do contributions made earlier on. Of course, working longer isn't always a possibility: Health considerations (for oneself, a spouse, or a parent) may interfere, or aging employees may not be able to hang on to their jobs. That's why working longer can't be the only fallback plan; investors need to make sure they have other success factors working in their favor, too.

Success Factor 2: A Well-Considered Social Security Strategy. Deciding when to file for Social Security is one of the most consequential financial decisions most Americans will make about their retirement. The 1980s and 1990s were all about maximizing portfolio returns. But the specter of twin bear markets in the 2000s, as well as ultra-low interest rates, shone a light on more mundane matters, including trying to get the most out of Social Security. Even casual students of Social Security planning have heard the admonition to not take Social Security at age 62, when they're first eligible, as doing so will result in a permanent cut to benefits. And for people who have longevity on their side, it may be better to delay benefits for as long as possible, because benefits increase for every year from full retirement age until age 70. Keeping those rules of thumb in mind is a great first step toward getting a Social Security plan moving in the right direction, but retirement planners can also take advantage of more sophisticated strategies, especially if they're part of a married couple. More and more financial planners are focusing on Social Security maximization, and there are also a number of online tools that can help craft a prudent Social Security plan.

Success Factor 3: A Large Enough Stock Allocation. The traditional lifetime glide path calls for accumulators to hold very high weightings in stocks, and then gradually peel back equity exposure as the years go by. But make no mistake: Pre-retirees and retirees may need plenty of stocks, too. The key reason is purchasing-power preservation. If inflation runs at 3%, it's hard to see how a portfolio of nominal bonds and cash yielding 2% to 3% is going to be able to hold up. Of course, there are other ways to hedge inflation risk, but stocks are the asset class with the highest probability of out-earning inflation over time. That argues for most retirees holding at least half of their assets in stocks coming into retirement.

Success Factors for Retirement, Part 2

Of course, holding a higher equity weighting also means higher short-term volatility, but that may be an acceptable trade-off when considering the bigger risk of running out of money prematurely.

Success Factor 4: A Sensible (and Dynamic) Spending Strategy. The size and composition of a retirement portfolio are just one side of the ledger. On the other side? The strategy used for extracting the cash needed from that portfolio on an ongoing basis. Even very large portfolios aren't big enough to last for an entire retirement if the withdrawal, or spending, rate is too high. That's why financial-planning researchers have been focusing so much energy on this area in recent years. Many experts think that the old 4% rule, which involves taking 4% of a portfolio's balance in year one of retirement and inflation-adjusting that amount thereafter, still gives a person with a 60% equity/40% bond portfolio good odds of not outliving their money over a 30-year retirement. But there's also widespread agreement that retirees can greatly improve their portfolios' longevity if they're willing to be flexible about withdrawals, reducing spending in lean years for the market and potentially taking a bit more in good ones. In addition to being willing to adjust their withdrawal rates, retirees may also want to be flexible about withdrawal strategies, using an income-centric approach in more yield-rich eras and relying more on rebalancing proceeds in others.

Success Factor 5: Flexibility on In-Retirement Living Expenses. Even people who aren't in the habit of driving 16-year-old cars (and don't plan to) can make their retirement finances better if they're willing to contemplate a less costly in-retirement lifestyle. One of the easiest ways to bring costs down without throwing quality-of-life considerations out the window is to consider downsizing homes. Like working longer, downsizing can have a positive impact on a few different levels. Even if you own your home free and clear, you're apt to have lower outlays for taxes, utilities, and maintenance costs than you did in your larger home. And the sale of a home that realizes a profit means more money for retirement.

Success Factor 6: Vigilance on Portfolio Costs. As a portfolio's asset allocation gets more conservative over time, its return potential declines as well. This means that investment-related costs, on a percentage basis, will extract an even bigger toll than they did when the portfolios was younger and earning a high return. Let's say a 50% stock/50% bond portfolio earns a 4.5% annualized return, on a pre-expense basis, over the next few decades. Assuming a 3% inflation rate, that's just a 1.5% real return. And unless investors are careful, nearly all of that return could disappear in investment-related and tax costs. After all, it's not unusual for funds to have expenses over 1%, and they're just one piece of the expense pie. The good news is that investment costs are one of the easier factors for investors to control. Another area to focus on is tax management. Retirees may want to hang on to tax-advantaged accounts for as long as possible. When it comes time to pull money out, investors should carefully consider which accounts to withdraw from, with an eye toward staying in the lowest possible tax bracket.

Returns and principal invested in stocks are not guaranteed, and stocks have been more volatile than other asset classes. Investing does not ensure a profitable outcome and always involves risk of loss.

Asset allocation is a method used to help manage risk. It does not ensure a profit or protect against a loss. This is for informational purposes only and should not be considered tax or financial planning advice. Please consult a tax and/or financial professional for advice specific to your individual circumstances.

This article contributed by Christine Benz, Director of Personal Finance with Morningstar.

Monthly Market Commentary

In recent international news, the eurozone and Greece agreed to extend Greece's aid program, which helped European and North American stock markets to dash to the upside along with higher interest rates.

Employment: The U.S. economy added a surprisingly strong 295,000 jobs in February, well ahead of the market's expectation that just 240,000 jobs would be added. The growth figure was also well above the 12-month average of 275,000 jobs added.

However, the trend over the past several years has been that, despite seasonal adjustments, job growth has looked remarkably strong in late winter and early spring, only to fall apart over the summer months. Based on this trend and other soft spots in the economy, Morningstar economists caution that this may be the best jobs report we see for some time.

The business and professional services sector added 51,000 jobs, which is great news because these jobs have long hours and great pay. This is also the sector that includes most of the office professionals who quickly come to mind when we think about quality jobs.

The unemployment rate dropped to 5.5%, the high end of the 5.0%–5.5% range considered to be the natural, or normal, rate of unemployment. This tends to support Morningstar economists' long-term thesis that we are approaching the point where labor market scarcities are going to become more prevalent.

This relatively low unemployment rate is also likely to make the Federal Reserve more prone to raise rates. The whole reason the Fed forced interest rates so abnormally low was to aid the employment market. That work now looks largely complete. However, with inflation rates (the other half of the Fed mandate) so low, they won't necessarily have to rush. Morningstar economists remain convinced that 2015 will be the year the Fed tightens, but the exact month this will occur remains frustratingly elusive.

Manufacturing: The ISM Purchasing Managers Index for manufacturing slipped modestly in February from 53.5 to 52.9. Year-over-year growth in industrial production (what ISM is meant to forecast) has remained relatively stable over the past several months. However, the move to 52 from 57 last summer suggests that manufacturing isn't accelerating any more. And the auto industry, while improving, is also beginning to slow.

After industrial production peaked at just over 5%, year over year, manufacturing growth is likely to drop back to a 3%–4% growth rate in 2015, but still above the long-term average of 2.6%. Nevertheless, this expected manufacturing growth reduction is one of the reasons that Morningstar economists are less bullish than others on the GDP outlook for 2015.

Housing: Home prices jumped by 1.1% between December and January, according to the latest CoreLogic report. Higher home prices at this point in the recovery are not necessarily a good thing for the economy. Higher prices have reduced affordability and certainly affected existing-home sales in 2014.

Gasoline prices were up almost 10% in February, after falling 17% in January. Furthermore, based on refinery issues, especially in California, and a relatively higher price of crude, the AAA is projecting that gasoline will be up at least another $0.20 in March, or about an additional 8%.

U.S exports didn't look good either, declining 2.9%, although labor issues at West Coast ports may be part of the problem. Weekly shopping center growth rates also continued to slow. Consumer incomes were one of the bright spots, with a month-to-month increase of 0.9%. However, consumers refused to spend their newfound wealth, at least for now, as the savings rate has moved up from 4.5% to 5.5% over the past two months. That could provide some fire power for additional consumer spending in the months ahead.

About Contour Financial

Contour Financial is a private wealth management business located in Orland Park, Illinois. We work primarily with middle income and wealthy clients. As a fee-only firm, all compensation is disclosed. For clients seeking investment management by our firm, assets are held at Charles Schwab Institutional, an industry leader.

This newsletter is the link to a resource that will answer your most important financial question, namely:

- If employed – When can I retire?
- If not employed – Can I stay retired?

Contour Financial will answer this question, suggest alternative scenarios, if needed, and implement investment strategies in order to reach your objectives.

Customized strategies are developed and implemented. Personalized service is provided to clients. Investment, retirement, tax, estate, insurance, cash flow and education planning are all integral parts to the process.

Contour Financial INCORPORATED

Cindy Menker

Contour Financial
9031 W 151st Street
Suite 107
Orland Park, Illinois 60462

cindy@contourfinancial.com
ContourFinancial.com

Tel:(708) 460-3800