

# Investor Insights & Outlook

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## Home Price Growth Returning to a More Sustainable Rate

It is certain that, after a series of fast-paced increases that peaked in late 2013, the rate of home price increases is moderating. As of November, the Case-Shiller Index is showing that home prices are growing at 4.3% year-over-year, which is a much slower rate compared to nearly a 14% pace reported in 2013. The prices recovered about 82% of the previous high, and 14 states are currently either above or close to the previous 2006 peak. Nonetheless, Nevada, Florida, Arizona, and a few other states still remain 20% or more below the peak, and it will certainly take many years for those prices to return to their pre-recession level. On the positive side, slower-growing prices are good news for prospective buyers and for the health of the housing market in general, as they should improve housing affordability, providing an essential boost to this so far anemic housing recovery.

Case-Shiller Home Price Index Annual Change, 3-Month Average



This article contains certain forward-looking statements which involve known and unknown risks, uncertainties, and other factors that may cause the actual results to differ materially from any future results expressed or implied by those projected statements. Past performance does not guarantee future results.

Source: S&P/Case Shiller. Data through November 2014.

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### Advisor Corner

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.

# The Many Faces of Risk, Part 1

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There is no question that risk carries a negative connotation for investors. But the simple fact about risk is that it's ever-present. There is more to risk than market volatility, and trying to avoid risk is like trying to avoid the oxygen in the room. You might think you're avoiding it by sticking with safer investments, such as bonds. But when you make moves like this, you're usually just swapping one kind of risk for another. In this case, you may have reduced short-term volatility risk, but you likely increased long-term shortfall risk: With a heavy emphasis on lower-yielding "safe" investments, your portfolio may not grow enough to meet your retirement needs or overcome inflation over the long term.

On the flip side, we may also mistake an upward trend in the market for the absence of risk. A strong performance streak doesn't mean there was no risk. It just means that risk didn't bite hard during that time period. Don't confuse being lucky with being risk-proof.

So, we can't avoid risk. But neither should we be oblivious to it. What we need to do is understand the risks we're taking, and remember risk's traveling companion: reward. This keys in on an important point: Risk isn't inherently bad. When you take risk, you can have good outcomes, too. Risks should have related and commensurate potential rewards. We invest in the market not because risk is bad and we expect to lose money, but because taking risk can be profitable. So, the question is not whether to take risk. Instead, it's what risks do you want to take, and how much?

## Types of Risk

As suggested above, there is more than one kind of risk, and to manage risk well, you need to consider the different types. For instance, investing risk is not all (or even mostly) about the market's volatility (the Dow's daily ups and downs on Fed talk, China's latest data, or any number of global worries).

When thinking about investment risk, you need to consider company fundamentals (what will cause this firm to succeed or fail), because that will ultimately

drive the stock price over time. There is also price risk. Even if the company is poised for tremendous success, how much are you paying to own a piece of it? If you overpay, you can still lose money, because stocks tend to revert to their fair value over time, even if they occasionally become under- or overvalued.

You also have to consider your own shortfall risk. Conceivably, you're investing in the market to fund some future expense (for instance, college or retirement). If you take money out of the market, or move money from stocks to bonds, what does that mean for your long-term earning potential, given the types of returns bonds tend to produce over long periods of time? Remember, funding that future expense is your primary objective, not avoiding every little dip in the market along the way.

But instead of fundamental, price, and shortfall risk, we investors tend to focus on short-term volatility because that's the thing we see every day, in real time. It's the most apparent and seemingly uncontrollable risk. Make no mistake, volatility may reflect real changes in a company's fundamentals, and that can mean a real loss of money for you. But volatility is often just noise, reflecting worries that won't have any lasting or appreciable effect on a company's operations. In these cases, we shouldn't let volatility risk leave the realm of paper losses.

That's easier said than done, of course, especially during a market crisis or correction. But one way of getting around that is by considering another type of risk: liquidity risk. That's the risk that you can't sell an asset (or at least can't sell it for a reasonable price) when you need to sell it. The upshot: If you have a short-term need for cash, then have cash on hand. That allows you to ride through the volatility risk of your other assets.

## The Many Faces of Risk, Part 2

### The Risks You Do Take Are Manageable

The good news is, even if you have to take some short-term risks you'd rather not, you can take the edge off in a number of ways. Diversification among asset classes may reduce marketwide or so-called systematic risk. In 2008, the bond market held up just fine even though stocks uniformly fell on their face. Holding assets that move in different directions at the same time makes for a smoother ride overall and gives you more options should you need to liquidate a portion of your holdings for some reason.

You may also want to consider diversification within one asset class. Holding several stocks (as opposed to just one) from the same industry and other industries may reduce company-specific risk (such as product-launch failure) and sector-specific risk (such as e-books and e-mail taking a bite out of paper company profits). Another way to manage fundamental risk is to invest in companies that have sustainable competitive advantages.

Dollar-cost averaging, or putting your money to work in smaller chunks over time, may reduce that risk. It also happens to be the de facto way that most people end up investing—with a little bit of money coming out of every paycheck. Another way to potentially reduce price risk is requiring a margin of safety before buying. All else equal, if you like a stock at \$50 per share, you should love it at \$30. Buying at a discount means you have room for error in your analysis, a buffer in case of an unforeseen complication, or the chance for extra return if everything goes as planned.

### Don't Let Risk Take You

Unlike the familiar risk of going to work for an immediate reward (a paycheck), when it comes to investing, the reward is typically delayed, while the perceived risk (specifically market volatility) is immediate. Because of short-term market gyrations, investors may also feel that they can't control or moderate their investment risk. So, there is a disconnect between perceived high and uncontrollable present risk on one side, and an uncertain future reward on the other. That just doesn't sound like a

good trade-off.

But that story is not complete. You also have to think about shortfall risk and the opportunity cost of not investing (in other words, the money you could have made over time but didn't because you weren't invested). You have to think about the cost of inaction, because not taking any action is potentially risky, too, just in a different way.

When you look at it this way, you should realize you can't avoid risk. So, don't let risk just happen to you. Since you'll end up taking risk in one form or another, you might as well take control, and take smart risks. Take risks in a way that you choose, in a form that you manage to reach your goals—knowing the trade-offs and the consequences and the rewards.

There is no guarantee that diversification, asset allocation and dollar-cost averaging will protect against market risk. These investment strategies do not ensure a profit or protect against loss in a declining market. In addition, since investing by dollar-cost averaging involves continuous investment in securities regardless of fluctuating prices, investors should consider their financial ability to continue purchases through periods of both low and high price levels.

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

This is for informational purposes only and should not be considered financial planning advice. Please consult a financial professional for advice specific to your individual circumstances. This article contributed by Christine Benz, Director of Personal Finance with Morningstar.

# Monthly Market Commentary

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In recent economic data, payroll numbers correct sharply, manufacturing continues to slow down fueled by the strong dollar and low oil prices, and the pace of home price growth increases as inventory levels remain low.

**Employment:** The U.S. economy added a disappointing 126,000 jobs in March. Certainly the over 300,000 jobs added late last year looked downright out of place. Job growth accelerated in a period when economic growth was slowing. Now with the much slower reported job growth in March and the substantial revisions to prior months, the employment data looks much more in line. However, the 126,000 jobs added in March is not the new normal, it was just an adjustment month.

The strong job openings data (from the end of February versus the jobs report, which is from the second week of March) confirms that the job market is not falling apart. In fact, the huge number of openings suggests that employers will need to pay more or be more willing to train workers before the pace of hiring will increase. Besides the job openings report, other metrics that point to a benign if not robust jobs market include initial unemployment claims, the labor sections of the small-business sentiment report, and various purchasing manager reports, as well as the ADP report.

**Manufacturing:** The ISM purchasing manager report continued to show a slowing—not panicky—manufacturing sector. The pace of deceleration has continued unabated since October and peaked way back in August. That weakness is now clearly visible in the month-to-month industrial production data that is now down three months in a row. The year-over-year data is at its early stages of deterioration, with more bad news likely with the softer March ISM report this week and a weak durable goods report last week.

The weakness in the ISM data was rather broad-based with just current production levels and prices paid subcomponents showing increases. Employment data was particularly weak, with that index dropping to 51.4, marking a second straight month of sharp

declines. ADP payroll data suggested that March manufacturing employment was basically unchanged from February. Order backlogs also dropped sharply in March, although that may be because the port strike settlement in late February enabled manufacturers to clear backlogs. In some more clearly bad news, export orders remained well below the 50 level that separates growth from contraction, falling from 48.5 in February to 47.5 in March. It will probably take either a pop in auto manufacturing or a restart of the housing industry to get the manufacturing data humming again. That's a real possibility by late summer, but probably not enough to help in the next month or two.

**Housing:** Recent pricing data suggests that home prices are on the rise again. According to CoreLogic, home prices increased 1.1% between January and February and were up 5.6% February over February. Year-over-year prices have been up for 36 consecutive months, or three years. The rate of home price growth has been slowing since fall 2013 when growth was as high as 11.9% compared with the current single-month reading of 5.6%. Still, it appears that the decline in the rate of home price appreciation has been stopped, with prices moving back up since a low reading of 4.7% in December. The three-month averaged, year-over-year data shows a similar pattern. We have also included CoreLogic-estimated results for March in the table below. We had estimated home price growth in 2015 at 4%–6%. Recent inventory data and price trends suggest that the high end of this range is now more likely.

**Auto sales:** On a more positive note, auto sales for March showed 17.1 million units sold (on a seasonally adjusted annual run-rate basis), the highest March number going back to 2000. Auto sales are one of the best indicators of consumer confidence, so this may be a sign that consumers are emerging from their malaise and could show some strength as we move into the spring.

# About Contour Financial

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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 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.

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