



# TAKING CARE OF YOU

ISSUE#: *One Hundred-Sixty-Eight*

*July, 2010*

## INSIDE THIS ISSUE:

- |  |   |   |
|--|---|---|
| 1. <i>Markets Section</i>                  | = | <i>Current Market Environment/Emergency Fund</i>      |
| 2. <i>Active Investment Management</i>     | = | <i>Participate In Up, Control In The Down Markets</i> |
| 3. <i>Current Best Funds</i>               | = | <i>Issue# 168 Fund Changes/Why</i>                    |
| 4. <i>Comprehensive Financial Planning</i> | = | <i>Budgeting</i>                                      |

## 1. MARKETS

### *Current Market Environment*

The market really took a beating in June. The beating was by two main issues. The early part of the decline was caused by worries over the European debt crisis, despite the fact that the domestic economy appeared robust enough. This was followed in early June by the shock and extreme disappointment over the extraordinarily weak May employment numbers. To top it off, the employment numbers were followed by a string of weaker-than expected economic reports. Some of the misses were more than trivial. The market reaction was sharp. Also, Wall Street opinion began to believe that the possibility of a “double-dip” was becoming more and more realistic.

As we see it, the battered market is now struggling with two issues. **First, how weak is the economy? Second, has the market’s steep decline already discounted the effects of any reasonable weakness?**

While momentum has slowed considerably, **it has by no means vanished.** All the latest indicators tell us that the economy is still growing – albeit, slowly. Private employment did increase by close to 100,000 jobs in June. The monthly manufacturing index was fairly positive in June, as was the employment subindex. New orders for business capital spending rose smartly.

The difficult June was followed by the best month of the year so far, July! The markets rebounded significantly due to better than expected earnings from companies. We believe that as earnings season winds down, the slowing of the economy will affect the speed of the U.S. market’s progress. **However, we still look for higher valuations ahead and many financial advisors and economists feel the bull market that started in March of 2009 is not over.**

### *Emergency Fund During Retirement*

Recently, a question has been brought to our attention about not just having an emergency fund, **but having an emergency fund in retirement.** This is a good question and needs to be addressed. Usually an individual needs to have an emergency fund in case they lose their income due to job loss, but if you are no longer working and you are living on social security, pension income, and/or draws on retirement plans, it is **unlikely** that your income will stop.

**However, there are other reasons besides replacing income that makes sense to have extra cash set aside.**

## **“TAKING CARE OF YOU”, Page 2**

First, is **unanticipated expenses**. Cars break down and require major repairs or need to be replaced. And houses can provide a seemingly inexhaustible supply of big-ticket expenses such as roof leaks, repainting, and other maintenance problems. Also, having cash to pay for unanticipated medical expenses is a very common need during retirement.

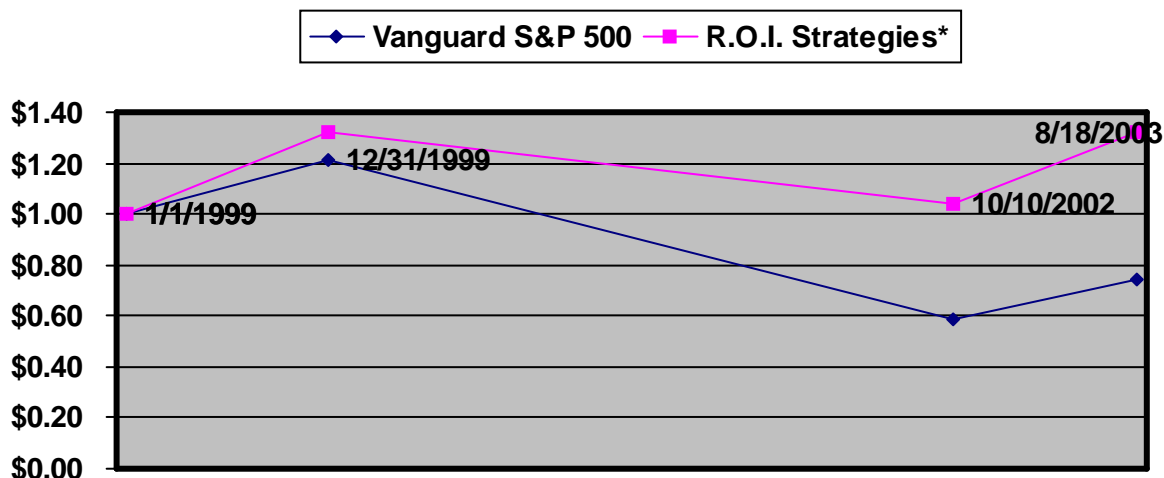
Another very important reason is **market fluctuations**. Most retirees will be looking to generate income from the money they’ve accumulated in 401(k)s, IRAs and other retirement accounts. The more you’ll be depending on income from retirement savings to fund your post-career lifestyle, the more important it is to have an adequate stockpile of cash.

Reasonable people disagree about how large a cash cushion is necessary for a buffer from market disruptions. When clients are getting close to a point in their lives where they will be drawing on their nest egg (retirement plans) they need to meet with R.O.I. to adjust their portfolio. These adjustments may include **increasing the size of their emergency fund (we encourage at least 6 months of living expenses), setting up a short-term account (to take care of draws for up to three years), and setting up a long term account (to beat long-term inflation and taxes and other needs, through the end of life)**. Once these accounts are set up, they will be adjusted based on amounts drawn from the short-term account and the market fluctuations of the long-term account. These adjustments will be discussed with clients during their annual reviews each year, over the phone, or during visits at the client’s request.

## **2. ACTIVE INVESTMENT MANAGEMENT**

### **PARTICIPATING IN UP MARKETS & CONTROLLING PARTICIPATION IN DOWN MARKETS**

Why important? The graph and comments below, from clients’ actual IRR% (a moderate allocation), clearly illustrate the tremendous value of **PARTICIPATING IN UP MARKETS & CONTROLLING PARTICIPATION IN DOWN MARKETS**:



## “TAKING CARE OF YOU”, Page 3

\* R.O.I. Strategies = ROI’s most common allocation, plus each bullet in the “ACTIVE INVESTMENT MANAGEMENT” column on the left side of this page

### **ACTIVE INVESTMENT MANAGEMENT**

#### OBJECTIVE

- Participate In Up Markets
- Control In Down Markets

#### ALLOCATIONS

- Asset Allocations (Secular/Cyclical Markets)
- Opposite Categories
- Different Classes
- Independent Classes

#### FILL ALLOCATIONS

- Use Best Funds
- Monitor Choices

#### CONTROL SWINGS

- Diversify Manager Styles
- Control Sector Concentration
- Allow Fund Managers To Make S/T Decisions
- Rebalance
- Fine Tuning Strategies

#### ADVISOR/CLIENT

- Motivate Advisor
- No Conflicts
- % Of Assets Basis
- Help Build Business

### **COMMENTS ABOUT THE VANGUARD S&P 500 GRAPH LINE**

The S&P 500 is an index that is supposed to represent the U.S. stock market. We use it in this illustration as a representation of what was experienced by many investors and many advisers who use the popular passive, index oriented investment management approach (also referred to as “buy and hold”). From 1/1/1999 to 12/31/1999 the Vanguard S&P 500 rose about 21%. Starting with \$1.00 on 1/1/1999, one would have about \$1.21 by 12/31/1999. By 10/10/2002 the S&P 500 had declined about -51%, and the \$1.21 would be worth about \$0.59. Getting the \$0.59 back to the 12/31/1999 value of \$1.21 would require growth of +105%! **As of 8/18/03, the Vanguard S&P 500 was only about \$0.74.**

### **COMMENTS ABOUT THE R.O.I. STRATEGIES GRAPH LINE**

From 1/1/1999 to 12/31/1999 the R.O.I. Strategies rose about 32%, i.e., **we Participated in the Up Market** (note, when the S&P 500 has large increases like 21% in 1999, we do not expect to beat the S&P 500 – we would be happy if we did 15%-18% in such a year – but we did very well in 1999). Starting with \$1.00 on 1/1/1999, one would have about \$1.32 by 12/31/1999. By 10/10/2002 we had declined about -21% (not -51%), and the \$1.32 would be worth about \$1.04, i.e., **we Controlled Participation in the Down Market**. Getting the \$1.04 back to the 12/31/1999 Vanguard S&P 500 value of \$1.21 would require growth of only +16% (not 105%) !!! Getting the \$1.04 back to the 12/31/1999 R.O.I. Strategies value of \$1.32 would require growth of only +27%!!! **This was accomplished about 8/18/03 (less than one year from 10/10/02)!!!**

The chart and comments clearly illustrate the **tremendous value** of participating in up markets **&** controlling participation in down markets, and, clearly illustrates **the tremendous importance of professional, active management to accomplish** these **two** critical objectives. Passive management cannot accomplish these two objectives because it would fully participate in up markets as well as fully participate in down markets. We cannot guarantee this kind of success in the future, but you know how motivated R.O.I. is try and do so.

### **3. CURRENT BEST FUNDS**

	<b>LAST MONTH</b>	<b>'10 YEAR TO DATE</b>	<b>1/1/97 THROUGH '10</b>
<b>ROI'S MPT INDEX*</b>	-2.6%	-3.10%	+82.1%
<b>ROI'S "BEST FUNDS"***</b>	-3.2%	-3.60%	+117.50%

\* ROI's MPT INDEX = An index based solely upon one Modern Portfolio Theory type of Asset Allocation to each of the following 12 Asset Classes, assuming from: (1) 1/1/97, an 11% Target Return (i.e., 70% in Stocks; 15% in Bonds; 15% in Anti-Inflation); and, (2) 3/1/03, a Moderate allocation (i.e., 50% in Stocks; 25% in Bonds; 25% in Anti-Inflation); using the average returns of all mutual funds in each Asset Class, Rebalanced on a monthly basis (data supplied by Morningstar).

\*\* ROI's "BEST FUNDS" = Using the accumulated yearly IRR % of an actual client's account that uses the same Moderate Asset allocation as in ROI's MPT INDEX, but includes all of ROI's other strategies.

**“TAKING CARE OF YOU”, Page 4**

**ISSUE# ONE HUNDRED-SIXTY-EIGHT BEST FUND CHANGES & WHY?**

(Funds or % in < > are new funds and allocations replacing prior choices. Current through Newsletter date.)

<b><u>STOCKS</u></b>	<b><u>BONDS</u></b>
<b>Aggressive Growth</b>	<b>US/LT, ST, Mtg, Convertible</b>
Fidelity Capital Appre 1 <sup>st</sup> Source (117%)	Fidelity Convertible (67%)
	DWS Short Duration (33%)
<b>Growth</b>	Delaware Corporate Bnd (33%)
Wells Fargo Adv (100%)	
Hotckis & Wiley (125%)	<b>Junk</b>
	Security High Yield (50%)
<b>Small Cap</b>	
Marshal Small Cap Gth (153%)	<b>Global</b>
AIM Triamark Small Co (119%)	Alliance Bern Glb Bond (100%)
	TCW Emg Mkts (62.5%)
<b>Equity Income</b>	<b><u>ANTI-INFLATION</u></b>
Invesco Mid Cap Val (125%)	<b>Asset Manager</b>
	Oppenheimer Global Opp (100%)
<b>Stock Index</b>	
Fidelity Spartan Market Index (100%)	<b>Ntrl Res, Utilities &amp; Metals</b>
	Gabeli (75%)
<b>Overseas: Int’l, World, SC, EM</b>	Fidelity Sel Material Port (50%)
Janus Overseas (85.7%)	Black Rock Energy Resource (50%)
Oakmark International Gth (69.8%)	<b>Real Estate</b>
Oakmark International (43%)	Fidelity Advisor Real Estate (92%)
Causeway Emerging Markets 52.65%	Dryden Global Real Estate (14.5)
AIM Dev. Mkt (85.7%)	

**THE “WHYS”**

**Allocation and Fund Changes** – No changes since last issue, but changes were made since this newsletter that will be reflected in the next issue.

[R.O.I. tracks each month’s consensus predictions for the Dow Jones Industrial Average (DJIA) for the upcoming six months, by the panel of “experts” in the Investment Advisor Magazine.]

<b><u>THE PREDICTION WAS:</u></b>		<b><u>THE DJIA WAS:</u></b>		<b><u>THE PREDICTION WAS OFF BY:</u></b>	
<b><u>MADE</u></b>	<b><u>FOR</u></b>	<b><u>DJIA</u></b>	<b><u>ACTUALLY</u></b>	<b><u>POINTS</u></b>	<b><u>PERCENT</u></b>
01/09	07/09	9644	8883	+761	+8.6%
02/09	08/09	9152	9325	-173	-1.8%
No Issue					
04/09	10/09	8641	9713	-1072	-11.0%
No Issue					
06/09	12/09	8668	10428	-1760	-16.8%
07/09	01/10	8824	10067	-1243	-12.3%

## “TAKING CARE OF YOU”, Page 5

08/09	02/10	8808	10325	-1517	-14.7%
No Issue					
10/09	04/10	9332	11009	-1677	-15.2%
11/09	05/10	9440	10136	-696	-6.87%
12/09	06/10	9728	10143	-415	-4.1%
<b>TWELVE MONTH ERROR RANGE =</b>				<b>-1760/+761</b>	<b>-16.8%/+8.6%</b>

*!!R.O.I. believes it is impossible to predict the short-term future. If the “experts” can’t reliably do so, what chance do you or R.O.I. have? Should we make large bets on short-term predictions?*

### 4. COMPREHENSIVE FINANCIAL PLANNING

#### THE MOST BORING (IMPORTANT) FINANCIAL SUBJECT OF ALL

In the previous issue we talked about “Protecting Yourself from Very Inconsiderate Relatives” (financial emergency planning). This time we want to discuss “The Most Boring (Important) Financial Subject of All” (**budgeting**, i.e., managing income **and expenses**). This subject used to be called boring, but **now** it effects the lives of so many of us or the lives of our children and grandchildren (and if it doesn’t now, it will in the future), that it **deserves** our: (1) Attention; (2) Time; and, (3) Efforts; before things get so bad that it **takes** all our: (1) Attention; (2) Time; and, (3) Efforts.

The controlling principle about budgeting can be stated as follows: “Before you can influence your **financial future**, you must first control your **financial moment**.” Another way to state this principle is: “Your budget provides the **fuel** (i.e., the **resources**) to drive your financial future → **No fuel = No future**.”

ROI believes there are four “**Budgeting Priorities**”:

1<sup>st</sup> = **Pay the Lord** (you can’t take it with you, and, faith precedes the miracle);

2<sup>nd</sup> = **Pay yourself** (any fool can spend – no talent and no discipline is required – it takes a wise person to **save**);

3<sup>rd</sup> = **Pay those who have to be paid** (the required payments to have food, shelter, clothing, **the necessities**);

4<sup>th</sup> = **Be selective and wise with the rest!**

The sooner we learn and put into practice these priorities, the better off we will be. The rest of this discussion will be about the 4<sup>th</sup> Priority = **Be selective and wise with the rest!** Specifically, we are going to discuss: (1) Controlling debt; and, (2) Using “Sinking Funds”.

**CONTROLLING DEBT**: Remember, debt is a **mortgage on your future**, i.e., something becomes so important for you to have it **now** that you are **sacrificing some of your future income** → **the HAVE NOW, PAY LATER SYNDROME**. Something this important should provide you with future value or income → that is why it is usually o.k. to borrow for a home (it will **almost** always grow in value over a long time), or education (it will almost always generate more income), but why it is probably wise to **save for everything else** (including transportation, because they go down in value and don’t produce more income). For example, instead of driving a “clunker” for a few years and saving to buy the new car, you buy the new car right now:

## “TAKING CARE OF YOU”, Page 6

### HAVE NOW, PAY LATER SYNDROME → THE NEW CAR

<u>Down Payment</u>	<u>Amount Borrowed</u>	<u>Interest Rate</u>	<u>Payback Period</u>	<u>Total Cost Of Car</u>	<u>Cost of Credit \$</u>	<u>Cost of Credit %</u>	<u>Worth of Car When “Paid For”</u>
\$ 2,000	\$18,000	8%	48 months	\$22,953	\$ 2,953	13%	\$10,000

### **COMPREHENSIVE FINANCIAL PLANNING**

#### INCOME & EXPENSE

- Emergency Planning
- Budgeting
- Taxes

#### KIDS/GRANDKIDS’ GOALS

- “Teach Them To Fish”
- Missions, Education, Marriages, and Home Down Payments

#### RETIREMENT

#### LONG TERM CARE

#### DEATH & DISABILITY

#### IDENTITY THEFT PROTECTION

#### ESTATE PLANNING

#### BUSINESS & ASSET PROTECTION PLANNING

In this example, a person pays an extra 13% in the form of future income for the privilege of owning an asset NOW that is probably going to lose 50% of its value in about four years. A bad syndrome!

**SINKING FUNDS:** What is a “sinking fund”? There are many expenditures over the course of a year (or years) that do not happen monthly, e.g., real estate property taxes, car and house insurance premiums, vacations and anniversaries, Christmas, home improvements, buying a car, etc. Most of these non-monthly expenses are foreseeable (you know about when they will happen) and can be valued (you know about what they will cost). A “sinking fund” is simply taking the value of the non-monthly expense, dividing it by the number of months till it happens, and setting that amount aside each month so the total value will be there when the non-monthly expense needs to be paid, e.g., car replacement cost of \$20,000 - \$10,000/future sale value of current car, in three years =  $(\$20,000 - \$10,000)/36\text{months} = \$278$  set aside/month.

Sinking funds are in addition to Emergency Funds, i.e., your minimum six months of Emergency Funds is over and above the total value of your sinking funds. If you have a Quicken type software package it is easy to set up an “asset account” for each sinking fund item, including your Emergency Fund, and to set aside each monthly contribution to each “asset account”, and to draw from the “asset account” when it comes time to spend that particular chunk of money for real

estate property taxes, car and house insurance premiums, vacations and anniversaries, Christmas, home improvements, buying a car, etc. If you don’t use a Quicken type software package, you can set aside each monthly contribution by writing a check to a separate envelope, or, set up a money market account for all of the sinking funds (and keeping tract on paper or in a ledger what part of this money market account is for each sinking fund item), and a separate money market account or savings account for your Emergency Funds.

Getting accustomed to using sinking funds is such a blessing to your finances because the money for these non-monthly expenses is “always there” when you need it, and, you never drain your Emergency Funds for a non-emergency expenditure that was simply not planned for. **Life is good, but even better when you use wise and simple accounting techniques to minimize financial surprises!**

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