NAPFA
Planning Perspectives

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NAPFA in the New Year!

In this issue of *Planning Perspectives*, Kevin Brosious examines investment risk by taking a historical perspective. Will markets take another unpleasant dive? Based on historical events, it's almost certain: "Highly improbable, unpleasant market events are happening with some regularity," Brosious says, "and there is every reason to believe we will continue to experience both short- and long-term significant market downturns." The good news? Since you know they'll happen again, you can prepare. The better news? The markets have always recovered from significant downturns.

Next, Joshua Itzoe considers President Obama's recently unveiled myRA. The plan aims to help low-income individuals invest for retirement—but will it work? "I definitely agree with the president that we need to help all Americans save more so they can retire successfully," Itzoe says. But he does take issue with how effectively myRA will encourage investment without automatic enrollment. While the plan has issues, it does call attention to the need for Americans at all income levels to plan for retirement.

Finally, Cheryl Sherrard lays out four principles that should guide women who are faced with decisions about financial planning—in other words, all women. "It is estimated that women will control two-thirds of the consumer wealth in the U.S. over the next decade," Sherrard points out. And yet many women still feel unprepared when faced with important decisions about managing their wealth. Considering that most women will end up controlling some portion of the nation's wealth at some point in their lives, Sherrard encourages them to be informed, responsible, passionate, and realistic about financial planning, leading to better decisions that will benefit everyone.

NAPFA Consumer Education Foundation
Promoting Consumer Financial Education

In past years, NAPFA has offered the public an opportunity to have their financial questions answered by professional advisors. This year, NAPFA continues to offer these "Jump-Start" online sessions in partnership with Kiplinger. The year's first session, "Jump-Start Your Retirement Plan," was held Feb. 20. NAPFA members answered hundreds of questions from consumers. The entire session is available here. Past and future sessions can also be viewed here.

Our next date is June 5, 2014 and will take place from 9:00 am - 5:00 pm ET.

NAPFA and Kiplinger will offer three more Jump-Start programs in June, September, and December.

Kiplinger Timely, Trusted Personal Finance Advice & Business Forecasts

Peel Back the Risk Onion

By Kevin Brosious, CFP®, CPA/PFS, MBA, Wealth Management, Inc. www.wealthmanagement1.com

When developing a portfolio for clients, one question I often get asked is, "Just how much risk am I assuming with my equity holdings, and how much could I lose?" The first thing I point to is the event still fresh in clients' minds—the Great Recession, and the associated drop in the S&P of almost 46 percent from October 2007 to March 2009. Most clients I speak to believe that this was a highly unusual event, not likely to be repeated. However, that was also said of the Great Depression, the 1987 market crash, and many other "one time" market events.

One popular measure of investment risk is standard deviation. Based on the historical standard deviation of the S&P 500, you have about a 0.5 percent chance that your portfolio will lose more than 43 percent in any particular year. If you look at S&P returns since 1913 (100 years), only in one calendar year did the S&P lose more than 42.5 percent—that was in 1931, when it lost 44.2 percent.

But just using the standard deviation to explain risk may be a bit misleading. Digging a bit deeper into the numbers can tell a different story and can better prepare you for seismic market events. For example, the 44.2 percent drop in 1931 that I noted above was preceded by two additional years of losses—9.5 percent in 1929 and 22.7 percent in 1930—and followed by an additional loss of 6 percent in 1932. So $1,000 invested in 1929 would have been worth only $367 at the end of 1932. Or how about the fact that if you invested $1,000 in April of 1930, by the end of 1932 your investment would be worth $140 (a loss of 86 percent). I wonder how many investors would "stay with the program" after an 86 percent loss of their investment?

Other notable "one-time" stock market events worth mentioning:

- 1945 recession: S&P lost 19 percent
- Bear market of 1973-'74: S&P lost 38 percent
- Black Monday, Oct. 19, 1987: S&P lost 20 percent
- Dot-Com Crash, January 2000 - October 2002: S&P lost 35 percent
- Asian Economic Crisis, Oct. 27, 1997: S&P lost 7 percent
- July 2002: S&P lost 15 percent in two weeks
- Since 2008, there were 11 days where the S&P lost 5 percent or more

It's also interesting to note the probability of some of these events as calculated by our current financial models. According to Richard Hudson (The Misbehavior of Markets), the probability of the 7 percent drop on Oct. 27, 1997, was one in 50 billion; the probability of the 15 percent loss in July 2002 was one in 4 trillion; and the probability of the October 1987 crash was one in 1050—so small a probability that it can hardly be measured.

So it appears that these highly improbable, unpleasant market events are happening with some regularity, and there is every reason to believe we will continue to experience both short- and long-term significant market downturns. The good news is that you know they will happen again and can prepare yourself for them. Keeping enough liquidity in your portfolio to meet your cash requirements over the next couple of years is a great way to protect yourself from having to sell an investment that is in a loss position to meet living expenses. Remember, over the long term, the S&P has returned on average about 10 percent per year and, regardless of the market downturn, it has always recovered and rewarded investors for their faith and patience.

myRA: Will Obama's Plan Work

By Joshua P. Itzoe, CFP®, AIF Greenspring Wealth Management, Inc. www.greenspringwealth.com

In January, President Obama directed the Department of the Treasury to create a new, government-backed retirement account dubbed "myRA." It aims to help lower-income Americans who are not covered by a plan at work begin saving for retirement. So the question is, "Will it work?" Or is the concept of myRA simply a nice talking point to include in a political speech? From my perspective, the answers are "no" and "yes," although I definitely agree with the president that we need to help all Americans save more so they can retire successfully. Here's a brief overview of how a myRA will work:

1. Employers can set up these accounts without cost and don't have to contribute to them.
2. The account will basically work like a Roth IRA—money goes in after-tax and can be withdrawn tax-free in retirement.
3. Like a Roth-IRA, contributions can be made up to $5,500 annually, and the same tax/penalty rules apply.
4. The accounts will be solely invested in government savings bonds (paying historically low yields) and are principal protected (meaning they cannot lose value).
5. The accounts are portable, meaning they can be kept when switching jobs.
6. There are no administrative fees.
7. Once an account reaches $15,000 or is open for 30 years, it gets converted into a Roth IRA.
8. Initial investments can be as low as $25 and as little as $5 for subsequent contributions.

In my opinion, there are a number of issues with this plan—namely, that the types of people these accounts target (lower-income and part-timers) simply don't make enough money to save. With no automatic enrollment requirement and no required employer contribution, what is the incentive to contribute? The issue these workers face is the same even when they are covered by a plan at work, even if the employer makes a matching contribution—they either don't have the money to save or don't join the plan because of inertia. The only thing that can get these people to participate is automatic enrollment.

Also, it's ironic that a myRA basically flies in the face of the Pension Protection Act of 2006 (PPA). Under PPA, companies were encouraged to adopt automatic enrollment, automatic escalation, and a "qualified default investment alternative" suitable for long-term retirement savings (such as a target date fund, balanced fund, or managed account—but not a principal protected bond fund). The myRA approach includes none of these things.

I applaud the president for his intent with myRAs, but like many things (political and otherwise), the devil is in the details. Given the fact that these workers could simply open a Roth IRA, do we really need another type of retirement account? While some companies may adopt these, I fear the utilization rate will still remain very low.

Financial Empowerment for Woman

By Cheryl J. Sherrard, CFP® Clearview Wealth Management clearviewwealthmgmt.com

It is estimated that women will control two-thirds of the consumer wealth in the U.S. over the next decade.[1] Whether this is the result of sweat equity from building a business, the disciplined savings as a corporate executive, or through an inheritance from a spouse or other family member, it brings with it great power and great responsibility. Control over this wealth presents an opportunity for women to demonstrate their values and priorities through the choices they make with their money.

There are lessons to be learned today, whether you are managing thousands of dollars or millions of dollars. The principles are the same, but it first takes a resolution on your part to begin the journey by engaging in your personal financial situation. The lessons to be learned can, in their simplest state, be condensed to the following four guiding principles.

1. Be informed

If the area of finance is foreign to you, you have a choice: to put your head in the sand and remain uneducated or to begin today to learn the ropes of your financial situation. As you know from other areas of your life, when you are lacking knowledge in a particular area, you search out the experts. Your financial education needs to include input from those whom you can trust—people who will truly help you to learn and understand, and who will be advocates for you in future financial decision making. Partnering with a financial advisor who is your fiduciary will help ensure they are always acting in your best interest.

Wherever you begin, strive to continue learning and expanding your own knowledge so that you stay engaged and make informed decisions about your future. This will serve you well when those decisions involve greater wealth and have potentially greater impact on those whose lives you touch. Even if you are not the primary breadwinner in your current situation, stay informed about the details of your family finances, so that there are no surprises down the road. Because the future is unknown and uncertain, you should always stay engaged in the economics of your situation. Ignorance is not bliss; ignorance puts someone else in control of your financial future.

2. Be responsible

The United States is one of the wealthiest nations in the world. There exists a culture of "excess," and most have become so accustomed to it that they don't even recognize it anymore. Every day, no matter the amount of your wealth, you make choices as to how you use that wealth. Those choices teach lessons to others, both directly with those whose lives are dependent on you, and indirectly with those who watch and learn from afar. Are you teaching wastefulness and self-centeredness, or are you teaching how wealth can be used to positively impact the lives of countless others? Responsible use of all your resources is a lesson that needs to be learned by this generation and passed on to future generations so that the future remains bright for all.

3. Be Passionate

As women, there seems to be hardwired within us an innate capacity to care about others and about our world. When we are in control of wealth, we are presented with

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a plethora of options as to how to invest. The beauty of having so many options available is that we can choose to invest with our values and speak loudly and clearly about what is important to us.

We have the opportunity to tailor our investing in such a way that our choices are a reflection of our values and the causes we support. It is possible to target certain areas we are passionate about to focus on for our portfolio investments. You may wish to invest in companies that are truly supporting environmental sustainability. Conversely, you may choose, for example, to exclude companies that support alcohol production if you consider this to be offensive. You have the choice to let your voice be heard.

Additionally, women tend to be the ones who control much of the charitable giving that occurs from within their families. Giving to causes you support can have a tremendous impact on others and can also serve to model desired behavior for future generations.

4. Be Realistic and Reasoned
Inaction is sometimes the easiest choice, but it is usually the most ineffective choice. No matter the excuse, when you do nothing, you are giving control of your future over to others. Whether you control a Fortune 500 company or spend your day helping mold the minds of children (yours or others), you make decisions each and every day to help shape the world in which you live.

Decisions about your wealth will have long-lasting physical, mental, and emotional effects, both for you and those whose lives you touch. Do not leave those decisions in the hands of others. There will be many advisors who will be more than happy to assist you with your wealth—choose wisely! This is not a decision to be taken lightly. Talk to other people to learn which credentials are meaningful. Check the disciplinary history of advisors you are considering and insist on someone who will act as your fiduciary, always putting your best interests first. Find someone to partner with in your financial dealings who will truly listen to your passions and your goals and work with you to design a blueprint for achieving those goals, one step at a time. You don’t have to tackle everything at once. Instead, prioritize the action items and systematically work your way through the list. The hardest step to take is usually the first one. Resolve to begin the journey today.

Women of today are intelligent, empowered, and in control of vast amounts of wealth. It is imperative that you take seriously the management of your wealth, doing so in a way that secures the future for both you and your family. That speaks to the “caretaker” inherent in all women. This year, go one step further and allow your wealth to speak clearly about your other priorities by investing with your values, giving back to causes you find worthy, and allowing your wealth to make a statement about what you consider to be important in the world.

[1]*U.S. Women Control the Purse Strings. Neilsen.com, April 2, 2013.*

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