

# The Rice Paper

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Issue 4

## Raymond James Financial Services

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We are enthusiastically looking forward to the start of Spring. We hope everyone has success planting their Forget Me Not seeds.

We will be sending out the educational seminar schedules soon and hope we can get most of you to attend in person or via web conferencing.

It is still our goal to meet with each of you this year; feel free to call us to set up an appointment if we have not contacted you as yet.

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## Lessons From the Antarctic

The past few years have been tumultuous to say the least. We live in a time of economic downturn, wars, and a prevalence of crime and dissent in our society. With all of the bad that goes on around us, we still have much opportunity and capacity to do good in this world. I recently came across the story of an early twentieth century explorer, Earnest Shackleton, his ship Endurance, and his crew. They give us an exceptional example of perseverance and overcoming hardship.

Shackleton and the crew of the Endurance were attempting to be the first group to cross Antarctica. The Endurance set sail on December 5th, 1914, from South Georgia Island. Their intended destination was Vahsel Bay in the Weddell Sea. They encountered unseasonably excessive amounts of pack ice, and the Endurance became ice bound. After nine months trapped in the ice, The Endurance succumbed to the constant pressure of the ice.

Shackleton ordered his 28 crew members to salvage what they could and to release the life boats. They set up camp on the ice floe and hoped that the ice drift would take them close to Paulet Island, where they knew that supplies were cached. They made several attempts to cross the ice floe by dragging the life boats and their supplies, but found the ice to be impassable. They calculated on March 17th that they were within 60 miles of Paulet Island. Several weeks later the ice floe broke in two. Shackleton ordered his men into their lifeboats and ordered them to row towards the nearest Island. After five days of constant rowing, in perhaps the most dangerous sea on Earth, the three life boats landed on Elephant Island.

Elephant Island was an inhospitable landing spot. Shackleton, concerned by the lack of resources on the island, decided to try a risky open boat journey to South Georgia Island. Shackleton rigged the sturdiest of the lifeboats with a mast and sail, and set out with five of his crew. Fifteen days later, the cliffs of South Georgia were in view; however, hurricane-force winds made it impossible to reach the island. The six men were forced to wait at sea in a life boat until the hurricane passed.

The following morning they finally made landfall on the uninhabited south shore of the island. Shackleton was afraid his boat was so severely damaged that they would not be able to sail to the other side of the island. After a brief rest, Shackleton and two other crewmen set out with only 50 feet of rope and a carpenter's adze, to cross the treacherous landscape of South Georgia. They were the first men to make the 22-mile journey and did so in 36 hours.

Immediately upon his arrival at the whaling station, he sent a boat to pick up the three men on the other side of the island, and began a plan to rescue his remaining crew still on Elephant Island. His crew was rescued from the island on August 30th, 1916, 634 days after they first left South Georgia Island. All 28 crew members (including one unfortunate stowaway) were alive and in relatively good health.

Those same principles of perseverance and tenacity apply to us today, just as they did to Earnest Shackleton and the crew of the Endurance. If we stay the course and continue to do well in our own lives, jobs, and families, we will overcome the trials of our time.

## Are We in a Bond Bubble?

Investors have been pouring money into bonds. Investment Company Institute statistics show that since January 2007, average net new money going into bond mutual funds each month has been roughly four times greater than net *outflows* from equity funds.\* So does that mean we're in the bond market's equivalent of the late-1990s tech bubble?

### What's been driving interest in bonds?

There are several reasons why bond funds have been attracting investor interest. First, in the wake of both the tech crash of 2000-2002 and the 2008 financial crisis, the Federal Reserve felt it needed to make credit more available by lowering interest rates. Over the last 10 years, the yield on the 10-year Treasury bond has fallen from 5% to well under 3% at the end of 2010.\*\* And for the first time ever, 5-year Treasury Inflation-Protected Securities (TIPS) actually paid a negative yield when they were auctioned last October.\*\*\* Because bond prices rise as interest rates fall, that has increased bond prices generally.

As a result, bonds have outperformed stocks in recent years. For the last 20-year period, total returns from stocks and bonds have been equal: 8.2%.\*\*\*\* And during the decade between January 2000 and the end of 2009, bonds actually outperformed stocks; the S&P 500 saw a total return of -0.9%, while long-term government bonds returned 7.7%.\*\*\*\* That outperformance has lured investors who may have forgotten that past performance doesn't guarantee future results, and invest in an asset class based on its recent history rather than its prospects for the future.

Demographics also have played a role. Many aging baby boomers who became accustomed to investing much of their IRAs and 401(k)s in stocks are beginning to realize that their time horizon for retirement isn't as long as it used to be, and that they should consider allocating an increasing percentage of their retirement portfolios to income-producing assets. The financial crisis also sent many frightened investors scurrying to put their money anywhere besides stocks.

Finally, diminished dividends from stocks have encouraged many investors to look elsewhere for income. During the tech boom, companies preferred to reinvest in growth or buy back stock rather than increase dividends, and according to Standard and Poor's, 2009 was the worst year on record for dividend payments. Though there has been some reversal of that trend in recent months, stingy dividends helped make bonds and their income more attractive.

### What to watch out for

No investing trend lasts forever without interruption. Here are some factors that could affect bond prices:

- Signs that inflation is picking up: Higher inflation means fixed income payments will have less purchasing power in the future, diminishing bonds' appeal as income vehicles.
- Fed reversal on interest rates: As the economy recovers, the Federal Reserve will need to withdraw the support it has given the bond markets. As it gradually ratchets up interest rates, bonds will begin to reverse their pattern of the last decade. Depending on the pace of the Fed action, that reversal could be swift. Rising interest rates typically mean falling bond prices, and longer-term bonds often feel the most impact because bond buyers are reluctant to tie up their money long-term if a better rate lies ahead.
- Lack of overseas interest in U.S. debt: Foreign buyers have been large purchasers of U.S. government debt. If foreign buyers show signs of turning away from U.S. debt, it could send shivers through the bond markets.
- Muni bond troubles: Some experts worry that defaults by cash-strapped state and local governments could become a problem.

However, balance those factors against the possibility of further sovereign debt problems abroad. Several European nations are still struggling to deal with their debt problems; another bout of global jitters like the one in spring 2009 could remind investors that the United States has never defaulted on its debt. Also, if the potential for deflation that the Fed is so concerned about turns into an actual decline in wages and prices, that could be a positive for bonds, since the income they pay would be more valuable as prices fall. Either way, now is an especially good time to keep an eye on your bond investments.

\*Average of monthly net new cash flows from January 2007 through September 2010 as reported in Investment Company Institute's "Long-Term Mutual Fund Flows Historical Data" as of Nov. 20, 2010.

\*\*Source: U.S. Treasury historical data on daily Treasury yield curve rates.

\*\*\*Source: "Record Setting Auction Data," [www.treasurydirect.gov](http://www.treasurydirect.gov).

\*\*\*\*10- and 20-year returns based on data on the Standard and Poor's 500 and long-term government bonds from *Ibbotson SBBI 2010*.



***Bond outperformance has lured investors who may have forgotten that past performance doesn't guarantee future results.***

## Retirement Plan and IRA Limits for 2011

Many retirement plan and IRA limits are indexed for inflation each year. Some of the key numbers for 2011 are discussed below.

### Elective deferrals

If you're lucky enough to be eligible to participate in a 401(k), 403(b), 457(b), or SAR-SEP plan, you can make elective deferrals of up to \$16,500 in 2011, unchanged from 2010. If you're age 50 or older, you also can make a catch-up contribution of up to \$5,500 to these plans in 2011 (also unchanged from 2010). (Special catch-up limits apply to certain participants in 403(b) and 457(b) plans.)

If your 401(k) or 403(b) plan allows Roth contributions, your total elective contributions, pretax and Roth, can't exceed \$16,500 (\$22,000 with catch-up contributions). You can split your contribution any way you wish. For example, you can make \$9,500 of Roth contributions and \$7,000 of pretax 401(k) contributions. It's up to you.

If you participate in a SIMPLE IRA or SIMPLE 401(k) plan, you can contribute up to \$11,500 in 2011 (unchanged from 2010). If you're age 50 or older, the maximum catch-up contribution to a SIMPLE IRA or SIMPLE 401(k) plan in 2011 is \$2,500 (unchanged from 2010).

### IRA limits remain the same for 2011

The amount you can contribute to a traditional or Roth IRA remains at \$5,000 (or 100% of your earned income, if less) for 2011, and the maximum catch-up contribution for those age 50 or older remains at \$1,000. You can contribute to an IRA in addition to an employer-sponsored retirement plan. But if you (or your spouse) participate in an employer-sponsored plan, your ability to deduct

Contribution limits: 2011 tax year*		
Plan type	Annual dollar limit	Catch-up limit
401(k), 403(b), govt. 457(b) plans	\$16,500	\$5,500
SIMPLE plans	\$11,500	\$2,500
Traditional and Roth IRAs	\$5,000	\$1,000

\*Contributions can't exceed 100% of your income. Special catch-up rules apply to 403(b) and governmental 457(b) plans.

traditional IRA contributions may be limited, depending on your income. Roth contributions are also subject to income limits.

### Some other key numbers for 2011

For 2011, the maximum amount of compensation your employer can take into account when calculating contributions and benefits in qualified plans (and certain other plans) is \$245,000 (unchanged from 2010).

The maximum annual benefit you can receive from a defined benefit pension plan is limited to \$195,000 in 2011 (unchanged from 2010).

And the maximum amount that can be allocated to your account in a defined contribution plan (for example, a 401(k) plan or profit-sharing plan) in 2011 is \$49,000 (also unchanged from 2010), plus age-50 catch-up contributions. (This includes both your contributions and your employer's contributions. Special rules apply if your employer sponsors more than one retirement plan.)



Income phaseout range for determining deductibility of traditional IRA contributions in 2011

1. Covered by an employer plan	
Single/head of household	\$56,000-\$66,000 (same for 2010)
Married filing jointly	\$90,000-\$110,000 (\$89,000-\$109,000 for 2010)
Married filing separately	\$0-\$10,000
2. Not covered by an employer plan, but filing joint return with a spouse who is covered	\$169,000-\$179,000 (\$167,000-\$177,000 for 2010)
Income phaseout range for determining ability to fund Roth IRA in 2011	
Single/head of household	\$107,000-\$122,000 (\$105,000-\$120,000 for 2010)
Married filing jointly	\$169,000-\$179,000 (\$167,000-\$177,000 for 2010)
Married filing separately	\$0-\$10,000

**Many retirement plan and IRA limits are indexed for inflation each year. Most of the limits for 2011 are unchanged from 2010.**

## Ask the Experts

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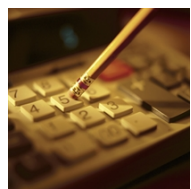
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### Understanding the math of recovering from losses

Everyone knows the stock market has its ups and downs, but just what's involved in recovering from a serious down? If you lose 10% one year but your

portfolio returns 10% the next year, are you even again?

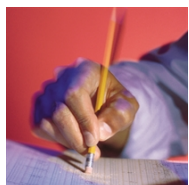
The short answer: no. The math of recovering from a loss isn't quite that symmetrical. You have to gain more than you lost to recoup all your losses. To understand why, let's look at a hypothetical example. Say you have a \$50,000 portfolio. In Year 1, you suffer a 10% loss and are down \$5,000. That leaves your portfolio worth only \$45,000.

In Year 2, the market rebounds and your portfolio rises by 10%. However, that 10% increase is based on a \$45,000 portfolio, not \$50,000. That means the 10% return adds only \$4,500 to your portfolio, not \$5,000, leaving you still \$500 down from where you started. You would actually have to earn a return of a little over 11% to get back to your original \$50,000.

The bigger the loss, the bigger that rebound needs to be to get you even. For example, if that \$50,000 portfolio had taken a 40% hit, as many did in 2008, you'd need almost a 67% increase to offset that \$20,000 loss and get back to the original \$50,000. That could take several years even if stocks perform well.

The challenge is compounded by investor psychology. Adjusting your asset allocation to aim for a higher return is one way to try to recoup losses faster. However, many investors find it difficult to take on additional risk after having watched their investments take a hit. And there's no guarantee that more risk will necessarily produce the desired result--at least not within the desired time frame.

The lopsided nature of recovery from market losses underscores why risk management is such a key component of successful portfolio management. Being realistic about the level of risk your portfolio involves and how much time you have to come back from potential downturns may help increase both your emotional and financial resilience.



### Are you sabotaging your own portfolio?

Individual investors' returns typically fall short of those for the stock market as a whole. Why? Because their returns are affected by their own behavior. Many studies

have shown that individual investors tend to buy and sell at the wrong times. When the market goes down, they panic and sell. When the market rebounds, many gun-shy investors are reluctant to invest again and postpone getting back into the market. As they watch prices rise, they get increasingly anxious about missing out on those returns. However, by the time these investors are comfortable with buying again, prices often have risen to the point that they're almost ready to turn down again.

That kind of behavior can be costly over the long term. Dalbar's *Quantitative Analysis of Investor Behavior for 2010* compared the performance of the average mutual fund investor between 1990 and 2009 (as measured by fund inflows and outflows tracked by the Investment Company Institute) to that of the average index fund based on the S&P 500.\*

The company found that returns for the average

investor trailed the S&P over that 20-year period by 5.6% because of investor behavior. Though there's no guarantee that the patterns of the past will continue in the future, previous studies also reached the same conclusion: that investors often earn less than a mutual fund's reported returns because of their own behavior.

How can you prevent self-inflicted portfolio sabotage? A disciplined approach to investing helps. Some techniques that can give you a framework for decisions that aren't based solely on emotion include establishing a target price based on fundamentals, dedicating specific pools of money to specific goals with defined time horizons, and rebalancing investments periodically. Also, understand your true risk tolerance. Knowing the type and level of risk involved in each of your investments and understanding how each has behaved relative to the overall market can help you stand firm despite losses.

\*Based on the average return for all funds listed in Lipper's U.S. Diversified Equity fund category.