Jon Kagan CFP®
CERTIFIED FINANCIAL PLANNER™

Soundings

What's New – October 2009

Quote of the month:

"Most human beings have an absolute and infinite capacity for taking things for granted."

- Aldous Huxley 1894 – 1963

I chose this month's quote to frame our upcoming seminar on **Estate Planning**. What would happen to your family if you didn't come home today? Understandably, most of us don't want to think about it and by default take for granted that things will work out. **Estate planning** is not just something wealthy people do to make sure the favorite nephew gets the beach house. It's about making sure your family is taken care of if, God forbid, you have a premature departure. Among the topics to be discussed, we'll cover the various legal documents and how they are used in estate planning, how the laws are changing and what effect it could have on your existing documents, and things to consider when choosing an executor or trustee. This year, we have a special guest speaker, ***Attorney Kristen Marks***, who will lend some new insight to this important subject. Check out her website at www.mypinklawyer.com and see why I'm excited about this year's event.

Upcoming Events

The Top 10 Disastrous Planning Mistakes People Make that Devastate their Families Oct 13

Seminar dates and locations are subject to change, please call Evelyn or Jan at 936-6686 for more details

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Market Update – Year to Date Returns

Major Stock Indexes	(As of 10/01/09)*
Dow Jones Industrials	10.7%
S&P 500 Index	17.0%
NASDAQ Comp	34.6%
Dow Jones World Index (ex US)	32.7%
Russell 2000 (small cap index)	21.0%

Major Bond Indexes	
Broad Market – Barclays Capital Aggregate	6.1%
High Yield Corporate - Barclays Capital	48.7%
Municipal Bond - Barclays Capital	14.2%

Lipper Mutual Fund Categories	
Large Cap Growth	29.1%
Large Cap Value	19.0%
Small Cap Growth	31.1%
Small Cap Value	27.6%
International	31.9%

Source: The Wall Street Journal and Barclays Website

- Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect investment performance. Individual investor's results will vary

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Market & Economic Commentary

We have certainly come along way since the ***generational lows*** of last March. To put those lows in statistical perspective, ***Raymond James Chief Market Strategist Jeff Saut*** recently noted, "*equity markets were at least three, and possibly four, standard deviations below norms. Remember that a three standard deviation event is something that is supposed to occur once every 750 years, while a four standard deviation event happens every 31,750 years.*" Given that spectacular freefall, it wasn't surprising to see the flipside when the news stopped getting worse. So here we are with the ***Dow*** up 47% since the March low and completion of the strongest quarter since 1998 and best third quarter since 1939. Where we'll be next week is anyone's guess but given the fact that we still sit more than 30% off the highs from October of 2007, there is enough cash on the sidelines to buy the entire ***S&P 500***, and we have nations with a billion people who are just discovering the wonder of capitalism, even with all the challenges facing our increasingly "global" economy, there are opportunities for those with a process, discipline and courage of conviction.

I'm going to shift gears now and talk about a subject nearly all of us will share at some time, how to come up with our **income in retirement**. The myriad of options available cover all the colors of the rainbow but in reality, they all entail the use of one of three broad methods: a **pension or annuity**; drawing income from **fixed income securities**; or **systematic distribution from a diversified portfolio** of multiple asset classes. Each has its own benefits and shortcomings and we'll briefly go through them below.

Pensions or **Defined Benefit Plans** shift the risk of retirement planning from the employee to the employer. They can be public, like those available to Government and Military retirees, or private like those formerly seen in the auto and airline industries. They may be indexed to inflation and have a survivor benefit to cover a spouse if the participant passes prior. Individuals not subject to a pension can create their own by buying an annuity from an insurance company and choose the features for their situation. The **biggest risk** with these arrangements is that they are backed by the *claims paying ability* of the organization…think: ***GM, AIG*** or ***Eastern Airlines*** and you'll see that nothing in life is without risk.

Next is the **Fixed Income** option where an individual purchases fixed income securities that pay dividends, typically **government bonds**, **corporate bonds**, or **certificates of deposit** and lives off the dividends or interest. This used to be the conventional wisdom, particularly for more risk averse investors who liked the fact that if these securities are held to maturity, they get a return of their principal (caveat to follow). The **risks** with this option include *default risk* (except for Government bonds), *inflation risk* (the income you receive stays fixed for the life of the security even when the price of "stuff" doesn't, *reinvestment risk* (your cd's earning 5% mature and current cd rates are 2%), and *interest rate risk* (if the prevailing interest rates are rising, the principal value of your fixed income investment will decrease because the potential buyer of your bonds can get a better rate on a new bond).

Finally, using **Systematic Withdrawals** from a diversified portfolio of multiple asset classes, an investor would have a predetermined allocation of stock, bonds, cash, and possibly alternative investments and live off a systematic distribution of that portfolio. Depending on a variety of factors, a distribution rate between 4 – 6% of the total portfolio would be used to provide monthly income with periodic reviews to assure the health of the plan. The **overall risk** of this strategy is a combination of the risks discussed previously with the addition of *market risk* associated with the stock or equity portion. This strategy is the basis of ***Modern Portfolio Theory*** which attempts to lower the overall risk of a portfolio by adding asset classes that react in different ways to different market and economic conditions in an attempt to have some zig while others zag in order to smooth out returns over time. In reality, few people use one method exclusively but tend to use a **combination of all three**

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and identify different income buckets for different types of expenses. The important thing is to have a plan and a thorough understanding of your cash flow situation so that it works in both the short and long term and accounts for changes in your life as well as the economy in which you live.

On a Personal Note

September 16th marked the **five year anniversary of *Hurricane Ivan***, an event that changed all of our lives down here in the greater Pensacola area. It would be too easy to tell a bummer of a story so I thought I'd share a funny one. About five years prior to the storm, we found an older house in pretty rough shape, but on a beautiful lot on the water. It had been vacant for nearly two years and as we cleaned the cockroach droppings from the pantry closet and I tried to comfort ***Kathleen*** who was wondering out loud what we had gotten ourselves into. I assured her everything would work out and we'd made a great investment. Privately, I remember thinking the best thing that could happen was a hurricane so we could just start over. Fast forward five years…our house had been transformed into a home with a bunch of love and gallons of ***sweat equity***. With ***Hurricane Ivan*** about 8 hours away, I made a final walkaround to check on the boards I put up around all the south-facing windows. At that time I noticed that where the old outdoor showerhead protruded from the siding, there was room for a driving rain to work its way in. We couldn't have that, it might lead to some longer term rot problems so it was off to ***Lowes*** to get some caulk for a quick repair. Talk about a case of ***monumental underkill***; when we were able to get back home the day following the storm, the back of the house was now in the front yard along with most of our "stuff". The good news is our insurance came through, we learned that "stuff" can be replaced, and to value what can't.

Probably the ultimate lesson on valuing the things that really matter comes from my friend, ***Jack deJarnette,* a United Methodist Minister on disability leave while he waits for a kidney**. He's got a couple *older models* that need to be traded in due to years of damage from anti-rejection medication that came with a heart transplant more than 10 years ago. Being the wonderful person that Jack is, 14 people have offered but given the stringent requirements placed on potential donors, all were eventually disqualified…until last week. Jack is scheduled to receive a transplant on October 26th from a man who walked into his church about a year ago and said that he heard a pastor needs a kidney and he's got one for him. Go to **www.jackdejarnette.blogspot.com** to visit Jack's blog and follow his story.

Well the ***H1N1 has come and gone at the Kagan household***. ***Collin*** went to bed a couple Wednesday's ago feeling a bit puny. He woke up at 5:00 the next morning with a 102º fever and pretty rough *gastrointestinal distress*. We got him on that miracle-drug ***Tamiflu*** later that morning and by Saturday, he was feeling pretty close to 100%. Not wanting to miss out on anything his younger bro' got, ***Al*** was pushing 103º when he woke up on Tuesday. ***Tamiflu*** to the rescue again, although with Al's *less accomplished pill-popping skills*, I almost had to wrap it in cheese and stick it down his throat! All's well that ends well and both the boys will be back to school tomorrow.

Warmest regards,

Jon

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