Investor Insights & Outlook

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Saving for an Emergency

According to a recent survey conducted by Bankrate.com, 28% of Americans have no emergency fund, up from 24% a year ago. About 49% of people surveyed said they had no emergency savings or less than three months' expenses.

The traditional prescription for life's financial emergencies is to hold three to six months' worth of living expenses in cash. Only 25% of those surveyed said they had enough to cover six months' or more of expenses. In a low-yielding environment, many are concerned that keeping aside six months' of emergency savings is a lot of money to have sitting in the bank earning next to nothing. While this is a valid concern, customizing your emergency fund to fit your personal situation may serve as a viable solution.

Consider holding a larger emergency fund (six months to a year) if you have a high paying job, are self-employed, work on a freelance/contract basis, have dependents, have a nonworking spouse, have high fixed expenses (mortgage, auto loan, tuition bills), or have a pre-existing medical condition that could result in hefty health-care bills if you were forced to purchase private health insurance. On the flip side, you may be able to get by with a smaller emergency fund if you:

1. Have a good degree of career flexibility because you are in a lower-paying position and/or haven't yet developed a specialized career path.

2. Have other sources of income that could help defray a large share of household expenses, such as a working spouse.

3. Have a great degree of lifestyle flexibility (for example, you would be willing to relocate).

Source: Bankrate.com Financial Security Index survey, June 25, 2012.

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Advisor Corner

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Bill Roller is experienced in financial planning and investment analysis. He focuses his consulting practice on estate, retirement, and financial planning for businesses and individuals. Bill started BR Capital Inc. in 2003 and registered it as an investment advisory firm in June, 2004. Before that he worked for a large Wall Street firm for over nine years. He served for seven years as a U.S. Army officer in Infantry and Special Forces (Green Beret) units. Bill is a Chartered Financial Analyst as well as a Certified Financial Planner. He is the past president of the Estate Planning Council of Southwest Washington. He earned a Bachelor of Science degree from the United States Military Academy at West Point in 1982, and a MBA from the Wharton School of Business in 1991. He provides the morning and afternoon market reports and financial commentary for AM 1360 KUIK. A link to Bill's articles and interviews is available at http://brcapitalinc.com. To subscribe to articles and daily market updates go to http://brcapitalinc.com/subscribe/

Monthly Market Commentary

January saw a mixed bag of economic news for both bulls and bears to feast on—negative GDP report, positive employment adjustments, and a good long-term housing trend overshadowed by inventory shortages of homes, new or used, in the short-term. Morningstar economists believe that the market's positive reaction to the seemingly bearish but actually bullish GDP report was the correct interpretation. However, bad weather, the bad GDP report, the temporary shortage of home inventories, and the increased payroll tax and tax refund delays will likely weigh on upcoming economic reports.

GDP: The first estimate of GDP indicated that the economy shrank 0.1% in the fourth quarter of 2012, compared with growth of 3.1% in the third quarter. Consumption, business investment, and housing components of GDP all did better than expected, while government and inventories were the main detractors. While the negative GDP number was shocking, closer examination suggested that government bill payers and overly cautious businesses were largely to blame for an otherwise excellent report.

Employment: January employment grew at a satisfactory pace, with 157,000 jobs added. More importantly, significant annual revisions showed exceptionally strong employment growth in the fourth quarter of 2012. Construction and retail were standout performers after the adjustments, while most other categories did not show meaningful changes. Employment growth for the whole of 2012 averaged 181,000 per month, up from 153,000 per month prior to the upward revisions. Unfortunately, the U.S. economy has still only just recovered 5.5 million of the 8.7 million jobs lost during the recession. The unemployment rate in January inched upwards to 7.9% from 7.8% the month before.

Housing: Housing starts soared in December, coming in at 954,000 units compared with just 851,000 units the previous month. The good news is the growth was geographically dispersed and included nice improvements in both single-family homes and apartments; the bad news is that current housing starts are still well below 50-year averages (about 1.5 million units). On the other hand, new-home sales in December came in at 369,000 units sold compared with the recovery record of 398,000 in November. In case you were wondering why there is such a huge variance between housing starts and new-home sales, the biggest difference is that new-home sales only reflect single-family homes while housing starts include a range of single-family homes to giant multifamily apartment buildings. Since the bottom of the housing crash, non-single family home starts have more than quadrupled, while single-family starts were up an impressive but more modest 66%.

Manufacturing: Although U.S. manufacturing isn't generally important enough to move the economic needle at this stage of the recovery, news in the last week of January was surprisingly and uniformly positive. Morningstar economists believe that given continued strong consumer purchases and improvements in China, a rebounding manufacturing sector should come as no surprise. However, the most recent GDP report does suggest that the manufacturers badly misgauged consumer demand in late 2012, and had shrunk inventories when they probably should have been expanding them. Outside the U.S., manufacturing in China and Europe has recently improved as well, with January's data indicating 24- and 10-month highs, respectively.

Auto: Excellent auto sales in January (15.28 million units) also proved to be encouraging news for the economy, with year-over-year sales up 14%. This number came very close to the highest month of 2012, which was November (15.5 million units), although November's number was aided by restocking after Hurricane Sandy.

Questions to Ask Before Venturing Into a Self-Directed IRA

A self-directed IRA enables investors to buy into asset classes that are often outside of the purview of fund companies and brokerage firms. These investments may include non-publicly traded real estate, private equity, and partnerships and joint ventures that may exhibit radically different performance patterns than stocks and bonds, a quality that bear-market-battered investors could be craving. In some respects, all IRAs are self-directed, in that as the account owner, you're entirely in control of what you put inside of your account. And on the surface, self-directed IRAs have features that are comfortably similar to conventional IRAs that hold stocks, bonds, or mutual funds. The contribution limits are the same, rollovers from other IRAs are permitted, and you can opt for a traditional or Roth version. However, investing in a self-directed IRA isn't as simple as sending a check and tuning out; far from it. In addition to analyzing the merits of a prospective self-directed IRA investment, it's also important to consider how the inclusion of a single, possibly large, and undiversified investment interacts with your other holdings. You also need to be aware of the different rules governing these accounts because you could run into serious trouble if you run afoul of them. Here are some of the key questions to consider before taking the plunge into the world of self-directed IRAs.

What will it cost? If you hold stocks or mutual funds in an IRA, your costs will be pretty transparent: mutual fund management fees and any commissions you might pay to buy and sell. Self-directed IRAs charge another layer of fees because you must go through a custodian, who in turn will invest in the assets on your behalf. As a result, there's typically a setup fee for a self-directed IRA as well as ongoing administrative costs; these costs can vary widely by custodian, so you really need to do your homework. Of course, investing in mutual funds or individual stocks isn't free, but taken together, the extra costs associated with self-directed IRAs mean that your investments will need to perform that much better than traditional stocks and funds just to pull ahead.

How does it fit with the rest of your portfolio? Even if you're sold on the merits of an investment you'd like to put inside of a self-directed IRA, such as a rental property, it's still important to consider how it fits with your overall portfolio. Are you sinking a disproportionate amount of your money into a single asset?

Do you thoroughly understand the rules? Self-directed IRAs come with a separate set of rules, the majority of which are designed to prohibit self-dealing, which is, essentially, obtaining use from an asset even though you're receiving a tax deferral on it. If the Internal Revenue Service learns of self-dealing, the entire sum in that IRA could be considered taxable and subject to the 10% early withdrawal penalty.

Funds in a traditional IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax-free, and can be withdrawn tax free if assets are held for five years. A 10% federal tax penalty may apply for withdrawals prior to age 59 1/2. Please consult with a financial or tax professional for advice specific to your situation. Diversification does not eliminate the risk of experiencing investment losses. Government bonds are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest, while returns and principal invested in stocks, commodities and real estate are not guaranteed. Real estate investment options are subject to certain risks, such as risks associated with general and local economic conditions, interest rate fluctuation, credit risks, liquidity risks and corporate structure. Investors should read the prospectus and carefully consider a fund’s investment objectives, risks, fees, and expenses before investing.

What's the Number?

"The 2012 Retirement Confidence Survey: Job Insecurity, Debt Weigh on Retirement Confidence, Savings," published by the Employee Benefit Research Institute in March 2012, includes the following highlights.

1) Only 14% of Americans are very confident they will have enough money to live comfortably in retirement. 42% of Americans identify job uncertainty as the most pressing financial issue facing Americans today.

2) 60% of workers report that the total value of their household's savings and investments, excluding the value of their primary home and any defined benefit plans, is less than $25,000.

3) 37% of workers in 2012 said they expected to retire after age 65, up from 11% in 1991. 62% of workers and 37% of retirees consider their current level of debt to be a problem.

4) 56% of workers report they and/or their spouse have not tried to calculate how much money they will need to have saved by the time they retire so that they can live comfortably in retirement.

5) 16% of workers and 11% of retirees are very confident that their investments will grow in value. But 67% of workers state that they are a little or a lot behind schedule when asked to evaluate their progress in planning and saving for retirement.

6) 24% of retirees are very confident about having enough money to cover medical expenses in retirement, and 18% of retirees are very confident about having enough money to pay for long-term care in retirement.

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