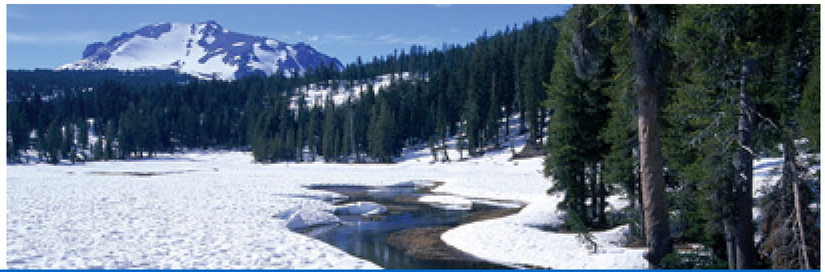

YOUR FINANCIAL FUTURE

Your Guide to Life Planning

February 2012

This month's edition of our newsletter should answer alot of questons for you. Please don't hesitate to call if we can clarify anything.

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Is Increased Inflation on the Horizon?

Worries about inflation have been cropping up more frequently lately, largely due to escalating commodity prices, which are pushing up consumer prices, both in the United States and abroad.

In Volatile Markets, Investors May Find Comfort in Dividends

As uncertainty at home and abroad roils the financial markets, income-minded investors seeking protection from the bumpy road ahead may find dividend-paying stocks offer an attractive mix of features and warrant a place in their equity portfolios.

The Three-Step Retirement Plan Tune-Up

Conducting an annual review of your retirement goals and strategy is a great way to help ensure that your plans for your financial future remain realistic and on track. With that in mind, taking the three easy steps outlined here will help you conduct your retirement tune-up.

College Planning: Teach Your Children to Save

Are you saving for a child's education? Be sure to include your child in your planning. Being part of the college planning process can be very educational for children, as it presents them with valuable financial lessons for the future.

Make a Plan to Reduce Your Debt

The recession -- and subsequent slow recovery -- has caused millions of Americans to focus even more closely on living within their means. If you are ready to face up to your own financial realities, one crucial step is to set out a plan of action.

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Is Increased Inflation on the Horizon?

Economists and market watchers have been warning investors about the prospect of increased inflation since the housing bubble burst in 2007.

Worries about inflation have been cropping up more frequently lately, largely due to escalating commodity prices, which are pushing up consumer prices, both in the United States and abroad. At the beginning of 2011, the inflation rate stood at a paltry 1.6%. By the end of the year, it had more than doubled to 3.4%.[1] And this could be just the start of a longer-term inflationary cycle. With an improving economy and soaring federal deficits, many experts feel that prices in the United States will inevitably pick up their pace even further.

Inflation Rates Around the World (as of December 31, 2011)[2]

Country	Rate
Brazil	6.5%
Canada	2.9%
China	4.1%
France	2.5%
Germany	2.1%
Greece	2.4%
India	9.3%
Italy	3.3%
Japan	-0.5%
Mexico	3.8%
Russia	7.0%
United Kingdom	4.8%
United States	3.4%
Venezuela	28.9%

Staying Ahead

For investors, staying ahead of inflation means choosing investments that are most likely to provide returns that outpace it. Here's a look at how a climbing inflation rate could impact various investment types and asset classes.

- **Domestic Stocks --** Although past performance is no guarantee of future returns, historically, stocks have provided the best potential for long-term returns that exceed inflation. An analysis of holding periods between 1926 and December 31, 2011, found that the annualized return for a portfolio composed exclusively of stocks in Standard & Poor's Composite Index of 500 Stocks was 9.83% -- well above the average inflation rate of 2.99% for the same period. However, over shorter time periods the results are not as appealing. For the 10 years ended December 31, 2011, the S&P 500 returned an average of only 2.92%, compared with an average inflation rate of 2.50%.[3]
- **International Stocks --** During the same 10-year span that ended December 31, 2011, the Morgan Stanley Capital International (MSCI) EAFE, which is composed of established economies such as Germany and Japan, outpaced U.S. inflation with an average return of 5.12%. The MSCI Emerging Markets index, which tracks developing world economies such as Brazil and China, was even more stellar, returning an average of 14.2%.[4]
- **Bonds --** Historically, investors have turned to shorter-term corporate and high-yield bonds for protection in rising-rate environments.[5] There are two types of bonds that receive a lot of investor interest when inflation starts to rise: Treasury Inflation-Protected Securities (TIPS) and I Savings Bonds. Both TIPS and I bonds are types of fixed-interest rate bonds whose value rises as inflation rates rise.
- **CDs and Other Cash Instruments --** The Federal Reserve is still keeping a tight lid on interest rates, forcing investors who hope to keep pace with inflation by investing in cash instruments facing a harsh reality. The rates on a one-year CD are averaging under 1%, while a five-year CD is yielding an average of under 2%, according to *Bankrate.com*. Money market and other bank savings accounts are also averaging well under 1%.[6]

Although many economists project overall U.S. inflation to remain modest in the near future, most see an uptick down the road. For investors, a well-rounded portfolio may be your best weapon. The key is to consider your time frame, your anticipated income needs, and how much volatility you are willing to accept, and then construct a portfolio with the mix investments with which you are comfortable. Consult your financial professional to discuss your specific needs and options.

[1]*Source: U.S. Bureau of Labor Statistics, January 2012.*

[2]*Sources: TradingEconomics.com; U.S. Bureau of Labor Statistics, January 2012.*

[3]Sources: Standard & Poor's; U.S. Bureau of Labor Statistics. The S&P 500 is an unmanaged index. It is not possible to invest directly in an index. Past performance is no guarantee of future results.

[4]Source: Morgan Stanley. The MSCI EAFE and MSCI EM are unmanaged indexes. It is not possible to invest directly in an index. Past performance is no guarantee of future results.

[5]Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price.

[6]Source: *Bankrate.com*, January 20, 2012.

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Dividend payouts are often seen as a sign of a company's financial health and management's confidence in future cash flow.

In Volatile Markets, Investors May Find Comfort in Dividends

As uncertainty at home and abroad roils the financial markets, income-minded investors seeking protection from the bumpy road ahead may find dividend-paying stocks offer an attractive mix of features and warrant a place in their equity portfolios.

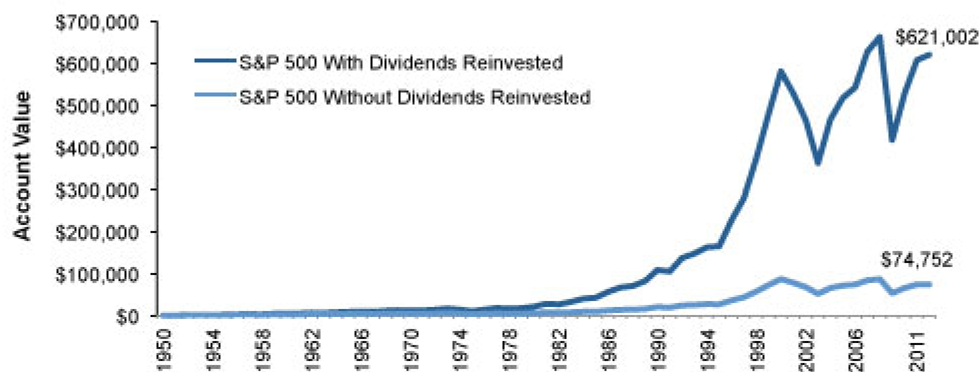
The appeal is simple: Dividend-paying stocks can provide investors with tangible returns on a regular basis regardless of market conditions.

The Benefits of Dividend-Paying Stocks

If you own stock in a company that has announced it will be issuing a dividend, or if you are proactively considering adding an allocation to dividend-paying stocks, history provides compelling evidence of the long-term benefits of dividends and their reinvestment.

- **A sign of corporate financial health.** Dividend payouts are often seen as a sign of a company's financial health and management's confidence in future cash flow. Dividends also communicate a positive message to investors who perceive a long-term dividend as a sign of corporate maturity and strength.
- **A key driver of total return.** There are several factors that may contribute to the superior total return of dividend-paying stocks over the long term. One of them is dividend reinvestment. The longer the period in which dividends are reinvested, the greater the spread between price return and dividend reinvested total return.
- **Potentially stronger returns, lower volatility.** Dividends may help to mitigate portfolio losses when stock prices decline, and over long time horizons, stocks with a history of increasing their dividend each year have also produced higher returns with considerably less risk than non-dividend-paying stocks. For instance, since 1990, the S&P 500 Dividend Aristocrats -- those stocks within the S&P 500 that have increased their dividends each year for the past 25 years -- produced annualized returns of 11.04% vs. 8.23% for the S&P 500 overall, with less volatility (14.14% vs. 15.22%, respectively).[1]

The Growth of Dividend-Paying Stocks, 1950-2011[2]



If you are considering adding dividend-paying stocks to your investment mix, keep the following thoughts in mind.

- **Dividend-paying stocks may help diversify an income-generating portfolio.** Income-oriented investors may want to diversify potential sources of income within their portfolios. Given current realities present in the bond market, stocks with above-average dividend yields may compare favorably with bonds and may act as a buffer should conditions turn negative within the bond market.
- **Dividends benefit from continued favorable tax treatment.** The extension of the Bush-era tax cuts helps to reinforce the current case for dividend stocks. The tax bill that passed in late 2010 extended the 15% tax on qualifying dividends and other forms of investment income through December 31, 2012.

Note that dividends can be increased, decreased, and/or eliminated at any time without prior notice.

[1]Volatility is measured by standard deviation. Past performance is no guarantee of future results.
[2]Source: Standard & Poor's. Stocks are represented by the S&P 500, an unmanaged index considered representative of the broad U.S. stock market. For the period January 1, 1950, through December 31, 2011. Past performance is not indicative of future results. Investors cannot invest directly in any index.

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Even if your personal outlook hasn't changed, keep in mind that uneven returns provided by different investments may have caused your portfolio to shift from your intended asset allocation.

The Three-Step Retirement Plan Tune-Up

Conducting an annual review of your retirement goals and strategy is a great way to help ensure that your plans for your financial future remain realistic and on track. With that in mind, taking the three easy steps outlined below will help you conduct your retirement tune-up.

Step 1: Review Your Retirement Goals

Your first step should be to review your retirement savings goals and assess whether anything significant has occurred during the past year that might affect either your outlook for retirement or your current strategies to prepare for it.

For example, have you decided to change the date when you'll retire? Or have you experienced any new milestones such as getting married, divorced, or having a child? Any of these events may affect how much you will want to save to fund the retirement you envision.

Step 2: Take a Fresh Look at Your Retirement Strategy

Your portfolio's specific mix of stocks, bonds, and cash, known as your asset allocation, should complement your financial goals, risk tolerance, and time horizon.[1] If you haven't taken a fresh look at your investments in a while, don't assume that your old asset allocation is still appropriate for your current needs.

Even if your personal outlook hasn't changed, keep in mind that uneven returns provided by different investments may have caused your portfolio to shift from your intended asset allocation. Given the market volatility that has occurred since 2007, if you have not reviewed your asset allocation since that time, there may be a good chance that uneven returns have caused it to change. If your asset allocation needs to be rebalanced, now may be the time for action.

Step 3: Consider Saving More

None of us know what the future may hold. A good way to improve the odds that you have saved enough for retirement is to save more, no matter how prepared you may already be.

If you have not already done so, consider funding an IRA. For the 2012 tax year, you can contribute a maximum of $5,000 and those aged 50 and older can make an additional catch-up contribution of $1,000. These limits are set annually by the IRS. More information can be obtained at www.irs.gov.

If you participate in a workplace-sponsored retirement plan -- such as a 401(k), 403(b), or 457 -- you can contribute up to $17,000 in 2012. Those aged 50 and over can add up to another $5,500. If you are eligible for a plan at work, but haven't enrolled yet, what are you waiting for?

Conducting a retirement tune-up is always a great idea, but don't forget to consult with your financial advisor to discuss what else you can do to help achieve retirement security.

[1]*Asset allocation does not assure a profit or protect against a loss in a declining market.*

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College Planning: Teach Your Children to Save

Many financial experts believe the best time to introduce children to college planning is when they are in the sixth, seventh or eighth grade.

Being part of the college planning process can be very educational for children, as it presents them with valuable financial lessons for the future. Children can earn money, learn about sources of financial aid, research potential colleges, and take other steps that may relieve their parents of some of the responsibility of college planning. In addition, some experts believe that if children are actively involved in planning for their future, they may be more committed when entering college and ultimately have a more successful experience than they would have otherwise.

Get an Early Start

Most children don't make plans for their higher education until they are well into high school, but the foundation for saving and planning for college can take place much earlier. Many financial experts believe the best time to introduce children to college planning is when they are in the sixth, seventh, or eighth grade. During this time, you may want to initiate discussions about college and explain the importance of developing good study habits and getting involved in extracurricular activities -- to instill the idea that your family supports higher education.

You may also want to encourage your children to begin thinking about the career they would like to pursue, which is likely to influence their choice of college, as well as to establish a savings account that could be earmarked for education expenses. In addition, you can teach basic lessons about compounding, investing, and other money management issues.

Take It to a Higher Gear in High School

By the time they reach high school, Many students are mature enough to plan for college at a deeper level, including the following.

- **Learning about college costs:** Students may gain a deeper appreciation of their family's financial sacrifices when they realize how expensive college is. They can learn about college costs from a number of sources, including the College Board (www.collegeboard.com) and the U.S. Department of Education (www.ed.gov).
- **Researching scholarships:** There are numerous Web sites with information about sources of financial aid. For example, www.fastweb.com and www.finaid.org contain search engines with data about thousands of scholarships with varying eligibility criteria. In addition, www.fafsa.ed.gov provides an overview of federal student aid programs. Also, local libraries and high school guidance offices may have information about state-sponsored aid programs and scholarships sponsored by local organizations.
- **Earning money:** High school students can set aside a portion of their wages from part-time or summer jobs for higher education expenses. Also, students may be able to obtain jobs that build on career interests as a way of solidifying their future plans.
- **Getting organized:** College planning encompasses numerous details, including visiting institutions that a student may want to attend, applying for financial aid, obtaining transcripts and letters of recommendation, and meeting deadlines. A high school student can take responsibility for making sure that important matters are tended to ahead of time. For example, if a student has a school vacation coming up, he or she could help organize a family trip to visit colleges of interest or spend some time completing college applications.

You and your prospective student may be able to think of more ideas that could add value to your family's efforts to save for a college education. Getting your budding scholar involved in the process -- financially and otherwise -- could ultimately be a pivotal lesson in responsibility that impacts his or her later success in life.

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Make a Plan to Reduce Your Debt

Once you have a record of your spending, compare your average monthly outlay with your monthly income.

The recession -- and subsequent slow recovery -- has caused millions of Americans to focus even more closely on living within their means. If you are ready to face up to your own financial realities, one crucial step is to set out a plan of action. Here are some key considerations to keep in mind.

Keep Track of Your Spending

It's hard to reduce your spending if you don't have a good idea of how much you are spending. Keep track of your typical monthly expenses for three months to find out where your money is going. To get an even more realistic idea, factor in some unexpected expenses -- such as auto and home repairs. Once you have a record of your spending, compare your average monthly outlay with your monthly income. If you have a surplus, this is the amount you can apply each month to paying down debt and building savings. If you have a shortfall, you'll need to examine your expenses more closely to see what you can potentially cut back or cut out.

Keep Saving

One way to establish good saving habits is to make saving even easier than spending. A handy tip is to set up separate savings accounts with separate goals attached to them. Here are three suggestions that can help you better allocate your savings.

- **Emergency Account:** Your goal for this account should be to build up at least three to six months of living expenses. This way, if you lose your job or need a lump sum to pay for a significant expense, you may not have to tap into your other savings or ring up more debt.
- **Family Account:** This account can help fund your children's school expenses (such as class trips and team uniforms) or vacations.
- **Investment Account:** This account should be reserved for general or long-term saving goals. Hopefully, you already have a retirement savings account (either through your workplace or on your own) and perhaps a college savings plan. But having another account to save for other longer-term goals -- maybe to start your own business or remodel your home -- can be a smart move.

Keep a Tight Watch on Your Credit Cards

If you've accumulated significant credit card debt, you've first got to stop the bad behavior. Paying off debt is easier once you stop using your credit cards.

- Pay off your highest interest credit card debt first, making sure you avoid the "minimum balance trap." Paying more than the minimum can make a big difference.
- Consolidate your debt by transferring outstanding balances to lower-rate cards. If you don't want to transfer your balances, you may be able to get your current credit card company to match the interest rate of a competitor.
- Cancel all cards except for the one that offers the lowest interest rate.
- Finally, set up a realistic payment timetable and stick with it. If you have trouble keeping pace, talk to a professional. The counselors at the nonprofit National Foundation for Credit Counseling can help develop a more structured plan for you. To find the nearest location, call 800-388-2227 or visit www.nfcc.org.

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