Demming Financial Services Corp.

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4th Quarter Newsletter

Fall 2014

Special Notes...

Items to review before year-end:

- Roth conversions
- IRA contributions
- RMDs
- 401K
- Estimated tax payments
- Charitable donations
- Annual gifting

As a friendly reminder, if you are still receiving statements from First Clearing and/or an individual fund company please contact us.

Also, please be sure to review the attached updated DFSC disclosure & privacy statements.

Happy Holidays!

Retirement Myths and Realities

Article Courtesy of Bob Veres

We all have some preconceived notions about what retirement will be like. But how do those notions compare with the reality of retirement? Here are four common retirement myths to consider.

According to the Bureau of Labor Statistics 2012 American Time Use Survey, retirees in 2012 spent 4.5 of their total 8 leisure hours per day watching television.

1. My retirement won't last that long

The good news is that we're living longer lives. The bad news is that this generally translates into a longer period of time that you'll need your retirement income to last. Life expectancy for individuals who reach age 65 has been steadily increasing. According to the National Center for Health Statistics, life expectancy for older individuals improved mainly in the latter half of the 20th century, due largely to advances in medicine, better access to health care, and healthier lifestyles. Someone reaching age 65 in 1950 could expect to live approximately 14 years longer (until about age 79), while the average 65-year-old American today can expect to live about another 19 years (to age 84) (Source: National Vital Statistics Report, Volume 61, Number 4, May 2013). So when considering how much retirement income you'll need, it's not unreasonable to plan for a retirement that will last for 25 years or more.

2. I'll spend less money after I retire

Consider this--Do you spend more money on days you're working or on days you're not working? One of the biggest retirement planning mistakes you can make is to underestimate the amount you'll spend in retirement. One

often hears that you'll need 70% to 80% of your preretirement income after you retire. However, depending on your lifestyle and individual circumstances, it's not inconceivable that you may need to replace 100% or more of your preretirement income. In order to estimate how much you'll need to accumulate, you need to estimate the expenses you're likely to incur in retirement. Do you intend to travel? Will your mortgage be paid off? Might you have significant health-care expenses not covered by insurance or Medicare? Try thinking about your current expenses and how they might change between now and the time you retire.

3. Medicare will pay all my medical bills

You may presume that when you reach age 65, Medicare will cover most health-care costs. But Medicare doesn't cover everything. Examples of services generally not covered by traditional Medicare include most chiropractic, dental, and vision care. And don't forget the cost of long-term care--Medicare doesn't pay for custodial (nonskilled) long-term care services, and Medicaid pays only if you and your spouse meet certain income and asset criteria. Without proper planning, health-care costs can sap retirement income in a hurry, leaving you financially strapped. Plus there's the cost of the Medicare coverage itself. While Medicare Part A (hospital insurance) is free for most Americans, you'll pay at least $104.90 each month in 2014 if you choose Medicare Part B (medical insurance), plus an average of $31 per month if you also want Medicare Part D (prescription coverage). In addition, there are co-pays and deductibles to consider--unless you pay an additional premium for a Medigap policy that covers all or some of those out-of-pocket expenses. (As an alternative to traditional Medicare, you can enroll in a Medicare Advantage (Part C) managed care plan; costs and coverages vary.)

4. I'll use my newfound leisure hours to ______ (fill in the blank)

According to the Bureau of Labor Statistics 2012 American Time Use Survey, retirees age 65 and older spent an average of 8 hours per day in leisure activities. (Leisure activities include sports, reading, watching television, socializing, relaxing and thinking, playing cards, using the computer, and attending arts, entertainment, and cultural events.) This compares to an average of 5.4 hours per day for those age 65 and older who were still working. So how did retirees use their additional 2.6 hours of leisure time? Well, they spent most of it (1.6 hours) watching television. In fact, according to the survey, retirees actually spent 4.5 of their total 8 leisure hours per day watching TV. And despite the fact that many workers cite a desire to travel when they retire, retirees actually spent only 18 more minutes, on average, per day than their working counterparts engaged in "other leisure activities," which includes travel.

Powerful Compounding

Article Courtesy of Bob Veres

Your teenager finished up their summer job and chances are the wages have been collecting in a bank account. What should happen with that money when your child goes back to school?

One possibility is to start a custodial Roth Individual Retirement Account, owned by your teenager. All you need is a custodial account with an adult co-signing (if the teen is under 18). That money can grow for many decades and come out tax-free 30 or 50 years down the road.

A 19-year-old who maxes out on a $5,500 Roth contribution every year until age 67, under the same rate of return assumptions, would see the account grow to $1,164,985.

How much are we talking about? If the money were to grow at an average rate of 5% a year (which, of course, is not guaranteed, but is in line with long-term averages for a balanced portfolio), then a $5,000 contribution at age 19 would grow to $52,006 by age 67. If your child waits until age 25 to invest the same amount in a Roth IRA, under the same return assumptions, the balance at age 67 would be just $38,808.

If that contribution becomes a habit, the numbers become more interesting. A 19-year-old who maxes out on a $5,500 Roth contribution every year until age 67, under the same rate of return assumptions, would see the account grow to $1,164,985.

Suppose your teen decides to spend some of that money, or use it for college tuition? Parents and/or grandparents can match whatever contribution the child decides to make, to bring the total back up to $5,500. The money in a Roth or other retirement account doesn't count toward the FAFSA financial aid form, so you don't have to worry about compromising the teen's financial aid eligibility. And having a hefty Roth IRA at retirement might address the possibility that Social Security won't be around, or as robust, when your kids eventually retire.

Sources:
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Third Quarter Investment Report: Moving Into Choppy Waters

Dear Clients,

You could say that the markets took a breather in the third quarter of 2014, but you would come to that conclusion only if you looked at the overall returns and ignored the drama of the past 30 days. The markets experienced a difficult month of September, giving up some of the gains from the prior eight months and causing investors to worry that we're about to experience more of the same. The end of the month was especially difficult, with a general market slide starting September 22, and some indices dropping more than 1% on the final day.

The Wilshire 5000--the broadest measure of U.S. stocks -- rose a meagre 0.37% for the third quarter even as it lost 1.71% in September. But the index is hanging on to a 7.26% gain for the year.

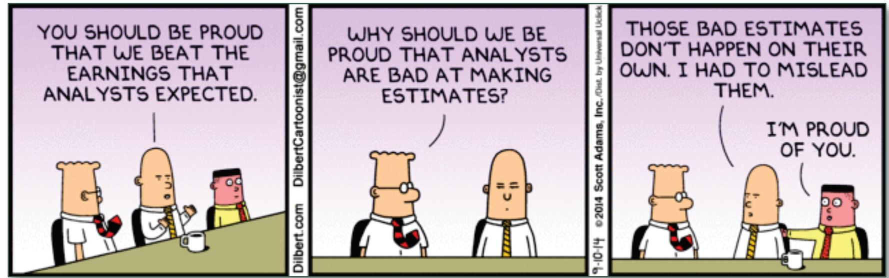
> *History tells us that it's a fool's game to try to anticipate market corrections, and that investors usually get rewarded for sailing through choppy waters...*

Large cap stocks were the market leaders over the past three months, but the gains were modest. The Wilshire U.S. Large Cap index gained 1.13% in the second quarter, and is now up 8.38% so far this year. The widely-quoted S&P 500 index of large company stocks posted an even smaller gain of 0.60% for the quarter. The index is up 6.7% since January 1, but it has fallen back from its record highs on September 18.

The news was less happy for smaller stocks. The Wilshire U.S. Mid-Cap index lost 3.54% in the third three months of the year, and is clinging to a 4.99% gain so far into 2014.

Small company stocks, as measured by the Wilshire U.S. Small-Cap, fell 4.98% in the third quarter (4.38% in September alone), but the index is hanging onto a positive 0.44% return heading into the year's home stretch. Meanwhile, the technology-heavy Nasdaq Composite Index managed to gain 2.45% for the quarter, and is up 7.88% for its investors so far this year.

The rest of the world put a drag on diversified investment portfolios. The broad-based EAFE index of companies in developed economies fell 6.39% in dollar terms during the third quarter of the year, and is now down 3.63% so far in 2014. The stocks across the Eurozone economies contributed to the foreign stock slide, dropping 7.37% for the quarter, but the red ink spilled over to most of the foreign indices in Asia as well. Ironically, the emerging markets stocks of less developed countries, as represented by the EAFE EM index, represented a bright spot, losing "only" 4.33% over the last three months, and is still up 0.26% so far this year.



Looking over the other investment categories, real estate investments, as measured by the Wilshire REIT index, fell 2.54% for the quarter, but the index is standing at a robust 15.08% gain for the first three quarters of the year. Commodities, as measured by the S&P GSCI index, fell 12.46% this past quarter, and now sit at a loss of 7.46% for the year.

The expected rise in bond rates never materialized, confounding the experts yet again. The Bloomberg U.S. Corporate Bond Index now has an effective yield of 3.07%, while Treasury rates held steady. 30-year Treasuries are yielding 3.20%, and 10-year Treasuries currently yield 2.50%. At the low end, 3-month T-bills are still yielding a miniscule 0.02%; 6-month bills are only slightly more generous, at 0.04%.

Nobody seems to have a convincing explanation for the recent stock market slump. The economy still seems to be pushing along in a long slow, steady growth process, and corporate earnings are well-above historical averages. Oil prices are at their lowest level since November 2012, consumer spending has rebounded, and although the Fed will cease its bond purchases this month, there is no indication that it is going to sell its inventory back on the market, and its policymakers are projecting low interest rates well into 2015. Corporate cash at larger corporations is near an all-time high.

But pullbacks don't always reflect reality. They are also affected by the sentiment of investors--in other words, human emotions and a crowd (or herd) mentality. Investors seem to be worried that stocks are overdue for a correction, and if these things operated on a schedule, they would be right. We are in the fourth-longest bull market since 1928, without having experienced even a small 10% correction since 2011. The Conference Board reported that U.S. Consumer Confidence slipped dramatically, and unexpectedly, in September, lending some credibility to the surmise that the investing herd has been startled--and their expectations appear to be creating market reality.

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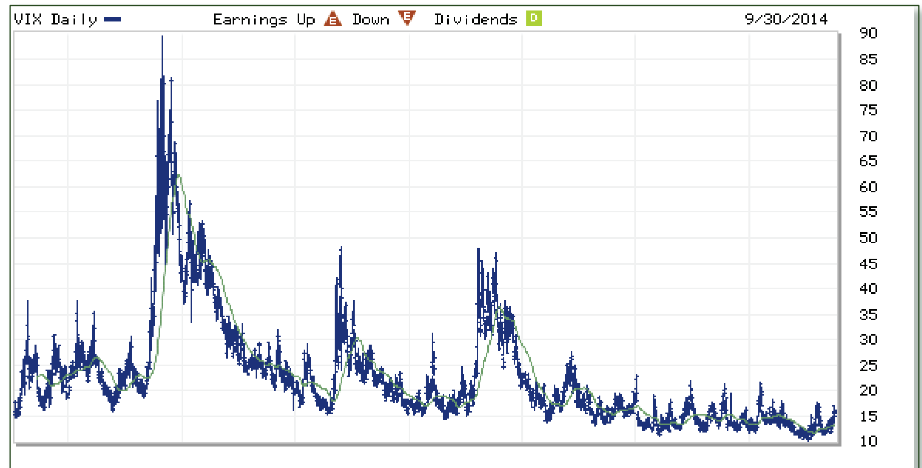
The best (although imperfect) way to chart investor sentiment is via the VIX Index, which measures the volatility of the market by tracking the behavior of S&P 500 index options. When the VIX spikes, it means that investors are excited or scared--as they seem to be now. The interesting thing about the long-term VIX chart--shown here starting in the third quarter of 2007, is the heartbeat-like rhythm of the spikes and drops, as if people get nervous in a kind of pattern. The 2008-2009 market meltdown shows up in the enormous spike toward the left, but if you let your eyes move to the right, you can see that volatility has been pretty moderate since the end of 2012.

CBOE Volatility Index (aka "the VIX Index")



Maybe it's just time for the "heart" that represents how investors feel about the markets to give another tick.

Does that mean we should take action? Unfortunately, nobody knows whether the markets are poised to act on the good economic news and move up, or are ready for another fearful selloff that would finally deliver that long-delayed correction. History tells us that it's a fool's game to try to anticipate market corrections, and that investors usually get rewarded for sailing through choppy waters, rather than jumping off the ship when the waves get higher.

You can't know in which direction the markets will experience their next 10%, 20% or 30% move. But unless you believe the world is about to end, you do know, with some degree of certainty, in which direction it will make its next 100% move. That's the best prediction of the markets you're likely to get, even if it doesn't come with a timetable.

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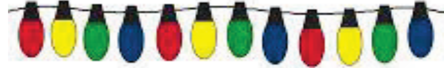
All of us at Demming Financial Services Corp. would like to wish you, and your family, a safe & happy upcoming holiday season!

Happy Thanksgiving!



Happy Holidays!