



# Investment Advisors

*Steady as You Grow*

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Quarterly Newsletter

## Households Unprepared for Retirement After Recession

By Danielle Andrus, AdvisorOne New research released Thursday by the Employee Benefits Research Institute found that the percentage of households that were on track for retirement before the financial crisis hit are now at risk.

Early boomer households that need to save more for retirement should look to increase their contribution to retirement accounts by 3% of their income each year until they retire. For a 90% chance of having sufficient retirement income, those households would need to increase their contributions by 4.3% of compensation.

The report assumes all workers retire at age 65 and begin withdrawing money from their retirement accounts when their basic expenses and uninsured medical expenses exceed their after-tax annual income from Social Security and any defined-benefit plans.

Over 47% of early boomers were estimated to be at risk of retirement shortfalls in 2010, according to the report; 43.7% of late boomers were at risk. The Center for Retirement Research's National Retirement Risk Index, however, showed "significantly higher at-risk percentages" for younger cohorts, according to the report. CRR used data from the 2007 Survey of Consumer Finances to find that 41% of early boomers and 48% of late boomers were at risk of retirement shortfalls.

Unsurprisingly, more affluent investors are least likely to be at risk of retirement shortfalls, according to the EBRI report. Over 23% of the highest income group was at risk, compared with 41.6% of the middle-income group, and 70.3% of the lowest income group.

### History of CPS Investment Advisors



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Founded by Chas P. Smith over 35 years ago in Lakeland, FL, Chas P. Smith & Associates, P.A. first began providing traditional tax and accounting services. The firm's emphasis on personal financial planning and concerns for its clients well being eventually brought the firm into the money management business in 1989.

The firm specializes in personalized money management for individuals, corporations and retirement plan investors; and is a Registered Investment Advisor with the U.S. Securities & Exchange Commission.

The owners of CPS are Chas P. Smith, James M. Luffman, and Peter C. Golotko. They are all Certified Public

Accountants, Personal Financial Specialists designated by the American Institute of Certified Public Accountants (AICPA), and have earned the Certificate of Educational Achievement Award in Personal Financial Planning by the AICPA.

## Dangers of Market Timing

Two of the most dangerous words in the investing world are “market timing.” Market timing occurs when investors try to predict which direction the stock market will head. While some investors have been known to make money timing the market, it is highly inadvisable for long-term investors to try this extremely risky strategy. Opponents of Market Timing: Most investors and academics believe it is impossible to forecast market movements. Such a technique amounts to gambling when compared with a sound investment approach. It fails far more than it works, and market timers often end up buying high and selling low. Furthermore, you run the risk of missing periods of exceptional returns. For example, over the past 20 years, a \$1 investment in stocks, as represented by the Standard & Poor’s 500®, would

have grown to \$5.75. If that same \$1 investment happened to miss the best 13 months of stock returns over the past 20 years, the ending value would have equaled only \$1.96. This would have been less than the value for an investor in a 30-day Treasury bill, a.k.a. cash, \$1.97. Only those who remained invested in stocks throughout the entire period were sure to get market exposure during the crucial hot months.

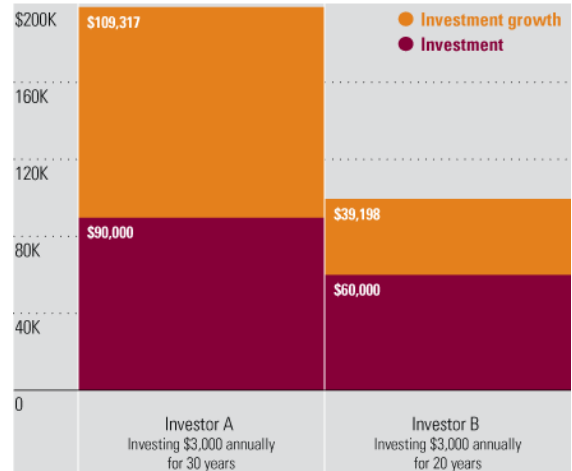
Advocates of Market Timing: On the contrary, a number of websites, newsletters, and other trading services boast they can time the market. While their returns may have in fact beaten the market by a considerable margin, it’s safe to assume that these systems can’t consistently hold up over the long term. On some occasions and during some stretches of time, market timing can help generate impressive profits. However, you must be familiar with the dangers behind such an approach.

## The Costs of Financial Procrastination

Retirement usually doesn’t start until you’re in your 60s but there is a good reason to start saving much sooner. The earlier you contribute to your nest egg, the more time your portfolio will have to grow in value.

The image illustrates the ending wealth values and effects of compounding of two investment portfolios. Consider two hypothetical investors who begin investing \$3,000 at an average annual rate of return of 5%. Investor A invests \$3,000 for a 30-year period, which results in an ending wealth value of \$199,317. On the other hand, investor B invests \$3,000 for a 20-year period, which results in an ending wealth value of \$99,198. Investor A invested an additional \$30,000 compared to Investor B. However, a large difference in the ending wealth value can be attributed to the compounding effect of the \$30,000 for the additional 10 years. In other words, your dollars saved now will be worth a lot more than your dollars saved in retirement.

### The Effect of Compounding



Source: This is for illustrative purposes only and not indicative of any investment. The image represents a hypothetical rate of return of 5%. The values represented do not account for inflation or taxes. Past performance is not a guarantee of future results. The opinions herein are those of Morningstar, Inc. and should not be viewed as providing investment advice. Please consult with your financial professional regarding such services.

# The Many Faces of Inflation

During the recent 2007–2009 recession, it seems all we've seen and heard about the economy was bad news: the housing market collapsing, 401(k)s suddenly being worth much less than before, a lifetime of savings almost disappearing in a few months, rising unemployment, and fluctuating prices. Now that the recession has officially ended in June 2009 and we're on the road to recovery, inflation may become a concern once again. In this uncertain economic climate, it may be helpful to learn about the different types of inflation and their immediate effects.

**Inflation:** Inflation is defined as a continuing rise in the general prices of goods and services. Simply put, if prices, on average, are going up in an economy, then you've got inflation. With a set amount of money in an inflationary environment, consumers are able to buy less and less over time. High rates of inflation can generate uncertainty, lower productivity and discourage investment. The leading measure of inflation in the United States is the Consumer Price Index (CPI). The government can change its monetary policy to control the money supply and keep inflation in check, although this is not the only variable affecting inflation. In November 2010, the Federal Reserve announced it would buy back long-term Treasuries in order to inject money into the economy, a policy called quantitative easing, which can trigger higher inflation.

**Hyperinflation:** Hyperinflation is extremely high, out of control inflation, caused by a steep increase in the money supply without a corresponding increase in the output of goods and services. Well-known examples include the German hyperinflation after World War I and the hyperinflation in Hungary after World War II. It appears that such an extreme phenomenon occurs mainly as a result of radical changes and prolonged economic instability.

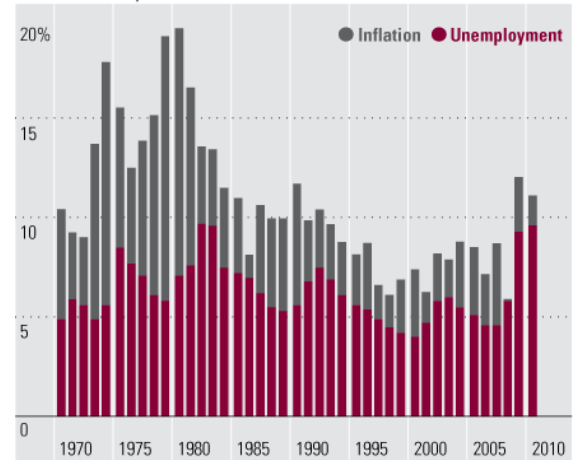
**Deflation:** Deflation is the opposite case: a general decline in the prices of goods and services. In the U.S., deflation occurred as recently as 2008 and 2009: The change in CPI was negative in the third and fourth quarters of 2008 and in the fourth

quarter of 2009, a clear indicator of deflation. The obvious positive effect here is lower prices—many argue that deflationary periods are good times to buy. The problem with deflation, though, is that consumers reduce spending and businesses stop growing, which is not good for the economy.

**Stagflation:** This is the worst-case scenario: high inflation and slow growth simultaneously.

Normally, there is an inverse relationship between inflation and unemployment; if the economy is able to tolerate a higher rate of inflation, lower unemployment can be achieved, and vice versa. But during a stagflation period, both inflation and unemployment go up. An interesting measure for stagflation is the misery index, which, as illustrated in the image, combines the unemployment and inflation rates. The U.S. experienced severe stagflation in the 1970s, when unemployment and inflation reached a combined high of almost 20%. There has been talk of stagflation during the recent crisis as well, but the potentially encouraging news is that the misery index is not nearly as high now as it has been in the past.

The Misery Index



Source: Inflation is represented by the Consumer Price Index, and unemployment by the national unemployment rate, not seasonally adjusted, from the Bureau of Labor Statistics.

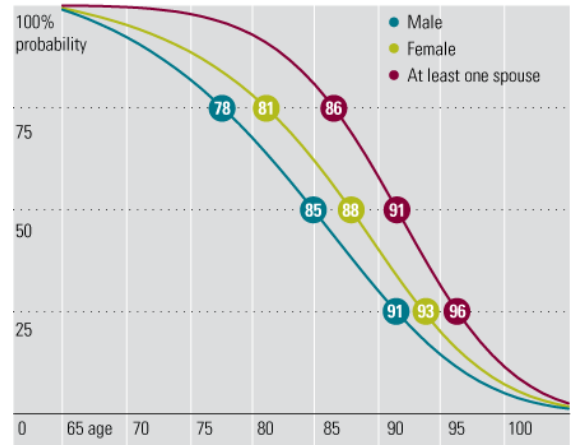
# Bittersweet

The Merriam-Webster Dictionary defines bittersweet as something that is pleasant alloyed with pain. This could also be associated with retirement. The sweet part is that people are living longer thanks to innovations in healthcare. The bitter reality is that when people live longer they risk outliving their assets.

Longevity risk is the possibility of outliving one's retirement savings. While longevity is generally a good thing, the risks associated with it are becoming a major concern for individuals entering retirement.

Luckily, longevity risk can be managed through proper planning and products. To plan properly, consider when you would like to retire, the number of years you anticipate in retirement, and your desired income level.

Probability of a 65-Year-Old Living to Various Ages



Source: Annuity 2000 Mortality Tables—Transactions, Society of Actuaries, 1995–1996 Reports.

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