Life Income Management™

Creating income for life.

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FINANCIAL OUTLOOK

JANUARY 2024

What's Better: Saving or Paying Down Debt?

Debt can be dangerous to your financial health. Thus, is it better to save or pay down your debt first?

The answer depends on a lot of things that are unique to each individual, such as your age, how much you've already saved, what rate of interest you're paying, and more. A review of the basics of financial planning is a good way to approach the subject. Here we outline how you should use income not dedicated to day-to-day expenses, in order of priority.

First Priority: Insurance

One of the best routes to financial ruin is to not have adequate insurance, so your first priority should be to have the right kinds of policies in the right amounts to protect you and your family. If you're young and unmarried, this means having basic health insurance. Beyond that, if you have a family, you probably need life insurance as well as short- and long-term disability insurance. In each case, you're looking to provide yourself or your survivors with a replacement for income you and they count on. The bottom line: if you have debt, it may make sense to make the minimum payments until you're properly insured and you have the next two priorities covered as well.

Second Priority: An Emergency Fund

Even if you don't have a family, you need to protect yourself against a job loss or major unexpected expense. The rule of thumb is to create an emergency savings fund equal to three to six months of your income. Not only does this give you breath-

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Managing Investment Risk

Risk — the possibility of losing money — is one of the most feared words in investing. So what gives some people the ability to control their emotions and make cool and calm decisions? Two main reasons are that they know how to measure risk and how to manage it.

Two Ways of Measuring Risk

Beta — Professionals have two common ways to measure risk. The first is beta, which is how closely a portfolio's performance matches or varies from that of a benchmark index. The benchmark for large-company U.S.-traded stocks is the S&P 500 stock index, while a general benchmark for bonds of medium-range maturity is the Barclay's Aggregate Bond index.[1] The performance of indexes is normally expressed as a percentage and reflects their total return, which is a combination of any interest or dividend payments and their change in price.

Beta is expressed as a number on an open-ended scale, and it can be a positive number, a negative number, or zero. A beta of 1.0 means a stock or portfolio's returns are identical in both size and direction to the benchmark, while a beta of -2.0 means the portfolio's returns are twice as large in the *opposite* direction of the index. For example, when the S&P 500 index return is 12%, a portfolio with a beta of 1.0 should also return 12%, while a stock with a beta of -2.0 should lose 24%. A beta of 0.0 means there is no patterned relationship between the two returns.

Standard deviation — A second way professionals measure investment risk is with standard deviation. Expressed as a percentage, it reflects a range of returns above and below an annual average rate of return for the stock or portfolio itself, without reference to a benchmark. It's standard deviation that measures the way many define risk: volatility.

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What's Better?

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ing space against hardships, it also affords you the flexibility to move in connection with a job change you might want to make.

You should make creating an emergency savings fund a priority. If you can't take care of priorities one and two while also paying for basic necessities, like groceries and gasoline, you're living beyond your means and should cut back on your spending.

Third Priority: Retirement Savings

Finally, it's imperative that you start saving for retirement as soon as possible. Time is both the best ally and worst enemy of the saver. Start saving too late, and it's possible that you'll need a rate of return you can only achieve in your dreams in order to accumulate enough for a worry-free retirement. On the other hand, even small amounts — as little as $25 a month — put away early enough can grow to sizable amounts by the time you're ready to retire.

With these three priorities covered, if and when you have money left over, it's time to consider making extra payments to tackle your debt.

Guidelines for Debt Reduction

There are a number of factors to consider when you're ready to start accelerating the pace at which you pay down debt:

- **Start with the highest interest-rate debt.** Instead of paying more on every one of your debts, concentrate on the one that charges the highest interest rate. In general, these will be store credit cards, followed by bank credit cards like Visa and MasterCard. Use all your spare cash flow to pay down one at a time.
- **Is it tax deductible?** Debt that you can write off against your taxes is generally considered good debt. In effect, the tax deduction reduces the interest rate by your marginal tax rate. In most cases, this means home mortgage interest.
- **What rate of return can you expect?** The most important consideration is whether you can earn more by investing your money than the interest rate you're being charged on your debt. If you can earn more in the financial markets than your interest rate, you should invest your money instead of paying off debt. If not, it's worth it to pay off debt.
- **How long until you retire?** This is a key consideration when you're thinking of paying off your mortgage, especially if it's near the end of its term. At that point, the tax benefits are minimal because most of your payments consist of principal, not interest. In addition, if you're 50 or older, the monthly cash flow you'd free up could be devoted to the extra $7,500 a year you can contribute, pretax, to a 401(k) plan in 2024. On the other hand, if you have 10 years or more to go on your mortgage, it could be smarter to keep making the minimum payments to retain the tax advantages.

Smart debt management is often overlooked as a way to improve your finances, yet it can be as powerful as smart investment management. Please call if you'd like to discuss this in more detail. ❍❍❍

Avoid Cosigning a Loan

To keep your credit rating high, avoid cosigning a loan for someone else. This can be difficult to enforce, since the request typically comes from a family member or friend. However, the reason this favor is typically needed is to satisfy a creditor who does not consider the person a good credit risk and wants additional assurance before granting the loan.

When you cosign a loan, you sign a legal document accepting responsibility for the entire debt. If the primary borrower falls behind in payments, the creditor can come to you immediately looking for payment. The creditor does not have to first exhaust legal remedies with the primary borrower.

Additionally, the primary borrower's late payment history is likely to appear on your credit report. The debt is also listed as your debt on your credit report, which may impair your ability to obtain another loan.

If you are a cosigner on a loan that the primary borrower can't repay, call the creditor immediately and try to negotiate. The creditor may agree to settle for a lesser amount to avoid legal or collection fees. But make sure the creditor agrees to keep your credit report clean for that lesser amount. When the debt is paid, review your credit report to make sure it is reported correctly. ❍❍❍

Investment Risk

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In statistics, when applied to investment returns, one standard deviation covers about two-thirds of all returns. So a portfolio that has an average rate of return of 9% and a standard deviation of 12% means that in six to seven years out of 10, the portfolio's returns range between -3% and 21%. In general, a lower standard deviation is better, because it reflects less chance of a negative return.

Techniques to Manage Risk

Individual investors can use several methods to help reduce the risk and volatility in their portfolios. These include:

- **Diversification.** The fewer the number of securities you own in your portfolio, the greater the risk that one or more will produce losses that reduce your ability to generate positive compound returns. In a stock portfolio, that usually means owning stocks of at least 10 different companies from at least five different sectors (such as, but not limited to, technology, consumer staples, finance, energy, and basic materials).
- **Asset allocation.** This refers to spreading your investments over the three classic asset classes (stocks, bonds, and cash) according to a formula that potentially matches the rate of return you need to meet your goals. The formula determines what percentage of your holdings should be from each asset class (e.g., 70% stocks, 25% bonds, and 5% cash). Because bonds and cash generate more steady (if smaller) average returns than stocks, the more of each included in your portfolio, the less volatile your overall returns should be.
- **Dollar cost averaging.**[2] This is a technique that puts price declines to your advantage. It involves making periodic purchases in the same dollar amount of the same securities, in good markets and bad. When you continue to buy shares when their prices fall, you buy more shares than when the prices are higher. This gives you more shares, which increases your dollar gains when prices start going back up. However, it neither guarantees a profit nor protects against loss in a prolonged declining market. Because dollar cost averaging involves continuous investment regardless of fluctuating price levels, investors should carefully consider their financial ability to continue investment through periods of low prices.
- **Portfolio rebalancing.**[3] This is a two-step process by which you restore your holdings to the proportions defined by your asset allocation strategy. The first step is to sell a portion of the investments in those asset classes where your holdings have grown to be larger than their prescribed percentage. The second step is to use the sale proceeds to buy more of the securities from those asset classes whose proportions have become too small. This provides a benefit similar to that obtained by dollar cost averaging.

Managing risk isn't about avoiding all losses, since they are an inevitable and normal part of the investment process. Instead, it's about minimizing your losses while achieving the rate of return you need to reach your financial goals. ❍❍❍

1 The Bloomberg Barclays US Aggregate Bond Index, or the Agg, is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States. Investors frequently use the index as a stand-in for measuring the performance of the US bond market.

2 Dollar cost averaging may help reduce per share cost through continuous investment in securities regardless of fluctuating prices and does not guarantee profitability nor can it protect from loss in a declining market. The investor should consider his/her ability to continue investing through periods of low price levels.

3 Rebalancing/Reallocating can entail transaction costs and tax consequences that should be considered when determining a rebalancing/reallocation strategy.

Avoid This Mistake

Finding a way to live decades in retirement without worrying about running out of money can seem like an overwhelming task. With all the potential for missteps, what is the one mistake you want to avoid at all costs? Dipping into your retirement savings. Unfortunately, since the funds in your 401(k) plan or individual retirement account (IRA) belong to you, they often seem like a tempting place to get funds needed for other purposes.

Tax laws don't help, since they often provide tax-advantaged ways for you to access those funds. Loans from 401(k) plans are not taxable events. When leaving an employer, you can withdraw money from your 401(k) plan (you will have to pay income taxes and possibly a 10% early withdrawal penalty). Contributions to Roth IRAs can be withdrawn at any time with no tax consequences. Withdrawals from traditional IRAs before the age of 59½ can be made under certain circumstances, such as to purchase a home or to pay for a child's college education, without paying the 10% tax penalty.

Saving for retirement is a difficult task for most people, without making it more difficult by using retirement funds for other purposes. Even if the amount seems small, don't withdraw funds from your retirement account. While it probably won't add significantly to your lifestyle now, it can grow to significant sums over the long term. For instance, assume you have $10,000 in your 401(k) plan. If you withdraw the funds and are in the 22% tax bracket, you'll have $6,800 left after paying income taxes and the 10% federal tax penalty. Keep the funds invested earning 8% annually on a tax-deferred basis and your funds could grow to $68,426 after 30 years, before paying any income taxes. *(This example is provided for illustrative purposes only and is not intended to project the performance of a specific investment.)*

Please call if you'd like to discuss this in more detail. ❍❍❍

Financial Data

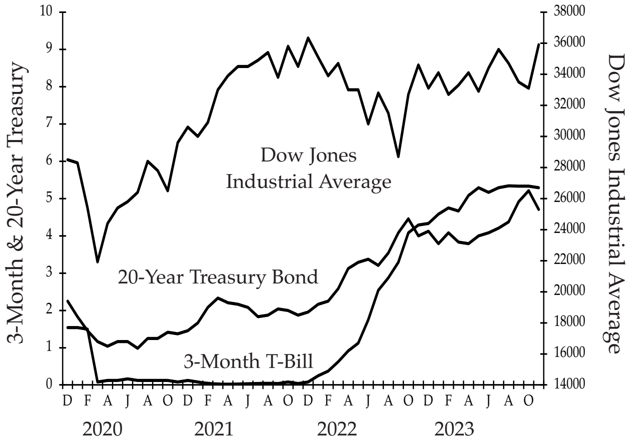
Indicator	Month-end Sep-23	Month-end Oct-23	Month-end Nov-23	Dec-22	Nov-22
Prime rate	8.50	8.50	8.50	7.50	7.00
Money market rate	0.48	0.61	0.47	0.33	0.31
3-month T-bill yield	5.33	5.33	5.28	4.35	4.29
10-year T-bond yield	4.59	4.88	4.37	3.88	3.68
20-year T-bond yield	4.92	5.21	4.72	4.14	4.00
Dow Jones Corp.	6.08	6.34	5.83	5.54	5.46
30-year fixed mortgage	7.90	8.23	7.75	6.80	6.84
GDP (adj. annual rate)#	+2.20	+2.10	+5.20	+2.60	+3.20

Indicator	Month-end Sep-23	Month-end Oct-23	Month-end Nov-23	% Change YTD	% Change 12-Mon.
Dow Jones Industrials	33507.50	33052.87	35950.89	8.5%	3.9%
Standard & Poor's 500	4288.05	4193.80	4567.80	19.0%	12.0%
Nasdaq Composite	13219.32	12851.24	14226.22	36.2%	24.1%
Gold	1870.50	1996.90	2035.45	12.3%	16.1%
Consumer price index@	307.03	307.79	307.67	3.3%	3.2%
Unemployment rate@	3.80	3.80	3.90	5.4%	5.4%

— 1st, 2nd, 3rd quarter @ — Aug, Sep, Oct Sources: *Barron's, Wall Street Journal*

4-Year Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield

December 2019 to November 2023



Past performance is not a guarantee of future results.

News and Announcements

Set Your Own Debt Limits

Credit can be a valuable tool that allows you to purchase major items and pay for them over time. Rather than allowing lenders to set credit limits for you, evaluate your financial situation and determine your own limits.

To find out where you stand with consumer debt, which includes all debt except your mortgage, make a list of your debts and monthly payments. Then calculate your debt ratio by dividing your monthly debt payments by your monthly net income. The general guideline is that your debt ratio should not exceed 10% to 15% of your net income, with 20% usually considered the absolute maximum.

Before purchasing something on credit, carefully evaluate whether it makes financial sense to do so. Some questions to ask yourself include:

- ❍ Should I wait and save the money so I can pay cash for the item?
- ❍ Will the cost of the item increase or decrease in the future?
- ❍ Is it really worth paying interest on the item so I can use it now?
- ❍ Will I still be within my designated debt limits if I add this new debt payment?
- ❍ Will the item still have value after I finish paying for it?

Setting your own debt limit and carefully evaluating whether you should purchase an item on credit should help you keep your debt under control. ❍❍❍

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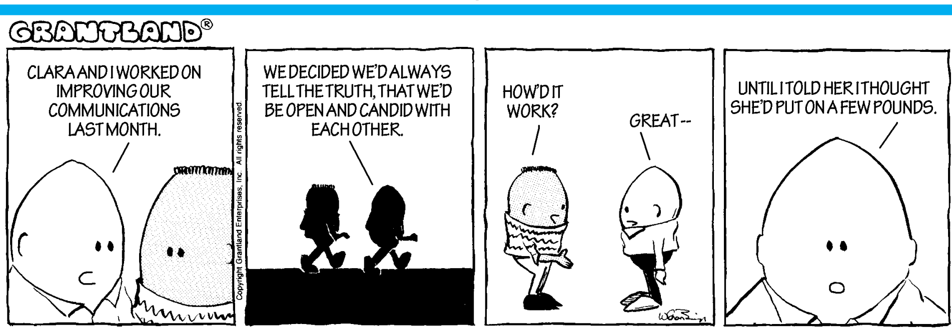

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Neither Asset Allocation nor Diversification guarantee a profit or protect against a loss in a declining market. They are methods used to help manage investment risk.

Indices are unmanaged and investors cannot invest directly in an index. Unless otherwise noted, performance of indices do not account for any fees, commissions or other expenses that would be incurred. Returns do not include reinvested dividends.
The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 actively traded "blue chip" stocks, primarily industrials, but includes financials and other service-oriented companies. The components, which change from time to time, represent between 15% and 20% of the market value of NYSE stocks.
The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general. It is a market value weighted index with each stock's weight in the index proportionate to its market value.
The Nasdaq Composite Index is a market-capitalization weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange. The types of securities in the index include American depositary receipts, common stocks, real estate investment trusts (REITs) and tracking stocks. The index includes all Nasdaq listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds (ETFs) or debentures.
The Consumer Price Index (CPI) is a measure of inflation compiled by the US Bureau of Labor Studies