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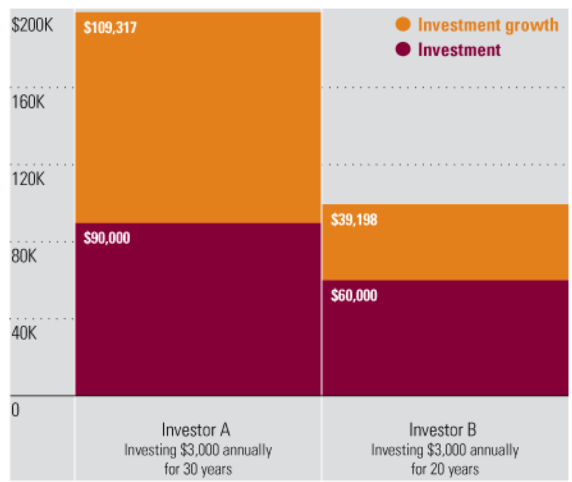
The Costs of Financial Procrastination

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.

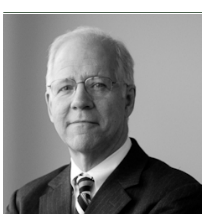
The image illustrates the ending wealth values and effects of compounding of two investment portfolios. Consider two hypothetical investors who begin investing $3,000 at an average annual rate of return of 5%. Investor A invests $3,000 for a 30-year period, which results in an ending wealth value of $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.

Advisor Corner



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Ron was a major force in building the investment firm and now manages more than $100 million of retirement assets for his clients. He specializes in the unique rules, investment management, distribution, and estate planning considerations for IRAs and other assets for retirement income planning. A Certified Financial Planner, Ron has served on the boards of the International Association for Financial Planning and the Institute of Certified Financial Planners. He has been a Chartered Retirement Planning Counselor, and was named to Ed Slott's Elite IRA Advisor Group®, a national network of IRA specialists. He is a member of the Connecticut Chapter of the Financial Planning Association and the Estate and Business Planning Council of Hartford. Ron received a BA in psychology from the University of Connecticut and an M.Ed. from Boston College.

Financial Preparations for a Natural Disaster

As residents of areas affected by Hurricane Sandy found out, a natural disaster can bring about not only emotional hardship, but financial hardship, as well. From keeping important documents safe and accessible to having enough cash on hand to get by until things return to normal, being prepared for a disaster is an important part of protecting your home and your family. It could be a natural disaster like a hurricane, tornado, flood, fire, mudslide, or earthquake. Or it could be something on a more limited scale like a power outage. Whatever the crisis, taking the steps below will help you better handle whatever might come your way.

Get Organized Before a Disaster Strikes: Chances are that's not at the top of your to-do list for the weekend, so it's very easy to procrastinate. But think of it this way: You buy insurance to protect you from catastrophes; disaster preparedness is just another kind of insurance that you prepare yourself. It doesn't have to cost a lot, but it could really save time and added frustration should something happen to you. Once you've got a plan, you only need to update it periodically.

Keep Important Papers and Documents Safe and Easily Accessible: You might need to gather your most important papers in a hurry. Do you know where they are? Can you grab them quickly and leave the house immediately if you need to? Here are some of the documents to which you may need access: IDs (driver's license, Social Security card, passport, birth certificate), financial documents (checkbooks, investment account numbers, passwords, and phone numbers, retirement account information, estate documents, insurance policies), and medical records. Most importantly, you'll need cash (at least enough to cover one to two weeks' emergency expenses).

You might also want to have a list of key contacts/phone numbers, which may include family cell-phone numbers and e-mail addresses, police, fire, and ambulance numbers, Red Cross and emergency response center local numbers, as well as your company's human resources department number.

Keep all these important papers in a plastic bag in your home safe, or in any safe place from where you can grab them quickly if you need to leave your home in a hurry. Also, it may be a good idea to leave copies of everything with your attorney and/or financial advisor, in case the original documents get lost or damaged.

Prepare for a Medical Emergency: What if you or a family member suffer an injury (or worse) when disaster strikes? Check your health-insurance coverage to determine out-of-pocket costs in case surgery or emergency treatment is needed, and try to set aside enough money to cover these costs. Designate a family member or close friend as your primary contact, and prepare a living will and power of attorney for health care (documents that specify your wishes in case you're incapacitated).

Create an Emergency Fund: Most experts recommend setting aside enough money to cover about six months of living expenses. But it is equally important that this money be easily accessible. It may be a good idea to keep about half in cash, ready to use (what if it's impossible to get to a bank in the aftermath of the disaster?), and the other half in liquid investments that you can cash out easily.

What to Do if Disaster Strikes: If your house has been damaged, you may need emergency shelter. The Red Cross or your local emergency response center should be able to help. Your property insurance agent can help you file a claim on your homeowners or other types of insurance policies. If your area has been declared a federal disaster area, you may qualify for financial relief. If you have been injured, you might need to file for disability benefits. If you are healthy but a family member needs your care, you may be able to take as many as 12 weeks of unpaid leave under the Family and Medical Leave Act without losing your job.

A Beginner's Guide to Credit Cards

Credit cards are magic little pieces of plastic that allow you to use money without having it, right? Wrong. The reality is that credit cards are magic little pieces of plastic designed to make money for the credit-card companies. Not being aware of your full responsibilities as a credit card holder can bury you deep in debt and significantly limit your access to credit in the future. Therefore, it is crucial for you, the consumer, to be aware of all the little details of credit-card transactions.

A credit card is a valuable convenience, since it means you don't have to carry cash around anymore. But it definitely does not mean that you can make unlimited purchases and not pay for them, as some people may think. With a credit card, all the purchases you make during a certain period of time are allowed to accumulate, and you receive a bill (statement) for the total amount spent at the end of that time period (usually a month). Once you get the bill, you have a grace period—normally 20 to 25 days—until the due date.

When you receive the bill, you'll notice you can make a minimum payment, or you can pay the balance in full. In other words, you owe $3,000, but you can make only a minimum payment of $1,000 and keep the other $2,000 for yourself. This is great, right? Wrong again. If you do not pay your balance in full, your credit card company will make money by charging you fees.

Finance charges and late fees: If you have an outstanding balance (money that was not paid on time) on your credit card, you will pay interest on that balance. There are various methods for calculating your outstanding balance (adjusted balance, average daily balance, previous balance, ending balance), so try to understand which method your credit card issuer uses. Credit-card issuers have to disclose the interest rate they charge, so make sure you know what your APR (annual percentage rate) is. If you are billed monthly, the interest rate used to calculate your finance charges will generally be your APR divided by 12. Also, credit -card rates can be fixed or variable, so if yours is variable make sure you understand why it varies and how.

If you pay your balance in full every time, you will manage to avoid finance charges, but it is still important for you to know what they are, just in case. Before you sign up for the card (not after!), read the payment rules carefully (they differ from one issuer to another). If you pay by check, mail the payment early or, even better, pay online. Be aware that paying late may result in an increase of your interest rate in the future.

In addition to finance charges, every time you delay payment you will have to pay a late fee, which can be substantial. It is obviously in your best interest to pay your balance in full every time and as early as possible. Also, when deciding which credit card to choose, look for a card with a low APR. It may have fewer bells and whistles, but it will save you money in the long run. A useful source of information on credit card rates is the website www.bankrate.com.

Annual fees, credit limit fees, cash advance fees, and balance transfer fees: Some credit card issuers charge an annual fee per card, usually assessed on your first statement. Fortunately, avoiding this one is simple: Choose a card without an annual fee. You can also be charged if your outstanding balance exceeds your credit limit. You can probably avoid this fee by requesting a credit limit increase, but this is tricky because then you'll be tempted to spend more. Card companies generally charge a fee for cash advances, which can be calculated as a flat charge per transaction or as a percentage of the total. You can also be assessed a fee for balance transfers. The point should be clear by now: It is in the credit card company's best interest to charge you all these fees, and it is in your best interest to avoid them. Make sure you know all the rules, and make all your payments on time.

Monthly Market Commentary

Recovery, full steam ahead? It would appear so. The stock market returned 11.02% during the first quarter of 2013, and the U.S. economy continues to grow at a slow but steady pace, despite apparent volatility and instability displayed by most major economic indicators.

GDP: For starters, real GDP growth rates have been highly volatile from quarter to quarter; for example, from 3.1% in Q3 2012 to only 0.1% in Q4 2012. However, it's important to keep in mind that the data includes some measurement and seasonal-adjustment issues that may blur the big picture a little bit. Morningstar economists forecast that GDP will grow at a slow, but sustainable 2.0%–2.5% rate in 2013, very similar to 2011 and 2012.

Employment: The private sector added only 95,000 jobs in March (compared with 254,000 in February). At first glance, this number is discouraging, and the lowest in nine months. However, similar to the case for GDP above, month-to-month data is volatile, influenced by weather and other seasonal factors, and often subject to revisions. Three-month average employment growth (YOY), a more reliable data point, does show slow erosion, but no catastrophic decline (2.1% in December, 2.0% in January, and 1.9% in February and March).

The Big Four: Given all the fiscal scares, Hurricane Sandy, volatile gasoline prices, and new taxes, the U.S. economy is doing surprisingly well, according to the Big Four economic indicators (private employment growth, retail sales, manufacturing, and real disposable income). Private sector year-over-year employment growth has been steady at 2% for almost two years, while retail sales growth (adjusted for inflation and excluding autos and gasoline) has been in the 2%–3% range for almost as long. Even U.S. manufacturing data hasn't been particularly volatile, especially if weather events are removed. Of the Big Four, only real disposable income has been very volatile, and most of that volatility is due to ever-shifting inflation rates (with food and energy showing the most volatility) and changes in government tax policy, not changes in wages.

Consumer: Consumer spending continues to drive the economy, constituting about 70% of GDP. Unfortunately, consumers were severely hit early in 2013 with soaring gasoline prices, a higher payroll tax, and delayed tax refunds. On the other hand, they also have a lot going for them, including lower inflation in many categories, better employment prospects, increasing home prices and related construction activity, and a much higher stock market and related wealth effects. While consumer spending is not as robust as it once was, it is clearly not falling apart in the middle of all the economic headwinds, either.

Quarter-end insights: A lot of fiscal issues were at least temporarily "settled" this quarter, helping to reassure both consumers and businesses. The fiscal cliff negotiations and the March sequestration resulted in a total deficit reduction of about $300 billion slated for 2013. The Fed plans on maintaining a relatively loose monetary policy, assuring investors that low interest rates and bond buybacks would continue to fuel further growth. As slow as this growth may be, the U.S. economy is better positioned and growing faster than many other developed economies. Some of the factors providing a longer-term advantage include newfound supplies of oil and gas, low electricity prices, more available land for building, and an improving auto industry.

In Europe, however, the situation isn't getting better, even when excluding the effects of the Cyprus situation. The Chinese economy seems to have bottomed, and future Chinese growth (if any) will likely be lower than previous peaks, and more likely to be consumption based than focused on infrastructure. Last, but not least, U.S. corporations are starting to invest for growth again (capital spending and acquisitions), which could prove to be an effective engine for further stock market appreciation.

Social Security for the Self-Employed

If you thought that running a successful business on your own was hard enough already, think again. As a self-employed individual, defined by the IRS as someone who operates a trade, business or profession, (either by yourself or as a partner), you are required to pay self-employment tax as well as income tax. Self-employment tax consists of Social Security and Medicare taxes, similar to those withheld from the pay of most wage earners. Failure to comply with IRS regulations may result in your business operations being jeopardized. The following are a few key facts to keep in mind:

1. The Social Security tax rate for 2013 is 15.3% on self-employment income up to $113,700. Should your net earnings exceed $113,700, you continue to pay only the Medicare portion of the Social Security tax, which is 2.9%. Starting this year, the Medicare tax rate for net earnings in excess of $200,000 ($250,000 for joint filers) is increased to 3.8%.

2. You need to have worked and paid Social Security taxes for a certain length of time to get Social Security benefits (no more than 10 years of work, which is equivalent to 40 credits). In 2013, if your net earnings are $4,640 or more, you earn the yearly maximum of four credits. If your net earnings are less than $4,640, you could still earn credit (depending on how you report your earnings).

3. Certain income does not count for Social Security and should not be included in figuring your net earnings. These include dividends from shares of stocks and interest on bonds, interest from loans, rentals from real estate, and income received from limited partnerships.

Tax law is ever-changing and can be quite complex. It is highly recommended that you consult with a financial or tax professional with any tax-related questions or concerns.

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