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ILLINOIS: State in Crisis

by Erica Amenda, CFP® *(continued from page 3)*

Standard & Poor's cut the state's credit rating from A+ to A in August because of a "lack of action" in tackling the state pension's massive unfunded liability. Moody's Investor Service downgraded the state earlier in the year to A2, the lowest among states Moody's rates and warned further downgrades are possible if no action on pensions is taken. This makes it more expensive to sell bonds for road construction and similar projects.

The takeaway here is that you should seriously consider finding an additional way to save for retirement along with your pension. This is to ensure your money outlives you and not the other way around. It has become exceedingly clear that you cannot 100% rely on a company or state to provide you with something as important as retirement. It is on all of us to take precaution and responsibility to ensure we can retire the way we want and deserve to.

BATES Briefings

Fall 2012

from George's Desk

The Morningstar Company publishes a report every month entitled "Fund Investor" that I have subscribed to for several years. It provides a fountain of information about mutual funds such as changes in managers, when a fund closes (or reopens) to investors, new trends in mutual funds plus pages of comparative performance for 500 of their "Fund Favorites."

In the October 2012 issue there was an interesting discussion between previous editors and the current editor about the mutual fund industry with a large portion focusing on the last twenty years. There are a number of observations and comments that I found noteworthy:

• Twelve years of performance history is much more important than three years.

• Multiple managers of a fund have been more reliable than a single manager. They specifically referenced Fidelity Magellan which twenty years ago was managed by Peter Lynch who produced one of the best if not the best record of any fund manager, but since then his successors have mostly produced sub-index results. They also referenced American Funds who pioneered the multiple manager method as having produced generally above index results while maintaining low expenses.

• One person commented that it is a lot easier to manage for yourself than to manage for other people. He followed that statement by adding, "I've developed more of an appreciation for the pressures fund managers and financial advisors face."

• Another commented on the lessons she has learned over the last twenty years such as "less is more and that the less complicated the better." She added that keeping things "plain vanilla" was a good strategy and especially avoiding "new trendy investment types is a good way to stay out of trouble."

Frankly, I found the whole article encouraging because these are people who expressed their opinions and recommendations in writing every month and had to live with the results which, not surprising, were not always correct.

That leads me to comment on the way I see the financial universe looking forward:

• I believe the U.S. stock market will be a decent place to invest, though I believe the headwinds of higher interest rates and higher inflation rates loom on the horizon.

• I believe cash, except for short-term needs for income or required distributions from retirement accounts, is at high risk of losing money due to the devaluation of the dollar against a basket of foreign currencies, higher inflation, and taxes.

• I believe the outcome of the pending election will have a significant impact on the longer term results depending on who wins.

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From George's Desk…

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• I believe bonds are a high risk investment due to extremely low current interest rates, the national debt, the ongoing government deficit spending, and the inevitability that when interest rates rise bonds will lose market value.

• I believe that the tremendous increase in oil and natural gas reserves bodes well for energy independence for the U.S. and lower energy costs than most other countries (assuming our government does not mess it up) will be a huge positive.

• Many including myself believe that relatively lower energy costs, higher shipping costs, and higher wages in emerging countries will induce a significant return of manufacturing to the U.S.

• I believe that international investing still holds significant promise of good investment results due to lower prices of foreign companies' stock, (especially Europe), the increasing demand by consumers in emerging countries to improve their standard of living, and the likelihood of a declining value of the dollar will increase our returns when we convert those foreign investments back to dollars.

I promised in my last column to report any comments I received, especially negative ones, on government programs that had been both effective and cost efficient. I received three written objections, a handful of verbal negative comments, and one who suggested that the Environmental Protection Agency has produced much cleaner air and water.

Of the written comments, two did not like me to express my political opinions when what they want from me is financial information and advice. My position on that subject is simply: political philosophy leads to government policy that has an extremely large influence on virtually all financial matters, e.g., taxes (both income and inheritance), interest rates, debt and deficits, so-called entitlement programs, medical care reform and virtually everything else financially related.

The one comment that really got my attention was regarding the EPA. My response to her was that I agreed that cleaner air and water certainly had been achieved and I could not think of any entity other than the Federal government that could have accomplished that. Though we have no benchmark for comparing whether the cost was reasonable, it probably does not matter. After further thought, though I still agree with the need for clean air and water, the authority and power that has been given to the EPA has resulted in companies and citizens having to resort to legal action to protect themselves from EPA policies that are unreasonable or subjected to outrageous fines.

I probably should add that for every opposing comment whether written or verbal, I have received many more positive comments.

Finally, as I stated in my last column, I do have an opinion, which I think I clearly stated; however, the comments I made were supported by websites of government agencies, or reports that, to my knowledge, have not been refuted. I readily agree there are differences of opinion and interpretation of that information.

As I have stated many times, but want to repeat, "I consider it a privilege and honor for the trust that so many of you have placed in me and my staff, and without my associates' support, I could not begin to do what I love to do – to help you." Thank you!!!

Plunging Off the Fiscal Cliff

Nearly 90 percent of Americans will see their tax bills rise next year by an average of $3,500 per household if Congress does nothing about the fiscal cliff, said Lori Montgomery in The Washington Post. The nonpartisan Tax Policy Center concluded that middle-income households earning between $40,000 and $65,000 a year would see their taxes go up by an average of $2,000, while the top 1 percent of earners would have to stomach an average tax hike of $120,000. Much of the tax bite will come from the expiration of tax cuts enacted by President Bush and the end of the payroll tax holiday. Congress could still extend both measures, but the clock is ticking.

Source: ***The Week Magazine***, October 19, 2012 issue

Mark your Calendar...

Our 2013 Client Appreciation Day is scheduled for April 27th.

www.batesfinancialgroup.com

We're pleased to announce that our website is now up and running!

We hope you'll take a few moments to visit us at www.batesfinancialgroup.com

ILLINOIS: State in Crisis

by Erica Amenda, CFP®

Illinois has earned fifth place among states with the highest debt per capita. The liabilities would cost every person in the state $21,067 to pay off, says State Budget Solutions, a nonpartisan advocate for budget reform. Only Alaska, New Jersey, Connecticut and New Mexico rank higher in terms of debt per capita. Additionally, Illinois has the fourth highest debt in the nation, with liabilities totaling $271 billion. Only California, New York and Texas are carrying more debt, according to the report.

Pension liability is by far the largest culprit, about $140 billion of the state's total debt. "It is the individuals and families who will ultimately bear this horrific financial burden if state governments do not get their budgets under control," said Bob Williams, the group's president. For years the state has failed to contribute enough money to the retirement systems for state employees, university staff, elected officials and teachers. That, combined with a poor economy, has left the pension system about $85 billion short.

In addition to underfunding, there are several other factors that led to the deficit. When the market took its big hits in 2008 and 2009, if your pension wasn't very well funded, it most likely had to sell assets while they were low to pay its obligations. This means the fund is becoming smaller rather than growing larger and puts the pension in jeopardy of being able to create enough income to pay the benefits of future years. Meanwhile, pension salaries in the past decade have risen more than inflation and more than the market, which means payouts for recent retirees have grown more than the fund has. Combining that with large waves of baby boomers retiring each year causes more stress on the fund. Advancements in modern medicine are also extending how long funds need to pay out to retirees. This means pension managers may feel pressure to assume higher levels of risk to meet the investment return projections of the state.

Pensions have morphed into a monster eating the state budget. The state must set aside more money yearly as a pension contribution, leaving less for other state functions. Illinois has not completely funded its full annual pension contribution in any year between 2005 and 2010. Just 45% of the state's pension liabilities were funded in 2010. The underfunding, however, has not led to any major overhauls. Over the past year, Governor Pat Quinn has called for an increase in the retirement age from 65 to 67, a 3% point increase in employee contributions, and reduced cost of living increases. However, intense opposition from state labor unions has stalled the legislation.

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CONCERNING HEALTHCARE COSTS:

I read an article in the July 16, 2012 edition of Forbes Magazine, entitled "***X-Raying Doctor Bills.***" The article headline is a little misleading in that it suggests doctor bills are an issue, when in fact the article is really about health care costs.

The article discusses a company called CASTLIGHT whose service-based business allows company employees to compare costs from different providers for the same test, exam, etc.

I bring this to your attention for two reasons:

One, it reminded me of a meeting that I attended a year ago in which two research analysts, who specialize in the healthcare industry, spoke about the endless double-digit annual increase in health insurance premiums. They commented that the cause was largely attributed to two things:

1. Seventy-five percent of healthcare is paid for by a third party, group health insurance or Medicare. This implies that since consumers are not aware of what specific treatments, procedures, tests, or exams cost because they do not have to write a check for those services, they do not have an incentive to shop around.

2. Americans live increasingly unhealthy lifestyles.

The second reason for bringing this to your attention is to relay a personal experience. Recently, I needed to have a specific exam, so I inquired of a hospital and other providers about costs. In doing so, I found a significant difference in price for the same exam. The bottom line is that one thing we all could do to help keep healthcare insurance costs from rising so fast is to do what we generally do in most other areas of our life–shop around.