Investor Insights & Outlook

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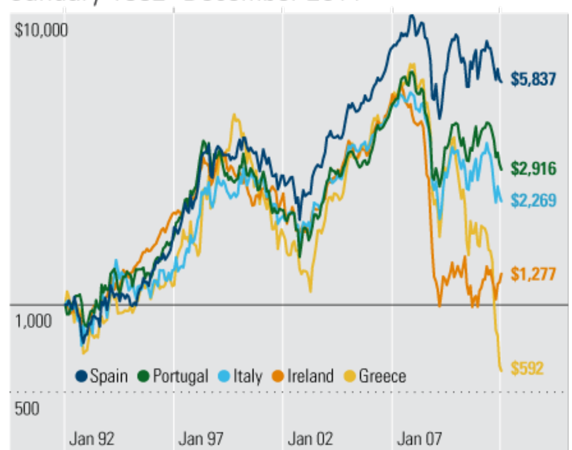
PIIGS Performance

The “PIIGS” acronym refers to the economies of Portugal, Ireland, Italy, Greece, and Spain. The term became popular during the European sovereign debt crisis in highlighting the weaker performance of these economies coming out of the economic downturn. As shown in the image, the PIIGS economies have yet to fully recover from the 2007 financial crisis and the subsequent European sovereign debt crisis. In fact, an initial $1,000 invested in Greek stocks at the start of 1992 would have yielded a mere $592 by the end of 2011 (a 41% decline in value).

If an investor desires to invest in international markets, it is important to remember to diversify across not just asset classes, but also country exposure. Diversification may minimize the financial impact to your portfolio if a specific country or region ends up in financial distress.

Growth of $1,000
January 1992–December 2011



Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Greece, Ireland, Portugal, Italy and Spain are each represented by the corresponding Morgan Stanley Capital International Index. Returns in U.S. dollars are based on the exchange rate over the selected time period. Returns and principal invested in stocks are not guaranteed. The 1992 start date for this analysis was chosen in order to analyze the most recent 20-year time period. International investments involve special risks such as fluctuations in currency, foreign taxation, economic and political risks, and differences in accounting and financial standards. Diversification does not eliminte the risk of experiencing investment losses.

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Advisor Corner

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Garner Financial Management utilizes global non-proprietary resources in order to design investment portfolios to meet all of your financial needs. We provide a customized and straightforward approach to financial growth, protection and management. Our fee-only structure is specifically designed to avoid conflicts of interest. As an independent advisor we utilize no proprietary investment products, and are free to select from all available investments. This investment process allows us to identify the most appropriate investment strategy and to focus on helping you attain your long-term financial goals.

The fiduciary role we assume in every client relationship is paramount. We understand the duty that we serve and hold ourselves to the highest personal and professional standards. It is our mission to grow and protect your wealth through integrity, passion and knowledge.

How Safe Is Your Cash?

Investors often ask the question, “Are money-market funds FDIC insured like certificates of deposit and savings accounts?” The short answer is no, money-market fund holders don't have the same guarantees that holders of CDs, money-market deposit accounts, and checking and savings accounts have. However, money-market fund investors were accorded extra protections when the financial crisis happened in 2008. At that time, a large money-market mutual fund, the Reserve Primary Fund, "broke the buck," meaning its holdings dropped in price, which in turn caused the fund's net asset value to drop lower than $1. That event created panic selling among some holders of money-market funds, prompting the Treasury Department to start a new program, similar to FDIC insurance, for money-market funds. Under the Treasury's program, investors who owned money-market funds before Sept. 19, 2008 (the date that the Treasury introduced the program) were guaranteed to be "made whole" if their funds' net asset values dropped below $1. The Treasury's program expired a year later, however, meaning that the Treasury, FDIC, or any other entity do not currently insure assets in money-market mutual funds.

That said, the fact that money-market funds aren't insured doesn't mean you should automatically eschew them. Yields on nearly all cash-like vehicles are low across the board right now, but at other points in time, money-market mutual funds might provide better yields than you'd obtain with other cash products. In addition, money-market funds also offer daily access to your money, which is not an option for CD holders. Finally, there's the convenience factor: If you frequently move money into your long-term investments from your cash accounts, holding a money -market fund with your investment provider can make these transfers seamless.

Since the introduction of the first money-market fund 40 years ago, there have been a very small number of funds that have broken the buck; all the rest have maintained stable net asset values. And following the financial crisis, the Securities and Exchange Commission, which regulates money-market funds, imposed more stringent standards, instituting new requirements for liquidity, credit quality, and maturity.

If you do opt for a money-market fund for your cash holdings, take a common-sense approach to ensure that you don't get stuck with an outlier. As with all investments, be on high alert if a money-market fund offers an appreciably higher yield than competing funds and does not have ultralow expenses; that can be a red flag that it's taking more risks than its peers.

It can also make sense to stick with money funds offered by very large providers with extensive operations outside of the money-market fund business. Thus, in a worst-case scenario in which a money-market fund's NAV falls below $1, the provider could contribute the cash to make investors "whole." Finally, if you have a lot of cash on the sidelines, it may be worthwhile to spread your positions among multiple providers for diversification purposes; you might also consider splitting your cash assets among accounts that offer FDIC protection as well as those that do not.

An investment in a money-market vehicle is not insured or guaranteed by the FDIC or any other government agency. The current yield quotation reflects the current earnings of the money market more closely than the total return quotation. Although money markets seek to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in them. Before investing in a money-market fund, you should carefully read all of the fund’s available information, including its prospectus and its most recent shareholder report.

The Ins and Outs of the 5-Year Rule for Roth IRAs

If you want to take a tax- and penalty-free withdrawal of the portion of a Roth that consists of investment earnings (amount above your initial contribution), you need to be age 59 1/2, disabled, or using the money to pay for a first-time home. However, there's more to this rule.

The five-year clock doesn't start on the day you opened or funded your Roth IRA account. Rather, it starts on the first day of the tax year for which the IRA is opened and funded. This means if you funded a 2011 Roth contribution in early April 2012, your five-year clock started on January 1st, 2011. This implies you could withdraw your investment earnings free of penalty and tax, provided you meet the other criteria for Roth IRA withdrawals (you're 59 1/2, disabled, or using the money for a first-time home), as of January 1st, 2016. The five-year waiting period doesn't start again each time you make additional contributions. Using the previous example, even if you made additional contributions for the 2012 and 2013 tax years (following your initial contribution for 2011), you'll still have satisfied your five-year holding period at the beginning of 2016, because your five-year clock started at the beginning of 2011.

Unfortunately, the five-year rule gets a bit more complicated if you've gotten the assets into a Roth through converting a traditional IRA. In that case, you need to be either 59 1/2 or five years must have elapsed since your conversion for you to be able to take penalty-free withdrawals on the converted amounts on which you paid taxes at the time of conversion. Moreover, if you've converted amounts to a Roth over a period of years, each conversion amount has its own five-year holding period. The penalty will be waived if you meet certain conditions (for example, if you're using the money for qualified education or medical expenses).

Whether a penalty applies depends on the nature of your IRA at the time of conversion, and hinges on the Internal Revenue Service's ordering rules for distributions. If you're taking a withdrawal from a Roth, the IRS assumes that contributions are withdrawn first (always tax- and penalty-free), followed by the taxable portion of a conversion, followed by the nontaxable portion of a conversion, followed by investment earnings. For example, let's say you had a $100,000 rollover IRA set up when you left your old firm, which you rolled into a Roth IRA in 2010. If you wanted to withdraw that money prior to age 59 1/2, you'd have to wait until 2015 to do so penalty-free. Because you owed taxes on your whole IRA amount at the time of conversion, that amount will be subject to the 10% penalty if withdrawn before five years have elapsed.

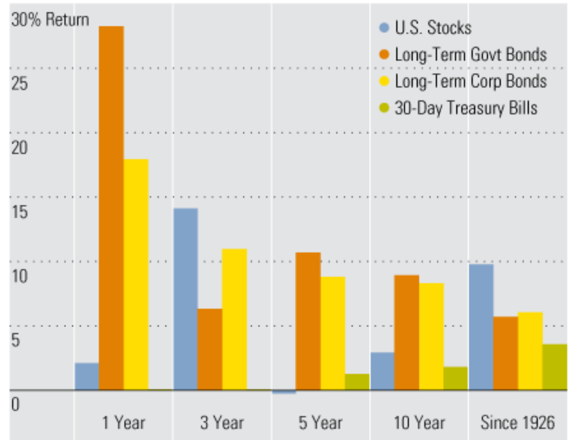
If you convert a traditional IRA that consists of nondeductible and deductible contributions, things get trickier. For example, you've built up $15,000 in a traditional IRA, $10,000 consisting of nondeductible contributions and $5,000 of deductible contributions. When converted, you'll owe tax on the $5,000 (money on which you never paid taxes). If in three years you need to withdraw $5,000, before you're 59 1/2, that amount will be subject to penalty because the IRS assumes that the amount withdrawn first is the taxable portion of your rollover, in this case, $5,000. Withdrawing the other $10,000 wouldn't trigger a penalty. Backdoor Roth IRA investors can usually avoid the 10% penalty because all or nearly all of their converted amounts will consist of money they already paid taxes on and they'll owe nothing in taxes at conversion.

Funds in a traditional IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax-free, and can be withdrawn tax free if assets are held for five years. A 10% federal tax penalty may apply for withdrawals prior to age 59 1/2. Please consult with a financial or tax professional for advice specific to your situation.

Recent Bond Performance Explained

For investors, it comes as a surprise that bonds have recently outperformed stocks. Investors often assume that stocks offer higher returns compared with bonds. Recent market conditions, however, have proved otherwise. The image shows that while stocks have outperformed other asset classes from a return perspective since 1926, they have struggled over the last 10 years. Don't be surprised at the higher bond returns in the past 1-, 5-, and 10-years. Besides the dot-com bubble and subprime mortgage crisis in the past decade, several unique events in 2011, such as the Arab Spring, U.S. credit downgrade and the sovereign debt crisis, led to a flight to safety into government bonds. Under these circumstances, investors are advised to stick with their long-term investing strategy and be aware that asset class characteristics may deviate in the short term based on current market conditions.

Unusual Stock and Bond Behavior 1926–2011



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