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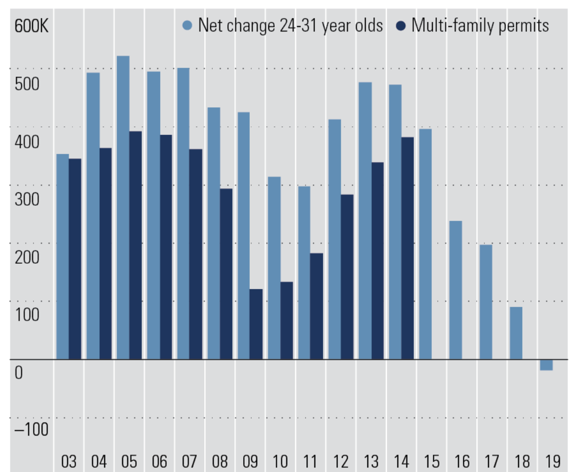
Aging Millennials Should Drive Up Single-Family Home Sales

ITI Financial Management/Troy E. Kennedy

- 4650 S. National, Ste. A-1
- Springfield, MO 65810
- 417-889-2550
- 877-889-2660 toll free
- 417-889-2559 fax
- tkennedy@itifinancialmgt.com

In this recovery, there has been a surge in interest in apartment buildings. Meanwhile, single-family home sales are still running about 50% below their previous peak. The chart illustrates what may be behind some of that change. Following the decline in the 24-31 year old cohort, that group is now growing again. Not surprisingly, so are multi-family permits and interest in apartment buildings over the last several years. Looking at the data for 2014-2019, that age dynamic will begin to shrink according to Morningstar economists. That's bad news for people building apartments, but great news for the overall economy. Single-family homes utilize more labor and more materials than apartment buildings do. So, as the age group begins to buy homes instead of living in apartments, it should drive up single-family home sales and boost the economy.

Demographics Drive Renting Business



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Source: Census Bureau, Morningstar

Troy E. Kennedy
Advisor/Principal

tkennedy@itifinancialmgt.com
417-889-2550

Advisor Corner

Mr. Kennedy's investment philosophy is the same that he has practiced over the last decade: securities markets are efficient and advisors primarily add value by coordinating the asset allocation for clients based upon risk tolerance, objectives, and time horizons. The firm has constructed 5 models for clients that vary in risk to meet the goals of each client. The firm primarily uses passive mutual funds in each model and uses select actively managed funds for bond, commodity, and real estate exposure. ITI uses several research resources, including many that were used over the last 20 years, to assist with the recommended asset allocation and the appropriate funds to utilize in each model. Mr. Kennedy is an Investment Advisor Representative of ITI Financial Management, LLC.

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In-Retirement Withdrawal Strategies

ITI Financial Management/Troy E. Kennedy

- ITI Financial Management is a fee only, non commissioned registered investment advisory firm headquartered in Springfield, Missouri. We presently manage approximately $70 million for over 175 accounts. In November 2009, Springfield Trust & Investment Company sold to a large out of town bank holding company. After 17 years as a shareholder/executive vice president with Springfield Trust & Investment Company, Troy Kennedy founded ITI Financial Management to continue to provide the highest level of personalized investment management and financial planning services. There are no fees to hire ITI nor are there any fees to terminate the relationship. It is truly a partnership with each client.

The standard sequence for a tax-efficient portfolio drawdown is required minimum distributions first. Taxable accounts next, followed by Traditional IRAs and 401(k)s. Roth IRAs and 401(k)s last. The overarching thesis is to be sure to tap those accounts where you'll face a tax penalty for not doing so (RMDs) while hanging on to the benefits of tax-sheltered vehicles for as long as possible. Because Roth assets enjoy the biggest tax benefits--tax-free compounding and withdrawals--and may also be the most advantageous for heirs to receive upon your death, they generally go last in the withdrawal-sequencing queue.

That's a helpful starting point for sequencing retirement-portfolio withdrawals, and it goes without saying that you should always take your RMDs on time. That said it may be a mistake to always follow this strategy. The reason is that your tax picture will change from year to year based on your expenses, your available deductions, your investment performance, and your RMDs.

In order to keep your total tax outlay down during your retirement years, it may be worthwhile to maintain holdings in the three major tax categories throughout retirement: taxable, tax-deferred, and Roth. Armed with exposure to investments with those three types of tax treatment, retirees can consider withdrawal sequencing on a year-by-year basis, staying flexible about where they draw their income bases on their tax picture at large. They can help limit the pain of an otherwise high-tax year by favoring taxable and Roth distributions, for example, while giving preference to tax-deferred distributions in lower-tax years.

For example, in a year in which they have high medical deductions that push them into a lower tax bracket, they might actually give preference to withdrawals from their Traditional IRA accounts, even though they have plenty of taxable assets on hand, too. The reason is that it may be preferable to take the tax hit associated with that distribution when they're paying the lowest possible rate on that distribution. Moreover, aggressively tapping tax-deferred accounts like Traditional IRAs in low-tax years will mean that fewer assets will be left behind to be subject to RMDs.

On the flip side, in a high-tax year--for example, when RMDs are bigger than usual due to market appreciation--a retiree might reasonably turn to her Roth accounts for any additional income needed. Although those Roth assets usually go in the "save for later" column under the standard rules of withdrawal sequencing, those tax-free Roth withdrawals (versus, say, paying capital gains on distributions from a taxable account or paying ordinary income tax on tax-deferred withdrawals) may help the retiree avoid getting pushed into a higher tax bracket than would otherwise be the case.

401(k) plans are long-term retirement savings vehicles. Withdrawal of pre-tax contributions and/or earnings will be subject to ordinary income tax and, if taken prior to age 59 1/2, may be subject to a 10% federal tax penalty. 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.

This article contributed by Christine Benz, Director of Personal Finance with Morningstar.

How Much Foreign Stock and Bond Exposure Do You Need?

ITI Financial Management/Troy E. Kennedy

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This is one of the central questions confronting investors putting together their portfolios, yet there seems to be no consensus. Some experts argue for highly globalized portfolios, with allocations to foreign and U.S. stocks and bonds mirroring their market values. But other experts believe that due to the extra costs and volatility that can accompany foreign stocks and bonds—and especially the foreign-currency swings that can occur when those market gains or losses are translated into U.S. dollars—less is more when it comes to foreign exposure. A related question is whether (and how) a portfolio's allocations to foreign and U.S. stocks and bonds should change over time.

Stock Allocations: Fully Global, U.S.-Centric, or Somewhere In-Between?

The issue of how much investors should stake in foreign stocks has been a contentious one for years. In the "less foreign is more" camp are experts who believe that because many U.S. blue chips are increasingly global in their reach, investors in them get exposure to foreign markets indirectly, while avoiding the extra costs and volatility associated with foreign stocks (foreign-currency swings in particular). At the other extreme are the "global market-cap agnostics"—those who suggest buying a basket of U.S. and foreign equities weighted according to their market values. The U.S./foreign allocations of global-market indexes have hovered around 50/50 for the past several years.

Meanwhile, most asset-allocation experts recommend a middle ground. Investors may not need to steer half of their portfolios to foreign stocks to obtain most of their diversification benefits. The rationale behind how much foreign exposure an investor may choose gets back to volatility. Because foreign stocks typically entail some currency risk as gains or losses are translated from foreign currencies to dollars, investors who want to reduce volatility may want to also reduce their foreign weightings accordingly.

Bonds: It's Complicated

Even though more than 50% of the world's fixed-income investments exist outside the United States, investing in foreign bonds has the potential to add cost and volatility to a U.S. investor's portfolio. Few asset-allocation experts are in favor of mirroring the global markets' allocation to U.S. and foreign bonds.

Because types of foreign-debt exposure vary so widely, one-size-fits-all recommendations are tricky. Investors could steer a larger share of their fixed-income portfolio to foreign sovereign bonds rather than corporate and/or local-currency-denominated debt.

The volatility issue can be addressed, at least in part, by hedging out the currency risk of the foreign bonds. That helps ensure that investors partake of foreign bonds' yields and any price changes, but not the currency-related impact when those returns are translated into dollars. However, hedging strategies entail costs, and in a low-returning asset class like bonds, those costs can take a big bite out of returns.

Past performance is no guarantee of future results. An investment cannot be made directly in an index. Diversification does not eliminate the risk of experiencing investment losses.

Returns and principal invested in stocks are not guaranteed, and stocks have been more volatile than the other asset classes. International bonds are not guaranteed. With international bonds the investor is a creditor of a foreign government or corporation. International investments involve special risks such as fluctuations in currency, foreign taxation, economic and political risks, liquidity risks, and differences in accounting and financial standards.

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Employment Growth Remarkably Strong in May, Wages Push Higher

ITI Financial Management/Troy E. Kennedy

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- 877-889-2660 toll free
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The U.S economy added 280,000 nonfarm payroll jobs in May, surpassing the consensus estimate of 220,000. Certainly there was some help from the addition of summer jobs in some industries, but generally it was a very strong and clean report. The jobs data also exceeded the 12-month average of about 255,000 jobs per month.

The job growth average for January through April was a mere 200,000 or so jobs added per month, well below the annual averages and a sharp falloff from a very strong autumn. Viewed on a year-over-year, averaged basis, the jobs market has been consistently strong since September 2014. The private sector employment rate has been growing at about a 2.6% rate. Adding in the lethargic government sector, nonfarm payrolls are expanding at a very healthy 2.3% rate.

Month-to-month wage progression was also robust at a 0.3% monthly rate (3.6% annualized) and some previous data was revised, perhaps confirming the overall strength of the jobs market. Though less dramatic, the year-over-year hourly wage growth rates also appear to be improving. Growth in hourly wages and the number of workers added are relatively similar at 2.6% and 2.2%, respectively. While the market always focuses on the jobs number, wage growth is nearly as important. At this stage of the recovery, hours worked provides little help to wage growth and that is the case again now. Combining all three factors, employees, wage rate, and hours worked, total wage growth has been little changed at about 5%.

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