August 2015 Vol.6 No.8

Inflation and Hourly Wage Growth

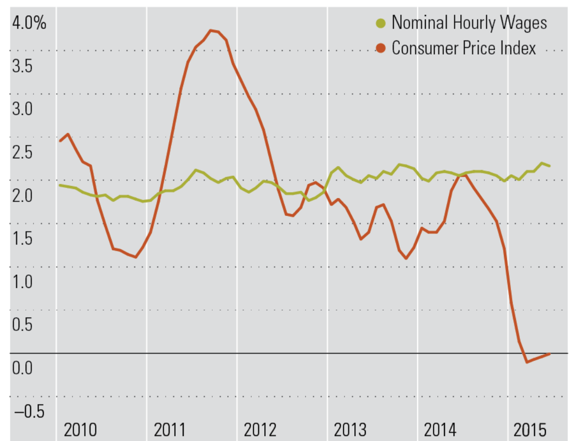
ITI Financial Management/Troy E. Kennedy

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

Wage growth is an important leading metric of consumer behavior, as higher wages increase disposable income, which in turn drives more spending. The chart depicts nominal hourly wage growth and the inflation rate (represented by the consumer price index) since 2010. Both metrics are on a year-over-year basis, and averaged for 3 months in order to smooth out the monthly seasonality.

What really stands out is that nominal hourly wages have been growing at a steady 2% rate for many years now, and they have recently accelerated just slightly to about 2.2%. What contributed to a huge increase in the real wage growth (not shown on the chart), however, was the collapse of the inflation rate that began in the second half of 2014, driven by lower oil and gasoline prices.

Inflation and Hourly Wage Growth, Y/Y, 3-Month Average



Source: Bureau of Labor Statistics, 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.

Four Retirement-Portfolio Withdrawal Mistakes to Avoid

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.

Some errors in retirement-portfolio planning fall into the category of minor infractions rather than major missteps. Did you downplay foreign stocks versus standard asset-allocation advice? It's probably not going to have a big impact on whether your money lasts throughout your retirement years.

But withdrawal rate errors can have more serious repercussions for retirement-portfolios. If you take too much out of your portfolio at the outset of retirement, and that coincides with a difficult market environment --you can deal your portfolio a blow from which it may never recover. Other retirees may take far less than they actually could, all in the name of safety. The risk is that they didn't fully enjoy enough of their money during their lifetimes.

Mistake 1: Not Adjusting With Your Portfolio's Value and Market Conditions. Even though the popular "4% rule" assumes a static annual-dollar-withdrawal amount, adjusted for inflation, retirees would be better off staying flexible with their withdrawals.

What to Do Instead: The simplest way to tether your withdrawal rate to your portfolio's performance is to withdraw a fixed percentage, versus a fixed dollar amount adjusted for inflation, year in and year out. That's intuitively appealing, but this approach may lead to more radical swings in spending than is desirable for many retirees. It's possible to find a more comfortable middle ground by using a fixed percentage rate as a baseline but bounding those withdrawals with a "ceiling" and "floor."

Mistake 2: Not Adjusting With Your Time Horizon. Taking a fixed amount from a portfolio also neglects the fact that, as you age, you can safely take more from your portfolio than you could when you were younger. The original "4%" research assumed a 30-year time horizon, but retirees with shorter time horizons (life expectancies) of 10 to 15 years can reasonably take higher amounts.

What to Do Instead: To help factor in the role of life expectancy retirees can use the IRS' tables for required minimum distributions as a starting point to inform their withdrawal rates. That said, those distribution rates may be too high for people who believe their life expectancy will be longer than average.

Mistake 3: Not Adjusting Based on Your Portfolio Mix. Many retirees take withdrawal-rate guidance, such as the 4% guideline, and run with it, without stopping to assess whether their situations fit with the profile underpinning that guidance. The 4% guideline assumed a retiree had a balanced stock/bond portfolio. But retirees with more-conservative portfolios should use a more-conservative (lower) figure, whereas those with more-aggressive asset allocations might reasonably take a higher amount.

What to Do Instead: Be sure to customize your withdrawal rate based on your own factors, including your portfolio mix.

Mistake 4: Not Factoring In the Role of Taxes. The money you've saved in tax-deferred retirement-savings vehicles might look comfortingly plump. However, it's important to factor in taxes when determining your take-home withdrawals from those accounts. A 4% withdrawal from an $800,000 portfolio is $32,000, but that amount shrivels to just $24,000, assuming a 25% tax hit.

What to Do Instead: It pays to be conservative in your planning assumptions. To be safe it's valuable to assume a higher tax rate than you might actually end up paying.

Disclosure: This is for informational purposes only and should not be considered tax or financial planning advice. 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.

Required Minimum Distribution (RMD) Tips and Traps

ITI Financial Management/Troy E. Kennedy

- The firm's investment philosophy is the same that Mr. Kennedy practiced at Springfield Trust & Investment Company, that the securities markets are efficient and that 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 18 years, to assist with the recommended asset allocation and the appropriate funds to utilize in each model.

The tax-deferred compounding you get via an IRA or a company retirement plan enables you to grow your savings without having to fork over taxes on your investment earnings year in and year out. However, at some point, required minimum distributions, or RMDs, will take effect. All retirees must begin taking RMDs from their tax-deferred retirement plans by April 1st of the year following the year in which they turn age 70 1/2. They must then continue to take distributions by December 31st of each year thereafter. Roth IRAs aren't subject to RMDs. However, you exert more control than you might think over the timing of your RMDs, as well as over which accounts you tap. Here are some tips for getting the most out of your RMDs, as well as some traps to avoid.

Do

1. Even though you must calculate your RMD amounts for each of your traditional IRAs, you can draw your RMD from the investment that's most advantageous for you. If you've assessed your asset allocation and determined it's time to rebalance, take your RMD from the IRAs that hold assets where you need to lighten up.

2. Rather than taking your whole distribution at year-end, consider spacing your distributions throughout the calendar year to obtain a range of sale prices for your longer-term assets.

3. Consider "bucketing" your IRA and retirement-plan assets. That means dividing assets into cash or cash-like accounts to help address RMD and other income needs, intermediate-term assets (such as bonds) that are next in line for distributions, and long-term assets.

4. Put your distributions on autopilot to avoid the last-minute rush to execute trades (or worse, to avoid missing the deadline altogether). If you go the autopilot route, be sure to maintain cash assets in your accounts to avoid having your fund company or brokerage firm sell a long-term asset that you would have preferred to hold.

5. Coach elderly parents on taking their RMDs.

Don't

1. Miss the deadline. You'll owe a tax penalty equal to 50% of the distribution amount you should have taken but didn't, as well as the taxes that are due on any retirement-plan distribution.

2. Pay a tax penalty without stating your case first. The IRS' website indicates that the penalty will be waived if "the shortfall in distributions was due to reasonable error and that reasonable steps are being taken to remedy the shortfall." If you've missed a distribution or didn't take as much of an RMD as you should have, you'll need to fill out an IRS form. You'll also have to submit a letter detailing why you had a shortfall in your distribution and what you're doing to remedy it.

3. Spend your RMDs right away unless you've analyzed your retirement plan's viability and determined that you can afford to splurge.

4. Plow the proceeds into a Roth IRA without doing your homework first. You need to have enough earned income (generally, that means income from a job) to cover the amount of your IRA contribution. For example, if you want to contribute $6,000 to a Roth, you'd need to have at least $6,000 in earned income to do so. Unfortunately, income drawn from your retirement accounts doesn't count. Note that you can't make additional traditional IRA contributions after age 70 1/2.

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.

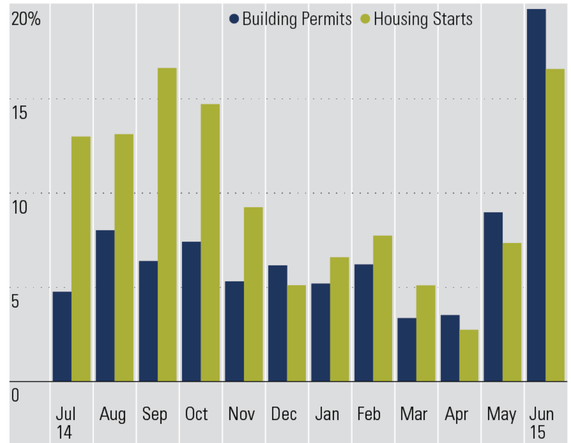
Housing Construction in Good Shape

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

The chart depicts the state of the housing construction industry, suggesting that there is still plenty of room to grow in this slow, but steady recovery we've seen so far. The latest starts and permits data from the Census Bureau, however, shows a slightly exaggerated picture, as it is the multi-family category that's been making overall housing construction look better than it is in reality. Both starts and permits picked up in June, as multi-family activity rose sharply amid expiring construction tax incentives for developers in the New York City area. As a result, the housing construction revival is probably not as strong as the numbers seem to currently suggest. Nonetheless, improvements for single-family construction still look healthy, and continue to trend up closer to the 10% rate year over year.

Building Permits Versus Housing Starts
Year-Over-Year Growth, 3-Month Average



Source: Census Bureau, Morningstar.

This article contains certain forward-looking statements which involve known and unknown risks, uncertainties, and other factors that may cause the actual results to differ materially from any future results expressed or implied by those projected statements. Past performance does not guarantee future results.