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# From the Desk of the Lev Rourk Group

U P D A T E

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## To Buy or Not to Buy

If you've been investing for years without a defined strategy, it's never too late to define your strategy and align your portfolio accordingly. Whether you're investing for the first time or buying new stocks to augment your current portfolio, there are five important questions to ask yourself:

**1. What's my objective?** Is your ideal stock one that pays a high dividend or one that doesn't pay dividends at all, but has a high rate of growth? Is it a stock with relatively little price volatility but lower potential gains, or one with a lot of potential risk and higher potential rewards?

How you answer those questions — and the stocks you choose — depends on your objectives. If capital preservation is your goal, for example, a lower-risk stock is probably your best bet. On the other hand, if you're young and growth is your target, a higher-risk, higher potential return stock may be the right one for you. Whatever your objective, defining that goal is the first step to selecting stocks for your portfolio.

**2. Is my portfolio diversified?** When considering which stock to purchase, determine whether you need to target your investment in certain areas to balance out your diversification.

Diversification is the single most important factor in managing the risks of a stock portfolio. You should be sure that your portfolio isn't concentrated in just one industry, but spread out over at least four or five. And there are other dimensions to consider as well: cap weighting (large-, mid-, and small-cap), style (value or growth), and geography (U.S.-based, developed markets, and emerging markets).

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## How You Can Use P/E Ratios

The price/earnings (P/E) ratio is the price you pay for $1 of a company's earnings. For example, if a company reports basic or diluted earnings of $2 per share and the stock is selling for $20 per share, the P/E ratio is 10 ($20 per share divided by $2 of earnings per share).

This ratio helps you determine if a stock is over or undervalued, helps compare companies in the same industry, and helps to compare the return you are actually earning from the company compared to other investments, such as bonds or real estate.

Here's how it works. Both Company A and B are selling for $50 per share. Company A has reported earnings of $10 per share and company B has reported earnings of $20 per share. Company A's P/E ratio is 5, while Company B's is 2.5. Company B is cheaper and is providing twice the earning power because for the same share price, an investor is getting $20 of earnings as opposed to $10 of earnings.

There are also variances in P/E ratios by industry, because there are different expectations for different types of business.

The bottom line is you have to do your homework. If you want to buy a stock because it has an attractive P/E ratio, make sure you know why. It may be a great stock to purchase and is just undervalued, but be aware if the company is losing business or is poorly managed. It may also be that the entire industry is weak. Don't buy a stock just because it's cheap. Many investors also use the price/earnings growth ratio, also known as the PEG ratio, because it also factors in the growth rate of a company. ✔✔✔

## To Buy or Not to Buy

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The benefit of diversification is that the up and down movements of different asset subclasses are not completely correlated, so that over time losses in one industry or subclass may be offset by gains (or lesser losses) in another.

**3. What's my expected holding period?** If you're looking to speculate or trade for fast gains, your expected holding period is short. In that case, you need to be sure you are timing your purchase so you're getting in near the beginning of an upswing, not the end of one. If you are buying for the long term, on the other hand, the price you pay is less critical, as long as you don't purchase a stock in the early stages of a steep decline in value.

**4. What's the prevailing market trend?** Recently, the market was so strong that almost any stock you bought was likely to go up in value. But in a trendless or bear (declining) market, it's a lot harder to find a winner, at least in the short and intermediate terms. That's because the majority of stocks move in the same direction as the market.

**5. At the current price, would I be paying too much?** To answer this question, you'll have to consider some basic fundamentals.

First, look at the stock's price/earnings (P/E) ratio, which is its price per share divided by earnings per share. How does it compare to the stock's normal range, and how does it compare to its direct competitors? If the P/E ratio is high, maybe the stock is overpriced. On the other hand, if it's low, it could either be a bargain or an indication of a fundamental weakness.

In addition to the P/E ratio, you should examine the stock's past and future earnings growth rate. Then look at its price/earnings growth ratio (PEG ratio). The PEG ratio compares the stock's P/E ratio to its five-year projected earnings growth rate. A PEG ratio of 1 to 1.5 is typically considered normal. A PEG of 2.0 or higher is often a sign that a stock is overpriced, while a PEG below 1.0 may be an indication that the stock is a good bargain.

Even the most seasoned investor, one who's comfortable with the five factors to consider when evaluating a stock, can benefit from the objective advice of a professional. As hard as we try, it's difficult to avoid getting emotionally tied up in our investments. Please call if you'd like help reviewing your stock investments. ✔✔✔

## Do You Really Need 70%?

A general retirement planning rule of thumb indicates that you'll need 70% to 80% of your preretirement income. But when you realize how much you need to save, it's tempting to question whether you really need even 70% of your preretirement income.

First, you should prepare a detailed analysis of your expected expenses after retirement. How much you will need depends in large part on how you plan to spend your retirement years.

How can you help ensure that your expenses will be lower? Consider these tips:

✔ **Pay off your mortgage.** Mortgage payments often consume 30% or more of an individual's gross income. Eliminating this expense can drastically reduce income needed for retirement. If you can't pay off your mortgage, consider selling your home and purchasing a smaller one for cash. Not only will you eliminate the mortgage payment, but a smaller home often results in lower utility bills, property taxes, and maintenance costs.

✔ **Get rid of other debts.** It's not unusual for consumer debt payments to equal 10% to 20% of an individual's take home pay. Try to enter retirement debt free.

✔ **Keep your automobile.** Instead of purchasing a new car every couple of years, keep your current car for as long as it's in good working order. That will eliminate car payments from your retirement budget.

✔ **Look for ways to reduce travel and leisure expenses.** Look for and use senior discounts. Plan activities for non-peak times, when rates may be lower.

✔ **Consider relocating.** The cost of living varies significantly from city to city and state to state. You may be able to reduce your living expenses substantially by moving to another locale. However, this is more than a financial decision. You also need to decide whether you want to move away from family, friends, and familiar surroundings.

✔ **Work at least part-time.** If you still don't have sufficient funds to support yourself during retirement, consider working at least part-time. Even a small amount of annual earnings can help significantly in funding your retirement. ✔✔✔

# Should You Consider Incentive Trusts?

An incentive trust is much like a traditional irrevocable trust, except that it sets specific conditions on trust distributions. Some people establish incentive trusts to make sure beneficiaries stay in the family business. Others want to encourage higher education or public service. Some want to discourage behavior. Still others want to encourage beneficiaries to get married.

If you think an incentive trust may be a useful part of your estate plan, consider the advantages and disadvantages. The advantages of incentive trusts include:

✔ If you write the conditions for disbursement properly, they provide objective criteria for when and how to make disbursements.

✔ They encourage beneficiaries to behave in ways that are important to you.

✔ They allow you to condition disbursement on your beneficiary's age, so you can decide when he/she is old enough to responsibly manage the inheritance.

✔ They can help you accomplish goals through your beneficiaries, such as continuing the family business or pursuing philanthropic interests.

But there are also disadvantages:

✔ While incentive trusts allow you to specify conditions for distributions, they restrict the ability of trustees to make different decisions if new circumstances arise.

✔ Incentive trusts can cause resentment among beneficiaries, who may feel it is not your place to tell them how to live their lives.

✔ Encouraging goals you think are important may cause beneficiaries to neglect other good opportunities.

✔ Incentive trusts may be plagued by the law of unintended consequences. You may instruct the trust to pay out a stipend for your beneficiaries to go to school, but that can encourage them to become professional students.

✔ Because incentive trusts are often more complicated than traditional irrevocable trusts, they may be more expensive to establish.

There are a number of issues that could affect the design and implementation of an incentive trust. Consider these points carefully:

✔ **Goals** — What behaviors do you want to promote? Think about what matters to you and your beneficiaries. What goals are fair and reasonable for you to expect your beneficiaries to achieve?

✔ **Coordination with your estate plan** — Incentive trusts are just one component of an estate plan. Decide whether you want to create a separate incentive trust or build incentive clauses into a trust designed for another purpose. Make sure the incentive trust doesn't conflict with or detract from other components of your estate plan.

✔ **Duration** — How long do you want the incentive trust to last? For grantors with substantial wealth, a trust may span many generations. Can you realistically set expectations for beneficiaries who aren't even born yet?

✔ **Beneficiaries** — Who will benefit from the monies disbursed from the incentive trust? Considerations here are similar to those for any kind of trust: who do you include and exclude?

✔ **Trustee designation** — The trustee of an incentive trust typically has a more difficult job than the trustee of a simple traditional trust, since he/she must decide when beneficiaries have met the conditions you specified. Make that job easier by writing conditions that are objective and easily measured. ✔✔✔

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# How Much Should Be Invested in Stocks?

One of the most often asked questions is how much of a person's portfolio should be made up of stocks. It's a good question, and one that doesn't always have a clear-cut answer. The percentate of stocks in your portfolio will vary depending upon a number of different factors, including your age, current net worth, and penchant for taking risks. Still, there are a few basic rules of thumb that are worth adhering to.

If you're saving for retirement, most financial planners will recommend that the younger you are, the more of your portfolio should be allocated to stocks. When we're young, taking risks tends to come along with less catastrophic consequences than when we're nearing retirement age. If formulas work for you, the general idea is to subtract your age from the number 100. For example, 30-year-olds will often do well by allotting 70% of their portfolios to stocks, while 60-year-olds may want to reduce this percentage to 40%.

Of course, age is just one factor that influences portfolio allocations, and there are more aspects that need to be taken into consideration to make the right decisions. The best way to ensure that your portfolio is properly divided is to work with a financial planner who is fully aware of your situation and can make educated suggestions about how to move forward with your investments. After all, a formula can only get you so far, and personal recommendations will always be more valuable than guesswork. ✔✔✔

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## Market Data

| Stocks: | Apr 22 | Mar 22 | Feb 22 | YTD | 12 Mon. |
|---|---|---|---|---|---|
| Dow Jones Ind. | 32977.21 | 34678.35 | 33892.60 | -9.2% | -2.6% |
| S&P 500 | 4131.93 | 4530.41 | 4373.94 | -13.3 | -1.2 |
| Nasdaq Comp. | 12334.64 | 14220.52 | 13751.40 | -21.2 | -11.7 |
| Total Stock Market | 41679.16 | 45847.30 | 44467.72 | -14.3 | -4.6 |
| **Precious Metals:** | | | | | |
| Gold | 1911.30 | 1942.15 | 1909.85 | 5.9 | 8.1 |
| Silver | 23.11 | 24.99 | 24.24 | 0.9 | -10.9 |
| **Interest Rates:** | **Apr 22** | **Mar 22** | **Feb 22** | **Dec 21** | **Apr 21** |
| Prime rate | 3.50 | 3.50 | 3.25 | 3.25 | 3.25 |
| Money market rate | 0.08 | 0.07 | 0.07 | 0.07 | 0.08 |
| 3-month T-bill rate | 0.89 | 0.61 | 0.36 | 0.08 | 0.02 |
| 20-year T-bond rate | 3.14 | 2.59 | 2.25 | 1.94 | 2.19 |
| Dow Jones Corp. | 4.33 | 3.72 | 3.31 | 2.48 | 2.37 |
| Bond Buyer Muni | 4.23 | 3.83 | 3.66 | 3.45 | 3.46 |

Sources: *Barron's, Wall Street Journal. An investor may not invest directly in an index.*



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