HELPING YOU UNDERSTAND THE COMPLEXITIES OF WEALTH MANAGEMENT AND PROVIDING SOLUTIONS AS UNIQUE AS YOUR GOALS

WEALTH MANAGEMENT NEWSLETTER

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INVESTORS ARE HUMAN, TOO

In 1981, the Nobel Prize-winning economist Robert Shiller published a groundbreaking study that contradicted a prevailing theory that markets are always efficient. If they were, stock prices would generally mirror the growth in earnings and dividends. Shiller's research showed that stock prices fluctuate more often than changes in companies' intrinsic valuations (such as dividend yield) would suggest.[1]

Shiller concluded that asset prices sometimes move erratically in the short term simply because investor behavior can be influenced by emotions such as greed and fear. Many investors would agree that it's sometimes difficult to stay calm and act rationally, especially when unexpected events upset the financial markets.

Researchers in the field of behavioral finance have studied how cognitive biases in human thinking can affect investor behavior. Understanding the influence of human nature might help you overcome these common psychological traps.

Herd mentality

Individuals may be convinced by their peers to follow trends, even if it's not in their own best interests. Shiller proposed that human psychology is the reason that bubbles form in asset markets. Investor enthusiasm (irrational exuberance) and a herd mentality can create excessive demand for hot investments. Investors often chase returns and drive up prices until they become very expensive relative to long-term values.

Past performance, however, does not guarantee future results, and bubbles eventually burst. Investors who follow the crowd can harm long-term portfolio returns by fleeing the stock market after it falls and waiting too long (until prices have already risen) to reinvest.

Availability bias

This mental shortcut leads people to base judgments on examples that immediately come to mind, rather than examining alternatives. It may cause you to misperceive the likelihood or frequency of events, in the same way that watching a movie about sharks can make it seem more dangerous to swim in the ocean.

1 *The Economist*, "What's Wrong with Finance?" May 1, 2015.

Confirmation bias

People also have a tendency to search out and remember information that confirms, rather than challenges, their current beliefs. If you have a good feeling about a certain investment, you may be likely to ignore critical facts and focus on data that supports your opinion.

Overconfidence

Individuals often overestimate their skills, knowledge and ability to predict probable outcomes. When it comes to investing, overconfidence may cause you to trade excessively or downplay potential risks.

Loss aversion

Research shows that investors tend to dislike losses much more than they enjoy gains, so it can actually be painful to deal with financial losses.[2] Consequently, you might avoid selling an investment that would realize a loss even though the sale may be an appropriate course of action. The intense fear of losing money may even be paralyzing.

It's important to slow down the process and try to consider all relevant factors and possible outcomes when making financial decisions. Having a long-term perspective and sticking with a thoughtfully crafted investing strategy may also help you avoid expensive, emotion-driven mistakes.

Note: *All investments are subject to market fluctuation, risk and loss of principal. When sold, investments may be worth more or less than their original cost.*

HOW TO GET A BIGGER SOCIAL SECURITY RETIREMENT BENEFIT

Many people decide to begin receiving early Social Security retirement benefits. In fact, according to the Social Security Administration, about 72 percent of retired workers receive benefits prior to their full retirement age. But waiting longer could significantly increase your monthly retirement income, so weigh your options carefully before making a decision.

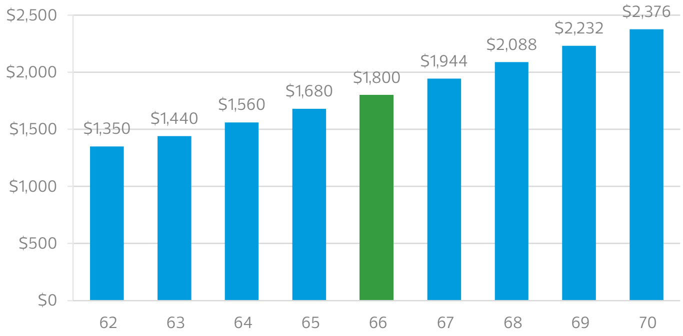
Timing counts

Your monthly Social Security retirement benefit is based on your lifetime earnings. Your base benefit—the amount you'll receive at full retirement age—is calculated using a formula that takes into account your 35 highest earnings years.

If you file for retirement benefits before reaching full retirement age (66 to 67, depending on your birth year), your benefit will be permanently reduced. For example, at age 62, each benefit check will be 25 percent to 30 percent less than it would have been had you waited and claimed your benefit at full retirement age (see table).

Alternatively, if you postpone filing for benefits past your full retirement age, you'll earn delayed retirement credits for each month you wait, up until age 70. Delayed retirement credits will increase the amount you receive by about 8 percent per year if you were born in 1943 or later.

The chart below shows how a monthly benefit of $1,800 at full retirement age (66) would be affected if claimed as early as age 62 or as late as age 70. This is a hypothetical example used for illustrative purposes only; your benefits and results will vary.



Birth year	Full retirement age	Percentage reduction at age 62
1943-1954	66	25 percent
1955	66 and 2 months	25.83 percent
1956	66 and 4 months	26.67 percent
1957	66 and 6 months	27.50 percent
1958	66 and 8 months	28.33 percent
1959	66 and 10 months	29.17 percent
1960 or later	67	30 percent

Early or late?

Should you begin receiving Social Security benefits early, or wait until full retirement age or even longer? If you absolutely need the money right away, your decision is clear-cut; otherwise, there's no 'right answer. But take time to make an informed, well-reasoned decision. Consider factors such as how much retirement income you'll need, your life expectancy, how your spouse or survivors might be affected, whether you plan to work after you start receiving benefits, and how your income taxes might be affected.

2 *The Wall Street Journal*, "Why an Economist Plays Powerball," January 12, 2016.

FIVE THINGS TO KNOW ABOUT INHERITED INDIVIDUAL RETIREMENT ACCOUNTS

When an individual retirement account (IRA) owner dies, the IRA proceeds are payable to the named beneficiary—or to the owner's estate if no beneficiary is named. If you've been designated as the beneficiary of a traditional or Roth IRA, it's important that you understand the special rules that apply to inherited IRAs.

It's not really your IRA

As an initial matter, while you do have certain rights, you are generally not the owner of an inherited IRA. The practical result of this fact is that you can't mix inherited IRA funds with your own IRA funds, and you can't make 60-day rollovers to and from the inherited IRA. You also need to calculate the taxable portion of any payment from the inherited IRA separately from your own IRAs, and you need to determine the amount of any required minimum distributions (RMDs) from the inherited IRA separately from your own IRAs.

But if you inherited the IRA from your spouse, you have special options. You can take ownership of the IRA funds by rolling them into your own IRA or into an eligible retirement plan account. If you're the sole beneficiary, you can also leave the funds in the inherited IRA and treat it as your own IRA. In either case, the IRA will be yours and no longer treated as an inherited IRA. As the new IRA owner (as opposed to beneficiary), you won't need to begin taking RMDs from a traditional IRA until you reach age 70½, and you won't need to take RMDs from a Roth IRA during your lifetime at all. And as IRA owner, you can also name new beneficiaries of your choice.

Required minimum distributions

As beneficiary of an inherited IRA—traditional or Roth—you must begin taking RMDs after the owner's death. In general, you must take payments from the IRA annually, over your life expectancy, starting no later than Dec. 31 of the year following the year the IRA owner died. But if you're a spousal beneficiary, you may be able to delay payments until the year the IRA owner would have reached age 70½.

In some cases you may be able to satisfy the RMD rules by withdrawing the entire balance of the inherited IRA (in one or more payments) by the fifth anniversary of the owner's death. In almost every situation, though, it makes sense to use the life expectancy method instead—to stretch payments out as long as possible and take maximum advantage of the IRA's tax-deferral benefit.

You can always elect to receive more than the required amount in any given year, but if you receive less than the required amount you'll be subject to a federal penalty tax equal to 50 percent of the difference between the required distribution and the amount actually distributed.

More stretching...

What happens if you elect to take distributions over your life expectancy but you die with funds still in the inherited IRA? This is where your IRA custodial/trustee agreement becomes crucial. If, as is sometimes the case, your IRA language doesn't address what happens when you die, then the IRA balance is typically paid to your estate—ending the IRA tax deferral.

Many IRA providers, though, allow you to name a successor beneficiary. In this case, when you die, your successor beneficiary steps into your shoes and can continue to take RMDs over your remaining distribution schedule.

Federal income taxes

Distributions from inherited IRAs are subject to federal income taxes, except for any Roth or nondeductible contributions the owner made. But distributions are never subject to the 10 percent early distribution penalty, even if you haven't yet reached age 59½. (This is one reason why a surviving spouse may decide to remain as beneficiary rather than taking ownership of an inherited IRA.)

When you take a distribution from an inherited Roth IRA, the owner's nontaxable Roth contributions are deemed to come out first, followed by any earnings. Earnings are also tax-free if made after a five-calendar-year holding period, starting with the year the IRA owner first contributed to any Roth IRA. For example, if the IRA owner first contributed to a Roth IRA in 2014 and died in 2016, any earnings distributed from the IRA after 2018 will be tax-free.

Creditor protection

Traditional and Roth IRAs are protected under federal law if you declare bankruptcy. The IRA bankruptcy exemption was originally an inflation-adjusted $1 million, which has since grown to $1,283,025. Unfortunately, the U.S. Supreme Court has ruled that inherited IRAs are not covered by this exemption. (If you inherit an IRA from your spouse and treat that IRA as your own, it's possible that the IRA won't be considered an inherited IRA for bankruptcy purposes, but this was not specifically addressed by the Court.) This means that your inherited IRA won't receive any protection under federal law if you declare bankruptcy. However, the laws of your particular state may still protect those assets, in full or in part, and may provide protection from creditors outside of bankruptcy as well.

HOW IS GROSS DOMESTIC PRODUCT CALCULATED IN THE U.S.?

The gross domestic product (GDP) is a measurement of the total value of all goods and services produced in the United States over a given time period. It is used by economists, government officials, market forecasters and others to gauge the overall health of the U.S. economy.

Although there are several ways of calculating GDP, the *expenditures approach* is the most common. It focuses on final goods and services purchased by four groups: consumers, businesses, governments (federal, state and local), and foreign users.

The calculation and a description of its components follow:

C+I+G+(X–M)

- **Consumption (C):** Also known as personal consumption, this category measures how much all individual consumers spend in the United States.
- **Investment (I):** Not to be confused with investments in the stock and bond markets, this is the amount businesses spend on fixed assets (e.g., machines and equipment) and inventories, as well as the amount spent on residential construction.
- **Government (G):** This category tracks the amount the government spends on everything from bridges and highways to military equipment and office supplies. It does not include transfer payments—for example, Social Security and other benefit payments.
- **Exports (X):** This is the value of goods and services produced in the United States. and purchased in foreign countries.
- **Imports (M):** This is the value of goods and services produced in foreign countries and purchased in the United States.

Historically, the United States has run a trade deficit, which means imports have outpaced exports.

Once the final GDP values are calculated, the percentage change is calculated from one time frame to the next, generally quarter to quarter or annually. Reported quarterly by the Bureau of Economic Analysis, these percentages can influence both investment markets and policy decisions.

WHAT IS THE MOST IMPORTANT COMPONENT OF GROSS DOMESTIC PRODUCT IN THE UNITED STATES?

We often hear in the media that consumer spending is crucial to the overall health of the U.S. economy, but exactly how important is it? Representing approximately two-thirds of overall GDP, consumption—the almighty consumer—is the largest driver of economic growth in the United States. Of the nearly $18 trillion in U.S. gross domestic product (GDP) (2015), American shoppers are responsible for a piece of the pie worth about $12 trillion.

Consumption is tracked by the Bureau of Economic Analysis, and is reported as personal consumption expenditures (PCE) in its monthly personal income and outlays news release. Since the late 1960s, PCE as a percentage of overall GDP has crept up from a low of approximately 58 percent to nearly 70 percent today.

PCE is divided into goods and services. The services category typically represents the largest part of PCE, accounting for more than 65 percent over the past two years. Examples of services include health care, utilities, recreation and financial services.

Goods are broken down further into durable and nondurable goods. Durable goods are those that have an average life of at least three years. Examples include cars, appliances and furniture. Nondurable goods are those with an average life span of less than three years and include such items as clothing, food and gasoline.

Durable goods represent approximately 10 percent of total PCE, while nondurable goods make up about 20 percent.

So the next time you're out shopping, for anything from a bottle of ketchup to a new car, consider that you're doing your part to fuel our nation's growth.

Sources: World Bank.org, accessed June 2016; Federal Reserve Bank of St. Louis, 2016; Bureau of Economic Analysis, 2016.

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