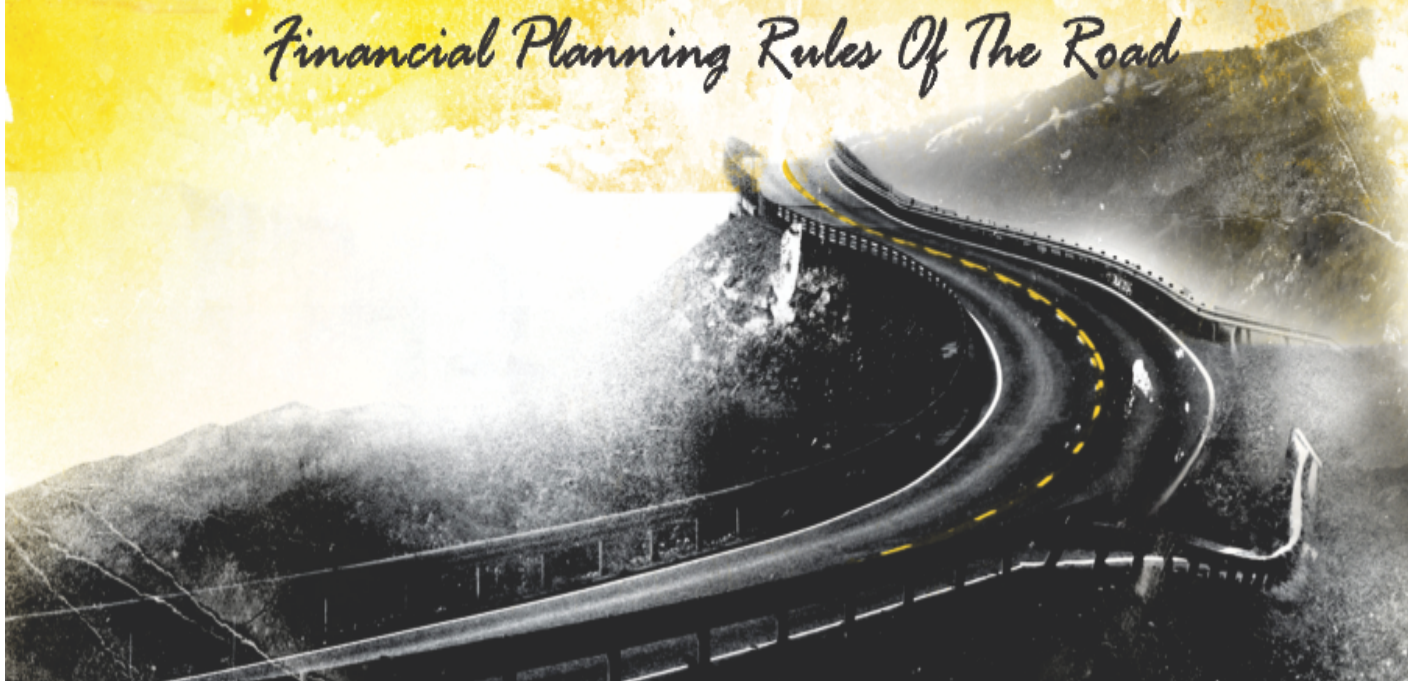


# FINANCIAL [GUARDRAILS]

*Financial Planning Rules Of The Road*



*The following guide was authored by both Richard Rosso, CFP, CIMA and Danny Ratliff, CFP, ChFC.*

---

Guardrails are forged to prevent navigators from veering off course. Financially, it's easy to drift off target or accidentally travel a path that places your wealth in jeopardy. **Not to fear:** Real Investment Advice's guardrails were created to help readers and clients keep their finances on track. These nine tenets focus on helping investors and individuals avoid common mistakes, not-so-obvious monetary pitfalls and the financial industry dogma that's so entrenched throughout media channels.

## Guardrail #1:

**Annuities should be planned, not sold.** Not all annuities are bad; unfortunately, how they're often sold is not always in the best interest of the consumer. Beware financial "experts" who perpetuate annuity false stereotypes as a self-serving agenda to generate business. The ultimate purpose of an annuity is to mitigate longevity risk (you can be on Earth a long time!), and provide a lifetime income for an individual, couple and survivors. The smartest way to understand if an

annuity is appropriate is to first determine whether the projected total wealth accumulated, current periodic investing, along with Social Security, pensions and other liquid assets can adequately sustain your household spending throughout your entire retirement. • If it's determined there's a shortfall, an annuity structure may be effective as a supplement to Social Security benefits as an income you cannot outlive. Always partner with a Certified Financial Planner who also acts as fiduciary (a professional obligated to take the highest and best care), to create a comprehensive financial or retirement plan to determine whether an annuity can complement your holistic investment strategy. Avoid variable annuities (a combination of mutual funds and insurance), if you're contributing to company retirement plans, Individual Retirement Accounts, or Roth IRAs. If you're ten years or longer from retirement, fixed or deferred income annuities for a portion of your savings may be considered.

## **Guardrail #2:**

**Consider a primary residence as a place to reside, not an investment.** We observe too often that primary residences are considered investments when in reality, depending on the mortgage outstanding, is more liability than asset. To calculate return from a primary residence, an owner must track every improvement and add it to the purchase price to calculate a cost basis. Taxes, maintenance and what you would have paid in rent vs. the mortgage payment must also be considered. According to Yale Professor Robert J. Shiller, noted expert on housing, co-creator of the widely-used S&P/Case-Shiller U.S. National Home Price Index, and author of several editions of the seminal book *Irrational Exuberance*, a house is a consumption choice, not an investment. Based on his historical research, real home prices (adjusted for inflation), have appreciated an average of 0.6% a year from 1915-2015. Of course, there are exceptions. Depending on the location, overall supply and demand, and uniqueness of the property, appreciation may deviate from national averages. However, these instances are not a typical homeowner experience. The definition of "investment" tends to be misused when capital is allocated to large expenditures like cars and homes. When financial resources are applied to long-term assets, the word "investment" is embraced to help us overcome buyer's remorse and make us feel good about our decisions. Thinking of a house as a place to reside and not an investment will help a buyer maintain perspective and not become "house poor."

## **Guardrail #3:**

**Never allow others to cross your personal financial boundaries.** It's a tough lesson for some, but once learned, never forgotten. There's nothing inappropriate about maintaining boundaries and saying "no" to obligations that may place your personal financial security in jeopardy. For example, we witness parents who extend themselves to co-sign for children. We know of those who lend to friends and family members only to be disappointed when loan obligations are not met. It's acceptable to establish in a household budget, charitable intentions and gifts; it's honorable to help people you love who are in need. However, it's best to understand upfront what the financial impact to your personal situation is going to be. Know your boundaries and adhere to them. If you say "no" enough, others will respect them, too.

## **Guardrail #4:**

**Create your own financial rules around debt control and savings. Then stick to them. No matter what.** Consider strict debt management and savings habits as the blend of robust soil which allows opportunities to be realized. Excessive debt and limited ability to buffer against financial emergencies can limit a person's ability to take on riskier but rewarding ventures like career change, entrepreneurial endeavors and risks that may lead to significant, long-term wealth.

**Real Investment Advice's guardrails are as follows:** *Mortgage debt: Primary residence mortgage = 2X gross salary. Student loan debt: Limited to one year's worth of total expense, tuition, room & board, expenses. Personal, unsecured debt (credit card, auto): No more than 25% of gross monthly household income.*

## **Guardrail #5:**

**Invest in yourself.** Human capital is a measure of the economic value of an individual's skill set. A passion to learn can increase capacity to earn. • Consider lifetime earnings as the financial fuel that drives wealth and savings. Seek to boost or learn new skills that will increase your value in the work place or facilitate an entrepreneurial venture. These are methods to maximize the return on you. • To put it in perspective, assuming 30 earnings years at the current median household income of \$59,345, an individual or family would earn \$1,780,350 over a lifetime. A goal could be to double that median income every decade, however that comes from focus, determination, and a little bit of luck.

## **Guardrail #6:**

**Good health is a significant contributor to financial and physical wellness in retirement.** • In a report from Healthview Services, a provider of cost-projections software, healthcare costs in retirement are rising twice as fast as the typical annual increase in Social Security benefits. Latest estimates outline total out-of-pocket spending for an average 65-year old couple retiring today could exceed \$400,000 when Medicare premiums, supplemental insurance and deductibles are included. Keep in mind that cost-of-living adjustments for Social Security are overwhelmed by the rising costs of Medicare Part B premiums. Healthview Services projects a 5.5% annual increase in healthcare costs over the next decade. Per Medicare Trustees as reported by Savvy Medicare, a training program for financial planners, Part B and Part D insurance costs have averaged an annual increase of 5.6% and 7.7% respectively, over the last 5 years and are expected to grow by 6.9% and 10.6% over the next five years. Preventative actions such as regular workout regimens, eating properly and healthy sleep habits can work to reduce the financial stress of the most significant costs retirees face.

## **Guardrail #7:**

**Realistic return projections, time horizons and inflation factors are crucial to successful planning.** Financial planning is far from perfect. After all, working with projected returns on risk assets like stocks, estimating how long a person may live and where inflation may be at the time of retirement, is an intelligent guessing game at best. Consider the plan a snapshot of your progress toward financial life benchmarks. Where you are, outlined direction of where you need to go. Are you on track to meet your needs, wants and wishes? A plan is a diagnostic; the exercise is one of financial awareness. Studies show that people who follow a retirement plan are more successful than those who don't. But know the common pitfalls you'll face, depending on the professional who creates the plan and where his or her loyalties lie. Unfortunately, most planning systems as well as planners tend to provide overly-optimistic outcomes with asset return projections and life expectancies that may be far from what you'll experience living in real world. Why? Most financial plans are created to push product. They're a means to a lucrative end for brokers. An afterthought. When in fact, a comprehensive financial plan should stand alone as a roadmap to financial success, and that includes recognition of how stock markets flow through cycles – bull, bear, flat and realistic assessments of inflation and life expectancies. Consider a second opinion of a completed plan if your first was generated by an employee of a big box financial retailer. Always seek a Certified Financial Planner who acts as fiduciary.

## Guardrail #8:

**Be vigilant of confirmation, recency bias and other emotions when it comes to financial decisions.** Money is emotional. It's impossible to avoid mixing feelings and finances. Success comes from recognizing cognitive and behavioral pitfalls and avoiding them as much as possible. Investors tend to seek opinions that agree with their perspective, which can lead to poor portfolio returns. Success comes from purposely considering those sentiments that disagree with yours. The exercise will open your mind to conditions rarely considered. For example, bulls and bears are myopic in their perspectives. At Real Investment Advice, we consider a view from greater altitudes. Our responsibility is to provide a robust view of overall conditions. Like eagles. And as an eagle, you'll ponder financial and portfolio decisions with a holistic mindset. It's very human to believe that current or recent market conditions will continue indefinitely into the future. Frankly, it's how financial media operates. Be wary of most as it perpetuates what is going on in the present with little regard for the past. The pundits employed by big-box brokerages, and financial media celebrities, prefer you forget the markets of 2000 and 2008. They're succeeding. These negative periods are being pulled into the mist of long-term averages. Averages are misleading. They have little to do with the limited time most households possess to begin and continue an aggressive savings and investing program. Rarely are the "pros" held accountable or freely admit their mistakes. Unfortunately, the public, so inundated with daily information and life, incurs most of the negative stock market impact and loses time (the most precious commodity), trying to break even. It's easy to get sucked in to a current phase, especially as we haven't witnessed an S&P 500 bear market (a decline of 20% or more), since 2008. Per technical analyst and author Gregory Morris in his seminal book *Investing with the Trend*, there have been 10 declines greater than 20 percent in the past 89 years. The average bear market from its beginning peak until it fully returned to that peak lasted over 5.5 years. Most individual investors experience longer recovery periods due to inflation, expenses and poor emotional responses (buying high, selling low).

## Guardrail #9

**Create a household financial wellness evolution.** We define financial wellness as consistent monetary success and pathos which leads to security and generates inner peace. The flow is uneven as stages of wellness ebb and flow along channels of a human existence. It's rarely perfect. However, there always exists a strong center or stasis that like a rubber band, an individual returns to after a deviation from self-defined financial norms. In other words, wellness isn't pretty, but there's beauty in its consistency. It represents a tumultuous soup of philosophies, experiences, ego, habits, perceptions and attitudes. Finances bolster with the victories, falter with the setbacks. The challenge is to assess and maintain alignment over time. More than almost anything else that defines you, financial choices made over a lifetime forge not only the path you travel today, but also the ongoing integrity (or lack thereof), of that road you take into the future. Your overall financial health may flow through to multiple generations long after you're gone, so it's worth understanding that money — your actions, how you treat it, is much bigger than any one individual. The ripples of your financial decisions have potential to carry through and buoy the lives of others or act as undercurrents and pull down everyone around you. Share openly financial successes and failures with your children, communicate legacy intentions before they require interpretation from legal documentations, learn to say no more often to requests that don't sit well with your fiscal security, and clearly define and live your money philosophy. Our guardrails were formed to keep navigators on the route to overall financial success. Deviations are normal and expected, such as the flow of events throughout a human life. However, those with boundaries adjust quickly and get right back on track. They'll remain grounded while others falter. Such are the rules of the road.