



Vision Financial Advisory

John D. VanDyke, ELP

Financial Advisor

5787 Balsam Dr.

Hudsonville, MI 49426

616-855-6244

269-978-7071

john.vandyke@visionfinancialpc.com

www.visionfinancialpc.com

The last 6 weeks have been a crazy ride! The Dow hit an all-time high on Sept. 19, then promptly lost more than 1,000 points over 3 weeks before rallying to set a new all-time high to close out October. Amazing.

This is a perfect example of the importance of "time in" vs. "timing of" the market. A strategy based on fundamental analysis, together with a long-range plan, represents a better method for building wealth over an extended time-frame vs. making adjustments based on hype that the media throw at us this week or next. I trust the articles in this version of the newsletter are helpful to you as you navigate your financial decisions for the long haul.

It's hard to believe we are already coming into the holiday season! Enjoy the changing weather, and the making of memories with your family and friends!

As always, we thank you for your business, and invite you to call us anytime with questions about your accounts or the markets, or to update us on your situation.

-jv

November 2014

Saving or Investing: Is There a Difference?

What Is the Federal Reserve and What Does It Do?

Financial Choices: College, Retirement, or Both?

What is duration, and why should I pay attention to it?

VISION

FINANCIAL ADVISORY CORP

DELIVERING FINANCIAL CLARITY

Saving or Investing: Is There a Difference?



Financially speaking, the terms "saving" and "investing" are often used interchangeably. But the concepts behind these terms actually have some important differences. Understanding

these differences and taking advantage of them may help you in working toward financial goals for you and your family.

Saving

You may want to set aside money for a specific, identifiable expense. You park this money someplace relatively safe and liquid so you can get the amount you want when you need it. According to the Securities and Exchange Commission brochure *Saving and Investing*, "savings are usually put into the safest places, or products, that allow you access to your money at any time. Savings products include savings accounts, checking accounts, and certificates of deposit." Some deposits may be insured (up to \$250,000 per depositor, per insured institution) by the Federal Deposit Insurance Corporation or the National Credit Union Administration. Savings instruments generally earn interest. However, the likely tradeoff for liquidity and security is typically lower returns.

Investing

While a return of your money may be an important objective, your goal might be to realize a return on your money. Using your money to buy assets with the hope of receiving a profit or gain is generally referred to as investing. Think of investing as putting your money to work for you--in return for a potentially higher return, you accept a greater degree of risk. With investing, you don't know whether or when you'll realize a gain. The money you invest usually is not federally insured. You could lose the amount you've invested (e.g., your principal), but you also have the opportunity to earn more money, especially compared to typical savings vehicles. The investment is often held for a longer period of time to allow for growth. It is important to note, though, that all investing involves risk,

including the loss of principal, and there is no assurance that any investing strategy will be successful.

What's the difference?

Whether you prefer to use the word "saving" or "investing" isn't as important as understanding how the underlying concepts fit into your financial strategy. When it comes to targeting short-term financial goals (e.g., making a major purchase in the next three years), you may opt to save. For example, you might set money aside (i.e., save) to create and maintain an emergency fund to pay regular monthly expenses in the event that you lose your job or become disabled, or for short-term objectives like buying a car or paying for a family vacation. You might consider putting this money in a vehicle that's stable and liquid. Think of what would happen if you were to rely on investments that suddenly lost value shortly before you needed the funds for your purchase or expense.

Saving generally may not be the answer for longer-term goals. One of the primary reasons is inflation--while your principal may be stable, it might be losing purchasing power. Instead, you may opt to purchase investments to try to accumulate enough to pay for large future expenses such as your child's college or your retirement. Generally, saving and investing work hand in hand. For instance, you may save for retirement by *investing* within an employer retirement account.

Why is it important?

Both saving and investing have a role in your overall financial strategy. The key is to balance your saving and investing with your short- and long-term goals and objectives. Overemphasize saving and you might not achieve the return you need to pursue your long-term goals. Ignore saving and you increase the risk of not being able to meet your short-term objectives and expenses. Get it right and you increase your chances of staying on plan.





The Fed's mission

The Federal Reserve is the central bank of the United States. Its mission is to provide the nation with a safer, more flexible, and more stable monetary and financial system. For more information on the Federal Reserve, visit www.federalreserve.gov.

Publications

The Federal Reserve releases several publications throughout the year, including the publicly available "Beige Book," which contains information on current economic conditions in each Federal Reserve Bank district, along with interviews with key business leaders, economists, and market experts.

What Is the Federal Reserve and What Does It Do?

If you follow financial news, you've probably heard many references to "the Fed" along the lines of "the Fed did this or that," or "market watchers are wondering what the Fed will do next." So what exactly is the Fed and what does it do, anyway?

What is the Federal Reserve?

The Federal Reserve--or "the Fed" as it's commonly called--is the central bank of the United States. Generally speaking, a central bank is a large, centrally controlled bank that's in charge of a country's interest rates, money supply, and banking system. Most countries have a central bank.

The U.S. Federal Reserve was created by the Federal Reserve Act of 1913, legislation that was enacted mostly in response to a series of financial panics. The Federal Reserve is charged with three main objectives: maximum employment, stable prices, and moderate long-term interest rates (the first two objectives are often referred to as the Fed's "dual mandate"). Over the years, the Federal Reserve's duties have expanded and evolved to include maintaining stability of the entire U.S. financial system.

How is the Fed organized?

The Federal Reserve isn't a single entity. It actually consists of four parts: (1) the Board of Governors, (2) the Federal Open Market Committee, (3) 12 regional Federal Reserve Banks, and (4) thousands of smaller member banks. What does each part do?

The Board of Governors--also called the Federal Reserve Board--is at the top. It consists of seven people who are nominated by the President and approved by the Senate. Each person is appointed for a 14-year term (terms are staggered, with one beginning every two years). The Board of Governors conducts official business in Washington, D.C.

The Chair of the Board of Governors--perhaps the most visible face of U.S. economic and monetary policy--is currently Janet Yellen, the former president of the Federal Reserve Bank of San Francisco. Dr. Yellen was sworn in on February 3, 2014, and is the first woman to hold this post. (Her term as Chair ends on February 3, 2018, and her term as a member of the Board of Governors ends on January 31, 2024.) Prior to Yellen, the Chair of the Federal Reserve was Ben Bernanke, who served from 2006 to 2014, and before him was the somewhat legendary Alan Greenspan, who served from 1987 to 2006.

Next is the Federal Open Market Committee, or FOMC, which is responsible for setting U.S.

monetary policy. The FOMC is made up of the Board of Governors and the 12 regional bank presidents. While all FOMC members discuss and debate economic policy, only 12 members have voting rights: all 7 Board of Governors members and 5 regional bank presidents (the president of the Federal Reserve Bank of New York is a permanent voting member of FOMC; the other regional bank presidents rotate as voting members). The FOMC typically meets eight times per year. When people wait with bated breath to see what the Fed will do next, they're usually referring to the FOMC.

Next are 12 regional Federal Reserve Banks that are responsible for typical day-to-day bank operations. The banks are located in Boston, New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco. (Rumor has it that in 1913 a Missouri senator would only vote for the Federal Reserve Act if his state were home to two regional banks.) Each regional bank has its own president and oversees the thousands of smaller member banks in its region.

So what does the Fed actually do?

The Federal Reserve does a lot of things, but one of its main functions is to set U.S. monetary policy. It does this primarily by: (1) setting the *discount rate*, which is the interest rate the Fed charges commercial banks on money it lends; (2) setting *reserve requirements*, which is how much a bank must hold in reserves; and (3) overseeing *open market operations*, which is the purchase and sale of government securities on the open market. Open market operations impact the *federal funds rate* (the interest rate that banks charge each other on overnight loans of federal funds), which in turn impacts the *prime rate* and the interest rates that consumers ultimately pay. The Fed's recent quantitative easing (QE) program, in which it has purchased mortgage-backed securities and U.S. Treasury bonds at regular intervals to increase the money supply, is a form of open market operations.

Why do people pay attention to the Fed? One reason is interest rates. People often look to the Fed for clues on which way interest rates are headed. Another reason is economic analysis and forecasting. Members of the Federal Reserve regularly conduct economic research, give speeches, and testify about inflation and unemployment, which can provide insight about where the economy might be headed. All of this information can be useful for consumers when making borrowing and investing decisions.



A juggling act

It's the paramount financial conflict many families face, especially as more couples start having children later in life. Should you save for college or retirement? The pressure is fierce on both sides.

Note

**All investing involves risk, including the possible loss of principal, and there can be no guarantee that any investing strategy will be successful.*

Financial Choices: College, Retirement, or Both?

Life is full of choices. Should you watch *Breaking Bad* or *Modern Family*? Eat leftovers for dinner or order out? Exercise before work or after? Some choices, though, are much more significant. Here is one such financial dilemma for parents.

Should you save for retirement or college?

It's the paramount financial conflict many parents face, especially as more couples start having children later in life. Should you save for college or retirement? The pressure is fierce on both sides.

Over the past 20 years, college costs have grown roughly 4% to 6% each year--generally double the rate of inflation and typical salary increases--with the price for four years at an average private college now hitting \$192,876, and a whopping \$262,917 at the most expensive private colleges. Even public colleges, whose costs a generation ago could be covered mostly by student summer jobs and some parental scrimping, now total about \$100,000 for four years (Source: College Board's Trends in College Pricing 2013 and assumed 5% annual college inflation). Many parents have more than one child, adding to the strain. Yet without a college degree, many jobs and career paths are off limits.

On the other side, the pressure to save for retirement is intense. Longer life expectancies, disappearing pensions, and the uncertainty of Social Security's long-term fiscal health make it critical to build the biggest nest egg you can during your working years. In order to maintain your current standard of living in retirement, a general guideline is to accumulate enough savings to replace 60% to 90% of your current income in retirement--a sum that could equal hundreds of thousands of dollars or more. And with retirements that can last 20 to 30 years or longer, it's essential to factor in inflation, which can take a big bite out of your purchasing power and has averaged 2.5% per year over the past 20 years (Source: Consumer Price Index data published by the U.S. Department of Labor, 2013).

So with these two competing financial needs and often limited funds, what's a parent to do?

The prevailing wisdom

Answer: retirement should win out. Saving for retirement should be something you do no matter what. It's an investment in your future security when you'll no longer be bringing home a paycheck, and it generally should take precedence over saving for your child's college education.

It's akin to putting on your own oxygen mask first, and then securing your child's. Unless your retirement plan is to have your children be on the hook for taking care of you financially later in life, retirement funding should come first.

And yet ...

It's unrealistic to expect parents to ignore college funding altogether, and that approach really isn't smart anyway because regular contributions--even small ones--can add up over time. One possible solution is to figure out what you can afford to save each month and then split your savings, with a focus on retirement. So, for example, you might decide to allocate 85% of your savings to retirement and 15% to college, or 80/20 or 75/25, or whatever ratio works for you.

Although saving for retirement should take priority, setting aside even a small amount for college can help. For example, parents of a preschooler who save \$100 per month for 15 years would have \$24,609, assuming an average 4% return. Saving \$200 per month in the same scenario would net \$49,218.* These aren't staggering numbers, but you might be able to add to your savings over the years, and if nothing else, think of this sum as a down payment--many parents don't save the full amount before college. Rather, they try to save as much as they can, then look for other ways to help pay the bills at college time. Like what?

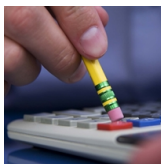
Loans, for one. Borrowing excessively isn't prudent, but the federal government allows undergraduate students to borrow up to \$27,000 in Stafford Loans over four years--a relatively reasonable amount--and these loans come with an income-based repayment option down the road. In addition, your child can apply for merit scholarships at the colleges he or she is applying to, and may be eligible for need-based college grants. And there are other ways to lower costs--like attending State U over Private U, living at home, graduating in three years instead of four, earning credits through MOOCs (massive open online courses), working during college, or maybe not attending college right away or even at all.

In fact, last summer, a senior vice president at Google responsible for hiring practices at the company noted that 14% of some teams included people who never went to college, but who nevertheless possessed the problem solving, leadership, intellectual humility, and creative skills Google is looking for ("In Head-Hunting, Big Data May Not Be Such a Big Deal," *New York Times*, June 19, 2013). One more reason to put a check in the retirement column.

Vision Financial Advisory

John D. VanDyke, ELP
Financial Advisor
5787 Balsam Dr.
Hudsonville, MI 49426
616-855-6244
269-978-7071
john.vandyke@visionfinancialpc.com
www.visionfinancialpc.com

Registered representative and securities offered through Securities Service Network, Inc., member FINRA/SIPC. Fee based advisory services offered through SSN Advisory, Inc., a registered investment advisor.



What is duration, and why should I pay attention to it?

The Federal Reserve's actions over the next year could be important to bond markets, particularly if and when the Fed decides to increase its target interest rate. Since bond prices typically move in the opposite direction from yields, rising bond yields will translate into a decline in bond prices.

If you have bonds or bond mutual funds in your portfolio, you might want to pay attention to the duration of each one. Technically, a bond or bond fund's duration calculates the length of time it will take to receive the full true value of the investment; duration takes into account the present value of expected future payments of interest and principal.

However, duration's biggest value to an investor is as a gauge of how sensitive a bond might be to changes in interest rates. The longer a bond's duration, the more its price is likely to be affected by an interest rate change. A mutual fund's duration can be found in its prospectus; for an individual bond, you'll probably need to ask your broker or the bond's issuer.

To estimate the impact of an interest rate

change on a specific bond holding, simply multiply its duration by the change in interest rates. For example, for a bond fund with a duration of 5 years, a 1% increase in interest rates would generally result in a 5% drop in the fund's value ($1\% \times 5 \text{ years} = 5\%$). Though the Fed's target rate is already at its historic low, the same principle would apply in reverse if interest rates were to fall. A 1% decline in interest rates would likely result in a 3% gain for a bond holding with a duration of 3 years.

Note: These hypothetical examples are intended as an illustration only and do not reflect the performance of any specific investment. They should not be considered financial advice. Before investing in a mutual fund, consider its investment objective, risks, fees, and expenses, which can be found in the prospectus available from the fund. Read the prospectus carefully before investing.

Bear in mind that duration can work somewhat differently for specific types of bonds—for example, floating-rate bonds whose interest payments get reset. That's also true for mortgage-backed bonds, since interest rate changes can cause homeowners to refinance their loans.



Have the rules for 401(k) in-plan Roth conversions changed?

Yes. Thanks to the American Taxpayer Relief Act of 2012 (ATRA), the rules for making 401(k) in-plan Roth

conversions have gotten substantially easier. (These rules also apply to 403(b) and 457(b) plans.)

A 401(k) in-plan Roth conversion (also called an "in-plan Roth rollover") allows you to transfer the non-Roth portion of your 401(k) account into a designated Roth account within the same plan. The amount you convert is subject to federal income tax in the year of the conversion (except for any nontaxable basis you have in the amount transferred), but qualified distributions from the Roth account are entirely income tax free. The 10% early distribution penalty doesn't apply to amounts you convert (but that penalty tax may be reclaimed by the IRS if you take a nonqualified distribution from your Roth account within five years of the conversion).

While in-plan conversions have been around since 2010, they haven't been widely used, because they were available only if you were otherwise entitled to a distribution from your

plan—for example, upon terminating employment, turning 59½, becoming disabled, or in other limited circumstances. But in that case, you already had the option of rolling your funds over (converting) into a Roth IRA.

ATRA eliminated the requirement that you be eligible for a distribution from the plan in order to make an in-plan conversion. Now, if your plan permits, you can convert any vested part of your 401(k) plan account into a designated Roth account regardless of whether you're otherwise eligible for a plan distribution. The IRS has also just recently issued regulations that provide additional clarity on how in-plan conversions work.

Caution: Whether a Roth conversion makes sense financially depends on a number of factors, including your current and anticipated future tax rates, the availability of funds with which to pay the current tax bill, and when you plan to begin receiving distributions from the plan. Also, you should consider that the additional income from a conversion may impact tax credits, deductions, and phaseouts; marginal tax rates; alternative minimum tax liability; and eligibility for college financial aid.