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Asset Management • Retirement, Tax and Estate Planning • Fee Only • No Commissions • Independent Advisor

July 8, 2021

Here is our newsletter for the 3rd Quarter of 2021

Market Update
In the 2nd quarter most asset classes had good gains. US real estate and commodities were the big winners, with gains of 11.7% and 16.2% respectively. All asset classes had positive gains, which is pretty unusual.

With interest rates moderating in the quarter, most bonds made up for their losses in the 1st quarter.

Over the last year, stocks, real estate and commodities all had big gains. The only losers were US Intermediate-term bonds and gold which had fractional losses.

Asset Class Returns- Ending 6/30/21

Asset Class	1st Qtr	One Year
US Large Cap Stock	8.5	40.8
US Small Cap Stock	4.3	61.8
Foreign -Developed Mkts Stock	5.2	32.6
Emerging Mkts Stock	5.2	38.8
US Intermediate-Term Bond	1.8	-0.4
Emerging Markets Bond	3.9	10.6
High Yield Bond	2.4	14.0
Inflation-Protected Bond (TIPS)	3.2	6.1
Cash	0.0	0.02
US Real Estate	11.7	34.3
Commodities	16.2	56.4
Gold	4.2	-0.7

Creating a Sustainable Financial Lifestyle
This is a piece I had in my newsletter back in 2011 which details how we help clients manage their cash flow. Here is an updated version.

Often the most neglected, yet most important aspects of our financial lives concerns managing cash flow. We help our clients build a plan that enables then to discover what is a financially sustainable lifestyle for them. Any business advisor will tell you understanding your current cash coming into and out of the business is crucial to success and it's no different for one's personal finances. As part of any financial plan we put together for our clients, analyzing cash flow enables us to produce many specific recommendations. Here are some of the issues we help clients address.

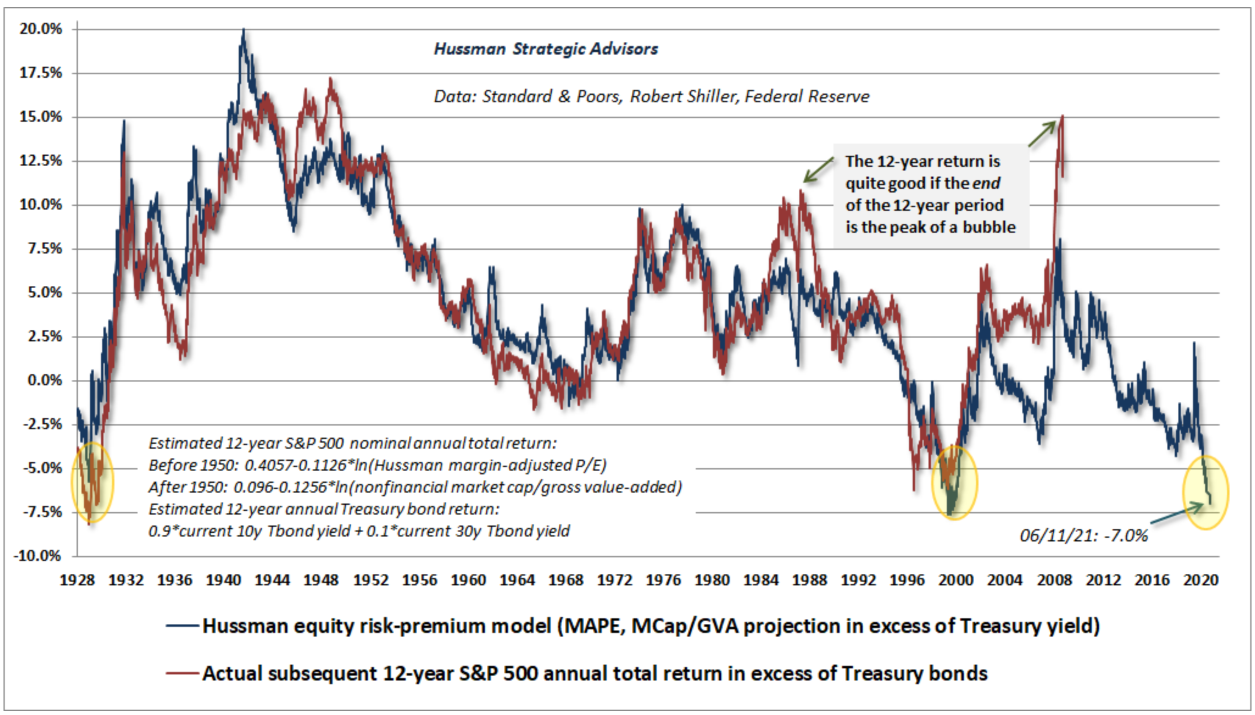
1. How much cash should you have in savings in case unexpected expenses or a drop in income occurs? How much is adequate depends upon several factors including the sources and nature of your income and expenses, insurance coverage, assets and debt.
2. Debt. This is a big problem for some and an opportunity for others. The first step is to make sure you have an adequate emergency fund so you never have to use credit card or other debt to fund living expenses. We help our clients work out a plan to pay down and/or restructure their debt and use the tax laws to their advantage. With home loan rates near record lows now is a great time to consider refinancing. Rates are around 4.0% (now 3.4%) for 30 year loans and 3.25% (now 2.5%) for 15 year loans.

3. Saving for short-term goals. Identify, quantify and set up accounts to save for future cars, vacations, college for the kids or other goals you may have.
4. Create a Budget. For many this is an unwelcome chore but there are many ways to accomplish this. The first step is to determine your current level of expenses. You could use one of the budget tools available such as Mint or Quicken.

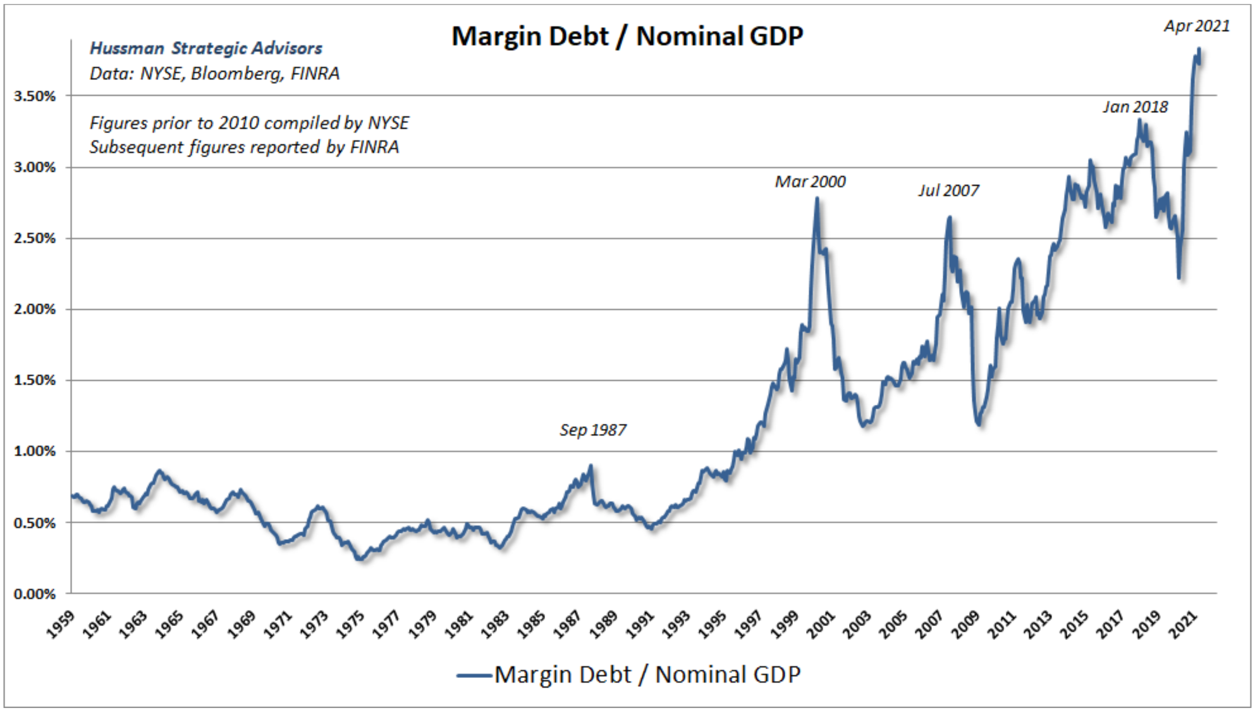
Understanding and managing your cash flow is probably the most important aspects of your finances. Higher or lower investment returns pale in comparison of importance.

Valuations from John Hussman

John Hussman's valuation chart for U.S. large cap stocks is rather busy, but just focus on the 3 low points in the graph. The negative 7.0% currently means his projected return for stocks on average over the next 12 years will be 7% less than the 10 year Treasury bond will earn, or roughly 6% annual loss on average for 12 years. Again, his measure is <u>not a good short-term measure or indication of market returns over periods of less than 10 years.</u> In fact, the projected returns were negative for most of the last 7 years, yet the stock market has had great gains over that period. Note the only other times his valuation has been this low is in 2000 and 1929.



The chart below shows the level of margin debt that is being used to buy stocks in the US. This value, as a percent of nominal GDP, has gone up about 70% over the last year and is at all-time highs. If you are not familiar, margin debt is used to double the amount of shares you can buy by using borrowed money from the broker. Unfortunately if the shares go down you can be forced to sell at a much lower price. In a big market downturn this margin debt will reinforce the downtrend in the market. So, caution and some cash on the sidelines is a very good idea.



An Alternative to CDs for Your Savings Account

Everyone needs a cash cushion in the bank that can be used in case you have unexpected expenses or your income drops. Jason Zweig with the Wall Street Journal presented an interesting idea in a recent article. Currently the highest yields you can find for a totally liquid savings account is about 0.4% (at CIT). With savings account yields so low some are turning to CDs. Unfortunately CDs are only yielding 0.5 to 0.7% for 1 to 2 year terms. These higher yields are hardly worth the loss of liquidity.

Another option is to buy Series I Savings Bonds from the US government. The good news is these are currently paying 3.54% plus every 6 months the value of the bond is increased at the rate of inflation as measured by the CPI. Note if inflation goes negative the bonds have a floor where the yield will not fall below zero. Also, interest on I Bonds is exempt from state and local taxation and for Federal tax purposes, the I Bond interest can be deferred until maturity or until it's redeemed.

The downside compared to savings accounts or CDs: I Bonds can't be liquidated until they've been held for at least 12 months, and if they're sold within the first 5 years they forfeit the last 3 months of interest. Note these are 30 year bonds with the yield fixed for 30 years. In addition, I Bonds can only be purchased at an amount of $10,000 per year per account holder. Lastly, I Bonds can only be purchased directly from the government by going to TreasuryDirect.com. So, if you have several tens of thousands of cash you want to keep just in case, the yields for I bonds are compelling.

Housing

Here is the latest look at housing prices from the Case-Shiller Home Price Index, which measures home prices in the 20 largest metro-areas. Year over year as of April 1st prices have gone up 15%. Note the rate of increase is even higher than during the boom in 2003 thru 2006. From the chart you can see prices took off right after the pandemic started. Prices are also increasing fast in smaller markets: just look on Zillow.com to see what your home is worth. Low inventories and low interest rates are fueling the boom. Your guess is as good as mine about what will happen going forward. Construction material prices are one of the reasons prices have spiked, but those have moderated recently. Higher interest rates would soften prices.

If you are thinking about buying, selling, refinancing or whatever else, give me a call.

Sincerely,

Stan Johnson
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Registered Investment Advisor
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