Cornerstone Independent Asset Management

M Financial Group™

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PARTICIPANT PERSPECTIVES

DOES YOUR RISK TOLERANCE NEED A REALIGNMENT?

Market volatility. A change in your time horizon. Different goals. These things can affect the amount of risk you feel comfortable taking with your investments. Your ability to tolerate risk influences the investment choices you make and may have a significant impact on your success in achieving your financial objectives. Periodically revisiting your risk tolerance is an important step in the portfolio review process.

A Moving Target

Your feelings about risk may change depending on what the markets are doing. During a prolonged period of market volatility, you may find your comfort level dropping, even if you previously thought you had a high tolerance for risk. If you're a conservative investor, an extended market upswing may have the opposite effect, encouraging you to take on additional investment risk.

In either case, basing investment decisions on market behavior instead of a well-thought-out investing strategy isn't the best plan. Instead, take time to reassess your feelings about risk. If they've truly changed, adjust your strategy going forward to reflect the changes.

More Than a Feeling

How much money could you afford to lose if investment values dropped significantly? Your ability to accept risk also depends on your financial circumstances and your time horizon for tapping your assets. If investment losses would leave your finances in jeopardy and you have a relatively short time frame before you'll need your money, your capacity for taking risk may be limited. Make sure you consider your risk capacity in your review.

A Realistic View

A long period of either strong or weak market performance may convince you that the current trend will continue indefinitely. Perceived risk is how much risk you think an investment holds. However, your perception of an investment's risk might not match its actual risk. In that case, you could be taking more or less risk than you should to remain within your comfort zone and still reach your goals.

Your financial professional can help you reassess your risk tolerance along with the level of risk in your portfolio.

MEASURING YOUR NET WORTH

Rising property values and a strong stock market can drive U.S. household net worth to record highs, even as household debt increases. What about your personal net worth? When it comes to your finances, are you getting ahead, treading water, or falling behind?

Taking a Picture

Doing a net worth calculation provides a snapshot of your financial situation at a particular point in time. Simply put, net worth reflects the value of your assets (everything you own) minus your liabilities (everything you owe). Your assets might consist of your home and other property, retirement savings, investments, cash, jewelry, and similar items. Your liabilities might include the unpaid balances on your mortgage, consumer and education loans, and credit cards.

Because asset values and outstanding liabilities are constantly in flux, it's important to assess the numbers on the same date — the last day of the year or the month, for example. After your assets and liabilities are itemized, your net worth can be calculated by subtracting your total liabilities from your total assets.

Digging Deeper

In addition to tracking net worth, you may find it helpful to look at selected financial ratios derived from your financial information.

For example, a basic liquidity ratio can help gauge your ability to handle a financial emergency, such as unexpected medical bills or loss of employment income. It's calculated by taking the total of your liquid assets (checking and savings accounts plus other assets that can quickly and easily be converted to cash) and dividing that number by your monthly expenses. The ideal number is between three and six (meaning you have enough liquid assets to cover between three and six months of living expenses). You may know this by another name: your emergency fund. Having an adequate emergency fund helps avoid the need to take on unwanted credit card debt or sell investments at an inopportune time.

Your debt-to-income ratio may be another appropriate ratio to monitor. It's calculated by dividing your total annual debt payments by your annual income. A low debt-to-income ratio indicates that you haven't taken on more debt than you can comfortably handle. In general, you want a number that is less than 36%.

Looking at Trends

Make it a practice to track your net worth and pertinent financial ratios from year to year. Aim to grow your net worth during your working years by saving, investing, and not taking on more debt than you can handle. By determining your net worth periodically, you can measure the progress you're making toward your financial goals.

DEALING WITH DEBT BEFORE YOU RETIRE

Should you make it a priority to retire your debts before you retire? As with other aspects of your financial planning, much will depend on your personal goals and situation. A debt-free retirement is a goal that many Americans share, if for no other reason than the peace of mind it can bring. If having to make debt payments would create undue financial and emotional stress, then you'll likely want to make a concerted effort to eliminate — or at least significantly reduce — your debts before you retire.

Making Choices

Absent a large influx of cash, you may not be in the position to pay off your debts all at once. When deciding where to allocate the extra dollars that are available for debt repayment, consider how much it's costing you to carry each debt.

Credit cards and consumer loans with high interest rates typically are prime candidates for paying off as quickly as possible. Although the money allocated to paying off these debts wouldn't be available to invest elsewhere, you'd essentially earn a return equal to the interest you'd otherwise pay.

Paying Off Your Mortgage

Your home mortgage may be your largest debt, and the one you'd most like to pay off before you retire. Before acting, see if there's a penalty for prepayment and review the loan amortization schedule to get an idea of how much interest you'd save by accelerating your payments.

With a traditional mortgage, the amount of each monthly payment that goes toward principal increases and the portion representing interest decreases as you get further into the loan term. So, paying off the loan a few years early may not save as much interest as you'd expect. Sometimes, keeping a mortgage and allocating additional cash flow to other investment opportunities can be good strategy. A financial professional can help you work through the analysis.

Finding the Money

Although the prospect of trimming your debt while saving for your future retirement may seem daunting, don't give up on the idea without examining your options. Are there ways you can simplify your lifestyle? Could you downsize to a smaller home? Drive a less expensive vehicle? Spend less on college for your children? Proactive steps taken now, before you retire, might go a long way toward freeing up the cash you need to pay off burdensome debt, beef up your savings, and improve your overall financial picture in the years ahead.

To learn more, please contact:

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