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A Funny Thing Happened on the Way to Higher Rates

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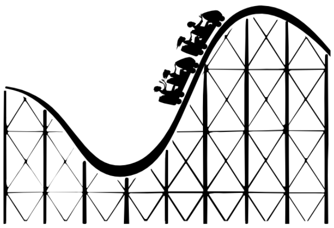


It's interesting how the markets can sometimes humble the best analysts. Take what's happening in the bond market. Last year, pundits pronounced that bond yields would rise in 2014. But, since the beginning of the year, yields have drifted lower, falling over a half a percentage point– *see Figure 1*. How long these lower rates may last is anyone's guess – think of momentum and riding a roller coaster for the first time. You can never tell when a drop will end and the next climb will begin. But when it does, there's that feeling in the pit of your stomach.

What's going on? An interesting article on Reuters, which centered on speeches and Q&A sessions given by former Fed Chief Ben Bernanke, may offer some clues. The former Fed chief (Bernanke's term ended in January) seemed unusually clear regarding his expectations that easy-money policies and below-normal interest rates are here for a long time to come. Investors must remember, however, that the Federal Reserve does not set long-term bond yields, but its policies are influential. If investors believe that any eventual hike in short-term rates might be delayed or very gradual, it can be reflected in long-term rates staying low. Given recent comments and current economics, we believe rates will continue to fluctuate in this narrow range until early 2015.

It's not just Treasury bonds Investment-grade corporate debt, real estate investment trusts (REITs) and junk bonds have all performed well, though junk debt has underperformed most of the fixed income classes *(Wall Street Journal, StockCharts, MarketWatch).*

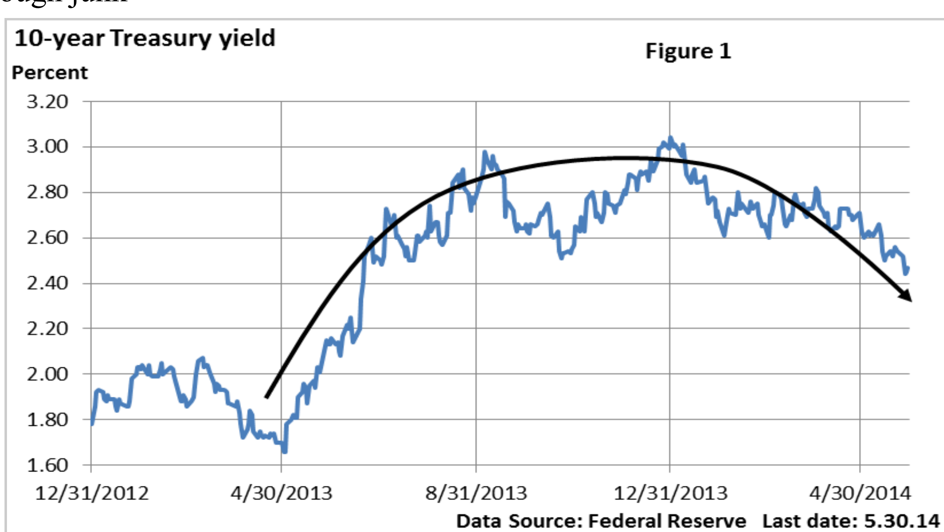
As investors have seemingly warmed to the idea that any rate hikes by the Fed are likely to be slow and gradual, cash has been flowing into bonds. The demand is pushing prices higher and rates lower.

It's not just in the U.S. The European Central Bank (ECB) has cut its key rate to 0.25%, and policy makers across the Atlantic have hinted that they may be ready to launch a U.S.-style program of bond buys *(ECB monthly press conference)*. At a minimum, overseas officials have said they may once again cut rates in the near term.

Patience (and low rates) won't pay the bills Investors seeking income continue to step outside traditional allocation models and thought processes. Corporations are trying to answer that need, as 421 of the 500 companies comprising the S&P 500 are now paying dividends. As this number of dividend payers nears levels not seen since 1998, the year-over-year S&P 500 annual cash dividend is set to achieve double-digit increases for the second year in a row. Buyer beware as many of the companies are first time dividend payers and may be short-term players in the dividend paying game. This is why we still favor companies like PepsiCo, which recently raised its dividend for the 55th year in a row. And ultra-conservative investors may want to consider long-term CD's from online Internet banks. Don't plan to hold the CD to maturity. Instead, we believe investors may be money ahead by accepting the higher rate today, and paying a minor interest rate penalty in a couple years.

Retirement Trivia: Which major US bankruptcy was the main catalyst for the creation of the Pension Benefit Guarantee Corporation?

A) City of New York
B) Studebaker
C) American Airlines
D) Lionel Corporation



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Is Your Physical Health A Retirement Sinkhole?

Earlier this year a massive sinkhole swallowed up nine classic Corvette automobiles at an estimated loss of $3,000,000. There's actually a security video of this hole gobbling up these iconic and very valuable cars.

While it's disheartening to watch these American classics vanish, it's a valuable reminder for new and future retirees' that their life savings can quickly disappear if they don't avoid their own retirement sinkholes. Most notably, their Physical health.

Most retirees are aware of the threat that medical expenses can have on their retirement funds. Fidelity estimates that a 65 year-old couple retiring in 2013 may need up to $220,000 to cover medical expenses throughout retirement.

That's a hefty price tag that is best offset by maintaining a healthy and active lifestyle. Yet, for many baby boomers, health and wellness have been put on the back burner as they focus their time and energy on maintaining their careers, aging parents, and adult children.

What's at risk is their ability to achieve the retirement they desire. One survey found that about 40% of respondents said it was difficult for them to kneel, stand for two hours, walk one-quarter mile, climb 10 steps without resting, sit for two hours, lift and carry 10 pounds, reach over their heads, push or pull a large object, or grasp small objects.

The way we translate that is 40% of retirees are going to struggle on a vacation that requires some walking, standing or holding onto a rail. It means spending time on the floor or in the yard with grandchildren is going to be painful and limited, instead of fun and engaging. Pastimes like gardening, biking, or watching a movie may also be less enjoyable than before.

The evidence is clear, allowing your body and physical health to slip into a retirement sinkhole carries consequences well finances.

Therefore, boomers need to realize that having a functional body in retirement is of equal, or greater, value than having the proper savings and allocation.

Retirement Trivia Answer:

Answer **b: Studebaker**

In 1963 when Studebaker terminated its employee pension plan more than 4,000 auto workers lost some or all of their promised pension plan benefits. As a result, Congress passed the Employee Retirement Income Security Act (ERISA) in 1974 which established the Pension Benefit Guaranty Corporation (PBGC).

Source: pbgc.gov