The Light

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Most Basic Rule of Financial Planning

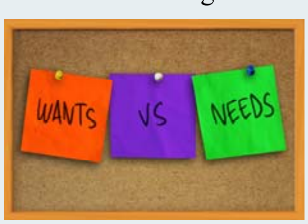
By Tim Rowsey, CPA, Investment Advisor Rep.

One of the most basic rules of financial planning is so simple and yet so challenging that many people have a difficult time ever fully embracing it. This is a concept that is applicable for a student finishing school and just entering the workforce, a couple raising children, or a retired person living on a fixed income. It is a concept that can enable people to build great wealth over time and also to enjoy a less stressful life. It runs counter to most Americans' popular view of life and how to live, but if it is mastered, it can be extremely fulfilling. What is this concept? ***"Spend less than you earn."***

This is not a new concept and in fact can be referenced even in literature of over one hundred years ago. Charles Dickens referenced it in David Copperfield, equating happiness with spending less than income and misery with spending more than income. See his quote below.

***"Annual income twenty pounds, annual expenditure nineteen nineteen and six, result happiness. Annual income twenty pounds, annual expenditure twenty pounds ought and six, result misery."* — Charles Dickens, David Copperfield**

There are two possible components of this wealth building equation. The first is reducing expenditures below the level of current income. The major challenge in this is that it requires discipline and self-denial. Much like going on a diet, the financial benefits are worthwhile long term but may require some short term sacrifice. The larger the margin between income and expenses, the greater the resources that become available for saving and wealth building. Most Americans today have some level of discretion on how they spend their income. The major challenge is deciding what is a need vs. what is a want.



With easy credit availability many people *Continued on page 2*

New Limits for 2019

By Chris Bevington, CPA, Investment Advisor Rep.

The Treasury Department recently announced inflation-adjusted figures affecting pension plans and other retirement related items for the upcoming tax year. With the new cost-of-living adjustment of 2.8% being the largest since 2012, several limits saw above average increases for the 2019 tax year. When considering that Medicare Part B premiums only rose by a little more than 1%, the majority of beneficiaries should see genuinely higher net payout in 2019.

After being stuck at $5,500 for six years, the IRA contribution limit has increased for the first time since 2013 to $6,000. The contribution limit for 401(k) plans, or similar workplace retirement accounts, increased from $18,500 to $19,000. Catch-up contribution limits for those 50 or older remain unchanged at $1,000 for IRAs, and $6,000 for workplace plans. Catch-up contributions are allowed for individuals even if they don't turn 50 until December 31, 2019.

Inflation adjustments also increased the amount of earned income subject to social security tax up from $128,400 to $132,900. This represents a 3.5% increase. Earned income, beyond these limits, is not subject to Social Security tax. This allows a small percentage of workers (less than 1 in 10) to escape paying Social Security tax on some, or most, of their income, depending on their earnings. Why not apply the payroll tax to all income? The straightforward answer is because there's an annual cap on what an individual can receive in Social Security benefits. Since there's a cap on benefits, there is also a cap on what amount of earned income is taxable.

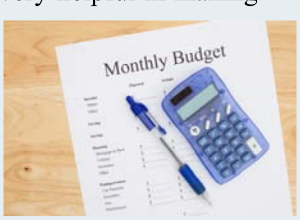
Individuals can begin drawing Social Security as early as age 62, knowing benefits will be reduced, versus what they would be if waiting until full retirement age. In addition to the reduction in benefits, also be aware of the earnings limit test for Social Security recipients who are less than full retirement age. If your earnings exceed $17,640 in 2019, and you are under full retirement age for the entire year, benefits are reduced by $1 for every $2 earned above *Continued on page 3*

Rule (continued from page 1)

today don't even realize that they are spending more than their income. Advertising and media tell us that we need to spend more, that we deserve it, that we shouldn't deny our spending wants and desires. Recent surveys indicate that for households that have credit card debt, the average amount owed is over $9,000. In reality for most people there are many decisions that we make that could be used to impact our expenditures. Where or how often do we eat out, what kind of car do we drive, how large is the house in which we live? How many cell phones do we have and what kind of plan are we on? Starbucks coffee, McDonald's coffee, or home brewed coffee? Every day we make choices on how we live and what costs are associated with our lifestyle.

In retirement planning for clients, I see a wide range of income levels that people expect in their retirement years. I have told the story before of meeting with two families in the same week and asking them how much income they needed to live comfortably in retirement. One family thought they would be happy with an annual income of $35,000 per year, while the second stated that they needed $100,000 per year. Obviously the retirement assets and income stream needed by the second family will be much larger than the first and will require much more savings to achieve.

One of the first steps in spending less than you earn is to know exactly how much you do earn and spend. For most people the income side of the equation is relatively easy to determine. The challenging part is knowing where all the money goes. One of the steps that we commonly suggest to clients is tracking all of their expenses for one month. Most people are shocked to see how much they spend on various categories if they actually commit to documenting every dollar spent for one month. This information can be very helpful in making informed choices about what to adjust if, in fact, the expenses exceed the household income. Once the outflows are known, a budget can be used as a tool to help keep expenses below income. A budget is nothing more than a financial spending plan. It is one of the tools that can help clients understand their choices relating to their income and stay on the path to spending less than they earn.



The other component of this equation is the income side. This is another way for the income to exceed the expenses if the income can be raised. There are several possible ways to increase this side of the equation. Some options would be to work more hours, get a second job, or if retired already, take a part time job. One trend we are seeing more and more is retired people working at least part time, both to increase the household income and also to have an outlet to interact with other people and get out of the house. Another income increasing option would be to start your own business. Another consideration is to sell an asset or something of value that you no longer really need. Today, there is a market for almost anything through Ebay or other venues.

While this concept of spending less than you earn may seem easier as income rises, I have been amazed through the years to see people with a relatively low income stream spend less than their income and accumulate significant assets over their lifetime. Many people in their seventies and eighties who grew up during the depression learned early how to control their expenses. Today many of these same people who have continued that careful spending lifestyle have resources significantly beyond their current spending needs.

If you have a desire to grow wealth over time, or to reach longer term goals such as retirement or saving for college, you need to begin with this basic principle. If you can in fact keep your spending beneath the level of your income, you will be taking the first major step toward reaching your long term goals and in the words of Charles Dickens trading "misery" for "happiness." ■

Limits (continued from page 1)

the limit. If your full retirement age occurs in 2019, you can earn up to $46,920 in the months leading up to full retirement age with no reduction in benefits. If your earnings exceed that, Social Security benefits are reduced by $1 for every $3 earned above the limit.

The chart below highlights the updated limits for retirement savings, annual gifting amounts, and additional information you may wish to consider when planning for the 2019 tax year. ■

Limitation	2018	2019
IRA Contribution limit	$5,500	$6,000
IRA Catch-up contribution (age 50 and over)	$1,000	$1,000
401(k) elective deferrals	$18,500	$19,000
401(k) catch-up deferrals (age 50 and over)	$6,000	$6,000
Other information		
Income subject to Social Security tax	$128,400	$132,900
Maximum earned income before SS benefits are reduced for those collecting SS before full retirement	$17,040	$17,640
Annual Gift Exclusion	$15,000	$15,000
Standard Mileage Rate	$0.545/ mile	$0.58/ mile
Social Security Cost of Living Adjustment	2.0%	2.8%

Market Recap

How the major indices performed in the 4th Quarter 2018

DOW JONES INDUSTRIAL AVERAGE
4th Quarter return -11.31% YTD return -3.48%

S & P 500 COMPOSITE
4th Quarter return -13.52% YTD return -4.38%

RUSSELL 2000
4th Quarter return -20.2% YTD return -11.01%

BARCLAYS AGGREGATE BOND
4th Quarter return 1.64% YTD return 0.01%

*All indices are reported Total Return which includes Dividends

Market Update

By Tim Rowsey, CPA
Investment Advisor Rep.

The fourth quarter was the worst quarter for equities in years.

Stocks saw significant declines in the fourth quarter with December capping off the quarter as one of the worst months for the stock market in a decade and the worst December since 1931. The Dow Jones Industrials lost over 11% in the quarter and ended the year with a loss of 5.6% (only 3.5% if dividends are included). The S & P 500 lost 13.5% in the quarter and also ended the year down 6.2% (only 4.4% loss with dividends included.) Small cap stocks, as represented by the Russell 2000 showed an even greater decline with a quarterly loss of 20% and a YTD loss of 11.1%. Believe it or not the losses could have been greater had the year ended on December 23rd. The market managed to recover almost 7% between that date and the end of the year.

Bonds showed small gains for the quarter.

The Barclays Aggregate Bond Index rose by 1.6% for the quarter. The Fed increased the benchmark interest rate another .25% in December as was widely expected. It appears that the stock market was anticipating no more increases, however, as stocks dropped significantly on that news. Two more rate increases were originally projected in 2019, however the Fed did indicate that they might be open to slowing that pace. Ten year treasuries dropped to a yield of 2.7%.

Stocks are well off their fall record highs.

Market volatility in the fourth quarter hit some new land-marks. Multiple 2% or more decline days were fairly common in December and the day after Christmas the Dow saw a 5% 1,000 point gain in a day. Tariffs on China and trade agreements have continued to put a damper on the market. In addition, the government shutdown and uncertainty have held the markets back. Moving into 2019 there is much more uncertainty on corporate earnings and even the overall state of the economy. Most experts believe that we are still at least a year or more away from any recession. If some of the uncertainty in the market settles down we will hopefully return to some steady growth in the equity markets. 2018 was a reminder of the importance of being diversified. For most investors this means holding at least a portion of the total portfolio in non-equity asset classes such as bonds or real estate. ■

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