

Life + Wealth Intersects

*A Wealth Coaching Publication for
Affluent Entrepreneurs
Family, Investments, Estate, Tax,
Wealth.*



Helping you
make wise choices
where life intersects wealth.

Special Points of Interest

- Is it wise to get out of the market?
- What does Abraham Lincoln say about government's role in the economy?
- Tax increases, tax cuts.
- A cheap alternative to national health care.
- A great investment idea; a fitness coach
- The good times of our youth were created by our parents
- Write it down!



If you know of a youth or young adult that is suffering from depression, please call Michael Lantz to introduce them to help free of charge.

For more information go to:

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Inside this issue:

| | |
|---|---|
| "Should I be getting out of the market?" | 1 |
| Abraham Lincoln Quote about Government | 3 |
| Taxes.... | 3 |
| How to cheaply fix our health care | 3 |
| What can we learn from the good times of our youth? | 4 |
| Write It Down by Jim Stovall | 4 |

Should I be getting out of the stock market?

by Michael C. Lantz, CPA/PFS, CFP®

I start by reminding you of the trade-offs and corresponding risks of such an action, while reminding you of the way markets work.

I've seen how many of you have changed your risk preference, but a change to the portfolio should only be considered once your counsel has led to a clear understanding of the consequences. The following are some key points to consider.

Risk Trade-Offs

A comprehensive wealth management solution must address multiple risks spanning the entire planning horizon. Managing risk in this context means determining the trade-offs associated with reducing or eliminating some risks at the expense of increasing or taking others. The following are three of the risks that any plan must weigh:

- Market risk** - the risk that stock prices will decline.
- Inflation risk** - the risk of losing long-term purchasing power.
- Longevity risk** - the risk of outliving your money.

Most of you who have asked the question above wants to get out of equities and has a desire to eliminate market risk, or the chance of further declines in the value of the portfolio. However, this action will magnify the risk of losing purchasing power, as a market-risk-free investment is almost guaranteed to lose money after tax and inflation. This loss of purchasing power could increase the chances that you will outlive your money, especially if you maintain a high level of spending relative to assets.

Sound advice is indispensable in this situation, as there is no "right" set of trade-offs. For example, an older investor with substantial assets relative to spending might never outlive his money, even if he invests in cash equivalents and accepts more inflation risk. His trade-off may be to give up the potential for philanthropy and/or the upside of a substantial estate for heirs in exchange for lower market risk. This may be a perfectly rational decision.

A younger investor with a longer horizon and/or higher spending relative to assets may also choose to eliminate market risk. However, he may have to offset higher inflation and longevity risks by accepting other trade-offs, such as working longer and/or significantly reducing long-term lifestyle expectations. Once again, this could be a rational choice.

The critical part of this analysis is that risk is multi-dimensional, and any decision to increase or decrease certain risks at the expense of others should be viewed as a long-term decision made with a thorough understanding of the trade-offs. This does not mean risk preferences can't change again in the future, but only that the client should assume that they won't.

Expectations and Market Timing

In contrast, it is more likely for those expressing a desire to get out of equities to regard their potential action as a temporary move to the sidelines rather than as a long-term or permanent decision. Their proposed strategy may be to ride out the storm in the shelter of the harbour—and set sail again when the weather improves.

There are obvious problems with this attempt to time the market. Once you decide to get out, the next question is when to get back in. You may feel it is more prudent to wait for stabilization or strengthening of the economy as a sign the market will recover. However, a recovery in the equity market will tend to lead a recovery in the economy. In this example, by the time the weather appears clear from the harbour, the tide may have already gone out. Then again, the primary motivation for a move to the sidelines may not be to time the recovery, but rather, to prevent further losses. Your intuition may be that the poor economic outlook, overall pessimism, and slew of bad news must surely correlate with a continued slide in stock prices. This logic will not necessarily hold, because market prices are set based on expectations from all public information.

For instance, security prices are generally a function of discounted expected future cash flows. Therefore, part of the recent decline in prices can be attributed to lower expected future cash flows due to the economic doom and gloom. Yet a market recovery could ensue even if future cash flows decline, provided they decline less than expected.

Regardless of whether you realizes it, extrapolating the recent past and assuming stock prices will continue to fall amidst the doom and gloom implies that new information will be worse than expected. It would be wise to concede, however, that news is unknowable, especially in terms of where it stacks up against expectations already priced into stocks.

Market Equilibrium and Expected Returns

Expected future cash flow is one part of the stock pricing equation. Another is the discount rate used, which is also known as the company's cost of capital or the investor's expected return.

(Continued on page 2)

“Should I be getting out of the stock market? (continued)”



“Before you weigh the risks and trade-offs associated with getting out of stocks, you may want to consider sticking around for the higher expected returns, given that they have already experienced the risk....buying stocks and continuing to hold them are basically the same decision.”

Michael C. Lantz
CPA/PFS, CFP®
Creator of “The Building
Block Investing Model™”

(Continued from page 1)

Market efficiency implies that risk and return are related. So, if economic doom and gloom represent an increase in risk, this suggests that a rise in the discount rate applied to lower expected future cash flows would also force a drop in stock prices. A rise in the discount rate means an increase in expected returns for the investor.

The intuition and economic logic behind this concept are powerful. There are no orphaned stocks. Every share has to be held by someone; and, for every seller there must be a buyer. In order for the market to clear, investors accepting the risk of buying or holding stocks in an environment filled with pessimism, uncertainty, and volatility are incented by lower prices and higher expected returns.

So, for every investor choosing to offload risk by decreasing equity exposure, someone else must take on that risk by increasing equity exposure. One side of the trade will not systematically “beat” the other. It is a risk preference that should be carefully considered before deciding which side of the trade to be on. Before you weigh the risks and trade-offs associated with getting out of stocks, you may want to consider sticking around for the higher expected returns, given that they have already experienced the risk.

Rather than dwelling on or extrapolating declining portfolio values, it is wise to view the drop in stock prices as a sunk cost. Buying stocks and continuing to hold them are basically the same decision, when you ignore taxes, and it may be useful to frame your decision in these terms.

Instead of focusing on why they should continue to hold a portfolio of stocks that was worth \$X and is now worth \$Y, try determining how they would deploy \$Y if they were a brand new client coming to you with cash to invest. A perspective framed in these terms will hopefully take the emphasis off the recent decline in value and focus on the recent increase in expected returns.

Time to Recover

An alternative to sticking around for higher expected returns is moving your portfolio to market-risk-free assets that offer lower expected returns. As discussed above, this may be a rational choice for some investors willing to trade market risk for other risks.

However, let's review another perspective to this decision by referring to the table below. It shows the approximate number of years to recoup a 45% decline assuming various rates of expected return. Before eliminating market risk from your portfolio, please consider the admittedly extreme example that at the current risk-free rate of roughly 2%, it would take nearly 30 years (ignoring taxes, transaction costs, and withdrawals) to recover.

| Expected Return | Approx. Number of Years to Recover a 45% Loss |
|-----------------|---|
| 2% | 30 |
| 3% | 20 |
| 4% | 15 |
| 5% | 12 |
| 10% | 6 |
| 15% | 4 |

No one can predict the future—and stock prices may decline further before they recover—but most of you should not have a short-term need for your invested assets since a long time horizon is a prerequisite for investing in equities. If long-term investors still want to flee the market, it will likely be instructive for you to contemplate the probability that stock markets around the world will not reach their previous highs within the next 30 years!

Conclusion

The decline in stock prices has certainly been dramatic and painful. Before this pain leads you to abandon your equity allocations, the following considerations can help you frame this decision with added perspective:

Risk is multi-dimensional: Eliminating one risk may magnify another.

Stock prices and the business cycle: A recovery in stock prices tends to lead a recovery in economic conditions, and there is no evidence that risk premiums become reliably negative during recessions.

Risk premiums and economic conditions: Risk premiums tend to be countercyclical (i.e., lower when economic conditions are strong and higher when they are weak).

Prices reflect all current information: More bad news will not necessarily cause further stock price declines; it is news relative to expectations that matters.

Payback time: Weigh the upside of higher expected returns against the probability that equity markets will not reach previous highs within the payback period associated with a market-risk-free investment.

Abraham Lincoln Quote about Government

Recently I've taken to the history books regarding the economy to make a rational decision regarding the recent stimulus bill passed by President Obama and the Congress.

First I wanted to answer a sensible question. Pres. Obama promised in his campaign that getting the deficit under control had to be a top priority. He was even harsh of Pres.

Bush's economic policies that soared the deficit to record levels (me too by the way). My question then, "If Bush's policies that soared the deficit to record levels in eight years was bad, how is doubling the deficit under Obama's and the Democratic Congress' plan in less than one year better?"

From my experience dealing with many successful small business owners the tax, borrow and spend policies proffered by this administration will kill entrepreneurial incentive, the back bone of this economy and the major contributors to job growth. Employers are now telling me how they have no incentive to produce or take additional risk under Obama.

Below are quotes from Pres. Obama's hero and mine too, Abraham Lincoln. He said, "You cannot help the poor by destroying the rich. You cannot strengthen the weak by weakening the strong. You cannot bring about prosperity by discouraging thrift. You cannot lift the wage earner up by pulling the wage payer down. You cannot further the

You cannot build character and courage by taking away men's initiative and independence. You cannot help men permanently by doing for them, what they could and should do for themselves."

"The American Republic will endure until the day Congress discovers that it can bribe the public with the public's money."

I hope there are a few entrepreneurial conservatives in Congress who will stand up to this massive debt and increase in the tax burden placed on the thrifty wealth creators in our country and start voting no on the administrations recent tax, borrow and spend policies.

(For those who may not agree with me, please call me and let me know why.)



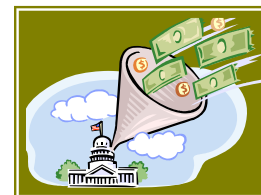
"The American Republic will endure until the day Congress discovers that it can bribe the public with the public's money."

Abraham Lincoln
16th President of the
United States

Taxes.....

I like what Peg Bracken said, "Why does a slight tax increase cost you two hundred dollars and a substantial tax cut save you thirty cents?" I've polled several people who for the most part are workers that have been affected by this economic downturn. The average wage of my survey group was \$31,894. I asked them if the \$400 tax savings from the administration's stimulus

package would help them. The answers were mostly consistent. "No", was there reply. They were going to mostly use it to pay off debt and some were going to save it. One intuitively said that the real stimulus needed to go to her employer, a real estate developer, to help him create opportunity. In her words, "I depend more on my employer than the government, give him help."



"I depend more on my employer than the government, give him help."

Anonymous employee

How to cheaply fix our health care system.

Plato said, "Attention to health is life greatest hindrance." From this introduces my recommendation for the government's role in national health care.

The EPA has already concluded we live in a toxic society by the results of their National Adipose Tissue Survey that indicates 80% of those tested had all 20 known toxins in their body. Toxins cause obesity and many other health related issues. Toxins in the form of antibiotics, hormones and pesticides we ingest from food. Other know toxins we breath and ingest from the water we drink. The government can start by teaching the American public the truth about the food we eat. It can regulate better the quality of food, especially fast food.

Most people I know do not focus any attention on health prevention. Just simple exercise and eating healthier can increase health so that very expensive health care to fix a problem can be eliminated and in the long run **substantially** reduce the cost of health insurance.

The government can take a role in promoting in medical schools prevention. Most doctors only focus on the symptoms and don't often ever teach a patient the cause and more importantly how to overcome the cause.

This approach would be far more cost effective and in turn over a generation, substantially increase the health of our society and lower the high cost of unhealthiness.



"...in the long run the money you spend on creating abundant health will be far less than the money you'll spend to correct ill health."

Michael Lantz
3X Ironman Finisher
Triathlon Coach

Helping You make Wise Choices Where
Life intersects Wealth.

Michael C. Lantz, CPA/PFS, CFP® Partner
Laura McCormack, Partner
Lantz Wealth Partners, Ltd.
7881 W. Charleston Blvd., Suite 220
Las Vegas, NV 89117

Ofc Phone: 702-579-7090
Mike's Cell: 702-497-9649 (text messaging okay)
Laura's Cell 702-858-6684 (text messaging okay)
Email: Laura@LantzWP.com or Mike@LantzWP.com
Web: <http://www.lantzwp.com>

*"The injury of prodigality leads to this,
that he who will not economize will
have to agonize."*

Confucius

Write It Down *by Jim Stovall*

In our society today, a promise, commitment, or intent takes on a more serious tone if it is put in writing. You can't buy a house, rent a car, or even subscribe to a magazine without putting something in writing.

When a conflict or disagreement arises, invariably someone will ask, "Did you get it in writing?" Reducing our thoughts and intentions to writing is the way we address our commitments to others. Unfortunately, too often in our personal and professional lives, we don't treat ourselves nearly as well.

I know people who would not think of going to the drugstore, shopping mall, or grocery store without taking a list of things they want to get. Logically, these people do not want to waste their time or another trip to the store. But many of these same people have never thought of writing down their short term or even long term goals. They spend more time planning their grocery list or their three-day weekend than they spend planning their life.

Just as putting a commitment in writing to someone else makes it more serious in our own mind, putting our commitments to ourselves in writing holds us accountable to our goals. If it's worthy of your time, effort, and energy, it is certainly worthy of being written down.

Just yesterday, I received a phone call from a former mayor of my city. Although I have not seen him in a number of years, he stays in

What can we learn from the good times of our youth?

How many of you have a photo like this one celebrating a 1st birthday? During most of our youth, our parents shielded us from uncertainty and risk. While they may have struggled to pay the bills, most of us never went to bed hungry, we had a roof overhead and clothes to wear.

In today's tough economic times, there are others that are benefiting from our sacrifice. While they may not understand our sacrifice and may even not express gratitude, they will learn and in turn, they too will provide that same security to those that eventually depend on them.



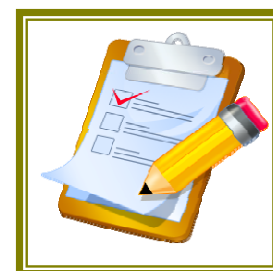
contact with me and many other people several times each year. My friend and former mayor is the best I have ever seen at staying in touch with those that matter to him. On each of his calls, he invariably asks me about my family, my colleagues, and our mutual friends.

Yesterday during his call, I asked him how he kept all of these names, dates, and relationships straight in his mind. He informed me that he actually has a filing system and a calendar so that he will not forget any of his friends, family members, or former colleagues on their birthdays, holidays, and special dates.

Some people might think it callous that he actually keeps a filing system and a special calendar for phone calls to friends. On the other hand, I admire and respect my friend for caring enough about people to write down their vital statistics and follow up by putting notations on a calendar. If you wouldn't go to the store without making a note to get milk, bread, and eggs, isn't it worth writing down your life goals and the people in your world that matter most?

As you go through your day today, resolve to put into writing your most important life goals and reminders to stay in touch with people that matter most to you.

Today's the day!



"If you wouldn't go to the store without making a note to get milk, bread, and eggs, isn't it worth writing down your life goals and the people in your world that matter most?"

Jim Stovall

Jim Stovall is the president of Narrative Television Network, as well as a published author of many books including The Ultimate Gift. He is also a columnist and motivational speaker. He may be reached at 5840 South Memorial Drive, Suite 312, Tulsa, OK 74145-9082, or by e-mail at JimStovall@aol.com.

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