Duane's Capital Ideas

Strengthening your financial future

How Much Risk Can You Take?

Many market shocks are short-lived once investors conclude the event is unlikely to cause lasting economic damage. Still, major market downturns such as the 2000 dot-com bust and the 2008-09 credit crisis are powerful reminders that we cannot control or predict exactly how, where, or when precarious situations will arise.

Market risk refers to the possibility that an investment will lose value because of a broad decline in the financial markets, which can be the result of economic or sociopolitical factors. Investors who are willing to accept more investment risk may benefit from higher returns in the good times, but they also get hit harder during the bad times. A more conservative portfolio generally means there are fewer highs, but also fewer lows.

Your portfolio’s risk profile should reflect your ability to endure periods of market volatility, both financially and emotionally. Here are some questions that may help you evaluate your personal relationship with risk.

How much risk can you afford?

Your capacity for risk generally depends on your current financial position (income, assets, and expenses) as well as your age, health, future earning potential, and time horizon. Your time horizon is the length of time before you expect to tap your investment assets for specific financial goals. The more time you have to keep the money invested, the more likely it is that you can ride out the volatility associated with riskier investments. An aggressive risk profile may be appropriate if you’re investing for a retirement that is many years away. However, investing for a teenager’s upcoming college education may call for a conservative approach.

How much risk may be needed to meet your goals?

If you know how much money you have to invest and can estimate how much you will need in the future, then it’s possible to calculate a “required return” (and a corresponding level of risk) for your investments. Older retirees who have sufficient income and assets to cover expenses for the rest of their lives may not need to expose their savings to risk. On the other hand, some risk-averse individuals may need to invest more aggressively to accumulate enough money for retirement and offset another risk: that inflation could erode the purchasing power of their assets over the long term.

How much risk are you comfortable taking?

Some people seem to be born risk-takers, whereas others are cautious by nature, but an investor’s true psychological risk tolerance can be difficult to assess. Some people who describe their personality a certain way on a questionnaire may act differently when they are tested by real events. Moreover, an investor’s attitude toward risk can change over time, with experience and age. New investors may be more fearful of potential losses. Investors who have experienced the cyclical and ever-changing nature of the economy and investment performance may be more comfortable with short-term market swings.

Brace yourself

Market declines are an inevitable part of investing, but abandoning a sound investment strategy in the heat of the moment could be detrimental to your portfolio’s long-term performance. One thing you can do to strengthen your mindset is to anticipate scenarios in which the value of your investments were to fall by 20% to 40%. If you become overly anxious about the possibility of such a loss, it might be helpful to reduce the level of risk in your portfolio. Otherwise, having a plan in place could help you manage your emotions when turbulent times arrive.

All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.
Key Retirement and Tax Numbers for 2018

Every year, the Internal Revenue Service announces cost-of-living adjustments that affect contribution limits for retirement plans, thresholds for deductions and credits, and standard deduction and personal exemption amounts. Here are a few of the key adjustments for 2018.

**Employer retirement plans**
- Employees who participate in 401(k), 403(b), and most 457 plans can defer up to $18,500 in compensation in 2018 (up from $18,000 in 2017); employees age 50 and older can defer up to an additional $6,000 in 2018 (the same as in 2017).
- Employees participating in a SIMPLE retirement plan can defer up to $12,500 in 2018 (the same as in 2017), and employees age 50 and older can defer up to an additional $3,000 in 2018 (the same as in 2017).

**IRAs**
The limit on annual contributions to an IRA remains unchanged at $5,500 in 2018, with individuals age 50 and older able to contribute an additional $1,000. For individuals who are covered by a workplace retirement plan, the deduction for contributions to a traditional IRA is phased out for the following modified adjusted gross income (AGI) ranges:

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single/Head of Household (HOH)</td>
<td>$62,000 - $63,000</td>
<td>$72,000 - $73,000</td>
</tr>
<tr>
<td>Married Filing Jointly (MFJ)</td>
<td>$99,000 - $119,000</td>
<td>$101,000 - $121,000</td>
</tr>
<tr>
<td>Married Filing Separately (MFS)</td>
<td>$0 - $10,000</td>
<td>$0 - $10,000</td>
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</tbody>
</table>

**Note:** The 2018 phaseout range is $189,000 - $199,000 (up from $186,000 - $196,000 in 2017) when the individual making the IRA contribution is not covered by a workplace retirement plan but is filing jointly with a spouse who is covered.

The modified AGI phaseout ranges for individuals to make contributions to a Roth IRA are:

<table>
<thead>
<tr>
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<th>2017</th>
<th>2018</th>
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<tbody>
<tr>
<td>Single/Head of Household (HOH)</td>
<td>$118,000 - $133,000</td>
<td>$120,000 - $135,000</td>
</tr>
<tr>
<td>MFJ</td>
<td>$186,000 - $196,000</td>
<td>$189,000 - $199,000</td>
</tr>
<tr>
<td>MFS</td>
<td>$0 - $10,000</td>
<td>$0 - $10,000</td>
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**Estate and gift tax**
- The annual gift tax exclusion for 2018 is $15,000, up from $14,000 in 2017.
- The gift and estate tax basic exclusion amount for 2018 is $5,600,000, up from $5,490,000 in 2017.

**Personal exemption**
The personal exemption amount for 2018 is $4,150, up from $4,050 in 2017. For 2018, personal exemptions begin to phase out once AGI exceeds $266,700 (single), $293,350 (HOH), $320,000 (MFJ), or $160,000 (MFS).

**Note:** These same AGI thresholds apply in determining if itemized deductions may be limited. The corresponding 2017 threshold amounts were $261,500 (single), $287,650 (HOH), $313,800 (MFJ), or $156,900 (MFS).

**Standard deduction**
These amounts have been adjusted as follows:

<table>
<thead>
<tr>
<th></th>
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<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single</td>
<td>$6,350</td>
<td>$6,500</td>
</tr>
<tr>
<td>HOH</td>
<td>$9,350</td>
<td>$9,550</td>
</tr>
<tr>
<td>MFJ</td>
<td>$12,700</td>
<td>$13,000</td>
</tr>
<tr>
<td>MFS</td>
<td>$6,350</td>
<td>$6,500</td>
</tr>
</tbody>
</table>

**Note:** The 2018 additional standard deduction amount (age 65 or older, or blind) is $1,600 (up from $1,550 in 2017) for single/HOH or $1,300 (up from $1,250 in 2017) for all other filing statuses. Special rules apply if you can be claimed as a dependent by another taxpayer.

**Alternative minimum tax (AMT)**

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2018</th>
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</thead>
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<tr>
<td>Single/Head of Household (HOH)</td>
<td>$54,300</td>
<td>$55,400</td>
</tr>
<tr>
<td>MFJ</td>
<td>$84,500</td>
<td>$86,200</td>
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<tr>
<td>MFS</td>
<td>$42,250</td>
<td>$43,100</td>
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**Exemption phaseout threshold**

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2018</th>
</tr>
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<tbody>
<tr>
<td>Single/Head of Household (HOH)</td>
<td>$120,700</td>
<td>$123,100</td>
</tr>
<tr>
<td>MFJ</td>
<td>$160,900</td>
<td>$164,100</td>
</tr>
<tr>
<td>MFS</td>
<td>$80,450</td>
<td>$82,050</td>
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26% on AMTI* up to this amount, 28% on AMTI above this amount

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2018</th>
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</thead>
<tbody>
<tr>
<td>MFS</td>
<td>$93,900</td>
<td>$95,750</td>
</tr>
<tr>
<td>All others</td>
<td>$187,800</td>
<td>$191,500</td>
</tr>
</tbody>
</table>

*Alternative minimum taxable income
Demographic Dilemma: Is America’s Aging Population Slowing Down the Economy?

It’s no secret that the demographic profile of the United States is growing older at a rapid pace. While the U.S. population is projected to grow just 8% between 2015 and 2025, the number of older Americans ages 70 to 84 will skyrocket 50%.

With roughly 75 million members, baby boomers (born between 1946 and 1964) make up the largest generation in U.S. history. As a group, boomers have longer life expectancies and had fewer children than previous generations.

Now, after dominating the workforce for nearly 40 years, boomers are retiring at a rate of around 1.2 million a year, about three times more than a decade ago.

Though the economy has continued to improve since the Great Recession, gross domestic product (GDP) growth has been weak compared with past recoveries. A number of economists believe that demographic changes may be the primary reason.

Spending shifts

The lower birth rates in recent decades generally mean that fewer young people are joining the workforce, so the consumer spending that fuels economic expansion and job creation could take a hit. When young people earn enough money to strike out on their own, marry, and start families, it typically spurs additional spending — on places to live, furniture and appliances, vehicles, and other products and services that are needed to set up a new household.

On the other hand, when people retire, they typically reduce their spending and focus more on preserving their savings. Moreover, retirees’ spending habits are often different from when they were working. As a group, retirees tend to avoid taking on debt, have more equity built up in their homes, and may be able to downsize or move to places with lower living costs. More spending is devoted to covering health-care costs as people age.

If a larger, older population is spending less and the younger population is too small to drive up consumer spending, weaker overall demand for products and services could restrain GDP growth and inflation over the long term. Less borrowing by consumers and businesses could also put downward pressure on interest rates.

A new normal?

The onslaught of retiring baby boomers has long been expected to threaten the viability of Social Security and Medicare, mainly because both are funded by payroll taxes on current workers. But this may not be the only challenge.

A 2016 working paper by Federal Reserve economists concluded that declining fertility and labor force participation rates, along with increases in life expectancies, accounted for a 1.25 percentage point decline in the natural rate of real interest and real GDP growth since 1980. Furthermore, the same demographic trends are expected to remain a structural impediment to economic growth for years to come.

Put simply, a nation’s potential GDP is a product of the number of workers times the productivity output per worker, and the U.S. workforce is shrinking in relation to the total population.

The labor force participation rate — the percentage of the civilian labor force age 16 and older who are working or actively looking for work — peaked at 67.3% in early 2000, not coincidentally the last time GDP grew by more than 4%. The participation rate has dropped steadily since then; in August 2017, it was 62.9%. This reflects lower birth rates, increased college enrollment, some men in their prime working years dropping out of the labor force, and large numbers of retiring baby boomers.

Many economists acknowledge that U.S. population trends are a force to be reckoned with, but the potential impact is still up for debate. Some argue that labor shortages could drive up wages and spending relatively soon, followed by higher growth, inflation, and interest rates — until automated technologies start replacing larger numbers of costly human workers.

Even if demographic forces continue to restrain growth, it might not spell doom for workforce productivity and the economy. Another baby boom would likely be a catalyst for consumer spending. Family-friendly policies such as paid maternity leave and day-care assistance could provide incentives for women with children to remain in the workforce. It’s also possible that a larger percentage of healthy older workers may delay retirement — a trend that is already developing — and continue to add their experience and expertise to the economy.

1, 3) The Conference Board, February 24, 2017
4-5) Federal Reserve, 2016
6, 8) The Financial Times, October 25, 2016
What can I learn from looking back on my financial situation in 2017?

If your financial plan for 2017 didn’t work out the way you wanted it to, don’t beat yourself up. Instead, ask yourself the following questions to determine what you can learn from reflecting on your financial situation in the last year.

Did you meet your financial goals and expectations for 2017?? Perhaps you started the year with some financial goals in mind. You wanted to establish a budget that you could stick to, or maybe you hoped to build up your emergency savings fund throughout the year. If you fell short of accomplishing these or other goals, think about the reasons why. Were your goals specific? Did you develop a realistic timeframe for when they would be achieved? If not, learn to set attainable and measurable goals for your finances in the new year.

How did your investments perform? A year-end review of your overall portfolio can help you determine whether your asset allocation is balanced and in line with your time horizon and goals. If one type of investment performed well during the year, it could represent a greater percentage of your portfolio than you initially wanted. As a result, you might consider selling some of it and using that money to buy other types of investments to rebalance your portfolio. Keep in mind that selling investments could result in a tax liability. And remember, asset allocation does not guarantee a profit or protect against loss; it is a method to help manage investment risk. All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

Are your retirement savings on track? Did you contribute the amount you wanted in 2017? Or did unexpected financial emergencies force you to borrow or withdraw money from your retirement savings? In that case, you can help your savings recover by contributing the most you can to your employer-sponsored retirement plan and taking advantage of employer matching (if it’s available to you). Contributing to a 401(k) or 403(b) plan can help you save more consistently because your contributions are automatically deducted from your salary, helping you avoid the temptation to skip a month now and then.

At Cannon Financial Institute, Inc., the program materials and instructor presentations are intended to provide program participants with ideas and guidance in the areas of planning, administration, and management. They are intended to stimulate thought and discussion. The materials and the instructor comments do not constitute, and should not be treated as, legal or other professional advice regarding the use of any particular planning technique, audit or compliance measure, policy, procedure or other such application of the information provided, or the tax consequences associated there with. Although every effort has been made to ensure the accuracy of the materials and the comments at the program, Cannon Financial Institute, Inc., and each instructor, individually, do not assume responsibility for any participant’s reliance on the written or oral information disseminated during the program. Each program participant should independently verify all statements made in the materials and comments made at the program before applying them to a particular fact situation. Each participant should independently determine the tax, nontax, and fiduciary liability consequences of using any particular information before recommending that technique to their institution, its management, its board of directors, a client or implementing it on a client’s behalf. The materials and the instructor comments should not be utilized as a substitute for professional service in specific situations. If legal, accounting or other expert assistance is required, the services of such a professional should be sought.

How did you meet your financial goals and expectations for 2017?? Perhaps you started the year with some financial goals in mind. You wanted to establish a budget that you could stick to, or maybe you hoped to build up your emergency savings fund throughout the year. If you did not meet the goals you had set, take a step back and ask yourself the reasons why. If your goals were not specific, reevaluate your expectations for 2018. If you had a less than ideal year financially, think about the steps you will take to improve your financial situation in the new year.

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What financial resolutions should I consider making as I look ahead to 2018?

A new year is right around the corner, bringing with it a fresh start for you and your finances. What will you do this year to help improve your financial situation?

Evaluate your savings goals. The beginning of the year is a great time to examine your overall financial plan. Maybe you want to buy a new vehicle this year or save money toward a Caribbean cruise next year. Perhaps you want to focus less on material items and more on long-term goals, such as your retirement savings. Regardless of what you are setting money aside for, make sure you come up with a realistic savings plan that will help you achieve your goals and avoid the risk of significant loss.

Pay down debt. Whether you owe money on your credit cards or have student loan payments to make, the start of a new year is a good time to develop a strategy to reduce your overall level of debt. Reducing your debt can help create opportunities to contribute toward other goals throughout the year. But unless you can definitely afford it, don’t plan to pay off all your debts in one fell swoop. Set a smaller goal that you’ll be more likely to achieve over the course of the year.

Automate as much as you can. Your plan to pay down debt can be accomplished more easily if you automate your bill paying, saving, and investing. Most banks, credit card issuers, retirement plan providers, and investment companies offer services that make payments automatic — allowing you to worry less about payment dates. The best part is that it might just take a few taps on your smartphone to make these processes automatic.

Think about organizing your financial documents. If your overall financial situation is already in good shape for the new year, consider taking time now to clear out and organize your financial records. Do you have important documents, such as your tax returns or passport, in a safe place? Are you holding on to records that you no longer need? Organizing your financial records now can save you time and frustration later if you need to locate a particular document.

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