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# THE HARBOR ADVISOR

## Retirement Versus Financial Independence: What's The Difference?

Historically we have referred to “no longer being gainfully employed” as retirement and while it has morphed from the ubiquitous gold watch retirement party at the end of a career, it hasn't moved that far. Today workers are likely to have 7-11 jobs in their career and will experience gaps in employment either by design or circumstance. Some suggest that individuals will enter and exit the workplace based on numerous factors. I think this mobility will depend on the availability of insurance coverage not tied to your employer as well as a good understanding of the amount of your capital and what it can provide you. Why not redefine the work year's continuum to include a broader, more conceptual view of your capital and its uses?

We prefer the concept of financial independence which is defined as the ability for one's portfolio assets to provide enough support to pay all expenses. Whether you choose to continue work for pay or not is a separate concept to explore. Financial independence can mean very different things to different people. Some see themselves engaged in an endless stream of golf, travel and leisure time or a return to school while for others it might be more of a switch from a time consuming, high stress job to a long held interest or hobby turned second career. Still others will continue to work without interruption. Defining what financial independence means to you personally is an important first step in planning for it and establishes the parameters for the financial piece of the equation. Once the boundaries are in place, there can be flexibility within them as the redefined standard post work years unfold.

Harbor staff have extensive experience in the identification and exploration of the concept of financial independence. We are engaged in conversations with our clients helping them explore their thoughts and encouraging the creation of a financial independence plan suited to them, their families and loved ones. We are available to assist you in this process.

In this quarter's newsletter we review company benefits, cover password possibilities and explore fees with 'Not All Fees Are Created Equal'. We hope you enjoy the newsletter and welcome your comments.



July 10, 2014

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### Financial Trivia

The first paper money authorized by Congress in the U.S. began in 1861 spurred by the need to finance the Civil War. Each of the first bills was personally signed by one of the clerks at U.S. Treasury.



## Second Quarter 2014 Market Recap

Despite many factors working against upward market movement, stock and bond prices continued their upward trend for the quarter. The Federal Reserve stayed on course by reducing its bond buy back program and pledged to continue to keep rates low in order to help foster further job development and economic improvement. The third Gross Domestic Product estimate for the first quarter of 2014 came in lower than previously estimated at a -2.9% annualized rate. The commentary on this pointed to cold temperatures and increased imports as possible causes of the decline. The overall real estate market took a breather from its fast pace, due to slightly higher mortgage rates, tighter lending standards and low

inventory. Data from China showed a slowing economy, particularly in its real estate market. The European Central Bank continued measures to stimulate economic growth by lowering lending rates below zero. On the positive side, both job and manufacturing growth continued, which pushed markets to historical highs.

The Barclays aggregate index returned 2.08%, the S&P 500 returned 4.69%, the Russell 2000 increased 1.70% and the MSCI EAFE returned 2.95% for the quarter.

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*“Retirement at sixty-five is ridiculous. When I was sixty-five I still had pimples.” – George Burns*

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### Fund Focus: SPDR S&P Regional Banking ETF

The recent addition of the SPDR S&P Regional Banking ETF (KRE) to the model provides exposure to a segment of the financial sector that differs from the broad financial services market, which includes mega banks and credit card companies. KRE consists instead of approximately 80 financial stocks, mostly small to mid cap banks. While we have incorporated broad financials into the model, embedded in several holdings, we have added KRE as a tactical play because of its more focused nature and growth opportunities.

Regional banks are less correlated to the broad market; their performance is more dependent on their local economies. These smaller banks have benefitted from increased loan demand and the refinancing boom, posting solid profits on the spread between rates paid on deposits and the rates earned on loans. The banking industry in general faces uncertainty surrounding regulations, interest rates and credit markets. Regional banks seem to be in a more nimble position to handle these risks. They have very little global exposure (currently 4% for KRE) and operate with less regulation and scrutiny than the big banks.

## Not All Fees Are Created Equal

Consider the plethora of investment vehicles and brokerage firms an investor has to choose from today. There are literally hundreds of ways one can invest in a vehicle that attempts to track the S&P 500. Some of these funds charge front end loads or have high expense ratios, others charge less than .10% per year and have no upfront loads or commissions. Most investor literature these days teaches us to be very skeptical of fees as they erode net returns to investors over the long run, however, this may not be true for all fees in the investment industry.

The results of a study conducted by David Nanigian of the American College may surprise you. He and his researchers ran a statistical model to assess whether the presence of one type of fee, redemption fees, actually boosted annual returns for mutual funds. Redemption fees act as a deterrent to short term traders as the fund imposes a penalty if shareholders sell their shares within a pre-defined period. The redemption fee goes into the general assets of a fund's portfolio to compensate for the additional trading costs. As investors are generally fee sensitive, this has led to a dramatic reduction in short term trading in mutual funds that charge redemption fees. Consequently, the portfolio managers are able to keep the portfolio fully invested and benefit from reduced cash drag, among other benefits. The Nanigian study finds that mutual funds with redemption fees outperform those without one by up to 1.4% per year and the redemption fee on performance regression model was statistically significant at the 1% level.<sup>1</sup> In practice, this may be somewhat irrelevant as short term traders tend to use common stock or ETFs as they are priced intraday, listed on exchanges and have no back end redemption fees.

At Harbor, we avoid short term trading as we believe it is a fool's game to time the market and trading costs as well as unfavorable short term capital gain tax rates drag down returns. We find the results of this study intriguing as we do invest in funds that impose redemption fees. In next quarter's newsletter we will explore another interesting phenomena found in mutual fund returns, namely that the fund returns often differ, sometimes considerably, from investor returns.

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<sup>1</sup> “Mutual Fund Redemption Fees Can Benefit Long-Term Investors” by David Nanigian, Journal of Financial Planning, May 2014

## Wealth Accumulation: Company Benefits, Part One

When thinking of wealth accumulation, company benefits may not jump to mind. However, in March of 2014 the US Department of Labor estimated that company benefits average 31.2% of employee compensation making company benefits an important resource for wealth building. This quarter we will deal with some of the insurance options that may be offered leaving some of the other offerings such as 401ks and cafeteria plans for next quarter. Below are a few possibilities and some suggestions to consider for each.

- **Medical insurance:** Consider extent of coverage (just you or you and your family), your cost versus what percentage the employer pays, type of plan, deductibles, co-pays and total out of pocket limits. If you have a choice within a group of health plans that your company offers, review the details of each and decide which is right for you based on your needs.
- **Life insurance:** This becomes more important as you add family obligations. Check the maximum and no or low cost options available through your employer and then augment with a separate policy for portability.
- **Dental insurance:** Consider whether preventative care is fully paid for as well as what coverage is offered on surgical and orthodontia. Also, look at deductibles, annual and lifetime maximums.
- **Vision/Eye Care insurance:** A benefit that not everyone needs, evaluate the cost of the insurance versus what is covered.
- **Disability insurance:** Important coverage that is often neglected. Depending on cost and your financial position you may want to self-insure for the short term and put your dollars into the long term insurance premiums.

Consider each coverage individually, do some research, consider your lifestyle and needs. Each year take the time to re-evaluate and update your choices based on any life changes or changes in the benefits themselves. Treat your benefits as the portion of your salary that they are and make the most of them.



## Website Passwords & 2-Factor Authentication

A good password is one that's hard to guess, but easy to remember. Many experts suggest making a password longer with three small words and even capitalizing the first letter of each word, saying this is superior to a shorter, random mix of letters and numbers. You can even use a longer phrase from your favorite movie or book and use punctuation, which will enable you to include capital letters, lowercase letters, numbers, and symbols. Other ways to create passwords can include using a code, doubling your password to make it longer, alternating letters and numbers, or using letters and numbers to write a word upside down.

However, experts also suggest using a different password for each site. When registering on websites that ask for your email address, never use the same password that you do for your email account. A password manager can come in very handy for this. The best password managers, such as LastPass and DashLane, offer a feature called two-factor authentication.

Two-factor, or two-step, authentication is a process that requires more than just your password to confirm your identity. It needs both "something you know," like a password, and "something you have," like a cell phone. After entering your password, you may get a code sent to your phone that you must enter in order to access your account. It's similar to entering a PIN number and then getting a retina scan. Passwords alone are very hack-able, and this tightens the security on any account that features it. Enabling this option on any website that features it and transferring all your passwords to a password manager will help protect your online presence and, in turn, protect your personal and financial information.

### Red Rocks

If you think of Red Rocks as just a venue for a show, you need to think again! At 6,450 feet above sea level, Red Rocks Park is a unique transitional zone where the Great Plains meet the Rocky Mountains. The diverse environment allows visitors to see birds, animals and plants of both regions. It is a geological phenomenon – the only naturally occurring acoustically perfect amphitheatre in the world!

Legends such as the Beatles, Jimi Hendrix, Neil Young and various opera stars have played at this open-air amphitheatre. One of the most famous concert videos ever released was filmed at this iconic venue - U2's 1983 "Under the Blood Red Sky" tour. Even occasional non-musical acts have performed here – Steve Martin's famous "A Wild and Crazy Guy". Every artist aspires to play on this magical, spiritual and emotional stage. Early-evening shows are especially beautiful, as the fading rays of a Colorado sunset frame the stage and paint the setting with pastel colors. There is no better place to see the stars!

In addition to the summer music series, Red Rocks offers a variety of recreation options from guided tours, hiking, biking, movie nights, yoga, and fitness challenges. It also has a visitor center that houses a full service restaurant, interactive displays, Performers Hall of Fame and a unique event space for weddings and meetings.

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Images: David Lat

## Harbor Happenings

### **Welcome Hank!**

Please join us in welcoming Hank Hammond as our new wealth management intern. He is pursuing a Bachelor's degree in Finance from the Leeds School of Business at the University of Colorado, Boulder and plans to graduate in May 2016.

### **Puttin' on the Leash**

Once again, Harbor co-sponsored the Humane Society of Boulder Valley's Puttin' on the Leash Gala. It was a fun evening and benefited a wonderful cause. This annual fundraiser raises money for the Humane Society of Boulder Valley and benefits the animals in their care, increases awareness of their mission and is a whole lot of fun.

### **Save the Date**

Harbor's Client Appreciation event will be Thursday, August 28. Watch your email and mail boxes for details.

## 2014 Closures

Our office is closed on the following New York Stock Exchange holidays in 2014: Monday, Sept. 1; Thursday, Nov. 27; Friday, Nov. 28 is a half day closure; Wednesday, Dec. 24 is a half day closure; Thursday, Dec. 25.

*The majority of our growth over the past 26 years has come from referrals from clients and other professionals. We thank those of you who have referred your friends and colleagues. If you know of anyone who might be interested in our services, please ask them to give us a call at 303-939-8788.*