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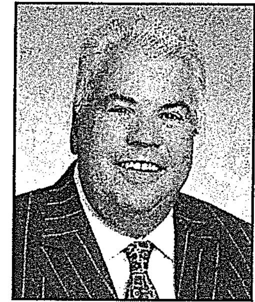

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Reclassifying Real Estate

PAGE 2 INSIDE

Publicly traded REITs and other listed real estate companies are being moved to a distinct Real Estate sector by S&P Dow Jones Indices and MSCI. The change could affect asset allocation decisions and draw attention to equity REITs as income-generating equities.

Facing Higher-Ed Inflation

Adjusted for inflation, published tuition and fees for public four-year colleges were 3.22 times higher for the 2015–16 school year than they were for 1985–86. Costs for private nonprofit colleges were 2.39 times higher.

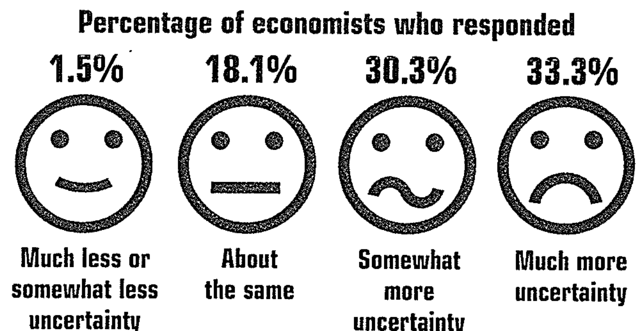
Source: College Board, 2016

Is the U.S. Election Adding to Economic Anxiety?

About one-third of the economists who participated in a March 2016 *Wall Street Journal* survey thought the current election was having somewhat negative effects on the U.S. economy, primarily by diminishing the confidence of consumers and investors.

Is the current election introducing more or less uncertainty into markets and the economy compared with other recent elections?

Percentage of economists who responded



Source: *The Wall Street Journal*, March 10, 2016

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Reclassifying Real Estate

New Sector Puts Equity REITs in the Spotlight

S&P Dow Jones Indices and MSCI are moving publicly traded real estate investment trusts (REITs) and other listed real estate companies from the Financials sector to a distinct Real Estate sector. In September 2016, there will be 11 headline sectors instead of 10; this is the first time a new sector has been added to the Global Industry Classification Standard (GICS) since it was created in 1999.[1]

The GICS is often used as a framework for portfolio construction. By some estimates, fund managers could shift as much as $100 billion to the Real Estate sector in a collective effort to follow the market weightings of various indexes.[2]

By drawing more attention to equity REITs as income-generating assets with the potential for capital appreciation, the change might also affect the asset allocation decisions of some individual investors.

Fixed-Income Appeal

A REIT is a company that uses the combined capital of a large number of investors to buy and manage income properties such as apartments, shopping centers, hotels, offices, and other types of residential, commercial, and industrial buildings. Publicly traded REIT shares can generally be bought or sold on an exchange at a moment's notice, making them more liquid than physical real estate investments, which involve transactions that can take months to complete.

Many REITs generate a reliable income stream regardless of share price performance, primarily because they are required by law to pay out 90% of their taxable incomes as dividends to stakeholders. In the first quarter of 2016, the S&P REIT index had a dividend yield of 3.9%.[3] *The performance of an unmanaged index is not indicative of the performance of any specific security. Individuals cannot invest directly in an index.*

REIT share prices can be sensitive to interest rates. As rates rise, steady dividends may appear less attractive to investors relative to the safety of bonds offering similar yields. On the other hand, current fundamentals, including modest economic growth, lower unemployment, and rising rents, are generally seen as positive conditions for REITs and other real estate businesses.

Diversification Tool

Breaking real estate out of the Financials sector acknowledges that the industry's business models and ties to underlying property markets produce a distinctive risk-return profile, including a relatively low correlation to the rest of the stock market.[4] Because the share prices of equity REITs don't rise and fall in lockstep with the broader stock market, including them in your portfolio could help reduce the overall level of risk.

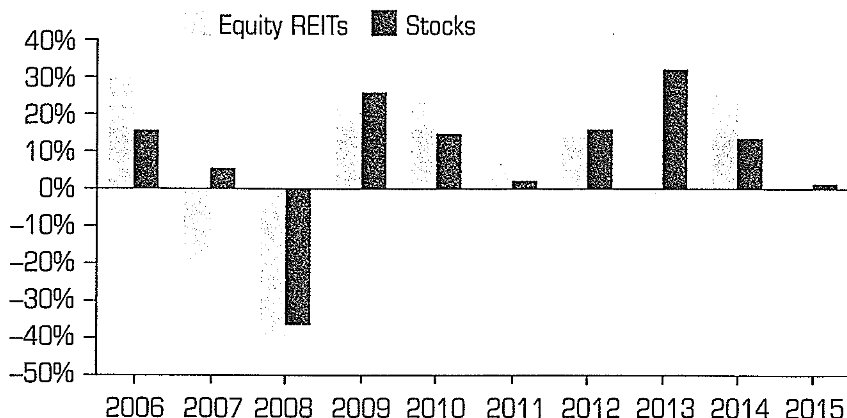
The return and principal value of all stocks, including REITs, fluctuate with changes in market conditions. Shares, when sold, may be worth more or less than their original cost. Diversification and asset allocation do not guarantee a profit or protect against investment loss; they are methods used to help manage investment risk.

REIT distributions are taxable to the extent they include any ordinary income and capital gains. Some REITs may not qualify as a REIT as defined in the tax code, which could affect operations and negatively impact the ability to make distributions.

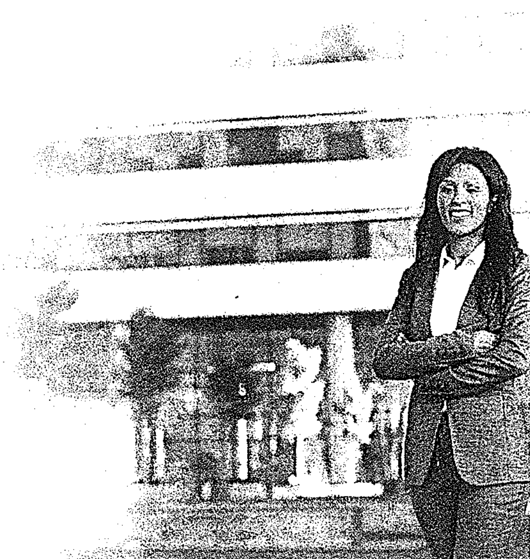
There are inherent risks associated with real estate investments that could have an adverse effect on financial performance. Such risks may include a deterioration in the economy or local real estate conditions; tenant defaults; property mismanagement; and changes in operating expenses (including insurance costs, energy prices, real estate taxes, and the cost of compliance with laws, regulations, and government policies).

1, 3) S&P Dow Jones Indices, 2015–2016
2) *Investor's Business Daily*, March 18, 2016
4) FinancialAdvisor.com, March 1, 2016

U.S. Equity REITs vs. U.S. Stocks: Annual Returns



Source: National Association of Real Estate Investment Trusts, 2016. REITs are represented by the FTSE NAREIT US Real Estate Index, Equity REITs. U.S. stocks are represented by the S&P 500 Composite Index Total Return. The performance of an unmanaged index is not indicative of the performance of any specific security. Individuals cannot invest directly in an index. Past performance is not a guarantee of future results. Actual results will vary.



Focused on College Funding

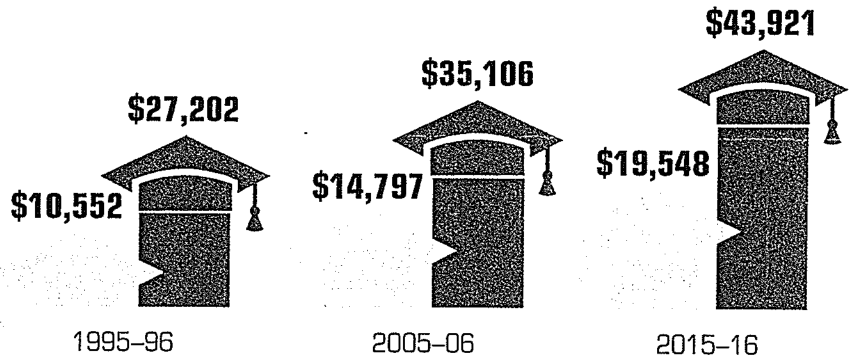
529 Plans Offer Flexibility for Families

In 2015, nearly 75% of college freshmen said cost was an important factor in selecting a school, while more than 20% said they turned down their first choice because they could not afford to attend.[1]

If one of your financial priorities is helping your family cover escalating college costs, you may want to take advantage of a Section 529 savings plan. Planning ahead and setting aside money over time could help expand your student's options when the time comes to make life-changing college decisions.

Climbing Costs

Average published tuition and fees, plus room and board



Source: College Board, 2015

Investing in Knowledge

The funds invested in 529 accounts grow tax deferred, and withdrawals are tax-free when used to pay qualified higher-education expenses, including tuition, fees, room and board, books, and supplies. Congress recently added computers, printers, other peripherals, education-related software, and even Internet access to the list of qualified expenses for tax year 2015 and beyond.

Many 529 plans include age-based investment options that tend to become more conservative as the child approaches college age. Owners of 529 accounts are allowed to change the investment options for their existing plan contributions twice per calendar year.

A Family Effort

Most states offer their own 529 plans, which may provide advantages and benefits exclusively for their residents and taxpayers. There are no income restrictions for participation, so anyone who wants to provide financial support can contribute to a 529 plan opened on a student's behalf. However, the 529 plan will not accept contributions after the beneficiary's account balances reach a fairly high limit that varies by state.

You can contribute up to the normal annual gift tax exclusion ($14,000 in 2016) per student without triggering gift taxes. As an alternative, you could contribute five times the normal amount ($70,000) in a single year, as long as you don't contribute any additional money for the next four years. Contributing to 529 plans also removes the assets from your taxable estate.

Grandparents who want to maintain control of 529 plan funds could open their own accounts for one or more grandchildren. There is no time limit on when the funds in a 529 plan must be used, and 529 plan assets can be transferred to another beneficiary in the same family (sibling, cousin, spouse, or even parent), if needed.

Families who expect to qualify for financial aid should be aware that 529 plan assets owned by grandparents are not considered in financial need calculations, unlike 529 accounts owned by students and parents. However, withdrawals from 529 plans owned by anyone other than the student or a parent count as student income for financial aid purposes and could have an impact on award money in later years.

When 529 plan withdrawals are not used for qualified higher-education expenses, earnings may be subject to ordinary federal and state income taxes and a 10% federal income tax penalty. The tax implications of a 529 plan should be discussed with your tax advisor because they can vary significantly from state to state.

As with other investments, there are generally fees and expenses associated with participation in a 529 plan. There is also the risk that the investments may lose money or not perform well enough to cover college costs as anticipated.

Before investing in a 529 savings plan, please consider the investment objectives, risks, charges, and expenses carefully. The official disclosure statements and applicable prospectuses — which contain this and other information about the investment options, underlying investments, and investment company — can be obtained from your financial professional. You should read these materials carefully before investing.

1) Higher Education Research Institute, UCLA, 2015

Enticing the Crowd: New Rules for Raising Capital Online

Equity crowdfunding platforms raised approximately $1.2 billion for U.S. start-ups in 2015, mainly from accredited investors — generally wealthy and sophisticated investors who meet certain criteria established by the Securities and Exchange Commission (SEC). That figure is expected to grow by 75% to 100% in 2016, with new SEC rules that allow the participation of non-accredited investors under specific conditions.[1]

How Crowdfunding Works

Crowdfunding is a nontraditional way to raise the money needed to launch or expand a small business. Instead of seeking a large cash infusion from an "angel investor" or venture capital firm, you could offer shares via an online funding platform to a larger group of people, each of whom takes a smaller stake in the company.

A funding portal could be used to explain your plans and attract investors, many of whom might be family members, friends, and customers in your own community. When equity is offered, your investors have a powerful incentive to promote your business among their own social networks.

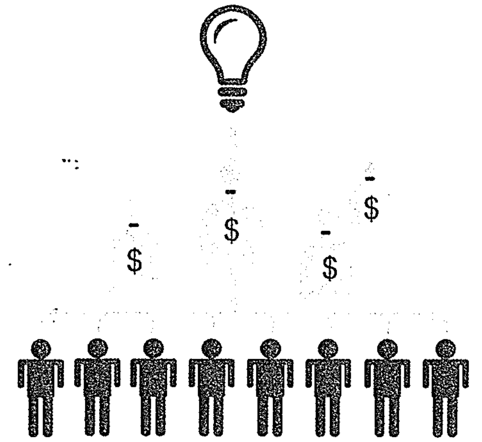
Most small investors (incomes or net worth under $100,000) will be able to invest a maximum of $2,000. Individuals with annual incomes or net worth of $100,000 or more can invest 10% of annual income, not to exceed $100,000 per year. Securities generally cannot be resold for at least one year.

New Rules in Play

A private company is generally allowed to raise a total of $1 million over a 12-month period through crowdfunding, presumably at a lower cost and with fewer regulatory requirements than a public offering.

Even so, crowdfunding companies must provide a long list of specific disclosures to the SEC, potential investors, and the intermediary that facilitates the transactions. Examples include the target offering amount, the fundraising deadline, descriptions of the business and its owners, the pricing of securities, and how the crowdfunding proceeds will be used. Financial statements may need to be accompanied by company tax returns and independently reviewed or audited.

Before making any investment commitment, investors must attest that they have reviewed the intermediary's educational materials, understand that the entire amount of the investment may be lost, and are in a financial condition to bear the loss. Investors must also complete a questionnaire demonstrating an understanding of the risks of any potential investment and other required statutory elements.



Equity crowdfunding is just one way businesses can obtain financial backing from the "crowd." Other ways include loans (peer-to-peer financing), rewards-based crowdfunding, and outright donations.

1) crowdexpert.com, 2016

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