

**Volatility is Not
Risk***The two should not be confused*

What is risk? To the conservative investor, risk is a negative. To the opportunistic investor, risk is a factor to tolerate and accept. Whatever the perception of risk, it should not be confused with volatility. That confusion occurs much too frequently.

Volatility can be considered a measurement of risk, but it is not risk itself. Many investors and academics measure investment risk in terms of beta; that is, in terms of an investment's ups and downs in relation to a market sector or the entirety of the market. . . If you want to measure volatility from a very wide angle, you can examine standard deviation for the S&P 500. The total return of this broad benchmark averaged 10.1% during 1926-2015, and there was a standard deviation of 20.1 from that average total return during those 90 market years.¹ What does that mean? It means that if you add or subtract 20.1 from 10.1, you get the range of total return that could be expected from the S&P two-thirds of the time during the period from 1926-2015. That is quite a variance, indicating that investors should be ready for anything when investing in equities. During 1926-2015, there was a 67% chance that the S&P could return anywhere from a 30.2% yearly gain to a 10.1% yearly loss.

**Robo-Advisors vs Human Advisors**

Investors have a choice today that they did not have a decade ago. They can seek investing and retirement planning guidance from a human financial advisor or put their invested assets in the hands of a robo-advisor – a software program that maintains their portfolio.

Why would an investor want to leave all that decision making up to a computer? In this era of cybercrime and “flash crashes” on Wall Street, doesn't that seem a little chancy? No, not to the financial firms touting robo-advisors. They are wooing millennials, in particular. Some robo-advisor accounts offer very low minimums and fees, and younger investors who want to “set it and forget it” or have their asset allocations gradually adjusted with time represent the prime market. In the 12 months between July 2014 and July 2015 alone, invested assets under management by robo-advisors more than doubled.¹ Even so, only 5% of investors responding to a recent Wells Fargo/Gallup survey said they had used a robo-advisor, and fewer than half those polled even knew what a robo-advisor was.²

A cost-conscious investor may ask, “What's so bad about using a robo-advisor?” After all, taxpayers and tax preparers use tax prep software to fill out 1040 forms each year, and that seems to work well. Why shouldn't investors rely on investment software?

The problem is the lack of a human element. Investors at all stages of life appreciate when a financial professional takes time to understand them, to know their goals and their story. A software program cannot gain that understanding, even with input from a questionnaire.

The closer you get to retirement age, the less appealing a robo-advisor becomes. The software they use can't yet perform retirement planning – and after 50, people have financial concerns far beyond investment yields. Investment management does not equal retirement planning, estate planning, or risk management.² **Additionally, robo-advisors have never faced a bear market.** They first appeared in 2010. Passive investment management is one of their hallmarks. How adroitly will their algorithms respond and rebalance a portfolio when the bears come out? That has yet to be seen.²

Does a robo-advisor have a fiduciary duty? Many investment and retirement planning professionals assume a fiduciary role for their clients. They have an ethical and legal duty to provide advice that is in the client's best interest. How many robo-advisors have developed the discernment to do this?³

The robo-advisor “revolution” may be fleeting. Why, exactly? The whole robo-advisor business model may

invite the demise of many of these firms. Robo-advisors pride themselves on low account fees, but as CNBC reports, those fees are now so minimal that many robo-advisors are having a hard time making back their client acquisition costs. Ultimately, robo-advisors may be remembered for the way they stimulated the financial services giants to offer low-minimum, low-cost investment tools.⁴ In fact, hybrid platforms have also emerged. Some robos now offer investors the chance to talk to a real, live financial advisor as well as actual financial planning services when an account balance surpasses a certain threshold. At the same time, some of the major brokerages have introduced robo-advisor investment platforms with potential human interaction to compete with the upstart investment firms that challenged their old-school approach.⁵ It appears the traditional approach of working with a human financial advisor may be hard to disrupt. The opportunity to draw on experience, to have a conversation with a professional who has seen his or her clients go through the whole arc of retirement, is so essential.

Some investors will never talk to a financial advisor in their lives. Just why is that? TIAA (formerly TIAA-CREF) surveyed 2,000 adults online and found some answers. Of those who hadn't consulted financial advisors: 55% feared it would be too expensive, and 49% said it was “hard to know which sources or whom I can trust.” Forty percent were unsure of what questions to ask a financial professional, and 38% said that it would be awkward discussing their finances with someone else.¹ These responses point to uncertainty about the process of financial and retirement planning. The process is really quite worthwhile, quite illuminating, and quite helpful. It is not just about planning to improve “the numbers,” it is also about planning ways to sustain and improve your quality of life.

— Barbie

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Robo-Advisors vs.

Human Advisors **P.1**Your 2018 Financial To-Do List **P.2-3**In-Office Workshops **P.4**

1 - tinyurl.com/hso3ahk [2/28/16]

2 - time.com/money/4616753/robo-advisor-online-financial-planning-advice/ [1/18/17]

3 - investopedia.com/terms/f/fiduciary.asp [2/21/17]

4 - cnbc.com/2016/06/14/is-the-twilight-of-the-robo-advisor-already-at-hand.html [6/14/16]

5 - forbes.com/sites/katherynthayer/2017/02/15/why-betterment-added-a-human-touch-to-its-roboadvisor-tool/ [2/15/17]

(Again, this is total return with dividends included.)¹ Just recently, there were years in which the S&P's total return fell outside of that wide range. In 2013, the index's total return was +32.39%. In 2008, its total return was -37.00%.² When statisticians measure the volatility of major indices like the S&P 500, Nasdaq Composite, or Dow Jones Industrial Average, they are measuring market risk. Trying to measure investment risk is another matter.

You can argue that investment risk is not measurable. How can investors measure the probability of a loss when they invest? Even after they sell an investment, can they go back and calculate what their risk was at the time they bought it? They only know if they made money or not. Profit or loss says nothing about risk exposure.

Most experienced investors do not fear volatility. Instead, they fear loss. They think of "risk" as their potential for unrecoverable loss. In reality, most apparent "losses" may be recoverable given enough time. True unrecoverable losses occur in one of two ways. One, an investor sells the investment for less than what he or she paid for it. Two, some kind of irrevocable change happens, either to the investment itself or to the sector to which the investment belongs. For example, a company goes totally out of business and leaves investors with worthless securities. Or, an innovation transforms an industry so profoundly that it renders what was once a leading-edge company an afterthought.

Accepting risk means accepting the possibilities of equity investing. The range of possibilities for investment performance and market performance is vast. History has shown that to be true, history being all we have to look at. It fails to tell us anything about the negative (or positive) disruptions that could come out of nowhere to upend our



What financial, business, or life priorities do you need to address for 2018? Now is a good time to think about the investing, saving, or budgeting methods you could employ toward specific objectives, from building your retirement fund to lowering your taxes. You have plenty of options. Here are a few that might prove convenient:

Can you contribute more to your retirement plans this year? In 2018, the contribution limit for a Roth or traditional IRA remains at \$5,500 (\$6,500 for those making "catch-up" contributions). Your modified adjusted gross income (MAGI) may affect how much you can put into a Roth IRA: singles and heads of household with MAGI above \$135,000 and joint filers with MAGI above \$199,000 cannot make 2018 Roth contributions.¹ For tax year 2018, you can contribute up to \$18,500 to any kind of 401(k), 403(b), or 457 plan, with a \$6,000 catch-up contribution allowed if you are age 50 or older. If you are self-employed, you may want to look into whether you can establish and fund a Solo 401(k) before the end of 2018; as employer contributions may also be made to Solo 401(k)s, you may direct up to \$55,000 into one of those plans.^{1,2}

Your retirement plan contribution could help your tax picture. If you won't turn 70½ this year and you participate in a traditional qualified retirement plan or have a traditional IRA, you can cut your 2018 taxable income through a contribution. Should you be in the 35% federal tax bracket, you can save \$1,925 in taxes as a byproduct of a \$5,500 regular IRA contribution.³

What are the income limits on deducting traditional IRA contributions? If you participate in a workplace retirement plan, the 2018 MAGI phase-out ranges are \$63,000-\$73,000 for singles and heads of households, \$101,000-\$121,000 for joint filers when the spouse making IRA contributions is covered by a workplace retirement plan, and \$189,000-\$199,000 for an IRA contributor not covered by a workplace retirement plan, but married to someone who is.²

Roth IRAs and Roth 401(k)s, 403(b)s, and 457 plans are funded with after-tax dollars, so you may not take an immediate federal tax deduction for your contributions to these plans. The upside is that if you follow I.R.S. rules, the account assets may eventually be withdrawn tax free.⁴ Your tax year 2018 contribution to a Roth or traditional IRA may be made as late as the 2019 federal tax deadline – and, for that matter, you can make a 2017 IRA contribution as late as April 17, 2018, which is the deadline for filing your 2017 federal return. There is no merit in waiting until April of the successive year, however, since delaying a contribution only delays tax-advantaged potential compounding of those dollars.⁴

Should you go Roth in 2018? You might be considering that if you only have a traditional IRA. This is no snap decision; the tax impact of the conversion must be weighed versus the potential future benefits. If you are a high earner, you should know that income phase-out limits may affect your chance to make Roth IRA contributions. For 2018, phase-outs kick in at \$189,000 for joint filers and \$120,000 for single filers and heads of household. Should your income prevent you from contributing to a Roth IRA at all, you still have the chance to contribute to a traditional IRA in 2018 and then go Roth.¹

Incidentally, a footnote: distributions from Roth IRAs, traditional IRAs, and qualified retirement plans, such as 401(k)s, are not subject to the 3.8% Medicare surtax affecting single/joint filers with AGIs over \$200,000/\$250,000. If your AGI surpasses these MAGI thresholds, then dividends, royalties, the taxable part of non-qualified annuity income, taxable interest, passive income (such as partnership and rental income), and net capital gains from the sale of real estate and investments are subject to that surtax.⁵ Consult a tax or financial professional before you make any IRA moves to see how those changes may affect your overall financial picture. If you have a large traditional IRA, the projected tax resulting from a Roth conversion may make you think twice.

What else should you consider in 2018?

Your 2018 Financial To-Do List

Things you can do for your future as the year unfolds.

Make a charitable gift. You can claim the deduction on your 2018 return, provided you itemize your deductions with Schedule A. The paper trail is important here.⁶

If you give cash, you need to document it. Even small contributions need to be demonstrated by a bank record or a written communication from the charity with the date and amount. Incidentally, the I.R.S. does not equate a pledge with a donation. Contributions to individuals are never tax deductible.⁶

What if you gift appreciated securities? If you have owned them for more than a year, you will be in line to take a deduction for 100% of their fair market value, and avoid capital gains tax that would have resulted from simply selling the investment and donating the proceeds. The non-profit organization gets the full amount of the gift, and you can claim a deduction of up to 30% of your adjusted gross income.⁷

Does the value of your gift exceed \$250? It may, and if you gift that amount or larger to a qualified charitable organization, the I.R.S. says you need to keep "a contemporaneous written acknowledgement" from the charity "indicating the amount of cash and a description of any property contributed." You must also file Form 8283 when your total deduction for non-cash contributions or property exceeds \$500 in a year.⁶

If you aren't sure if an organization is eligible to receive charitable gifts, check it out at irs.gov/Charities-&-Non-Profits/Exempt-Organizations-Select-Check.

See if you can take a home office deduction. If your income is high and you find yourself in one of the upper tax brackets, look into this. You may be able to legitimately write off expenses linked to the portion of your home exclusively used to conduct your business. (The percentage of costs you may deduct depends on the percentage of your residence you devote to your business activities.) If you qualify, part of your rent, insurance, utilities, and repairs may be deductible.⁸

- 1 - cbsnews.com/news/I.R.S.-allows-higher-retirement-savings-account-limits-in-2018/ [10/24/17]
- 2 - forbes.com/sites/ashleaebeling/2017/10/19/I.R.S.-announces-2018-retirement-plan-contribution-limits-for-401ks-and-more/ [10/19/17]
- 3 - turbotax.intuit.com/tax-tips/tax-planning-and-checklists/4-last-minute-ways-to-reduce-your-taxes/L3eJ81kRC [11/9/17]
- 4 - irs.gov/Retirement-Plans/Traditional-and-Roth-IRAs [10/25/17]
- 5 - bbt.com/wealth/retirement-and-planning/retirement/medicare-surtaxes.page [11/9/17]
- 6 - irs.gov/taxtopics/tc506 [9/21/17]
- 7 - tinyurl.com/yc6ecpq8 [10/12/17]
- 8 - irs.gov/businesses/small-businesses-self-employed/home-office-deduction [10/26/17]
- 9 - fool.com/retirement/2017/04/29/whats-my-required-minimum-distribution-for-2017.aspx [4/29/17]
- 10 - smartasset.com/retirement/is-social-security-income-taxable [7/19/17]

Open an HSA. If you are enrolled in a high-deductible health plan, you may set up and fund a Health Savings Account in 2018. You can make fully tax-deductible HSA contributions of up to \$3,450 (singles) or \$6,900 (families); catch-up contributions of up to \$1,000 are permitted for those 55 or older. HSA assets grow tax deferred, and withdrawals from these accounts are tax free if used to pay for qualified health care expenses.¹

Practice tax-loss harvesting. By selling underperforming stocks in your portfolio, you could record at least \$3,000 in capital losses. In fact, you may use this tactic to offset all of your total capital gains for a given tax year. Losses that exceed the \$3,000 yearly limit may be rolled over into 2019 (and future tax years) to offset ordinary income or capital gains again.³

Pay attention to asset location. Tax-efficient asset location is an ignored fundamental of investing. Broadly speaking, your least tax-efficient securities should go in pre-tax accounts, and your most tax-efficient securities should be held in taxable accounts.

Review your withholding status. Should it be adjusted due to any of the following factors?

- * You tend to pay a great deal of income tax each year.
- * You tend to get a big federal tax refund each year.
- * You recently married or divorced.
- * A family member recently passed away.
- * You have a new job, and you are earning much more than you previously did.
- * You started a business venture or became self-employed.

Are you marrying in 2018? If so, why not review the beneficiaries of your workplace retirement plan account, your IRA, and other assets? In light of your marriage, you may want to make changes to the relevant beneficiary forms. The same goes for your insurance coverage. If you will have a new last name in 2018, you will need a new Social Security card. Additionally, the two of you, no doubt, have individual retirement saving and investment strategies. Will they need to be revised or adjusted once you are married?

Are you coming home from active duty? If so, go ahead and check the status of your credit and the state of any tax and legal proceedings that might have been preempted by your orders. Make sure any employee health insurance is still there, and revoke any power of attorney you may have granted to another person.

Consider the tax impact of any upcoming transactions. Are you planning to sell (or buy) real estate next year? How about a business? Do you think you might exercise a stock option in the coming months? Might any large commissions or bonuses come your way in 2018? Do you anticipate selling an investment that is held outside of a tax-deferred account? Any of these actions might significantly impact your 2018 taxes.

If you are retired and older than 70½, remember your year-end RMD. Retirees over age 70½ must begin taking Required Minimum Distributions from traditional IRAs and 401(k), 403(b), and profit-sharing plans by December 31 of each year. The I.R.S. penalty for failing to take an RMD equals 50%

of the RMD amount that is not withdrawn.⁹ If you turned 70½ in 2017, you can postpone your initial RMD from an account until April 1, 2018. The downside of this is that you will have to take two RMDs in 2018, with both RMDs being taxable events – you will have to make your 2017 tax year RMD by April 1, 2018 and your 2018 tax year RMD by December 31, 2018.⁹ *Plan your RMD wisely.* If you do so, you may end up limiting or avoiding possible taxes on your Social Security income. Some Social Security recipients don't know about the "provisional income" rule – if your adjusted gross income, plus any non-taxable interest income you earn, plus 50% of your Social Security benefits surpasses a certain level, then some Social Security benefits become taxable. Social Security benefits start to be taxed at provisional income levels of \$32,000 for joint filers and \$25,000 for single filers.¹⁰

Lastly, should you make 13 mortgage payments in 2018? If your house is underwater, this makes no sense, and you could argue that those dollars might be better off invested or put in your emergency fund. Those factors aside, however, there may be some merit to making a January 2019 mortgage payment in December 2018. If you have a fixed-rate loan, a lump-sum payment can reduce the principal and the total interest paid on it by that much more. Talk with a qualified financial or tax professional today. Vow to focus on being healthy and wealthy in 2018.

— Jim and Mico



assumptions. A "black swan" (terrorism, a virus, an environmental crisis, a quick evaporation of investor confidence) is always a possibility. Next year, the performance of this or that sector or the small caps or blue chips could be spectacular. It could also be dismal. It could certainly fall in between those extremes. There is no way to calculate it or estimate it in advance. For the equities investor, the future is always a flashing question mark, regardless of what history tells or pundits predict.

Diversification helps investors cope with volatility & risk. Spreading assets across various investment classes may reduce a portfolio's concentration in a hot sector, but it also lessens the possibility of a portfolio being over weighted in a cold one. Volatility is a statistical expression of market risk, constantly measured. Volatility, however, should not be confused with risk itself.

— Shawn



Fun Facts About \$1 Bill

- * Thirteen is an important number - there are 13 arrows in the eagle's left talon, 13 stripes on the Great Seal, 13 stars and 13 steps on the pyramid.
- * Arrows in eagle's left talon represent war while the olive branch in the right talon represents peace
- * As long as you have three-quarters of a bill you can exchange it for the whole bill
- * Salmon Chase was first to appear on the dollar bill
- * Circulates for 5.8 yrs & represents 45% of bill production
- * There were 11.7 billion \$1 bills in circulation in 2016
- * Has the oldest design of any bill in circulation since 1963
- * Cheapest note to produce, at 4.9 cents per note
- * Track your \$1 bill at www.wheresgeorge.com
- * Not made of paper, rather 75% cotton and 25% linen
- * MDCCLXXVI at the bottom of the pyramid is the symbol for 1776, when the Declaration of Independence was signed.

- 1 - c.standardandpoors.com/sites/client/generic/axa/axa4/Article.vm?top-ic=5991&siteContent=8088 [3/31/16]
- 2 - ycharts.com/indicators/sandp_500_total_return_annual [3/31/16]

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2018 LPL Outlook

*Featuring: LPL Senior
Analyst, Colin Allen*

February TBD

6:30—7:30 PM



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