



Money Matters

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Making Lemonade Out of Lemons

Over the last year we have been handed trillions of lemons! We can make predictions and strategize all day and night regarding our plans. However, the way I see it, if you are on your career path of life the best way to make a sweet jug of lemonade is by **dollar cost averaging**.

Many investors are afraid their lemons are rotting. Remember, fortunes are not made during bull markets. Wealth is created during tough times in which difficult choices can hinder your efforts or make you stronger.

Brett Arends with the Wall Street Journal reviewed data from the Great Depression to see how dollar cost averaging might have helped during the worst crash in history. He also believes, "When you choose to dollar cost average you are giving up any attempt to time or catch the absolute bottom of the market" and "legions have been lost" trying to do so.

During the most severe period of the crash from 1929-1932, an ill-fated investor began dollar cost averaging \$100 per month at the highest point in the market (September 3, 1929) and lost about 66% of his money. As horrible as that sounds, here's a better way to frame the situation according to Arends:

1. The complete peak to trough collapse was 89%

An 89% loss is only applicable to an investor who didn't have any additional investment during the market decline – unlike the investor who made regular contributions. By dollar cost averaging, continuous infusions are made at lower costs essentially protecting the total investment. The example below shows that dollar cost averaging shelters this investor's losses to only -26% compared to -41% with no additional investments:

Dollar-Cost Averaging

Month	Return	Invested	Total Invested	Value	Total Loss \$	Total Loss %
1	-10%	\$100	\$100	\$90	-\$10	-10%
2	-10%	\$100	\$200	\$171	-\$29	-15%
3	-10%	\$100	\$300	\$244	-\$56	-19%
4	-10%	\$100	\$400	\$310	-\$90	-23%
5	-10%	\$100	\$500	\$369	-\$131	-26%

No Additional Investments

Month	Return	Invested	Total Invested	Value	Total Loss \$	Total Loss %
1	-10%	\$500	\$500	\$450	-\$50	-10%
2	-10%	\$ -	\$500	\$405	-\$95	-19%
3	-10%	\$ -	\$500	\$365	-\$136	-27%
4	-10%	\$ -	\$500	\$328	-\$172	-34%
5	-10%	\$ -	\$500	\$295	-\$205	-41%

This concept on paper seems very easy to do, but in reality, as we are seeing today, it is very challenging and can test an investor's commitment to strategy and discipline.

2. After taking into account extreme deflation, the actual real dollar return was softened

The profound level of deflation during the Great Depression helped cause the collapse. Instead of inflation, where a dollar declines in value, deflation causes the value to increase. So looking at a real return basis after deflation, the loss wasn't as depressing because the purchasing power of a dollar was more.

3. Establish foundation for rapid recovery

Once the market bottoms and continues an upward path, an investor who has dollar cost averaged through the downturn will recover faster. Using the previous scenario, we will assume the market recovers after the fifth month and the investor stopped investing money. By month ten, the investor who dollar cost averaged will have a +19% return! Whereas if no additional investments were made the portfolio would still be in the red at -5%.



Dollar-Cost Averaging

Month	Return	Invested	Total Invested	Value	Total Loss \$	Total Loss %
5	-10%	\$ 100	\$ 500	\$ 369	-\$131	-26%
6	10%	\$ -	\$ 500	\$ 405	-\$95	-19%
7	10%	\$ -	\$ 500	\$ 446	-\$54	-11%
8	10%	\$ -	\$ 500	\$ 491	-\$9	-2%
9	10%	\$ -	\$ 500	\$ 540	\$40	8%
10	10%	\$ -	\$ 500	\$ 594	\$94	19%

No Additional Investments

Month	Return	Invested	Total Invested	Value	Total Loss \$	Total Loss %
5	-10%	\$ -	\$ 500	\$ 295	-\$205	-41%
6	10%	\$ -	\$ 500	\$ 325	-\$175	-35%
7	10%	\$ -	\$ 500	\$ 357	-\$143	-29%
8	10%	\$ -	\$ 500	\$ 393	-\$107	-21%
9	10%	\$ -	\$ 500	\$ 432	-\$68	-14%
10	10%	\$ -	\$ 500	\$ 476	-\$25	-5%

Although the market took 22 years to break even during the Great Depression, someone who regularly invested through the most miserable years was on solid ground by 1933 – and by 1936, would have doubled his money! Although the slide in 1938 would have set him back for a while, overall, he would have to lose 50% *before* any losses would eat into his original investments – that's risk protection!

Operational News

2009 Required Minimum Distributions Waived

Last December's passage of The Worker, Retiree, and Employer Recovery Act, granted a temporary waiver of the required minimum distribution (RMD) from retirement accounts for the 2009 tax year. This waiver applies to IRAs, employer-sponsored retirement plans (i.e. 401(k), 403(b), and QRPs), as well as Inherited IRA accounts!



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Take a Guess:



1. What is the number of S&P 500 stocks that made money in 2008?
2. How many pages are in the Emergency Economic Stabilization Act of 2008 based on Paulson's proposal?
3. Price of crude oil in July 2008 was \$147.27 per barrel, in July 2002 it was \$17.84 per barrel. What was the price in December 2008?
4. What was the estimated dollar loss in home values by the end of 2008?
5. What is China's rank among the biggest holders of U.S. debt?
6. What is the percentage increase in tuition and fees at four-year public universities for the 2008-2009 school year?

Answers: 1) 31; 2) 451; 3) \$33.87; 4) \$2 trillion; 5) #1; 6) 6.4% *Source- Journal of Financial Planning, 2009