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MARCH 2003

Should You Invest Globally?

For much of the 1990s, the U.S. stock market significantly outperformed international stock markets. Never a particularly large percentage of U.S. investment portfolios, international investments drew even less attention during this time. But the U.S. stock market has just experienced the third consecutive year of negative returns, with many expecting U.S. stocks to encounter below-average returns in the future. Is now the time to take another look at international investments? Before deciding, consider the following:

Return potential. During the 1990s, the U.S. stock market clearly outperformed international stocks. But that was not always the case — international markets outperformed U.S. stocks during the 1980s. A study of 10-year annualized returns for the Standard & Poor's 500 (S&P 500) and the Europe, Australasia, and Far East (EAFE) index from 1970 to 2000 found that the EAFE outperformed the S&P 500 in 15 of those 21 periods (Source: *AAII Journal*, October 2001).* After U.S. markets dominated in the 1990s, are international investments set to start outperforming? While no one knows for sure, there may now be opportunities to find investments in other parts of the world that are more attractively priced.

Diversification. One of the primary advantages cited for international investing is to reduce the volatility in a portfolio through diversification. The theory is that when the U.S. stock market is declining, investments in other parts of the world may counter that trend. Recently, however, it appears that during periods of crisis, stock markets throughout the world have moved in the same general direction. How accurate is this assessment?

One way to measure the benefits of diversification is to look at the correlation of two asset classes. A positive correlation means that the prices of the two assets move in the same direction. A correlation of +1 indicates that the assets move together very closely in the same direction. A correlation of -1 indicates that the assets move in opposite directions. A correlation close to 0 means that there is no relationship in the price movements of the two assets. The lower the positive

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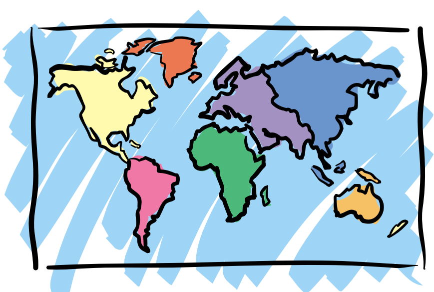

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Updating Documents

Whether this is your first, second, or subsequent marriage, you'll want to review major documents. Even if you've been married for some time, it's not a bad idea to take a look at these documents:

✔ **Estate planning documents** — If this is your first marriage, you may not even have estate planning documents. In that case, at least get a simple will and durable power of attorney. For those entering a subsequent marriage or with children, thoroughly review your estate planning documents. You may need to make changes to provide for your spouse while also protecting your children. Due to changes enacted by the 2001 Tax Act providing for the gradual elimination and then reinstatement of the estate tax, you should review your estate planning documents every couple of years.

✔ **Asset ownership** — Review how assets are titled to ensure they are consistent with your estate planning goals. If assets are owned jointly with rights of survivorship, that will take precedence over any provisions in your estate planning documents.

✔ **Assets with beneficiaries** — This would include life insurance policies, retirement plans, and individual retirement accounts (IRAs). For assets with named beneficiaries, those designations will take precedence over your estate planning documents. For retirement plans and IRAs, new regulations issued by the Internal Revenue Service in April 2002 significantly changed how beneficiaries must take distributions from inherited plans.

✔ **Business arrangements** — If you are a partial owner of a business, review any agreements dealing with what happens to the business if you die or want to sell your interest. The agreement may need to be changed to make provisions for your spouse. ❍❍❍

A Global Investing Strategy

If you want to invest in international investments, consider a systematic approach such as the following:

1. Decide what percentage of your portfolio should be allocated to international investments. That percentage will depend on several factors, including your risk tolerance, time horizon for investing, and comfort level with foreign investments. Consider allocating at least 10% to global investments, since less than that will typically have little effect on your return.

2. Decide whether you want to invest based on countries or companies. There are two basic approaches to international investing:

✔ A top-down approach analyzes various markets to determine which countries or regions of the world are likely to experience above-average investment returns. Individual investments in those countries are then selected.

✔ A bottom-up approach analyzes specific companies, selecting those that exhibit strong fundamentals. Which country that company is located in is typically not a factor.

3. Get familiar with the available investment options. There are numerous investment vehicles in the international arena. Understand the basic choices so you can make informed decisions about which alternatives to choose.

4. Understand the risks involved in international investing. In addition to the risks associated with domestic investing, international investing has unique risks:

✔ **Political and economic trends** — Many government decisions can impact a country's investments, including nationalizing industries, changing investment regulations, or adopting more stringent trade policies.

✔ **Currency fluctuations** — A foreign investment's return is based on two factors: the investment's actual return and the impact of currency fluctuations. If the U.S. dollar declines compared to the other country's currency, your investment will increase in value and vice versa.

✔ **Market volatility** — Volatility tends to be more pronounced in foreign markets, especially in emerging markets.

✔ **Information** — It's generally more difficult to find information about foreign investments. Also, financial reporting practices in other countries are different than those in the U.S.

✔ **Transaction concerns** — Transaction costs can be higher in foreign countries and delays can occur in settling trades.

5. Review specific investments. Once you have decided how much to allocate and have become familiar with international markets and the alternatives available, you are ready to start investigating specific investment opportunities.

6. Monitor your investments. You should periodically review your international investments, along with your other investments, to ensure that conditions at that company or in that country have not changed dramatically. ❍❍❍

Financial Planning and Aging Parents

Start discussing financial matters with your parents when they are in their early 60s. Include all immediate family members to prevent future misunderstandings, making sure to cover the following:

Where are personal records kept? You don't need to know specifics, but should find out where important records are located. Determine where they keep details about insurance policies, investments, deeds, birth and marriage certificates, pension information, bank statements, estate planning documents, credit card information, and outstanding debts.

Who are their advisers? Ask for a list with names, addresses, and phone numbers of all advisers and physicians. Get details about any medical conditions and medications being taken.

What are their monthly income and expenses? This will help you determine whether they have sufficient income to pay bills. If they don't, you may be able to help them change investment selections or find ways to increase their income.

Do they have adequate insurance? Make sure your parents have adequate health insurance coverage and have made provisions for long-term-care needs. If they aren't interested in long-term-care insurance but you fear the burden of long-term care may fall on you, you may want to obtain the insurance for them.

Do they have up-to-date estate planning documents? Don't ask for specifics, just make sure documents are in place so their wishes will be carried out. Find out if they have a durable power of attorney and a health care proxy.

What are their preferences for the future? Find out where your parents would like to live if they're not physically able to live in their current home. Discuss in detail what procedures they want performed to prolong life in the event of a terminal illness. Determine their preferences for funeral arrangements.

While these topics are sometimes not easy to discuss, they are important to know in case you need to help your parents with financial matters. Please call if you'd like to discuss your parents' finances in more detail. ❍❍❍

Invest Globally?

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correlation or the higher the negative correlation, the more risk that will potentially be eliminated. Typically, asset classes are considered to have good diversification benefits if they have correlations of 0.6 or less. Until recently, the correlation between the U.S. stock market and the EAFE was 0.5 or less (Source: *AAII Journal*, October 2001). As of early 2001, however, that correlation had increased to 0.75 (Source: *Money*, September 2001). While that reduces the diversification benefits, it remains to be seen whether the correlation stays at these higher levels or comes down to historical levels. Also keep in mind that the correlations listed above relate to foreign stock markets overall. The correlation between the U.S. stock market and specific foreign stock markets can be significantly different.

Currency fluctuations. When considering international investing, make sure you understand the significant role of currency fluctuations. Your return from an international investment is comprised of two components: the investment's return in local dollars and the impact of any currency fluctuations. Part of the reason U.S. investments dominated in the 1990s was due to the strong U.S. dollar. Now, the U.S. dollar is starting to show some weakness against other currencies, which could bolster the returns of foreign investments.

Investment opportunities. The U.S. stock market now represents only slightly more than 50% of the total market capitalization of the world (Source: *Reuters Business Report*, February 20, 2002). Limiting yourself to U.S. stock investments means eliminating nearly half of the world's investments from consideration. In a number of industries, the world's leading companies are not U.S.-based companies.

Now may be a good time to take another look at international investing. Keep in mind, however, that international investments may not be suitable for everyone. In addition to the risks associated with domestic investing, foreign investing has unique risks, such as currency fluctuations, political and social changes, and greater share price volatility. Please call if you'd like to discuss international investments. ❍❍❍

* The S&P 500 is an unmanaged weighted index generally considered representative of the U.S. stock market. The EAFE is an unmanaged index of 1,000 foreign stocks generally considered representative of stock markets outside the U.S. Investors cannot directly purchase an index. Past performance is not a guarantee of future results. This information is presented for illustrative purposes only.

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A Lower Cost of Living

Are you searching for ways to significantly reduce your living expenses? Have you given any thought to relocating to a less expensive city? For some, this strategy may not work. Perhaps you live close to your parents or grown children and don't want to move too far. Or maybe demand for your career is concentrated in major cities, so you couldn't find a job in another city.

But if you don't have personal ties to your current city or your job isn't dependent on where you live, moving to another location can significantly lower your cost of living. This is a strategy often used by retirees looking to stretch their retirement income. But it can also make a big difference in your cost of living while you are working, hopefully allowing you to put more away in savings. Not only can you lower your living costs, but often you can move to a locale that has a climate you enjoy more or local attractions more in keeping with your personal interests. ❍❍❍

Financial Thoughts

Approximately 25% of U.S. households have a net worth of $10,000 or less (Source: Consumer Federation of America, 2002).

Once the Social Security trust funds are depleted, revenues from payroll taxes will pay approximately 73% of current Social Security benefits (Source: Social Security Administration, 2002).

Investors allocate approximately 90% of their stock investments to U.S. stocks (Source: *Journal of Financial Planning*, August 2002).

Approximately 50% of employers changed health care plans in order to shift more of the cost to workers. Workers help pay for more of the costs through higher premium contributions, higher deductibles and co-payments, or smaller wage increases (Source: *Journal of Financial Planning*, August 2002).

Average retirement savings declined from $120,000 in 2001 to $93,000 in 2002, a decline of 22.5%. In a recent survey, 52% of the baby boomer respondents indicated that they are concerned about saving enough money for retirement, compared to 29% in 2001 (Source: *National Underwriter*, August 26, 2002). ❍❍❍