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Element Financial Group



Helping Clients Focus on What Matters Most

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Inflation and Your Retirement

Some people remember the “good old days” when gasoline prices were as low as 25¢ per gallon. Others recall when a can of soda cost 15¢. Realistically speaking, prices tend to rise over time—sometimes steadily and sometimes abruptly. In the years ahead, **inflation** will most likely decrease the purchasing power of your money, which means that during retirement your dollars will buy less than they do today.

It is easy to misinterpret inflation as the rise in price of *individual* goods and services. Actually, inflation is the increase in the average price level of *all* goods and services. For example, the price you pay for oranges may rise during the winter due to unseasonably cold temperatures in Florida. On the other hand, the average price of all other items in your local supermarket, like peanut butter and paper towels, may remain relatively level. In this case, the increase in the price of oranges is not a result of inflation but, rather, a function of **supply** and **demand**.

Inflation can result when either 1) the total of all goods and services demanded exceeds production, or 2) the amount of all goods and services supplied by producers decreases. Note how, in the above example, the supply and demand for the oranges had no effect on inflation. However, changes in supply and demand on a broader scale can result in inflation.

Consider these economic scenarios: Suppose business is booming, unemployment is low, and the average worker's wages are increasing. As a result, consumers have more disposable income available and will, therefore, be able to purchase more goods and services. Average prices tend to rise under these circumstances due to the increase in *demand* for all goods and services.

In the second scenario, suppose the economy is suffering. As unemployment rises and wages remain stagnant, consumers will be unable to purchase additional goods and services. As a result, producers will slow down production and raise prices in order to cut losses associated with decreased production. In this case, average prices tend to rise due to a decrease in the *supply* of all goods and services. This cycle can be vicious.

It is important to keep in mind that individual consumers are not the only market participants that can affect the economy. Businesses, government agencies, and foreign markets also spend billions of dollars on U.S. goods and services. Their spending, or lack thereof, can equally influence increases or decreases in supply and demand that, in turn, can result in inflation.

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Estimating College Costs

For many people, a child's college education is the second most expensive purchase (after that of a home) they will ever make. For parents and grandparents who wish to estimate the cost of a college education, the following tables can facilitate an educated guess.

According to The College Board's *Trends in College Pricing 2010*, the average annual cost of in-state tuition, fees, room, and board at a four-year public institution is \$16,140 for the academic year 2010–2011. For a private institution, the cost of tuition, fees, room, and board is \$36,993.

Public colleges and universities experienced an increase of almost 6% from the prior year, 2009–2010, and private colleges and universities experienced an increase of over 4%.

If the cost of a college education increases by 6% annually, and your child enters a private college in the 2020–2021 academic year, the estimated tuition will be \$71,456. Based on the projections below, a four-year education would cost approximately \$285,000. For young families, skyrocketing cost projections can lead to sticker shock, but there are strategies that can help

you keep pace with tuition hikes. The College Board reports that almost 75% of undergraduate students receive some type of financial aid. In addition, the Federal government offers tax breaks for education savings, as well as other credits and deductions for taxpayers currently facing college costs.

The table below can help you to estimate the approximate annual cost of tuition, as well as room and board, for a four-year undergraduate education based on the year a child will enter college, the inflation

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Projected Higher Education Costs						
School Year	Public Colleges & Universities			Private Colleges & Universities		
	3% Inflation	6% Inflation	10% Inflation	3% Inflation	6% Inflation	10% Inflation
10–11	\$16,631	\$17,135	\$17,830	\$38,118	\$39,275	\$40,867
11–12	17,137	18,192	19,697	39,277	41,697	45,146
12–13	17,658	19,314	21,760	40,472	44,269	49,873
13–14	18,195	20,506	24,038	41,703	46,999	55,096
14–15	18,748	21,770	26,555	42,972	49,898	60,865
15–16	19,319	23,113	29,336	44,279	52,976	67,238
16–17	19,906	24,539	32,408	45,625	56,243	74,279
17–18	20,512	26,052	35,801	47,013	59,712	82,057
18–19	21,136	27,659	39,550	48,443	63,395	90,649
19–20	21,778	29,365	43,692	49,917	67,305	100,141
20–21	22,441	31,176	48,267	51,435	71,456	110,628
21–22	23,123	33,099	53,321	52,999	75,863	122,212
22–23	23,827	35,141	58,904	54,611	80,542	135,009
23–24	24,551	37,308	65,072	56,272	85,510	149,146
24–25	25,298	39,609	71,886	57,984	90,784	164,764
25–26	26,068	42,052	79,414	59,748	96,384	182,017
26–27	26,861	44,646	87,729	61,565	102,328	201,077
27–28	27,678	47,399	96,916	63,437	108,640	222,132

Figures are estimated projections based on the average cost of tuition at public and private universities for the 2010–2011 academic year.

Economic Comfort in Troubled Times

What if you were to get in an accident, damage your car, and become disabled? What if your house was to burn down or your business was burglarized? What if something were to happen to you and your loved ones had to support themselves? Insurance helps to provide a safety net for each of these hardships.

Protect Yourself

Insurance has become a necessary and valuable part of our lives. Personal insurance, including **automobile**, **umbrella liability**, and **property insurance**, fulfills vital social needs and, in many ways, promotes public safety. By helping people restore or replace their property and belongings, insurance serves a valuable function.

Obviously, insurance cannot eliminate or prevent liability lawsuits, much less predict them, but it *can*

help protect the owners of homes, automobiles, businesses, and other property from the potential effects of a lawsuit. Insurance cannot finance the purchase of a home, automobile, or business, but it *can* make facing some of the risks involved in owning a home, operating a vehicle, or running a company more manageable. While insurance cannot prevent property from being damaged or destroyed, it *can* help provide the money to replace property or to find a suitable place to live.

Health and long-term care insurance alone cannot save lives, but it can help pay for timely medical attention and long-term care services that may eventually save lives. **Life insurance** can help families maintain their financial independence by providing much needed funds when a loved one dies. **Disability income insurance** can help replace a portion of the income of a disabled

breadwinner and preserve a family's standard of living. In short, insurance can—and does—help protect individuals, families, and businesses from potential financial difficulty as a result of unexpected events.

Lighten Your Burden

People may buy insurance because the law or lenders require it, or because they want to know that they may be indemnified for unpredictable losses. The decision may be based on the amount of risk they are willing to tolerate and the amount of protection they desire. Simply stated, the proper insurance coverage can help to lighten your burden when facing difficult circumstances.

To learn more about personal insurance coverage for your specific situation, speak to a qualified professional—because it never hurts to have a safety net. ■

estimating college costs

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forecast, and the choice of a public or private institution.

By starting a disciplined savings plan *now*, you may be better positioned to meet your child's future education needs. The following table shows the return of a variety of monthly savings contributions, earning 6% interest, for intervals of 5, 10, and 18 years—the average college age. This hypothetical example assumes a 25% Federal tax rate and 3% inflation.

Many parents postpone planning education funding because the task

seems overwhelming, or they think saving the required amount of money will force them to compromise their current lifestyle. While these are legitimate concerns, they need not stop you from establishing and maintaining an effective plan. Whether considering a public or private college for your child, the key to effective

planning is to begin saving as early, and as much, as possible. ■

Save per Month	Savings Growth at 6%		
	5 Years	10 Years	18 Years
\$50	\$3,109	\$6,454	\$12,339
\$100	\$6,219	\$12,909	\$24,678
\$250	\$15,549	\$32,273	\$61,696
\$500	\$31,099	\$64,546	\$123,392
\$1,000	\$62,199	\$129,093	\$246,785

For illustrative purposes only. Not indicative of any particular savings vehicle or insurance product.

How Are Your Charitable Donations Being Spent?

If you are making a large donation to a charity, you may have a specific goal in mind for the use of the money. Whether it is to fund a particular program or support a new project, you may want some control over how your donation is used by the charity. This may be accomplished through **donor advised funds** or **private foundations**.

Many larger public charities offer donor advised funds, which involve

an agreement between the donor and the charity that it will consider the donor's wishes with respect to the use of donations. However, the agreement is non-binding, and the charity exercises final control over the disposition of the funds.

A private foundation may be a better choice for donors who do not want to rely on the ultimate discretion of a public charity regarding the use of contributions. A private

foundation is a nonprofit organization, whose funds and programs are managed by its own trustees or directors. The benefits of increased donor control come at a price, with restrictions on the types and amounts of gifted funds.

For more information regarding these charitable giving strategies, the rules governing their uses, and tax benefits, consult your legal and tax professionals. ■

inflation and your retirement

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To a certain extent, *some* inflation may be a sign of a healthy economy. In fact, one of the economic policy goals of the United States government is to maintain an inflation rate ranging from 0% to 3% per year. On the other hand, too much inflation or no inflation at all can be a sign of troubling economic times. Thus, one of the greatest challenges facing policymakers is to make decisions that will create desired inflation results.

There are two Federal economic policies used in an attempt to control the economy. **Fiscal policy**, which falls under the auspices of Congress, uses taxation and spending as a means to increase employment, stabilize prices, and boost economic growth. In contrast, **monetary policy**, which is controlled by the Federal Reserve Bank (the Fed), manipulates the money supply

and short-term interest rates in an attempt to spur growth or control inflation.

Congress and especially the Fed look at the **Consumer Price Index (CPI)** when making policy decisions. The CPI is considered by many to be one of the best measurements of inflation. The CPI gauges the average change in prices paid by urban consumers for a fixed market basket of goods and services over a period of time. Each month, the CPI is calculated, and constant fluctuations in the CPI will ultimately result in Congress or the Fed taking appropriate measures to attempt to regain control of inflation. However, in the short term, it is the Fed that holds the ability to react quickly. Congress, as we all know, requires political debate and the passage of legislation before fiscal decisions can be carried out.

In addition to creating higher costs for goods and services, inflation creates depreciation in currency values. In other words, as prices increase, the purchasing power of your income (dollar for dollar) decreases. During sound economic times, price increases will usually be accompanied by wage increases that are equal to, or greater than, inflation. However, during economic downturns when wages remain level, the cost of living increases as your purchasing power diminishes.

In actuality, regardless of what state the economy is in, one of your greatest long-term financial challenges may be planning for your retirement savings to outpace inflation. Therefore, it is always important to take inflation into consideration, not only as you save, but also as you make purchasing decisions. ■

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