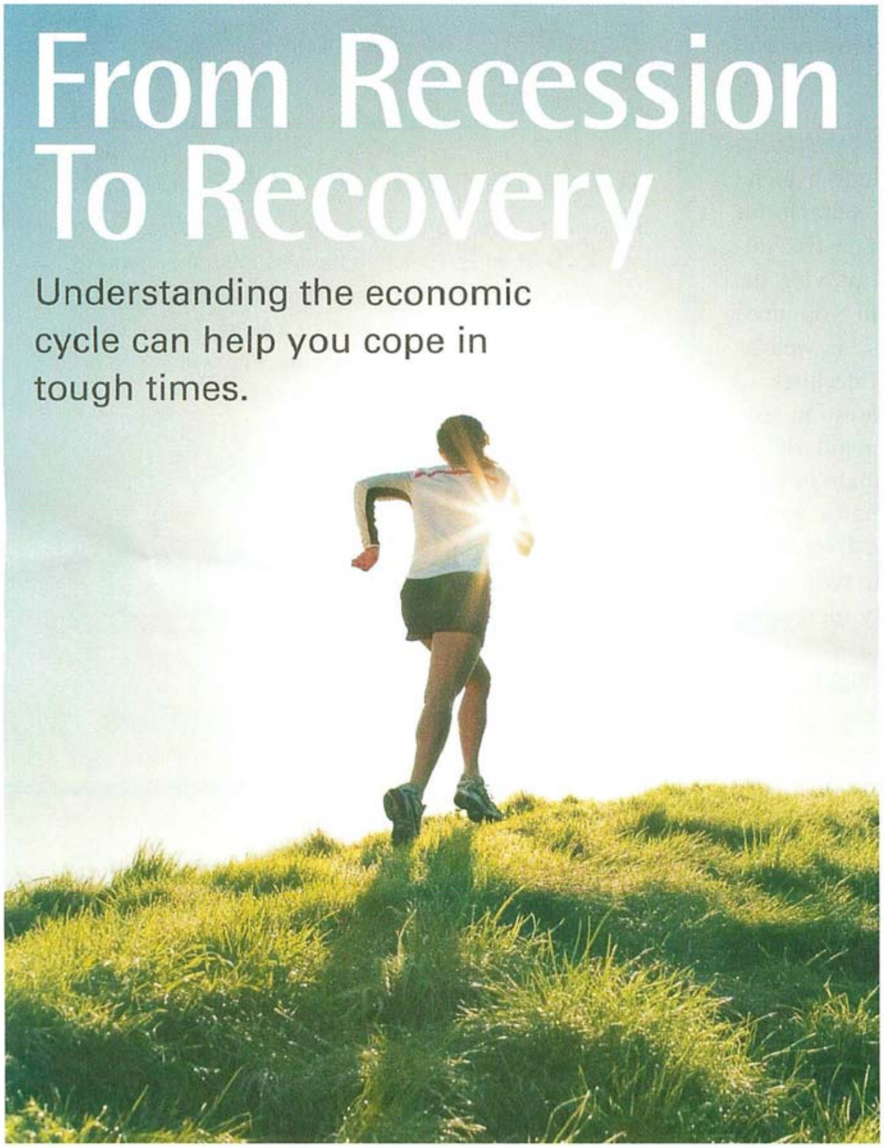
invest

IT'S YOUR FUTURE

From Recession To Recovery

Understanding the economic cycle can help you cope in tough times.



Pacing Yourself with Stocks

The current bear market may tempt you to shift assets away from stocks and into cash. But some of the market's best days come as stocks rebound from their low points—so missing even a handful of those rallies can severely reduce your long-term returns. Consider the chart below: It shows the hypothetical growth of a $10,000 investment made in February 1989 if the money were invested in stocks continuously through February 2009, compared with its growth if the investor missed the market's best days.[1] As you can see, the greatest growth takes place when stocks are held over the long term.

Why Stay Invested?

How $10,000 in stocks over 20 years would have fared had you...

[1]Returns are based on performance of the S&P 500 Index from February 1989 to February 2009. You cannot invest directly in an index.

A recession can seem never-ending. Unpleasant as they are, downturns are a normal part of the economic cycle. As you ride out the weak economy, it may help to know that the stock market typically begins to rebound before a recession ends.

Learning more about the relationship between the economic cycle and the market can help you navigate turbulent times more steadily.

What is a recession?

The economy alternates between periods of strength and weakness. The National Bureau of Economic Research defines a recession as "a significant decline in economic activity spread across the economy, lasting more than a few months." Since 1945, the U.S. has experienced 12 recessions—about one every five-and-a-half years.[1] Each recession—barring the current one, which has yet to resolve—was followed by a period of economic growth.

Typically, recessions serve to correct problems that developed when the economy was strong. In the current recession, for example, many consumers and corporations are trimming their debts and expenses. Such efforts can be painful in the short term, but they can help to position the overall economy for future growth.

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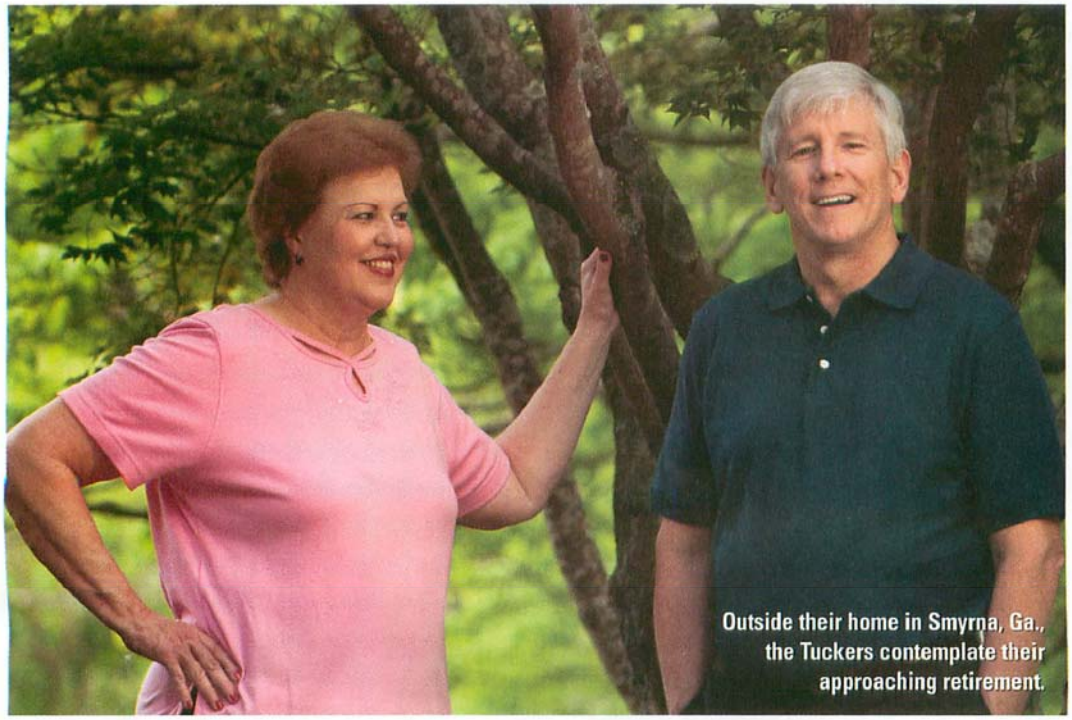
"We've paid off the house. Now what?"

Debt-free, this couple needs to jump-start their savings.



Outside their home in Smyrna, Ga., the Tuckers contemplate their approaching retirement.

Chuck and Vicki Tucker are ahead of the game in a big way. They recently finished paying off their auto loans, credit cards and the mortgage on their Smyrna, Ga. home. Aside from the $1,000 they donate to their church each month, they have few expenses now that their four children are grown.

But as they approach retirement, the Tuckers are worried that their $150,000 in savings isn't enough. Chuck expects only a modest pension when he retires from his job as an engineer for an aerospace company. They recently consulted with Kathleen Campbell, a financial planner based in Fort Myers, Fla., to discuss ways to grow their retirement savings.

At a Glance

Chuck and Vicki Tucker
Ages: 56 & 60
Home: Smyrna, Ga.
Family: Four grown children
After Tax Income: $6,000 monthly
Expenses: $3,000 monthly
Retirement Savings: $150,000

Preparing for emergencies

With their debts behind them, the Tuckers have an extra $2,000 of discretionary monthly income. Their first priority, says Campbell: Bolster their rainy-day fund. "Double your cash cushion to six months' worth of expenses, or $18,000, so you can handle unforeseen costs," she urges. The couple should reach that goal in less than five months.

Rebuilding for retirement

While their emergency fund grows, the Tuckers can focus on their investments. After suffering losses last year, Chuck shifted all his 401(k) plan account's assets into very conservative short-term bond funds. "I did the radical thing," Chuck says. Campbell advises that he immediately move at least 30% of his 401(k) assets into stock funds. The goal: Provide growth potential to fight inflation throughout their retirement years. Currently, short-term bond funds earn approximately 1%,[1] far below the rate of inflation (3.8% in 2008).[2]

Once the Tuckers increase their emergency fund, says Campbell, they can put the $2,000 a month in their nest egg. To start, each should open a Roth IRA account. Roth IRAs are funded with after-tax money, but their investment growth is tax-free. With the bulk of the Tucker's savings in Chuck's tax-deferred 401(k) plan, a Roth IRA's tax-free withdrawals will make it easier for the couple to manage their tax bill in retirement. This year, Chuck and Vicki can each contribute up to $6,000 (which includes $1,000 in "catch-up" contributions for savers age 50 or older), so $1,000 a month over 12 months should fully fund both Roth IRA accounts for the year.

Committing to a plan

That leaves the Tuckers with another $1,000 a month. Campbell says Chuck could use the money to boost his salary deferral to his 401(k) from 8% to the plan's 19% maximum. That would be just enough to take full advantage of his employer's 50% matching contribution.

By the time Chuck reaches age 65, if the Tuckers follow Campbell's savings program, their nest egg could potentially grow to more than $500,000, assuming a 6% annualized investment return.

Chuck believes they can get on the right track. "I'm going to dedicate myself to this," he says. "We're ready to roll." ■

[1] Morningstar, Inc. [2] Bureau of Labor Statistics.