ROCKBRIDGE
INVESTMENT MANAGEMENT

FINANCIAL COMMON SENSE

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Rockbridge Investment Management is a group of like-minded professionals working with a select group of clients with whom we can have a significant impact. Everything we do is focused on building and preserving wealth for our clients. We help remove complexity so clients can focus on the simple but difficult process of successful investing.

Life Events to Consider: Buying a House

by Mike Antonacci

Whether it's your first house, you are relocating to a new area, or you are upgrading to your "forever" home, buying a house is one of the most significant purchases you will make. Properly budgeting for the costs to buy, finance, and maintain the new home can help set you up for financial success and keep you from feeling "house poor." While there are many considerations that go into finding the right house for you and your family, reviewing the points below will start you off on a solid foundation (pun intended!)

How much can you afford? - 3 primary rules of thumb include:

- Maximum purchase price is 3x your gross household income.
- Housing-related payments (mortgage, taxes, homeowner's insurance) should be less than 28% of your monthly gross household income.
- Total debt payments should be less than 36% of your monthly gross household income.

What type of mortgage to get and how much to put down:

- The most common types of mortgages are conventional mortgages. Conventional mortgages have a fixed interest rate and vary in duration, with 15 or 30 years being the most common.
    - A 30-year mortgage will generally have the lowest monthly payment but a higher interest rate.
    - A 15-year mortgage is the opposite. Your interest rate (and therefore the overall cost of the mortgage) will be lower, but your monthly payments will be much higher.
- Regardless of the term length, lenders typically require you to make a down payment of 10% to 20% of the purchase price. If you put less than 20% of the purchase price down, you will likely be required to pay Private Mortgage Insurance (PMI). This insurance protects the bank in case of a home mortgage default and is typically between 0.5% and 1% of the loan amount each year.

What are some of the other costs to consider?

- *Property taxes and homeowner's insurance* – Property taxes can add a significant amount of cost on a home. Taxes vary by state and by county; however, it is not unreasonable to assume that if you are targeting a $1M+ home, you should estimate paying $25K to $40K a year in property taxes. Property taxes may be included as a portion of your monthly mortgage payment, or you may need to pay them directly during the year. Don't forget to take advantage of state programs, like New York's STAR program, which can reduce your property tax burden.

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Life Events to Consider: Buying a House *Continued*

While not nearly as expensive, homeowner's insurance goes up as the purchase value of the home increases. It may be advantageous to bundle your various insurance policies together through one carrier. Often insurance companies will provide discounts for having homeowner's, car insurance, umbrella policy, etc. with them.

- *Closing costs* - Most mortgages will have some form of closing costs associated with them. The fees cover the loan recording and processing, attorney costs, title insurance, appraisal and various other new mortgage requirements. Expect closing costs to be approximately 2%-5% of the loan value.

- *Maintenance and upkeep expenses* – Homes can be expensive to maintain. Routine repairs and improvements on an older home can be a few thousand dollars a year. Major repairs such as replacing the roof, or damage from a weather event, can cost tens of thousands of dollars and can be unexpected. Plan on budgeting about 1% of the home value for annual maintenance.

How to title the property?

- *Tenants by the Entirety (TBE)* – For married couples, this is typically the default titling option. Advantages of TBE include creditor protection in certain circumstances and probate avoidance when the first spouse passes away. Just like with owning property as joint tenants with rights of survivorship (JTWRS), the deceased tenant's share passes to the surviving tenant via operation of law and not through the decedent's Will or revocable trust.

- *Tenants in Common* – In some instances, it will be advantageous to own the property jointly as tenants in common. The main difference between tenants in common and TBE or JTWRS is that each tenant can direct the passing of their interest through their Will or revocable trust. This is advantageous if real property is needed to fund a testamentary trust, such as a credit shelter trust.

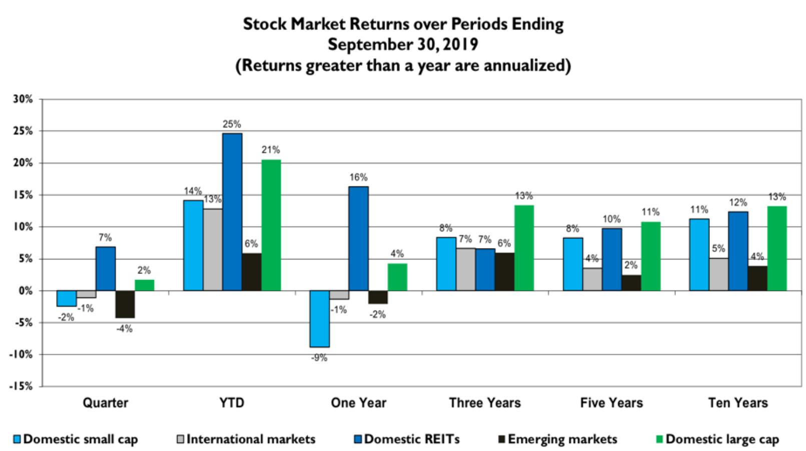
- *In Trust* – For those using a revocable trust (or trusts) as part of their estate plan, making sure to title the property in the name of the trust(s) is essential. Usually the attorney who drafts the trust will also draft a deed to transfer existing property into the trust(s). If a trust is already in place and you are purchasing new property, the new property should be purchased directly in the name of the trust(s).

So, whether you are purchasing a first home, a forever home, or perhaps a second (or third) property, there are a number of considerations (financial and otherwise) that should be reviewed beforehand. Proper planning will not only help you acquire the house of your dreams but can also help make sure that dream does not end up in a financial nightmare down the road.◆

Market Commentary *by Bob Ryan*

Stock Markets

It was generally an off quarter for stocks, except for Real Estate Investment Trusts (REITs). The year-to-date numbers look good. Recent periods show variability among individual markets as well as within various time periods - REITs continue to do well, no doubt reflecting declining interest rates. One theme running throughout the past ten years' stock returns is the better-than-average numbers for domestic stocks versus international stocks. While this behavior is clear by looking back, investment decisions are made by looking ahead. Markets have no memory so we can't bank on superior results from domestic markets continuing.



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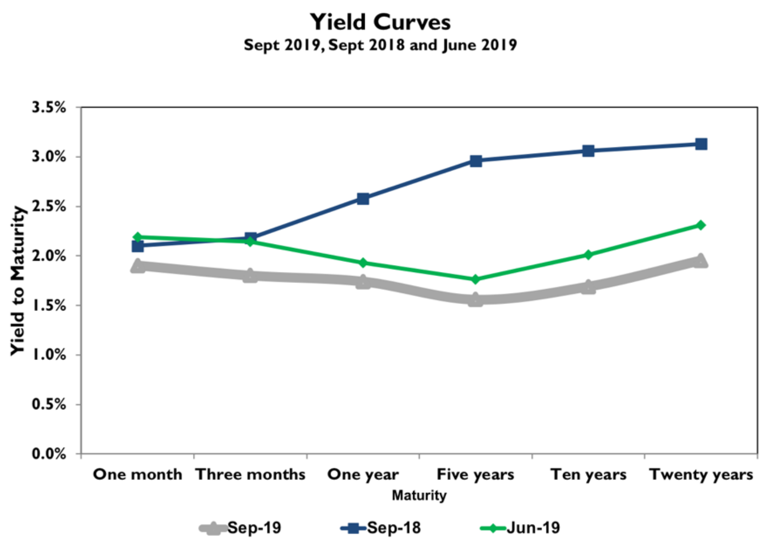
Market Commentary *Continued*

Another theme in these ten-year numbers is that the domestic large-cap market (S&P 500) returns consistently exceeded those of other benchmarks. Expected earnings and growth drive stock returns, and any surprises that alter these expectations produce volatility. S&P 500 stocks are well-followed by analysts; there is no reason to think that they will consistently provide positive surprises. So, what's going on? It may be simply that S&P 500 stocks are the default investment when investors desire more risk in the face of anemic returns in other markets. These results are by and large unrelated to company earnings and investments opportunities – suggesting a "passive management bubble". If that explains some of what is happening, then the relative results in this market won't go on forever.

We know that maintaining a globally diversified stock portfolio has the best chance for long-term success. However, because domestic markets, especially the S&P 500, are so popular and familiar, it has been especially difficult for investors to maintain strategic commitments among several other markets this time around.

Bond Markets

A yield is what you earn by holding a bond to its maturity. Changes in yields drive returns – falling yields are positive; rising yields negative. The longer a bond's maturity, the greater the impact a given change will have on prices and returns.



The Yield Curve is a picture of how these yields vary across several bond maturities. Shown to the right are U.S. Treasury securities a year ago (September 2018), at the end of last quarter (June 2019) and today. Not only can changes help us better understand bond returns, they can also be useful predictors of the direction of interest rates. The sharp fall-off over the past year means positive bond returns, especially at the longer end – the long-term Treasury benchmark (7-10 yrs.) earned nearly 10% while the short-term benchmark (1-3 yrs. Treasury) earned only 3%. Bond returns were positive over the past quarter reflecting the downward shift in the Yield Curve.

Last year's curve is typical; the more or less "flat" curve we see today is not. However, it is consistent with expected lower rates in the future. The story behind this prediction is that the Fed will continue to reduce rates to fight the upcoming economic decline. However, while there is some indication of a slowdown, neither the stock market, nor labor markets (where unemployment is at historical lows) seem to anticipate much of a slowdown. The recent cut in interest rates is more in response to political pressure – at these levels the effect of any decrease will be mostly perception.

Recessions and the Tools to Respond

There is a lot of noise about a coming recession. While the numbers still look reasonable, the tools to respond may not be as potent this time around. The hue and cry for the Fed to reduce interest rates notwithstanding, and with rates at historically low levels and massive Treasury securities on the Fed's balance sheet, there is not much room for monetary policy to make a difference. As far as fiscal policy is concerned, the Government is already running substantial deficits due to the recent tax cut. The positive impact may be behind us and with today's political dysfunction, the opportunity to do more with fiscal policy may not be available. A lot of uncertainty – little wonder the stock market is volatile. With the large tax cuts in place and an accommodative Fed, we have enjoyed a nice ten years that may be difficult to repeat. ◆

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Check out our Blog!

Ethan Gilbert, an advisor here at Rockbridge documents another example of how markets are difficult to predict. This time, the evidence comes from how far off economists were a year ago when asked to forecast interest rates. The same logic applies to average investors, those who try to outsmart the market usually end up worse off because of it. Be sure to read the full article on our website blog at www.rockbridgeinvest.com/financial-common-sense/. ◆

Returns from Various Markets

The following table shows the returns from various markets over periods ending September 30, 2019:

Market/Asset Class	Quarter	YTD	1 Year	3 Years	5 Years	10 Years	20 Years
FIXED INCOME							
3-Month US Treasury Bills	0.57%	1.81%	2.39%	1.54%	0.98%	0.54%	1.82%
Bloomberg Barclays US Agg Bond	2.27%	8.52%	10.30%	2.93%	3.38%	3.75%	5.01%
Bloomberg Barclays 1-5 Yr Credit	1.14%	5.69%	6.67%	2.72%	2.61%	3.13%	4.44%
DOMESTIC STOCKS							
S&P 500	1.70%	20.55%	4.25%	13.40%	10.84%	13.24%	6.33%
S&P 500 Value	2.83%	20.01%	5.56%	10.61%	8.48%	11.56%	6.29%
S&P 500 Growth	0.72%	21.06%	3.25%	15.74%	12.82%	14.72%	5.89%
Russell 2500	-1.28%	17.72%	-4.04%	9.52%	8.57%	12.22%	9.21%
Russell 2500 Value	0.13%	15.41%	-4.35%	6.87%	6.98%	11.00%	9.55%
Russell 2500 Growth	-3.18%	19.97%	-4.11%	12.34%	10.22%	13.49%	7.92%
MSCI US REIT	7.69%	26.82%	18.31%	7.27%	10.11%	13.00%	11.18%
INTERNATIONAL STOCKS							
MSCI EAFE	-1.07%	12.80%	-1.34%	6.48%	3.27%	4.90%	3.72%
MSCI Emerging Markets	-4.25%	5.90%	-2.02%	5.98%	2.33%	3.37%	7.06%
U.S. Consumer Price Index	0.16%	2.12%	1.63%	2.05%	1.51%	1.74%	2.14%

Note: These results were developed by simulating past returns in the various markets included in each benchmark, assuming the reinvestment of dividends and other earnings. The BofA Merrill Lynch 3-Month U.S. Treasury Bill Index represents money market/cash; the Bloomberg Barclays US Aggregate Bond Index represents the total U.S. bond market; the Bloomberg Barclays 1-5 Yr Credit Index represents the U.S. corporate bond market; the S&P 500, S&P 500 Value Index and S&P 500 Growth Index represent the domestic large-cap market; the Russell 2500, Russell 2500 Value Index and Russell 2500 Growth Index represent the domestic small-cap market; the MSCI U.S. REIT Index represents the U.S. real estate market; the MSCI EAFE Index represents the developed international equity market; the MSCI Emerging Markets Index represents international emerging markets. Benchmark Portfolio returns include Real Estate and Emerging Markets allocations beginning in July 2011. Benchmark Portfolio returns do not include allocations to these asset classes prior to June 30, 2011. Benchmark portfolio returns include Corporate Bond Market as of January 1, 2019 and do not include an allocation to this asset class prior to this. This data is presented to show the long-term relationship between returns at various levels of investment risk. It is not intended to present performance results experienced by clients of Rockbridge Investment Management, but is intended to provide a benchmark against which actual performance might be judged. Also, readers should recognize that future investments would be made under different economic conditions. It should not be assumed that future investors would experience returns, if any, comparable to those shown above. The information given is historic and should not be taken as any indication of future investment results.

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