Ingram FINANCIAL GROUP
Wealth Management | Investments | Insurance

INGRAM INSIGHTS Newsletter
May 2016

Understanding Stock Market Indexes

No doubt you've seen headlines reporting that a particular stock index is up or down. But do you know what an index is, and how understanding the nuts and bolts of a specific index may be helpful to you?

An index is simply a way to measure and report the fluctuations of a pool of securities or a representative segment of a market. An index is developed by a company that sets specific criteria to determine which securities are included in the index based on factors such as a company's size or location, or the liquidity of its stock. For example, the S&P 500 is an index made up of mostly large-cap U.S.-based companies that Standard & Poor's considers to be leading representatives of a cross-section of industries.

The company that develops the index tracks the performance of its components and aggregates the data to produce a single figure that represents the index as a whole. Virtually every asset class is tracked by at least one index, but because of the size and variety of the stock market, there are more stock indexes than any other type. It's important to note that the performance of an unmanaged index is not indicative of the performance of any specific security. Individuals cannot invest directly in an index.

Comparing apples to oranges

Since indexes encompass a wide range of securities, it's important to know what segment of the market a particular index covers. For instance, a composite index follows a specific stock exchange. The Nasdaq Composite Index includes all the stocks listed on the Nasdaq market. Conversely, sector indexes track securities in a specific industry.

Even indexes that include the same securities may not operate in precisely the same way. Generally, indexes tend to be either price-weighted or market capitalization-weighted. If an index is price-weighted, such as the Dow Jones Industrial Average, the impact of each stock on the overall average is proportional to its price compared to other stocks in the index. With a price-weighted index, the highest-priced stocks would have the most impact on the average. For example, a 1 percentage point drop in the price of a stock selling for $80 per share would have more impact on the overall index's performance than a 1 percentage point drop in the price of a stock that had been selling for $40 a share.

If an index is market capitalization-weighted or market value-weighted, such as the Nasdaq Composite Index or the S&P 500 Composite Index, the average of the index is adjusted to take into account the relative size of each company (its market cap) to reflect its importance to the index. Stocks with a larger market capitalization have a greater influence on how the index performs than stocks with a smaller market capitalization. For example, if the stock of a $10 billion market-cap company drops by 1 percentage point, it will drag down the index's performance more than a 1 percentage point drop in the share price of a $1 billion market-cap company.

Though an index adheres to a set of guidelines for selection of the securities it includes, the company that oversees the index generally reviews the security selection periodically and may make occasional changes. For example, some indexes may rebalance if an individual security grows so large that it dominates the index. Others have a limit on how much of the index can be devoted to a particular sector or industry, and may rebalance if the proportion gets skewed.

Indexes are worth watching

Stock indexes can provide valuable information for the individual investor. If checked regularly, an index can provide information that may help you stay abreast of how the stock market in general, or a particular segment of it, is faring. However, understanding the differences between indexes and how each one works will help you make better use of the information they provide. All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

Nearing Retirement? Time to Get Focused

If you're within 10 years of retirement, you've probably spent some time thinking about this major life change. The transition to retirement can seem a bit daunting, even overwhelming. If you find yourself wondering where to begin, the following points may help you focus.

Reassess your living expenses

A step you will probably take several times between now and retirement--and maybe several more times thereafter--is thinking about how your living expenses could or should change. For example, while commuting and dry cleaning costs may decrease, other budget items such as travel and health care may rise. Try to estimate what your monthly expense budget will look like in the first few years after you stop working. And then continue to reassess this budget as your vision of retirement becomes reality.

Consider all your income sources

Next, review all your possible sources of income. Chances are you have an employer-sponsored retirement plan and maybe an IRA or two. Try to estimate how much they could provide on a monthly basis. If you are married, be sure to include your spouse's retirement accounts as well. If your employer provides a traditional pension plan, contact the plan administrator for an estimate of your monthly benefit amount.

Do you have rental income? Be sure to include that in your calculations. Is there a chance you may continue working in some capacity? Often retirees find that they are able to consult, turn a hobby into an income source, or work part-time. Such income can provide a valuable cushion that helps retirees postpone tapping their investment accounts, giving them more time to potentially grow.

Finally, don't forget Social Security. You can get an estimate of your retirement benefit at the Social Security Administration's website, ssa.gov. You can also sign up for a my Social Security account to view your online Social Security Statement, which contains a detailed record of your earnings and estimates of retirement, survivor, and disability benefits.

Manage taxes

As you think about your income strategy, also consider ways to help minimize taxes in retirement. Would it be better to tap taxable or tax-deferred accounts first? Would part-time work result in taxable Social Security benefits? What about state and local taxes? A qualified tax professional can help you develop an appropriate strategy.

Pay off debt, power up your savings

Once you have an idea of what your possible expenses and income look like, it's time to bring your attention back to the here and now. Draw up a plan to pay off debt and power up your retirement savings before you retire.

Why pay off debt?

Entering retirement debt-free--including paying off your mortgage--will put you in a position to modify your monthly expenses in retirement if the need arises. On the other hand, entering retirement with mortgage, loan, and credit card balances will put you at the mercy of those monthly payments. You'll have less of an opportunity to scale back your spending if necessary.

Why power up your savings?

In these final few years before retirement, you're likely to be earning the highest salary of your career. Why not save and invest as much as you can in your employer-sponsored retirement savings plan and/or your IRAs? Aim for the maximum allowable contributions. And remember, if you're 50 or older, you can take advantage of catch-up contributions, which allow you to contribute an additional $6,000 to your employer-sponsored plan and an extra $1,000 to your IRA in 2016.

Account for health care

Finally, health care should get special attention as you plan the transition to retirement. As you age, the portion of your budget consumed by health-related costs will likely increase. Although Medicare will cover a portion of your medical costs, you'll still have deductibles, copayments, and coinsurance. Unless you're prepared to pay for these costs out of pocket, you may want to purchase a supplemental insurance policy.

In 2015, the Employee Benefit Research Institute reported that the average 65-year-old married couple would need $213,000 in savings to have at least a 75% chance of meeting their insurance premiums and out-of-pocket health care costs in retirement. And that doesn't include the cost of long-term care, which Medicare does not cover and can vary substantially depending on where you live. For this reason, you might consider a long-term care insurance policy.

These are just some of the factors to consider as your prepare to transition into retirement. Breaking the bigger picture into smaller categories may help the process seem a little less daunting.

Ingram FINANCIAL GROUP
Wealth Management | Investments | Insurance

Winter Haven | 799 Overlook Drive | Phone 863-326-9833 | Toll Free 800-425-8242 | Fax 863-875-1855
Online | www.ingramfinancialgroup.com