



# YOUR FINANCIAL FUTURE

Your Guide to Life Planning

July 2010

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## In This Issue

### Diversification Can Help Bring Balance to Your Portfolio

Understanding how diversification works may provide insight on the best ways to put it into practice. Financial professionals often look at a statistic known as correlation, which measures the historical tendency of two investments to move in tandem in response to market and economic developments.

### College Loans: Should Parents or Students Take the Plunge?

Deciding whether parents or students should borrow to fund a college education depends on each family's individual circumstances. Here are some of the things you need to know before you make your decision.

## Diversification Can Help Bring Balance to Your Portfolio

There are many areas in life where people look for balance -- work and play, saving and spending, to name two. Balance also applies to investing, where diversification, the practice of holding a mix of investments, may help to balance risk and return.<sup>1</sup>

Understanding how diversification works may provide insight on the best ways to put it into practice. Financial professionals often look at a statistic known as correlation, which measures the historical tendency of two investments to move in tandem in response to market and economic developments. The closer the correlation of two investments is to 1.00, the more closely they have moved up or down together. A correlation of zero means that returns have not been related, and a negative number indicates they have moved in opposite "directions."

### Lesson From the Past

The long-term behavior of stocks and bonds provides an example of how paying attention to correlation may help reduce risk.<sup>2</sup> During the 20-year period ending December 31, 2008, the correlation between stocks and bonds has been close to zero.<sup>3</sup>

What does that mean in practice? There may be times when stocks zig and bonds zag. For example, stock investors who maintained an allocation to bond funds potentially could have limited losses during the market downturn of 2000 to 2002, when bonds performed well. Just remember, past performance is no guarantee of future results.

When discussing diversification strategies, you may want to review the correlation table below with your financial advisor. A look at the numbers may reveal strategies for building a portfolio that does not fall too far out of balance.

Correlation With Large-Cap Stocks, 1989-2008 <sup>4</sup>	
Foreign Equity	0.59
Real Estate Investment Trusts	0.58
Municipal Bonds	0.22
Cash	0.12
Government Bonds	(0.04)

<sup>1</sup>There is no guarantee that a diversified portfolio will enhance overall returns or outperform a nondiversified portfolio. Diversification does not ensure against market risk.

<sup>2</sup>Investing in stocks involves risks, including loss of principal. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price.

<sup>3</sup>Source: Standard & Poor's. Past performance does not guarantee future results.

<sup>4</sup>Source: Standard & Poor's. For the period from January 1, 1989, to December 31, 2008. Large-cap stocks are represented by the S&P 500 Index; foreign equity by the Morgan Stanley Capital International Europe, Australasia, Far East (EAFE<sup>®</sup>) Index; real estate investment trusts by the NAREIT Equity Index of all publicly traded REITs; municipal bonds by the Barclays Municipal Bond Index; cash by the Barclays 3-Month Treasury Bill Index; and government bonds by the Barclays Long-Term Government Bond Index. Foreign investments involve greater risk than U.S. investments, including political and economic risks and the risk of currency fluctuations, and may not be suitable for all investors. Municipal bonds are subject to availability and change in price. They are also subject to market and interest rate risk if sold prior to maturity. Interest income may be subject to the alternative minimum tax. Municipal bonds are federally tax free, but other state and local taxes may apply. Government bonds and Treasury bills are guaranteed by the U.S. government as to the timely payment of principal and interest, and, if held to maturity, offer a fixed rate of return and fixed principal value. Past performance does not guarantee future results.

During the 20-year period ending December 31, 2008, the correlation between stocks and bonds has been close to zero.



## College Loans: Should Parents or Students Take the Plunge?

Deciding whether parents or students should borrow to fund a college education depends on each family's individual circumstances. Given the current malaise in the credit markets, many private lenders have tightened standards and made it more difficult and more expensive for borrowers (both students and parents). At the same time, many families, facing dwindling personal assets and rising college expenses, are searching for strategies to pay the bill.

### Federal Student Loans -- Your First Stop

Whether the student or the parent does the borrowing, your first and best option for securing a loan is to go directly to the federal government. Stafford loans designed for students and Parent Loans for Undergraduate Students (PLUS) for parents are the most frequently used federal loans.

The key benefits of Stafford loans include:

- Low, fixed interest rates
- Income-based eligibility (indicated by data filed on the Free Application for Federal Student Aid [FAFSA])
- Repayment deferral until after graduation

Like many borrowing programs, Stafford loans present both benefits and drawbacks. On the upside, they allow borrowers to defer repayment until after graduation. Given the challenging economic climate, the federal government has announced an Income-Based Repayment Plan that takes effect July 1, 2009. Payments are capped for graduates whose student loan debt is high relative to income and family size. Specific criteria to qualify are available at [studentaid.ed.gov](http://studentaid.ed.gov). The cap was intended as a benefit for graduates who do not earn significant income. On the downside, Stafford loans carry annual borrowing limits that often are not high enough to cover a year of college costs.

### What Parents Need to Know

Parents who intend to fill their child's college funding gap via a PLUS loan must undergo a credit check in order to qualify. Those who are deemed creditworthy can borrow up to the full cost of attending college, including the cost of room, board, and books. The interest on a PLUS loan is variable and may change annually. In addition, PLUS loans require parents to begin a repayment schedule immediately.

For students and parents alike, borrowing through the federal education loan program, as well as through private loan issuers, offers tax deductions on interest paid.

Paying for college is a long-term commitment. Determining how to cover the costs should take into consideration a family's current financial needs as well as its short- and longer-term financial goals. Be sure to talk to your financial advisor and tax professional.

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