Outlook

A Quarterly Newsletter from Roffman Miller Associates

When does one plus one equal three?

I spoke with a client recently who asked me, “after a disappointing year like 2015, and a rough start to this one, what are you going to do differently in 2016?” My answer was, “I hope you’re not expecting anything different because we certainly are not changing the way we invest. I don’t consider a year where the market basically broke even as a very big disappointment. As a long-term investor I am prepared to experience some truly disappointing years but hopefully not too many as difficult as 2008. The good news is that our investment philosophy and disciplines over the past 25 years have helped us weather the tough times. Your finances are in good shape and you are able to meet your retirement goals.” The client’s response was “thank you, sometimes I just need a little reassurance.”

When you write a newsletter as long as I have it’s hard not to repeat yourself but after that conversation with our client it’s clear that maybe sometimes we all need a little reassurance. So if you’ve heard this before you’ll probably hear it many more times: at Roffman Miller we invest in businesses that we think have excellent long-term prospects. Companies with strong foundations and management that will do what’s best to strengthen and grow over many years. Success has come from being patient and disciplined, and those principles will guide us well into the future. No one knows with any certainty where the market is going in the short term. Having spent most of my adult life in the investment business I’ve learned not to try to predict market’s short-term direction. Instead, our team of investment professionals focuses on the companies we own, which is a lot more rewarding than guessing where the market is headed.

If you’re wondering about the origin of my question, ‘When does one plus one equal three?’ the answer is when DuPont and Dow Chemical merge and then split into three separate companies, as was announced in December. In the short run this merger will weigh on the price of both companies; but it is the longer term that really makes this combination interesting. The transition from two companies to three will probably take a few years and at this point looks like a potentially rewarding plan. We certainly have time to decide if we will keep the three separate companies or pick and choose – if I could make the decision today I would keep all three companies and give the separate management teams time to work their long-term plans.

Since I mentioned one of our companies, DuPont, I thought I would quickly mention two other companies that we’ve held for many years. Warren Buffet recently talked about his five favorite income stocks. I was happy to see that IBM and Procter & Gamble made that list because neither company has done well in the last year. Not that Warren Buffett can’t make mistakes, but it’s always nice when the greatest investor of our time agrees with our thinking. Of course there are always different opinions, that’s how the market works. Every time someone buys a stock there’s someone on the other side selling. A good example is that a well-respected professor recently called IBM a yield trap. I’m not going to mention the professor’s name because I’m not looking to pick a fight - I’m simply hoping that he will be proven wrong over time.

One of the foundations of Roffman Miller is that we do our own research. So I’m happy to report that I’ve been doing a considerable amount of research on retirement. I’m spending most of my time in Florida where I am able to observe people who are retired on a daily basis; I hope to become an expert in all the good things about retirement. If you have any questions or need advice, I will be happy to talk to you.

I wish all of you a healthy, happy, and prosperous New Year.

Sincerely,
Peter Miller
Chairman and Founder

8 January 2016

Miscellaneous News

Brokerage Statements

Every Roffman Miller client should be receiving monthly statements, either electronically or through the mail, from their broker-dealer. Please let us know immediately if you are not receiving monthly statements. You should also take some time each month to review the statements and let us know if you have any questions.

Last Chance to Contribute to your IRA or ROTH IRA

If eligible, you have until April 18th, 2016, to contribute to your IRA or Roth IRA. The maximum amount for 2015 is $5,500 with a $1000 catch up for those ages 50 and over. Call your advisor or accountant to find out more information about maximizing your tax savings with a traditional or Roth IRA.

It is also time to start thinking about 2016 contribution limits

IRA and ROTH (over 50)	$5,500 ($6,500)
401(k), 403(b) and 457 plans (over 50)	$18,000 ($24,000)
Simple IRA (over 50)	$12,500 ($15,500)

Social Security Change

On November 2nd when President Obama signed the *Bipartisan Budget Act of 2015* certain Social Security loopholes available to dual income families were effectively cut off. The "file and suspend" and "restricted application" methods that had become popular with couples and could amount to thousands of dollars more in Social Security benefits over their lifetimes will no longer be available. Fortunately, if you are already receiving benefits under "file and suspend" or "restricted application," you are grandfathered and will continue to receive the same benefits. If you're the right age and still interested in those provisions, there is a grace period before they are outlawed. So if you haven't yet filed and are 66, or are turning 66 by May 1, 2016, you should still be able to take advantage of the strategy.

For all the press this is receiving, the AARP reports that only one-tenth of 1 percent of all eligible Social Security recipients took advantage of file and suspend. And another important thing to remember, especially for dual high-earner couples, is that waiting until you are 70 before starting to collect your benefits is by far the greater way to increase the amount of money you will receive in lifetime benefits. The file and suspend method may have added thousands of dollars to your benefits, but by waiting until you're 70 to collect you could still add hundreds of thousands of dollars to your benefits.

Here is an example from Boston University's Laurence Kotlikoff, co-author of the best-selling "Get What's Yours: The Secrets of Maxing Out Your Social Security Benefits," "Say you've got a 60-year-old couple, both high earners, thinking of taking their benefits at age 62. If they go ahead with that plan, they'll get about $1.2 million in benefits (total, at present value). Before the change, if they had optimized - with one filing and suspending and the other taking spousal benefits at age 66, they would have gotten $1.6 million - but only $50,000 of that would be in spousal benefits. Waiting will still net them an extra $350,000, Kotlikoff says."

It becomes more complicated if one partner is a high earner and the other is a low earner, and each case needs to be examined on its own. The new rules do apply to divorcees, but do not apply to widow or widowers. We will encourage you to work with an experienced Social Security Agency representative as we develop your income plan for retirement.

Paulette Greenwell, Vice President

Slow Money

Since the tech boom of the late '90s there has been more and more 'fast money' on Wall Street. Fast money really doesn't have an official definition, but I take it to mean the money controlled by day-traders, momentum investors, and gamblers. All you have to do is watch the CNBC show 'Fast Money' to see that this is money in the market for reasons other than research and fundamentals.

One of the most influential companies during the tech craze was Seattle based Microsoft Corporation. In the 16 years since the company's share price peaked at nearly $60 per share (adjusted for a split in 2003), many individual investors have turned their backs on the stock.

Just about everyone knows who Microsoft is. The company was founded in 1975 by partners Bill Gates and Paul Allen. Then based in Albuquerque, they launched their first product and had 1976 full year revenues of $16,005. Seven years later, with the IBM PC operating system as their main offering, sales totaled $55 million. The company went public in 1986.

Over Microsoft's 40-year existence the world has gone through a PC revolution (remember 'The Computer' was Time Magazine's 1982 *Machine of the Year*, sandwiched between *Men of the Year* Lech Walesa, 1981, and Ronald Reagan/Yuri Andropov, 1983), a tech crash, and a rise in mobile computing that threatens the very core of Microsoft's existence, the Windows operating system for PC.

But now is not the time to worry about the future of Microsoft. Under the leadership of Satya Nadella, only the third chief executive in the company's history, recent gains in the stock price (+16.7% in 2015) may have as much to do with company fundamentals as they do with the removal of a shroud of uncertainty about the future direction of the company. It is true that the era of the PC seems to be over. As evidence of that, PC unit sales have fallen each year since peaking in 2011. But under Nadella Microsoft is perceived to have finally accepted and adjusted to the new world order of tech where mobile and cloud strategies are imperative, and where enterprise (corporate) solutions need a clear and tangible roadmap.

Microsoft's Office Suite, a perennial profit center for the company, is now a subscription service. Instead of plunking down a few hundred bucks every other year to upgrade Microsoft Word for your home computer, users are now charged an annual fee that covers major and minor upgrades on an on-going basis. This new business model is working – there are over 18 million individual subscribers to Office 365, as it's called, including me. In addition there are tens of millions more corporate subscribers. Microsoft's contribution to the cloud not only includes Office, but also Xbox and search engine Bing. But those are internal applications of cloud computing. Investors are closely following the rapid growth of Azure, a cloud computing infrastructure service deployed via 100 globally distributed data centers, serving over 1 billion customers. The company believes Azure is more flexible than competitive cloud service offerings and allows corporations to keep more of their data off the public grid.

Many investors will tell you "Microsoft hasn't done anything since the '90s." I beg to differ. 1999 *was* a good year: revenues were $19.7 billion. Net income $7.7 billion, or 71 cents per share. Fast forward to fiscal 2014 when revenues totaled over $86 billion and net income was $22 billion, or $2.67 per share. Profits in 2014 were greater than revenue in 1999! Clearly the company was doing *something* all those years, but it's not hard to figure out why people have hard feelings about the stock – the fast money of 1999 had pushed stock prices to extremes. Microsoft and a lot of other companies were simply overpriced. At some point over the past decade, however, Microsoft's valuation and clean balance sheet intersected with an attractive stock price; the dividend grew, and despite some business uncertainties it began to look like a decent investment opportunity again.

Microsoft

Part of the reason for this column on Microsoft is to remind you of all the good things about the company today; I almost left out the part about the 2.6% dividend yield and $70 billion net cash on their balance sheet. But also in part this is a story about investing in great companies for the long-run, acknowledging market cycles, and always keeping an eye on valuation.

2015 was a challenging year for investors to figure out; there were many ups and downs, but in the end the market indexes were relatively flat for the year. That doesn't tell the whole story though; the average stock in the S&P 500 was down 3.8% for the year according to research by Bespoke Investment Group. And excluding four stocks, the index overall would have been down 4.8%. As Peter mentioned, we can't tell you what the next move will be for the markets in 2016. I can't tell you what the next move for Microsoft will be. But I can tell you that we'll continue to find and research opportunities in good companies that we believe hold long-term promise for our investors.

Mark Frombach, Chief Investment Officer

Who Should Own 529 Plans, Parents or Grandparents?

Whether the owner of a 529 college savings account is the parent or a grandparent can have a major impact on a student's eligibility for federal financial aid.

FAFSA, the Free Application for Federal Student Aid, considers both assets and income in their eligibility calculation.

Assets: 5.64% of parents' assets, including parent-owned 529 plans, are factored into the expected family contribution (EFC). Students are expected to contribute 20% of assets they own outright (after a small allowance). Grandparents' assets (or any third-party's assets) are not taken into consideration and thus have zero negative impact on financial aid. So when it comes to assets, grandparent-owned 529s have the clear advantage.

However, this advantage is not enough to offset the severe disadvantage grandparent-owned 529 accounts have when it comes to income.

Income: While distributions from parent-owned or student-owned 529 plans are not reported as income for purposes of financial aid, distributions from grandparent owned 529 plans count as "untaxed student income" on the next year's FAFSA. Student income is assessed at a steep 50% rate in the EFC calculation.

For example, let's assume a grandparent withdraws $30,000 from a 529 plan. Assessed at 50%, this distribution would reduce the student's financial aid eligibility by up to $15,000. By comparison, a parent owning this $30,000 in their 529 account would only shrink the student's aid by a maximum of $1,692.

One way a grandparent can avoid this negative consequence is to use their 529 assets for their grandchild's senior year. Ideally the grandparent waits until the parents have filed for financial aid the last time, during the student's junior year. Since the student's final FAFSA has been filed, the student income going forward is irrelevant.

Another option is to transfer ownership of the 529 account to the parent. Of course, by doing so the grandparents are giving up control of the account. Not all states allow ownership changes; if your state doesn't allow ownership changes you can transfer the account to one of the vast majority of states that does and then make the ownership change.

Of course, the grandparent could always gift money to the parent (or pay tuition directly to a university) and avoid the hassles of timing withdrawals or transferring ownership at some later date.

Finally, I would like to mention two things. One, many private and some public colleges grant their own aid and use different assessment formulas. Two, please keep in mind that this is a high-level review of what can be a complex topic, so please consult your CPA who understands your unique set of circumstances and the impact of your choices.

Kevin Cooke, Investment Manager

Family Addition

Congratulations to RaRa and her family on the birth of her son Noah (pictured, right). Noah was born December 3rd. He weighed in at 6 lbs, 8 oz, and measured 19 inches. Both mom and baby are doing well. Many thanks to Shannon Sainato who is filling in until RaRa returns to work on January 20th.

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