

## DO YOU REALLY KNOW WHAT'S IN YOUR BOND PORTFOLIO?

Let's face it, stocks are just sexier. I can't recall ever hearing someone at a cocktail party talk about the killing they made in bonds. Most people own bonds to counterbalance the "risky" part (stocks) in their portfolio. But investors shouldn't just assume the bonds or bond funds they own are "safe"—bonds carry risk too, and uncovering the potential risks lurking in one's bond allocation have in many ways gotten harder, even though bonds have performed nicely this year as interest rates have declined.

For starters, let's review some of the fundamentals everyone should understand about bond risk. Simply speaking, bonds (and for our purposes we will focus on corporate bonds) have two key risk factors that we try to manage—**credit risk** (the risk of the bond issuer defaulting) and **term risk** (the time period until a bond's maturity).

It stands to reason that the longer the time until a bond matures, the more risk it carries. The unknowns (future solvency, future economic conditions, future interest rates) have more risk over 10 years than 5 years so all things being equal a 5-year bond is less risky than a 10-year bond.

Credit rating agencies (CRAs) assess bond issuers credit-worthiness through ratings, with scores from AAA (the best) to C (in default). "Investment grade" bonds are those with BBB ratings or higher.

With interest rates and bond yields low, some investors have either knowingly or unknowingly bought riskier bonds (either lower quality, longer maturity or both) in an effort to capture more income. Over the last decade, the proportion of investment grade bonds rated BBB has increased from 32% to 47%. We would contend that this has increased the risk for investors—especially for clients of brokers or wealth managers who tilt bond allocations toward the lower end of the investment grade spectrum.

One challenge for do-it-yourself investors is that one cannot rely on CRAs alone. Market prices tend to reflect problems with bonds before CRAs do. For example, earlier this summer Moody's downgraded the credit rating of Boeing, citing issues related to the 737 Max jet. In the week prior to Moody's downgrade the price of Boeing bonds fell slightly (about .7%) representing about 20% of the bond's estimated annual income.

Over the last four years, our bond strategy has been one focused first and foremost on safety. We strive to position our bond allocations in such a way so that when the equity markets encounter turbulence, the "safe" part of our portfolios will not suffer the same fate. While bond yields of 2-3% aren't very appealing, we know the dangers that can occur in bonds should we be overly aggressive. As Warren Buffett says, "you only find out who is swimming naked when the tide goes out."

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## SUMMER VACATION: ONE FAMILY'S ADVENTURE IN FREE FUN

Years ago I loved to watch *Inside the Actors Studio*—I seemed to learn a great life nugget from each episode. One takeaway from Mike Myers' appearance that I've remembered was the importance of creating free fun. His quote was something along the lines of "creating your own fun is always more memorable."

As a parent I explored ways to create family traditions that were indirectly exercises in free fun. We usually engage in these activities on our summer vacation. Let me share three creative ways we've done that:

### THE NAME GAME

We got this idea from friends of ours. You can play with 6 people, but 8–14 is the optimal number. Everyone writes a name (proper noun) on a scrap of paper and puts it in a bowl. One person reads each of the names aloud, just one time. One person starts by trying to guess the name submitted by someone in the group. If they guess correctly, that person becomes part of their team. If the guess is incorrect, then that person gets to guess. Play continues until the last person to remain unguessed is the winner.

### TEAM SUPPERS

Great for large families. We divide our family into 3, 2 person teams. Each team is responsible for preparing dinner one night

during our vacation. We've also added a "signature cocktail" in recent years. You'll be surprised how fun this makes family dinners—and preparation doesn't fall to one person.

### BEACH GOLF

An easy (and free, if you have golf balls lying around!) variation on bocce ball and corn hole. On the firm sand of a beach you dig 6 small holes (5–7" wide and 3–4" deep), 3 at one end and 3 another 25–40 feet away. Divide into teams and each team member rolls 3 balls trying to get them into the holes at the far end. We've introduced this game to several other families and have had numerous beach walkers stop and take notice.

**Great ideas are where you find them,  
and free fun is more memorable!**



## PUTTING JOHNNY ON THE PAYROLL

We are asked from time-to-time whether our clients can pay their children or whether their child can open a Roth IRA. The IRS allows parents to pay a child up to \$12,000 per year, with neither the parent nor the child owing any income tax. Parents who are self-employed or own a business can also deduct the wages paid to their child.

A child can contribute to a Roth IRA, provided they have earned income. For example, I've paid my children a small wage to scan, file and make copies around my office. In addition, I offer to match whatever they contribute to a Roth IRA, up to their earned income. This strategy allows the child to keep half their earnings to spend as they desire, helps instill the habit of paying themselves first, helps teach them about investing and builds a

nest egg for them to use down the road. One of the benefits of a Roth IRA is that it can be used prior to age 59½ without penalty for a first-time home purchase.

For a child that contributes \$5,000 a year at age 15, they'd accumulate over \$30,000 by the time they graduate from college.

We love to help instill sound financial habits. Give us a call if you'd like to learn more!



# SHOULD YOU GET AN “EXECUTIVE” PHYSICAL?

As we age, we’re more appreciative of good health. The nature of our mortality risk changes as we age. Prior to age 45, mortality is more likely to occur from an accident. After age 45, health related deaths (cancer, heart disease) become the common cause. A friend recently decided to undergo an “executive physical” in hopes that he could develop a game plan to live a healthy and vibrant life for the next 30 years. As he half-jokingly said to me after his EP, “I’ve gone from living to eat to eating to live.”

Given the ever-increasing complexity of our health care system, is it worth the expense to get an executive physical (EP)?

An EP normally is a day long preventive and diagnostic exam which assesses lifestyle, genetic risk factors and improvements to behavior. Among the tests typically administered that go beyond a normal annual physical are a resting EKG, a cardiac stress test and depending on one’s sex and family history, colonoscopy, bone density scan, VO2 max test, sleep test and more extensive lab work.

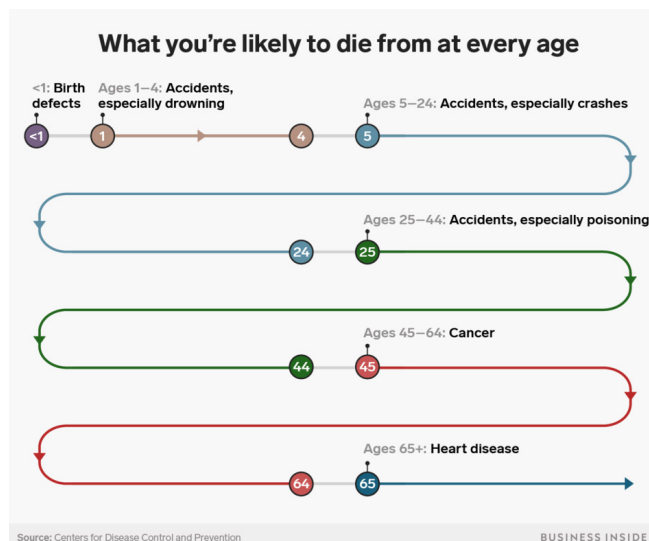
Most insurance plans do not cover the cost of an executive physical, which typically cost \$3,000–\$5,000.

I spoke with several physicians to get their perspective on the value of an EP. One suggested the value of an EP depended on one’s commitment and engagement level during a routine physical. “Most patients get counseled on diet, weight and exercise—but too few change their habits or adopt a new lifestyle,” one doctor told me. “Too many people define ‘health’ as the absence of disease. Will paying more for essentially the same advice increase the likelihood of behavior change?”

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Another physician told me, “If a patient isn’t symptomatic, but has a family history of a particular disease the EP may be beneficial. It may uncover something or conversely determine that the patient has a low probability of occurrence.”

Physical health is similar in some ways to fiscal health—the habits to achieve it aren’t a mystery, but instilling the proper habits to achieve it can be elusive.







## BEHIND THE SCENES

**Mike Palmer** was interviewed by *Spectrum News* on stock market volatility.

**Ark Royal Wealth Management** was recently recognized by *Financial Advisor* magazine as the top RIA firm in NC in the under \$100 million AUM category for the second year in a row!

*“Wealth is the ability to fully experience life.”*

HENRY DAVID THOREAU



### *The* CORNERSTONES *of* ARK ROYAL WEALTH MANAGEMENT



**To nurture a culture that puts our client's interest first—always**



**To be truthful at all times, to be intellectually honest with ourselves  
and with our clients, even if it isn't what they want to hear**



**A commitment to lifelong learning, and a passion for applying  
our wisdom efficiently and effectively every single day**



**Align what you say, what you do and what you think to honor  
yourself, your family and our firm**

