Financial questions? We've got answers

By Brent Hunsberger, The Oregonian

October 18, 2009, 7:15AM

Time for an It's Only Money mash-up. Because sometimes there's just a lot to chew on.

This mash-up is about wills, stocks and bonds. That's not to say it's about the death of stocks or bonds. We're not that bearish, even with the return of rain.

The Dow hit 10,000 last week. Now what?

Who knows? Stocks appear to be overvalued relative to their expected earnings. But the government is setting interest rates so low that equities remain a very attractive place to invest money.

"Is the market overdue for a correction? Yes," says George Hosfield, chief investment officer for Ferguson Wellman, a Portland firm managing $2.2 billion in assets. "Could it correct materially? Yes. Could it correct after it runs up another 20 percent? Yes."

If you got out of the market last fall and haven't gotten back in, you've missed a huge opportunity to recover much of your losses. If you're still not in, you should probably wait for the market to decline again, as many predict it will, Hosfield says. Or ease back in slowly.

"It doesn't have to be all or nothing," he says. "If you're nervous now, take a little out (of stocks) and hope it wasn't your worst trade. A little. Things are getting better, not worse."

At a minimum, take a look at your asset allocation targets. Your stocks-bonds balance could be tipped too heavily toward stocks now. If so, consider realigning it.

"Maintaining an appropriate asset allocation and not monkeying it around very much is the best course," says Barnes Ellis Jr. of Baker Ellis Asset Management in Portland.

An editor at The Oregonian asks: Is the bond market really the safe haven everyone thinks it is?

Probably not -- for the long term, at least. Here's why.

When stocks hit their low point in March, some money managers noted, accurately, that bonds generally had outperformed stocks over the past 40 years. But there were two big reasons for that, at least one of which we won't see going forward.

First, double-digit interest rates in the 1970s and early 1980s led to unusually high bond yields at that time. (The **federal funds rate**, the interest rate at which banks lend money to one another overnight, hit 20 percent the first week of 1981; banks' **prime lending rate** hit 21.5 percent the last week of 1980.)

Investors who bought a 30-year Treasury bond in **February 1982** were rewarded with a handsome yield of 14.6 percent, according to treasurydirect.com.

Second, declining interest rates and low inflation over the past 25 years were good for bond prices. When interest rates decline, bond prices increase.

The first could happen again, preferably to a lesser degree. Experts say inflation will jump in coming years because of all the money the government is pumping into our economy to stimulate it.

The latter really can't. Interest rates are about as low as they can go.

"This could be the worst time for buying bonds I've ever seen," Ellis says. "The government is effectively driving money back into risk assets by effectively reducing interest rates to zero."

When you invest in a bond, returns are reaped two ways. The first is on the regular (often semiannual) interest payment it promises. The second is when its purchase price goes up.

When interest rates go up, bond prices decline. For bond prices to continue to increase as they have, interest rates would have to dip into negative territory, as **Roger Ibbotson** and Peng Cheng of Ibbotson Associates noted in Morningstar Advisor. That means bondholders would actually pay money to keep their bonds.

If you think that will happen, I've got some stardust to sell **you**.

What's more, the fixed payments (or coupons) of today's bonds lose value as inflation increases.

So, it's hard to see how bonds could be the great investment they were. Prices probably won't increase, so you won't earn much from selling a bond. In fact, you could lose money. You'll have to rely on a bond's yield, or regular payment stream. And those yields right now are very low. The 30-year Treasuries **auction last week** yielded 4 percent.

"Bond returns will not be what they have been going forward," says Paul Vermilya, president of Compass Investment Advisers in Portland and a former bond trader for First Interstate Bank. "It is impossible mathematically."

Baker Ellis has 15 to 20 percent of its clients' money in cash or short-term securities as the firm waits for interest rates to increase to buy longer-term bonds. "Nobody will want your bond that earns 3 percent when inflation is 4 percent," Ellis notes.

That said, bonds or bond funds still have a place in your 401(k) or investment portfolio because they'll soften the blow of any future wild swing in stocks. Which will happen again. Guaranteed. Just keep a closer eye on your bond funds than normal should interest rates shoot up suddenly, or hedge with inflation-protected bonds (TIPS) or a gold fund, Vermilya says.

Dorothy Jansen of Gresham read It's Only Money's August column on wills and wondered: Is a handwritten will recognized in Oregon, as long as it's signed in the presence of two witnesses and notarized?

Yes it is, says David Streicher, an estate planning attorney and CPA at Black Helterline in Portland.

In fact, state law says, "The will must be made in writing. It need not be written by the testator." (Testator, for you non-estate attorneys, is the person leaving the will.) "It may be written in any language, by hand or by any other means."

The key is having two witnesses.

"It doesn't matter whether the will is written longhand or typed," he said.

Incidentally, wills drafted in Oregon need not be notarized, he says. They simply need to be signed by two witnesses who saw each other witness the will, according to the Oregon State Bar.

That prompted other questions: What's the difference between a holographic will and a handwritten will?

A "holographic will" normally refers to a handwritten will signed in the presence of no witnesses, Streicher says. Some states allow such wills, figuring that you don't need witnesses to authenticate it; you can just match the handwriting.

These types of wills are valid in California. Oregon, however, does not recognize them if they're drafted here.

Is a holographic will drafted in California valid in Oregon?

Yes, says Valerie Vollmar, a law professor at Willamette University whose estate forms are widely used by Oregon attorneys. Oregon recognizes holographic wills drafted in states that allow them.

Why do about half of U.S. states allow holographic wills?

"The concern is that people will think it's too expensive or too complicated to go and have a lawyer draft a will for them," Vollmar says. "The thought is it's important for people to be able to write down what their wishes are at their death. This is one way for people to do that.

"The problem is," she adds, "they may not be very good drafters."

Brent Hunsberger does not give individual financial advice but welcomes comments or questions about his column and blog.