MONEY TALK

Editor: Dixie Butler, CFP®, CDFA™, EA **Summer/Fall 2015**

A Case for Investing in Emerging Markets

An emerging market economy or "EME" is loosely defined as an economy with low to middle per capita income. Countries that are referred to as an EME can be small or large. As an example, even though China is a very large country and somewhat of a dynamo in the areas of natural resources and people resources, it is considered an EME because it is in the throes of economic development and various reform programs. China is emerging by opening up its markets to the global scene — emerging from a closed economy to an open market economy. Among other challenges, China is trying to reform its exchange rate system and attract local and foreign investment. They are "in transition," and hence not stable, which increases an investor's risk. The above explanation holds true for all EMEs — not just China.

Adding EMEs to an investor's portfolio equates to "taking on more risk and hopefully cashing in on where the growth is today." It is always difficult to pick winners — especially when there are so many types of risk to consider when investing in an EME versus investing in the good ole USA. Political risk is the big kahuna. If a country falls back into its prior economic reform policies and open capital markets become threatened, investor panic could be its downfall. Because the risk of investing in an EME is higher than that of an investment in a developed market, panic and knee-jerk reactions are far more common.

Diversifying a portfolio by using an asset allocation strategy is the basic premise of how U.S. Advisors structure their client portfolios. Emerging market mutual funds are used in approximately 40% of our portfolio models. The overall percentage of emerging market funds used is 5 to 7 percent, and our fund picks are well diversified by countries and companies.

By investing in EMEs has U.S. Advisors actually added risk to their client's portfolio, or have they diffused risk? Dixie Butler would argue that when investing in EME mutual funds risk has been diffused from the portfolio as various asset classes often do not move in tandem, nor do the individual emerging countries move in tandem with one another. EMEs have their own political and social issues specific to their country and not necessarily specific to other EMEs. These issues and other problems can affect the stability of their individual capital markets without affecting others.

When an investor places a bet on a specific country, or just a few countries, their risk increases significantly. If their bet goes south,

they lose everything. Investing in a well diversified EME mutual fund is probably a safer way to go, which is the path that U.S. Advisors chooses.

Even though the process of emergence may be slow, difficult, stagnate, and might even become totally unglued, diversifying your investment dollars among different countries and different types of companies makes sense. According to Dixie Butler, this is where "diffusing risk" comes into play — through diversification, and yes even with emerging market investments.

With risk comes the possibility of greater reward, and conversely greater losses could occur. No one and no place is safe from the "R" word! Guts and a long-term perspective with a well diversified portfolio is key.

IMPORTANCE OF LIFE INSURANCE

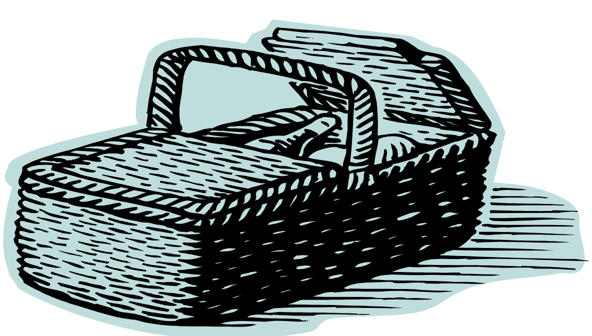
Life insurance is one piece of the financial planning puzzle that is sometimes overlooked or not calculated properly. Having the appropriate amount of coverage is critical to the financial security of those who financially depend on you. When trying to evaluate how much coverage you will need, first ask yourself **"who depends on me financially (spouse, children, parents, partner, etc.), how many years will this financial dependence last, and approximately how many dollars will be needed to fulfil my financial obligations."** The next part of the equation which must be considered is that you could die tomorrow. When purchasing life insurance, people often have a tendency to think in terms of dying from old age. Wrong! If we all knew that we would die from old age, then there would be no need for life insurance. Your financial plan would simply take your ultimate demise into consideration, hence all dependents would be accounted for and financial provisions would be made in your plan, and most likely with little or no insurance (since the evaluation would be based on "old age" for yourself and dependents alike). Life insurance in its simplest form, as with all types of insurance, is for the **unknown.**

Asset Allocation

When constructing a portfolio using an asset allocation strategy, asset classes take priority over individual asset selection. Asset allocation aims to balance risk and reward by allocating a portfolio's assets according to an investor's financial and investment goals, tolerance for risk, and investment time horizon. The three main asset classes are equities (stocks), fixed-income (bonds), and cash. Within these three broad asset classes are many "sub-classes," and in the case of mutual funds various "management styles."

There is no simple formula for establishing the right asset allocation for every individual, or for every type of market behavior. It is indeed a difficult task. However, the structure of the asset allocation strategy can be built, as stated above, by taking into consideration your age, your appetite for risk, and your investment objectives.

The old adage of not putting all your eggs in one basket is a consideration in attempting to reduce portfolio risk. Beware, as the basket has many compartments and considerations.



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Money Talk is a free publication, published and distributed semi-annually by U.S. Advisors, Inc.

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About Dixie Butler — she is a Certified Financial Planner, a Certified Divorce Financial Analyst, and is an Enrolled Agent, entitling her to practice before the IRS. She has been in the investment and financial industry for over 25 years.