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**MENTOR**
C A P I T A L

September 2009

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Mentor Monthly Missive

In this issue:

- 'No thanks' to leveraged ETFs
- Beware timeshares
- Money-management tips for college graduates
- Limited-time offer – receive commission-free electronic equity trades

'No thanks' to leveraged ETFs

Leverage – using borrowed money to juice investment returns – is a form of market-timing that we believe is not only dangerous, but unsuitable for individual investors.

Members of Mentor Capital's advisory team never employ leverage when working with client portfolios.

Investors leverage their investments by using margin. Perhaps they believe that the stock market is poised for big gains, so they put up their current investments as collateral to buy more investments. When markets rise, leverage can enhance returns. When they fall, leverage can worsen losses. It's a risky game that most individual investors shouldn't play.

Another form of leverage recently has gained popularity in the financial markets: Exchange traded funds (ETFs) that internally employ leverage. These are stock or bond funds that are designed to compound the return of a particular index by using borrowed money. The problem is, most investors using these vehicles don't understand them and aren't aware of their risks.

For example, an investor may assume that a leveraged ETF will deliver double the return of an index. But a closer look at the prospectus reveals that it promises twice the *daily* return of an index. This is not monthly, or even annually. These investors are making an assumption about compounding that is simply false. In addition, compounding a negative return always has a more pronounced impact than compounding a positive one.

Our advisors do make wide use of stock and bond ETFs:

- They can be very efficient. Expense ratios are sometimes less than one-tenth those of actively managed mutual funds – the result being that more returns accrue to the investor, rather than fund management.
- They are style specific and style consistent. Because we use asset allocation models designed to enhance returns and minimize risk, it's important to know that the ETF we buy today will hold the same-style assets next year or five years from now.

But we stay away from leveraged ETFs and their cousins, inverse ETFs. Even most companies that offer leveraged ETFs say that they aren't suitable for long-term investors. When we invest in stocks or bonds for our clients, we do so under the assumption that they will be held more than short-term. We believe that a diversified, properly allocated portfolio of stocks and bonds will provide good returns over a period of years, but we don't pretend to know which way the markets will turn this week or next.

If you would like to know more about how we use ETFs in client portfolios and how our asset-allocation models are structured, call one of our advisors.



Beware timeshares

We've never been big fans of vacation timeshares – buying the right to use a resort property regularly for a period of time.

We generally don't like them because they're long-term commitments that can sour when lives change – which they often do. What seems like a good deal today may become an albatross tomorrow. Also, timeshares are somewhat inflexible, and you may not be able to go where you want, when you want.

The biggest issue for many is maintenance fees. This is a monthly or annual charge the timeshare owner is contractually obligated to pay to ensure that the resort is kept up-to-date and well-maintained.

Maintenance fees often run between \$400 and \$1,200 a year. One of the worst contracts we've seen requires payment of maintenance fees for 99 years. If the timeshare owner dies, the estate, as the new owner, is obligated to continue paying.

Timeshares are not investments, although they're often sold as such, so don't expect any appreciation. In fact, according to the Timeshare User's Group, timeshares that actually sell on the secondary market bring only between 30% and 50% of the price initially paid.

So if in spite of the drawbacks you're still sure you want to buy a timeshare, read the fine print. If you're not comfortable with the terms and not certain that you want to enter into a long-term contract, plan your own vacations.

If you already own a timeshare that you no longer use, you may be able to negotiate a severance of the contract – but that can be expensive. There are services that will do this for you, but for a substantial fee. Call for details.



Money-management tips for college graduates

It's tough being a 2009 college graduate. The unemployment rate for young college graduates, at 5.9%, is the second-worst on record – barely below the 1983 rate of 6.2%.

Finding a job is only the first challenge for a recent college grad. The economic outlook continues to be uncertain. Plus, there are all kinds of details new graduates have to deal with: paying off student loans, opening bank and retirement accounts, choosing health insurance, finding an apartment, buying a car, and figuring out how to save and invest.

It's not easy to master money management during the best of times, and it's especially hard to navigate the challenges in a downturn. Still, many of the same basic principles apply in good times and bad. This is a great time to share some tips with recent graduates. They can pay dividends for a lifetime:

Start Saving Early

Whether you call it an emergency fund or just reserves, having cash in the bank is important at any time. In the bigger picture, having savings also means much more than just having money in an account. People who save, for the most part, have learned to live within their means. Most likely, they have a handle on how to budget and how to shop carefully.

Read the Fine Print

Nearly every transaction these days seems to require a written agreement, from leases to health-club memberships to cell-phone services. You'll learn quickly about the costs buried in the fine print once you miss a payment or find yourself on the hook for a \$200 termination fee for breaking a cell-phone contract. To avoid that headache, ask

yourself some key questions. How can you end this agreement? How can the other side terminate the deal? What exactly will you be paying and when? And what happens if a payment is late or missed? Knowing the significant details will help you make better decisions and avoid much grief later on.

What is the Total Cost?

Over and over, salesmen will try to lure us into buying a nicer car or house or taking on a longer loan by touting the monthly payment. But if you want to keep more of your hard-earned money for yourself, calculate the full cost including interest and fees before weighing the monthly bill.

Debt Must Be Managed

Taking on some debt can sometimes pay off, such as when we borrow to buy a home or invest in education. At times, we need to pay off a major purchase or medical bill over a few months. But while debt can be useful, more often than not, debt is a continuing drag on our finances that limits our choices. Use email or text message alerts to remind you when the bill is due and alert you if you are near your credit limit. Pay your bill on time and in full every month.

There Is a Permanent Record

It's not your academic transcript that will stick with you, but how you manage your money. Credit scores, calculated by credit bureaus based on how much debt you have and how well you manage it, will follow you through your adult life. Over time, that score will affect how much you can borrow, the interest rate you'll pay, what you'll pay for insurance, whether you can rent the apartment you want and sometimes whether you get a certain job. A good credit score is an asset that will help you get ahead financially.



Limited-time offer – receive commission-free electronic equity trades

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