



HARRISON LAZARUS ADVISORS  
*GIVING LIFE TO YOUR FINANCES™*

# Chapter 1 – The Financial Assessment

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It doesn't matter where you are in your financial process, at the beginning, the middle or the end, if. Whether you have a penny or a million dollars to your name, the important thing is where you want to go. Think about what you want and more importantly, why? Here might be a few reasons:

- a. You want to retire someday soon,
- b. Perhaps you want a new car or home,
- c. Maybe some money for your children's' education.

Let's say you are starting this process at the beginning of the year. You don't want to just rush in. Instead, think about what you want have at the end of the year and then begin looking at where you are now and how you are going to reach your year-end goal. As January rolls on, start gathering some of the relevant documents you receive in the mail:

- 1 Annual account statements
- 2 Forms 1099, 1098 and W-2.

For the first item regarding annual account statements, let's say you have \$10 thousand in a money market account earning 1%<sup>1</sup> interest per year. Assume you don't need the money anytime soon (or at least not until next year). Why not move that money into a savings account earning 2% interest per year. That's \$200 in interest per year, twice as much as the checking account earning \$100 @ 1% year - I'll take an

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<sup>1</sup> This is not the actual current rate; it is a simple percentage for illustrative purposes.

extra \$100, how about you? Let's take this example a step further and assume you don't need the money for a couple years - perhaps you are saving for a couch or a car. Why not move that money into a bank checking account earning 4% interest per year. That's \$400 in interest per year, four times as much as the checking account earning \$100 @ 1% year - I'll take an extra \$300, how about you?

Here are a few ways to boost your returns:

1. Begin a money market account at [https://www.paypal.com/us/cgi-bin/webscr?cmd=\\_upgrade-interest-marcom&outside=1](https://www.paypal.com/us/cgi-bin/webscr?cmd=_upgrade-interest-marcom&outside=1) (.68% Annual Percentage Yield (APY) rate as of 2/5/09)
2. Open a savings account at [http://home.ingdirect.com/products/products.asp?s=Orange SavingsAccount](http://home.ingdirect.com/products/products.asp?s=OrangeSavingsAccount) (2.20% APY rate as of 2/5/09).
3. Start a checking account at <http://providentchecking.com/> (3.76% Annual Percentage Yield (APY) rate as of 2/5/09)

These are recommended because of their high yield and flexibility in addition to the ease to transfer funds in and out of your existing accounts, plus no minimum balance is required. However, if federal deposit insurance corporation (FDIC) coverage is important to you, then stick with the 2<sup>nd</sup> and 3<sup>rd</sup> options (e.g., savings and checking accounts) because money market accounts are not insured.

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Let's take this example a step further and assume you don't need the money for 5 years or more - perhaps you are saving for a house. Why not move that money into a bond and/or stock mutual fund account earning on average 11% interest per year. That's a \$1,000 more per year than in the checking account earning \$100 @ 1% year- I'll take an extra \$1,000, how about you?

But before you invest all your money seeking a 10% average annual return, ask yourself a few questions:

1. Why are you saving money? Education, buying a house, retirement, etc.
2. When might you need to access those funds?  
Emergencies, recession, or maybe you won't need to touch your funds.
3. What type of investment is going to integrate your timeline and goal into wealth? A money market, bond, or mutual fund

Once you have answered these questions, you can determine the amount of risk you are willing to take. The longer the timeframe, the more risk you can take and still meet your goal. The shorter the timeframe, the less risk you can take. Complete the following five questions to assess your risk tolerance.

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**Score: 19 - 25 = Growth Investor** - You may be able to tolerate significant short-term ups and downs in your account value to enjoy potentially higher returns.

For more risk and higher returns, stocks are a more likely choice. For less risk and lower returns, bonds are a more likely choice.

### *Investing in stocks and/or bonds*

The main difference between stocks and bonds is your role as an owner or a lender.

### *Stocks*

As a stockholder, you are an owner, who shares in the profits of the company owned through dividends. Your owned shares may also increase in value, which you can capitalize on when you sell the shares. On the other hand, they may decrease in value, and you can lose money upon sale if the share price is less than the purchase price.

Take a look at the example in Table 1-1, stocks and bonds don't just automatically go up 10% per year, they go up and down every day, week, month, year at different rates. This is why it's important that you determine the appropriate investment mix for you. The biggest value to you is to be in the market.

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## *Bonds*

A bond is a debt security, similar to an I.O.U. When you purchase a bond, you are lending money to a government, municipality, corporation, federal agency or other entity known as the issuer. In return for the loan, the issuer promises to pay you a specified rate of interest during the life of the bond and to repay the face value of the bond (the principal) when it “matures,” or comes due.

Among the types of bonds you can choose from are: U.S. government securities, municipal bonds, corporate bonds, mortgage and asset—backed securities, federal agency securities and foreign government bonds.

Because bonds typically have a predictable stream of payments and repayment of principal, many people invest in them to preserve and increase their capital or to receive dependable interest income.

## *Choices, choices, choices*

With thousands of stocks and bonds to choose from, how do you make a good choice? The most effective and efficient way is to buy a mutual fund or Exchange Traded Funds (ETF) which are managed by investments companies that pool your money with thousands of other investors like yourself and invest it in stocks, bonds and other securities for you. Buying

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a mutual fund or ETF (vs. buying individual stocks or bonds) benefits you as follows:

1. More diversified portfolio – Most mutual funds own several hundred stocks and/or bonds. Proper diversification allows the fund to achieve the highest return at the lowest risk given its objectives.
2. Professional management – Fund managers and their teams spend their days calling, meeting, corresponding and researching their investments held through their funds to verify they're meeting the fund's (and ultimately your) expectations.
3. Low fees – Most charge a nominal management fee (.2% - 2% of invested assets) that cover the costs of performing the services in step 2. This cost is significantly lower than the amount of time, money and effort it would take you to create a similar diversified portfolio.
4. Accounting – Most mutual fund companies automatically keep track of your purchases, cost basis, sales and gains/losses and send this to you monthly, quarterly or at least annually for your tax returns. In addition, the Securities and Exchange Commission and accounting firms audit the company's records and disclosures.
5. Varied investments – This includes money markets, bonds, stocks, growth, value, income, growth & income, small cap, large cap, blended, hybrid, asset allocation, sector, specialty, socially responsible, U.S., global, international, and even funds of funds. Giving you a wide range of options to choose from.

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6. Returns – You will not make a financial killing in mutual funds, but you are also not likely to get financially killed either.

This last benefit about choices can also be overwhelming because there are around 10 thousand mutual funds to choose from and it is difficult to choose just one of them. Here are a few recommendations:

1. Bond fund – Less potential long-term return with less year to year fluctuations. Fidelity Capital & Income, Vanguard Short term Investment grade or GNMA bond funds are some examples.
2. Blend of stocks and bonds – This is a fund with a mixture of bond and stocks. Vanguard Wellington or Oakmark Equity Income are good examples.
3. Stock fund – More potential long-term return with more year to year fluctuations. Vanguard Total Stock Market Index is an example.

You don't need to make it complicated to generate a decent return over the long term. As you get more experience you can add more funds or use ones for different purposes, but if you have more than 10 funds, you probably have too many. This is true whether you have \$1,000 invested or \$1 million.

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## *Other investments*

Investments I generally don't recommend are precious metals, collectibles, annuities, limited partnerships, time-shares, cash value life insurance, hedge funds, commodities, and CDs because they don't make good investments for most people. However, they are profitable sales items for sales people and that's usually why they promote them heavily - not because it is in your best financial interest but because it is in theirs.

## *Getting organized*

Anytime is a good time to organize your finances and an exceptionally good time is January and February when you receive your tax forms 1098, 1099, and W-2's.

These forms help for 3 reasons:

1. W-2's tell you how much you received and 1099's tell you how much you spent on your mortgage,
2. They are a report card for how you did during the past year.
3. Those forms give you an opportunity to organize your tax records so you are ready to prepare your tax returns (discussed in the next chapter).

1098's tell you about your largest expense. These forms are sent to you by financial institutions if you borrowed money to pay for your condo, loft, or home and how much interest it cost

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you. 1099's tell you about your income. This form puts in black and white for all the interest, dividends, capital gains or other unearned income you earned during the year.

The last form is the W-2. This reports your wages, any taxes withheld and other items we'll talk more about in chapter 2.

Next time you receive a statement in the mail, spend a minute or two and think about what you want it to look like in the future (1 year, 2 years, 5 years). Adjust it if necessary to help you meet your desired objective. Remember the overall objective is not to work for wealth; it is for your wealth to work for you.

### *Getting it automated*

With the advance of financial services on the internet, you can now see the big picture with all of your assets, liabilities, income and expenses in one place. There are online money management tools, which keep your transactions and account balances automatically up-to-date. This can be done for free at a several web sites:

1. <http://www.harrisonlazarus.com/login.html>
2. <https://www.mint.com/login.event?task=S>, or
3. [https://moneycenter.yodlee.com/moneycenter/mfaregistration.moneycenter.do? flowId=mfaregistration&c=csit key %3AVZI14EfWF4rGSHQ1F6NEZWFU%2Bo8%3D&l= flowId:](https://moneycenter.yodlee.com/moneycenter/mfaregistration.moneycenter.do?flowId=mfaregistration&c=csit_key%3AVZI14EfWF4rGSHQ1F6NEZWFU%2Bo8%3D&l=flowId)

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Of course, if you prefer not to have your financial information online, you can buy software at:

1. <http://quicken.intuit.com/?src=www.quicken.com#> or
2. [http://www.microsoft.com/money/ProductDetails.aspx?pid=004&active\\_tab=Compare](http://www.microsoft.com/money/ProductDetails.aspx?pid=004&active_tab=Compare)

Whatever you choose, these applications can help you to get and stay organized, to better understand your current financial picture and build one that you desire.

### *Why you are doing this*

Take another look at the Power of Compounding worksheet on the next page. You can see that even small savings can make a huge difference over a relatively small period of time. The more consistent you can be in saving, the more opportunity you will have to see your money grow. Even a small amount will allow your capital to grow much faster than if you are saving nothing. Wherever you are, starting now will not only help you build a fortune, it will save you one too, and who doesn't like a two-for-one deal?

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## Power of Compounding

<u>Day</u>	<u>Amount</u>
1	\$0.02
2	\$0.04
3	\$0.08
4	\$0.16
5	\$0.32
6	\$0.64
7	\$1.28
8	\$2.56
9	\$5.12
10	\$10.24
11	\$20.48
12	\$40.96
13	\$81.92
14	\$163.84
15	\$327.68
16	\$655.36
17	\$1,310.72
18	\$2,621.44
19	\$5,242.88
20	\$10,485.76
21	\$20,971.52
22	\$41,943.04
23	\$83,886.08
24	\$167,772.16
25	\$335,544.32
26	\$671,088.64
27	\$1,342,177.28
28	\$2,684,354.56
29	\$5,368,709.12
30	\$10,737,418.24

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