MARKET RECAP

After the strong performance in the first quarter of 2013, the domestic equity markets continued to advance but experienced some instability during the second quarter. Stocks, as measured by the S&P 500 Index, rose 4.31% in the months of April and May, only to drop 1.34% in the month of June. Overall, the S&P 500 Index captured 2.91% in gains for the quarter ended June 30, 2013. Despite the mixed performance in the second quarter, the S&P 500 is up 13.82% on a year-to-date basis.

Smaller U.S. companies, as measured by the Russell 2000 Index, gained 3.08% for the three-month period and are up 15.86% year to date. Over the second quarter, Large Value stocks posted higher returns than Large Growth stocks, and Small Growth stocks outperformed the Small Value stocks. On the international stage, domestic markets continued to outperform foreign markets, as the MSCI EAFE index posted a loss of 0.98%. The MSCI EAFE is up 4.10% year to date, and the immediate future of the international markets remains uncertain with the financial turmoil caused by the European sovereign debt crisis and the recent increase in volatility in the emerging markets.

After an unimpressive first quarter, the Barclays U.S. Aggregate Bond Index returned -2.32% over the second quarter and -2.44% year to date. The Fed’s continued easy monetary policy and the most recent bond-buying program have driven the interest rates down to historic lows over the last few years. As the interest rates have bottomed out, bond prices have also reached new heights, and are experiencing downward pressure. This impact is shown in the latest negative returns of the Barclays U.S. Aggregate Bond Index. The current low interest rate environment has also contributed to the latest “yield chase” in the fixed income markets, as investors have gravitated toward riskier assets in search for higher returns.

The chart below shows the major index and style category returns for the quarter, year-to-date, one-year, three-year, and five-year time periods ended June 30, 2013:

<table>
<thead>
<tr>
<th>Index/Category</th>
<th>2Q13</th>
<th>YTD</th>
<th>1YR</th>
<th>3YR</th>
<th>5YR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Barclays Agg</td>
<td>-2.32</td>
<td>-2.44</td>
<td>-0.69</td>
<td>3.51</td>
<td>5.19</td>
</tr>
<tr>
<td>S&amp;P 500 Index</td>
<td>2.91</td>
<td>13.82</td>
<td>20.60</td>
<td>18.45</td>
<td>7.01</td>
</tr>
<tr>
<td>Russell 2000 Index</td>
<td>3.08</td>
<td>15.86</td>
<td>24.21</td>
<td>18.67</td>
<td>8.77</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>-0.98</td>
<td>4.10</td>
<td>18.62</td>
<td>10.04</td>
<td>0.63</td>
</tr>
<tr>
<td>Morningstar Large Cap Value</td>
<td>3.28</td>
<td>14.93</td>
<td>23.03</td>
<td>16.87</td>
<td>6.01</td>
</tr>
<tr>
<td>Morningstar Large Cap Growth</td>
<td>2.02</td>
<td>11.05</td>
<td>17.22</td>
<td>16.51</td>
<td>5.56</td>
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<tr>
<td>Morningstar Small Cap Value</td>
<td>2.70</td>
<td>15.28</td>
<td>25.61</td>
<td>16.70</td>
<td>9.31</td>
</tr>
<tr>
<td>Morningstar Small Cap Growth</td>
<td>3.52</td>
<td>16.03</td>
<td>22.25</td>
<td>18.57</td>
<td>8.33</td>
</tr>
</tbody>
</table>

Source: Morningstar.com; Russell.com

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RETIREMENT READINESS

Lately, the buzz phrase in the retirement world seems to be “retirement readiness,” often accompanied by images of a smiling couple relaxing on a beach, warm breeze in their hair, and a beautiful sunset as the backdrop. It is great to dream of such leisure after a lifetime of hard work, but if we took an honest look at the financial realities of our “retirement readiness,” what would we see? Here is a sobering statistic for all of us: according to a U.S. Government Accountability Office survey, the median account balance for participants in defined contribution retirement plans is only $22,800, and the median account balance among workers age 60 – 64 is only $60,600.

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As you will see in this letter, this statistic supports the general consensus that we are far from retirement readiness as a nation.

There are a few ways to gauge one’s retirement readiness, and to a large degree, it is a rather personal topic. There are so many variables to consider when assessing a personal level of retirement readiness, including family circumstances, health issues, and size of household debt, to name a few. For the purposes of this letter, we will keep the discussion broad and demonstrate that the best way to reach sufficient retirement readiness is through the good old discipline of saving.

**How much do I need at retirement?**

One way to address the financial goals of retirement is income replacement: how much of your pre-retirement income you would like to replace during retirement. Let us, for example, consider a pre-retirement income of $50,000. If the participant wants to replace 75% of this income, this would translate to $37,500 in post-retirement annual income. The question is, how big does your nest egg have to be for it to generate $37,500 annually during retirement? Social Security benefits typically replace only 30 – 40% of pre-retirement income, and the difference, or the "income Gap," should be covered by the annual income generated by your retirement savings. In order to address this income Gap, industry experts suggest the “Rule of 25,” which involves multiplying your Income Gap by 25 in order to estimate the size of the nest egg you will need to bridge the gap. In our above example, if we assume 35% replacement of pre-retirement income through Social Security benefits (at $17,500), our income Gap would be $20,000. Multiplying this Gap by 25, the resulting $500,000 represents the amount that the participant will have to amass by retirement age in order to replace 75% of her pre-retirement income. (This final sum would change depending on your need to replace less than or greater than 75% of your pre-retirement income and could change depending on other variables.) The calculation above brings to sharp focus the shortcomings of the national median average in retirement savings mentioned in the opening paragraph of this letter.

Another aspect of retirement readiness is to consider the standard of living one would like to maintain. You might start by asking yourself, "what do I want to do once I retire?" Catching up on a lifetime’s worth of reading in your backyard will cost you much less than going through the same reading list on a sailboat as you cruise around the world. The standard of living you expect during your retirement years will help determine the amount of your pre-retirement income you need to replace, and therefore, how much in savings you should have at retirement age.

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**Mirror, mirror on the wall...**

Common industry best practices include a belief that participants should save at a rate of 6% of gross income per year, and subsequently increase the savings rate each year to reach 10% by age 35. Over time, experts suggest that for most people, saving 15% of gross income per year is required in order to reach a successful retirement. Contrary to these ideals, J.P. Morgan’s 2009 – 2011 survey showed that on average, contribution rates start at 5%, and increase slowly, reaching 8% of salary by age 44 and 10% by age 59. There is a huge discrepancy between what we should be doing, and what we are actually doing. Even though the fastest way to build one’s retirement nest egg is to save more, the reflection that we see on the mirror of retirement readiness shows that we are not doing what is best for our future.

If you have not yet started to save for your retirement, it is never too late to begin. Be sure to take full advantage of any employer matching program, in which the organization will contribute a certain percentage of your own contribution to your retirement account for up to a certain portion of your pay. An example of this is a 50% match up to 6% of your salary. For every dollar you contribute into the plan, the employer will contribute 50 cents, up to 6% of your pay. In this example, if your contribution is less than 6%, you are foregoing the generous employer match. If your budget allows for the full 6% contribution, it is important to take advantage of the matching program. Many employers now have automatic enrollment and automatic escalation of contributions to your retirement fund to help you get started on your path toward retirement goals.

Even if you are already participating in your employer’s 401(k) or 403(b) plan and are taking advantage of a matching program, saving even more now will pay off in helping you reach your retirement goals. A study at the Center for Retirement Research at Boston College shows that small behavior changes, such as saving 3% more of one’s income, can produce significant changes in retirement readiness (Munnell, et al. 2006). As mentioned above, evaluate your budget to see if a total contribution of 10% to 15% of your annual income is possible for your 401(k) or 403(b). For the year 2013, the IRS allows contributions up to $17,500, and people 50 years of age and older may contribute an additional $5,500 in their 401(k) and 403(b) accounts. You may also want to explore establishing an IRA (Traditional or Roth), where you may contribute up to an additional $5,000 per year (this amount increases to $6,000 per year for those 50 years old and above).

The long term effect of extra savings is demonstrated in the graph below.

In the graph, the blue line represents the growth of your savings over 40 years, if you invest $10,000 at the onset, reinvest the dividends and interest, but do not contribute any more to your savings. This example assumes an annual return of 5%. As you can see, the power of compounding resembles a snowball effect, helping you to grow your retirement nest egg from $10,000 to $70,400 in 40 years. In addition to investing $10,000 and reinvesting the income, what if you decided to contribute an additional $1,000 annually to your retirement fund for 40 years? It takes thought, discipline, and planning, but as you can see by the red line, you begin with $10,000 and in forty years, amass $191,200. The power of compounding, partnered with the discipline of saving for the future consistently and patiently through your working years, can better prepare you for your post-retirement years.

To reap the most benefit from your investments, you should start saving as early as possible, diversify your portfolio, and lastly, stay patient and disciplined. Achieving your retirement goals should not only mean sunset on a beautiful beach. Retirement readiness refers to matching one’s financial reality with post-retirement expectations, whether they are replacing a certain percentage of pre-retirement income or maintaining a certain standard of living. If you have questions about your retirement readiness, you can always reach out to your plan provider or to CBIZ Retirement Plan Services at the contact information provided on the bottom left corner of page 1 of this letter.

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