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# Cadence *clips*

FOCUSED ON WHAT MATTERS MOST.

## Opportunity Cost: Why That \$1.69 Cup of Coffee Really Costs \$5.00

Opportunity cost is a rarely used concept to most people because even though we know there's a long-term impact to our short-term spending, most people do not actively try to calculate the true cost of those spending decisions, even the big ones. We feel, and share, your pain. In order to fully evaluate the impact of spending more money on one car, or one house, or even one cup of coffee versus another, the brain has to function at a level much different than its original prehistoric job description of looking for dry caves, sharp rocks and slow deer.

For the remainder of this article, we'll define opportunity cost as the difference between a dollar spent today and the value of that dollar saved instead. To illustrate the long-term benefits of factoring opportunity cost into normal life decisions, consider the spending habits of two couples. We're going to keep this basic, so we're only going to look at how these couples go about buying cars and buying homes, and we're only going to look at some of the expenses associated with each activity, albeit those we feel have the biggest impact on the total cost of ownership of those two types of assets.

Over a 40 year period, each couple is going to purchase 8 cars. They'll finance each car for five years and own them for a total of ten. Couple A is going to consistently purchase a

Honda Accord, and in this example consider the 4 cylinder 2014 Accord EX-L as the type of car they would buy. Couple B is going to consistently purchase an Acura sedan, like the 6 cylinder 2014 Acura TL, because they like that little bit of extra luxury and more than little bit of extra pick up. The Honda is \$7,700 less expensive and gets 5 miles more per gallon than the Acura. If all vehicles are driven the American average per year, and given some additional assumptions around average gasoline prices and finance rates over those 40 years, we're looking at the Hondas costing \$173 less per month than the Acuras in today's dollars.

Additionally, the couples want to move out of their apartments and into houses. They're both looking at houses ranging between \$350,000 and \$400,000. Couple A chooses a \$350,000, 2,053 square foot, three bedroom, one and a half bath home. Couple B chooses a \$400,000, 2,400 square foot, four bedroom, two and a half bath home. They each put 20% down and get mortgages at 5%. We estimated the larger home was 15% more expensive to heat, cool, and satisfy the town's tax collector, resulting in the cheaper home costing \$334 less per month over the 30 year mortgages. We did take into account the long-term, minimal amount homes appreciate in value relative to inflation but not the cost of upkeep, furnishing, lawn care, etc.

To give this comparison the full treatment (without going too crazy), we looked at long term auto loan rates, mortgage rates, current and assumed future heating oil and electric rates, and current and assumed future gasoline rates. We also assumed that the difference between what couple A and couple B spent over the years was saved by couple A and earned 6.5%.

After a lifetime of systematic decisions, where one couple habitually chose the less expensive options when buying cars and their home and the other habitually chose the more expensive, couple A has over \$1 million more dollars, just from one home purchase and one new car every five years. The breakdown of which expenses contributed to that \$1 million are:

Expense Source of Difference Saved	Final Value of Difference Saved	In Today's Dollars
House Down Payment	\$ 66,144	\$ 25,339
Monthly Mortgage	\$ 244,951	\$ 93,838
Monthly Tax/Utility	\$ 124,653	\$ 47,753
Auto Acquisition Costs	\$ 40,510	\$ 11,271
Monthly Auto Loans	\$ 411,267	\$ 114,425
Monthly Gasoline	\$ 160,765	\$ 44,729
	\$ 1,048,289	

If it's not cars, it's going to Disney World in Florida every year instead of Storyland in New Hampshire, it's buying lunch instead of brown bagging it, or it's any number of other items all added together that over the course of decades can give some people substantially less money saved than others.

If people understood the \$50,000 more expensive home will really cost \$167,000 more in today's dollars (and probably more given the costs we ignored), or the car with the \$7,700 higher sticker price will really cost around \$21,300 more in today's dollars (also probably more), would they value the less expensive choices more? These decisions, especially the big ones and the habitual ones, should not be made without an understanding of the long term consequences.

Even something as simple as buying coffee a few times a week has an opportunity cost that is surprisingly meaningful. Would people go to Dunkin Donuts three times a week for that medium coffee instead of making it for themselves at home before they left for work if they knew it was really costing them \$5.00 instead of \$1.69, and that over the course of their working lives that simple habit is costing them \$53,000? That's an expensive cup of joe to be sure, but provided they know they are already saving enough to achieve their goals, then only the caffeine need keep them up at night.



## HALLOWEEN SPENDING FACTS

Speaking of opportunity cost...Here are some facts about Halloween spending:

- Average spending on Halloween has increased 54.7 percent since 2005, with total spending estimated to reach \$6.9 billion in 2013.
- 43.6 percent of people plan to dress up and will spend a total of \$2.6 billion on costumes.
- 13.8 percent of those celebrating will take the extra time to find the perfect costume for their favorite four-legged friend, and will spend approximately \$330 million.
- Celebrants will spend \$2.08 billion on candy and \$360 million on greeting cards.
- Second only to Christmas in terms of spending on decorations, Americans will spend \$1.96 billion on life-size skeletons, fake cobwebs, mantle pieces and other festive decorations.

# Five Tips to Help You Protect Your Identity

## 1 *Protect your Checkbook*

Have only your first two initials and last name put on your checks. Should someone get a hold of your checks, he or she will not know if you use just your initials when you sign, but your bank will.

## 2 *International Travel Safety*

The Bureau of Consular Affairs, U.S. Department of State recommends making two photocopies of your passport identification page, airline tickets, driver's license and the credit cards that you plan to bring with you. Leave one photocopy of this data with family or friends at home; pack the other in a place separate from where you carry the originals. It is also recommended that you pack an extra set of passport photos along with the photocopy of your passport's information page to make replacement of your passport easier in the event it is lost or stolen.

## 3 *Signing Your Credit Card*

You may have heard that you should write "Photo ID Required" on the back of your credit cards rather than your signature, however your cardholder agreement requires you to sign your cards. Should you desire to add another level of security, there is nothing to stop you from signing your name and also writing "Ask for ID."

## 4 *Copy Your Wallet's Contents*

Photocopy the front and back of every license and card you keep in your wallet. It makes knowing exactly what was in there and exactly whom to call a lot easier should your wallet go missing or be stolen. Don't carry this copy with you, though, for should you lose it that's a lot of sensitive information.

## 5 *Cancel Stolen Cards Immediately & Call Credit Bureaus*

Finally, should your checks, credit cards, licenses, etc. get stolen, cancel the cards immediately, file a police report in the jurisdiction you believe the theft occurred, and call the three national credit reporting bureaus as soon as possible. That way should someone use your information to try and obtain credit, a fraud alert will have been placed on your file to let anyone looking to extend that credit know your information has been stolen and they need to contact you by phone to authorize the new credit. The initial fraud alert stays on file for 90 days. You can also request an extended fraud alert, which stays in effect for seven years. Fraud alerts can also be requested online via the credit bureaus websites. Here are some helpful phone number and web addresses to have on hand:

Social Security Administration Fraud Line: 800.269.0271 or [www.socialsecurity.gov](http://www.socialsecurity.gov)

Equifax: 888.766.0008 or [www.equifax.com](http://www.equifax.com)

Experian: 888.397.3742 or [www.experian.com](http://www.experian.com)

TransUnion: 800.680.7289 or [www.transunion.com](http://www.transunion.com)

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