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(Mr. Fox wears Ermenegildo Zegna. Details on p. 114.)

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Disaster Insurance

The right way to build your family's emergency fund

Even if your hobbies don't include cliff diving, there comes a time in every life when calamity strikes. Yet a surprising number of guys aren't prepared for the expense—whether it's a pile of medical bills or a five-figure plumbing emergency. According to one recent survey, fewer than four in 10 people have enough cash on hand to cover three months of living expenses. And nearly 30 percent of those who do are *losing* money: By failing to earn at least 3 percent on their funds, they aren't keeping up with inflation.

In case you haven't noticed, interest rates are at a five-year high. But they won't be forever. By acting now to whip your emergency fund into shape, you can build your cash reserve quickly without tying up your money in a long-term investment or rolling the dice in the stock or bond markets.

How much do you need? If you have a solid portfolio and two earners in your household, three months of living expenses is probably enough, says Richard Coppa, the founder of Wealth Health, a financial planning firm in Roseland, New Jersey. But if you're an entrepreneur, you work on commission, or you have lots of dependents, a six-month cushion is a safer bet.

The first step is to shift existing cash out of low-yielding accounts. One of the best places to keep your fund is a no-fee, online savings account. You can't write checks against it, but you can link it electronically with your checking account and access the money in a few days. Leading online banks now offer interest rates of 5 percent or more, including the Citibank Direct eSavings account; *EmigrantDirect.com*, run by New York's Emigrant Savings Bank; and *HSBCDirect.com*.

If you're in a high income-tax bracket, a tax-free money market fund with check-writing privileges may be your best choice. To compare a tax-free fund's yield with taxable funds, you must divide it by 1 minus your tax rate (For your tax rate, check out the rate calculator at *moneychimp.com/features/tax_brackets.htm*). Say you're in the 35-percent tax bracket and are considering Vanguard's Tax-Exempt Money Market Fund (symbol: VMSXX), which recently yielded a deceptively low 3.4 percent. By converting that yield to its "taxable equivalent" using the formula: $3.4\% \div (1 - 35\%) = 5.23\%$, it turns out to offer a better return than Vanguard's taxable money fund—and even tops most e-savings accounts.

To be sure, eking out extra returns on your emergency cash isn't as sexy as watching your tech stocks take off. But if you need money in a pinch, you'll have enough drama on your hands. That's when boring looks beautiful. TRACY BYRNES

THE SAVVY INVESTOR
What to do when interest rates start dropping

WADE INTO THE BOND MARKET
Prices of existing bonds go up when interest rates drop. To capture a return without risking too much volatility, invest some cash in a short-term bond fund, which holds fixed-income securities maturing over a couple of years. Morningstar senior fund analyst Scott Berry recommends sticking with a low-cost option such as the Fidelity Short-Term Bond Fund (symbol: FSHBX).

LOCK IN A FIXED CASH RETURN
As market rates fall and pull down yields on money funds, shift some cash into CDs. You can buy them with maturities of one to five years and roll funds coming due from the shortest-term CD into the longest-term one. This "laddering" strategy enables you to lock in a higher overall rate and maintain access to your cash, says financial planner Barry Vosler, of LPL, in DeWitt, Iowa.

ESTABLISH A HELOC
The cost of a variable-rate loan, called a home-equity line of credit (HELOC), has doubled in the past two years, but borrowing against your house could once again be attractive when rates start declining. Interest expense on loans up to $100,000 is tax deductible. With the housing market softening, now is the time to set one up. "Access to credit is based on the value of your home when the loan is approved," says financial advisor Richard Coppa.

HOW I WOULD INVEST $1K $10K $100K $200K

By Bill Brodsky, chairman and CEO of the Chicago Board Options Exchange, the largest options exchange in the United States

$1,000
My wife and I are deeply committed to Syracuse University, our alma mater. I'd contribute this sum to the school's book conservation program, which my wife recently endowed. The program supports workshops to train students in preservation techniques.

$10,000
I'd donate it to the Israel Emergency Campaign, part of the United Jewish Communities, a charity that aids Jewish people here and in Israel—and that has a proven track record of efficiently balancing administrative and program costs.

$100,000
I'd give Syracuse and the Israel Emergency Campaign $25,000 each and make equal contributions from the remainder to my four grandkids' 529 savings plans. We invest in the Utah Educational Savings Plan, which offers a good index-fund option.

$200,000
I'd give $30,000 to charity and invest the rest in a selection of exchange-traded funds that provide exposure to U.S. and foreign stocks, including iShares Dow Jones Select Dividend Index (symbol: DVY) and the MSCI EAFE Index (symbol: EFA).

STEPHEN SAVAGE