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Four Steps to Debt Reduction

Easy access to credit can contribute to a lifestyle that starts out with debt and gets worse as spending pressures increase. If you've accumulated debt, how can you dig yourself out?

Calculate Exactly What You Owe: List your debts and minimum monthly payments, due dates and interest rates. Rank debts from highest rate to lowest. Decide if any debt is worth keeping. Consider mortgages and college loans since interest on most mortgages is tax deductible and many college loan rates are reasonable.

Set Up a Budget and Start Eliminating Your Debt: A budget helps you decide how much extra cash you can devote to paying debt. It also helps you identify expenses that you can cut back on, which leads to more cash to further reduce your debt.

Lower Your Borrowing Costs: Compare what rates credit card firms are offering. Then get your current credit card company to match the attractive rate you discover. Or, transfer your current higher interest-rate balance to a company offering a lower rate. However, make sure you find out how long this lower rate will last and what the regular ongoing rate will be. Also, be on the lookout for balance transfer fees.

Cash Is King: Try to stick to cash and/or use a debit card. Unless you have developed a disciplined approach to pay off the balance, do all you can to avoid using a credit card. Find one card with a low rate for situations that may require one, like Internet purchases, but be sure to pay it off every month.

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Advisor Corner

I pride myself in offering you expert financial advice along with personalized service. Assisting you in reaching your financial goals is my business and I take that responsibility very seriously.

As an objective and independent fee-only wealth manager, my sole interest is to ensure my recommendations meet your financial goals.

COMPASS Wealth Management, LLC is a client-focused wealth management firm dedicated to providing superior advice to individuals, families, and corporate retirement plans.

Our wealth management services include investment management, retirement and gift planning, education funding, and other advisory services.

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Monthly Market Commentary

- During June, investors worried about a "soft patch" in the economic recovery and the stock market slid as a result until the final week of the month.
- Employment and existing home sales data reported during the month of June were disappointing, supporting the concern investors had regarding a "soft patch."
- COMPASS expects that economic growth will reaccelerate during 2011's second half, though the rate of growth is likely to remain subpar.

June saw markets reacting strongly to a mix of positive and negative economic news, including a speech by Fed chairman Bernanke that didn't mention additional quantitative easing, and Greece narrowly avoiding a bond crisis for at least the next few months. After six weeks of declining markets, investors were finally rewarded when, based on a surprisingly strong purchasing managers' report and reported increases in housing prices and pending home sales, the market gained more than 6% in the last week of June.

GDP: The third and final read on real GDP for the first quarter of 2011 was revised upward to 1.9% from 1.8% because of lower imports (subtracted from GDP) and higher inventory adjustments. A significant portion of this GDP increase was due to autos, which is worrisome, because future GDP growth expectations may prove to be overstated.

Employment: Employment data was abysmal for June, growing a pitiful 18,000 compared with 25,000 in May and 217,000 in April. The April and May numbers were also revised downward from previous reports to a total of 44,000. Small gains in the private sector barely offset continued government job losses on primarily the local level but also at state and federal levels. The unemployment rate inched up slightly to 9.2% from 9.1%.

Housing: On a seasonally adjusted annual basis, May existing-home sales were lower than they were in April. May inventories, at 3.7 million units, were little changed from April, with the month of supplies number still sitting at 9.3 months. However, both the Federal Housing Finance Administration and the Case-Shiller Home Price Index reported a rise in home prices in April, representing the first increase in 11 and 8 months respectively. Pending home sales also increased by 8% from April to May, leading to early signs that housing may have finally hit a bottom.

Manufacturing: The ISM Manufacturing Index increased in June, along with a better-than-expected industrial production figure and a strong durable goods report. According to Morningstar economists, one of the causes for these numbers was increased production at Nissan and Toyota, with Nissan almost back to normal in the U.S. and Toyota up to 80% of normal. Another factor was better weather conditions; June did not experience the same negative impact from bad weather as in May.

Personal income and consumption: Real, inflation-adjusted incomes remained relatively flat through May as accelerated inflation eroded away most consumer gains. Inflation-adjusted consumption numbers fell in April and May, primarily because of declining auto sales caused by high prices and short supply. Gasoline and food demand were also quite soft in response to higher prices, although more recently gasoline and agricultural prices have declined—the U.S. Department of Agriculture reported increased planting and stored stocks for corn and soybeans.

Retail sales: The International Council of Shopping Centers report for June was particularly strong; it noted that falling gasoline prices and warmer weather were helpful factors that allowed consumers to spend more freely.

Quarter-end insights: The Japan disaster's effect on major supply chains and high gas prices resulting from unrest in the Middle East were two important factors that slowed down the economy during the first half of the year, but more fundamental indicators were also in play. Inflation and real wage growth are key concerns for consumers, who are ultimately driving the recovery (and holding up surprisingly well despite said concerns). However, with real wage growth moving into negative territory on a three-month moving average basis, consumers may not have any disposable income left with which to drive the recovery. The good news is that, in the long term, decent productivity growth, favorable demographics, and an eventual real estate recovery are positive drivers.

With QE2 Over, What's Next?

By Louis E. Conrad II

- The second phase of quantitative easing, a monetary stimulus policy also known as QE2, recently ended.
- In this article we review what QE2 was meant to accomplish and what can be expected now.

On June 30, the Federal Reserve (the Fed) completed its historic Treasury bond purchase program, which was dubbed QE2, an abbreviation for the second round of quantitative easing that Chairman Bernanke announced in August 2010 and began implementing in November. Though the program is technically over, its ramifications have been far reaching and have influenced the performance of investment markets. In this article we review the concept of quantitative easing, what is likely to happen next, and investment implications.

What Is Quantitative Easing?

As defined by Wikipedia, quantitative easing is "an unconventional monetary policy tool used by some central banks to stimulate the national economy when conventional monetary policy has become ineffective." In November 2008, during the midst of the financial crisis, the Fed embarked on the first round of quantitative easing (QE1). At the time the Fed had already used its primary (and conventional) monetary tool, establishing short-term, interbank lending rates, by setting the Federal Funds rate at effectively 0%. However, due to the damage that the financial crisis had inflicted on the economy and the financial services sector, the Fed implemented QE1, as well as other programs, as part of a monetary stimulus program to enhance the liquidity of financial institutions and the functioning of financial markets.

Before the beginning of the Great Recession, the Fed's balance sheet held $700 - $800 billion of Treasuries, considered to be the safest government debt in the world. As part of QE1, the Fed expanded its balance sheet by purchasing $600 billion of lower quality debt, primarily mortgage-backed securities. By March 2009, the Fed's balance sheet had grown to $1.75 trillion.

Ultimately, the Fed decided in August 2010 to embark on QE2 because of the U.S. economy's sluggish growth and the Fed's concern that the U.S. could suffer from deflation, or a decline in the prices of goods and services, which would lead to an economic contraction. During the quantitative easing that ended last month, the Fed purchased $600 billion of longer term Treasuries. QE2 resulted in not only asset price inflation as seen in the stock market, but also higher commodity prices that can crimp economic growth. Since QE2 was announced, the U.S. stock market climbed 9%, while commodities gained 16% and gold increased 10%. Inflation is now evident, whereas nearly one year ago deflation had been the concern.

What Happens Next?

Since the beginning of the financial crisis the combination of fiscal and monetary stimulus, the responsibility of Congress and The Fed, respectively, has cumulatively reached levels never seen previously. Without new stimulus programs, some have grown concerned that the economy would suffer and perhaps "double dip" into a new recessionary period. Though QE2 supported the prices of riskier assets like stocks and commodities, as well as improved consumer confidence and employment levels, economic growth should continue, though at a subdued level.

What Is the Investment Impact?

With the Fed's elevated purchases of Treasuries past, bond markets may experience less liquidity and heightened volatility. Ultimately, since the Fed had been a major purchaser of Treasuries, prices of these securities may begin to slowly decline, leading to an increase in interest rates. Once the Fed is convinced the economy is growing at a reasonably stable level and unemployment is trending down, it is likely to increase the Federal Funds rate, but this is unlikely to occur until 2012. Continued economic growth will also pressure interest rates higher. On the other hand, any shock to the economy would lead to a flight-to-quality and lower interest rates for Treasuries, if only on a transitory basis.

In Case of Emergency

- COMPASS generally recommends that clients maintain an emergency fund that amounts to 3-6 months' worth of living expenses.
- How large your emergency fund should be depends on (1) whether you are working or retired; (2) if working, the likelihood of losing your job and the potential duration of unemployment; and (3) whether you own or rent your residence, for example.

Nobody likes to think about the possibility of job loss, serious illness or other major expenses. But these are all possible in an uncertain world, and having an emergency fund in place can help if such situations arise.

An emergency fund is a money market, savings or checking account where you keep a specified amount of money to cover expenses. The important part here is that the money is stored in an investment vehicle that allows quick and easy access to funds. But you do not touch the money in this financially liquid account unless a real emergency pops up. No ifs, ands or buts.

Setting up an emergency fund is usually the first step toward building a solid financial plan. If you don't already have one in place, start building one as quickly as you can. It obviously takes perseverance to stash money from each paycheck into your emergency fund, but it may be well worth it one day.

How much cash should you put aside? Most financial advisors recommend to first aim to keep enough money in the fund to cover at least three months of expenses. However, as your take-home pay increases or your expenses grow, you may need to keep six months or even as much as a year's expenses in your fund.

Take it one step at a time. Once you've saved enough to cover three months of expenses, try for the six-month mark, and so on. Easier said than done, sure, but if you treat your emergency fund like any other must-pay monthly bill, it will undoubtedly grow over time.

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