July 2014 | Vol. 4 No. 7 | "Morningstar's Best Client Newsletter"

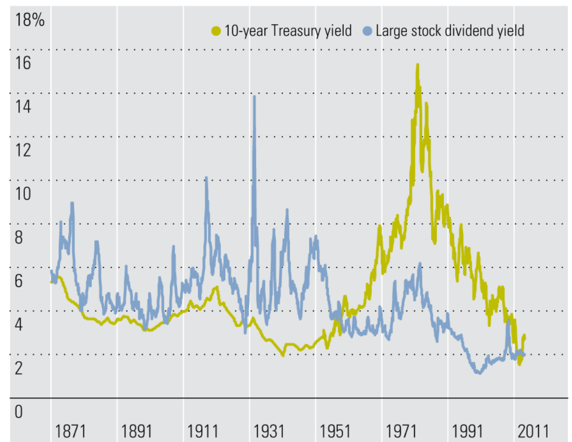
Large Stock Dividend Yield Versus 10-Year Treasury Yield

- In an article back in October 2011, COMPASS highlighted the fact that the S&P 500's dividend yield was greater than the 10-year Treasury yield.
- As we stated then, "when this has occurred in the modern era, stocks significantly outperformed bonds during the following 1 - 3 years."
- Since October 2011, the S&P 500 has gained more than 75%. While stocks are no longer inexpensive on an absolute basis, they remain cheap relative to bonds.

In the recent context of likely-to-rise-at-any-time interest rates, it may be interesting to take a look at the historical relationship between stock and bond yields. As illustrated in the image, stock dividend yields were much higher than 10-year government-bond yields before 1957, with dividend payouts a form of compensation for the additional risk of investing in stocks.

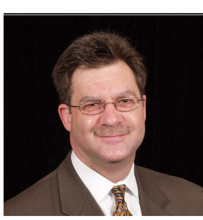
In the more modern period, this relationship has changed. As capital appreciation became a bigger driver of stock performance, bonds became the main engine for potentially steady income generation. After 10-year Treasury rates significantly declined following the 2008 financial crisis, stocks yielded more than 10-year Treasury bonds for the first time since 1957. Recent rising interest rates, however, have pushed government yields above stock dividends once again.

Stock and Bond Yields
January 1871–March 2014



Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Stocks are not guaranteed and have been more volatile than the other asset classes. Dividends are not guaranteed and are paid solely at the discretion of the stock-issuing company. Government bonds and Treasury bills are guaranteed by the full faith and credit of the U.S. government as to the timely payment of principal and interest. U.S. government bonds may be exempt from state taxes and income is taxed as ordinary income in the year received. With government bonds, the investor is a creditor of the government. In general, the price of a debt security tends to fall when interest rates rise and rise when interest rates fall. Securities with longer maturities and mortgage securities can be more sensitive to interest-rate changes.

Data: Large stock dividend yield is represented by monthly S&P Composite Index. 10-year Treasury yield is based on the monthly yield of 10-year government bonds. Both indexes are from Robert J. Shiller's Data Library



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More about COMPASS Wealth Management, LLC

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Five Estate-Planning Tasks That You Shouldn't Put Off

- This article highlights the basic estate planning tasks that most should consider, including the drafting of essential documents, such as wills, durable powers of attorney, and health care proxies.
- However, COMPASS also recommends that you obtain HIPAA releases so that appointed loved ones, including your spouse, have access to your medical information.
- Though COMPASS does not provide legal advice, we do provide referrals to competent estate planning attorneys who can provide the necessary counsel.

Keeping tabs on the estate-planning rules during the past few years has been a little like watching Olympic-level table tennis: The action moves quickly, and it's difficult to keep up. However, no matter how laws and rules change, there are a few basic tasks that are actually pretty evergreen and that everyone should execute. Five such estate-planning to-dos are outlined below.

1) Update Beneficiary Designations. Even people who have never set foot in an attorney's office may have laid the groundwork for an estate plan if they filled out beneficiary designation forms for their financial accounts. Those designations, in fact, trump other estate-planning documents when it comes to distributing assets, so it's worthwhile to periodically review them to make sure they're up-to-date with your current situation—if you've gotten married or divorced, for example. (How would your spouse feel if you inadvertently left your 401(k) account to your brother?) People who have drafted estate-planning documents such as wills should ask their attorneys to help them review beneficiary designations to ensure that they sync up with other estate-planning documents.

2) Designate Legal Guardians. Parents of young children should designate legal guardians who will look after their children if the parents should die or otherwise be unable to care for their minor children. It is important to focus the discussion on actual child-rearing abilities and willingness to do the job. What is not helpful is to get hung up on hurting anyone's feelings or bypassing friends or family members who might expect to be guardians but aren't the best choice. Most importantly, a guardian should be willing and able (emotionally and financially) to take care of your children if the need arises, so an essential step is to discuss the responsibilities with the potential guardian beforehand.

3) Create a Living Will and Last Will and Testament. A living will tells your health-care providers and your loved ones how you would like to be cared for if you should become terminally ill and unable to express your wishes yourself. It is called a "medical directive" in some states. This document details your views toward life-support equipment. Not to be confused with a living will, a last will and testament details how you'd like your assets and possessions distributed after your death.

4) Draft Powers of Attorney. A basic estate plan should also address what would happen to your affairs if you are still living but incapacitated. A power of attorney is a document that specifies who will handle your affairs if you are unable to do so. You'll need to draft two separate documents: one that names your power of attorney for health-care decisions and another for financial matters (often called a durable power of attorney). The person you entrust with your power of attorney for health care will, ideally, live in close geographic proximity to you. The person you name on your durable power of attorney form should be detail-oriented and comfortable with financial matters.

5) Name an Executor. Your executor will gather all of your assets after you're gone and make sure they are distributed in accordance with your will. Ideally, your executor will be someone who's comfortable with numbers and good with details, and will also be able to find the time to work on your estate. It's common to name family members as executors, but in more complicated situations it might be preferable to use a professional, such as a bank trust officer, to serve as your executor. It's a good idea to tell your executor that you've named him or her, and also provide details on how to obtain access to important documents, such as your will and a master directory detailing all of your accounts.

This information is for informational purposes only and should not be considered as legal or financial planning advice. Please consult a legal and/or financial professional for advice specific to your individual circumstances.

Monthly Market Commentary

Economic data from the past month revealed some positive trends, with upbeat employment numbers for June being the biggest headline. In addition, weekly shopping center data from the ICSC have now broken out to new highs; auto sales exceeded all expectations in June despite some strong headwinds, and pending home sales made one of their biggest jumps in the history of the now 5-year-old recovery.

GDP: The last GDP revision was a huge bomb, now showing a massive and unexpected first-quarter decline of 2.9%, from a previously estimated rate of decline of just 1.0% and the original estimate of 0.1% growth. Two thirds of the revision was due to negative revision to the effects of the Affordable Care Act, and a third was due to an expected revision in net exports. Based on the nature and size of this revision, plus a poor consumption report for April and May, economic growth of 2% in 2014 is now starting to look aggressive even to the most optimistic. Because of the consumption data in April and May, it looks like the best-case scenario for the second quarter is now somewhere around 3% GDP growth.

Employment: The June employment report was strong as the economy added 288,000 total jobs compared with the 12-month average of 208,000. Professional and business services, which tend to be higher-paying jobs, were the strongest sector with a gain of 67,000 versus a 12-month average of 53,000. Despite all the positive news, the longer-term private payroll growth rate, using an average of three months of data compared year over year, ticked up to 2.1%, which is right in line with the slow and steady pace we have experienced over the past two years.

The unemployment rate decreased by 0.2%, to 6.1%. The labor force participation rate was unchanged at 62.8%, which is a positive because it means that the unemployment rate went down because of increased employment and not workers leaving the job force. Over the past year, the unemployment rate has dropped 1.4%.

Housing: Both new homes and existing homes moved nicely higher in May than in April and were considerably above expectations. This may be a sign that interest in housing in general is improving. With the labor market growth continuing, weather improving, mortgage rates down again, and home price growth slowing, the picture looks good over the next several months, and housing may be a bright spot in the second-quarter GDP report after negative results in the fourth quarter of 2013 and the first quarter of 2014.

Home price growth, however, continues to slow. Some of the more drastic slowing in growth rates has been on the West Coast where annually growth rates that may have soared as much as 30% at one point have now moderated to 20% or less, according to Case-Shiller. The rest of the nation in general has seen a slowing in price increases, but not nearly as dramatic. Remember, we are talking about slowing growth rates and not price declines. For the full year, Morningstar economists are expecting 5%–6% increases in home prices, a much more palatable level for homebuyers.

Consumption and Personal Income: The poor GDP report for the first quarter was followed by even more disappointing consumption data, which now showed consumption expenditures slumped 0.2% in April and 0.1% in May. (The May data had a lot of quirks including a large drop in food spending and a massive swing in utility bills.) However, the month-to-month data has proven to be exceptionally volatile, while year -over-year data averaged over three months has shown almost rulerlike growth at around 2.0%. The income report provided at least a small antidote to the GDP and consumption reports, notching its fourth consecutive month of growth. Income growth for May was 0.2% (or 2.4% annualized), which should have fueled more spending growth than it did.

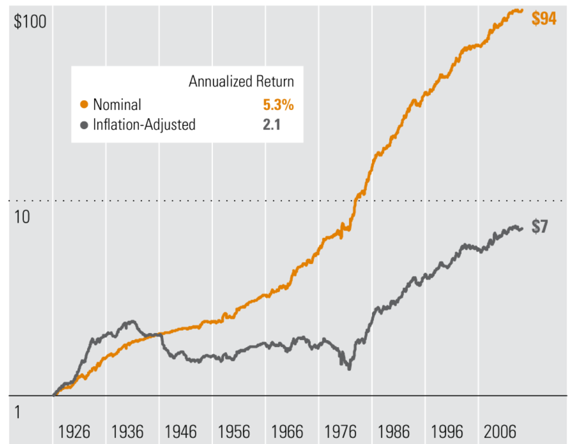
Inflation, not Rising Rates, Biggest Bond Threat in the Long Term

- As this short piece illustrates, inflation can be a meaningful detriment to the real returns achieved by investors.
- For a lower potential return asset class, such as bonds, inflation can have a much greater proportional impact on your returns.

Since the beginning of 2013 when rates started to rise, investors have been concerned about a potential decline in bond performance. In general, bonds tend to perform poorly in times of rising interest rates, but by worrying about rates investors may lose sight of an even bigger long-term threat: inflation.

Over the long term (since 1926) investors have lost 3.2% (the difference between 5.3% nominal and 2.1% inflation-adjusted) in return every year to inflation. Compounded over almost 89 years, the difference in ending wealth values is astounding: A $94 nominal value becomes only $7 when adjusted for inflation. Investors may be well advised not to neglect inflation risk while focusing on interest-rate risk.

Intermediate-Term Government Bonds
January 1926–March 2014



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Data: Nominal performance of intermediate-term government bonds—Ibbotson SBBI U.S. Intermediate-Term Government-Bond Index, total return. Inflation-adjusted performance of intermediate-term government bonds—Ibbotson SBBI U.S. Intermediate-Term Government-Bond Index, inflation-adjusted return. Inflation—Consumer Price Index. The data assumes reinvestment of all income and does not account for taxes or transaction costs.

2013 FIVE STAR PROFESSIONAL Wealth Manager MULTI-YEAR WINNER

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