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COMPASS Economic and Market Update

Back on August 4th in the midst of daily 400-plus point swings for the Dow Jones Industrial Average, I sent an e-mail to clients with my latest thoughts on the economic and market environment. The thoughts expressed then are still current today. The world is fixated, as it should be, on developed nations' staggering debt loads and anemic economic growth. Resolving these issues is a long-term structural challenge.

The economic growth that the U.S. and Europe have enjoyed since the late 1990's was fueled by leverage—developed nations financed their spending with huge sums of borrowed money. In the U.S., this was accomplished through the issuance of U.S. Treasuries. The bill for living beyond our means is coming due. To pay down the debt means either less government spending and/or higher taxes—both are impediments to economic growth.

Consequently, economic growth among the developed nations is likely to be subpar for several years. Normally economic expansions following severe recessions are more robust—not this one. The damage done to the financial system, job and housing markets, and consumer and business confidence was significant.

The U.S. stock market reacted violently to these events, correcting by 20% from its recent high in April to its low at the beginning of October. Since then, the S&P 500 has jumped 11%, expressing optimism that Europe may be closer to a solution. The U.S. stock market is certainly cheap and U.S. Treasuries are expensive by historical standards. The S&P 500 has been offering a higher dividend yield than the 10-year Treasury yield. When this has occurred in the modern era, stocks significantly outperformed bonds during the following 1 – 3 years.

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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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Planning for the Unexpected

By Louis E. Conrad II

- Too often I find clients have inadequately prepared for life's misfortunes, which can ultimately also place undue emotional and financial stress on their loved ones.
- Properly prepared and maintained estate planning documents aid in your ability to not only direct how your affairs are handled, but also reduce the stress on family members.

All of us should have a plan to meet the unexpected financial and medical events that confront us in life. I recommend that clients have at least the most basic of estate planning documents and then maintain them consistent with their current wishes.

Wills and Trusts

A will is a set of written instructions outlining how probate property should be distributed after the owner's death. Probate property is essentially property that is not distributed to a joint owner, through a trust, or through a beneficiary designation.

Naming a guardian for any minor children is perhaps the most important nonfinancial reason for having a will. Without a will, a state court will determine who will become the guardian of your children if you and your spouse are deceased. If you are the parent of minor children, you should also consider a trust that will dictate how your assets will be managed on behalf of your children until they reach the age of majority or some later age.

In general, trusts are a tool to manage your estate's financial, real estate, or other tangible assets. Though there are many different types of trusts that can be established with different purposes, a personal trust is a legal arrangement that is created to hold assets for the benefit of a beneficiary. Trust assets avoid the probate process and public view, and may also reduce the amount of estate taxes that would otherwise be due upon the grantor's death.

Durable Power of Attorney

With a durable power of attorney (DPOA), you legally delegate authority to another person to manage your financial affairs in the event you are unable to do so. A DPOA can be used if you become disabled or incapacitated, on either a temporary or permanent basis. The person you appoint becomes your attorney-in-fact and can deal with your bank and investment accounts, credit cards, and other personal financial accounts.

Health Care Proxy

A health care proxy enables a family member or trusted friend to make decisions about your medical care if you are unable to do so. Such a medical directive can reduce family conflicts and the time necessary to make medical decisions. Although sometimes appearing as separate documents, a health care proxy will often include two other important directives, a HIPAA release and a living will.

HIPAA, the acronym for the federal Health Insurance Portability and Accountability Act, provides authorization to health care providers to allow access of your medical information to those you appoint. Without a HIPAA release, your spouse or other family members will not have access to your medical condition or records.

A living will outlines your wishes in the event you require extreme medical intervention or life support decisions. While not legally enforceable in Massachusetts, a living will can provide guidance to others.

A properly crafted estate plan, implemented with the documents outlined above, allows you to express your wishes and provide clear direction in a legally enforceable manner for your financial affairs and medical care. It can also reduce family conflict and their stress when they are called upon to make decisions on your behalf.

Monthly Market Commentary

September was filled with uncertainty, which continued to weigh both on businesses and investors. The European debt crisis, with its unknown effects and unclear resolution, has troubled the markets, causing increased stock-market volatility and a significant decline in financial-sector stocks. Not even Federal Reserve chairman Ben Bernanke could calm market sentiments with his “twist” plan, announced after an extended two days of discussion at the Federal Open Market Committee meeting. Despite 2011 being the third year of a presidential term, which historically has been good for stocks, the S&P 500 was temporarily in bear market territory as of Oct. 4, with a 20% decline from its most-recent 2011 high.

GDP: Second-quarter GDP growth was revised up to a final reading of 1.3% from 1.0%, driven mainly by export data. A weak dollar, a revival of the manufacturing sector, strong capital goods sales in emerging markets, and powerful agricultural sales have allowed the U.S. economy to trudge along at an anemic rate with strong exports in the first half of 2011.

Employment: Employers added 103,000 jobs in September, led by gains in the professional and business services and health care, sectors, as well as the 45,000 Verizon Communications employees that returned to work. Similar to August, private-sector growth continued to be offset by contractions in the government sector. In order to effectively put a dent in unemployment rates, job growth of about 150,000 is required per month. Unemployment remained flat at 9.1%.

Manufacturing: The ISM Manufacturing Index inched up slightly—indicating that manufacturing was expanding but still very sluggishly. An ongoing concern was the lackluster performance of new orders and backlogs, which hinted at a potential contraction in demand going forward. Durable goods orders, on the other hand, pointed toward a continued moderate uptrend in manufacturing.

Quarter-end insights: The second-quarter of 2011 continued to defy predictions by economists, with the U.S. economy neither collapsing nor breaking out on the upside. In the wake of persisting uncertainty from the European debt crisis and its contagion effects, along with the U.S. budget debacle in August, investors and corporations became more cautious. Investors seeking yield continued to bid up more-defensive portions of Morningstar’s stock investing universe, seeking stocks that provided income in addition to capital gains. Riskier sectors with less good news, including financials, basic materials, and energy, continued to sell at larger discounts than the overall average. Corporations with near all-time-high profit margins and large amounts of cash were still unwilling to spend or hire significantly given the economic and political uncertainty and the lack of investor confidence. In fact, merger-and-acquisition activities as well as stock buybacks (financed with money borrowed at exceptionally low rates) started to pick up. Consumer spending remained relatively strong, pushing ahead slowly, cautiously and consistently despite setbacks from the lingering effects of earthquakes, hurricanes and budget crises. However, consumers were selective with what they purchased and consistently punished businesses that raised prices too quickly. Gasoline demand in the U.S. declined for three quarters in a row, corresponding closely with the recent acceleration in gas prices. Auto sales and apparel sales were the same, as price hikes from Japan’s supply-chain issues (for autos) and increased cotton prices (for apparel) caused sales to fall. Netflix saw its stock price drop following a pricing change. With regard to inflation, Morningstar economists believe that a slower world economy and a resolution of the Libyan situation should help drive oil prices (the key driver of high inflation) lower in the months ahead. Food prices should also begin to fall as crops are harvested and some of the dismal weather conditions around the world abate. A resumption of Japanese auto shipments should also help drive auto prices lower in the months ahead.

Social Security Beneficiaries Get a Raise

By Louis E. Conrad II

- After a two-year drought, Social Security recipients will see their benefits increase by 3.6% in 2012.
- However, for many, that increase will be reduced by higher Medicare Part B premiums.

Following two years without a raise, Social Security beneficiaries will receive a 3.6% cost-of-living increase for 2012. Unfortunately, many seniors will incur higher Medicare Part B premiums that will reduce their net Social Security benefit.

The 3.6% benefit increase, to be enjoyed by 55 million Social Security beneficiaries, amounts to $43 more each month for the average retiree, or a total of $1,229. In 2010 and 2011, inflation was too low to trigger a cost-of-living adjustment based on the Consumer Price Index used for the Social Security program.

Medicare is expected to announce its 2012 Part B premiums as early as next week. Part B premiums, which cover doctor visits, are deducted directly from Social Security disbursements. For some seniors, about one-quarter of their Social Security raise could be lost to higher Part B premiums.

By law, Medicare Part B premiums must be set each year to cover 25% of the program's costs. Premiums were kept at 2009 levels for about 75% of beneficiaries because there was no cost-of-living adjustment in 2010 and 2011 for Social Security. Consequently, the Part B premium increase in 2010 and 2011 was borne by the remaining 25% of Medicare recipients, which included new enrollees and higher income families, as well as low income beneficiaries who have their premiums paid by Medicaid. The 2009 premium level is $96.40 per month, though most of those who enrolled in 2010 pay $110.50 per month and most of those who enrolled in 2011 pay $115.40 per month. Those who have been paying premiums based on 2009 levels will see the biggest percentage increase in 2012 premiums.

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