Tuning out the noise

With the financial meltdown from the fall of 2008 now nearly 6 years in our rear view mirror, this seems like a good time to re-visit investment philosophy. I have always believed in modern portfolio theory. This school of thought holds that an investor can reduce the overall volatility of his portfolio and increase return by using asset class diversification. Re-balancing is an important attribute of this buy and hold strategy.

In the midst of the 2008/2009 crisis, some financial reporters questioned the use of buy and hold strategy and even claimed the approach to investing was dead. Hedge fund strategies and alternative investment ideas were promoted alongside tactical (code for market timing) asset management. Ironically, the past six years have favored the buy and hold investors. Hedge fund managers, tactical analysts and alternative investment managers have been soundly beaten by the S&P 500 index over the past six years. What can we learn from this? I believe alternative investments (Commodities, managed futures, REIT's, Private Equity etc..) have a place in most every investor's portfolio. These investments can further reduce a portfolio's volatility. The key for investors is not to substitute this approach for modern portfolio theory, but to use these investments as a compliment to traditional holdings.

Doug Lagerstrom

Here are some inspirational quotes that have given me insight. I hope that you find something insightful and inspirational for yourself, or for someone you wish to share these with.

It is not what you **do** for your children,
but what you have taught them to **do for themselves,**
that will make them successful human beings.
~Ann Landers~

Hold the vision
Trust the process
~Author Unknown~

Your problem has already been solved,
You just haven't gotten to that point in time yet.
~Sue Moses~

10 Words of Wisdom

Be the change
What you think, you become
Where there is love there is life
Learn as if you will live forever
Your health is your real wealth
Have a sense of humor
Your life is your message
Action expresses priorities
Our greatness is being able to remake ourselves
Find yourself in the service of others
~Gandhi~

Andrea Baird

MMM Good

Hillyard Holiday Treat

Cinnamon swirly pie crust for Apple or Pecan Pie!

Prep time: 10 minutes
Total Time: 10 minutes

1 Refrigerated pie crust
1 tablespoon unsalted butter
2 teaspoons ground cinnamon
1 large white egg
1 teaspoon water

Directions:

1. Unroll pie crust on a lightly floured surface. Brush with butter and sprinkle evenly with cinnamon. Roll up tightly and slice into 1/2 inch rounds, like miniature cinnamon rolls.
2. Press miniature cinnamon rolls, flat side down, evenly into the bottom and sides of a 9-in glass pie plate. Brush pie crust lightly with egg white/water mixture.
3. Prepare your pie filing as directed and pour into prepared pie crust.

Lynn Hillyard

Win/Win Situation

Before the real estate meltdown of 2008/2009, large lenders were notorious for bundling the Jumbo Loans (loans that exceed $625,500) on their balance sheets and selling them on the secondary market. Obviously this proved to be disastrous. According to Inside Mortgage Finance, an industry newsletter, the secondary market for Jumbo Mortgages is doing worse than a year ago. Only 2.3% of all jumbo mortgages originated in the first half of 2014 have been sold on the secondary market compared with the peak of 49.3% in 2005. WHY IS THAT?? Lenders benefit because keeping these jumbo loans in their portfolio allows them to reap the profits themselves. Consider this example. According to Cameron Findlay, chief economist for Discover Home Loans, low interest rates that banks pay on their deposits have translated into cheap money that can be funneled into jumbo loans with attractive returns. Savings accounts pay average annual yields under 1%. By comparison, banks can earn an average 4.14% on a 30-year, fixed rate jumbo mortgage, according to mortgage-information site HSH.com as of September 5.

Believe it or not, the phenomenon above has created an advantage for borrowers as well. By keeping the loans in their portfolio, jumbo lenders may have more flexibility with qualification standards, so borrowers may get slightly better terms on down-payment minimums and debt-to-income ratios. In addition, because the jumbo loans are held by the banks that make the loans, they are able to lower the rates to attract desirable borrowers. According to HSH.com, as of September 5, 2014, jumbo loans have carried lower average fixed interest rates than smaller home loans for 5 consecutive weeks, the longest such stretch since at least 1986.

In summary, we, as consumers, are able to borrow more at lower rates and favorable conditions. Lenders on the other hand make more money on the money that we borrow, which in-turn means that they are less likely to package the loans and sell them on the secondary market. Hence, A WIN/WIN SITUATION

Allen Minassian

What is a bond?

A bond is a debt contract in which one party lends cash to another for an agreed period of time at an agreed interest rate. The interest rate is the fee the borrower pays to the lender for borrowing and that interest rate fee is paid to the lender periodically. At the end of the agreed period the borrower returns what was borrowed. So essentially an investor is lending money to a borrower when s/he 'buys' bonds or 'invests' in bonds.

The primary concern when investing in bonds is getting your money back at the end of the agreed period.

When investing in bonds and trying to determine risk an investor must know a great deal about the bond issuer (borrower).

1. What does the borrower intend to do with the money?
2. How long until I get my principal back? (agreed period).
3. Can I do better elsewhere?
4. How much tax will I pay on the interest?
5. Most importantly, what is the likelihood I will need my money before the contract ends?

Will I get my money back?

The primary concern when investing in bonds is getting your money back at the end of the agreed period. This credit risk is a fundamental principle of the interest rate charge. The more likely I get all my money back, the lower the credit risk, and therefore I require a lower interest rate to buy your bond. Think of it this way. As a bond investor you will want a higher interest rate from Greece or Detroit than say Australia or Switzerland. The same applies to corporations. You are more likely to get your money back from Apple than Radio Shack. You would want a higher interest for Radio Shack bonds (much higher) than Apple bonds.

When will I get my money back?

Let's say it's 1993 and a company that rents out video tapes of movies to customers is experiencing great demand for its service. It decides to expand, but needs money. This company is called Blockbuster Video and it decides to issue bonds to investors for an agreed period of 20 years. At the time Blockbuster

(Continued on page 4)

Client Corner

Congratulations to Patrick J. Clinite for completing a 3000 piece puzzle last month! You can see the original puzzle in our office.

Political Picture

You might be wondering why a financial newsletter would have a political picture section. Although we do not offer any judgments of political policies (it's just out of the area of our expertise), we do analyze the effect these policies may have on the economy and the financial markets. It is simply naïve to think that policies passed in Washington have no effect on the pricing of financial assets in New York.

> ...financial recommendations should take into account all relevant information, including the political environment.

We believe it is within our role as your financial advisor, therefore, to monitor the political environment and determine the effect that new regulations, tax policy, and laws will have on the economy and subsequently the financial markets. Although there is generally a lag between a new policy and its effect on the economy, the financial markets often anticipate the expected effect policies will have on the economy and respond immediately.

We don't believe it is prudent to guess the direction the political winds will blow and base investment advice on that opinion. However, at Private Wealth Solutions, we do believe that financial recommendations should take into account all relevant information, including the political environment. In future articles in this section, do not look for judgments on the wisdom, or lack thereof, of current fiscal policy. Instead you should anticipate an analysis on the likely effect of current or potential future laws, taxes and policies on the economy and the financial markets.

What is a bond (continued)

was growing and the proceeds were to be used for productive purpose. Both great reasons to be an investor in Blockbuster Video bonds. But in 2010

> *The most critical role of an advisor is to reduce risk when collective opinion and markets reach extremes.*

Blockbuster filed for bankruptcy. Since the principal wasn't due until 2013, bondholders did not receive all their money back. The term of a bond needs to be factored when judging risk because the future is difficult to predict. The longer the term, the more difficult it is to predict repayment and the greater the risk of being paid back. So the longer the bond contract the higher the interest rate an investor should look to receive.

I've found that a simple understanding of bonds, accompanied by a degree of common sense, are the best ways to prevent poor choices with regards to investing. When fear or greed are at extremes, simple common sense is often removed from investment decisions. The most critical role of an advisor is to reduce risk when collective opinion and markets reach extremes. From my view we are near that extreme in bonds.

Kumbie Mtunga

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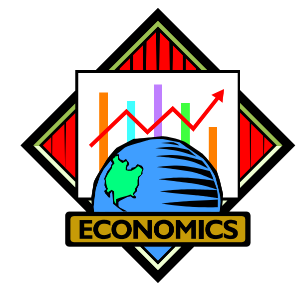
Generational Wealth Management



When Ben Bernanke began the process of bringing the Federal Funds rate to essentially 0%, the stated goal of the Federal Reserve Bank (Fed) was to stabilize the economy and bring unemployment to 6%. The Fed also launched an unprecedented quantitative easing program (QE) to patch up the financial system and get the economy growing again. The initial asset purchases (QE1) by the Fed were followed by more buys several times in 2009. When the economy failed to respond adequately by October 2010, the Fed upped the ante with QE2. This process of buying US treasury bonds was thought to lower long term US interest rates. The Fed believed that these lower rates would encourage businesses to borrow, grow, and hire more employees. QE3 followed shortly after. The Federal Reserve announced this year that they will conclude their policy of Quantitative easing in October.

> *Ironically interest rates for long term US treasury bonds will likely remain low after the Fed stops buying them*

Ironically interest rates for long term US treasury bonds will likely remain low after the Fed stops buying them. The European Central Bank (ECB) has adopted their own accommodative monetary policy (lower interest rates) and their own version of QE. German government bonds now yield 1.04% for 10 years, Italy is at 2.37% and Spain is at 2.2%. Overseas investors are tempted to pick up some good old US treasuries at 2.42%, especially when the dollar is likely to strengthen now that the Fed is stopping QE.

Historically the Fed has simply withdrawn bank reserves (reduced the supply of money) to increase the federal funds interest rate to slow the economy and control inflation. This time, the Fed plans to target money market mutual funds and other non-bank financial instruments. The Fed will set a federal funds range from zero to 0.25% and then use overnight reverse repo agreements to set the lower boundary of that range. Regardless the strategy, the result will likely be the same according to Fed minutes. Low rates for a prolonged period of time.

Big Borrowers

US government debt is currently $17.7 trillion

US government debt equals $152,159 per taxpayer

Student loan debt is $1.296 trillion

Mortgage debt is $13 trillion

California State debt is $424 billion

Source: www.usdebtclock.org

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