Outlook

A Quarterly Newsletter from Roffman Miller Associates

13 April 2011
Volume 5, Issue 2

Keeping a Promise

According to the headlines, the first quarter of 2011 was the best in twelve years for the Dow Jones Industrial Average. The Dow, comprised of 30 stocks, gained 6.4% and led the broader S&P 500 index which rose 5.4% over the three months.

Peter Miller
President

Not a bad performance for the US stock markets, given the many challenges that faced corporations, governments, and investors so far this year. In fact, besides the headline mentioned above it was difficult to find good news during the quarter. The two biggest news events of the quarter were the Japanese earthquake (together with the ensuing tsunami and nuclear disaster) and the rising rebellion in Libya and several other areas in North Africa and the Middle East. Those events alone, with their impact on the global manufacturing supply chain, consumption, energy policy, and oil prices, had the potential to decimate recent investment gains. The markets did, in fact, react ï after initially shaking off the initial reports of the Libyan revolt that began on February 15th, oil prices quickly spiked upward by 12% and the US markets, which were up about 6% at the time, gave back some of their year-to-date gains. Three weeks later when disaster struck Japan, our markets were back to where they started the year.

What the two events have in common is the fact that while each was conceivable, neither one was predictable. Not surprisingly, one of the greatest challenges for us as investors is always to take into consideration the many possible outcomes of the complex global economic environment that we all live and work in today, and to choose investments and allocations that are most likely to withstand those events that we simply cannot predict.

I promised last quarter that if the market did well then I would keep my letters short. In keeping with my promise, Iôll end this note here but not before pointing out that not only did the market do well but far more importantly to us the individual investments that we own have performed well and have exhibited an encouraging wave of events such as stock splits, buybacks, and dividend hikes. If you would like to schedule an appointment to discuss your investments, allocation, and our outlook, please give us a call.

-Peter Miller

Social Security 101

A few months ago my mother-in-law started to do research on Social Security. This is the first year she is eligible to collect Social Security benefits (I hope she doesn't find out I just gave away her age). After trying to make sense of the information on her own, she realized she needed more guidance. Many of our clients are in a similar situation, approaching the topic for the very first time, and realizing that there is much more to making the decision of when to start taking their benefits than just their age.

The earliest a person can start receiving Social Security retirement benefits is age 62. Since the payout for early benefits is only 70% of the full benefit, many people choose to continue working while drawing benefits. But, there is a cost to working. The earnings limit is $14,160 in 2011 for beneficiaries who are age 62 through the full retirement age of either 66 or 67. For every $2 earned over the limit, $1 is withheld from your social security benefits! In the year you reach full retirement age the earnings limit increases to $37,680. Then, for every $3 earned over that limit, $1 is withheld from benefits. **Starting with the month you reach full retirement age, you can get your benefits with no limit on your earnings.**

Many people have a spouse who is not the same age. This brings up the question: **If one spouse of a married couple filing a joint tax return retires and starts taking Social Security, will the other working spouse's salary count as earned income toward the limit (discussed above) and possibly reduce the benefit amount?** No. The earnings limit applies only to the income of the person who is collecting the benefit. It is that person's income that determines whether benefits are reduced.

Where a spouse's income *will* have an effect is in the taxation of Social Security benefits if a joint federal income tax return is filed. Some people have to pay federal income taxes on their Social Security benefits. This usually only happens if you have other substantial income (such as wages, self-employment, interest, dividends and other taxable income) that must be reported on your tax return. If you:

- **file a federal tax return as an "individual"** and your *combined income** is
    - between $25,000 and $34,000, you may have to pay income tax on up to 50 percent of your benefits.
    - more than $34,000, up to 85 percent of your benefits may be taxable.
- **file a joint return**, and you and your spouse have a *combined income** that is
    - between $32,000 and $44,000, you may have to pay income tax on up to 50 percent of your benefits
    - more than $44,000, up to 85 percent of your benefits may be taxable.
- **are married and file a separate tax return**, you probably will pay taxes on your benefits.

*Please note this new definition, courtesy of the Internal Revenue Code, which seems to have been developed strictly for this situation**:**

Your adjusted gross income
+ Nontaxable interest
<u>+ ½ of your Social Security benefits</u>
= Your "***combined income***"

Some people are going to choose to work even as they begin to collect their Social Security benefits. Whether that is in a consulting capacity or a part time job, the income they receive will impact their federal retirement benefits and their taxes. I know that each time I present this information more questions are asked. Please feel free to email me at susan@roffmanmiller.com with any questions you may have on Social Security and I will attempt to answer them in upcoming segments of our newsletter.

\- Susan Arnold

Whip Inflation Now

"WIN" It was the 70s, but I can still remember it as if it were yesterday. Rocky leans in close to Adrian, who has just awoken from a coma, and she whispers to him..."WIN!" Well, that's not exactly the WIN I set out to write about, but I believe we are beset with all the same drama and predictable outcomes of this 1979, $7million (cost) blockbuster. WIN, or Whip Inflation Now, was Gerald Ford's very public attempt to quell the rising tide of mid-1970's inflation. The plan included stirring a grassroots movement that encouraged more personal savings and controlled spending, the latter by the private sector as well as through tighter public fiscal policy. I can't say whether or not the campaign had any measureable effect, but I can say with confidence that inflation was not whipped until years later with different, more aggressive, tactics.

This relates to today as we continue to be in a period where prices of many things are rising, but the "official" measures of inflation have not yet reflected what the majority of us perceive or actually feel as an impact on our wallets. "Core" inflation, that government measure that leaves out the effects of food and energy prices, has not moved dramatically. But look at this table of items we consume regularly, and observe the increases over the past 52 weeks:

Item	One year change in price
Gasoline	+52%
Fuel Oil	+50%
Diesel Fuel	+49%
Corn	+128%
Oats	+83%
Soy	+47%
Wheat	+84%
Butter	+31%
Coffee (Colombian)	+50%
Beef	+17%
Sugar	+50%
Aluminum	+13%
Copper	+50%
Silver	+118%

There are several contributing factors to rising prices. Further, just as many things can lead to rising prices, rising prices can also lead to many things.

Many parts of the world are growing at a rate of two or three times the growth rate of the US. Those populations, such as in Brazil or China, are beginning to ramp up consumption of goods and services from a base much lower than what we are familiar with here in this country. Not only will these people need more food, but they'll need more roads to transport it; more trucks to deliver it; more fuel to run the trucks, and the list goes on and on. The more the demand for these goods, all else held equal, the higher the price that can be asked for them. That is one of the factors contributing to rising prices around the world. As a side note, I believe this demand trend to be a long-term phenomenon. Within that longer term trend, however, I think we may be seeing a bit too much exuberance right now and I'm concerned that investors who are new to commodities investing may be being led down a dangerous path.

An increase in energy costs (i.e. oil & gas) will likely lead to an increase in cost of nearly everything. As it applies to our clients, this is bad news for retirees or any investors who are depending on a fixed pension or interest from investments as they are now faced with rising prices and yet still low interest rates. (continued on back page)

Company Visits

This winter we attended the Consumer Analyst Group of New York annual conference. Over the course of several days, we were able to meet with management teams from:

- Pepsi
- Diageo
- Church and Dwight
- McCormick & Company
- JM Smucker
- Sara Lee
- General Mills
- Kellogg
- Hormel Foods
- Clorox
- Procter & Gamble
- HJ Heinz Co.

Whip Inflation Now (continued)

Weŏve written several times over the past year of the issue of low interest rates, the pending specter of inflation, and the challenges of investing in this environment. Iŏd like to re-emphasize some of the methods we are utilizing to achieve returns in a period of time where there are predictable outcomes (for example, one possible outcome is the Fed raising interest rates severely to stop prices from rising just as they did in the early 80ŏs) but far too many unknowns to reliably predict the right one.

First, stocks have historically been robust investments in inflationary times. When prices of energy and raw materials go up, corporations tend to raise their product prices to maintain profitability. While they can then generate the same *percent* of profits, their cash flow is actually increased through the process and this cash can ultimately be passed on to shareholders through (for example) rising dividends. As an investor, this means an investment whose cash flow may keep up with, or stay ahead of, your rising expenses.

Many of us also own bond portfolios which are vulnerable to inflation in at least two ways ï one, bonds typically pay a *fixed* rate of interest. So, no matter how much extra profit or cash flow the issuing corporations experience, they are obligated only to pay you the stated rate of interest on your bonds. That can be an issue if your expenses keep rising but your income remains stagnant. And this problem can be extended to any pension which does not have a COLA (cost of living adjustment) provision.

The second way bonds are hurt by inflation is more indirect. The usual method of quashing inflation is for central banks to raise interest rates. Theoretically this slows the economy down which decreases demand for goods and services and removes the upward pressure on prices. And yet while high interest rates are good for bond investors, theyŏre only really good if you werenŏt fully invested before the rates went up. If you owned a bond, letŏs say, paying 4% and now that same bond is available paying 5% then your bond is worth less than it was before rates went up. Note; it is not *worthless*, just worth less than it was before.

Roffman Miller is currently managing income allocations with a portfolio approach where appropriate. This means that we are including different elements to the portfolios, each serving a different purpose, but all working in concert to deliver what we believe to be a superior risk adjusted return. For example a portfolio today may consist of one or more of the following: a bond ladder, treasury inflation protected securities, floating rate bonds, high yield bonds, REITs, high dividend common stocks and preferred stock.

The Fed will probably raise rates this year or next if the US economic outlook remains positive. Several other countries have already begun to raise rates. Will this bring inflation back in check? Or will higher rates stop our recovery in its tracks? No one really knows; I think its best to understand the many potential outcomes and to be prepared to earn investment returns no matter what happens.

- Mark Frombach

Contact Information

Roffman Miller Associates, Inc.
1835 Market Street
Suite 500
Philadelphia, PA 19103

Tel: 215-981-1030 Toll-free: 800-995-1030 fax: 215-981-0146
www.roffmanmiller.com info@roffmanmiller.com