Outlook

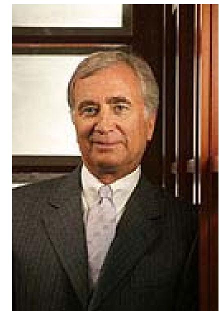
A Quarterly Newsletter from Roffman Miller Associates

10 July 2012

To worry or not to worry? That is the question.

If you are the kind of person who pays attention to all the negative headlines, you may be surprised that the markets are still showing a decent return for the first half of the year. The second quarter was negative but not as bad as one would think. In fact, the quarter ended with a positive note from the Euro-zone. While Europe's problems are far from over, their latest summit showed a willingness to address their problems.

So if we don't want to worry about Europe anymore, what else is out there? Many of you may have heard the term "fiscal cliff." Unless there is a change in the current law, taxes will go up by $600 billion at the end of the year. While at the same time, federal spending will drop by $130 billion. This could send the economy 'over the cliff.' The big concern is that congress will not or can not reach a compromise. Most of us believe that Washington is dysfunctional. So why should we believe that congress would get it right? But before we give up, remember that this is an election year. Whoever wins is not going to want to be seen as the ones that push the economy into a free fall. There should be some sort of compromise with neither side getting all they want.



Peter Miller
President

One other concern is what some are calling the "war on savers". The Fed zero interest rate policy has had the effect of safe havens such as bank CD's or money market funds yielding close to nothing. Worry-free investments have never yielded so little. Your choice is to live with zero return on your money or invest in riskier asset classes. At the same time, many of the tax increases I talked about are aimed at investment gains. The Federal Reserve is keeping interest rates as low as possible because it hopes that will help the economy. Of course, the mounting debt that our government must pay interest on is being helped by these low interest rates but that can't go on forever. The answer is a strong economy that will increase tax revenue and the demand to borrow, and that will lead to higher interest rates paid to savers.

So what's my point? First off, we had much to worry about for the first half of the year yet the market has given us a decent return. Second, it is our job as your money manager to do the worrying. That is what you hired us for. Third, we all know that to worry does no good. Easy to say, but hard in practice. I'll leave you with this quote, "Worry does not help tomorrow's troubles, but it does ruin today's happiness."

As always, if you have any questions or if you would like to come in to review your portfolio, do not hesitate to call me.

-Peter Miller

One Word: Plastics

As we notice the changes in our spending habits we should also note the change in how we pay for things. Plastic payments account for 53% of consumer purchases compared to 43 percent in 1999, according to a survey by the American Bankers association and Dove Consulting. Plastic has the advantage of security over cash because a PIN is required for debit purchases and a signature for credit purchases. Over the past few years credit card issuers have improved rewards and benefits as well. Even debit cards have joined the game. Some benefits available on credit and debit cards include:

Price Protection: It helps you save money on many products that you buy entirely with your card. If an eligible item is purchased and you see it in a printed advertisement for less at any retail store within a stated amount of days of the original purchase date, simply file a valid claim and the credit card company will refund the difference.

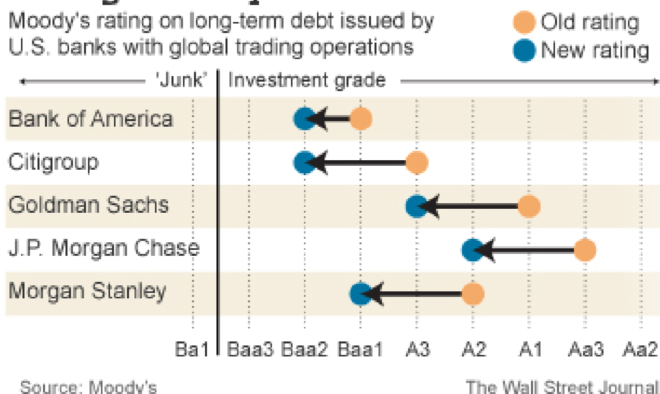
Purchase Security: Within a stated number of days from the date of purchase and at the discretion of the benefit manager, they will replace, repair, or reimburse you for eligible items of personal property purchased entirely with your eligible card in the event of theft, damage due to fire, vandalism, accidently discharged water or certain weather conditions.

Warranty Services: This will allow you to have extended warranty protection on your purchases. The extended warranty protection is available to extend, in some cases doubling, the time period of the original manufacturer's written policy when an item is purchased entirely with your eligible credit card. And it is free.

There are many more benefits available to card holders that are specific to each card but many people are unaware of the benefits extended to them. It pays to contact your credit card company and request a guide to your benefits so that you may begin to take advantage of them. Below are links to the basic benefits from the two largest issuers:

http://usa.visa.com/personal/cards/debit/index.html
http://www.mastercard.us/debit-card-standard.html

Lori Hartman



We all hear about the danger of issuing **credit cards** to **college students**. Well, here's some interesting news:

Outstanding **student loans** were $904 billion as of 3/31/12. Outstanding **credit card debt** was $866 billion as of 3/31/12. (that is everyone's credit card debt, not just the students')

source: Federal Reserve

Review/Outlook

Before we begin here, I encourage you to read my letters from July, 2011, and January, 2012. Why? Because 2012 so far resembles 2011 for investors: a rapidly rising market, a crisis or two overseas, markets falling, interest rates defying gravity once again and declining even further, and then, as earnings are reported, markets recovering to a level based more on economic activity than on crisis or herd mentality. In the wake of a similar situation last July, I closed this column with the notion that there was still opportunity for investors in stocks.

But why take the risk? Because the price for safety has never been higher. According to Bankrate.com, the best 2-year CD rate I can get today is 1.09%. That is from Ally Bank (FDIC guaranteed, of course. But if you didn't know, Ally's parent company is the former GMAC which is 73% owned by you and I, the taxpayers, in exchange for roughly $16 billion in TARP 'bailout' money). If you are looking for something 'safer,' the two-year treasury bill is paying about a quarter of one percent and the ten-year treasury bond about 1.65%.

Most of us are looking for a return in excess of those rates just mentioned; further, most of us are willing to assume a modest amount of risk in return for a moderate return on our portfolios. But investors are backed into a corner; in order to meet their income needs, they are forced to take on more and more risk. One option is to look for overseas bonds. However, stable countries like Japan and Germany are offering yields similar to ours. Alternatively, you *can* find a 5% two-year bond issued by Spain or Italy. But how certain are you that you'll get your principal returned?

Meeting your income needs and growing your portfolio at the same time means balancing your risk and return goals. Modern Portfolio Theory has been hailed as the holy grail of risk/return optimization for much of the past 60 years. Basically, MPT suggests that there is a portfolio that can be constructed which is the least risky for every desired portfolio return - for example, if you wanted to earn 8% over time you could plug all your data into a series of equations and MPT would give you the proper asset allocation to achieve your goal with minimum risk. It doesn't pick stocks and it can't say that you'll be able to live with that kind of risk, but it does show how investors can move up and down the risk scale to something that feels more appropriate. And, it points out that some choices will lead to lower returns.

In the past decade, many detractors have tried to poke holes in MPT claiming that what it really is is an academic exercise in portfolio construction – a controlled laboratory experiment that no longer applies now that the market seems to be dominated by computers and 'fast' traders. What the detractors are missing is that it isn't the theory that's wrong, it's the *application*. Like any sort of mathematical model, your output is only as good as your assumptions. In looking at investments, many people look backwards at what they did and then project those results forward . Investors really need to alter their assumptions by looking *forward*, projecting what types of returns could be made on the available asset classes given the conditions that exist *today*. Plus, investors (as opposed to traders) are looking to increase value over time, not over night.

When I look at the situation today, there appears to be quite a bit of risk for the equity investor. The European markets, China slowing down, US Debt, everyone has their problems. The net effect of this may be keeping stock prices down, as many investors just don't want to pull cash off the sidelines and commit money to stocks. To me, at this point of great pessimism, there just might be some decent returns to be enjoyed in stocks over the next market cycle simply because prices today are note over-inflated. This argument, pressed even further, would have me conclude that not only should we own the durable dividend paying companies today, but also a healthy dose of growth stocks and some exposure to growth markets.

We've had over twenty years of a bull market in *bonds*, as we've explained several times in this newsletter. Conversely, we've seen stocks consolidating (that is market jargon for 'moving sideways') for 12 years, with returns well below average. I can not tell you what will happen in the short run. And I don't know if we'll earn the historical averages ever again on any asset class. But looking forward, these patterns of the past few decades should reverse and show that today the relative value is in stocks, not bonds.

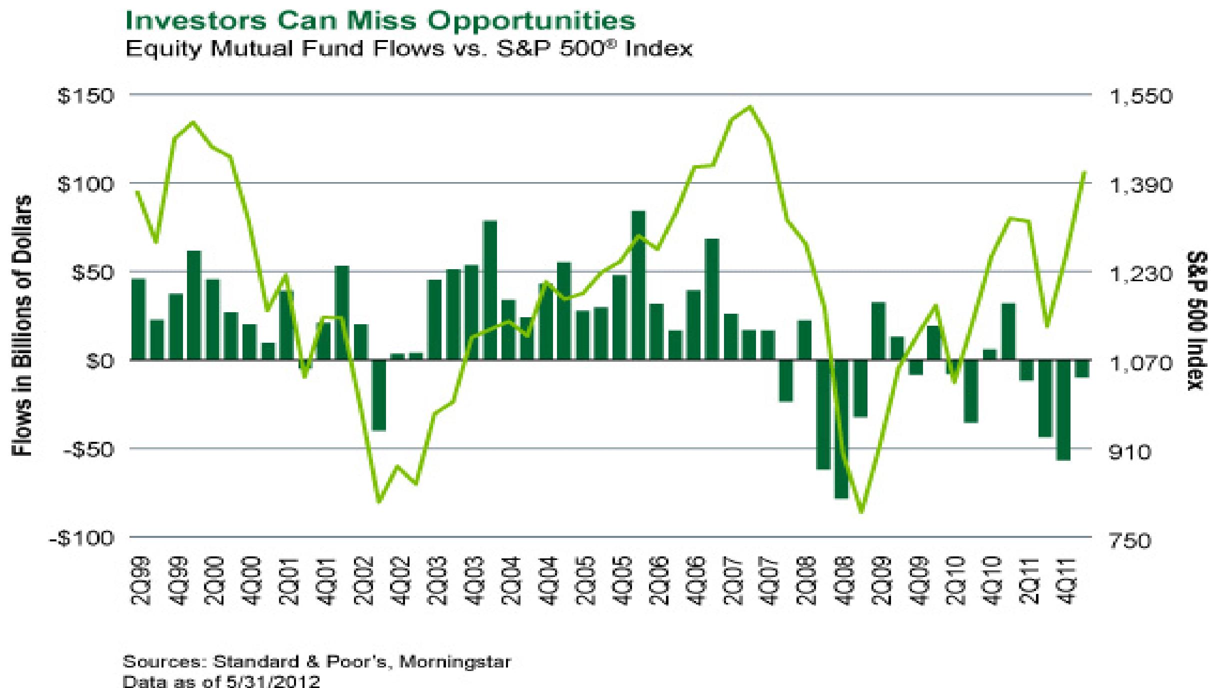
In January 2012, I said that the principles of investing were not dead and that the US would be a good place to be investing in the stocks of multinational, dividend paying companies. Forgive the repetitive nature of the message, but we still believe that to be true.

Mark Frombach
Chief Investment Officer

Investor Behavior

Everyone has heard the old adage: sell high and buy low. It makes sense to buy stocks when they are undervalued. It also makes sense to take profits when stocks are overvalued. So why do most investors do exactly the opposite? When I analyze mutual fund inflows and outflows they always show that the masses sell low and buy high. This type of investor behavior coincides with the basic human emotions of fear and greed. When people are afraid their instinct is to run. In this case running from the market shows itself in mutual fund redemptions. Moreover when the stock market is doing well people tend to get a little greedy. As a result mutual fund inflows increase during periods of strong market performance. Emotions lead to market timing and poor investment results. At Roffman Miller we encourage our clients to be investors; not traders. Investing in good companies and having the discipline to adhere to a long term investment plan will produce the best results.

Bob Hoffman



Companies we've met with in 2012

So far this year, we've had the opportunity to meet with the CEOs and other members of management from the following companies:

IBM	UGI Corp	Texas Instruments	Medtronic
Honeywell	Washington Real Estate	Johnson and Johnson	Hershey

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