

# Outlook

A Quarterly Newsletter from Roffman Miller Associates

## Yale Beats Harvard - Again

You would think that this headline is from a sports page. Actually it's from the Wall Street Journal and it refers not to football but to the Yale University's endowment returns versus Harvard University's endowment returns. For fiscal 2016 Yale's endowment gained 3.4% while Harvard had a 2% loss over the same period. This makes 6 years in a row that Yale has out-earned rival Harvard. Other colleges and university endowments tracked by Cambridge associates had an average return of -2.7% for fiscal 2016. So you could say that at least Harvard outperformed the average, but not by much.



Harvard was a pioneer in shifting from a plain vanilla portfolio of stocks and bonds to alternative investments like hedge funds, private equity, and real estate. Yale also made the same shift but the difference was that they farmed out their capital to outside managers. Harvard maintains a staff of more than 200 that manage the money in-house, and pays the top executives more than any other school. Their last CEO was paid \$13.8 million in 2014 compared to \$1.6 million paid to the endowment chief at MIT. Harvard Management Company just named another new CEO, their fourth in the last decade. Yale has had the same investment chief for the last 31 years.

So what's my point? You might think that my message is that if Harvard can't manage their own money themselves then how can the average person. But that's not it. My point is that 'plain vanilla' is not a bad way to go. Of course that's the way we manage money at Roffman Miller – research, asset allocation, and nothing too fancy. Over the last five years Harvard had a +5.9% per year return versus a 60/40 stock bond portfolio return of +8.9%. Harvard reported an average annual return of 5.7% over the last decade. A 60/40 US stock and bond mix would have returned 6.9% a year for the same time period (my source for this data is the Harvard Management Company 2016 Annual Report).

Over the last 40 years I've seen one new investment strategy after another after another. They come and go from the Dogs of the Dow to computers trading at warp speeds. Picking the right companies is hard enough but it's what has worked longer and in the end better than any of the other hundreds of alternative strategies.

As always I welcome your thoughts and comments. I can still be reached by phone and even email. Thank you for your confidence in us.

Sincerely,  
Peter Miller  
Chairman and Founder

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## Power of Attorney – Types that are Frequently Used

The Power of Attorney (POA) is a useful Financial, Healthcare and Elder-planning tool. The purpose of this legal document is to allow another individual (referred to as an ‘agent’, ‘attorney-in-fact’, or ‘POA’) to act on behalf of an account owner or ‘principal.’ The agent will typically have the same powers as the account owner, but those powers can be classified as Limited or Full.

Limited Powers of Attorney typically have narrow or specific powers when connected to a brokerage account. Those powers are typically: authority to trade securities, update certain account information (but not address changes), gather information and to speak with the firm about the account. The Limited POA does not have the authority to withdrawal or transfer funds.

In addition to the authority granted in the Limited version, a Full Power of Attorney allows the POA to withdraw funds from an account.

Both versions of the POA documents are available in simple ‘fill in the blank’ formats from most bank and brokerage companies. The main problem with these versions is that the powers cease to exist when the account owner is incapacitated or declared mentally incompetent. Those are unfortunately the situations where we actually need an agent to get things done on our behalf.

A powerful planning option is the use of the *Durable* Power of Attorney. This is a custom document typically drawn up by your estate planning attorney that allows an agent to act on your behalf and provides that those powers granted to the agent shall not be affected by the subsequent disability or incapacity of the principal or by the lapse of time.

Most powers of attorney become effective immediately upon execution by the principal. If the principal is wary about giving powers immediately upon signing, the principal can draft the POA document in such a way that the powers are not effective until the occurrence of a triggering event, typically the disability of the principal. This is called a *Springing* Durable Power of Attorney. While this is a good option for some, the primary disadvantage is due to the triggering event, where a third party is likely needed to conclusively establish the disability. Therefore, the document should clearly define the term ‘disability’ and who determines it.

No Power of Attorney document is valid after the principal’s death, so this is just one part of a thorough estate and financial plan. As always, please discuss your individual circumstances with your Attorney and we’ll work together to find the best way to add a POA to your accounts if necessary.

### FRAUD ALERT

The Federal Trade Commission and the National Association of Realtors® are warning home buyers about an email and wire transfer scam. Hackers have been breaking into some consumers’ and real estate professionals’ email accounts to get information about upcoming real estate transactions. After figuring out the closing dates, the hacker sends an email to the buyer, posing as the real estate professional or title company. The bogus email says there has been a last minute change to the wiring instructions, and tells the buyer to wire closing costs to a different account. But it’s the scammer’s account. If the buyer takes the bait, their bank account could be cleared out in a matter of minutes. Often, that’s money the buyer will never see again.

If you’re buying a home and get an email with money-wiring instructions, STOP. Email is not a secure way to send financial information, and your real estate professional or title company should know that.

What steps can you take to avoid becoming a victim of this scam?

- Before sending any wire, review the applicable invoice and request for wire transfer very thoroughly
  - Contact the party who is receiving the wire *by phone* to confirm the wire instructions before sending the wire
  - Use a secure messaging system when you are sending wire transfer instructions
  - And, of course, always use secure passwords for your email accounts
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## Apple.. time to Upgrade?

We've all heard many times that to be a successful investor you need to stay invested through the tough times. To me, 2016 was set up to be one of those tough years: we had the worst start in 100 years for the stock market, and since then the geopolitical scene has been one disaster headline to another from Syria and Russia to North Korea, and even here in the US where the presidential election process seems to be focused more on divisiveness than unity. Strangely, through it all, stock prices in the US have generally held up well.

What's been tough for me this year is finding companies with desirable investment characteristics trading at prices we're willing to pay. Today, more than any time in recent memory, the market is awarding premium prices for stability. Companies like McCormick and Johnson & Johnson almost certainly won't grow very quickly, but they are more likely to grow steadily, stay solvent and pay dividends even through a prolonged financial drought. Those types of companies have seen their stock prices rise appreciably over the past few years. The problem is that it's hard to make money in stocks if you have to pay those premium prices today. There are other companies that have great potential growth, but because of some uncertainty about that growth their stock prices are not fully pricing in their potential.

Let's look at Apple Inc., which as of this writing is the world's most valuable company. The total market capitalization of the company today is approximately \$609 billion. What makes a company so valuable? In this case it's the iPhone. The phones make up about 2/3 of Apple's total annual revenues, and Apple sells roughly 40-50 million iPhones every quarter (that's about 500,000 iPhones each day). That sounds great until you take a moment to remember your history.

Think back to all the dominant consumer electronics companies over the past 50 years: RCA, Sony, COMPAQ, Dell, Nokia, Blackberry. They all have two things in common – they were the biggest, most popular electronics manufacturing companies of their era. And now, they're not. Today that dominant company is Apple and that worries a lot of people.

I'm not sure how the Apple story will end, but I believe they still have a long way to go. Last year the company had total sales of \$233 billion and a net profit of over \$50 billion. This year they will fall short of that, and that lack of growth is one of the things that worries investors. But I could argue that if profits at Apple fell 10% each year over the next 20 years, the company would earn about \$400 billion for investors over that time period. It's not a bad 'worst-case' scenario.

There is great competition today in the connected world of hardware and software. In the past, the hardware manufacturers have all suffered from the commoditization of their products and lost their ability to earn great profits (think personal computers). Apple is a hybrid, providing both hardware and software, and also acting as a gatekeeper to anyone else providing software on their system. Apple is also the relevant and trusted technology brand for a generation of youth who will be technology decision makers in the decades to come, so there is room for their products to serve government and big business, like IBM does today. And of course, there are new horizons – operating systems in automobiles are in their infancy, as are smart homes. These are huge, untapped markets that will generate hardware and software/services revenues for years to come.

Apple will need to continue to innovate in order to stay among the leaders in technology. As an investor or a potential investor, I'd like to see a continued commitment to research and development, but without wasting my money on moonshot projects. I'd also like to see the \$2.28 per share dividend continue to grow (it has grown 30% over the past 3 years) and stock buybacks as appropriate. And finally, I'd like to see Apple enter a new market – if rumors are true and they are designing an electric car, I think they can outsell Tesla in a few short years. For all its headlines, Tesla will sell less than 100,000 vehicles this year. For reference, Ford will sell over 2.5 million. Now think about the number of loyal customers that Apple already has – 40 to 50 million every three months! I really have no idea if there is an Apple car in our future but this is an example of a market that has already been disrupted and now needs to be perfected. Keep in mind that the price tag of Ford and Tesla put together would amount to about half of the cash that Apple now holds. The power of Apple's balance sheet leaves them with a lot of flexibility.

It's hard to know what the next move is for a company like Apple. In my portfolio I like the comfort of the companies I mentioned earlier, with more predictable sales and dividends. But I also don't mind paying a modest price, like 13x next year's earnings, for a company with solid management that employs brilliant people who design spectacular products. A well-built portfolio has room for both.

Mark Frombach

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## Company News

Select news from companies that we follow

**Johnson & Johnson** announced a \$4.3 billion acquisition of Abbott Laboratories' eye-surgery unit, Abbott Medical Optics. This division makes equipment for Lasik procedures and cataract surgery. The division also produces eye drops and optical solutions. This unit had sales of \$1.13 billion last year and the acquisition is expected to be accretive to earnings within the first year.

**Google** just turned 18 years old and it's amazing what they've accomplished in such a short time. The company counts one billion people around the world who use each of Google's premier services: Chrome, Google Maps, Android, YouTube and Gmail. According to Google that's more than a third of the online global population. In just 18 short years Google has a market cap greater than \$500 billion, making it one of the largest companies in the world.

**3M** bought back \$2.1 billion worth of stock in the first half of 2016. They plan to buy an additional \$2 billion to \$4 billion by the end of the year. This year marks the 100<sup>th</sup> consecutive year of dividend payments for 3M. Also 3M has *increased* its annual dividend in each of the last 58 years.

**PepsiCo** opened a new restaurant in Manhattan called the Kola House. It's a farm to table concept that is meant to appeal to consumers looking for a high quality meal. They are not offering Pepsi products or co-branding in any way - this non-branded restaurant is an entirely new business for Pepsi.

## Don't Fear the Fed

With the Federal Open Market Committee (FOMC) considering the timing of their next rate-hike and the now-and-then dramatic headlines of a bond bubble, I thought it might be a good time to review what that might mean for bond investors. First, cash flow (coupon payments and return of the par amount) and the total annualized return (yield-to-maturity) at the time of purchase, barring issuer default, remains the same if the bond is held to maturity. Second, if you sell prior to maturity at a value lower than your purchase price, it does not automatically mean you lost money on the investment. Third, if and when the FED raises its overnight lending rate, it does not mean the rest of the yield curve will move by the same amount or even the same direction. Even with a crystal ball for FED policy, there are other components of the market that could make us wrong even if we get the FED policy part right. We feel clients would be worse off if the confusion and fear of higher rates keeps us holding onto cash for another year waiting for those elusive higher rates. This is among the reasons we continue to fill in the end of our bond ladders with maturing issues and new cash.

Ryan Crooks, Investment Manager

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