

MARKET UPDATE NEWSLETTER

Bad Month in a Bad Quarter

Following the disappointing market performance and uncertainty that was felt by many in May, June began with optimism and hope. However, the lingering jitters in Europe and concerns regarding the Gulf oil spill led to the second straight month of negative returns for the S&P 500. The quarter ended near the lows for the year leaving the S&P 500 down -5.23 for the month, -11.43 for the quarter, and -6.65% for the year. This marked a dramatic turnaround of nearly 15% since the year's highs in April. Stocks were not the only asset class to feel pressure in June, as once again, certain types of bonds and commodities posted losses for the month. This flight to safety was evident by the historically low yields investors received in the two-year US Treasury bond.

The main economic headline of the month was the job report illustrating that newly hired census workers buoyed unemployment statistics, which remained just under the psychological level of 10%. Inflation stayed relatively benign at the consumer level, which allowed the Federal Reserve to keep its target rate just above zero. However, the Bureau of Labor Statistics said wholesale prices continued to be higher on a year-over-year basis. The Bureau of Economic Analysis said GDP for Q1 came in at 2.7%, substantially lower than the previous quarter's 5.6%.

July will prove to be an important month as many companies will report their earnings for the second quarter which was certainly an eventful three months. Also, the inflation vs deflation debate is back at center stage as market participants join the longer-standing economists' view that deflation is still a potential danger in this environment. We will remain very in-tune to this issue.



Investment Outlook Summary

Asset Class	Outlook	Commentary
Cash / Stable Value	<ul style="list-style-type: none"> Still maintaining higher levels of cash 	Higher levels of cash help protect your portfolio in sharp downturns, provide capital to buy when opportunities present themselves, and have not shown to significantly hurt performance as the market has rebounded.
Bonds / Fixed Income	<ul style="list-style-type: none"> Slightly positive on bonds in general Cautious of Treasuries for the long-run Positive on Treasury Inflation-Protected Securities (TIPS) Positive on floating rate bonds Positive on emerging market bonds 	<p>While bonds seem fairly valued, they provide a level of income in a low interest rate environment. Bonds have performed well in the latest "flight to safety."</p> <p>Primarily used for safety, but with yields at historic lows and the risks of future inflation present, treasury owners may not be paid adequately for the potential risk.</p> <p>Essentially, these are treasury notes with an interest rate tied to inflation. Used for safety, but the future interest paid will increase with inflation. <i>Caution should be heeded if deflation presents itself.</i></p> <p>A rising interest rate environment is positive for floating rate investments. <i>While rates are currently not rising, they are expected to rise sometime in the next 12 months.</i></p> <p>As this asset class develops and matures, there will be great potential for investors over the coming years. We will be looking to add these over time.</p>
Stocks	<ul style="list-style-type: none"> Still cautious of stocks—below normal levels of exposure Positive on preferred stocks Positive on dividend paying stocks Utilizing covered call strategies to hedge Selective of international stocks Positive on Brazil, Canada and Australia Avoid much of Europe, the U.K., and Japan 	<p>The stock market has been correcting for the past month, and reduced exposure may help protect your portfolio a bit from the big market swings. <i>Caution should be heeded if deflation becomes present.</i></p> <p>Preferred share class stocks currently seem to offer investors value based on price and yield.</p> <p>Many of the traditional dividend paying companies are more attractively valued than the general stock market.</p> <p>Covered call options strategies can provide extra income to your portfolio while you own stocks. We are looking to utilize this strategy a little more with the increased volatility in the markets.</p> <p>International diversification is still very important to your portfolio, however individual country selection will likely play an increasing role in international stock performance.</p> <p><i>Global markets have been performing poorly just as the markets here in the US have. The long-term opportunities remain.</i></p> <p>The economists and market strategists we follow have warned about Europe for almost a year, it is now front page news. Current solutions appear to be a band-aid to a much larger problem inherent in a shared currency. <i>The story hasn't changed.</i></p>
Alternate	<ul style="list-style-type: none"> Positive on Gold and Silver Negative on the Euro Positive on energy trusts 	<p>Primarily used as an inflation hedge, but also a currency hedge. The risks of global currency dilution are present. <i>Gold and silver has been performing ok during this latest flight to safety.</i></p> <p><i>Our negative outlook on the Yen has been removed due to the Yen strengthening during this flight to quality environment. We continue our long-term negative outlook on the Euro.</i></p> <p>Many energy trusts provide a good dividend source with the potential for capital gains. <i>Looking more attractive.</i></p>

Italics denote a change from last month

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Putting your Retirement Dollars on Red?

When it comes to forecasting your retirement, the label "Monte Carlo" might not be what you have in mind, but it should be. While images of gambling and exotic destinations may come to mind, using Monte Carlo simulation as an analysis tool for forecasting your retirement is the best bet for putting the odds in your favor. While the methodology has been around for decades and used in numerous fields of science, it has been rarely utilized and poorly understood by the general investment industry and thus not utilized for their clients. Monte Carlo simulation, over the past few years has finally become the method of choice for wealth professionals. Monte Carlo simulations project and illustrate the probability that you'll reach your financial goals, and can help you make better informed investment decisions.



What it takes to create a retirement forecast

All financial projections combine known inputs with assumptions to forecast unknown outcomes. In the case of a retirement projection, inputs consist of income, savings, lifestyle amount, and time; assumptions consist mainly of future inflation rates, portfolio rates of return, and a future desired lifestyle — the outcome being whether or not you run out of money. Estimating these assumptions (specifically, predicting portfolio returns) accurately is difficult at best.

So what is wrong with the way financial professionals have been forecasting retirement scenarios?

The method most commonly used for retirement analysis has always been "straight-line" forecasting. It is the simplest of methods and easiest to understand. Simply put, if you have \$100,000 today and earn a 10% rate of return over 7 years, you will end up with about \$200,000. (Your mortgage works the same way only backwards. You start with a large balance, make equal payments for 30 years, and voila' you own your house.)

But what if you don't earn 10% *each* year? When years have different returns, they can still average 10% but the end results are not the same. The results are most skewed when we have periods of negative returns, circa 2000 to 2009. It's the equivalent of noting that the average temperature in Minnesota is 45 degrees with slight chance of precipitation, and then recommending that you wear a medium-weight jacket everyday of the year. How many days out of the year do you think you'll be comfortable? I'm guessing five.

How is Monte Carlo simulation different?

Monte Carlo simulation or "Monte Carlo analysis" calculates the same scenario over and over again using a range of variable assumptions instead of a static assumption. Each "calculation" runs up to a thousand simulations. The result is a range of possible outcomes, with some outcomes more likely to occur than others. More like the uncertainty experienced in the real world. In the case of retirement forecasting, portfolio returns are the single biggest assumption with the most uncertainty. Your portfolio may be up 20% one year and down 10% the next. Monte Carlo analysis not only accounts for this, it assumes it will happen.

The outcomes created by Monte Carlo simulation are also presented in a manner that is more useful than those of the straight-line method. The straight-line method usually presents a simple summation of the average rate earned, ending with an absolute dollar value. Instead of an ending dollar value, the results from a Monte Carlo simulation are presented as a probability of success (not running out of money). For example in retirement forecasting, your results may state that you have a 60% chance of success if you retire at age 55, an 85% chance if you wait until age 60, and a 90% chance if you wait until 64. Results of this nature paint a clear image of what the uncertain future might look like to help you make informed financial decisions today. Don't bet on only Black or Red, and watch out for that pesky Double-Zero.