Smart Insights

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How Will the Market React to the Election Year?

Our clients have been asking us what to expect for the market in the upcoming election year.

Here's the answer: We don't know. We do know that of the last 24 presidential election years, 21 of them have turned in a positive performance and only 3 have been negative. There doesn't seem to be any bias for political parties. Speculating about "why" has become a popular pastime here at Smart Investments. One thought is that financial markets simply don't like uncertainty. Policies that have broad and potentially detrimental consequences for business are left undefined. That is the definition of uncertainty. It's possible that as the candidates for the office are chosen and the debate begins, investors begin to see the effects of the possible policies. That helps remove some of the uncertainty. Now in possession of some knowledge regarding possible policy results, the markets can focus on the impact of either Policy A or Policy B (depending on who wins) and develop plans for each alternative. Maybe reducing the policy shifts from infinity to 2 reduces uncertainty and allows the investors to focus on more fundamental items like earnings and balance sheets. They can also plug in the effects of Policy A or Policy B. I think what really happens is that the markets figure out that whatever the policy is, it can be dealt with. Having an undefined policy prohibits that, and puts a lid on business investment in people and production, and therefore the market. I think chances of the markets closing higher in December 2012 seem favorable if only from a historic standpoint. We should encourage our candidates to debate early and often. Let's get the issues out and in plain sight. That will not only help us all make an informed decision, but help businesses decide to take a risk and hire a few new people.

In the long run, our markets will be healthier and more profitable for it.

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MERRY CHRISTMAS and a HAPPY NEW YEAR!

One thing you can say about the investment business – it's full of ups and downs! 2011 has certainly been the proof of that theory. We have hopes that 2012 brings less volatility, and that the world economy begins to get its feet back under it.

Whatever 2012 brings, we offer you our thoughts for a Very Merry Christmas, and best wishes for your health and prosperity in the New Year!

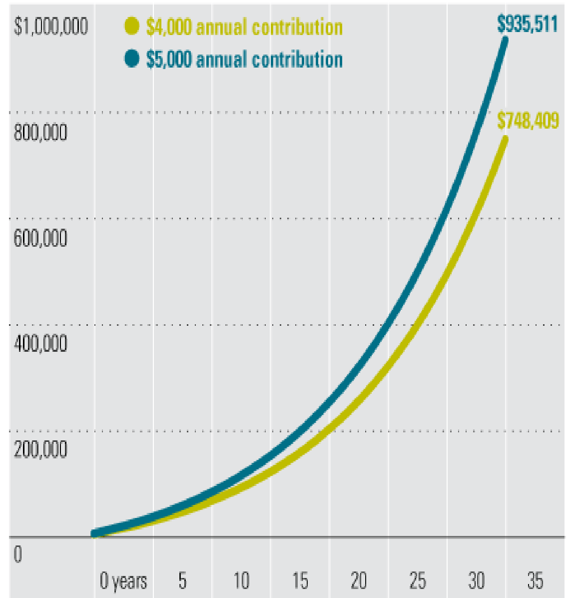
Thank you for your business!

Don’t Forget to Raise Your IRA Contribution

In 2012, contribution limits for both traditional and Roth IRAs (individual retirement accounts) will remain the same as in 2011: $5,000 a year for those 49 years of age or younger. If you are 50 or older, the maximum contribution is $6,000. This limit can be split between a traditional and a Roth IRA. These annual contribution limits are imposed by the Federal Government.

The graph shows both a $4,000 and $5,000 annual contribution growing at a hypothetical 8% annual return. Notice the dramatic impact on the ending value of the portfolio. This may be a great time to re-evaluate your financial situation and increase your annual investment to your IRA. Even if you are unable to max out your contribution, any increase you can afford may help you reach your savings goals more easily in the long run.

Hypothetical Growth of Annual IRA Contribution

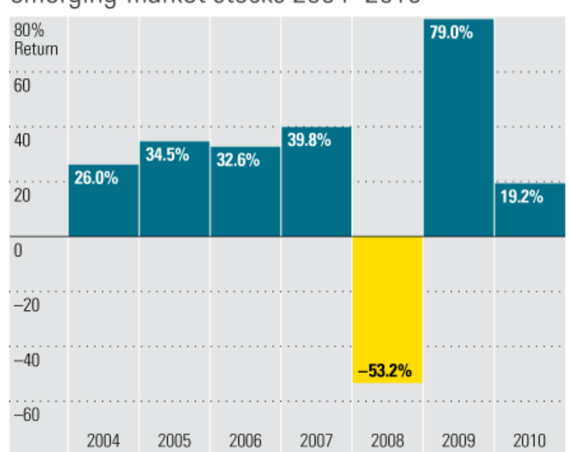


This is for illustrative purposes only and not indicative of any investment. Funds in a regular IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax-free as money withdrawn is not taxed. Penalties may apply for withdrawals prior to the age of 59 1/2.

Overconfidence: False Perception

Consider the performance of emerging-market stocks from 2004 to 2010. For the first four years, stocks in these regions produced impressive returns. Based on this stellar track record, a typical investor may expect more of the same. Well, 2008 was quite dismal for emerging-market investors, as they lost more than half of their investment—53.2%. In 2009, however, emerging markets rebounded, producing a return of 79.0%. In 2010, emerging-market returns were still positive, but down to 19.2%. When investing, investors must consider the possibility of another year like 2008 in the future. Strong positive returns may be enough to create overconfidence among investors. Investors should avoid overestimating their ability to predict future outcomes and avoid focusing on only the upside potential while dismissing the possibility of poor performance.

Historical performance of emerging-market stocks 2004–2010



Source: Emerging-market stocks are represented by the Morgan Stanley Capital International Emerging Markets Index. An investment cannot be made directly in an index. Returns and principal invested in stocks are not guaranteed. International investments involve special risks such as fluctuations in currency, foreign taxation, economic and political risks, liquidity risks, and differences in accounting and financial standards. Emerging-market investments are more risky than investments in developed markets.

What did you say?!?

From Bear to Bull, NAV to Par, making sense of all the lingo that goes along with investing can get a bit confusing. I thought it would be good to take a couple words or phrases to go over in each of our newsletters. That way we can slowly ease you in, carefully, not to bore you, with key vocabulary words! As always, we are here to help, so if there is any phrase or word that you don't fully understand, please feel free to email me and I will include that in an upcoming issue.

Bear or Bull market: Often times you will hear the talking heads refer to a "Bear or Bull" market, with no explanation of what that means. Some say the origins of these terms date back to the 17th century, from the proverb that it was unwise "to sell the bear's skin before one has caught the bear." Or it could be taken from the way the two attack. The bull starts low and thrusts its horns towards sky, while the bear attacks down upon its prey. To apply this to present day, a "bearish investor" believes the market to be on a down cycle, thus prices and revenues will decline. A "bullish investor" believes that the market is headed on an upward cycle, thus prices and revenues will increase.

Mutual Funds: What exactly is a Mutual Fund?? I like to think of them like a basket of investments! A little bit of this, a little bit of that, but with a general idea of an investment goal or strategy. Mutual funds are a great way to expand your portfolio. Instead of picking one or two stocks to invest in, you are able to invest in multiple investments. Each mutual fund is different, and they never invest randomly. Each fund manager shops for products that fit its investment strategy and manages its portfolio to meet its financial goals.

Is your goal to bring in income? If so, an Income fund might be a possible fit. An income fund would have bonds and large companies, such as Verizon or Kimberly Clark, in the basket, which would provide monthly income through dividends and principal/ interest payments. Thus, monthly income for you.

If you have some time before retirement, say 25-30 years, a growth fund would be a good selection. With time on your side, you have the chance for your investments to grow over a long period of time. These mutual funds would include smaller companies with the potential to grow over the coming years. Microsoft, Apple & Wal-Mart all were once considered small companies. Over the years, as we all know, they have become some of the world's largest and most profitable companies. These are perfect examples of what a growth stock represents.

Diversification is a useful tool to any investment strategy. Even if income is your main objective, you still might incorporate a growth fund in your portfolio along with other investments such as stocks or bonds. Although diversification does not ensure a profit or a promise against any losses, by mixing your portfolio with different funds like the ones discussed above, you have a greater chance of minimizing the volatility in your portfolio.

- Ali Arciniega

Now, Time for Some Fun Facts!!

Important Note!!

- Ali tried the champagne trick and it works!! Tip: It takes a couple minutes to get going, so be patient!!

Aoccdrnig to a rscheearch procejt at Cmabrigde Uinervtisy, it deosnt mttaer waht oredr the ltteers in a wrod are, the olny iprmoatnt tihng is taht the frist and lsat ltteer be in the rghit pclae. Tihs is bcuseae the huamn mnid deos not raed ervey lteter.

*Even Antarctica has an area code. It is 672.

*Every U.S. president with a beard has been a Republican.

*Each day, more than $40 Trillion Dollars changes hands worldwide.

*The average four year-old child asks over four hundred questions a day.

*If you put a raisin in a fresh glass of champagne, it will rise and fall continuously

*In 1987 American Airlines saved $40,000 by eliminating one olive from its First Class salads.

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