



VOLUME 2, ISSUE 3

# THE (NOT SO) ALMIGHTY DOLLAR

JUNE 16, 2008

MONTHLY NEWSLETTER AND UPDATE

Valued clients, friends, relations, competitors and professionals,

Welcome to the first monthly edition of our newsletter. If you have any suggestions or have any topics you would like to see addressed here, please e-mail Jeff at [jsproles@sprowles.com](mailto:jsproles@sprowles.com).

While doing research for a client I noticed that the 10 year average total return for the Standard & Poor's 500 Stock Index went below 10% at the end of last year for the first time since 1982. This happened as the total return for 1997 of 33.4% was replaced by 5.5% for 2007. The average annual return for the 10 years was 7.2%.

Part of this drop is attributable to the three year stock market horror show from 2001 to 2002. 2007 and 2005 delivered single digit years and that didn't help. Many of my clients were not investing during the 1970s and their perceptions of the stock market formed during the long bull market from 1983 through 2000.

I have vivid memories of 1973 and 1974. From my point of view it is important to put stock market volatility in context and not get overly concerned about relatively short term swings. Funds in the market should have a time frame of five years or more.

On the other hand, I think it is prudent to take a long view. There are some troublesome aspects about our domestic economy that do not bode well for long term prosperity. If we don't reform our profligate ways and do something about our national savings rate, trade deficit, dependence on oil and national budget it is hard to imagine a positive long term growth scenario without taking some serious medications.

Jeff Sprowles, CFP®

## Intra-Quarter Update

- S&P 500 – domestic large cap
  - 3/31 to 6/13 3.3%
  - YTD (6.5%)
- Lehman Intermediate Gov Bonds
  - 3/31 to 6/13 (3.4%)
  - YTD 0.8%
- 90 Day U.S. Treasury Bills
  - 3/31 to 6/13 0.8%
  - YTD 1.6%
- Emerging Markets ETF (EEM)
  - 3/31 to 6/13 5.1%
  - YTD (4.9%)
- Jeff's Current Stock Outlook
  - 75% of target

## MARKET COMMENTS

Most of my clients have hired me to manage their financial plan and invest a part or all of their investment portfolios. There are times when the investment part is relatively easy. This is not one of those times. The current market is what some professionals call a "trading market" which is a fancy way of saying it is volatile. This can be an indication that the market is turning and if so we might be on the verge of a bear market. One of the newsletters I take suggests that if the Dow Jones Industrials Average drops below a certain point that we are heading for one of the worst markets ever.

One can also hear professional commentators suggest that the worst of the sub prime/ credit melt down is over and the retail stocks have been beaten as much as they can be beaten.

As it happens I am relatively optimistic for the rest of 2008 and expect stocks to end the year in positive territory which is up from the present 6.5% in the red. I wish I could feel that optimistic about the long term. It is likely that my present 50% allocation to international stocks may be increased to 60% in the near future as I continue to worry about long term prospects for our domestic economy.

### JEFF'S PICK:

Brazil – EWZ

As I write this none of the stock based exchange traded funds (ETFs) that I use are particularly attractive. I have been hesitant to invest cash in the market. EWZ has a price/earnings ratio below 15. It and EWC – Canada are the only holdings I am purchasing at the moment.



Certified Financial Planner

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- - - **FINANCIAL FABLES AND SOLUTIONS** - - -

This year the Nicklebys had to pay the minimum tax due as calculated under the AMT system. This amount was higher than their regular tax liability. Because Mrs. Nickleby and her husband were unsure as to the details of AMT and why they had to pay it, they contacted their financial planner to learn more.



Jeff Sprowles and Associates LLC offered the following information to their clients:

Alternative Minimum Tax is calculated along with a person's or couple's regular tax liability. The higher of the two is the one that must be paid. AMT was created as part of the tax reform act of 1969 in response to 155 high-income tax payers escaping income tax in 1966.

What started as a way to make sure everyone has at least some tax liability has slowly evolved into many taxpayers' nightmare—despite their level of income. It is predicted that almost 1 in 3 tax payers will pay AMT by 2010.

The real problem is that politicians and taxpayers alike are in a real bind. The AMT cannot be repealed because the cost of doing so would be \$790 billion.

They have been using “patches” on a yearly basis to make up for AMT not being adjusted for inflation. The 2007 “patch” cost \$51 billion.

Among the many downsides of AMT is the way it affects singles and married couples. Singles have been and will be affected far less than married couples.

The original AMT was aimed at tax shelters. The elements most likely to push taxpayers into AMT now are a large number of personal exemptions, high state and local tax deductions and interest deductions.

**WHAT TO DO?** Calculation of AMT starts with adjusted gross income. Whenever possible we suggest those “on the cusp” of AMT problems consider tax-free vehicles for their fixed income and money market funds.

We also recommend coordination of investments and planning with accountants so penalties for under payment of estimated taxes can be avoided.



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**FACT OR FICTION??**

In last month's newsletter we discussed stock market performance in the first year of a presidential cycle. To the right is a table illustrating performance in the second year of a presidential cycle. The average from 1934 to 2006 is 10.3% which compares unfavorably to the 13.0% for all years from 1932 to 2007. It is somewhat better than the average for the first year in the cycle of 8.2%.

As one looks at the chart it is tempting to rationalize some of the big swings. P/Es ratios below 15 preceded high years in 1950, 1954, 1958, 1982 and 1986. 1998 was a tech bubble year. This kind of thing can drive one batty. The implication of the chart is that absent some powerful reasons 2010 may be higher than 2009 but lower than 2011 as far as stocks go.

I take the presidential cycle into account when I make my quarterly analysis of the current stock market. I also look at price/earnings ratio and the relationship of yield on stocks to that of 5 year U.S. Treasuries.

The current outlook is not good from a presidential cycle and price/earnings ratio point of view. On the other hand the real yield on the S&P 500 is about 2% compared to negative 0.4% on 5 year Treasuries. This suggests some combination of increase in stocks, lower corporate earnings and higher interest rates.

Year	Tot Ret	Prev P/E
1934	-1.4%	17.3
1938	31.1%	16.8
1942	20.3%	10.1
1946	-8.1%	14.3
1950	31.7%	6.6
1954	52.6%	11.1
1958	43.4%	13.7
1962	-8.7%	17.8
1966	-10.1%	18.6
1970	4.0%	18.0
1974	-26.5%	12.0
1978	6.6%	10.8
1982	21.4%	9.2
1986	18.5%	10.1
1990	-3.2%	14.1
1994	1.3%	22.8
1998	28.6%	19.1
2002	-22.1%	26.1
2006	15.8%	20.7