

# THE JENTNER REPORT

Wealth Management Strategies from Jentner Financial Group

Fall 2010



## FOLLOW THIS INVESTMENT GUIDANCE TO IMPROVE YOUR RESULTS

Would you like to improve your investment results? There may be no better way than following the recent manifesto laid out at the London School of Economics by Paul Woolley, a former top official at the International Monetary Fund and a senior fellow at the school. In his lecture Woolley advised investors to limit their annual investment turnover and to avoid hedge funds and other alternative investments. Most of all, he advised acting like a business owner.

### Earnings, not prices

Too many investors think only about day-to-day market price swings. Instead, they should concentrate on the business performance of the companies issuing their stocks: over the past 100 years, businesses have offered a 5% average annual growth in capital and an annual income payment of about 4.5%.

If you want to capitalize on those cash flows, keep your turnover down – in other words, don't do a lot of buying and selling. Turnover not only creates many transaction costs that reduce returns, it also generates short term gains that incur taxes, Woolley said.

### No alternatives

Investors unhappy with poor stock market returns and high volatility have moved money into alternative investments such as hedge funds and private equity investments.

That is a mistake. Such investments often use leverage to achieve results, borrowing money to magnify returns. Unfortunately, this can result in big losses. Another downside to such alternative investments is their lack of transparency: they don't have to report their activities in the same detail as publicly traded investments.

Woolley advises investors to stick to securities traded on a public exchange. Only those securities typically offer full disclosure and are subject to full federal and state regulation.

*Act like a business owner  
and understand costs,  
turnover and transparency.*

Finally, know what your investments cost. If you are investing in an annuity or insurance product, understand how much you are paying in fees and commissions. Insist that agents who sell you any investment or insurance product reveal how they are remunerated.

## INSIDE THIS ISSUE

- The President's Word** 2  
Duties vary by advisor
- Recent trends no guarantee** 2  
Trend-hopping can let you down
- Savings, confidence, and more** 3  
A round up of financial behavior
- Offered a high yield? Run away!** 4  
Ponzi schemes lurk in HYIPs

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## The President's Word

## INVESTORS MAY EXPECT TOO MUCH OF BROKERS, INSURANCE AGENTS



Three of four investors have unrealistic expectations of the level of care that financial advisors at brokerage firms are required to give, found a recent survey: 76% of investors said “financial advisors” at firms such as Merrill Lynch and UBS should put the client’s interests first.

However, brokers have no fiduciary duty to clients, says the report by the Consumer Federation of America, AARP, and the North American Securities Administrators Association. Brokers are merely required to offer clients “suitable investments,” a standard of care much lower than the fiduciary standard.

In contrast, Investment Advisors registered with the Securities and Exchange Commission (SEC) are required to put their clients’ interests first and to adhere to all fiduciary standards.

“Investors are clueless when it comes to the different standards of care that apply to brokers and investment advisors,” said Barbara Roper of the Consumer Federation of America.

Consumer groups are waiting for the SEC to propose a universal standard for giving investment advice, as required by the financial services overhaul approved by Congress. Most consumers support a fiduciary standard for all advisors that requires disclosures of fees or commissions and any potential conflicts of interest. The brokerage industry has given this tentative support, although insurance agents – also not bound by fiduciary standards – oppose it, based on comments received by the SEC.

Bottom line: selection of a financial advisor matters to your financial future.

Bruce A. Jentner, President  
Jentner Financial Group

## TREND-HOPPING INVESTING INVITES DISAPPOINTMENT

As decision makers we spend a lot of time on the past, projecting recent trends forward, expecting things will pretty much go on as they have been. Unfortunately, this tendency, called “recency bias” in cognitive psychology, is a poor guide for the future.

Nowhere is this truer than in investment markets. Compare gold and stocks, for example. Gold has been on a roll for 10 years as investors realize it is a store of value protecting them from the devaluation of paper money due to high government debt, and as the stock market – with price-earnings ratios not yet in the single digits – has not necessarily hit bottom.

**Gold bugs**

A decade ago gold hovered under \$300 an ounce. By early November it had surpassed \$1,400 an ounce, a gain of over 16% per year, compared to a 1% per year loss on U.S. stocks. Gold bugs believe its value will only increase by such means as government deficits, devalued currencies, even worldwide financial collapse. Many also rely on momentum: because gold has gone up for 10 years now they expect it to continue. As the price climbs, more buyers jump in.

**Not always a winner**

Every time investors get manic over a certain investment they seem to forget it can also go down. Morningstar notes that in the 30 years through July 31, gold returned just 2% per year, vs. 10.7% for American stocks.

Gold, like all investments, tends to revert in price to a mean. The last time gold rose – from \$33 an ounce to \$850 in the 1980s – its subsequent crash was followed by two decades of declines. Gold’s return since 1933 has been just 4.7% per year.

Although current trends may last some time, the idea that gold – or any other investment (remember real estate? Dot-com stocks?) – will continue to rise without fail is a dangerous belief.

Gold also provides no income to spend or reinvest, and if the price isn’t going up the owner is losing to inflation. Nor is gold cheap: if you hold it directly you pay transportation, storage, and security costs. Those same costs are subtracted from your returns on gold funds or ETFs. In contrast, in this age of ultra-low-cost trading fees, ownership costs for stocks and bonds are small.

**A bad decade for stocks**

U.S. stocks have fallen over the last 10 years, but price-to-earnings ratios have not hit the single-digit levels they did in the post-1982 bear market. Yet stocks today trade at cheaper valuations than just about any time in the last decade and dividends paid on solid common stocks are well above yields on U.S. Treasury securities.

Two bear markets and a decade-long string of losses have convinced

some investors that this is the way equity markets work. They ignore the differences between now and 1982, when inflation was very high and interest rates had soared. Today interest rates and inflation are very low and the world economy is very different. The principle of reversion to the mean suggests that the next 10 years will see above-average stock returns that will bring long-term market averages back up to their mean.

**The Jentner Financial solution**

A diversified portfolio of stocks, bonds, and commodities provides the opportunity to participate in whatever is performing well, without taking the unnecessary risk of being overly concentrated in what could be performing poorly. Diversification plus periodic, disciplined rebalancing to capture gains of appreciated investments and the purchase of investments that are out of favor, provide an opportunity to sell high and buy low.



## Savings shortfall, still confident, &amp; more

The average American household faces a pretty stiff retirement fund deficit – \$90,000 to be precise, says the Center for Retirement Research at Boston College. It used Federal Reserve statistics to look at the retirement savings of 70 million households with workers between the ages of 32 and 64. It says its estimated household shortfall is conservative, because it doesn’t project any future cuts in Social Security benefits. “It’s a measure of how far behind Americans are in their retirement savings today,” a spokesman said.

**Investors hang in**

Two years of rollercoaster financial markets have done little to shake investor confidence, says the Center for Audit Quality in Washington, DC. Its survey showed that investor confidence stands at 68%, just a little below the 70% level during the 2008 crash. However, confidence in government plans to fix the economy dropped from 31% to 22% over the last year.

**The young like Roths**

Younger savers are converting to tax-free Roth IRAs at a faster pace than any other group, says Fidelity Investments. It may be that the many years of tax-free growth ahead of them makes up for the requirement to pay taxes today on any IRAs converted to Roths.

**Social Security online**

When should you take Social Security – early, at normal retirement age, or later? In order to help you make this difficult decision, the Social Security Administration offers an online estimator to help compare different retirement options. The calculator will use your own earnings record; you don’t have to manually enter information. [www.socialsecurity.gov/estimator](http://www.socialsecurity.gov/estimator).

**Where the rich are**

Looking for a millionaire match-up for your single child? While North America still has the highest number of millionaires at 4.7 million, the Far East is becoming a good bet, says Boston Consulting Group. China has the third highest number (Japan is second) and Hong Kong and Singapore have the highest number per capita.

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## OFFERED A HIGH YIELD? RUN AWAY!

Low interest rates at the bank and scary volatility in investment markets have created a market for shady high-yield investment programs (HYIPs) that prey on unsophisticated investors, warns the Financial Industry Regulatory Authority, which regulates U.S. securities firms. If you are offered a high-yield investment that promises safety, liquidity, and above-market interest rates, don't invest anything, FINRA warns.

The FBI's investigations of high-yield scams have jumped 105% in the last year alone, FINRA says. Hundreds of websites are touting high safe yields, and thousands of investors have lost money on them.

### Nearly all are frauds

"The reality is virtually every HYIP we have seen bears the hallmarks of fraud," FINRA says. A typical HYIP is nothing more than a Ponzi scheme, using payments from new investors to pay out interest to previous investors.

The investment programs are not registered with regulators and are sold by unlicensed individuals.

The Internet has become a prime trolling ground for sales, FINRA says. Hundreds of sites tout individual programs, and other sites purport to "rank" the programs based on their performance. Shady operators have also taken to using social media like YouTube, Facebook, and Twitter to create a false social consensus on the value of the plans.

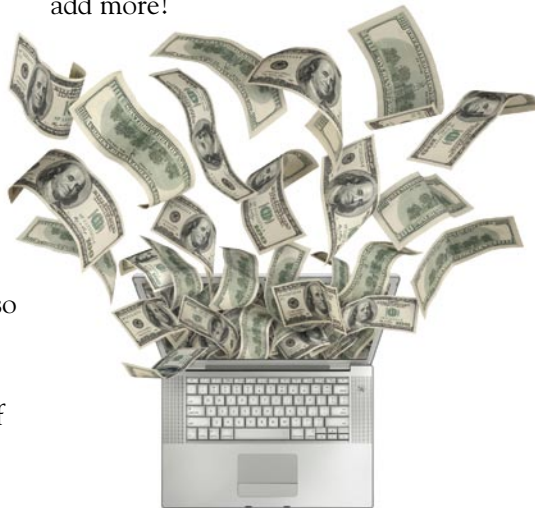
Some web sites even openly acknowledge that HYIPs are Ponzi schemes, but claim to teach investors how to get in early and get out before the scheme collapses.

### Clues to a scam

You can spot a potential scam by its claims of high, unsustainable yields, an unclear explanation of how the plan expects to make money, lack of information about the operators, operations located outside of the United States, and incentives given to recruit new investors.

Skepticism is your first defense. FINRA advises ignoring books, seminars, and websites that offer strategies for using HYIPs. You should also recognize undue persuasion at work. Testimonials and rankings are a key tactic of fraudsters. "Remember: credibility can be faked," FINRA says.

Finally, if you have already put money into one of these scams, do not add more!



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*"Financial life planning provides better wealth management by asking smarter questions, listening more carefully and applying sound financial and investment strategies to help you achieve personal and objective goals. It is not something different or new; it's simply planning the right way."*

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