A Bernanke Bump in the Road

The U.S. stock market added a positive second quarter to a solid first quarter, and finished the first half of 2013 with double digit returns. The S&P 500 index* returned 12.6% in the first half of 2013. According to the Lipper data** published in the WALL STREET JOURNAL, in the 2nd quarter, U.S. stock fund returns ranged from 0.18% for small value style funds to 4.25% for midcap value style funds. Global stock funds lost 3.05% in the quarter, and emerging market stock funds were down 7.91%. In the quarter, value style funds outperformed their growth style counterparts, and large cap funds did better than their small cap and midcap counterparts. Stocks did well from April 1st until late May hitting new highs; the overall U.S. stock market was up almost 6%. From late May to June 28th, the market gave back some of those gains, finishing the quarter up 2.72%. In June, the bond market hit the "Bernanke bump". The Fed Chairman hinted that there could be a potential tapering of the Fed's bond buying policy. The abrupt spike in interest rates caught many by surprise. 10 year Treasury bond yields rose .36% in May, and .43% in June, finishing the quarter at 2.49%. The average bond fund lost 2.22% in the quarter. Long term bond funds lost 5.3%, and Inflation protected funds (TIPs) lost 7.26%. As interest rates rose, dividend paying stocks and municipal bonds were particularly hard hit. Gold, often considered an alternative to turmoil in the stock and bond markets, also fell 23% in the quarter. As of this writing, U.S. stocks have returned to their May 17th highs, shaking off concerns about the potential actions of the Fed. However, interest rates have continued to rise. I continue to feel that stocks will outperform bonds over the next few years. History supports positive returns in the U.S. stock market in the second half of 2013. In the 116 year history of the Dow Jones Industrial Average, the index posted positive first half returns 71 times. In 50 of these years, or 70%, the second half was also positive. I do however expect at least one rougher patch before year end. There may be an opportunity to increase equity weightings at lower prices late in the summer. If you are considering any changes to your current asset allocation this year, proceed cautiously and incrementally.

★★★★★★★★★★

"The perilous search for yield continues" Vadim Zlotnikov, Alliance Bernstein, WSJ 7/1/13

★★★★★★★★★★

14 Ironwood Lane, Dover NH 03820 603.343.4388 WWW.DPLRETIREMENTADVISORS.COM

Last quarter I expressed some concerns about the excessive sale of annuity products as a solution for income needs in retirement. My concerns included the potential high cost, restrictions on liquidity, and the recent pullback by insurers of attractive withdrawal features. Last week, the Congressional Budget Office published a Working Paper entitled "Optimal Annuitization with Stochastic Mortality Probabilities" (Working Paper 2013-05). In spite of a title that only an actuary could love, and page after page of complex equations, this 44 page report written by CBO employee Felix Reichling and Wharton professor Kent Smetters came to similar conclusions. They wrote "We find that most households should not annuitize any wealth, and the optimum level of aggregate net annuity holdings is likely even negative".

Another insurance product in the news recently is Long Term Care Insurance. Long term care and assisted living services are both complex and expensive. The range of services starts with home care, (with or without medical assistance), to Senior Day care facilities, to various levels of independent living facilities, and finally to skilled nursing care. Even the Affordable Care Act did not attempt to cover long term care; the drafters deemed it too expensive. LTC insurance policies came about in the 1980s and '90s, with the intent to provide policyholders with better access to high quality nursing homes and home based health care than Medicaid.*** Unfortunately, the insurers grossly underestimated rising medical costs. Since 2010, five of the ten largest sellers have discontinued sales. For the insurers who remained in this business, annual premiums have recently increased by as much as 25% to 77%. This put their policies out of reach for many new prospects, and severely impacted existing customers. According to the American Association for Long Term Care, the average annual premium at age 55 for a LTC policy is now $2,065.00.

All insurance products are designed to address a specific risk or risks. They provide policy holders with options to better manage their risks and avoid catastrophic losses, in exchange for a premium. Insurance planning should be an integral part of any financial plan. But the above examples demonstrate that insurance products should not be purchased without careful research, and the understanding that their costs and benefits may change over time. There is no part of your financial plan that should be considered "Set it, and forget it". Do not hesitate to contact me with any questions you may have about the effectiveness of insurance products in your financial plan.

Dennis P. Lynch

*The S&P 500 Index is a price weighted index of 500 actively traded stocks. Investments cannot be made directly into an index.

**Lipper, a division of Thompson Reuters, manages a mutual fund performance tracking and rating system. Lipper Indexes allow an investor to compare a particular mutual fund to other funds utilizing a similar investment style. A Lipper index is composed of the 30 largest funds of a given investment style. For more information about Lipper's methodology, visit their web site at www.lipperweb.com/research/IndexComponents.aspx.
***WALL STREET JOURNAL, 7/2/13