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Optivest Outlook – Hope for 2011

Fourth Quarter 2010

US Economy- After a mid-year slow down, the economy is continuing to improve in an asymmetrical fashion. Manufacturing and housing are still very weak while technology, service and energy/commodities are gaining ground. The US dollar is in a global race for the weakest currency among western nations as the result of Z.I.R.P. (zero interest rate policies), continued massive Federal Reserve bond purchases and improving exports. This has caused a whiff of inflation, sending gold and base commodities higher, along with a potential peak in the price of Treasury Bonds.

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For decades, the strength of the US economy had led the way out of recessions. Not this time. America, Japan and Euroland (ex. Germany) (AJE) are all lagging and now dependent on the strength of the developing world economies. Primarily the economies of China, India, Brazil, Russia, Mexico and South Korea are leading the way with 5 to 10% GDP growth vs. 1 to 2% for the AJE. These younger populations, eager for Western style goods and urbanization, are driving retail sales, commodity prices and local inflation. Their continued economic and political stability is essential for the AJE economic recovery.

US Stock Market- Investors have been through a lot since 9/11/2001 – two recessions, wars, loss of home value and rising unemployment, which combined have greatly hurt US consumers. The stock market has reflected their sentiment, acting as a giant mood ring, changing wildly only to end up near the same levels nine years later. However, the real US economy has done much better than this sentiment would indicate. After-tax corporate profits from current profits hit an all time high last quarter and have increased at an average 8.8% annual rate since 9/11/2001 (Bureau of Economic Analysis). The problem with the stock market has been a lack of confidence, not performance in US companies.

This increase in profits, corresponding healthy large company balance sheets and sideways stock prices mean that equities are a much better value today. However, the flash crash, low CD rates, double dip fears, anti-business federal policies, potential tax hikes and high unemployment have pushed consumers into the bond market at the expense of stocks. This is alarming because retail investors are usually wrong as a herd. In March of 2001, investors had the highest amount ever in stocks; in February of 2009, they had the peak level of cash in history; and today, they have the most ever in US bonds. We believe investors crowding into bonds are courting disaster. It's a good time to start taking profits in your long-term bonds and invest in stocks for the coming recovery years. Near term, industry rotation and selectivity will be rewarded as the uneven recovery continues. In this environment, stock selection and long/short management styles will continue to outperform ETF index funds and market timing techniques. We are employing very successful stock managers in core, small cap and emerging markets to exploit these opportunities.

Fixed Income- While Optivest clients have also enjoyed outsized bond returns this year, we have transitioned into emerging market debt (non US dollar), laddered muni-bonds, floating rate funds and income commodity funds. All of which should continue to offer 5% plus yields while benefiting from the continued drop in the US dollar and eventual rise in interest rates that will hurt typical bond portfolios. A one percent move in the yield on Treasury Bonds may not seem like much, but when they go from 2.5% to 3.5%, it is a 40% gain, crushing the price of the bonds. That move may not happen until late 2011, but we are prepared.

Real Estate- The commercial real estate market is in a state of waiting. Tenants are waiting for business to pick up, landlords are waiting for relief from lenders, lenders are waiting for their balance sheets to improve and everyone is waiting for employment growth which should produce increased demand for occupancy. A few regions in the northeast and south are picking up some steam but for most, the waiting game continues. We continue to find attractive R.E.O. properties to buy at distressed levels in selective markets. Investor interest in these types of purchases has picked up and we are happy to discuss with you whether these opportunities are suitable for you.

Unemployment- The continued extension of unemployment benefits is artificially keeping our unemployment rate high. Weekly benefits, for anyone who has earned at least $11,000 in a previous quarter, are about $450 (less about $15 in state tax). This totals about $1,750 after-tax per month, or the equivalent of about $13.60 per hour (pre-tax). Move in with a friend (or back to Mom's & Dad's) and there is little incentive to work at Walmart or other available low paying jobs. Elimination of extended benefits (currently at 99 weeks) and long-term tax credits for new hires would spur supply and demand for the unemployed, and reduce our budget deficit to boot.

The Future- We believe that the spirit of innovation, economic freedom and entrepreneurship that has defined America in past crisis will again prevail in this recovery. With Republican pick-ups in both houses combined with public outcry over state and national spending, public worker's pensions, debt and taxes, the Obama Administration will be dragged back toward center politics and policies. Businesses will carefully and effectively start spending their cash hoards on growth and our economy will once again be the envy of the world. Barring a protectionism trade policy and higher taxes, 2011 should provide good stock market returns as investors' moods improve and attention is focused on how profitable our big multi-nation companies really are.

The Joy of Giving

Early in my career as a Wealth Advisor, I met a very generous man. He had sold his company for $25 million and put $17 million of the proceeds into a private foundation. Our directive, as his Money Manager, was to create $100,000 of cash flow every month enabling him to donate it anonymously to charity. This foundation was as important to him as building his business had been and he held our feet to the fire each and every month. You would not pick him out of a crowd, as he lived in a modest tract home and drove an American car, except for one thing: he always had a joyful, content smile on his face. Sure, you might think that smile was easy to achieve, as after all, he still had $8 million ($6 million after taxes). Easy or hard, it left an impression on me and a clear picture of a joyful giver.

A few years later, while volunteering with a youth organization, I learned about a poor, single mother donor. She believed in the program and wanted to contribute, but she was on a very tight budget. Her solution was to give up her daily fast food lunch and instead bring a sandwich from home, which allowed her to give $50 a month. She probably smiled too as she ate her PB&Js.

These two, along with countless others along the years, taught me that regardless of your stage in life, you can better the world around you instead of merely passing through it. About 10 years ago, my family started a family foundation so we could help fund our charitable interests. While we did not sell a business, we instead funded it with cash from my earnings; starting at 10%, then 15% and eventually 20% of my take home pay. We first funded local projects and programs with which we were familiar and then slowly entered into national and international projects. My business was growing steadily and, as the donations became more significant, we gravitated toward programs that were the most effective. Often we involved our growing children in the process and started taking our family vacations to visit and donate our time to the programs we supported.

Today, our family foundation is the Optivest Foundation and is funded from both Optivest companies. We contribute 10% of the top-line revenue, allowing hundreds of thousands of dollars to be put to great use each year. In the last couple of years, our giving has funded the construction of two orphanages and a medical clinic, rescued women from forced prostitution, dug numerous fresh water wells and sent aid to Haiti and six other countries. We also provided funding for local benevolence and scholarships. These checks are far more rewarding to write than those for things we honestly don't really need. Our family vacations have purpose and many co-workers and clients have joined us on trips to help in third world countries.

The joy of giving is not found in writing the checks but rather the joy is in witnessing lives transformed. We were in a remote part of Indonesia to see our medical clinic's first day of operation. About 30 people, many of whom had walked for two days to get there, were lined up. The first patient was a pregnant mother who was diagnosed and successfully treated for cerebral malaria. Another 48 hours without treatment, she and her unborn baby would have died. The clinic has since treated thousands of cases of malaria and other maladies.

You don't need to give financially to transform lives or make the world a better place. I have found equal joy in participating on house building projects in Tijuana, Mexico, teaching inner-city children to ski or college students wilderness skills. We all have life skills that could benefit others. And best of all, Tricia's and my behavior has seemed to rub off on our children as our boys have done Eagle Scout projects for the betterment of the community and our daughter joined the Peace Corps out of college. While my motivation to give is Biblically based, seeing a grateful recipient is motivation enough.

I encourage you, no matter in what season of life you find yourself, to invest some time and resources helping others this Holiday season. Who knows, you just might end up with a joyful, content smile yourself.

Optivest- Optivest is a regional multi-family office wealth manager specializing in helping retiring entrepreneurs. To receive their quarterly newsletter and investment commentary, contact Traci Crays at 949-363-8686 or traci@optivestinc.com.