OPTIVEST

Turning Success into Peace of Mind.

Quarterly Newsletter

Second Quarter 2011

Contact Us

24901 Dana Point Harbor Drive
Suite 230
Dana Point, California 92629
949-363-8686

or visit our website:
www.optivestinc.com

US Economy- The US Economy continues to chug along, rising for a seventh consecutive quarter, fueled by strong corporate earnings, a long awaited drop in unemployment, renewed consumer confidence and earnest attempts to focus on our out of control budget deficits - all of which caused the stock market to post its best first quarter since 1998 (after a 6.4% pull back, which fit neatly into our last quarter newsletter's 5-7% pull back forecast). However, the news has not been all good. The CPI rose almost 2% (8% annualized) over the quarter as the dollar continued to fall and commodities, led by oil, rose swiftly. Inflation is heating up around the world and foreign central bankers are starting to raise interest rates. It is only a matter of time before our zero interest rate policy comes to an end.

US Stock Market- Having risen so fast in the first four months of the year, we expect the US stock markets to enter a sideways trading zone for most of the summer before finishing up 10%+ for the year. Emerging markets, after their first quarter under performance due to Japan's supply chain and regional inflation fears, should again outperform US markets. European stock markets, driven by the P.I.G.S. (Portugal, Italy, Greece and Spain) outperformed the US markets as their serious efforts to reduce government spending and reign in debt were rewarded (are we watching?).

Interestingly, despite the Dow Jones' rise to over 12,750, it is at a lower trailing 12 month P/E ratio (15 vs. 17) than a year ago – showing that earnings have been rising even faster than stock prices. We continue to be positive on US and EM stocks, emphasizing the equity hedge fund managers we have been utilizing (call us for details).

Interest Rates and Fixed Income - Medium and long-term interest rates settled into a sideways pattern over the first four months of 2011, digesting their swift rise during the last few months of 2010. However, as QE2 wraps up over the summer and inflation continues to rise, we believe interest rates across the maturity spectrum will go up by 50 bps by year-end. Optivest clients have enjoyed outsized returns over this period as our "inflation balanced bond" strategies took advantage of these trends. Unless serious steps are taken to address our climbing debt (see below), we believe these trends will continue.

US Public Debt - According to the US Treasury Department, our national debt was $14,309,159,097,877.65 at the end of April. That is about $46,000 for each of the approximately 305,000,000 people in the US. Unchecked, this amount is expected to double by 2021 according to the Congressional Budget Office (CBO). By my estimate, this current per capita debt is higher than the net worth of 95% of our country's individuals. It is no wonder that the S&P credit agency has warned that we may lose our long standing "AAA" credit rating.

These debts eventually have to be paid. This can only happen in two ways: 1) the Federal government running at a surplus (vs. deficit) for decades from much higher tax revenues and/or significantly lower spending (aka the Ryan budget) or; 2) a severely devalued US dollar and consequential multi-year high inflation – resulting in a cheap currency to pay off old, solid currency debt. The recent battle that Congress and Obama had over reducing $38 billion from our 2011 budget (approximately 1% of our discretionary spending – Deutsche Bank) leads one to believe that current steps to address our increasing deficits have a long way to go.

However, I am nevertheless optimistic about our future. Like a home mortgage, our national debt does not need to be paid back next year. The key is to balance our budget and cap our debt at our current 70% of GDP which would result in our dollar soaring again. Wishful thinking I know, but I believe the public is finally waking up to our government spending dilemma and will now tolerate reductions in the future benefits of the seemingly untouchable programs like Social Security and Medicare (and public pensions in California). A good place to start would be indexing for our current longer life expectancy and "means testing" to extend benefits to only those without other means. These changes will be unpopular for sure, but Americans now understand belt tightening and the dangers of living beyond their means. While it will take decades of changes to fully address the problems created by decades of overspending (and inefficient spending), serious progress in this direction will boost foreign and domestic confidence in the US policy making. This in turn would unleash the current historically high levels of corporate and household cash reserves back into producing business growth. This phenomenon is now being coined "expansionary fiscal contraction" and we can all hope it starts to work soon.

Inflation - With our Federal deficit and debt problems, commodity prices surging and the US Dollar down to within 5% of its all time low, inflation is on everybody's mind. Yet Chairman Bernanke is not perturbed about run away inflation and considers recent commodity price gains unsustainable. Let me unpack why that might be true over the next 12-24 months.

Prices of all goods are subject to supply and demand and when goods get too expensive, such as $5 gasoline, demand drops and prices eventually adjust back down (like the summer of 2008). The only way that prices can sustain long-term up trends is if wages push demand. Right now, wages are not rising much and lag the CPI and other inflation indexes. Furthermore, wages are likely to lag for many more quarters as unemployment remains stubbornly high and there is considerable excess capacity in service, manufacturing and construction businesses. Interestingly, as the cost of raw materials like food, cotton, oil and metals have risen sharply over the last 12 months, US home prices have fallen 3.3% (Case-Shiller 20 city index) along with electronic items, bandwidth, and used luxury goods like boats.

Eventually, if the Dollar weakens enough and inflation pushes prices out of reach for consumers, workers will strike for higher wages. If this happens when unemployment is down and excess capacity is used up, workers will succeed. Until then, consumers have choices of how to spend their money and raw materials have limits on how high they can go before demand falls.

Summary - Every year, over my 33 years as a Financial Advisor, I have heard investors lament that "when the current market worries are resolved, they will feel comfortable and invest more." And every year, new worries crop up as old worries are resolved. There has never been, nor will ever be, a worry free investing environment. Our mission at Optivest is to sort out the potential damaging worries from the mere "noise" to capitalize and protect investor's capital as the ensuing trends develop.

For now, the global economic recovery and expansion are providing good return opportunities despite the occasional "noise" causing short-term set backs. However, we remain vigilant, watching the big worries (like our government debt) and its potential influence on the financial markets.

Mark Van Mourick
CEO

Family Office Services

We would like to remind our clients and friends about Optivest's Multi-Family Office service offerings. Like a single family office for an individual wealthy family with hundreds of millions to invest, we provide the full range of investing, financial accounting, risk management, estate planning and tax services along with concierge referral services with our economies of scale. We are providing these services both in-house and via strategic alliances with the best outside service providers. This open architecture combination of top professionals, working in concert for our valued clients, produces one of the finest advisory teams in the country.

Optivest's In-House Services:

- Investment advisory, fiduciary money management and asset allocation
- Full portfolio aggregation reporting
- Personal income and balance sheets
- Budgeting, bookkeeping and bill paying
- Tax planning, reporting and defending
- Real estate property management in 8 states through Optivest Properties

Further, we work with coordination and accountability with these important related industry partners:

Optivest's Wealth Management Alliances:

- Personal property and casualty risk management – Hubb/Chubb
- Personal health research and surgery – Private Health
- Business and estate tax planning – Brown & Streza
- Residential real estate sales and mortgages – McMonigle Group
- Local aircraft chartering – STA Jets
- Family foundation consulting – Next Generations
- Life and estate insurance – Chamberlin Group

Optivest has chosen to work with these top service providers for their excellent reputations and service to high net worth families. Optivest receives no compensation for our endorsement or referrals. We also maintain good relationship with top local high-end resorts, restaurants, jewelers, yacht charters, auto dealers, retailers, contractors and caterers through our membership in the "Luxury Marketing Council." Next time you desire a competent new relationship with one of these excellent service providers, give us a call to make an introduction for you. Our goal is to help provide intelligent peace of mind to all aspects of your life.