

# KIELY WEALTH ADVISORY GROUP, INC.



From Left To Right: Joe Kiely, Scott Below, Katie Burr, Brownie Cordell, and Kellie Kiely

## BEHIND THE SCENES

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### OPENING THOUGHTS

The end of the third quarter capped off what was one of the most eventful years in the history of our financial markets and the economy. It's been exactly one year since the weekend that shook the foundations of Wall Street (i.e. when Lehman Brothers collapsed, Merrill Lynch vanished as an independent entity, and AIG was taken over by the U.S. government). It's hard to believe, but just one year ago we were facing the vast unknown abyss of the mortgage crisis, the global financial system was on the verge of collapse, and we were about to enter the most severe recession any of us has seen. In stark contrast to one year ago, the Federal Reserve now estimates the economy grew 2% or more during the third quarter of 2009 and they believe we will see positive growth in the fourth quarter as well. In other words, the economy is far healthier today than it was a year ago and the recovery is going much better than most observers (ourselves included) expected. But while both the velocity and magnitude of the recovery have been extraordinary, we still have a long way to go before the economy returns to anything resembling "normal." Like a patient recovering from a serious illness, there will likely be some tough days ahead and setbacks are to be expected.

In light of what's happened, we believe it is important to briefly summarize where we've been over the past year, where we are today, and the prospects for a healthy economy going forward. Of course, we'll include our usual dose of financial education by highlighting a few valuable lessons from last year's near-collapse of the financial system.

#### The Sordid Details

When Lehman Brothers was allowed to fail one year ago, the short-term capital flows required for normal operations of our global financial system suddenly dried up. And with global capital flows immobilized, the global economy began grinding to a halt. This was an unsettling period because the mechanism behind the freeze-up of the capital markets was uncertainty over how tenuous the "unregulated" credit default swap (CDS) situation had become - and resultant fears over the solvency of the world's largest financial firms. (For a detailed discussion of these topics please review our 2008 year-end newsletter and our first quarter 2009 updates.) In effect, we faced an acute blockage of our most essential economic artery and the situation was very grave. Fortunately, over the weeks and months that followed, the Federal Reserve and Treasury acted as skillful financial surgeons and managed to revive the capital markets via a spate of new programs and infusion of new capital. Their

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#### BENEFICIARY UPDATE REMINDER

WE WOULD LIKE TO REMIND YOU TO UPDATE YOUR IRA BENEFICIARIES IF NEEDED! THIS IS A VERY IMPORTANT PART OF YOUR FINANCIAL PLANNING AND SHOULD NOT BE OVERLOOKED.



actions opened the capital-flow blockage and allowed the lifeblood of the economy to begin flowing again...and just in time.

**Let's Be Frank**

Most people have limited knowledge of the complexities of the world's capital markets and don't understand how important they are to our economic survival. But like arteries to the heart, financial markets are the main conduits through which everything essential for economic life flows. Without sound, efficient capital markets, economies all over the world would collapse and even the most highly developed economies would quickly revert to third-world conditions. Many people look to the stock market every day for clues to our economy's health, but the credit markets are a much bigger force in terms of economic wellbeing. When credit markets are healthy and functioning normally, all is well. But when credit flows become interrupted economies will quickly begin to wane. Fortunately, by the end of 2008, it became clear that the capital markets had been repaired to the point where they were able to support basic economic activity, even though significant impairments still remained. Since that time, the financial markets have continued to make steady improvement, but it's important to point out that they still have a ways to go before reaching the point of full recovery.

**Fear and Greed**

Unfortunately, few investors knew about the "behind the scenes" healing taking place last December and January (unless you attended one of our client dinners) and they were understandably worried about what else could go wrong. When fear sets in, investor intellect and sound investing fundamentals often get thrown out the window in favor of emotional, kneejerk reactions. Emotion causes investor's time horizons to unconsciously shorten and panicked investors tend to look for any tidbit of bad news to validate their emotional pessimism. And, given the highly sensationalistic bias of the news media, you don't have to look very far to validate your fears. Unfortunately emotions (i.e. either fear or exuberance) are poor long term investment guides. For example, in February 2000, at the apex of the tech stock bubble, a Gallup Poll asked a sample of investors: "Do you think that now is a good time to invest in the financial markets?" and 78% of respondents agreed that it was. Of course, it turned out to be a terrible time to invest. By March 2003, only 41% of the same investors thought it was a good time to invest. Of course, that would have been a great time to invest. Do you see a pattern there? The bottom line is that during February and early March of this year, many supposedly long-term oriented investors allowed

emotions to guide their investment decisions and fled from the stock market in droves...at the absolute worst possible time.

**The Numbers**

We understand why people have been concerned about their investments...who wouldn't be concerned when the media had many of us convinced we were entering the next Great Depression? This is precisely why we've spent so much time over the past year writing about investor psychology and dangers of emotionally-driven investment decisions. By educating people about the mistakes investors have made in the past, we hope our clients and non-clients alike will be able to use this knowledge to help resist the herculean pull of emotion on their investment decision making. Knowledge really is power, which is why we rely so heavily on what we call "evidence-based" investing. There are decades of research behind everything we do, from our diversification strategies - to the selection of our fund managers - to the way we rebalance our portfolios. We focus on investing strategies and techniques that have been proven to be effective over time and we avoid strategies and techniques that have proven ineffective. The numbers below tell you why this is so important...

As the returns below indicate, since the market bottom on March 9, 2009, we have experienced one of the greatest runs in stock market history. Unfortunately, for investors who panicked, the results have been devastating.

Russell Style Index Performance 03/09/2009-09/30/2009			
Value	Blend	Growth	
65.28%	59.74%	54.23%	Large
83.11%	75.25%	68.04%	Mid
81.50%	77.60%	73.77%	Small

On average, the overall stock market has risen roughly 70% since the March lows. Those who maintained their long-term focus and remained invested have recovered nicely. Unfortunately, those who panicked and sold out have missed one of the biggest market moves in our history. This remarkable bounce-



back and the recent behavior of our financial markets provide us with an excellent opportunity to reinforce a number of our longstanding educational messages:

1. *No one can predict short run moves in the financial markets – particularly in stocks.*
2. *In the short run, the stock market can be extremely volatile both on the upside and downside.*
3. *The importance of appropriate diversification has never been more important.*
4. *Stock investors must have a long term time horizon – at least five years – and must adhere to their horizon regardless of market conditions. (When investors lose sight of the long-run and focused on the short-run they become less comfortable with risk and volatility in their portfolio and are more likely to panic and sell near market bottoms.)*
5. *Investors need to focus on items they can control – like diversification, rebalancing and manager selection – rather than on things they can't control.*
6. *In today's world, investors need to expect the unexpected – and thus plan for a rainy day.*
7. *Investors need to understand the insidious impacts of fear and greed on their decision making.*
8. *The stock market, driven by emotion, tends to overreact in both directions. Large dips have therefore historically been followed by large bounce-backs.*
9. *Rebalancing should be a key component of every investor's strategy.*
10. *And as Warren Buffet says, "Be fearful when others are greedy and greedy when others are fearful."*

## SO HOW DID WE GET HERE?

Just two years ago our financial markets were characterized by rampant optimism. In November 2007, a number of indexes hit all-time highs and investor concerns were set aside as minor annoyances. During that time, we repeatedly wrote how unusual it was for us to experience such a long period without a significant (10% or more) dip in the S&P 500 and warned of the likelihood of increased volatility in the future. In contrast, six months ago the market was overwhelmed by pessimism and investor concerns were unparalleled. At that juncture we wrote about the exceptional levels of volatility these concerns evoked, evidenced by the record number of days in which the major stock indexes lost 5% or more. Many investors, it seemed, had lost all hope. But we also wrote about a

number of clear indicators that the selling was overdone and we discussed the innovative programs that were put into place by the Federal Reserve and Treasury. Of course, we encouraged our clients to stay the course and maintain their the long run focus. We also pointed out the incredible opportunities available to those investors who remained patient over time.

Today, the financial markets lie somewhere between those two extremes and many investors remain quite nervous. That's not necessarily a bad thing...as a certain level of anxiety is generally healthy for financial markets. What gets investors in trouble isn't usually the existence of pessimism or optimism - but the existence of either in excess. So even though today's balance of pessimism-to-optimism has a decided tilt toward pessimism, we don't view this as a negative. In fact, we think caution in the current market environment is probably warranted. Provided, of course, that caution doesn't cross the line into panic and elicit hasty financial decisions. The good news is that there are still many excellent opportunities for investors who are prepared to weather short term volatility. We spend a lot of time listening to what the best managers on the planet have to say and are reassured that most continue to feel there are still some very good investment opportunities for those who are selective and patient.

### The Case for Optimism: Valuations

As of October 2, 2009, the S&P 500's aggregate earnings per share (EPS) over the last twelve months was \$53. As a result, the index's current price-to-earnings (P/E) ratio stands at 19.3 times last year's earnings.

$$S\&P500's\ current\ level\ is\ 1,023 = \$53 \times 19.3$$

This P/E ratio is higher than its historical average of approximately 16.4 times earnings since 1954. This suggests that U.S. stock valuations aren't as excessive as they were earlier this decade, but it also indicates that they are also no longer cheap.

Looking ahead, First Line reports that analysts believe S&P 500 EPS for 2010 will be \$75. If these estimates bear out - and if investors are willing to pay the historical average of 16.4 times previous year's earnings - this implies a future value for the S&P 500 of 1230 - which is roughly 20% above today's S&P 500 level of 1023. (**Note:** *The S&P 500 traded as high as 1250 prior to the Lehman Brothers collapse.*) Of course, Wall Street estimates are not exactly known for their pinpoint accuracy. Still, the downturn has forced many companies to become more efficient, resulting in remarkable productivity gains



through the recession. So assuming the economic recovery continues at even a modest pace, one could reasonably expect to see a respectable rebound in both demand and revenue growth from recent levels.

However, at this point we think it's prudent to approach earnings estimates with a healthy bit of caution. If we were to assume the S&P 500 will end 2010 with an EPS of \$65, which is roughly midway between today's \$53 and the \$75 Wall Street is hoping for, and a P/E of 17 times earnings (which is reasonable because P/E ratios generally remain well above historical averages throughout economic recoveries) this would provide a theoretical S&P 500 value of 1105 - which is still comfortably above today's stock market levels. It's impossible to predict what the markets will do from year to year, of course, but these valuation scenarios suggest a strong possibility of continued gains. Additionally, keep in mind that there is about \$3.5 trillion in cash sitting on the sidelines in the wake of this recession. If the economy shows signs of significant improvement, much of that money will be forced back into the equity markets.

#### **The Case for Optimism: Common Sense**

Let's look at stock market valuations from a slightly different perspective. Currently, we know the S&P 500 is trading almost 16% below where it traded the day before Lehman Brothers collapsed, while the Russell 2000 is roughly 20% below its pre-Lehman level. In contrast to the pre-Lehman era, we know today's companies are in better shape financially, with stronger balance sheets, little inventory, streamlined labor forces, higher profit margins, more transparent books, and a stronger likelihood of positive earnings surprises going forward. One of the largest reasons the stock market has continued its positive trend over the past quarter was that fully 73% of the S&P 500 firms topped expected earnings forecasts! It's not unreasonable to expect this trend to continue as the recovery continues.

Beyond the issues facing the global economy, there are many underlying positives that are cause for optimism if we look out two or three years or more. (For an excellent summary of these positive forces, I would encourage you to read "The Case for Optimism" in the August 14<sup>th</sup> issue of Business Week.) Basically, the article notes powerful entrepreneurial forces under the surface will drive economic growth - just as they always do after recessions - and that economic growth will tend to drive stock prices up. Examples of these forces include the positive impacts of technology, the recovering US housing market, the revitalization of world economies, and the

incredible energy from the developing world's educated youth and emerging middle class. Where some see ashes, others see opportunity. And just like we saw in the stock market in March, the global financial crisis has created a wealth of economic opportunity for savvy entrepreneurs and business people to capitalize on.

#### **The Case for Pessimism**

If you want a reason to be pessimistic, all you have to do is pick up a newspaper or switch on the television. As we go forward, there are numerous issues we need to address. But it is important to remember that in contrast to last year, this time we know what those issues are. Last year, when Lehman Brothers was allowed to fail, no one knew how bad the mortgage derivatives situation was, or how leveraged the balance sheets of our largest financial firms had become. As a result, the short-term capital necessary for the global financial system to continue operating suddenly dried up because market participants had no idea who they could trust. And the global economy essentially hung in the balance, paralyzed by fear of the "unknown." We were basically in uncharted waters - blown off course by the rapid rise of unregulated and little - known financial instruments and exotic trading strategies at some of the world's largest financial services firms. In contrast, this year we know exactly what the issues are and can therefore attack them head-on and without fear. Knowing exactly what the issues are makes them no less serious, but they become much easier to address...and solve.

#### **The Issues**

The issues the economy currently faces are numerous. Among them, we feel the most important include housing, commercial real estate, health care, unemployment, bank solvency, consumer confidence, business investment, a weak dollar, U.S. budget deficits, expansive monetary policy, and global terrorism. That's just the ten economic issues we heard mentioned today on CNBC...and we could easily come up with many more. However, our greatest concern isn't the issues we are aware of - but the ones we're not aware of! Things like unregulated trading in highly leveraged and hopelessly complex financial derivatives...or a terrorist with the ability to release nerve gas or radioactive material in a highly populated area. These are the kinds of things that concern us the most. And while it is clear that we have a number of significant problems on the horizon, it's important to remember that we always have a number of significant problems on the horizon. At the end of this newsletter the "10 Questions with Joe" section will cover each of the issues listed above.



## OUR PORTFOLIOS

Over the past year we have proactively rebalanced our client portfolios a number of times to maintain target allocations given the rapidly changing financial market conditions. In January, we did our usual year-end tweaking to rebalance portfolios where needed. In February and early March, we harvested tax losses where appropriate and made strategic moves into asset classes we viewed as both grossly undervalued and of limited downside risk. These assets included discounted corporate and convertible bonds, which turned out to be very good investments for our client portfolios. As the markets have bounced back, we continue to rebalance as needed—selling asset classes that have become overweighted and adding to asset classes that have become underweighted. We believe this proactive approach has resulted in more conservative portfolios that are less risky. And we have achieved this without sacrificing upside potential.

### Being Proactive

At this point, we would like everyone to take the time to examine their portfolios carefully to make sure they are comfortable with their current balance between stock and bond funds. Based on our communications with each individual client we feel comfortable with the allocation of your portfolio. However, sometimes things change and this can affect your time horizon or your personal risk preferences. So please call your advisor if you have even the slightest concern about the way your portfolio is allocated. At this point in the year, we recognize we have had a significant rally on the upside. In fact, when you look over your personal portfolio returns you'll see just how good it has been. However, we also recognize that runs of this magnitude don't last forever. At some point a correction will invariably occur. No one knows when this will happen, of course, but you should be prepared for a potential dip and recognize that we will use any dip to rebalance our portfolios – again - just as we always do. Overall, we feel very good about the direction of our economy and the financial markets long-term, but since large rallies are often interrupted by short term corrections it only makes sense to be prepared for one at this point. So please take a few minutes to be as proactive as we are...and look over your portfolio to be sure you are comfortable with the allocation of your investments.

### Our Managers

When we build our stock portfolios, we do so with the long term in mind. Our goal is to remain fully diversified across the “entire” stock market and to use the best managers we can find for each specific area of the stock market. We you examine the returns of each of our managers please take note of the following information. First, we have seven “active” stock managers who have generated year-to-date returns in excess of 30%. Second, two of our bond fund managers are up over 30% year to date. This is a real luxury in that it has allowed us to use corporate bonds, which reduce the volatility of our portfolios, while still earning returns that beat many of the major stock indexes. Situations like this are rare, of course, but when they occur it's important to take advantage of them. We are glad we were able to both identify the opportunities in the fixed-income markets and act on them for our clients. We just hope no one expects 30% gains in bond funds over the next few quarters...

### Market Recoveries

We know not every manager is going to beat his or her benchmark every quarter, and during atypical periods like this it's not unusual to see a few managers underperform over the short run. Rapid recoveries often occur in stages, with a few very specific asset types or stock market sectors leading initially, eventually followed by others. In the current recovery, lower quality companies have been the biggest gainers to date. This means that funds with a preference for holding higher quality firms have tended to lag somewhat relative to their benchmarks. This doesn't concern us, as market leadership tends to be transitory and higher-quality firms will eventually have their day. It also provides an opportunity to buy quality assets (and managers) on sale by rebalancing away from funds that have significantly outperformed to those that have not.

### Market Returns

Before delving into the problem areas of our economy we would like to leave you with one last positive taste in your mouth. As you know, the stock market has been tale of two periods. From the beginning of the year through March 9, 2009, the stock market declined sharply, with the S&P 500 falling more than 25% and the Russell 2000 declining more than 30%. Of course, those declines came on the heels of a devastating fourth quarter of 2008. However, since hitting bottom on March 9, 2009 stocks have increased in value for seven consecutive months, with only a few short pauses. At the end of third quarter the S&P 500 was up more than 17% year-to-date, while

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the Russell 2000 was up just under 21%. This turnaround has caught almost everyone off guard – but in a good way – and has caused many to wonder if this market run can continue. We believe the answer is yes, over the long run, but we would be shocked if stocks continued going up in a straight line. As long term investors, we need to recognize that there will be bumps and bruises as we go forward. However, given the way we build portfolios, we'll be able to take advantage of these dips and we'll be able to do so in a timely manner. Now let's look at some reasons for optimism by tackling your ten questions with Dr. Joe.

## 10 QUESTIONS WITH DR. JOE

**1. Dear Dr. Kiely: I have heard a number of financial experts comment on the impending crisis in Commercial Real Estate. What are your thoughts on commercial real estate market and do you think this will derail our recovery? M. B.**

**Hey M.B.:** I have heard the same dire forecasts. Basically, commercial real estate companies and real estate investment trusts have had their rents slashed and the value of their holdings (buildings, strip malls, etc) reduced by a considerable amount. This is no different from the residential real estate market...except in one huge way, which I'll address in a second. First, you should know that our government is fully aware of the issues our commercial real estate market faces and the Treasury has thus instituted a number of programs to help ease the burden of refinancing their debt. Second, they have provided incentive to banks who work with commercial properties owners to ease their burden. Finally, commercial property owners do this for a living, so they know which programs are available, and they know how to use them. This is where commercial owners differ significantly from residential owners - they know how to use the government programs to get them through this tough patch. So, in a nutshell, there are going to be some tough days ahead in the commercial real estate market, but nothing that is not insurmountable.

**2. Dear Dr. Joe, What do you think about all of the government spending and printing of money? I believe our deficit will bankrupt our country and leave our grandchildren with nothing! Can you comment? M.P.**

**Dear M.P.:** Thank you for bringing up a very heated and controversial topic. Remember, our economy is dependent on four broad groups to drive its growth over time. In a nutshell, our economy is driven by Consumers, Business Spending, Government and Exports minus Imports. Since we know consumers and business' are cutting back, that leaves Government and Exports to drive the short term growth in our economy. (I'll cover Exports/Imports in the next question) In my opinion, when times are tough, the role of government is to get us through the short term until consumers and business' recover. When they recover, the goal (long term) should be for government to exit the picture.

From an economic perspective, if the government did not intervene in a number of financial markets, we would be in a boatload of trouble today. When you examine what the Federal Reserve and the Treasury have done over the past year, it's hard not to be impressed. In essence, they preserved our financial markets, and now have begun exiting a number of programs as private money has come in. This is how government programs should work. Many people seem focused on what's wrong with a few of the ideas rather than looking at the large number of very successful programs that have worked. For over sixty years, the Federal Reserve has managed the banking system and increased and decreased the money supply with mostly excellent results. On this front we feel comfortable.

When you examine our Fiscal policies, it is clear that we are going to have greater deficits over the short term. Unfortunately, this happens every time we have a recession. Government revenues simply decrease, while government expenditures increase. Of course, the current administration has also inherited a number of entitlement programs and a rather large deficit. And they have inherited a bloated economy that has imploded from the use of too much debt - on many levels. In our opinion, many of the emergency programs that have been instituted by our government are needed in the short run. The temporary programs like expanding unemployment coverage and "cash for clunkers" make sense to us as they bridge that gap between good and bad times. On the other hand, it is the longer term entitlement programs of Medicare and Medicaid that concern us the most, which means the U.S. deficit problem is really a health care issue over the long term. For my thoughts on health care...read on.



**3. Dear Dr Kiely, What do you think about the weaker dollar? How will a weaker dollar hurt and help us over the short and long run? Thanks for your insight. E.F**

**Dear E.F.:** At this point, a weaker dollar actually helps us by making our goods and services cheaper relative to those produced in other countries, thus making us more competitive worldwide. As our domestic companies sell more goods and services both at home and abroad, this will help our economy grow. Remember, for the longest time, our dollar was extremely strong, which made imports cheap, and exports expensive. During that time, everyone complained about the size of our trade deficit. Right now, there is a great deal of short term speculative trading that is driving the dollar down. In the short run, this helps us out. Over time, we believe the value of the dollar will increase as our economy recovers. Thus, we don't think the value of the dollar really has a huge impact on stock values and/or long term investors over time.

**4. Dear Dr. Kiely, What do you think about our health care system? J.M.**

**Dear J.M.:** WOW, talk about a loaded question!! Actually, the issue of how health care services are distributed to the public in this country is the biggest issue we will all face in our lifetimes. As a small business owner, I can attest to the inefficiencies that exist in terms of care, access, and cost. If we started a new system from scratch it would be impossible to come up with a more convoluted and inefficient system. So, how we deal with health care system over the next few years will dictate how healthy our country is...both literally and fiscally. Obviously, we need to increase competition between providers, create efficiencies with technology, reduce unneeded waste and create incentives for people to be pro-active regarding our health. If we don't tackle these issues innovatively, I suspect we will see both Medicare and Medicaid benefits greatly reduced and eventually eliminated. In the long run, if we don't fix the current system, we will have no choice...and many of the entitlement programs that currently exist will be eliminated.

**5. Dear Dr. Kiely, Can you provide an update on the strength of banks balance sheets? And can you update us on the strength of the financial system as a whole? E.O.**

**Dear E.O.:** No problem. This is one of the government's success stories. In the short run, the Fed and the Treasury provided much needed capital to the financial system and have since exited a number of the programs (like the

Commercial Paper market and TARP) as private companies have taken over. Today, banks have stronger balance sheets because they have more equity in the form of greater reserves. In fact, many of the larger banks have more reserves than they have ever had. That said we will see additional banks fail going forward and it is unlikely that we will see bank lending increase in any significant way for a while. Many observers would like to see banks lend more, but individuals and businesses that are in good shape financially, have no need to access credit at this juncture. Those that are struggling financially will have acute problems accessing credit today - but we think this reflects a return to more sensible lending practices versus an unwillingness on the part of banks to lend. The days of easy credit are over and those who can't afford loans are no longer going to get them. To us, that's a good thing in the short run and bodes well for the long-term recovery of our financial services industry.

**6. Dear Dr. Joe, What do you think about the overall economy and the how do you think the unemployment rate will affect our recovery? Also, can you provide a link to a website that examines the economy in a basic way? E.M.**

**Dear E.M.:** We believe the economy is headed in the right direction long term. However, we believe there are a number of short term hurdles that we need to work through over the next few years...many of which have been discussed above. One of my favorite websites is [usatoday.com](http://usatoday.com). If you click on the money section and scroll down past the daily market numbers on the left, you will find a very nice interactive graph called the "Economic Outlook" that uses some very nice graphics to provide info on some basic "economic indicators" like interest rates, building permits and the money supply. It's simple and fairly comprehensive and I think it portrays an accurate picture of where we're headed over the next year. Basically, the index forecasts a strong recovery in the last half of this year (propelled by the current fiscal stimulus) and a more gradual rebound in the first half of 2010. If this is true, we will see unemployment start dropping by the end of next year.

**7. Dear Dr. Kiely, Do you think the stimulus is working? E.S.**

**Dear E.S.:** In a word...Yes. Remember in 2001 and 2002, the Fed cut interest rates 17 times and our government enacted a different form of stimulus program in the form of a war. (Remember, whether you supported the wars in Iraq and Afghanistan (or not), the production of all those

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tanks, planes, uniforms, ammo, etc. stimulated the economy.) Back then, I spoke most nights and pleaded with people to invest in the stock market...if they had a long term time horizon. And of course, as it turns out 2003 and 2004 were huge years for the market. This year, the Fed and the government enacted a number of programs to strengthen our financial markets and stimulate our economy. We just experienced one of the strongest seven month runs in the stock market and our economy will turn positive this quarter. On top of that, our financial markets are much stronger than they were a year ago. So, yes, I believe the current stimulus is helping. And, while not perfect, the stimulus is clearly helping the economy recover faster than many thought possible.

**8. Dear Dr. Kiely, Why does the stock market continue to go up even with the expected deficits? B.M.**

**Dear B.M.:** The stock market is made up of almost 7000 companies. Each company's value is a function of their current price and their expected future cash flows. Some company's cash flows will be affected by our deficits, while other will grow regardless of what the deficit does. So there is no direct correction between stock market values and the size of the deficit. Furthermore, most of us have lived with deficits our entire lives. Ever since I can remember we have had significant deficits and to date they have not harmed the long term growth of our economy. If you go back and look at debt as a percentage of our gross domestic product (GDP), it has hovered around 50% of our GDP since the 1940's. For example, in 1940, it represented 52% of our GDP. In 1950, after the war our federal debt was 94% of our GDP. However as the economy expanded after the war our debt ration came down. Since 1990, when debt was around 55% of GDP, it has steadily increased to 70% in 2008. This year, the debt is expected to reach 90% of our GDP again. This isn't a concern to us unless the debt percentage doesn't return to normal levels a few years from now once the recession is over. Obviously, we all would prefer a government that has less debt versus more. But in times of recession, like now, running deficits serves as an economic stimulus and it makes sense. Running deficits in times of economic prosperity, however, is another question and it's clearly something our politicians always seem to have trouble with.

**9. Dear Dr. Joe, Is the TARP program working? W.F.**

**Dear W.F.:** Not only is it working, but the taxpayer has actually made money. Remember, most of the TARP money was invested in banks in the form of preferred stock

that paid a 5% dividend. Furthermore, since the government took a stake in those banks they basically became part owners. And as owners, they have forced their partners to clean up their balance sheets and their compensation structures. Many people have complained about the program...but the proof has been in the pudding. The government is getting paid back and they are earning a profit on the money they invested - to boot.

**10. Dear Joe, What is your biggest worry regarding the economy & stock market going forward? K.B**

**Dear K.B.:** Last quarter, I was really worried about the reappointment of Ben Bernanke. Had he not been reappointed, I would have worried about the autonomy of the Federal Reserve, which is necessary in two ways. First, we don't want politicians running our Federal Reserve and our banking system. Politics can create an unnecessary conflict of interest when it comes to monetary policy. Second, we need a voice of reason in government to put pressure on our elected officials to reduce the deficits without worrying about their job security. By reappointing Bernanke, we accomplished both goals...as he is for the short term stimulus programs, and against long term deficits.

This year, I worry about the "unknown." Today, we know what most of the economic issues are, so I don't worry that much about most of the economic issues. In a market driven economy, most of the issues work themselves out over time. Instead, I worry about health care and hope we have the wisdom to take it head on. I worry about global warming and hope we have the foresight to reduce our global "carbon" emissions. And I worry about a terrorist event, like a dirty bomb. Each of these issues is extremely serious and potentially very damaging to the future of our economy...and in the last two cases, all of mankind. All of these issues need to be dealt with sensibly and in a timely manner.



## A FINAL NOTE

As usual, we want to thank each of you for your continued confidence in our services. Our overall philosophy, which combines the best managers with research-driven asset allocation strategies, has provided excellent returns to all of us over the long term. As we go forward, we remain committed to continuing to refine and improve these proactive strategies. As always, our goal is to provide each of our clients with the best possible mix of assets given their particular situation.

If you need anything or your goals or time horizons have changed, please do not hesitate to contact us. We are here to serve your financial needs, whatever they may be. Thank you for your kind comments, your considerate referrals and your feedback regarding this newsletter.

Enjoy this wonderful fall...

**~ Joe and The Gang at KWAG**

## COMPLIANCE NOTES

### **A Personal Note from KWAG's Chief Compliance Officer**

Frequently, we have questions about our Past Performance Recommendations Chart (the mutual fund performance numbers on the following pages). Specifically, many clients have asked how often we update this chart with the most current mutual funds we are using. While we update the performance of these funds quarterly, the list of mutual funds only changes annually. A brief explanation follows:

Throughout the year we add and remove mutual funds from our "approved list of mutual funds." The reasons behind these removals and/or additions are many. For example, a mutual fund manager may have changed; the fund may not be performing like we would like; or the style of the mutual fund may have changed. Regardless of these internal changes, we only change the recommendation list you see in our newsletter one time a year. This decision is based on regulations set by the government and recommendations from our compliance attorneys. So at the beginning of each year (January Newsletter) please pay special attention to the updated funds on our Newsletter Past Performance Recommendations. This will be your performance chart for the calendar year.

If you ever have questions about a specific mutual fund, you can always contact your advisor for more information on that fund. As always, thank you for your continued confidence in our firm. Please let us know how we can assist you in any way and improve our services.

Best Regards,  
Katie Burr  
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# KIELY WEALTH ADVISORY GROUP, INC.

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### \*IMPORTANT DISCLOSURE INFORMATION

**Performance results** represent results reported by each reflected mutual fund during the corresponding time period. Kiely Wealth Advisory Group, Inc. ("KWAG") currently utilizes these mutual funds in managing actual client portfolios. However, the individual mutual fund performance results **do not** reflect the results of any specific KWAG client portfolio or any KWAG composite.

**Past performance** may not be indicative of future results. Therefore, no current or prospective client should assume that future performance will be profitable, or equal either the performance results reflected or any corresponding historical index. The historical index performance results are provided exclusively for comparison purposes only, so as to provide general comparative information to assist an individual client or prospective client in determining whether the performance of a specific investment meets, or continues to meet, investment objective(s). It **should not** be assumed that any account holdings will correspond directly to any comparative index. The performance results do not reflect the impact of taxes.

**Please Note:** the individual depicted mutual fund results **do not** reflect the results of any specific KWAG client portfolio or any KWAG composite. **For reasons including** variances in portfolio account holdings, market fluctuation, and any account contributions or withdrawals, the performance of a specific client's account may have varied substantially from the indicated reported mutual fund results. In addition, the above results only reflect the results as reported by each respective mutual fund company. Portfolios managed by KWAG would also incur a KWAG advisory fee, the deduction of which would result in decreasing the reported performance results. **For example:** a KWAG advisory fee of 1% compounded over a 10 year period would reduce a 10% return to an 8.9% annual return).

**Please Remember:** In the event that there has been a change in a client's investment objectives or financial situation, he/she/it is encouraged to advise KWAG immediately. Different types of investments and/or investment strategies involve varying levels of risk, and there can be no assurance that any specific investment or investment strategy (including the investments purchased and/or investment strategies devised or undertaken by KWAG) will be either suitable or profitable for a client's or prospective client's portfolio. **In addition,** the mutual funds depicted are funds that KWAG may utilize and/or recommend as of specific date, and are subject to change without notice. **Accordingly,** no client or prospective client should assume that the above reflected mutual funds serve as the receipt of, or a substitute for, personalized advice from KWAG, or from any other investment professional. **Information** pertaining to each depicted mutual fund is set forth in each respective fund's prospectus, a copy of which is available directly from each mutual fund company or from KWAG upon request.

**All performance results** reflect the performance results reported by each respective mutual fund to Morningstar, and have not been independently verified by KWAG. KWAG also maintains all information supporting the reflected mutual fund performance results.

**Information pertaining** to KWAG' advisory operations, services, and fees is set forth in KWAG' current disclosure statement, a copy of which is available from KWAG upon request.

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