



4th Annual Charity Golf Outing & Dinner

Save the Date

Monday, September 13th

Hopewell Valley Golf Club
Hopewell, NJ 08525

to benefit



Our goal for this year's golf outing is to raise \$25,000 for Bonnie Brae, a residential treatment and special education center for troubled adolescent boys.

Since 1916, Bonnie Brae has been helping their boys to overcome their personal and family difficulties and build new futures as good citizens—productive in their families and home communities.

Please contact us to learn more about how you can support us in our quest to help Bonnie Brae.

For more information about Bonnie Brae, please visit their website: www.bonnie-brae.org

PRESTIGE WEALTH MANAGEMENT GROUP

Retirement Distribution Specialists



2nd Quarter 2010 Newsletter

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Prestige Wealth Management Group



JULY 2010

The second quarter of 2010 reminded us that things can look unnecessarily gloomy the morning after a party. It's true that growth appears to be slowing from the first quarter, and the markets acted as if they needed to sober up from last year's stimulus-induced recovery. While many investors are still concerned about a double-dip recession, several indicators are pointing toward continued global growth.

The second quarter was a bad time for most stock investors. The Dow Jones Industrial Average (DJIA) ended the second quarter down 10% and was down 6.3% for the first 6

months of 2010, although it is up 49.3% from its 12-year low of 6,547 on March 9, 2010. The Standard and Poor's 500 Stock Index also dropped during the second quarter, with a loss of 11.9%, and was down 7.6% year-to-date. The NASDAQ fell 12% for the quarter and was down 7% for the 6 months ending June 30, 2010. Currently, the stock market is extremely volatile—in fact, for the first eight trading days in July, there has been an increase of over 6% for the DJIA, S&P 500, and the NASDAQ.

In this issue, we take a look at the impact of the European debt crisis on U.S. markets, bonds, inflation vs. deflation, Bear vs. Bull markets, balancing the budget and investing in a rising tax environment.

On a different note, plans for our 4th Annual Charity Golf Outing are in full swing. This year, the proceeds from our golf outing will benefit Bonnie Brae, a residential treatment and special education center for adolescent boys. Since 1916, Bonnie Brae has been helping boys overcome their personal and family difficulties and build new futures as good citizens—productive in their families and home communities. Our goal is to raise \$25,000 to support their mission. You should have received an invitation to participate in our golf outing earlier this month, but if you would like more information, please call us at 908.782.0001.

We continue to strive to keep you informed of the markets and tax laws. We hope that you enjoy this quarter's newsletter.

Sincerely,

Roy Williams, ChFC
Chief Executive Officer

Steven Linden, CPA
Chief Financial Officer

Tom McCabe, CPA
Chief Operations Officer



The European Debt Crisis

Many overseas stocks, especially the European stock market, took a double blow—they fell more sharply than U.S. shares in local currency terms, and the strengthening of the dollar further reduced their value when translated back into dollars. The debt crisis that spread across many parts of Europe is seen as one of the biggest threats to the performance of the U.S. stock market over the next 12 months, according to a survey of professional money managers. (Source: Russell Investments—Investment’s Latest Quarterly Survey May 31, 2010)

Investors shouldn’t totally ignore or give up on Europe—at least not yet. The weaker Euro will make European products more competitive in foreign markets. Plus, profits generated in other currencies will translate into a greater number of Euros, which means higher earnings for European companies. While these investments involve special risks including greater economic, political and currency risks, the primary reason to hold European stocks today is that they are cheap compared to most other stock market exchanges.

Bonds

For investors who own bonds, that part of your investment portfolio has most likely come through the recent market turmoil in fairly good shape. However, don’t take that steady performance for granted. While safe from a credit perspective, Treasury investments still entail interest-rate risk.

Many professional money managers worry that the huge stimulus the Federal Reserve and the U.S. government have provided to the economy over the past few years will inevitably push up both interest rates and consumer prices. While the threat does not appear imminent, it is not too early to take steps to help protect the bond part of your portfolio. That is why over the past seven months we have made significant changes in our clients’ bond portfolios. Individual situations will vary; therefore these strategies and products may not be appropriate for all investors. It is important to speak with an investment professional prior to investing or making changes to your existing portfolio.

There is still a good deal of pessimism caused by a number of recent investor concerns:

- *BP Oil Crisis*
- *Are we headed toward inflation or deflation?*
- *Lack of trust and confidence in the global economy and world leaders*
- *Social Security concerns*
- *The housing market*
- *Growing U.S. Deficit*
- *High Unemployment*

Rising interest rates and renewed inflation would be a double blow to bond investors. When interest rates rise, the market value of existing bonds falls and in an inflationary environment, the purchasing power of bonds’ fixed income payments usually drops as well. This can be more pronounced for longer-term securities.

Many factors, including the European debt crisis, have sparked renewed worries about the durability of the global economic recovery and have probably delayed the time when the Fed might start raising interest rates. Many economists expect this to begin by the first half of 2011 to hopefully avoid a return of inflation. If the federal government has to sell larger

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quantities of Treasury bonds to finance its enormous budget deficit, this would add to the upward pressure on interest rates. Higher interest rates would most likely push down the prices of many kinds of bonds.

Inflation vs. Deflation

Should you worry more about inflation or deflation? Financial markets are sending mixed signals, so it seems that investors fear both scenarios. Many economists are not worried about inflation, since the latest government figures show that U.S. consumer prices, excluding food and energy, were up only 0.9% in April from a year earlier, which is the lowest level in 44 years. (Source: WSJ, May 20, 2010, A1)

According to most economists, deflation is more dangerous than most forms of inflation. When prices fall, consumers often put off their purchases to get great bargains later. There is a significant amount of money sitting on the side in money market accounts, bank accounts and Treasury Bills—\$8 trillion, according to some estimates. When you combine a sizeable chunk of available money with extremely low interest rates (0.16% on the Treasury Bill as of July 12th, the lowest rates on record), in many cases the end result is inflation!

Hypothetically, let's review an investor that wanted to earn \$3,000 per month from their investments. If their money is invested in Treasury Bills that are earning a little less than 0.1%, in our example, the investor would need \$36 million to generate \$3,000 per month! Without that large sum, the investor would likely add money from their principal to their earnings to reach the \$3,000 mark. This would create demand for alternate investments, which might push the price up for these investments, which could lead to inflation! (Material discussed herewith is meant for general illustration and/or informational purposes only. This example is not indicative of any specific investment product or investor.)

Wall Street loves a Goldilocks economy – one that is neither “too hot” and likely to fuel inflation and higher interest rates (both bad for stocks), nor “too cold”, which often crimps corporate profits. In some respects we are seeing such an economy today, one that has struck a “just right” balance between growth and inflation. (Source: Economist June 5, 2010 pg. 18)

Bear Market vs. Bull Market

Stocks still remain under pressure, with the Dow being hurt by concerns about Europe's debt-plagued economy and China's efforts to slow its growth. While the market action during the second quarter has been discouraging, there are a number of reasons to still maintain the course:

- ***The Dow has yet to issue a major sell signal.*** The question is whether or not the pullbacks indicate a Bear market or merely a correction in a Bull market. Based upon the indicators, it is more likely that this is a blip in the Bull market—no cause for panic! Corrections are a natural part of the economic cycle. In order to plan your investment strategies properly, it is best to look at the long term rather than the short term. Corrections can be scary, but we've seen them before and we'll see them again. The retrenchment that began in late April is no different.



- **Stocks are reasonably valued.** The S&P index trades at roughly 13% expected 2010 earnings—modest relative to 20-year norms and very modest relative to bond yields. Many U.S. stocks are similarly cheap, and high-quality stocks are unusually cheap relative to low-quality stocks. Many stocks have raised or initiated dividends this year, whereas only 2 companies have cut or suspended dividends. (Source: Dow Theory Forecasts, June 14, 2010) Recent readings on inflation, interest rates, and corporate earnings (widely viewed as among the most important drivers of stock prices) have been favorable.
- **U.S. companies are holding more cash in the bank than at any point in history.** While this indicates persistent worries about financial markets and about the sustainability of the economic recovery, it may also represent a longer-term behavioral shift. Although this has helped many companies reduce their worry about short-term borrowing as banks continuing to pull back on lending, they are earning almost no interest on their holdings of cash, making it more difficult for them to achieve expected returns. Therefore, many economists believe that they are either going to use this excess cash through hiring, investments, or to make payouts to shareholders in the form of dividends or share buybacks. (Source: WSJ June 11, 2010 C1)

All these indicators are at least slightly encouraging for most stock investors. Profit-estimate trends suggest Wall Street analysts are becoming more optimistic about the future; however, there is no guarantee that these results will be achieved. Unfortunately, sentiment can change quickly at any time. Diversification is still extremely important.

There are roadblocks to a successful recovery. For example, the housing market is crucial. The severity of the recession has eroded the credit quality of many households and business borrowers, and many banks remain hesitant to lend. In addition, if interest rates increase, mortgage rates will most likely rise along with them. This would reduce the ability of some investors to make their mortgage payments and could, in turn, cause more problems for both the banking and housing economies.

Unfortunately, real estate didn't do well either for the second quarter. New-home sales fell almost 33% in May, the biggest drop since 1963 when the government began keeping records. The median price of a new home (\$200,000) is down 9.6% from a year ago. This was primarily due to the expiring of the first-time homebuyer's tax credit at the end of the quarter.

The recovery that started last summer with the help of Government stimulus now hopes to evolve into a self-sustaining expansion. In the first quarter of 2010, GDP reached an all-time high. Following the Great Depression, the U.S. took 15 years to return to its previous GDP level. Japan's growth took nearly as long to recover following its "lost decade" of the 1990s. But in just a few quarters, the U.S. economy has taken monumental steps toward recovery. (Source: WSJ, June 8, 2010 A19)

Bulls argue that corrections are part of all Bull markets and that stocks will get back on track as investors refocus on the favorable fundamentals. Bears argue that expectations for earnings' growth are widely optimistic and that stocks are not cheap considering the risk of a double-dip recession in the U.S. The outlook for many Bears is clouded by growing worries about Europe and the vitality of the U.S. job market. Jobs are a major key toward recovery; unfortunately, many economists believe that unemployment will still be above normal (8.6%) by the end of December 2011. (Source: WSJ, June 10, 2010 A8)

We also need to remember that many of the unemployed were downsized with packages and are between 55 and 65. The wave of baby boomers turning 60 started in 2006 and gets larger every year. In the foreseeable future, many of these individuals are in the unemployment numbers and are retiring early when downsized.

Although retail sales are bouncing back from recessionary lows, hiring in this sector is returning at a much slower pace. This bodes poorly for unemployed Americans who have long looked to retail for a dependable source of jobs. In the short-term, we have a jobless recovery, and if you don't have employees, you don't have customers. Only Government payrolls are up substantially year over year. (Source: Barrons, June 14, 2010 pg 32)

Federal Reserve Chairman Ben Bernanke offered reassurances about the economy in testimony to the House Budget Committee last month, saying that a new recession was unlikely and that the Fed still expected the U.S. economy to grow at 3.5% annual rate in the months ahead. However, his tone was cautious, given the headwinds facing Europe and the recent turmoil in financial markets. (Source: WSJ June 8, 2010 A19)

Balancing the Budget

Our nation's financial position does not look good. We have never in modern times faced such dangerous, ongoing imbalance between the levels of federal spending and revenues. Our federal debt represents 90% of our economic output—the highest since the end of World War II—and more than half is owed to foreigners.

In addition, we have fewer workers funding Social Security payments for each retiree and no proven plan to control rapidly rising health care costs. The primary ways to balance our budget are to curb government spending and/or increase taxes. Unfortunately, most taxpayers will be affected by these changes.

Investing in a Rising Tax Environment

This report is not meant to be political, but many of the problems that we are faced with today are the result of earlier issues. President Obama has had to “pick up the pieces” and try to reconcile these items, including dealing with the recession and the resulting significant drop in federal tax revenues. To address the mounting deficit, there have been a number of different proposals to increase taxes on affluent families.

This year, Congress enacted the largest social program in decades. To finance this sweeping national healthcare program, Congress approved an additional 0.9% tax on employment compensation in excess of \$250,000 (\$200,000 in the case of individual taxpayers) and an additional 3.8% tax on taxable investment income earned by families with Adjusted Gross Income (AGI) above \$250,000.

Furthermore, it is likely that additional tax revenues will be needed to finance mounting federal expenditures. The deficit is still projected to grow significantly, even before incurring additional costs of economic stimulus, healthcare reform, and the increase of Social Security and Medicare outlays. The bulk of new



taxes would likely be borne by higher-income families. Many taxpayers are unsure whether or not this is “fair,” for while the wealthiest 1% of Americans own 35% of the total net worth in the nation (Source: Edward N. Wolf, New York University, By The Numbers), they already pay more in Federal income taxes than the bottom 95% combined. (Source: Fortune May 24, 2010 pg 52)

There are also a number of proposed tax changes in the works. However, the odds of a tax increase will probably be higher after the fall elections—is anyone surprised? Many affluent taxpayers should also be on the lookout for changes in the estate tax laws. The estate tax expired at the end of 2009 and has been zero for 2010. Unfortunately, it is scheduled to return next year with top estate tax rates at 55%! That compares with 2009’s \$3,500,000 exemption and a top estate tax rate of 45%. Many taxpayers are expecting/hoping for a reinstatement of last year’s exemption and rates. We will keep you posted.

Conclusion

Unlike when we experienced our sub-prime crisis, Europe has not provided a fiscal stimulus. So, there is a possibility of Europe slowing down, which could then cause global growth to slow.

The problems facing the equity markets today are no longer an anomaly. The market has battled many catastrophes. Remember SARS? How about the Asian Bird Flu? Or even the Great Stock Market Crash in 1987? Guess what? The stock market is based more on psychology than on numbers. Unfortunately, confidence is an important and fragile commodity. Confidence in big U.S. banks and the resilience of the U.S. economy has been hurt by the worries over Europe’s problems, but feelings are notoriously unreliable.

Since 1950, economic expansions have lasted 6 times as long as economic contractions. Economic expansions are defined as “trough to peak” periods and economic contractions are defined as “peak to trough” periods. The average expansion has lasted 62 months while the average contraction has lasted 10 months. (Source: By The Numbers) So think long term—for yourself and your beneficiaries—and don’t forget the power of positive thinking.

One of the worst things that you can do is obsess over the stock market, minute to minute. If you do that, you’re likely to buy when people are optimistic about rising prices and the market is expensive, and bail out when pessimism reigns and the market is relatively cheaper. One of the best things you can do is to ignore the day-to-day peaks and valleys. You can ride out short-term volatility without losing sleep (or at least not much) if your food-and-lodging money is not at risk, so remember whether in up or down markets, keep a cash reserve large enough to cover your living expenses for a minimum of 3 to 9 months.

If you have any questions or would like more information on the material presented in this newsletter, please do not hesitate to contact us at 908.782.0001.

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There is no guarantee that a diversified portfolio will outperform a non-diversified portfolio in any given market environment. Rebalancing investments may cause investors to incur transaction costs and, when rebalancing a non-retirement account, taxable events will be created that may increase your tax liability.

This optimism about the future does not minimize the fact that we have gone through one of the worst economic periods in market history. Remember that equity markets are volatile and an investor may lose money and there is no guarantee that securities will appreciate. This material contains forward looking statements and projections. There are no guarantees that these results will be achieved.

The price of commodities is subject to substantial price fluctuations of short periods of time and may be affected by unpredictable international monetary and political policies. The market for commodities is widely unregulated and concentrated investing may lead to higher price volatility.

In general, the bond market is volatile, bond prices rise when interest rates fall and vice versa. This effect is usually pronounced for longer-term securities. Any fixed income security sold or redeemed prior to maturity may be subject to a substantial gain or loss. The investor should note that investments in lower-rated debt securities (commonly referred to as junk bonds) involve additional risks because of the lower credit quality of the securities in the portfolio. The investor should be aware of the possible higher level of volatility, and increased risk of default.

Investments in real estate have various risks including possible lack of liquidity and devaluation based on adverse economic and regulatory changes.

Sources: Wall Street Journal (6/8/10, 6/10/10, 6/11/10), Business Week (), New York Times (), By The Numbers (3/15/10, 5/24/10, 6/14/10), Barron's (6/14/10), Times Magazine (5/3/10), Kiplinger's Personal Finance (6/9/10, 8/2010), The Economist (6/5/10, 6/19/10), Bob LeClair's Finance Newsletter (), Forbes (7/19/10), USA Today (), Nick Murray Interactive (September 2009), Fortune Magazine (5/24/10, 7/5/10), Market Watch (7/8/10), Dow Theory Forecasts (6/14/10), Investment News (7/6/10), AARP Magazine (June 2010), Monday Morning Outlook Newsletter (6/7/10). MDP, Inc.

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