

Investor Insights & Outlook

January 2012

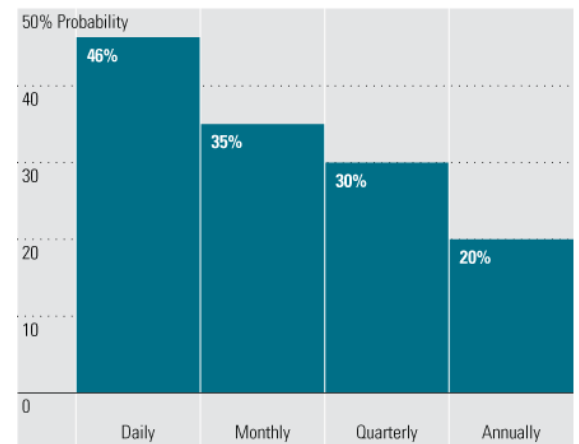
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Investment Updates

Short-Term Focus: Coping with Near-Term Fluctuations

Instant access to real-time quotes and media reports can make it difficult for investors with a long-term investment horizon to stay focused on their goals. In reality, these daily market movements may not be as extreme as they seem. As investors look longer term, their perception often changes. Short-term market fluctuations can be quite volatile, and the probability of realizing a loss within any given day is high. However, the likelihood of realizing a loss has historically decreased over longer holding periods. The image illustrates that while the probability of losing money on a daily basis over the past 20 years was 46%, the probability dropped dramatically when analyzing an annual time period—20%. Periodic review of an investment portfolio is necessary, but investors shouldn't let short-term swings affect their view of the future.

Probability of losing money in the market 1991–2010



Source: Stocks are represented by the Standard & Poor's 500®, which is an unmanaged group of securities and considered to be representative of the stock market in general. An investment cannot be made directly in an index. Returns and principal invested in stocks are not guaranteed. Probability of loss is calculated as the number of negative periods divided by the number of total periods using the specified frequency of data.



Cindy Menker
cindy@contourfinancial.com
(708) 460-3800
ContourFinancial.com

Advisor Corner

Cindy Menker, CFP™, CPA, MBA is President of Contour Financial, Inc. The firm, located in Orland Park IL, specializes in retirement planning and investment management. Tax planning, including tax preparation, is also offered.

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What Is Up with Gold?

With the runup on gold during the past few years, many investors have been enamored with its short-term performance and are aching to jump into it. Never mind that gold itself has almost no intrinsic value or that the price is largely determined by what other buyers are willing to pay. The past decade, with market crashes and uncertainty, has caused many investors to flee to the safety of gold, but looking longer term, gold might not be as attractive as it appears. An investment of \$100 in stocks beginning in 1980 would have grown to \$2,838 by November 2011. That \$100 invested in bonds over the same time period would now be \$2,186. And if one had invested that \$100 in gold in 1980, it would be a measly \$333 today.

History has shown that given the volatility of the price of gold, both stocks and bonds outperformed gold in the long run over the past 30 years by providing higher average returns. Stocks and bonds also outperformed gold over a 20-year time period. A starting point of 1980 was chosen because, not unlike today, the price of gold was then at all time highs. With gold fervor rampant, a speculative investment in gold, then, would have resulted in not-so-stellar results today, even with gold's recent performance.

Gold is not without its merits. It has traditionally been considered a good hedge against rising inflation rates, given its ability to preserve purchase power. Gold is also commonly considered a safe haven in times of political and currency crises. As fears of a double-dip recession mount, gold may be considered a tool for diversification, because it generally does not react identically to the same economic or market stimuli as stocks and bonds. A well diversified portfolio of stocks, bonds, and gold has the potential to produce a more appealing risk-and-return trade-off over various time periods.

Compound Annual Returns

	1 yr	3 yrs	5 yrs	10 yrs	20 yrs	30 yrs
Stocks	7.8	14.1	-0.2	2.9	8.3	10.8
Bonds	19.4	8.5	9.5	8.4	9.0	10.6
Gold	26.2	28.9	22.0	20.3	8.1	4.9
60/40 portfolio	12.9	13.2	5.3	6.2	9.4	11.4
50/40/10 portfolio	14.7	14.6	7.4	7.9	9.5	10.9
50/30/20 portfolio	15.3	16.5	8.5	9.0	9.4	10.4

Diversification does not eliminate the risk of experiencing investment losses. Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Gold, like any other coin or bullion, is subject to investment risks like perceived scarcity, its quality, current demand, market sentiment, and economic factors. There are material differences between investing in gold versus investing in stocks and bonds. Such differences may include investment objectives, costs and expenses, liquidity, safety, fluctuation of principal or return, insurance, tax features, and any other investment characteristics.

Source: Data as of November 30, 2011. Stocks in this example are represented by the S&P 500® index, which is an unmanaged group of securities and considered to be representative of the U.S. stock market in general. Bonds are represented by the 20-year U.S. government bond. Gold is represented by the Federal Reserve (2nd London fix) from 1980-1987 and the Wall Street Journal London P.M. closing price thereafter. Portfolios are rebalanced every 12 months.

Common Investing Mistakes

Almost all of us have made investing mistakes. The key is not to make the same mistake twice. These mistakes can directly affect whether or not you achieve your desired goals. By repeating even just one mistake, individual investors can quickly become their own worst enemy. Below are some common mistakes that many fall prey to and some suggestions on how to sidestep them.

Starting Too Late

The first mistake a large number of investors make is waiting too long to initiate a long-term investment plan. The earlier you can start the investment process, the more likely it is that the plan will succeed. For example, let's consider two investors—Bill and Tim. Bill began investing \$5,000 per year 30 years ago. Tim began investing \$10,000 per year 20 years ago. Assuming a hypothetical return of 10% per year, Bill's ending wealth value was \$822,470 compared to \$572,750 for Tim. Thanks to the power of compounding, a small amount of money, wisely invested early on, can turn into a large sum over time. Avoid procrastinating; start investing today.

Lack of Diversification

By investing all of your money into just one asset class, industry, or company, you are placing all of your eggs into one basket—and this can be extremely risky. It is better to combine a variety of investments, such as stocks, bonds, and cash, which are unlikely to move in the same direction. Your risk exposure should be lessened as a result.

Chasing Past Performance

Yesterday's hot stocks or mutual funds may not be today's best investments. A good number of investors purchase assets when they have already reached their peak, only to watch their performance subsequently suffer. It may be a good idea to choose investments with a history of good performance as well as quality management.

Lack of Research

No matter what type of investment you plan to make, be sure to conduct the proper research. It is unwise to allocate your money to an investment you do not understand. There are a number of helpful resources that you can explore—ranging from public information to professional advice. Take advantage of these when possible.

Unrealistic Expectations

Many investments require time to grow. Investors often become frustrated with the early performance of their investments, decide to sell too quickly, and move the proceeds into other investments. This will result in too much trading, which is not only expensive, but also usually unnecessary. It is important to maintain a long-term view and to not be distracted by short-term results.

Overconfidence

Confidence is a good thing, but overconfidence can cause investors to improperly select investments. Too much assurance in one's knowledge and ability can lead investors to focus on the upside and deemphasize the potential downside of investments. Instead, a solid financial plan constructed by a professional can go a long way.

Monthly Market Commentary

2011 ended with the S&P 500 almost flat after a tumultuous year. As Europe continued to be of concern, markets loved the coordinated central bank maneuver that ensured liquidity across global financial systems in order to calm panicky investors. Although a global economic slowdown is very real, given the possibility of a European financial contagion and a slowdown in China, the U.S. could potentially be the engine of worldwide growth in 2012.

Employment: December saw the addition of 212,000 private-sector jobs, mostly from large increases in delivery personnel, retail sales workers, and construction workers. The holiday season and the boom in online shopping activity accounted for the two former, while unusually warm weather in December helped the latter. While sizable, the private sector has lost 8.8 million jobs throughout the recession and has only gained back 2.8 million of these jobs. At current growth rates, three additional years are still required to recoup all these jobs. The government sector, on the other hand, continued to shed jobs (another 12,000 jobs in December). This brings the total number of government jobs lost since the recovery to almost half a million. The unemployment rate fell to 8.5% in December, aided mainly by increased employment with some help from labor force dropouts.

Manufacturing: Both government new-order reports and industrial-production reports indicated that the U.S. industrials sector was not declining, with some reports even showing signs of modest growth. Positive new-order reports are particularly important—they help predict production and employment in the upcoming months. The most-recent durable-goods order report reflected strong numbers for autos and airplanes, while others, such as non-defense capital goods, slowed. Higher inventory levels and better pricing for autos and Boeing's anticipated production jump to satisfy deliveries for its 787 Dreamliner contributed to these numbers.

Consumer: This holiday season was a great time to be a consumer, as opposed to a retailer. As

consumers continued to spend and take advantage of phenomenal deals and discounts, some retailers saw their margins decline as a result. Luxury and low-end retailers did relatively well, but companies serving the middle market, such as Best Buy and Target, struggled. Apparel companies were hit especially hard, given the unusually warm weather in December.

Housing: Stringent lending standards and general attitudes toward home ownership continued to hold back the housing market despite housing affordability remaining at a record high with low prices and low mortgage rates (now below 4%). This could be seen in the 7.3% jump of pending home sales (homes that go under contract but have yet to close, pending appraisals and financing) in November compared with October, which are now at their highest levels in 19 months. However, the housing market continues to underperform, and home prices are still more than 30% below previous highs over the last decade. A catalyst, such as a stronger employment market, may be required before the housing market starts to improve significantly.

Year-end Insights: 2011 saw the U.S. economy grow, but at a much slower rate than predicted by many economists. Poor weather, oil and gas price shocks caused by political unrest in the Middle East, and supply-chain disruptions related to the Japanese tsunami all contributed to the first half's abysmal growth rates. Growth accelerated, as oil and gas prices fell back down and production facilities came back online in the second half of the year. 2011 also brought to light the severity of the European sovereign debt crisis and the slowdown of China's economy, causing investors and companies alike to sit on the sideline, weary of another global recession. Morningstar economists believe that the U.S. economy has more potential for upside than downside in 2012 as consumers continue to spend, manufacturing picks up, U.S. oil production increases, and the housing market becomes stronger.

About Contour Financial

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 Cindy Menker

Contour Financial
9031 W 151st Street
Suite 107
Orland Park, Illinois 60462

cindy@contourfinancial.com
ContourFinancial.com

Tel: (708) 460-3800
