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DEEP ROOTED THOUGHTS

FEBRUARY 2010

Why would I want to pay tax on my entire IRA now?

Throughout my career, I have found incredible consistency among the clients I have assisted in their desire to minimize their income taxes to the fullest extent allowed by the law. In 2010, the government has created a window of time during which all taxpayers, regardless of their income level, can convert their Traditional and Spousal Rollover IRAs to Roth IRAs. Roth IRAs are wonderful investment vehicles which grow tax free like Traditional IRAs but have the added benefits of tax-free distributions and no requirement to take minimum distributions upon reaching age 70. The catch to the conversion is that you must pay income tax on the entire taxable distribution from your Traditional IRA at the time of the conversion. (There is an election that can be made to defer the income tax over the 2011 and 2012 tax years, but the fact is that the income tax consequences are unavoidable upon conversion.)

Assuming your income tax rate stays constant from now through the years during which you will withdraw funds from your IRA, there is no difference in the amount of dollars you will receive after taxes whether you convert to a Roth IRA or not. However, current and future tax rates are only one of the factors to consider when evaluating Roth IRA conversions.

So who should be doing Roth IRA conversions this year? Clearly there are some situations that are perfect candidates and others where the conversions may be detrimental. The challenge is in analyzing the situations that are less obvious and determining which families would benefit from the Roth structure despite the near term tax consequences.

If your facts fit the following pattern, you should strongly consider converting some or all of your Traditional IRA in 2010:

- You have taxable accounts which can pay the taxes due on the conversion
- You have a large Net Operating Loss (NOL) carry-forward from your 2009 income tax return that can offset the income generated from the conversion
- You are NOT in the highest marginal income tax bracket
- You do not anticipate rapidly spending down your IRA account or may never need to touch your IRA accounts in retirement due to the availability of other funds
- You think your future tax rates will be the same or higher than they are now

If you have non-IRA accounts with which you can pay the taxes due on a conversion, the math reveals that you will benefit from doing a conversion because you will have a relatively larger portion of your wealth in a tax-free account following the conversion than you did previously. This will allow for greater growth of your investments.

If all or most of your wealth is held in Traditional IRA accounts, the arguments for converting are not as compelling. In fact, you should not rush to convert if your situation includes the following:

- You are living primarily on your IRA accounts
- You are in the highest marginal income tax bracket
- You have minimal investment assets in taxable accounts
- You believe your future income tax rates will be lower than they are currently
- You have a short life expectancy

There are other factors that make converting more or less attractive but the major ones are included above.

The flexibility available for conversions is significant. You can choose to do a partial conversion rather than a complete conversion. You can reverse the conversion the following year if the account has declined in value. You can create multiple Roth IRAs from a single Traditional IRA.

One conversion strategy that takes maximum advantage of the rules and provides the highest likelihood of success is converting a Traditional IRA account into multiple Roth IRA accounts. Each of the Roth IRA accounts would have a specific investment focus. For example, you might choose to have a Roth IRA account invested solely in emerging market stocks, small company stocks, real estate, or other asset classes with high expected returns and correspondingly high volatility. If all the Roth IRA accounts appreciate in value the first year, they can be combined into a single account for simplified management the following year. If one or more of the Roth IRA accounts loses value, you can reverse the conversion for the account(s) that loses value while retaining the benefits of the accounts that appreciated.

There are no taxes or penalties related to reversing a Roth IRA conversion but the reversal must be completed by the income tax filing date of April 15th or as late as October 15th of the following year if extensions of time to file are granted.

2010 presents us with some new financial planning opportunities and challenges. The ability to convert Traditional IRAs to Roth IRAs is just one example. As always, we look forward to discussing the opportunities with you and helping you find the most appropriate solutions.

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DEEP ROOTED THOUGHTS

MARCH 2010

B

ottoms up!

One year from the bottom of the worst recession in our lifetime, it is important to reflect on the recovery and the lessons learned about financial risk taking. Through March 19, 2010, the S&P 500 stock market index has risen over 71% from the low set on March 6, 2009. The most recent twelve month market performance is the best twelve month post-recession performance in U.S. market history. Despite this impressive return, a 132% improvement is required to raise the market back to the peak level attained in October of 2007 from the lows set in March of 2009. Thus, we are still in need of a few more years to fully recover the losses in the stock market. In fact, we will need to average 17.6% annually to complete the recovery in the next two years. If the stock market advances at around six to seven percent annually, it will take five more years to complete the recovery.

For Oak Wealth Advisors clients, the loss in portfolio value from the recession was painful but nothing close to the 57% decline for the market. In most client portfolios, new high water marks will be set in 2010 as the recovery from the March 2009 lows continues. The biggest reason for the faster recovery has to do with staying invested in the market with well diversified portfolios. Rebalancing and tax loss harvesting also add value to the portfolio management process as does the implementation of low cost, tax efficient investments.

We can all take comfort that the average bull market lasts for fifty-six months. While our most recent bear market plunge needed only seventeen months to completely erase the sixty-month bull market run that preceded it, we are now starting the thirteenth month of a new bull market. We should probably not expect a ten-year bull market run like the one we had that began back in October of 1990 that drove the S&P 500 up over 400%. The market fundamentals do not portend such significant growth in the stock market in the near future. Hopefully, we can achieve moderate growth as the economy continues to recover and consumer confidence continues to build.

As the market recovery allows us to safely peek out from the shells that many had been hiding under during the recession, we can look back and find four truths that we should never forget regarding investment risk.

First is the importance of liquidity. It may feel great to have wealth on paper, but what really matters is wealth that can be monetized. In times of trouble, cash is king. If your wealth is illiquid, recessions can be especially painful. During the recent recession, investors who were forced to sell their illiquid assets in some cases received pennies on the dollar for what the carrying value had been for their investments.

Oak Wealth Advisors has always favored and only recommends liquid investments. Many firms attempt to differentiate themselves with access to illiquid investments that can give an investor a feeling of being special. While the diversification benefits of owning an illiquid investment can statistically benefit a portfolio, after factoring in expenses, taxes, the lack of access to information, and the inability to cash out on demand, they are much less attractive for individual investors. In fact, the incremental diversification benefits of illiquid investments like hedge funds, private real estate deals, and venture capital opportunities are minimal for an investor who already holds a well diversified portfolio. In summary, if the investment requires you to sign a legal agreement, you probably should not be investing any money that you consider essential for your well being.

The second truth is that you should never own anything that you do not understand. Surprises are great for kids' birthdays. They are much less enjoyable when they hit your investment portfolio. The swings in the prices of stocks and bonds, known as the volatility of their prices, have gotten more extreme over the past decade. Sometimes the prices rebound; sometimes they do not. Understanding an investment's inherent risks, cost, tax characteristics and purpose in a portfolio are key elements in avoiding negative surprises.

The third lesson is that over-reliance on models can be dangerous and potentially catastrophic. Whether the model forecasts your annual living expenses for the rest of your life, your net worth at various ages, or the growth of a particular investment, no financial model can deliver foolproof results. The financial services industry is filled with sales people armed with financial models developed by impressive staffs. They provide beautiful, compelling illustrations that often provide comfort in numbers. The sad fact is that the numbers are stale and unreliable shortly after they are created. The variables used in the models are constantly changing and often in unpredictable ways. The best solution to evaluating your needs and resources is to periodically update the numbers that you are reviewing and reflect on whether or not you are progressing toward your goals.

In the investment world, there are numerous examples of investment firms who developed sophisticated models that they believed would provide better than market returns. While many may work well in the short term, most will fail over longer periods of time. We have seen and read stories about overconfidence in models leading to the destruction of firms and it is a leading reason for the collapse of the derivatives markets in 2008.

Finally, the fourth point to remember is that that the types and sources of risks are continually changing. This is the most challenging of the lessons because it requires us to remain diligent and circumspect. Even if you could develop a bulletproof solution for your portfolio incorporating all knowable information today, tomorrow brings new developments and potential challenges to our future success. Asking questions, staying informed, and never becoming complacent are our best defenses against risks to our financial well being.

Oak Wealth Advisors appreciates the confidence that you have placed in us and we look forward to riding the current bull market with you. We promise to keep the most recent recession's lessons in mind and will endeavor to keep you apprised of new potential risks as they arise.

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DEEP ROOTED THOUGHTS

JUNE 2010

Sovereign debt? That's someone else's problem, right?

Nations get into trouble when they do not manage their financial affairs prudently. Often it seems the easiest way to balance a budget is to simply borrow the money that is needed. Sovereign debt includes borrowing in the form of bonds, bills, and notes issued by a country's government. The media has recently begun to highlight the large debt burdens that many countries are facing. This article provides more information about how this phenomenon of increasing sovereign debt is impacting global economies and individual investors.

Until the last century, the responses to countries not honoring their debt obligations were relatively easy to anticipate. First, the country that was owed the money would stop doing business with the country that failed to pay its obligations. Next, if the army of the country that was owed the money was superior to the country that did not pay, they would often attack and take physical assets as repayment with a little extra extracted as payment for overdue interest and penalties. While this is now considered barbaric for civilized countries and is greatly complicated by the interconnectedness of the global economy, it was relatively efficient and served as a strong deterrent to avoid debt crises.

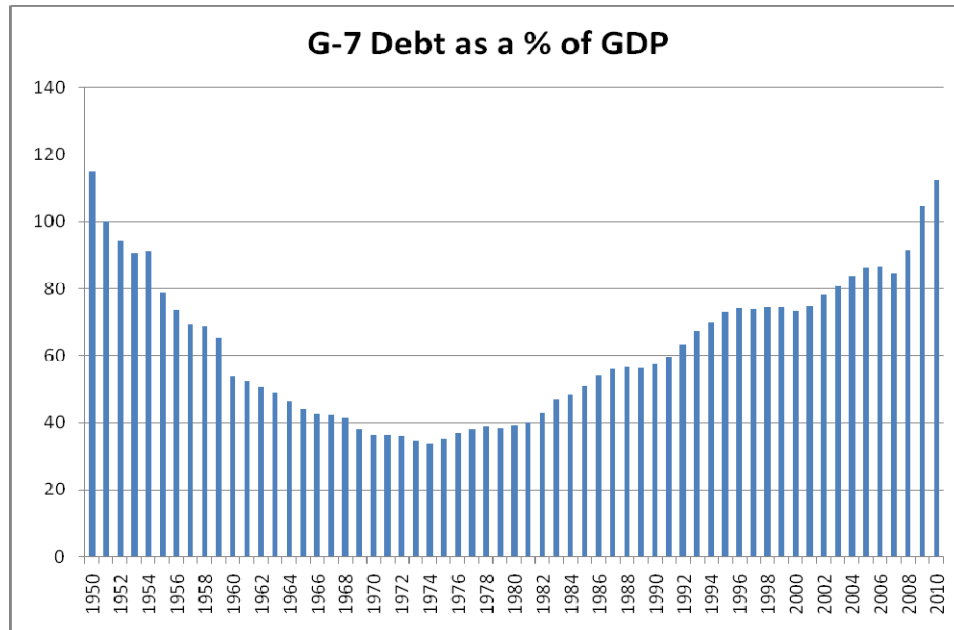
That was then, this is now.

Today there are many countries with bulging debt burdens, not just one or two as we have experienced in the past. The levels of debt have risen to high levels at a period when interest rates are at historic lows and we are in a global recession. The recession and low rates increase the difficulty the various countries face in rectifying the situation.

While the sovereign debt levels complicate international relations and trade, they also impact individual investors indirectly. While there is no immediate need to load up on ammunition and non-perishable food, better decisions can be made if we understand the current conditions and have a framework for how sovereign debt crises have played out in the past.

Governments have been defaulting on their debt for as long as records have been kept. At the annual Chartered Financial Analyst conference I attended in May in Boston, Niall Ferguson, a Harvard professor who is widely considered to be the world's leading economic historian, illustrated how Greece has been a perpetual offender. In addition to not being surprised that the Greek government recently repeated its previous financial failures, he offered some sobering statistics about the magnitude of the current global debt load.

As the chart below illustrates, even the seven industrialized nations that have led global growth for the past century are incurring debt loads that are reminiscent of where they were at the end of World War II. The G-7 consists of the United States, Canada, France, Germany, Italy, Japan, and the United Kingdom. The countries in the G-7 have debt loads that are now exceeding their total annual productivity. In simpler terms, they owe more than they make.



Source: IMF

The debt loads have arisen due to structural failures to balance budgets, recessionary growth declines, and most recently bail-out funds related to the global real estate and financial crises. Most experts agree that these numbers are likely to get worse in the near future. In fact, the Organization for Economic Cooperation and Development (OECD), which includes North America, Europe less Russia, Australia, and New Zealand, forecasts that their 2010 budget deficits will be six-times higher than they were in 2007 (prior to the recession).

Some countries whose sovereign debt burdens have been in the news recently include:

| <u>Country</u> | <u>Debt as % of GDP</u> |
|-----------------------|-------------------------|
| Japan | 227.0% |
| Greece | 115.0% |
| Belgium | 102.7% |
| United States | 93.6% |
| United Kingdom | 81.7% |
| Ireland | 75.9% |
| Spain | 69.6% |

A recent study by Credit Suisse evaluated the riskiness of sovereign debt for twenty five nations across multiple factors. Their research pegged Iceland and Greece as the two riskiest countries. No surprise there. India and Brazil, two emerging economies that had been considered very risky just a decade ago, were rated in the top third. Disappointingly, the United States was right in the middle with nations such as Argentina, Columbia, and Kazakhstan rated safer. While we have no interest in buying any bonds issued by Kazakhstan, it is disconcerting to see how the debt levels of the developed nations have negatively impacted their credit worthiness.

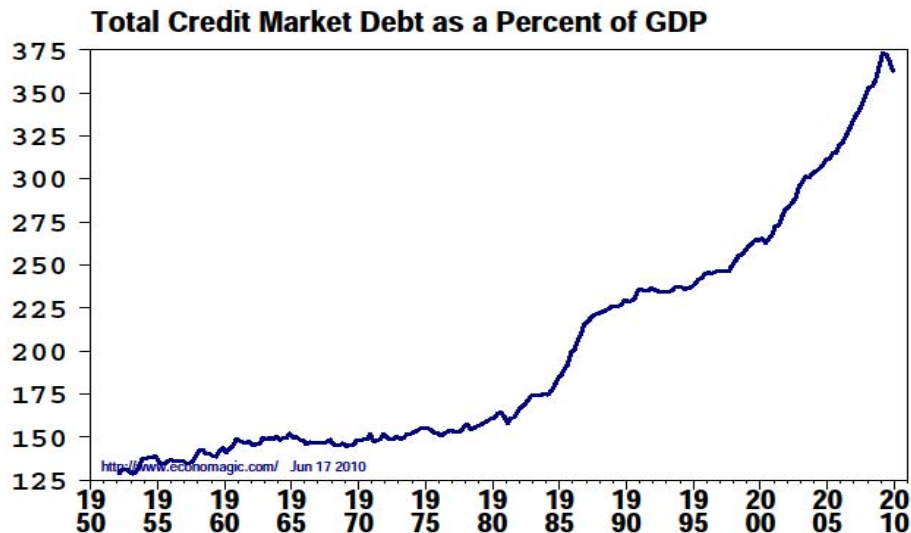
What can be done?

As Niall Ferguson points out, fiscal reform (spending less and taxing more) becomes increasingly challenging when the majority of people are receiving entitlements and transfers and are not paying into the system. This is currently the situation around the world. Inflation, which devalues the outstanding debt, can work assuming those who hold the debt do not object to getting paid less in real terms. With more than half the U.S. debt owned by people and entities outside our borders, it is unlikely that they will accept this solution. Global growth can also close the gap but it will be constrained by higher taxes, increased government regulation, higher tariffs and other trade barriers, and decreased leverage at both the corporate and household levels.

As bad as the situation is in Japan, almost all of their debt is owned by the Japanese. Therefore, their government can keep rolling over the debt with fewer consequences because they are just delaying repaying themselves. Conversely, the United States now has numerous creditors around the world who expect to be repaid on schedule.

There are no easy answers to reduce the global debt levels. The few courageous responses that have been offered recently have come from across the pond. Newly elected British Prime Minister, David Cameron, explained “The decisions we make will affect every single person in our country. And the effects of those decisions will stay with us for years, perhaps decades to come.” In Germany, Chancellor Merkel is pushing for similar austerity measures. While the austerity policies are not politically popular, they seem essential if we want to return to the prosperous growth levels that were enjoyed in the last two decades of the twentieth century. As the G-7 debt chart illustrated, it took decades to build the debt levels to their current state. It will likely take another decade of concerted and coordinated efforts to reduce them back to more acceptable levels.

In the United States, where the sovereign debt level is now around 90% of GDP, a more shocking picture emerges when the total credit market is evaluated relative to the country's output. If household, corporate, and financial institution debt are added to the government debt total, then we are actually carrying a composite debt burden that is over 350% of GDP. The amount is almost triple where it was in the 1950's. Over the past two generations, American businesses and American households have increased their borrowing in pursuit of more. We are probably going to have to be satisfied with less in the next decade if we intend to rein in the outstanding debt.



Even J.P. Morgan, who is relatively bullish and feels that the U.S. consumer may be able to buy enough goods and services to mitigate the global debt crisis, soberly observes that increased global financial regulations will add further constraints to the growth of economies and add additional governmental costs which will likely need to be paid for with more debt.

PIMCO, arguably the world's most respected bond manager, projects a very bumpy five-year period for the investment markets. PIMCO feels that stagflation (high inflation coupled with high unemployment) is possible in the United States due to recent policy decisions and the potential pull-back of consumer spending. Globally, they feel that the United States is still the safest country in which to be invested, however they point out that the developing economies of Brazil, India, and China provide higher growth opportunities than the U.S. or any of the other G-7 nations. Interestingly, Brazil, India, and China also have much lower Debt-to-GDP ratios than most of the developed nation economies.

PIMCO also cautions that we should expect more extreme outcomes (both positive and negative) than we have seen in prior decades as countries work their way out from their debt burdens. Their official outlook is for investment returns to be in the 4% to 6% range, before taxes and expenses, for a diversified portfolio for the next three to five years.

At the individual level, these global challenges require a re-evaluation of the expected returns from the investment markets and some recalculations regarding how much can be safely withdrawn from a portfolio by those who are in retirement.

In what should we invest?

The answer is probably not gold. Many pundits have suggested that gold will always be a safe investment and could triple in value if China requires the U.S. to back its currency with gold. Maybe. With the current price of gold hovering near \$1,250 an ounce it seems to be shimmering. In 1980, gold was \$850 an ounce. On an inflation-adjusted basis, that one ounce of gold from 1980 should be worth \$2,400 today. It is worth only half that much. Therefore, I am not convinced that gold is a great store of value nor a great hedge against future inflation.

Bond investing becomes more challenging as fears of rising interest rates, inflation, credit downgrades, and slower growth combine to depress bond prices. It is also unclear whether longer-term interest rates will rise when the U.S. government eventually raises the short term rates. The uncertainty around bonds leads to greater discounts being applied to their values. Credit quality and yield have become increasingly important in evaluating bond investments.

Stock market volatility makes holding large positions in stocks uncomfortable for many investors. However, stocks have historically been a great way to overcome inflation and grow wealth. Even in low return environments, all portfolios should have exposure to stocks.

A well diversified portfolio with a variety of investments that are not highly correlated will help avoid major losses in wealth. We will continue to seek new, viable investments and approaches that increase the diversification in client portfolios and help to improve expected returns while decreasing the volatility of the portfolio. History suggests that periods of lower returns should be expected. If lower returns are unavoidable, keeping costs low and tax efficiency high will allow investors to keep the greatest percentage of available returns. We must keep faith in human ingenuity and investment market resiliency. Better days will follow. Much as we saw in 2009, they can come quickly and trying to time them is impossible.

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DEEP ROOTED THOUGHTS

AUGUST 2010

Bond bubble? Aren't bonds supposed to be safe investments?

The perception has long been that investing in bonds is a safe way to generate investment income without much risk. Today, numerous articles and letters to the editors of financial publications are sounding the alarm bells about the risks of investing in bonds. This issue will address those warnings and explain a prudent approach to bond investing in the current market.

Is there a bond bubble?

In an August 18, 2010, letter to the editor at *The Wall Street Journal*, Wharton School finance professor Jeremy Siegel refers to the current state of the investment markets as the Great American Bond Bubble. Based on the historically low rates currently available for investing in U.S. Treasury bonds, he proffers that an investor may be better served simply by investing in high-dividend paying stocks. While Professor Siegel is able to win column ink in *The Wall Street Journal* due to his position at a prestigious school, it should have been disclosed that he and his co-author serve as board members and research heads at Wisdom Tree. Wisdom Tree is a firm that sells funds consisting of high-dividend paying stocks. Instead, *USA Today* and other publications increased the exposure to Professor Siegel's comments by printing articles that picked up on his "Bond Bubble" forecast.

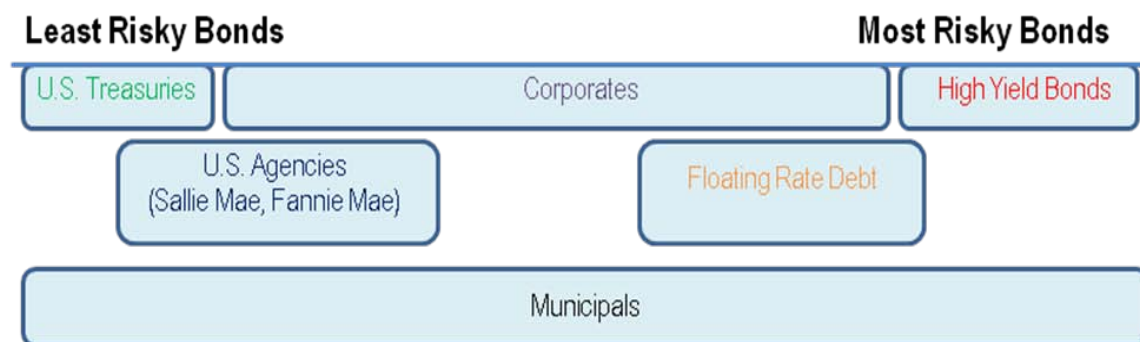
Rather than taking *The Wall Street Journal* to task for failing to disclose the conflict of interest, we will explain how Treasury Bonds cannot ever be the center of an investment bubble. A typical investment bubble is formed when prices escalate to great heights and the investor is at risk of losing much or all of their investment if the direction of the market turns against them. In the 17th century, tulips in Holland represented one of the first documented investment bubbles; the technology stock crash earlier this century is a more recent example. Unlike tulips or tech stocks without any earnings, U.S. Treasury security investing relies on confidence in the ability of the U.S. government to repay the notes. Only if the U.S. government defaults on its direct obligations would an investor risk losing their principal, assuming they hold their bonds until maturity. (The maturity date is the date on which the principal is repaid to the bond holder.) Therefore, while new investors in Treasury securities may be locking in very low returns, they do not face the risks associated with investing in bubbles. In the tulip and tech stock crashes, there was no safe way to exit the investments when no one wanted to own them.

U.S. Treasury bills, bonds, and notes are known as "risk-free" assets because the U.S. Government has never defaulted on them. In fact, they are used as the measuring stick for the relative investment risk of all other investments. In simplest terms, you would never want to own an investment with a lower expected return than a U.S. Treasury security with the same investment time frame because you would be taking greater risk for a lower expected return.

What are the risks of owning bonds?

The next issue to address is why you would want to own U.S. Treasury securities if their expected returns are so low. The answer is safety. Any time there is uncertainty in the investment markets or global tensions are rising, demand for the safest investments increases. During the bleakest days of the recent recession, and more recently in April when it looked like Greece was about to join Iceland in declaring sovereign bankruptcy, there was a tremendous demand for Treasury securities which increased prices and decreased yields on the bonds. (The yield is the amount of income the bond pays.) If you are buying Treasuries at the same time that demand is peaking, you will be accepting a very low return for holding your investment until maturity. If you need to sell your bond before maturity, and market interest rates have risen from the date of your purchase, you will lose a portion of your principal.

Holding other variables constant, bonds with the highest risk of default will have the highest yields. Treasury securities are at the other end of the spectrum. The difficulty evaluating the credit worthiness of different bond issues has been headline fodder in recent years. The major rating agencies were criticized for giving some bonds the highest ratings only to have those same bonds going into default just months later. Conflicts of interest were seen as a major problem with the ratings process; but even without the conflicts, it can be difficult to predict the repayment ability of an issuer with any degree of certainty. The following chart illustrates the relative riskiness of different types of bonds commonly held by investors:



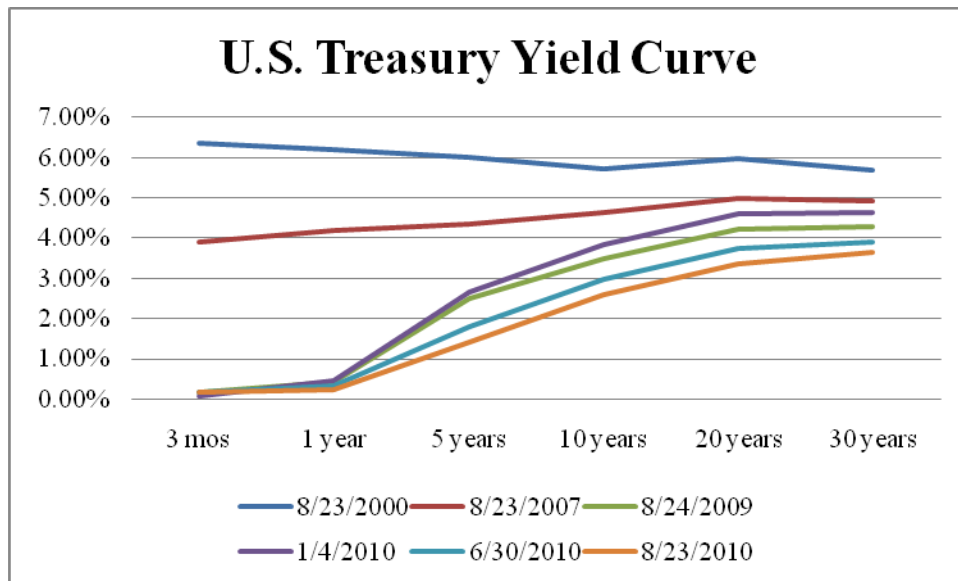
As can be seen in the chart, the range of municipal bond credit quality runs the gamut. Some municipal bonds are backed by Treasury securities (known as pre-refunded) and have virtually no credit risk. Other municipal bonds are backed by revenue streams that can come under significant pressure. Therefore, when investing in bonds of any type, and especially municipal bonds, it is essential to invest with a bond manager who continually performs due diligence on all bonds held in the portfolio and others that are under consideration for purchase.

Don't bonds generate attractive rates of income?

In addition to evaluating the credit quality of a bond, it is also important to consider the time to maturity of the bonds being purchased. Typically, the shorter the time to maturity, the lower the yield. Conversely, the longer the time to maturity, the higher the yield. In periods of deflation, when goods and services are expected to cost less in the future than they do today, the yield curve as it is known can become inverted with shorter maturity bonds offering higher yields than longer term bonds.

One topic that has been receiving attention recently has been the low levels of yield across the yield curve. The government sets the rates of return on the shortest end of the curve through different policy measures, and the market sets the rates for the intermediate and longer term periods. While the government can actively buy back certain longer-term securities to influence the yields along the curve, the market ultimately determines the rates.

As the chart below illustrates, yields have been falling for the last decade, especially the yields at the shortest end of the yield curve. The chart also shows that the curve has steepened. That is, the yield on the short end of the curve is now much less than it is on the longer end of the curve. At the start of the decade, the yield curve was flat and slightly declining. At that time, the stock market was performing very well and investors had to be incented with high yields to pull even short-term money out of the stock market to buy bonds



The good news for investors who have owned bonds over the last decade is that the falling rate environment led to capital appreciation in addition to the yield generated from bond investing. For investors who sold bonds while rates were declining, they locked in profits. The challenge for investors today is that rates do not have much room to fall and are in fact at near historic lows across the yield curve. As rates rise, investors will need to hold bonds until maturity to avoid capital losses or work with skilled bond managers who may not hold the bonds to maturity but will attempt to add value through credit (risk) analysis and yield curve positioning.

Just like it is impossible to accurately time investing in the stock market so as to be in the market on the good days and out of the market on bad days, attempting to forecast future interest rates and future shapes of the yield curve is perilous. Many top bond managers expect the slow economic recovery to keep the longer-end (10-30 years) of the yield curve relatively stable, while they expect the shorter-end (less than 3 years) to rise modestly when the interest rate increases come. Will they be right? Only time will tell. In recent years, the Federal Reserve has been giving the market more time to react to their planned future intentions for setting short term interest rates. By providing this guidance, the bond market can react in a more orderly fashion, allowing bond portfolios to be adjusted without tremendous shocks to the principal value of the portfolios. On August 10th, the Federal Reserve said “inflation is likely to be subdued for some time.” This recent message suggests that it will be many months before short-term interest rates rise as the Federal Reserve will wait to raise rates until they believe inflation is a threat.

How should you invest in bonds in today's market?

The risk today for investors buying bonds is that they may be locking in yields that are insufficient to meet their total return needs with little hope for falling rates to provide capital gain opportunities. Some people are addressing this risk by holding cash today with the expectation of buying bonds at a later date, after the rates have risen. This strategy sacrifices the opportunity to capture the currently available yields even if they are at historically low levels. The fact is that yields may be low for several more years. Also, there are no guarantees that when short term rates rise, investors will see any movement in longer-term rates. Market timing is a dangerous strategy. Instead, investors should seek yield from different types of bonds and spread their risks over a greater variety of issuers. This strategy provides for greater current income and the added diversification reduces the default risk of any single issuer and the performance risks of any one segment of the bond market.

Municipal bonds are especially attractive in advance of the rise in personal income taxes that takes effect on January 1, 2011. As illustrated above, municipal bonds exist in all different credit qualities and maturities. Having exposure to them provides federally tax-free income and in some instances income that is also free from state income taxes. On an after-tax basis, municipal bonds provide better returns for most clients than taxable bonds of similar credit quality. (Taxable bonds include Treasury bonds, agency bonds, corporate bonds, floating rate debt and high-yield bonds). The increased demand for municipal bonds that has always followed increases in income tax rates should provide some downside protection for holders of municipal bonds. The demand for municipal bonds is expected to be strong for many years as the demographic trends show increasing numbers of retirees who will need income to support their lifestyles.

The bond investing experts are shying away from Treasuries, including Treasury Inflation Protected Securities (TIPS). Instead, since they expect the economy to continue its slow recovery, they are buying corporate bonds and other riskier bonds and increasing the maturities of the bonds in their portfolios. Dan Fuss and Kathleen Gaffney at Loomis Sayles are not concerned about near term inflation. They expect interest rates to "remain low for longer than expected." Bill Gross of PIMCO cites the global demographic trends in his expectations for a slow growth period for the next five to ten years. PIMCO has been buying bonds with longer maturities in an effort to generate more income during a period when they feel comfortable that rates are not likely to rise. In summary, the experts do not think the economy will get much worse, but they caution that the recovery will take several more years before growth returns to historical rates.

A well diversified bond portfolio with exposure to a variety of different issuers and a variety of different maturities is the best way to capture some yield while minimizing the risks. During the final four months of 2010, we will seek to add more bond diversification and greater municipal bond exposure in client portfolios. Unfortunately, the slower growth economic environment which we are in requires us to accept lower expected returns for our portfolios. While we can take some comfort that the prospects for near-term inflation are low, Oak Wealth Advisors will not forget the negative impact that inflation can have on a portfolio. The importance of tax-efficiency in the portfolio is heightened by the rising income tax rates that are coming over the next three years. Oak Wealth Advisors will continue to keep its focus on helping clients retain as much return as possible from their investments after accounting for fees and income taxes.

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DEEP ROOTED THOUGHTS SEPTEMBER 2010

Volatility -- is it here to stay?

In 2010, most stock market experts predicted a relatively modest year following a calamitous 2008 and a dramatic recovery in 2009. While the S&P 500 stock index is up around 4% year-to-date as we near the end of September, the ride has been anything but smooth in producing these relatively moderate return results. In the paragraphs that follow, I will illustrate the impact of volatility on a portfolio and offer our rationale for why Oak Wealth Advisors believes we will have volatile markets for the foreseeable future.

When 0% is not 0%.

Marketers of investment products that have high volatility (i.e. returns that swing much higher or lower than the market averages) often ignore the impact of their product's volatility on the wealth of the investor. They will advertise that over a 10-year period their *average return* is one or two percent better than the market. At face value, that is a compelling argument to invest in their product. However, you have to consider the impact of the volatility of the returns.

Impact on a \$100,000 Portfolio

| | Year 1 Return | Year 2 Return | Average Return | Compound Return | Value at End of Year 2 |
|---------------------|--------------------------|--------------------------|---------------------------|----------------------------|-----------------------------------|
| Portfolio #1 | 50% | -50% | 0% | -13.4% | \$75,000 |
| Portfolio #2 | 10% | -10% | 0% | -0.5% | \$99,000 |

As can be seen in the above illustration, average returns do not tell the whole story. In fact, if the return pattern experienced by Portfolio #1 were to persist for a decade, despite having an average return of 0%, the ending value would be less than 1/4th of initial \$100,000 value. Volatility, if left unchecked, can do significant damage to a portfolio.

Diversification matters!

After the recession of 2007-2009 (it officially ended in June 2009) there was much press declaring the death of diversification because seemingly all equity investments fell dramatically. While most stocks did tumble, proper diversification means holding investments other than stocks including investments in a variety of bonds and some alternative asset classes like real estate and commodities. In the last recession, for diversification to have benefited an investor, the bond allocation had to have a heavy dose of U.S. Treasury bonds.

This year, traditional diversification has worked wonderfully. Municipal bonds, corporate bonds, and even TIPS which got off to a sluggish start, have produced very attractive returns. Real estate, in the form of REITS, and gold have been the best performing asset classes. Stocks, while advancing moderately through the first three quarters of the year, have done so in dizzying fashion.

2010 volatility has exceeded all expectations.

In the midst of a recession or during the rebound off the bottom of a recession, volatility is to be expected. In the year following the recovery from the bottom of the recession, less volatility should be anticipated assuming no major crises arise in the political or economic arenas. In 2010, the biggest market concern has been the weakness of some European economies. While not ignoring the sovereign risks that arose this year, in general, 2010 has been a relatively uneventful year in terms of crises impacting the investment markets.

Therefore, we should have experienced very little volatility in 2010, right? Actually, we had the worst stock market performance for a month of May in seventy years. The worst month of August returns in a decade has been followed by the best month of September returns in seventy years. These record-setting months have been more volatile than the May, August, and Septembers in the middle of prior recessions or major crises!

Our government claims to have decreased the uncertainty and improved the oversight in the investment markets with its recent financial legislation. The near-term results do not reflect their claims.

With technology advances growing exponentially, the ability for institutional traders to exploit minor opportunities continues to increase. The technology improvements also make information available instantly. Instead of gradual data dissemination and patience in analyzing and reacting to it, news is now acted upon instantaneously. The immediacy of action contributes to the volatility and there are no signs that the speed of technology is going to slow in the future.

How can individual investors minimize the impact of volatility?

Three simple rules can help individual investors minimize the negative impact of volatility. First, avoid being a stock picker or an owner of large positions in single stocks. This is not your father's stock market and owning GE, IBM, and Exxon is no longer a sure path to financial security. Second, do not have more exposure to stocks in your portfolio than is necessary to meet your goals and achieve a proper level of diversification. Third, expand the variety of low-cost, tax-efficient investments in your portfolio. Greater diversification is perhaps the only "free lunch" remaining in the investment world. Volatility is best reduced by greater diversification and less volatility leads to greater wealth creation.

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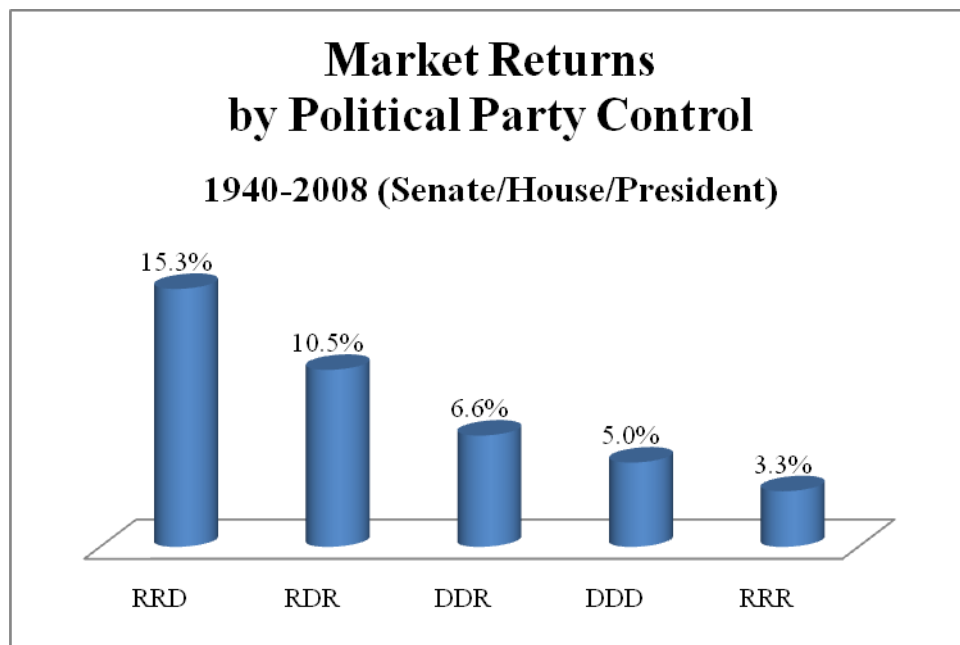
DEEP ROOTED THOUGHTS OCTOBER 2010

Vote with your wallet?

The investment markets have already been reacting as if they know the outcomes of the mid-term elections. We have experienced abnormally robust returns in September and October. These returns are due in some measure to the expectation that the Republicans will win enough seats in Congress to slow or derail the programs the Democrats have been advancing. While some believe that the investment markets favor Republican control of government because the Republican platform is pro-business, the fact is that the best market returns have come during periods of political gridlock.

Gridlock Is Our Friend

For those who experience the frustrations of commuting on our nation's highways, gridlock can be a daily grind. For investors who want to grow their wealth, political gridlock can be a very good thing. The chart below shows the performance of the S&P 500 index during periods of one party control and during periods of gridlock.

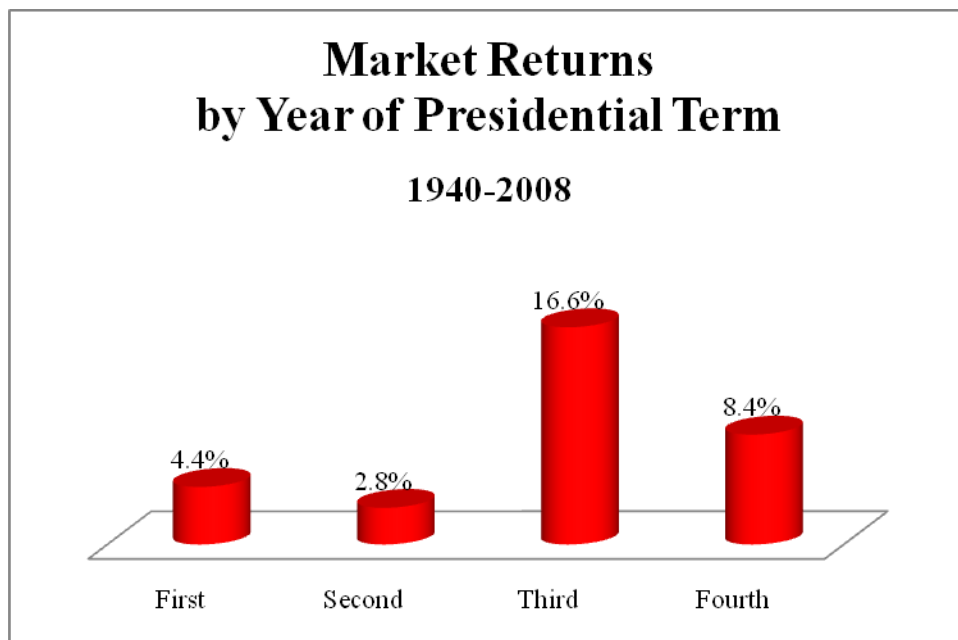


Data Source: Fact Set and JP Morgan Asset Management

As can be seen in the illustration on the preceding page, the best market performance comes with Republican control of Congress and a Democratic President. The best investment performance with a Republican President comes with a divided Congress. Interestingly, when one party has full control, the stock market performance is the weakest. This is further evidence that the stock market dislikes the uncertainty and change associated with one party controlling both branches of government.

Hooray, President Obama's Third Year Is Near!

The fact that President Obama is approaching the third year of his reign portends good news for the investment markets. History suggests that the third year of a Presidential term is by far the best year for stock market performance. The same theory about the markets disliking change can be applied here. By the third year of a Presidential term, the legislative changes that the President wants to implement are widely known as are the likelihoods for their successful passage. Gridlock generated by mid-term elections often accompanies the third year of a President's term if voters want to see less change than has been proposed.



Data Source: Fact Set and JP Morgan Asset Management

Hopefully this data provides some insight into how markets view politics. This data however is anecdotal and nobody should make investment decisions based solely on past trends. If 2009 was included in this study, the returns for an all-Democratic Congress and Presidency would be better, as would the returns during the first year of a Presidential term.

Be sure to exercise your right to vote in November!

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DEEP ROOTED THOUGHTS

NOVEMBER 2010

Be thankful for the important things.

As we approach Thanksgiving, I wanted to share with you some research I have read over the course of the year that centers on the relation between money and happiness. The results suggest that we may be overlooking the things for which we should be truly thankful. Hopefully you will consider how these findings apply to your life.

Money Can Buy Happiness

Madison Avenue tells us regularly that if we purchase the right items, we will be happier, smarter, prettier, wealthier, and thinner. Recent research done collaboratively by Michael Norton at Harvard Business School and Elizabeth Dunn and Lara Aknin at the University of British Columbia confirm that money can buy happiness, but there is a catch. You have to give it away.

The study done by Norton, Dunn, and Aknin started by asking people how much happier they would be if they earned different levels of income. In general, people significantly overestimated how much happier they would be at a higher income level. In fact, above the U.S. median income level of around \$60,000, the researchers found very little additional happiness at higher levels of income. This does not indicate that money does not matter, only that once you have a reasonable amount of it, having more will not make you much happier.

I believe the more interesting results from their research can be found in how people value the utility of their money. By utility, I am referring to the benefits they can derive from spending it. In this part of their study, they gave participants between \$5 and \$20 and told them to spend it. Half were asked to spend it on themselves, and half were told to spend it on others. Those who spent their money on others, regardless of whether it was a gift for a friend or family member or a charitable donation, reported a much higher level of happiness than those who spent the money on themselves. Interestingly, there was no difference in happiness between those who spent \$5 and those who spent \$20. The conclusion is that it is not how much you spend, but how you spend it that will lead to greater happiness. Also, we tend to overestimate the joy we will feel from buying something for ourselves and underestimate the satisfaction that comes from doing something for someone else.

Use The Proper Scorecard

It is normal to assume that the person with the bigger house, nicer car, and better vacation is happier than you are. It is relatively easy to add up the value of their possessions to determine if they have more stuff than you do. However, in a recent Merrill Lynch survey, more than half

of the retirees who responded said that if they had to live their lives over again, they would have focused more on life goals and less on financial goals.

One way to determine if you are spending your time and money in ways that truly reflect your values is to answer a few questions and compare the answers to how you are living.

Question #1: Imagine you won a \$100 million lottery. What would you do with the money? What would you buy? Where would you go?

Question #2: Imagine you were just diagnosed with a rare disease that will take your life in exactly ten years. How will you spend the money you have? Where will you go? Who will you spend time with?

Question #3: Imagine you are told that you will have only 24 hours to live. What did you not accomplish in your life? What would you do differently if had the chance?

While we all have different backgrounds, there are similarities in how most people answer these questions. Most of us will list a handful of big-ticket items we would buy if we had the unlimited resources in Question #1. A couple of big ticket items, usually including some world travel, are common among the responses to Question #2. In answering Question #3, most people wish that they had been more creative and altruistic with their time and money. Perhaps when faced with your own mortality you will wish that you had done more for your community, the planet, or some organization that has meaning to you. Maybe you will wish you had developed stronger personal relationships or fixed broken ones. Interestingly, most responses to Question #3 do not require much money.

Be Thankful For The Meaningful Relationships In Your Life

In a recent issue of Fast Company magazine, Alex Bogusky, the creative genius behind the rapid ascension of the Crispin Porter + Bogusky advertising agency in the late 1990s and early 2000s, explained his sudden departure from the top of the advertising world to pursue something more meaningful to him. Despite being named the Creative Director of the Decade by Adweek magazine in 2010, Bogusky stated, “I guess I just don’t aspire to corporate legacy. I am convinced that the greatness that matters more is the greatness people achieve through helping each other, through collaborating, more than the greatness that’s achieved by grabbing all you can or getting all you can or building all you can. The ‘you’ needs to go away for there to be the real greatness to things.” Cynically you could argue that after making millions, maybe he just got tired or did not need any more money. I would like to think he recognized that there was something more he wanted to accomplish that could not be measured on a financial statement.

Bogusky’s career change and the research pieces help me to focus on what I value most and appreciate about my career. I treasure the trust you have placed in me and the opportunities you present for us to solve problems together. I am truly thankful for you and the relationships I have with all of my clients.

I hope that during this season of Thanksgiving that you can find the time to tell all the important relationships in your life how much you appreciate them. While we all strive for financial independence, it is our social interdependence that makes us who we are.

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