



**Inside this issue:**

Tax Friendly Retirement	2
MoneyLink	2
Climbing the Wall of Worry	3



**Special points of interest:**

- Markets Closed - April 22 (Good Friday), May 30 (Memorial Day)
- Time is running out! You have until April 15th to make your 2010 IRA contribution!
- As you get older you may wish to change your asset allocation. Call us to schedule a review.

## Climbing the Wall of Worry

It seems like only yesterday when I wrote the January newsletter, but here we are at the end of Q1 2011 already. Like most of the East Coast, we've had a brutal winter in Vermont and spring so far is cold and wet. This has given us many excuses to stay indoors and at work which has proven to be both interesting and rewarding.

The first quarter narrative pretty much continues from the fourth quarter of last year with an upward trend of +5.4% for the S&P 500 in Q1 and a trailing year return of +13.4% (ex dividends) for the broad equity market. Just like Q4 2010, we had a mid-quarter break this time precipitated by the terrible disaster in Japan. While the pullback was significant at around minus 90 S&P points it was also fairly brief and proved to be merely a hiccup along the road to the aforementioned positive quarter. Given the run up of the last two years (we celebrated the second birthday of this bull market on March 9th this quarter) I frankly expected the news of Japan to result in a more significant correction than we experienced— perhaps in the 10+ percent range rather than the 6-7% correction that we got. While worries abound, the market chugged ahead none the less.

Which (how conveniently) brings us to the title of this quarter's piece. "Climbing the wall of worry" is



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an old Wall Street adage that prescribes that durable bull markets climb higher despite bad news or worries of the economic, geo political, or "newsy" variety. The notion is, I believe, that markets that forge ahead despite bad news are inherently stronger and more fundamentally based than those that stumble on bad news. It was impossible for me as I reviewed the quarter's strong performance to not recall the "wall of worry" adage as I remembered the recent economic and news events.

The issues of concern that come most readily to mind include:

- ◆ The terrible devastation caused by the Japanese earthquake and *Continued on page 3*

## First Quarter 2011 Market Wrap

<u>Market Indexes</u>	<u>% Change from 12/31/10</u>
S&P 500	+5.4%
DJIA	+6.4%
NASDAQ Comp	+4.8%
MSCI EAFE	+2.7%
Russell 2000	+7.6%

<u>Mutual Fund Yardsticks</u>	<u>% Change YTD</u>
Equity Income	+5.8%
Large Cap Growth	+5.2%
Balanced	+3.8%
Gen US Taxable	+1.1%
Intermediate Bond	+0.9%



## Tax Friendly Retirement

In more and more retirement planning meetings we are having the discussion with clients about moving to tax friendly states in retirement. A recent Fidelity Research Institute Study noted that two-fifths of retirees moved after they retired and my guess is that this number will *increase* as baby boomers join the ranks.

Which states are the most tax friendly? It turns out this is not a simple question. States raise revenue through a variety of taxes: sales, income, property, and estate taxes just to name a few. So to really answer the question you need to consider **all of these** and their impact on your *particular* situation.

**Sales Tax:** All states except Alaska, Delaware, Montana, New Hampshire, and Oregon collect sales taxes. This tax is probably not a major factor for the average retiree, but there are big differences in states. The highest sales tax rates are Cali-

ifornia (8.25%), Indiana (7%), Mississippi (7%), New Jersey (7%), Rhode Island (7%), Tennessee (7%), Minnesota (6.875%) and Nevada (6.85%).

**Income Tax:** 41 of the 50 states impose income tax. New Hampshire and Tennessee only tax dividends and interest. There are 7 states with **no income tax:** Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming. Digging a bit deeper, however, the treatment of income varies substantially state by state. For example, many states (27) fully exclude Social Security benefits from state income taxes. Vermont is one of only 6 states that tax Social Security income to the extent that it is taxed by the federal government. If you are lucky enough to receive a pension, you will want to consider the 10 states that exempt federal, state and local government pensions from state income tax—Alabama, Hawaii, Illinois, Kansas, Louisiana, Massachusetts,

Michigan, Mississippi, New York and Pennsylvania.

**Property Tax:** Property taxes can be one of the cruelest taxes since it is levied on the value of your home and has no direct relation to your income or ability to pay. However all 50 states offer some property tax relief programs based on age and/or income, with Florida, Arizona and California being particularly favorable to retirees. In general, many *southern states* have low property taxes, whereas the *Northeast and Midwest* taxes are among the highest. Alabama has the lowest property taxes (the median was \$328 in 2006) vs. New Jersey with the highest (\$5773).

**Estate Tax:** 15 states, including Vermont, Massachusetts, and New York impose an estate tax in addition to the federal tax on estates and the exclusion amount is often significantly lower than the current \$5,000,000 federal threshold.



So if reducing your overall tax burden is your goal, which states should you consider? **The top 10 most tax friendly states are:** Alaska, Nevada, Wyoming, Florida, New Hampshire, South Dakota, Tennessee, Texas, Louisiana and Arizona. Not surprisingly **the least tax friendly states include** New Jersey, New York, Connecticut, Maryland, Hawaii, California, Ohio, Vermont, Wisconsin and Rhode Island. Of course, taxes should only be part of the factors you consider. When you are looking at affordable states you should also factor in the prices of homes, heating costs, and other living expenses.



## MoneyLink

One really nice feature that can be added to your Schwab Brokerage account is *MoneyLink*. MoneyLink is the electronic funds transfer service that allows you to move money between your Schwab account and your bank account. It's a great tool for making periodic or recurring transfers and it can also be used on an "as needed" basis. We have clients use this to make monthly deposits to their investment accounts, and conversely some that use this to establish a periodic stream of income in retirement. **The process is safe, secure and very easy to use.** One client recently commented that the entire process took about 30 seconds! The actual transfer of funds is processed within one business day of the request—much more timely than the U.S. Mail. And unlike wire transfers there is no fee to process the funds transfer.

To establish MoneyLink for the first time, we need to fill out a simple Schwab form with your signature and a voided check of the bank account to which you are linking. If you would like the ability to make "on demand" transfers, you will need to have a Schwab Alliance login and password to access your account. That's it.

Please call if you would like any more information or if you would like us to set this up for you.



## Climbing the Wall of Worry (cont from page 1)

### MARKET TALK

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tsunami, the still uncertain resolution of their nuclear reactor situation, and the certain economic toll all this will take on the third largest economy of the world.

- ◆ The European sovereign debt debacle that continues to bubble up from time to time with one bailout done and perhaps two or three to go.
- ◆ Dismal real estate numbers in much of the U.S. that show no sign of near term improvement.
- ◆ Oil prices reaching a 33 month high this morning above **\$108 per barrel** and gasoline rapidly approaching \$4/gallon.
- ◆ Corn reaching an all time high, *up 121%* over the past year with many other food and manufacturing commodities on a similar upward trajectory.

Taken out of context these bullet points could be downright discouraging and yet the equity markets continue to grind upward led by the positive trends in corporate earnings. This is the classic “wall of worry” market—grindingly moving forward, confounding the fearful, aggravatingly positive in the face of adversity. I have no idea how this will work out in the end (my crystal ball works as badly as everyone else’s) but to me, this market has the feel of 2003-04 or even 1982. Remember, so long as there are non-believers, we’re okay.

Beware the day when “everyone” knows the bull market is obvious.

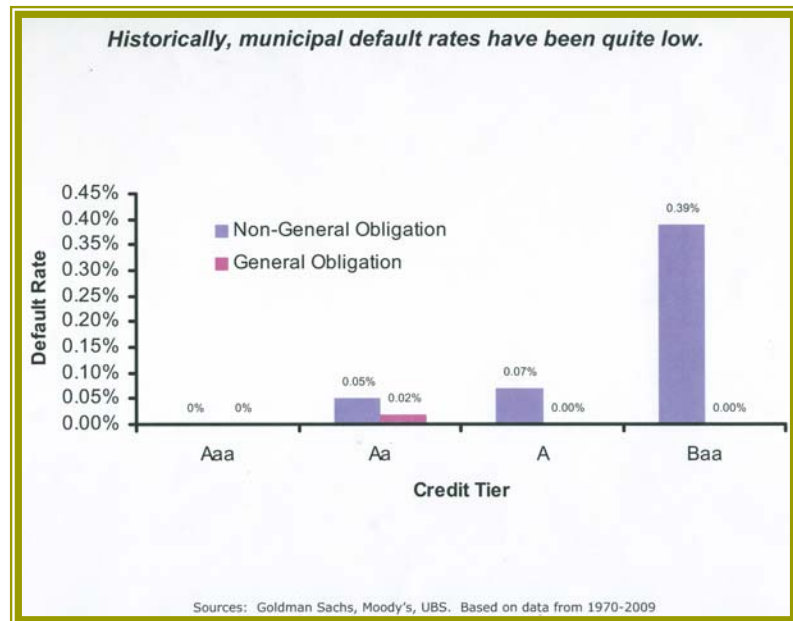
### So how are we positioned now?

As I have been for quite awhile now, I remain cautiously optimistic on the equity markets—less so on the fixed income markets. In general (particular portfolios may vary):

- I have full to slightly underweighted bond allocations in place most often in short, 1 to 5 year ladders to provide adequate yield while reducing interest rate risk.
- I view the municipal bond market more as an opportunity than a risk overall. Selectivity and quality are key though.
- I am working towards a 5-10% cash position depending on the portfolio. This allows me to be slightly defensive as well as provide liquidity for opportunistic purchases.
- Inflation is a concern and I have been moving the portfolios to reflect it and profit from it where possible.
- I have been adjusting our foreign holdings and prefer emerging markets to established markets. This is currently a work in progress as appropriate for the portfolio.



Historical view of municipal bond risk



Please remember to contact Sokolowski Investment Advisors, LLC if there are any changes in your financial situation or investment objectives or if you wish to impose, add, or modify any reasonable restrictions to our investment management services. A copy of our current written disclosure statement discussing our advisory services and fees continues to remain available for your review upon request.