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Market Commentary

***"Full of sound and fury;
signifying nothing."
Macbeth***

I've spent a good part of my morning pulling together numbers and information from 2011, ruminating as it were on the year just past. It's an annual ritual during the first work week of the New Year; one that I follow as an occupational hazard but also by temperament if truth be told. I enjoy the pause that the changing of the year gives us—in between the "out with the old" and the "in with the new" there's a moment to reflect about what I might have done that proved correct and helpful and what, perhaps despite my best efforts or intentions, didn't work out so well. More importantly, it is a moment to learn, to attempt to gain some wisdom to take forward in the New Year. After all, having spent another year, it seems only fair to gain a bit of wisdom in trade.

But I digress. As I looked at the numbers and considered the past year's events, that quote from Shakespeare's Macbeth popped into my head. (Macbeth is my favorite Shakespearean play. Who can resist the foggy Scottish moors, witches and ghosts?) I decided it was an apt description for 2011.

For as we began 2011 with some hope that the world economy might continue to heal from the 2007 financial/real estate meltdown, optimism faded into the summer months as fears of a secondary recession surfaced. Indeed, the stock market spent the

first half of the year climbing to net gains of over 8% only to reflect those fears by August in a nasty correction to net -13%.



As the year progressed the fiscal disaster that is Europe just couldn't be ignored and our collective blissful ignorance morphed into overblown fear for the "European contagion". In reflecting on the many discussions I had over this period I believe that while the negative nature of the August correction was disconcerting, it was the volatility of the equity markets that pushed the fear gauge over the limit for some investors. For example, through the August to November 2011 period the Dow averaged a daily intraday swing of 270 points while the S&P 500 was either up **or** down 2% 35 separate times in 2011 according to the Wall Street Journal. The markets were providing the fury; the sound was courtesy of a hyper ventilating popular press that knew a good way to sell papers when they saw it.

A funny thing happened on the way to a Euro disaster though; the Euros continued to find a way to muddle through during the fall months. And those pesky U.S. corporations just wouldn't follow the script either, generally racking up solid profits as

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Special points of interest:

- Markets closed—Martin Luther King Day (1/16), Presidents' Day (2/20).

Tax time! Enclosed are 2011 Realized Gain/Loss Reports for your taxable accounts to help you prepare your returns.

- You have until April 15 to fund your IRA for 2011.

Fourth Quarter 2011 Market Wrap

<u>Market Indexes</u>	<u>% Change in Q4</u>
S&P 500	+11.2%
DJIA	+12%
NASDAQ Comp	+7.9%
MSCI EAFE	+2.9%
Russell 2000	+15%

<u>Mutual Fund Yardsticks</u>	<u>% Change in Q4</u>
Large Cap Growth	+9.29%
Balanced	+6.05%
Gen US Taxable	+1.98%
Intermediate Bond	+1.32%
International Stock	+4.57%

2011 drew to a close. It was difficult to hear but under the gloomy noise, there was a steady under tone of positive economic surprises—strength in retail, a strengthening purchasing managers index, slightly better employment numbers, low inflation, and a resilient GDP to name a few. From the depths of the October lows the markets did begin to listen and responded with a year-end rally that brought us back to, well, ...zero, more or less.

After the Euro, the Arab spring, the Japanese tsunami, Occupy Wall Street, and all the noise, the S&P closed 2011 down a slight -0.003% , barely enough to notice. The NASDAQ closed down -1.8% and the Dow 30 gained $+5.5\%$ for the year. Gold was up 10% after a wild ride, but the average hedge fund lost -5% for the year. There was fury, there was sound, but did the near zero stock market return signify nothing?

I think the answer is both yes and no depending on the time frame. Certainly for all the tumult of 2011 ending the year at breakeven seems to signify nothing. As one market wonk put it—*it didn't seem fair to go through all that for nothing*. I suppose we could leave it at that, but I think that in the markets the process is important as well as the result. The result may have been zero for the S&P but the intra year moves were symptomatic of things we should pay attention to. There were shorter term items that created what market watchers call “headline risk” such as the Japanese earthquake and the Arab spring. There were also many big idea issues that the markets grappled with—the relative economic power of the U.S. versus Europe versus China and the implosion of

the European economic and social system being perhaps the ones that demand our long-term attention. It seems that the significance of 2011 was not in the end result, but rather in the struggle. It all bears watching because in the struggle we witnessed the market reaction to a wide variety of economic and political issues—some of which were temporal and some of which we will struggle with again in 2012 and beyond.

Amazing Karnak

Every few years for some masochistic motive I can't understand, I venture some thoughts about the future. There is simply so much going on that's so critical to us right now that I am compelled to stick my neck out again. Here are a few thoughts:

•**Europe:** I remain cautiously optimistic that the Euro politicians will find a way to muddle through their debt crises—slowly, haltingly, hair pulling frustratingly. If they fail we will have shorter term market problems here and they will descend into depression. If they muddle through (which is success in Euroland) they will avert disaster and begin a long recession. Europe is a real wild card and presents us with a potential “damned if we do, damned if we don't” problem. On any given day we could either be positioned too defensively or not defensively enough.

•**China:** China is a top down control economy and has chosen an economic policy of slowing its growth. In 2011, the economy responded and slowed from $+9\%$ GDP to $+6-7\%$ GDP growth. Their stock market also dropped -22% last year. I believe China will execute a “soft landing” in 2012 rather than a crash. China is an economic powerhouse, but they will not take over the world economy any time in the near future. Their wild

card is also Europe— they sell more goods there than they do to the U.S.

•**The FED:** I don't have to go out on a limb here—the FED will keep interest rates low for the foreseeable future—just as they have said that they would. The bond bubble will therefore remain inflated for another year or two and prolong the imbalances it creates.

•**The 2012 US Election:** Even I fear to tread here and it's too close to call. For our investment purposes what we need to know is that the markets will not wait until November—they will react just as they did in 2008 when the direction of the outcome becomes clear— sometime around August, give or take.

•**US Markets:** I believe that the US stock markets will be the best house on a bad block this year. Our slow GDP growth will look better than no growth Europe. Our currency will strengthen against the Euro and our Treasury market will continue to be the world's safe haven in times of stress. I believe strong American corporations that are more US sales centric or at least non-European sales based will provide good growth. If they pay a dividend so much the better.

In a sense, Europe is buying us a little time to get our fiscal house in order. We share the same debt excesses with them. It is solely because of the Euro's 17 nation structure that their system imploded before America's did. Their weakness has become our strength, but only for the time being. Debt is only a bill deferred. In Europe, the bill is due today. Our bill is deferred only so long as Europe is working out its payment schedule.

Farewell 2011!

MARKET TALK

Sokolowski Investment Advisors
95 College St.
Burlington, VT 05401

Phone: 802-489-5342
Fax: 802-489-5344
Email: rws@siawealthadvisors.com
Website www.siawealthadvisors.com



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This holiday season we chose to give back to the community by donating to local non-profit organizations. Among them were the Lund Family Center, COTS, Counseling Service of Addison County, Child Care Resource, and the Governor's Institute of Vermont.



Transitioning to Retirement

For most people, the check list of adult life looks something like this:

- ◆ Attend College ✓
- ◆ Find a Job ✓
- ◆ Get Married ✓
- ◆ Buy House ✓
- ◆ Have Children ✓
- ◆ Pay for College ✓
- ◆ Save for Retirement ✓
- ◆ Retire ????????????

The last step—retirement— is somehow more scary than the rest. It is, after all, the end of the list. There is no time to make up for mistakes. Intuitively it seems like it must be more difficult than all the rest because it is so final. There are certainly many questions that come up for which you may not have answers. Among the ones that we hear most often are:

When should we start Social Security? Age 62, 66, or 70? What are the pros and cons?

What should I do with my 401k?

How can I set up an income stream from my investments?

Can I afford the medical premiums and out of pocket medical expense in retirement?

What if I get sick—do I need long-term care insurance?



How much can I safely take out of my accounts without outliving my money?

Every situation is different, and having worked with many clients over the years we can offer guidance, perspective and answers. Approaching retirement shouldn't be frightening, but it should be something that you plan for and we are here to help with this transition.

The best time to start planning for retirement is **NOW**. Whether you are 30, 42, 55, or 60 there is no time like the present. With people living longer (well into their 90's) we are now planning on a 30-35 year duration for retirement.

Turning question marks into check marks is easy when you have a partner and a plan.

Service with a Smile by Mike Reynolds

More than 20 years ago, I passed my General Securities Representative Exam (the Series 7) and the Uniform Securities Agent State Law exam (the Series 63) in preparation for becoming a Registered Representative. I was working at the Merchant's Trust Company in Burlington training as backup for their discount brokerage office. I believe I was there less than a week when the manager of their discount brokerage office quit her job. I guess it was a case of being at the right place at the right time; I was offered the job. Times being what they were, I accepted the job on the spot. Starting date: immediate. Training: none. Raise: to be determined in a year (if I made it!). That was how I rose to be the manager of the Merchant's Discount Brokerage.



I knew that I wasn't going to dazzle potential clients with my knowledge or years of experience, so I focused on providing the best possible customer service while I learned the ropes. Pulling from prior job experiences helped. I used to work with my brother who was a golf pro in southern Vermont. He taught me early on to smile and be courteous to everyone. At the Merchant's Trust I taught my staff (initially one part-time employee) to greet people with a smile and a helpful disposition. Through the years, I increased my knowledge of the industry and operations, but I never forgot to treat people the way that I would want to be treated.

Unlike a great sales pitch with more immediate results, providing excellent service is long-term strategy and the results are manifested over a period of time. I remember an elderly woman who stopped in my office and asked for help transferring the title on a stock certificate to her nephew. She explained to me that she had already been to two other brokerage offices in town and that no one would help her. Although this wasn't a normal part of our business I told her I would be happy to help. She offered to pay me, but I declined. I told her to let her friends know about her experience and that would be payment enough. A short time later her nephew stopped in, thanked me, and opened a sizable account. Further, he told his friends about our service and my business was off and running.

Providing great service also means being a good listener. You can't help people and step into their shoes unless you ask questions, listen for the answers and find out what they need. Many of the things that have made me successful in business are based on life lessons and common sense. To this day I still thank my brother for teaching me to treat everyone with care and compassion.



New IRS Tax Reporting Requirements

When Congress passed the Emergency Economic Stabilization Act in 2008 they changed the way that custodians (like Schwab) report cost basis to the IRS. This will be phased in over *several years* and your 1099-B that you receive in February will mark the initial change. For the tax year 2011, Schwab will report cost basis for equities acquired on or after January 1, 2011. In 2012 the requirements will be extended to mutual funds, ETF's and Dividend Reinvestment Plan (DRIP) shares. The following year (2013) will expand the coverage to options and fixed income.

You will notice a new 1099 form layout including the cost basis, date of purchase, holding period (long-term or short-term), and wash sale information. We will continue to provide you with Realized Gain and Loss reports for all your holdings and are happy to try to answer any questions that you may have about these changes.