Comprehensive FINANCIAL PLANNING INC.

January 15th, 2013

Here is our newsletter for the 1st quarter of 2013.

The Markets
U.S. stocks had a pretty flat 4th quarter. By contrast foreign equities had a big rebound of around 8%. For all of 2012 equities had a very good year with gains of 16% in the U.S. In the second half of the year foreign markets reversed a multi-year trend of underperforming the U.S. market and posted a 19% gain for the year.

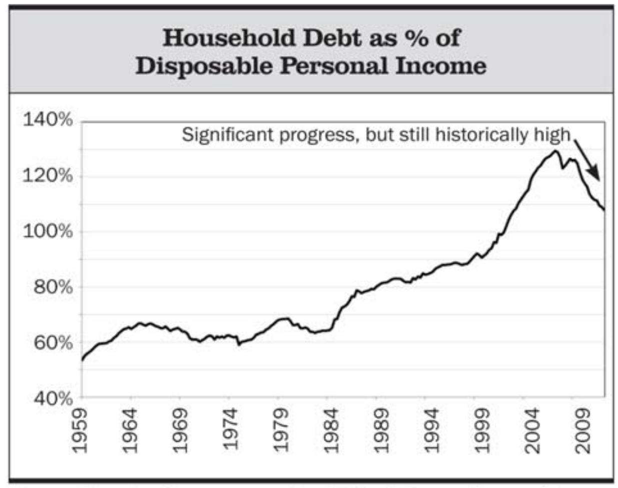
The U.S. total bond market index gained 4.1% for the year. High-yield bonds gained 15% while emerging market local currency bonds gained 15%. The only major asset class which was down for the year was commodity futures with a 1% loss.

Our Portfolios
For 2012 all our portfolios had good returns that were close to our benchmarks despite being significantly underweight equities. In general our alternative funds, emerging market local income funds, high-yield bond funds and foreign equity funds all did very well while our U.S. equity funds did poorly. Our strategy of getting close to market returns while taking less risk in the equity markets worked well.

In December we implemented significant changes to our portfolios. These changes set our overall allocations to less bonds, more alternatives and more foreign equities than our previous allocations with only a slight increase in potential volatility. Our portfolios are positioned in a moderate but not excessively cautious way that should provide adequate returns in up markets and provide good downside protection during down markets.

Our Outlook on the Economy and the Markets
Our expectation of slow economic growth that we have had since 2009 has largely been right on over the past four years. Europe actually fell into a mild recession in 2012 and the U.S. and Japanese economies grew at 2.2% and 1.7% respectively. Going forward our overriding theme of continued sub-par, slow growth and possible recession is still in place, driven by the continuing deleveraging process and recovery from the 2008 financial crisis.

For the U.S., households, businesses and financial firms have made progress in reducing and restructuring their excessive debt over the last few years (see chart). For the last five years a big portion of growth in the U. S. economy has been attributed to federal government actions, including large deficit spending. This year and for years to come this will turn around with higher taxes and reduced spending. Goldman Sacks estimates the economy will be hit with a slowdown of around 1.75% this year just due to the fiscal cliff deal struck after the New Year. So an economy growing at just over 2% could see most growth wiped out by the fiscal cliff deal with additional effects to come (debt ceiling, entitlements, etc.). So while the economy is showing improvement in some areas such as housing, the added headwind from the feds will keep growth in the intermediate term.



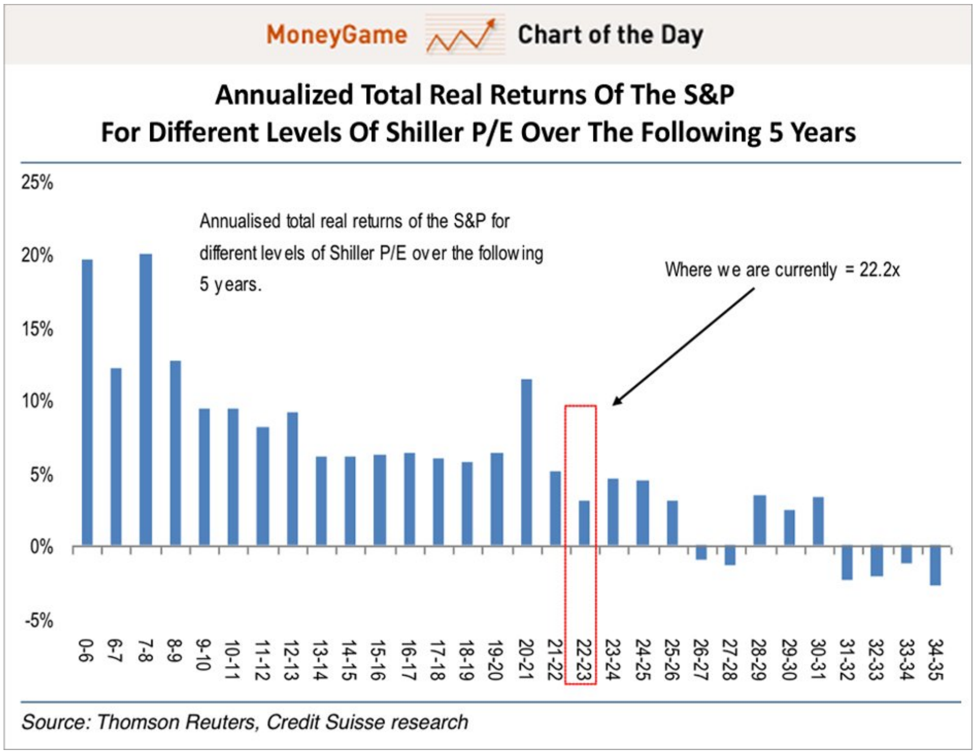
Source: Board of Governors of the Federal Reserve System/Bureau of Economic Analysis. (Data as of 9/30/12.)

The Eurozone also has made progress in dealing with their crisis by promising to do whatever it takes to support the union by outright purchases of sovereign and bank debt and providing support for the weaker southern European countries. This has at least taken the worst case scenario off the table for Europe with another financial crisis having been averted for now. Europe is also further along in doing the difficult work of right-sizing government spending vs. taxation. They fell into recession last year and expectations are low for growth going forward. The good news is markets have this priced into most assets and they are making progress in stabilizing their financial system.

Are Stocks Cheap?

The quick answer is definitely not in the U.S. I have discussed our preferred method of measuring equity valuations across the markets in past newsletters as the Shiller P/E ratio. This measure from the Yale economist Robert Shiller uses earnings averaged over 10 trailing years in an effort to smooth the effect on huge swings in earnings as the economy grows, stalls, contracts and recovers throughout the business cycle. Credit Suisse looked at past U.S. stock market returns for 5 years following different levels of the Shiller P/E ratio and their analysis is shown in the chart on the next page.

The average Shiller P/E over the last more than 100 years is just over 16 compared to the current level of about 23. The chart shows the general, but far from perfect correlation of higher P/E ratios resulting in lower stock returns going forward. Note they are talking about 5 years. This method, nor any alternative method, can tell us what the markets will do over the next year or even two. The chart also does not show the variability in the data for each P/E ratio range. However this and other evaluations I have seen strongly suggest equity returns over the next 5 years will fall around a range with a mid-point of about 4-5% per year on average in the U.S. Note P/E ratios are lower in the foreign markets which is why we increased our allocations there recently.



All in the Family
One of the more rewarding aspects of being an advisor is helping multiple generations with their financial challenges. Here are a few examples of how I have been able to help.

- A client had me review his elderly father's investments. His father was in poor health and moving into a nursing home. He wanted to understand the investments and what changes should be made to help pay for his support. His father's Will was changed many years earlier to exclude his ex-wife, long estranged from the family, and designated his son to inherit all his holdings. Turns out all his net worth was set to go to his ex-wife, set by beneficiary designations in his accounts, (which were never changed when he and the wife split) overriding the wishes established in his will. He immediately changed all the beneficiary designations on his accounts.
- After inheriting a large value of government savings bonds from her father that he had bought over a 30 year period, my client asked me to make recommendations on what she should do with them. These savings bonds are tax deferred, meaning interest accrued on the bonds are not taxed until the bonds are cashed in. After a complete review we determined that her father had chosen to go ahead and pay the tax when accrued on some of the bonds. This took some time for the client to go thru countless tax returns to determine what tax had been paid. The IRS does not offer much help here. They assume unless you can prove otherwise that tax was not paid on the bonds. Without a review she may have paid the tax twice. Doing so also enable her to set up a plan to cash in the bonds that had little tax to pay first so she could continue to defer taxation as long as possible.

- Three years after her mom passed away my client asked me to advise her on all her financial matters, including working with her mom's out-of-state estate attorney and CPA to help settle her estate. This is still a work in progress but in six months we have gained an understanding of the tax ramifications, transferred all the assets in two trusts and her mom's estate accounts and put them in one account titled in her name. I also recruited an estate attorney here in Colorado who advised her on how to set up her own assets and what estate documents she should have to ensure her estate passed per her wishes to her kids.

The above examples illustrate the benefits of working with your parents well <u>before</u> the inevitable day arrives and helping your parents and you understand what will happen when that day comes. Today is a good day to start the conversation.

Thank you for your continued interest and let me know how I can help.

Sincerely,

Stan Johnson, CFP(R)
Comprehensive Financial, Inc.
Registered Investment Advisor