

Volume XXIV, Issue I

# THE HARBOR ADVISOR

## How to Define a Winner

Recent reading has reminded me of two principles of planning and investing that have been paramount in my now almost 31 year career. One is that I have been advising clients in one of the greatest bull equity markets of all time and the other is that there is no end game in investing. How do these two principles fit together? What do they have in common?

Let's examine each. The equity markets have been on a 40 year tear, buoyed by a credit expansion policy which has positively affected market prices. The trajectory has not been smooth (as I alluded to in last quarter's letter) but the opportunities have been present. If you have known me long, you know how we managed to make good returns in both good times and bad, but we did not face flat returns for an entire decade like the 70s. We all know there are investment groups and individuals who have lost money in these excellent market years, but many more would join their ranks in a truly negative investment environment.

Which brings me to, "Does this make me a savvy investor or market maven, a winner?" We don't know, any more than we know what will happen with the markets, the world economy, the weather or what our Congress will do with the deficit (but we have some pretty good guesses there). The point is that calculating overall returns for a portfolio is a never ending game; it can span our lifetimes, so you really can't measure success. We track returns for shorter periods but we all know the fallacy of taking a too-short view of money and planning success. So where does this leave us?

My suggestion is ask yourself these questions: "Why do I invest? What do I hope to achieve by planning? Is it the highest return along with bragging rights with my friends? Is it financial comfort and peace of mind, or is it to achieve a better life style or to provide my children with a good start in life? Or maybe to make the world a better place?"

Then, how do I achieve this goal or my group of goals? Answering these questions provides a solid basis for investing, planning, gifting and spending. With some thought and personal examination we can all be winners.

In this quarter's newsletter look for 1988 trivia, our usual focus on an investment position, and a helpful 2013 checklist in the living well and living smart section.

Drop in and see us anytime, we would love to see you!



April 15, 2013

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## 1988 Trivia

In 1988 Ronald Regan was president. Interest rates were at 10.5%, a gallon of gas was 91 cents, and a postage stamp cost 24 cents. The S&P 500 was at 260 (vs. over 1500 first quarter of 2013). Harbor Financial Group was formed in Cherry Creek, Colorado.



## Q1 2013 Market Recap

The US economy continued its expansion during the first quarter with the housing market leading the way. The improving jobs sector was a contributing factor to the growth in the housing market. As a result, housing prices rose due to high demand and a tight supply of desirable homes. During the quarter, consumers faced escalating gas prices and additional payroll taxes. Yet, overall spending rose, as reflected by increased sales in the retail, building material and auto sectors. While equity markets soared to new levels, the quarter was not without volatility. In Europe, the situation in Cyprus was a reminder that the

European Union still faces many challenges in resolving its economic crisis. In Italy, inconclusive elections raised concerns that the government could become unstable and veer away from progress made during the previous prime minister's reign.

Equity indexes reported strong returns for the quarter. The S&P 500's return was +10.03%, Wilshire 5000 +10.69%, Russell 2000 +12.03%, and MSCI EAFE +4.39%. The BarCap Aggregate Bond index posted a negative return of -0.13%.

*"Just do it" – Nike ad slogan launched in summer of 1988*

### Fund Focus: Cambiar Small Cap Fund

This quarter's fund focus highlights a fund run by a Denver based investment firm. Cambiar Small Cap Fund focuses on US equities below \$3 billion in market capitalization abiding by the firm's four criteria: quality, valuation, value creation and upside. Similar to Harbor's investment philosophy, the fund seeks high quality companies that exhibit defensible characteristics and strong financials. Unique to Cambiar, any potential investment must clear a proprietary 'High Hurdle Rate' over a 12-18 month timeframe. This hurdle identifies companies that have the potential to deliver at least a 50% total return over the timeframe.

In addition to the above criteria, CAMSX maintains a concentrated portfolio with anywhere from 45-55 equities. This high conviction approach may lead to tracking error (a measure of how closely the fund's performance follows its benchmark) when investment ideas do not pan out, however the fund has a strong track record of out-performance relative to its benchmark since inception. For these reasons this fund has a place as a core active manager in our portfolios.

## Interest Rate Risk Revisited

We'd like to revisit a topic we wrote about back in Q1 2010 discussing interest rate risk and portfolio construction in light of today's market environment. Our original point was that investors need to pay attention to interest rate risk at all times, but especially following recessionary periods after central banks have artificially lowered interest rates to stimulate the economy. Our concern at present is that despite our ultra-low interest rate environment, investors continue to invest in long dated fixed income perhaps unaware of the consequences.

Taxable bond mutual funds have raked in, on average, over \$200 billion a year<sup>1</sup> in investor's money since the beginning of 2010, the largest by far of any mutual fund category. A 10-year Treasury stated a 3.7% nominal yield at the beginning of 2010 and is currently at approximately 1.9% (meaning price has increased). Inflation, as reported by the February CPI index, has risen to 2%. This implies a negative real rate of return for 10 year Treasury investors which is evident in the -.60% yield offered by a 10 year Treasury Inflation Protected Securities (TIPS). Note that a negative interest rate here indicates the investor is willing to PAY the issuer interest to preserve capital.

Another component of fixed income analysis we discussed is duration. Simply put, duration measures the sensitivity of a bond's price to interest rate movements. Suppose, in the above example you realize that negative real returns are currently present in 10 year treasuries so you go out on the yield curve and buy a mix of longer maturity bonds with a duration of about 15 and a yield of 3%. It only takes about a 20 basis point increase in interest rates to completely offset an entire year of yield. Consider that point with the fact that we are on the very low end in an interest rate cycle and you can understand our concern for today's core fixed income investor.

For many investors an allocation to core fixed income remains a familiar and attractive concept because it has delivered steady income and total return with lower than equity volatility for the past 30 years. While we disagree that there will be a spectacular burst of the bond bubble, we believe there are better risk adjusted returns found elsewhere. We have been researching alternatives for our portfolios and will be discussing these during our quarterly performance calls over the next few weeks.

<sup>1</sup>ICI.org

## Social Security: A Very Brief Lexicon

In all the banter about strategies for maximizing your social security benefits the implications can get lost in the jargon. Here is a brief glossary of terms being used and why they are important.

- Full retirement age (FRA):** This is the age at which you will receive 100% of the benefits due to you. To find your FRA follow this link. (<http://ssa.gov/pubs/ageincrease.htm>)  
**Why it's important:** If you file early (before your FRA) your benefits will be reduced. If you wait to file until later your benefits will be permanently increased .06% per month for each month you wait to file after your FRA up to age 70.
- Spousal benefits:** Either spouse can claim a benefit at their FRA of 50% of their spouse's benefit as long as their spouse has filed for their benefits.  
**Why it's important:** This is most important for a lower earning or non-working spouse but can be of use in other situations as well (see File & Suspend below).
- File and suspend:** Here is where things begin to get a bit more complicated. It is possible to file for your benefits at your FRA but then suspend, not actually receiving any benefits until your age 70 in order to receive the increased percentage for waiting.  
**Why it's important:** Why would you want to do this? Because if your spouse is also at FRA you must file for benefits before they can file for and receive their spousal benefits. Your spouse can begin receiving their monthly spousal benefits at their FRA and hold off filing for their benefits until later in order to receive the increased percentage for waiting.
- Do over:** For a 'do over' you begin taking your benefits at whatever age you decide but later, (but within a twelve month period), return all of the money and wait to reset your benefits to an increased amount.  
**Why it's important:** It gives you an out in case you file and then change your mind and decide to work a little longer or decide to wait for the increased percentage.

More information and various calculators are available on the social security web site ([www.ssa.gov](http://www.ssa.gov)) or the AARP web site ([www.aarp.org](http://www.aarp.org)).



## How to Check Your Social Security Report Online

Several years ago due to budget cuts the Social Security Administration halted the mailing of the annual benefits statements. While there is no date in sight to resume the statement mailing in 2012 the SSA did make online statements available. With a few minutes of your time you can still check up on what is due you from social security in your retirement years.

- Go to [www.ssa.gov](http://www.ssa.gov)
- Under popular services click on 'get your Social Security Statement online'
- Click on 'Create an Account'
- Read the terms of service and click the box that you agree to the terms
- Enter your personal information (this consists of name, address, social security number, etc.)
- Answer additional security questions
- Choose a User Name (8 to 20 letters and/or numbers) and Password (8 characters minimum with at least one uppercase letter, one lowercase letter, one number and one symbol) for your account
- Answer additional security questions (in case you lose or forget your User Name and Password)
- Log in to your account and click on 'Estimated Benefits'

You may also wish to check your earnings record while you are logged on for any errors.

### Living Well/Living Smart

#### Beat the Year-End Rush!

NOW is an excellent time to get a jump on your financial chores. Consider beating the year end rush and getting these items started or even finished now:

- If applicable, take your required distribution from your IRA
- Make an annual contribution to your child's 529 account
- Consider any estate planning that might be done this year and phone your attorney for an appointment
- Check your credit report at [www.annualcreditreport.com](http://www.annualcreditreport.com)
- Check the [www.missingmoney.com](http://www.missingmoney.com) web site for unclaimed property
- Discuss with your accountant whether or not you might be eligible to contribute to a Roth or traditional IRA for 2013 and, if needed, open accounts
- Pull a social security statement from [www.ssa.gov](http://www.ssa.gov) to check your benefits (see article to the left for how to's)
- Review your savings plan – consider contributing the maximum to your 401k or other retirement savings plan and adding to the amount you save from personal funds
- Review your beneficiaries and make changes if necessary – we highly recommend that you include a contingent beneficiary
- Check your company benefits for any updates, new offerings and appropriateness to your current situation

As always, give us a call if you have questions or if we can be of assistance with any of these items.

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Images: Lars Sundström, Fleur Suijten

## Harbor Happenings

### **Performance Webinars**

Our next quarterly performance webinar is scheduled for 4/18 at 12:15 p.m. Check your email inbox for registration information. As always, please let us know if you have any questions.

### **Privacy Policy and New ADV Available**

A full copy of Harbor's updated ADV (the form used by investment advisers to register with the SEC) is now available on our web site. Please notify us if you would like a hard copy and we will send one by mail.

## 2013 Closures

Our office is closed on the following New York Stock Exchange holidays in 2013:

Mon, May 23, Thur, July 4, Mon, Sept 2, Thur Nov 28, Fri Nov 29 is a half day closure, Tue, Dec 24 is a half day closure, Wed, Dec 25.

Securities offered through Schwab Institutional. Member FINRA & SIPC

## **Telephones to Twitter- A 25 Year Retrospective**

Do you remember a time when the S&P was at 260, interest rates were 10.5%, average income was \$24,450, and a gallon of gas cost 91 cents? How about the year the Persian Gulf war ended? It was 1988, a time of big hair and bigger shoulder pads, Ronald Regan was president, the Stealth bomber was unveiled and the Hubble Space Telescope was originally scheduled to launch. Harbor Financial Group was established that same year. We are celebrating our 25th year and we could not have done it without you!

So, to borrow from Nike's famous 1988 ad campaign we decided to "Just do it". We have a number of fun events planned; be on the lookout for trivia from 1988 in our newsletter, the top 25 things I have learned in the past 25 years in our blog and a party to celebrate where it all began.

Stay Tuned!

