

THE HARBOR ADVISOR

Current Returns Aren't the Whole Story

Investing is a long term and often tricky proposition. A widely held opinion is that the best asset in a portfolio is the highest producing one, if one investment returns a lot we inherently think we should own a lot of it, right?

Unfortunately not. The risk associated with any investment plays a big role in the decision of how much to own. Diversification is another factor. Since we don't know how each asset class will perform at any given time, successful portfolios have a mix of performing and non-performing assets, the total return on which tends to be higher over time.

Yet another factor is that investment opportunities come in waves or cycles and you need to be prepared to take advantage of the opportunity. If you are always fully invested you will have difficulty maneuvering quickly enough to capitalize on an opportunity that arises. Having a portion of your portfolio in cash or similar investments meets this need. It certainly may not yield much if anything but it does provide an opportunity reserve, diversification away from the riskier and higher yielding assets and you can spend the cash for things you need. That is a pretty simple and sometimes overlooked use of cash. We want cash to hold its value, be there if equity prices fall or if a good real estate opportunity comes along, and we want it there if we need to cover an expense. The fact that it does not earn much currently does not diminish its value to a portfolio. It does not stack up well on the return chart or help tell a fun story at a party, but nothing spends quite like cash.

Expert investors agree, Donald Yacktman has kept approximately 20% cash in his portfolio for years and out performs the S&P regularly. Our experience at Harbor has also been positive, holding a low yielding asset can and often does pay off in many ways.

Thanks to those who joined us for our Boulder cheese, salume, wine and beer tastings and our Rockies game in Denver. A good time was had by all, we look forward to seeing everyone at one of our fall events.



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Financial Trivia

ZOMBIES

Also called the living dead, zombies in the financial world are companies that continue to operate even though they're bankrupt.



Third Quarter 2014 Market Recap

There was no shortage of geopolitical conflicts during the third quarter. Global markets reacted to concerns surrounding Russia's activity in the Ukraine. The situation in the Middle East escalated, prompting the U.S. and allies to employ air strikes against ISIS targets in Iraq and Syria. Markets were also ruffled by Argentina's default in July, deepening the country's economic problems.

Global growth was also hampered by weak economic data from Europe and China. Europe's economy has been growing at a sluggish pace, raising concerns that some countries are at risk of falling into recession. China's economy showed further signs of slowing as well, with exports and real estate troubles being contributing factors.

Despite the strains on global markets, the U.S. economy continued to grow, although not robustly by any means. While the housing market, consumer confidence and manufacturing numbers were less strong, employment increased by approximately 224,000 per month during the quarter. The Fed announced its plan to end its quantitative easing program this fall, in light of positive employment situation, rising incomes and low levels of inflation.

Returns were mixed for the quarter. The Barclays Aggregate Bond index increased 0.18%, the S&P 500 was up 0.62%, the Russell 2000 was down 7.65% and the MSCI EAFE was down 6.39%.

"Autumn is a second spring when every leaf is a flower." Albert Camus

Fund Focus: Harding Loevner Frontier Markets

This quarter's fund focus highlights Harding Loevner Frontier Markets (HLFMX). Frontier markets are those that have yet to develop into the "emerging" class. Countries which are classified as "frontier" are known for their relatively high economic growth, a large number of young people, an expanding middle class to support local business, and natural resources that have the ability to draw profits due to increasing worldwide demand. This specific fund focuses on both bottom-up as well as top-down strategies when building the portfolio. The bottom-up strategy determines the sector and country portfolio weightings through a focus on company-specific investment decisions. A top-down country analysis focusing on monetary, macro-economic, and political risk is also employed to mediate the risk associated with bottom-up investing in frontier markets. We at Harbor like how diversified the portfolio is. The portfolio encompasses many geographic regions, from Africa to the Middle East to the Gulf States, and also focuses on a large array of different sectors including but not limited to consumer staples, healthcare, materials, and telecom services.

Is There a Change on the Wind?

It has now been 6 years since the beginning of the last financial crisis. As you may remember, at the time, the Federal Reserve's response was to take multiple extreme measures to help stabilize the US economy. One of the strategies taken was the reduction of short-term interest rates to 0%, where they have remained ever since. These low rates have created challenges for those living on a fixed income as well as many businesses, such as banks and insurance companies that rely on the higher rates. The Fed's goal at the time was to use a low interest rate environment to encourage households to borrow for such items as homes and autos in order to stimulate the demand for those products. The intent was also to encourage businesses to invest in capital expenditures for their business, hire more workers and thereby increase production. From an investment standpoint, the low rates have caused money to flow into the stock market, as rates on cash and bonds have paled in comparison and investors looked for alternatives.

The strategy does seem to have benefitted the economy and now that the economy is stronger, the Fed has been considering increasing rates to a more normal level. The determination of when to make this change requires near faultless timing. Increasing the rates too soon could increase inflation above the Fed's target range and put pressure on borrowing costs. Fed Chair, Janet Yellen, indicated in September that, depending on the state of the economy, the first rate hike may occur as early as mid 2015. Statistics that will be considered in the timing will be employment, wage growth, bank lending, housing and the outlook for future economic activity. Inflation will be monitored as well with the goal of sustaining a 2% or less inflation rate. As long as the data warrants the rate increase, economists expect that the stock market should be able to weather the increase without difficulty.

At Harbor, we continue to invest in bond funds of high quality and with short to intermediate durations as a way to prepare for the future interest rate increases. Consumers can further prepare by locking in to a fixed rate mortgage if their current mortgage has a variable rate ARM, paying down lines of credit that are tied to a Fed Funds rate and keeping credit cards and other loans paid down. Using these strategies will help minimize the downside of rising rates and position investors to capitalize on the advantages.

Wealth Accumulation: Company Benefits (Part 2)

Last quarter we dealt with the insurance piece of company benefits. This quarter we will look at some of the other possible offerings and some things to consider.

- **401(k)/Retirement Plan:** If possible within your budget, maximize your contributions. If not possible to maximize, fund enough to take full advantage of any matching funds your company might offer.
- **Flexible Spending Account:** These accounts, funded each pay period with pre-tax money, can help offset the cost of your medical and dependent care expenses. The disadvantage of these accounts is that any funds not used by the end of the year are lost to you, so careful attention to the amounts added should be taken.
- **Pension Plans:** Quite valuable in the past, pension plans are fast disappearing from the employee benefit ensemble, being replaced by 401(k)s or other options. With these plans, the company funds an account that accumulates over time and becomes available at a certain age as defined by the plan.
- **Employee Stock Ownership Plan (ESOP):** This is an excellent benefit that allows you to buy company stock at a discounted price, often 10 to 15 percent. As with the 401(k) contributions, it pays to maximize your purchases here. You should, however, take care that your overall investment portfolio doesn't get over-weighted with the company's stock. ESOP shares can usually be sold either immediately or after a set period of time allowing you to diversify.
- **Profit Sharing Plans:** This can be an excellent benefit, or not, depending on the profitability of the company. It may be stated as a percentage or an 'up to' amount. If evaluating a job offer, asking what the company has paid historically for your position for the last few years can give you an idea but remember that there are no guarantees.

There are a multitude of other possibilities for company benefits including tuition reimbursements, health club memberships, mobile phone reimbursement, parking reimbursement and the like. As with your insurance coverage, consider each offering individually, doing your research, and considering your lifestyle. Each year take the time to re-evaluate and update your choices, thereby making the most of the total package your company is offering.



Closing the Age Gap on Smartphone Users

Accusations of smartphone overuse have generally been targeted at younger users. But as smartphone technology continues to infiltrate our society on a social and business level, older generations, notably citizens of developed countries over 55, are observing a shift in their lives as well.

By the end of 2014, one in four citizens will be over the age of 55.¹ Companies in the mobile device industry are struggling to adapt to this shift and are constantly searching for ways to improve usability for the older generations. One in four over 55's with a smart phone have never downloaded an application, which causes major issues for app-development companies whose livelihood relies on these downloads¹. Critics might say that the apps are programmed by younger people for younger people, yet a huge market exists for companies who can appeal to an older demographic with relevant applications that are easier to use and view. The gap between generations of smartphone users is estimated to close completely by 2020, according to Deloitte, and the technology to appeal to both groups will surely follow².

¹ "The Smartphone Generation Gap: Over-55? There's No App for That." Deloitte. 1 July 2013. Web. 15 Sept. 2014.

² Zekaria, Simon. "Phone Addicts of the World, Unite." The Wall Street Journal 4 Sept. 2014. Web. 12 Sept. 2014. <<http://blogs.wsj.com/personal-technology/2014/09/04/phone-addicts-of-the-world-unite/?mod=ST1>>.

Living Well/Living Smart

Sleep & Coffee

A good night's sleep has typically been regarded as one of the most important things for those trying to live a productive and happy life. However, what exactly this means has been up for debate. Knowing exactly how much sleep to get, and when to get it may make all the difference in the world.

We all hear stories of entrepreneurs and Wall Street analysts getting 3 to 4 hours of sleep in any given night, and they seem to run some of the most powerful companies in the free world. However, this does not mean that this is a sustainable level of sleep. It can lead to mistakes and poor decisions on the job. These individuals don't necessarily lead desirable lifestyles, and as we've seen, are prone to make very poor decisions. Charles Czeisler, a sleep specialist at Brigham & Women's Hospital in Boston says, "Missing a night's sleep degrades our neurobehavioral performance". The appropriate amount of sleep helps keep our minds and bodies sharp.

Also, the recommended amount of sleep may be lowered from 8 hours down to between 6.5 and 7.5 hours a night. Researchers at the Center for Disease Control suggest that sleep patterns that fall in this range result in longer lasting energy throughout the day, and even lower mortality rates. And after 7 hours, research shows that more sleep is not more beneficial to the human body.

The timing of your first cup of coffee each day may also affect your efficiency. Studies have shown that during the time in which many people are having their morning cup of coffee, the body is "naturally caffeinating" by producing cortisol. Having the first cup simultaneously blunts the effects of caffeine, and results in increased tolerance to caffeine. Studies show that your first cup of coffee should come in the afternoon, around 2 o'clock, in order to maximize your energy throughout the day.

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Images: Nat Arnett

Harbor Happenings

Welcome Charlotte!

We are happy to announce that Charlotte Lane has joined Harbor's team as our new Office Manager. She is responsible for overall office management and organization, day-to-day operations, scheduling and special projects. Look for her at the front desk the next time you stop in!

Two Client Appreciation Parties

Thank you to all of our clients and associates that joined us for one or both of our recent events.

For our Boulder area clients we held our traditional wine and cheese event in our Boulder office. As always the wine and beer were fabulous and a good time was had by all.

For our Denver area clients we enjoyed a Rockies game at Coors Field in a corporate suite. This was Harbor's first baseball game client event and hopefully not the last.

Year End is Around the Corner!

Year-end continues to get more challenging for the financial industry with more delays and red tape every year. Consider acting now to make sure everything needed is completed before the end of the year. Possible tasks:

- If applicable, take your required distribution from your IRA or inherited IRA.
- Make a contribution to your child's 529 account.
- Consider any estate planning that might need to be done before year-end and phone your attorney for an appointment.
- Discuss with your accountant whether or not you might be eligible to contribute to a Roth or traditional IRA for 2014 and, if needed, contact us to open the account.
- Take care of any gifting, transfers of stock or cash that might need to be done by year-end.

Please contact our office today if we can help with any of these items. Thank you!

2014 Office Closures

Our office is closed on the following New York Stock Exchange holidays in 2014: Thursday, Nov. 27; Friday, Nov. 28 is a half day closure; Wednesday, Dec. 24 is a half day closure; Thursday, Dec. 25.