GLOBAL
WEALTH ADVISORS LLC
Registered Investment Advisor

INSIGHTS

Michael J. Krencicki, MSF, CFP®   October 2008   James M. Knaus, MSM, CFP®

Is It Different This Time Or Will The Gloom Subside?

If the financial news has you hanging your head, thinking about hiding your money under the mattress, turn off the TV, and take a deep breath. We've been here before.

Breathless talk of bank bailouts, the collapsing dollar, record oil prices, and mounting foreclosures has many investors nervously eyeing the safe haven of CDs, gold, and low-yielding Treasury bonds. Yet while a well-diversified portfolio might include some of those assets, overemphasizing them could carry a high cost in terms of lost opportunities and long-term losses.

It's hardly a secret that our current economic woes are linked to what had been a phenomenal rise in home prices that started during the late 1990s and gained momentum after the Sept. 11, 2001 terrorist attacks. Spurred by historically low interest rates and other factors, inflation-adjusted home prices rose 85% between 1997 and 2006, according to Yale University economist Robert Shiller, who developed the S&P/Case-Shiller Home Price Indices in the 1980s. It was the biggest national housing boom in U.S. history, and historic booms tend to be followed by historic busts. According to the S&P/Case-Shiller Home Price Indices, median home prices fell 8.9% nationwide in 2007, and that has sparked an explosion in foreclosures, a pervasive credit crunch, a slump in earnings for financial institutions, and plunging consumer confidence.

Financial stocks, now volatile and significantly off their highs, had been roaring ahead for years, helped along by the popularity of mortgage-backed securities. As home prices rose, mortgage activity soared, and banks repackaged bundles of home loans to sell to other investors.

By December 2006, the stock of financial companies had bubbled up to account for a record 22.3% share of the Standard & Poor's 500 stock index—almost 10 percentage points higher than in December 1999. But many of the bundled mortgages were of the notorious subprime variety. When the housing market cooled, defaults on those loans began, and soon financial institutions were swallowing huge losses. Their share prices plunged, and by April 2008, financial stocks were back down to a 17.2% share of the S&P.

As often happens when a bubble bursts, many investors found themselves over-concentrated in the hardest-hit sectors. Their financial holdings, which had been growing rapidly for years—and thus came to represent a disproportionate share of their portfolios—suddenly fell off the table. But the broader market has also suffered. The Dow Jones Industrial Average, after reaching an all-time high of 14,279.96 on Oct. 11, 2007, fell as low as 10,731.96 on July 15, 2008.

A similar chain of events occurred during the early 1980s. Energy stocks, which had comprised only 15.7% of the S&P in 1970, surged to a 28.2% weighting by 1980—and then fell to 11.6% in 1985.

That rise and fall was mirrored by

(Continued on page 4)

A Personal Note From Global Wealth Advisors

This quarter's newsletter once again offers a variety of topics to satisfy your appetite for financial nuggets. From articles dealing with market volatility to estate and income taxes and retirement planning, we trust you'll be pleased.

In recent weeks, we've seen continued market turmoil, with additional government support of financial companies in crisis. This was done to stabilize our financial markets and provide reassurance to foreign investors. Although we've seen the Lehman Brothers bankruptcy, the acquisition of Merrill Lynch, and the AIG bail-out, be assured that Schwab Institutional is a sound broker dealer and custodian for your investments. And if you have friends who are unsure about their current financial advisor relationship, please have them contact us for an objective discussion.

And of course this Fall we will witness an historic Presidential election. Whichever party is victorious, there is much to be done in Washington to address this country's domestic and foreign policies for the incoming administration.

We will continue to monitor the national and international developments, confident that the global markets will continue to function properly.

Thanks for your continuing referrals. We appreciate your confidence.

Jim Knaus Mike Krencicki

They Don't Call Them Trusts For Nothing

Maybe you heard the story about the 60-year-old oil heiress who died and left everything to her husband. He was 71 and died just two months after remarrying a much younger woman, who inherited his first wife's fortune. The heiress' children got none of it. Or perhaps you heard about the man who left his son $500,000, which he used to buy a house with his wife. Two years later, they divorced, and she got the house in the settlement.

Then there's the one about a couple that inherited $250,000 from an uncle but received none of it because the IRS exercised its right to take the inheritance to satisfy back taxes.

Obviously, these aren't the kinds of stories that you want people to tell about your family. To avoid the possibility of such trouble, you may need to establish a trust.

A trust is an agreement in which you transfer ownership of property to a trustee of your choosing, who then manages it for the benefit of your loved ones. The trust can be funded during your lifetime or at your death. Typically, it costs between $1,000 and $2,000 to set up a trust, although you might spend more depending on where you live, the legal advisor you use, and the complexity of the trust.

Trusts have long been used by the wealthy to reduce estate and income taxes, but more and more middle-class people are finding trusts can benefit them, too. Appreciation in real estate values over the long term, stock market gains for astute investors, and the slow march of inflation have thrown many middle-class individuals into higher income tax brackets and left them facing the prospect of estate taxes that could decimate the value of bequests to their loved ones.

Life is full of surprises, but experts say that you can trust a trust

A bypass trust can ensure that a married couple maximizes its combined estate tax exemption of $4 million (for 2008); a charitable remainder trust can reduce estate taxes while allowing you to do good for your community; and a life insurance trust can help guarantee the amount your heirs will receive. You can also use a trust to direct how the assets you leave behind will be managed, and to ensure that your bequests end up with the intended heirs.

The oil heiress, who had thought she was too young for estate planning and had feared that her 25-year-old son and 27-year-old daughter would squander the money, could have used a trust. She might have set aside some assets in the trust for her children until they were older, or she could have appointed a trusted friend or advisor as trustee to disburse the assets.

A trust also would have left the divorcing son in a better bargaining position to keep his house. Had his father left the money in a trust, allowing a trustee to buy the house for the son, the wife wouldn't have been able to get it. And the IRS could not have seized the assets in a trust established for the beneficiary with tax problems.

Life is full of surprises, but you can trust a trust. ●

Don't Wait Until The Last Minute On Taxes

Most people wait until the last couple of weeks in December to do year-end tax planning. By then, however, it's often too late to shuffle things around. It's like waiting until the day before Christmas to do your holiday shopping—all the bargains are gone. Waiting until the 11th hour with your tax planning could mean missed opportunities, particularly when you need to get tax information from one professional to another. Consider acting on these four ideas before the end of the year.

Manage AMT exposure. The alternative minimum tax continues to affect millions of taxpayers in the middle and upper income tax brackets. When your tax bill under the AMT formula exceeds your regular tax, you pay your regular tax plus the excess AMT amount above your regular tax. Are you going to exercise incentive stock options, realize hefty capital gains, or take large deductions for state and local taxes, miscellaneous itemized expenses, or accelerated depreciation? If so, you stand a chance of being ensnared by the AMT.

When the AMT applies, the tax rate is 26% for incomes less than $175,000; 28% if above, which may actually be lower than your regular income tax bracket. Once you know you're going to be caught in the AMT boat, you might actually save by pushing additional income into that year.

To manage your AMT exposure, you'll need to project your income and deductions over multiple years. You may want to shift income to years in which the AMT gives you a lower tax rate, while pushing deductions that would be lost under the AMT into non-AMT years. Deductions allowed under both tax regimes, such as charitable gifts, save you more the higher your tax bracket.

Finally, if you know the AMT is coming, avoid private-activity municipal bonds, whose income is taxable if you owe AMT. The sooner you figure out if you'll be caught by the AMT, the better chance you have for planning around it to

Smart Moves Five Years From Retirement

The notion of outliving your retirement income is not a happy one, and now, with tens of millions of baby boomers about to embark on decades of life after work, anxiety is running high. But with some wise preparation, you can create a retirement strategy that keeps you comfortable and financially secure.

Here are five critical moves to consider five years in advance of your retirement deadline.

1. Visualize your retirement. Steven Covey, author of *The Seven Habits of Highly Effective People*, famously suggested: "Begin with the end in mind." So before you crunch the first number, dig deep and imagine what you want from retirement. You might begin by making sure you want to retire at all. These days, more and more people are deciding to continue working, at least part time. And if you will leave work behind, how will you spend your time? Pursuing adventure travel? Kicking back at your lake cottage? Downsizing and moving to a new community?

If you're married, talk to your spouse about what she or he envisions. It's important that you get on the same page about your plans and goals. Once you've identified your objectives, determine what they'll cost and consider where your income will come from—Social Security, a company pension, distributions from your 401(k), rental property income, interest and dividends on other savings, or perhaps an inheritance.

2. Examine your footprint. Most people underestimate what retirement will cost, but a simple cash-flow planning exercise can help set the record straight. Start with your core living expenses, and project those out for the next five years, adding in other goals that will require funding: helping a child with wedding expenses, for example, or a house renovation.

Next, consider what your expenses will be in retirement. It's likely the early years will be more active—and more expensive. A big cost that many pre-retirees don't see coming is health insurance, which can easily run $16,000 a year for a married couple until age 65, when Medicare kicks in. Thanks to health care costs and other rapidly increasing expenses, many financial experts now suggest retirees have as much income during retirement as when they were working.

3. Address your liabilities. There's good debt and bad debt. As you approach retirement, it's critical to get rid of anything on which you're paying double-digit interest rates. That likely includes credit cards and possibly even car loans. For longer-term obligations, if you're paying between 5% and 7%, that's probably all right, particularly if it's on a mortgage or home equity loan for which some of the interest may be tax deductible.

4. Max out your savings. You're in your peak earning years, and now is the time to push hard to save all that you can. Many experts recommend saving 20% of your income as a rule of thumb. At the very least, make the maximum allowable contributions to your retirement plan and, if eligible, to an IRA as well. This is your last, best chance to increase the size of your nest egg and your income during retirement.

5. Fine-tune your investment portfolio. One factor to consider during this crucial period is whether stock options, restricted stock, or company stock you own outright in taxable or tax-deferred accounts leaves you dangerously overexposed to the fortunes of your company. You may do well to diversify, to the extent you can, even if it generates taxable capital gains. But now is also the time to revisit your overall asset allocation. The risk of major losses on the eve of retirement argues for a more conservative approach, yet it's important for your portfolio to continue growing, now and during retirement.

We would be happy to review with you your current retirement plan and asset allocation in view of your goals for your years after work. Please give us a call.●

lower your taxes.

Don't miss a chance to deduct college costs. This year, more liberal rules apply to deducting payments for college tuition and fees. If you're single and make between $65,001 and $80,000, or married and earning from $130,001 to $160,000, you may deduct the first $2,000 in costs. If your income is below those ranges, the first $4,000 in college costs are deductible; above the ranges, zilch. Don't let an extra dollar of income cost you. If you are close to the upper end of the income ranges, plan now for ways to defer income to maximize this deduction.

Plan business opportunities. Businesses may deduct the first $128,000 of assets purchased in 2008. But buy too much and you'll save less, because the maximum deduction is reduced by each dollar of equipment purchased in excess of $410,000. And this deduction can't create, or add to, a business loss. However, you can deduct as bonus depreciation half of the cost of new property you don't write off.

Corporations, meanwhile, can stretch their cash flow this year. Only 80% of estimated tax for the third quarter is due by the usual September 15 deadline. The remainder may be paid October 1.

Review state tax changes. Not all moves reducing your IRS bill slice local taxes. Some states have declined to adopt recent federal tax breaks, while others have rewritten laws in response to fiscal crises. Examine your state's latest rules at www.taxsites.com/state.html. ●

Marriage Doesn't Mean Owning All Your Assets Jointly

Marriage is all about togetherness. Yet when it comes to owning assets, too much togetherness may not be financially healthy.

Owning assets jointly is more convenient than individual ownership, and it's the simplest way to avoid probate after a spouse's death. But couples often should consider separating their assets. Here's why:

Estate tax implications. Estate rules let spouses leave unlimited property to each other tax free. That's okay when the first spouse to die leaves everything to the second, but the second death could result in a whopping tax bill. Couples likely to have estate tax issues could acquire property individually to help maximize the value of each other's estate tax exclusion. While owning a house jointly is important for giving both spouses equal claim if they divorce, other assets can and should be held separately in roughly equal shares.

Dividing jointly owned property. How you take title also affects who can inherit your property. If you own it individually or jointly as "tenants in common," each of you may specify in your will that you want a particular asset or share of an asset to go to a designated heir. However, if you take title as "joint tenants" (with rights of survivorship) or "tenants by the entirety"—the most common form of ownership for married couples—you won't be able to say how assets are split. That may work if you and your spouse share the same beneficiaries. But it could be a problem if, for example, you're in a second marriage and want to divide assets among children from different marriages.

Consider John and Mary. Because they own their property as tenants in common, each holds 50%, and John can bequeath his share to children from a prior marriage. Mary won't automatically inherit John's interest.

But if they hold their assets as joint tenants or tenants by the entirety, the surviving spouse becomes the sole owner of everything the couple owned together. It won't matter that John's will names his children as beneficiaries; if he dies first, the title documents will govern, and Mary will decide how assets are divided when she dies.

Other considerations. Owning assets separately is especially important if your combined net worth is at or above the IRS estate tax exemption—$2 million in 2008 and $3.5 million in 2009. Once you approach those levels, it pays to consider ways to separate assets. Also, since joint-tenancy assets can be taken by creditors or lost in lawsuits once an individual's assets are exhausted, doctors or others who can be sued easily will want at least half of their assets in their spouse's name.

Deciding how to hold title to your assets is not a simple decision, as state laws differ and each situation is unique. We can work with your attorney to help decide what's best for you and your spouse. ●

Will The Gloom Subside?

(Continued from page 1)

the boom and bust of technology shares in the late 1990s. By August 2000, information technology stocks had risen to account for one-third of the S&P 500. When that bubble burst, that sector's weighting fell to 14.3% within a year.

Bubbles That Went Bust

Sector	Boom	Bust
Energy stocks	28.2% of S&P 500 in 1980	11.6% of S&P 500 in 1985
Internet-related stocks	33.6% of S&P 500 in 2000	14.3% of S&P 500 in 2001
Financial stocks	22.3% of S&P 500 in 2006	17.2% of S&P 500 in 2008

Source: Standard & Poor's

While many investors suffered losses when these bubbles popped, the economy soon recovered, and it will happen this time, too. There's no way to know exactly when that will occur, but the point is to remain invested and diversified. That lets you take advantage of lower prices and puts you in position to benefit when the market inevitably turns upward.

Think about which investors had the best results during past bubbles. Was it those who panicked and fled the markets after the bubble burst—or those who made short-term adjustments but stayed invested and bought more while prices were low?

We're now in a transition from a market where growth and revenue reigned supreme to an era when a strong balance sheet will be most important to investors. When the economy is shaky and the market is well off its highs, it often makes sense to turn toward solid companies in steady industry sectors, such as consumer durables, and put less emphasis on high-flying prospects.

Sure, the stock market probably will remain choppy for a while, as the economy continues to recover from the nation's house-happy hangover. But savvy investors will see the situation as just another great, post-bubble buying opportunity. ●