Fagan Financial Report

Registered Investment Advisers

VOLUME 19, ISSUE 4 FOURTH QUARTER 2014

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TO OUR CLIENTS

Which of the following would prompt you to respond quicker – "there's popcorn in the lobby" or "there's a fire in the lobby?" Suffice it to say that if you are like the vast majority of us, the potential for a fire would get you out of that seat a lot faster than the potential for some popcorn. The logic is simple – fear is a greater motivator than greed. Investing works in a similar fashion. This is why investors tend to buy near the top and sell near the bottom. Although not foolproof, by developing, implementing and adhering to a mid- to long-term strategy, a long-term perspective and a disciplined approach to managing your portfolio, your chances of success in the investment arena will improve.

We begin this newsletter with the above because the short-term noise and news currently raising volatility in both the equity as well as fixed income markets has most likely caused some to question their commitment to their investment strategy. With this in mind, we thought it appropriate to reiterate where we stand on the economy, fed policy and the financial markets.

With a high degree of conviction, we believe that the Federal Reserve will maintain an accommodative stance regarding monetary policy longer than the consensus anticipates. We believe this because allowing, some say even encouraging a little inflation is a far better outcome than raising interest rates sooner rather than later and risking a deflationary environment. In fact, a noted inflation hawk, St. Louis Federal Reserve Bank President James Bullard, reversed his stance with regard to monetary policy stating that "Inflation expectations are declining in the U.S. That's an important consideration for a central bank. And for that reason I think that a logical policy response at this juncture may be to delay the end of the QE."

Although not physicians by any stretch of the imagination, from what we have read, the potential for the morphing of Ebola, a virus named in 1976 after a river in Zaire (we did not know that it was named after a river or initially became a health concern that long ago) into an epidemic in the United States, is a very low probability event. However, the news created by any contagion has a high short-term impact on investor psychology. Although this impact cannot be ignored, it should also not be overemphasized by long-term investors.

We do not believe the recent pullback in the market is cause for longer-term concern. Despite the fact that over the short-term stocks may get weaker before rallying, we do not believe that this is a repeat of 2008. Every correction is not the start of a bear market. Stop fighting the last war. American consumers and corporations, including financial institutions, are in much better condition than they were in 2007. Corporate balance sheets have been fully repaired while personal balance sheets continue to improve.

We continue to favor investing predominantly domestically. The United States was the first to go into the financial crisis several years ago, tackle most of the issues that caused it head on and emerge from it better off. Although also along the curve, most countries, especially Western Europe, are still dealing with the repercussions of the financial crisis.

Finally, the long-term is more predictable than the short-term. Maintain a three-, five-, even a ten-year perspective. If history is any guide you will be happy you did. That said, we do realize that the market has been volatile recently and with this in mind, please feel free to contact us with any questions, concerns or should you wish to get together to discuss your portfolio.

CORPORATE EARNINGS SEASON ABOUT TO KICK OFF

As we prepare to enter first quarter earnings season, we have assembled some strategies for dealing with the volatility which is sure to accompany these corporate reports.

You either have faith in the benefits of investing or you do not. Changes in the value of your portfolio should not alter that faith. It is not ironic that market downturns challenge this assumption. The news media jumps on stories of lost wealth and investors tend to get caught up in those stories. However, keep in mind that despite the horrific bear market experienced during 2008, the stock market is within ten percent of its all-time high. You either believe in the fairness and longer-term opportunities of investing or you do not. If you think the playing field is stacked against you, get out now as stocks have doubled over the past three years rather than getting out during a period of crisis.

Going about our daily business of financial planning and managing money, we are quite often asked the question “how often should I review my account.” To that we may respond, “how often should you shovel your driveway in the winter or water your lawn during the summer.” More specifically, the answer is whenever it needs it. When you have a change in your life, be it marriage, a new baby, a change in jobs, retirement or the death of a spouse, review your financial situation. When the stock market is volatile, has lost more than ten percent or for that matter gained more than ten percent, review your financial situation.

Investing is not a static environment. You shouldn’t review your portfolio merely on a quarterly basis. The stock market does not experience volatility merely because it is the end of a quarter. Review your portfolio as the values change or as noted above, as you experience changes in your life.

Have a plan to deal with the potential for a negative short-term outcome in a specific investment you have made or perhaps a downdraft in the overall stock market. By nature people are optimistic. We like to think good things will happen to all of our investments. However, as you know, that is not always the case. So have a plan for dealing with a negative outcome. Panic is not a strategy (nor is greed). Assess your situation and develop a sell discipline.

Don’t fight the last battle or the ghosts of 2008. Investors have a tendency to miss opportunities because they remain afraid of a similar bear market like the one of a few years ago. Allocate your investments according to your objectives and then as noted above closely monitor that allocation. That is your best chance of success. Otherwise, you’ll be getting 0% to 1% in the bank which also puts your retirement plan and/or retirement income at risk.

Holding some cash can be a strategy. If you are a bit skittish, a bit conservative or need a level of comfort, keep ten to twenty-five percent of your investment portfolio (this excludes your vacation, rainy day, short-term money) in cash. You’ll sleep better at night and who knows, you might be able to put this cash to work at lower market levels.

THE BOTTOM LINE – Establish a well-designed financial and investment plan. Then, monitor, evaluate and, as necessary, make changes to that plan along the way. This seems logical and simple. However, when fear of monetary loss and emotions get in the way, watch out. That is a certain recipe for buying high and selling low! Avoid this by sticking to your plan and being disciplined.

More than 25 Years Serving the Investors of the Capital Region

AMERICANS BEARISH ABOUT THE ECONOMY

A report released during July 2014 by the Board of Governors of the Federal Reserve System detailing findings from a September 2013 survey and entitled "Report on the Economic Well-Being of U.S. Households in 2013" found many Americans a bit bearish about the economy and also their particular situation. Although the findings of the survey were not very surprising, many were certainly noteworthy. A selected few follow below.

"Over 60 percent of respondents reported that their families are either "doing okay" or "living comfortably" financially; another one-fourth, however, said that they were "just getting by" financially and another 13 percent said they were struggling to do so."

"Thirty-four percent reported that they were somewhat worse off or much worse off financially than they had been five years earlier, 34 percent reported that they were about the same, and 30 percent reported that they were somewhat or much better off."

Regarding home ownership or renting, "45 percent of homeowners who had owned their home for at least five years reported that the value of their home was lower than in 2008, 20 percent believed the value of their home was the same, and 27 percent believed it was higher than in 2008." Meanwhile, "the most common reasons cited by renters for renting rather than owning a home were an inability to afford the necessary down payment (45 percent) and an inability to qualify for a mortgage (29 percent)."

Regarding the obtainment of credit, "31 percent of respondents had applied for some type of credit in the prior 12 months" while "one-third of those who applied for credit were turned down or given less credit than they applied for."

Regarding debt pertaining to education, "24 percent reported having education debt of some kind. Among those with such debt , the average amount of all education debt (both for the respondent's and other's education) was $27,840 with a median of $15,000." Somewhat troubling was the finding that "some households struggle to service this debt, with 18 percent of those with debt for their own education indicating that they were behind on payments for these loans or reporting that they had loans in collections."

Regarding savings, "among those who had savings prior to 2008, 57 percent reported using up some or all of their savings in the Great Recession and its aftermath" and "48 percent of respondents said that they could completely cover a hypothetical emergency expense costing $400 without selling something or borrowing money."

On retirement, the survey found that "almost half of respondents had not planned financially for retirement, with 24 percent saying they had given only a little thought to financial planning for their retirement and another 25 percent saying they had done no planning at all."

Finally, a whopping "31 percent of respondents reported having no retirement savings or pension, including 19 percent of those ages 55 to 64, and 25 percent didn't know how they will pay their expenses in retirement."

We consider the findings part and parcel with a slow recovery from a credit-induced recession. Most recessions are interest-rate induced or ones where in response to an economy that is expanding at a pace the Fed deems unsustainable or where inflation is occurring above the Fed target, interest rates are hiked to the point that they choke off growth and/or inflation. Once interest rates decline, economic growth resumes. Conversely, a credit-induced recession is one in which over time, consumers have accumulated too much debt, impairing their balance sheets. In response the economy slows. The Federal Reserve, in an effort to get the economy going again, cuts interest rates. However, consumers respond only gradually and begrudgingly as it takes some time to work off the excess debt, quite often five to ten years.

Even after five years since the official end of the Great Recession, the outlook of many Americans is still being impacted by the lagging indicator that is the Labor Market as well as corporate restructuring and a slow-to-hire public sector.

COSTLY RETIREMENT PLAN MISTAKES

With the migration from company sponsored Defined Benefit Plans to Defined Contribution Plans such as a 401(k), 403(b) or Deferred Compensation (457), it is critical to choose the correct plan, allocate your assets according to your objectives and designate the appropriate beneficiary(ies). Having been in business for over twenty-five years we have been witness to some mistakes in each category.

Assuming that you are in a combined Federal and New York State tax bracket of 30%, it is generally to your benefit to choose a retirement plan that allows for tax deductible contributions. If we use the tax brackets above as an example, for every $1,000 deposited into the plan, your tax savings would be $300. Therefore, saving $1000 would only cost you only $700. The other $300 would be tax savings. As a rule of thumb, remember that it is better to choose plans that allow for tax deductible contributions if you are in a relatively high tax bracket versus plans that do not allow for tax deductible contributions. The opposite holds true if you are in a low tax bracket.

Most company sponsored plans now offer tax deductible contributions defined as a Traditional 401(k), 403(b) or 457 as well as Roth 401(k), 403(b) and 457. Traditional plans offer tax deductible contributions and taxable withdrawals while Roth plans offer non-deductible contributions and tax-free withdrawals. Keep in mind that regardless of whether you choose the Traditional or Roth, both may levy tax and penalties should you need the money prior to normal retirement age. Please check with your tax advisor prior to investing.

After selecting the plan that fits your needs, your next job is to fund the plan. Under this category, try to deposit at least an amount that maximizes your employer match, should there be one. Most employees tend to become too conservative with their investment strategy or concentrate their deposits into company stock. Both are mistakes. As a rule of thumb, we would recommend those under fifty with more than ten years until retirement invest on no more than a 3:1 ratio of stocks to bonds. Those over fifty with five to ten years should use a ratio of no more than 2:1 stocks to bonds while those within five years of retirement 1:1 stocks to bonds. Those under forty with more than twenty years until retirement should invest nearly their entire balance in the stock market. Once again, every situation is different so consult your advisor.

An asset allocation mistake that we have also noticed is having an over-concentration of contributions and accumulated balances in the stock of the company you are employed by. In the Capital District, some employees of General Electric have deposited more than 50% in their company stock (or more). We believe that in so doing, you are assuming an undue amount of company specific risk and creating an undiversified portfolio that has a low correlation and low level of predictability relative to the total stock market. This can lead to a high level of volatility and poor performance.

On the flip side, upon retirement and the attainment of age 70½, make certain that you are taking mandatory retirement distributions. Coordinate this with your planner and/or tax advisor. Also, keep in mind that the tax on the withdrawal that should have been made but was overlooked is fifty percent, a pretty steep penalty.

Let’s now touch on the designation of a beneficiary or beneficiaries. First and foremost, make certain that you designate a beneficiary. Should you fail to choose a beneficiary, your estate becomes the beneficiary by default. If married, you will lose the valuable spousal rollover option as well as the option to stretch the payout beyond the life expectancy of the beneficiary. Finally, make certain that you designate contingent beneficiaries that will receive the proceeds from your retirement plan should the primary beneficiary predecease the account holder.

Largest Holdings Regardless of Asset Class
Ranked by Market Value as of September 30th, 2014.

Percent of Total Assets Managed	Company Name	Symbol	As of Sept 30, 2014	As of Aug 31, 2014	As of July 31, 2014
9.75%	Cash & Equivalents		1	1	1
3.06%	Loomis Sayles Bond Fund	LSBRX	2	2	2
2.99%	DoubleLineTotal Return	DLTNX	3	5	4
2.99%	Gilead Sciences, Inc.	GILD	4	4	7
2.92%	SPDR Dividend ETF	SDY	5	3	3
2.85%	Apple Computer	AAPL	6	6	6
2.75%	MetWest Tot Ret Bond Fund	MWTRX	7	7	5
2.28%	Nike, Inc.	NKE	8	9	10
2.11%	Conoco Phillips	COP	9	8	8
1.95%	RidgeWorth Flt Rate	SAMBX	10	10	9
1.80%	Google, Inc.	GOOG(L)	11	11	11
1.71%	General Electric	GE	12	12	12
1.55%	Celgene Corporation	CELG	13	15	18
1.52%	Baird Core+ Bond Fund	BCOSX	14	16	16
1.52%	Income Fund of America	IFAFX	15	13	20
1.47%	PIMCO Diversified Income	PDVDX	16	14	14
1.45%	MasterCard, Inc.	MA	17	17	15
1.44%	JP Morgan Chase	JPM	18	18	17
1.34%	Visa, Inc.	V	19	19	19
1.29%	Bank of America	BAC	20	21	21
1.23%	Ridgeworth High Income	STHTX	21	20	13
0.98%	Hartford Financial Services	HIG	22	27	28
0.97%	Parnassus Equity Income	PRBLX	23	26	24
0.97%	Express Scripts Co.	ESRX	24	24	25
0.97%	Altria Group, Inc.	MO	25	29	29
0.92%	Harley Davidson	HOG	27	25	23
0.88%	Hertz Glbl Hldgs	HTZ	28	23	26
0.63%	Ford Motor Company	F	40	22	22

Portfolio Concentration: Top 25 holdings represent 53.82% of the Assets Managed at Fagan Associates as of September 30th, 2014.

Largest Mutual Fund Holdings as of September 30th, 2014

Domestic Equity Funds	International Equity Funds	Balance/Fixed Income/ Muni Fund/ETF
Parnassus Equity Income Fund	Oakmark Global Select	Loomis Sayles Bond Fund
Dow Jones U.S. Broad Mkt Index	Harbor International Fund	Double Line Total Return Fund
Schwab 1000 Fund	Oakmark International	MetWest Total Return Fund
Scout MidCap Fund	Tweedy Browne Global Value	Ridgeworth Floating Rate Fund
Oakmark Fund	Templeton Foreign	Baird Core Plus Fund

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•"The Record Review" – an outline of our column that appears in the Troy Record every Sunday.

• "Widely Helds" – a look at the price action and news releases from the most widely held stocks.

•A spotlight on one or some of our **mutual fund holdings or EFT holdings.**

•A look at the upcoming week, including economic data and earnings reports.

•Monthly notable changes to our investment portfolios after the close of the prior month.

* Periodic interviews with other industry professionals, including mutual fund managers, insurance professionals, accountants & attorneys.

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