New England GUILD
Wealth Management & Investment Advisors

WEALTH MANAGEMENT COMMENTARY

PROTECTING AND BUILDING YOUR FINANCIAL FUTURE

SPRING 2012 (860) 236-3301 (800) 254-8453 www.neguild.com

Market Spotlight

Index	Returns			
	Qtr	Annual		
	1ST Qtr	1 YR	3 YR	10 YR
Equities				
S&P 500	12.6%	8.5%	23.4%	4.1%
Russell 2000	12.4%	-0.2%	26.9%	6.5%
MSCI AC World exUS	11.2%	-7.2%	19.1%	7.3%
MSCI AC World	11.9%	-0.7%	20.8%	5.3%
REITs	10.8%	13.5%	44.5%	10.4%
Barcap Agg. Bond	0.3%	7.7%	6.8%	5.8%
90 Day T-Bills	0.0%	0.0%	0.1%	1.9%

Global financial markets closed out a buoyant first quarter led primarily by asset classes that were out of favor last year. Amid perception that a worst case scenario was averted in Europe, most risk assets such as global equities, high yield and emerging market bonds outperformed, while perceived safe havens such as US Treasuries lagged. The strong rally seen in US markets was attributable in large part to gains in technology and banking stocks, with a 50% surge in Apple shares accounting for 14% of the S&P 500's 12% rise for the quarter. To that point, an analyst for the Financial Times quipped, "There are now four asset classes; stocks, bonds, commodities and Apple!" REITs also had another strong quarter.

We are now three years into the recovery and the US financial system continues to heal. At the same time, improved economic data and fundamental factors remain positive for equities. Corporate profits continue to push higher driven by improvements in productivity; the manufacturing sector is growing; bank lending is increasing; auto and retail sales are strengthening as consumer spending accelerates; unemployment is slowly easing; housing affordability is improving, with housing prices becoming more favorable than rental market alternatives; interest rates remain low; and cash rich companies are shareholder-friendly, buying back stock and raising dividends.

That said, we have a long way to go, and there is no shortage of threats to the US recovery: oil prices, a recession in Europe with severe structural problems that have been "kicked down the path"; weaker growth in China with the hope for a "soft landing"; political uncertainty associated

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Investment Commentary: Pearls of Wisdom

Recently two of the most respected, and most independent-minded, investors we know (Jeremy Grantham and Warren Buffet) have written pieces that contain insight into the essence of their investment philosophy and principles. We don't necessarily agree with every tenet, but each is worth pondering. Rather than trying to plagiarize or paraphrase, we think it best to simply quote selectively from their respective pieces.

Jeremy Grantham, CIO of GMO Investments, in his Quarterly Letter of February 2012 offers 10 pearls of wisdom for "individual investors setting out on dangerous investment voyages:" Here are a few:

- ***Believe in history.*** "You absolutely must ignore the vested interests of the industry and the inevitable cheerleaders who will assure you that this time it's a new high plateau or a permanently higher level of productivity, even if that view comes from the Federal Reserve itself."
- ***Neither a lender nor a borrower be.*** "If you borrow to invest, it will interfere with your survivability. Leverage reduces the investor's critical asset: patience."
- ***Don't put all of your treasure in one boat.*** "This is about as obvious as any investment advice could be. It was learned by merchants literally thousands of years ago."
- ***Be patient and focus on the long term.*** "Wait for the good cards. Individual stocks usually recover, entire markets always do. If you've followed the previous rules, you will outlast the bad news."
- ***Recognize your advantages over the professionals.*** "By far the biggest problem for professionals in investing is dealing with career and business risk; protecting your own job as an agent. The second curse of professional investing is over-management caused by the need to be seen to be busy, to be earning your keep."
- ***Try to contain natural optimism.*** "Optimism has probably been a positive survival characteristic. But optimism comes with a downside, especially for investors: optimists don't like to hear bad news."

Warren Buffet's Berkshire Hathaway shareholder letters are all classics. In this year's letter he states that "investing is forgoing consumption in order to have the ability to consume more at a later date." The corollary to this is that "the riskiness of an investment is not measured by beta (volatility) but rather by the probability of that investment causing its owner a loss of purchasing power over his contemplated holding period. He then goes on to comment on three major categories of investment possibilities:

1. ***"Investments that are denominated in a given currency include money-market funds, bonds, mortgages, bank deposits, and other instruments.*** Most of these are thought of as "safe." In truth they are among the most dangerous of assets. Over the past century these instruments have destroyed the purchasing power of investors in many countries, even as the holders continued to receive timely payments of interest and principal. This ugly result, moreover, will forever recur."

2. ***"Investments that involve assets that will never produce anything, but that are purchased in the buyer's hope that someone else – who also knows that the assets will be forever unproductive – will pay more for them in the futures"***. . . And then the old proverb is confirmed once again: "What the wise man does in the beginning, the fool does in the end." The major asset in this category is gold, currently a huge favorite of investors who fear almost all other assets.

3. (Warren's preference) ***"Investment in productive assets, whether businesses, farms or real estate. Ideally, these assets should have the ability in inflationary times to deliver output that will retain its purchasing-power value while requiring a minimum of new capital investment."*** "I believe that over any extended period of time this category of investing will prove to be the runaway winner among the three we've examined. More important, it will be by far the safest."

We offer these insights because of our belief that in today's environment it is critical that investments be anchored in principles which have withstood the test of history.

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with upcoming elections throughout the world; continued geopolitical worry, particularly in Iran; and the unknown effects on the economy once stimulative policies have ended. For example, while the Fed's near-zero interest rate policy can help to heal the economy, it doesn't address longer-term structural issues; and the unknown impact of such policies on future inflation, interest rates, and asset prices creates further uncertainty.

This March marked the 3-year anniversary of the equity market trough following the collapse of Lehman Brothers in September 2008 and the subsequent financial crisis. Although the S&P is still 10% off its peak level on October 9, 2007, it has seen a sharp rebound through the end of last quarter, up 122% on a cumulative basis or 29.8% annualized. These strong returns were seen across most asset classes amidst a backdrop of events including a global financial meltdown, a deepening sovereign and banking crisis in Europe, unprecedented central bank actions, a Japanese tsunami, an Arab spring, a federal budget deadlock and an historic downgrade of US debt.

The inability to predict such events as we've experienced these past three years and the subsequent market reaction, points out once again the importance of adhering to one's investment objectives and staying invested during times of uncertainty. We continue to believe that it is a time for investors to be cautious and patient. But we also believe that a balanced portfolio that takes into account the timing of cash flow needs, rather than one designed for either doomsday or certain recovery, will help achieve investment success. From an individual perspective, we've watched significant monies flow out of equities and into bond funds, suggesting that investors know bonds are safe and that stocks are not. To that, we think Mark Twain said it best: "It ain't what you don't know that gets you in trouble. It's what you know for sure that just ain't so"!

Bond Risk

We have been surprised by the continued inflows of investor deposits into bond mutual funds. It strikes us that perhaps the lay investor perhaps doesn't fully appreciate the risks in bonds. It is true that over the past 10 years bonds have out-performed stocks with far less volatility. It is also true that since 1980 bond returns have exceeded their yield from the coupon alone because of the decline in interest rates, from 15.9% in 1981 to 2.1% currently. Treasury bond yields are now near their lowest levels of the past 70 years!

So what's not to like about this? Simply that, when you come to the end of the line, you must turn around. Bond yields can't go much lower, and when they begin to rise, then bond returns will be less than their coupon yield. The math alone suggests that over the next three to five years, total returns from bonds are likely to be very modest nominally and negative when adjusted for inflation.

When interest rates rise, bond prices fall (and vice-versa). For example, if interest rates rise by 100 basis points (1%), intermediate-term treasury bonds might fall in value by 5.0% (equal to their duration). Shorter term bonds would fall less than longer-term bonds since they are able to reinvest at the new higher yields sooner as bonds mature. Bonds with higher coupons that, in addition to interest rate risk, may be exposed to other types of risks such as credit or default risk also tend to be less sensitive to rising interest rates alone. Because bonds represent an important tool in the management of portfolio volatility, we still use bonds in portfolios. However, we now tend to favor bond funds with emphasis on the types of bonds mentioned above and on yield-oriented equity funds in the face of our concern with the probability that future interest rates will more likely be higher than lower.

We Are Pleased to Announce

Claudia Flannery joined us in February as a Client Service Associate. We were drawn to Claudia by her customer service experience, outstanding organizational and communication skills, and her warm personality.

Claudia has worked at The Travelers, Hilb, Rogal & Hobbs, Brown & Brown of CT, and Robert Hensley & Associates, with experiences in customer service, marketing, and corporate communications. She holds a CT Insurance Producer License in Life & Health and Property-Casualty. In addition, she has been active as a volunteer caseworker for the American Red Cross in the Service to the Armed Forces division.

Claudia received her Bachelor of Arts degree from Marymount College. She and her husband Bernie live in New Hartford. Their son James serves in the U.S. Army and daughter Erin is an attorney. We are delighted to have her at The Guild.

Excursion: Inn at Castle Hill

Interested in an absolutely wonderful meal and a lovely overnight stay? Consider the Inn at Castle Hill in Newport, Rhode Island. The Inn is a converted mansion sitting atop a bluff with unobstructed, three-sided views of Newport Harbor. Along with the original mansion, the Inn offers cottages, both cliff side and beachside. The rooms in the original mansion are gracious, oozing old world charm. One should also consider adding dinner (or other meals for that matter) to fully appreciate the splendor that the Inn offers. While the cost of dinner can be pricey, each course is splendidly paired with wine, the meal is unparalleled. Only the best NYC restaurants can compare. Reservations for both rooms and dining can be a challenge during the summer months so plan far ahead if you can.

QUOTE: *"Bonds promoted as offering risk-free returns are now priced to deliver return-free risk."* — Shelby Cullom Davis (many years ago)

Our firm continues to grow by referrals from our clients. Thank you for recommending us.

PRINCIPALS OF THE NEW ENGLAND GUILD, INC.

Harold L. Rives III, CPA
E. Patrick Logue, CPA
Eliot P. Williams, CFA
Susan M. Grayson