



May 28, 2010

D3 Business Update:

Starting on May 15th, we began the annual update of the financial plans for our Comprehensive and Retainer clients. Our goal is to finish all updates by June 30th. **As a reminder, we update your financial plan every year to so that you can re-evaluate how much risk you have in your financial life. This helps you to determine how much risk you want to assume in your investment portfolio.** With all of the uncertainty and volatility in the markets, this effort is designed to provide you with valuable insights to help you project your financial well being.

We have two interns this summer; Brad Schwer and Evan Plumb. Both are finance majors at Illinois State. They will be working in the office, part time, between June 1st and August 15th.

As we shared with you last month, we were invited for the second year in a row to attend the Barron's Winners Circle Conference for the Top Independent Investment Advisors in the nation. **For a second year in a row, we have learned that we offer more high quality services, have a more highly educated staff, and charge lower prices than our competition. As a result, for new clients we are going to raise our fees.** If you know of anyone that can benefit from our services, have them call before July 1st before our fee increase.

D3 Market Comments:

Global stock markets around the world have fallen more than 10% since the last week of April for several reasons. European governments were slow to acknowledge and address the reality that the Greek government would not be able to pay off their existing debt, and issue new debt, with out assistance. By the time a rescue plan for Greece was announced, the markets were already worrying that the same problem could spread to Spain and Portugal, and possibly, Italy and Ireland. The subsequent massive bailout plan announced earlier this month by European governments to support their government bond markets provided little relief to investors. **The markets are now worried about the financial health of European banks, which have significant holdings of government debt. This is causing European interest rates to rise.** Several European governments are planning big budget cuts to reduce their deficits, which bond investors are demanding if they're expected to buy more bonds. Stock investors are worried that these budget cuts may undercut the very fragile economic recovery in Europe. The lack of investor confidence in Europe's future financial and economic health has caused the value of the Euro to fall over 15% relative to the U.S. dollar.

One story that's garnering very little press, but is impacting global stock markets, is the 20% decline in the Chinese stock market. The Chinese government is taking new actions to slow the country's booming real estate market. The government is raising mortgage rates, requiring larger down payments, and prohibiting multiple property purchases. Also, an index of

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manufacturing activity in China has fallen to its lowest level in 6 months. Investors are concerned that the government will take additional measures to slow the economy. News that tensions are rising between North and South Korea are not helpful to investor confidence in Asia. **Consequently, investors are selling risky investments in most asset classes, and buyers are not yet jumping in, which has been accelerating the price declines.**

The optimists point out that this is the fifth market decline of greater than 5% since the stock market began to recover in March, 2009, which is consistent with previous market rebounds in the 1970's, 1980's and 2002. Also, the declining Euro should not significantly impact U.S. exports, since Europe represents less than 15% of U.S exports. With the stock market reducing its assessment of global growth and the dollar rising relative to other currencies, oil prices have fallen by almost 10% over the past month, and gasoline prices are starting to fall, which helps American consumers.

D3 Investment Outlook and Strategy:

Despite the falling stock market, most economists don't believe, at this point, that the problems in Europe will significantly impact the economic recovery in the U.S. We've been writing about gradual improvements in some sectors of the economy for the past few months, and those improvements are continuing, including an increase in hiring. Generally, American companies are in strong financial health, with large cash balances and lean payrolls, and have been reporting improving profits for the past 3 quarters. However, there is still considerable uncertainty regarding the policies that European governments will employ to resolve their debt crisis. Investors are closely watching the strategies being used by the Chinese government to slow their economy. A lesson we have all learned over during the past two years is that global stock markets now tend to move in the same direction. **Consequently, we expect the heightened volatility in the global stock markets, including here in the U.S, to continue throughout the summer.**

We attend conferences to discuss the latest investment and financial planning strategies with our peers to learn some new ideas on how to better serve our clients, and to listen to presentations by thought leaders on trends our industry. At the Barron's Winner Circle Conference, Peter participated in two sessions which focused on the use of "**Alternative Investments**" in client portfolios. Alternative investments are meant to improve diversification and reduce risk in client portfolios by utilizing "alternative" strategies or investment products. Many alternative investment funds use 1) derivatives, like options or futures, to opportunistically short sell various asset classes, 2) invest in hedge funds, or 3) invest in funds that buy and sell entire companies. The objective of these strategies is for the fund's value to either rise, or remain relatively stable when the stock market declines, and participate, to some degree, when the stock market rises. While some alternative funds met their objectives during the financial market crisis of 2008 and 2009, many did not. Two negatives for investing in these types of

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funds is that client funds are usually locked up with the manager for several years, and the management fees can be significantly higher than a mutual fund. During the financial crisis, the clients of many advisors learned that they could not raise cash in their portfolios by selling these products, while the values continued to fall. **At D3, many of our clients own two mutual funds which utilize an alternative strategy: the Permanent Portfolio and the PIMCO Commodity Return Fund, both of which have reasonable management fees, and can be bought or sold on any business day.** We're currently researching other funds in this category.

We're also exploring mutual funds which use alternative strategies to generate income for clients needing cash to fund their life styles, or the RMDs from their IRAs. Part of our strategy is to build client portfolios so they can generate enough income to meet their needs. By doing this, other investments won't have to be sold at potentially inopportune times to fund withdrawals. **Essentially, we are trying to increase the certainty of cash flow while minimizing the negative consequences of selling assets in declining markets.** One fund we are currently researching is the institutional share class of the Eaton Vance Global Macro Absolute Return Fund.

We have included two charts from a presentation by Chris Davis, from Davis Advisors. **He presented at the NAPFA conference that Don attended last week.** The first chart shows monthly returns of the S&P 500 index from 1929 to 2009. Two take aways from this chart are 1) that there is always a lot of day-to-day "noise" in the stock markets and 2) 62% of the time the monthly returns are positive. **The second chart shows that if you strip out the noise and look at 10-year average rolling returns for the same index from 1929 to 2009, there have been only 11 time periods** where the returns were below 5%, and only 5 where they have been negative. Now history is not necessarily a guide for the future, but this shows that if we can plan for cash flow needs and focus on the long term, our chances for success greatly improve.

Last But Not Least:

Happy Memorial Day! We at D3 are grateful to the service men and women who have kept this country free. Thank you for your confidence. Please keep us in mind if you know someone that has questions about their financial situation, retirement planning or investment needs.

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