Hallett Advisors 25 YEARS 1987–2012

Investor Insights and Outlook

VOLUME 4, ISSUE 1

JANUARY 2013

To The Cliff and Back

The Grand Canyon Skywalk is a transparent horseshoe-shaped cantilever bridge near the Colorado River on the western side of the Grand Canyon in Arizona.

Standing on the Skywalk, hanging over the edge of a cliff, 3,600 feet above the Canyon floor, looking straight-down is for some, a terrifying experience. For others, the so-called "Fiscal Cliff" became the stuff of nightmares.

The good news is the skywalk is perfectly safe (though not for the faint of heart) and the "Fiscal Cliff" is more a product of imagination than reality (though I suspect Congress will still give us more sleepless nights).

Our public's widespread financial anxiety can be partially blamed on the increasingly sensationalized "tabloid format" of our media, which continuously searches for the next great market catastrophe. As my friends at Drach Market Research Advisors noted, "The media narrative throughout 2012 largely focused on two stories: the European fiscal problems and the domestic financial challenges. The tone was increasingly negative despite markets being up from the first day of 2012 and never looking back. The S&P 500 did not see a single trading day end below its 2011 closing value."

In Fact, the S&P 500 Index advanced over 13% for 2012. This reason for celebration got lost in the noise. The continuous stream of negative media reporting is akin to an older child telling his or her younger sibling to "watch out for monsters hiding under your bed." No wonder the youngster suffers from nightmares!

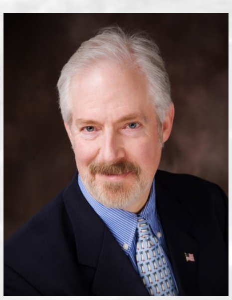
Reasons for Optimism

- We have some clarity regarding the federal income tax rates. Are we done with this issue? Certainly not, yet your new collective tax rates still remain at relatively low historic levels. Just for fun, check out the highest marginal tax rates applied to incomes during the Eisenhower and Kennedy presidencies. Talk about the "good old days". (Call me if you need help with the answer).
- Our economy continues to slowly recover from the Great Recession. Since the March 2009 lows, all of the major market averages have more than doubled in value. The popularly quoted "Dow Jones Index" has rallied more than 6,550 points.

Continued on page 4

Inside this issue:

Dividend Income During Downturns	2
Chasing Performance	3
Don't Forget to Raise Your IRA Contributions	3
To The Cliff and Back (continued)	4
Risk, Not Volatility, Is The Real Enemy	4



Advisor Corner

Thank you for the opportunity to serve as your advisor.

Hallett Advisors
Plan Well • Live Well

James D. Hallett, MSFP CFP AIFA
jim@hallettadvisors.us
360-457-6000

Dividend Income During Downturns

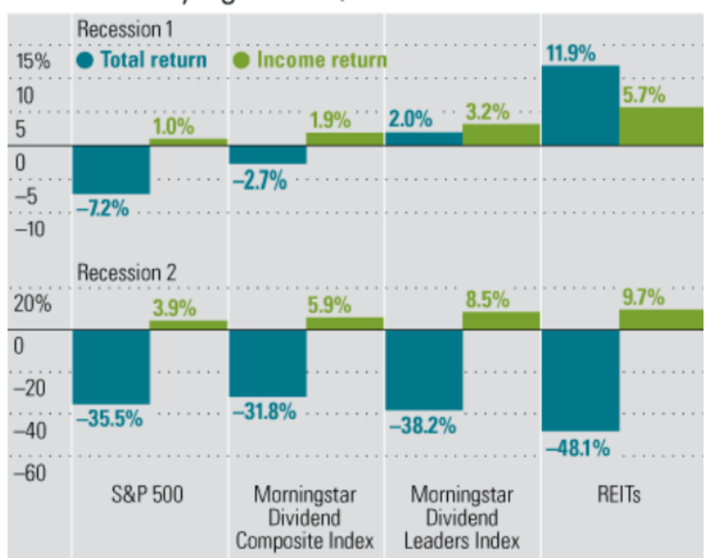
During a recession, the stock market can lose significant value. This could have a large impact on portfolio returns. Predicting the duration and extent of recessionary periods is almost impossible. During such times, income-producing investments such as dividend -paying stocks and REITs may soften losses, particularly when investors incur negative returns. This means that, if and when dividends are paid out, they have the potential to act as a cushion and are positive whether stock returns are positive or negative.

The image compares the total return and income return for the S&P 500 index, Dividend Composite index, Dividend Leaders index, and REITs for the past two recessions in 2001 and 2007. As seen in the image, dividend-paying stocks and REITs produced higher income returns relative to the S&P 500 over the given time periods (however, keep in mind that REITs are far more risky than their typical common stock counterparts). Stocks that pay dividends may serve as an income source while also providing investors with exposure to the growth potential of the stock market.

Dividends are not guaranteed and are paid at the discretion of the stock-issuing company. Diversification does not eliminate the risk of experiencing investment losses. Government bonds are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest, while stocks and REITs are not guaranteed and have been more volatile than the other asset classes. REITs are subject to certain risks, such as risks associated with general and local economic conditions, interest rate fluctuation, credit risks, liquidity risks and corporate structure. REITs must distribute at least 90% of taxable income annually to shareholders.

The Morningstar Dividend Composite Index captures the performance of all stocks in the U.S. Market Index that have a consistent record of dividend payment and have the ability to sustain their dividend payment. Stocks in the index are weighted in proportion to the total pool of dividends available to investors. The Morningstar Dividend Leaders Index captures the performance of the 100 highest yielding stocks that have a consistent record of dividend payment and have the ability to sustain their dividend payments. Stocks in the index are weighted in proportion to the total pool of dividends available to investors. Recession data is from National Bureau of Economic Research (NBER) and defined by the periods March 2001–November 2001 and December 2007–June 2009. NBER does not define a recession in terms of two consecutive quarters of decline in real GDP. Rather, a recession is a recurring period of decline in total output, income, employment, and trade usually lasting from six months to a year and marked by widespread contractions in many sectors of the economy.

Returns of the S&P 500®, Dividend-Paying Stocks, and REITs



Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. S&P 500 is represented by the Standard & Poor's 500®, which is an unmanaged group of securities and considered to be representative of the stock market in general. REITs are represented by the FTSE NAREIT All Equity REIT Index®. Morningstar Dividend Composite is represented by the Morningstar Dividend Composite Index, and Morningstar Dividend Leaders by the Morningstar Dividend Leaders Index. Income return and total return are represented by the compound annual return over the given time period.

Chasing Performance

Investors often endure poor timing and planning as many chase past performance. They buy into funds that are performing well and initiate a selling spree following a decline. This becomes evident when evaluating a fund's total return compared with the investor return. Overall, the investor return translates to the average investor's experience as measured by the timing decisions of all investors in the fund.

The image illustrates the investor return relative to the total return for a given fund. Over the short term, both the total and investor returns were positive and relatively similar. Over a 10-year period, however, total return greatly exceeded investor return. Investors who attempted to time the market ran the risk of missing periods of exceptional returns.

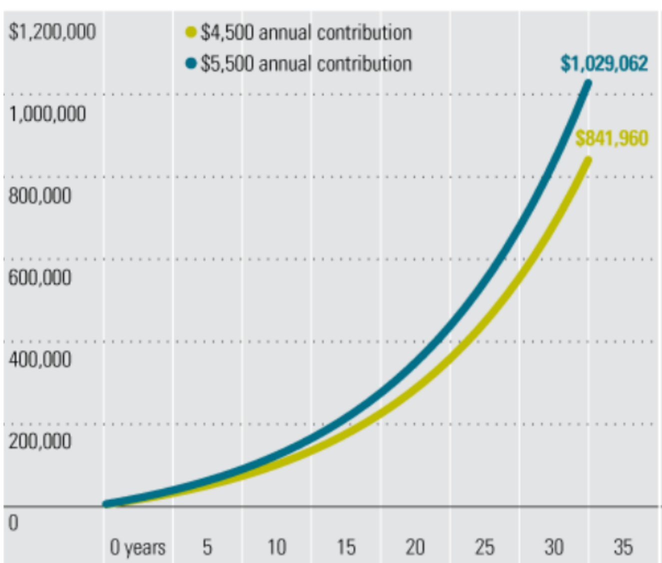
By staying focused on your financial plan rather than "The Market" you can enhance your investment return potential.

Comparison of a Fund's Return Performance Over Time

Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. Returns and principal invested in stocks are not guaranteed. Morningstar investor returns measure how the typical investor in that fund fared over time, incorporating the impact of cash inflows and outflows from purchases and sales. It is not one specific investor's experience, but rather a measure of the return earned collectively by all the investors in the fund. Total return measures the percentage change in price for a fund, assuming the investor buys and holds the fund over the time period, reinvests distributions, and does not make any additional purchases or sales. Investor returns are not a substitute for total returns but can be used in combination with them. Data as of October 2012.

Source: The fund illustrated in this example was selected from Morningstar's open-end database.

Hypothetical Growth of Annual IRA Contribution



This is for illustrative purposes only and not indicative of any investment. Funds in a regular IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax-free as money withdrawn is not taxed. Penalties may apply for withdrawals prior to the age of 59 1/2.

Don't Forget to Raise Your IRA Contribution

In 2013, contribution limits for both traditional and Roth IRAs (individual retirement accounts) will increase to $5,500 a year for those 49 years of age or younger. If you are 50 or older, the maximum contribution is $6,500. This limit can be split between a traditional and a Roth IRA. These annual contribution limits are imposed by the Federal Government.

The graph shows both a $4,500 and $5,500 annual contribution growing at a hypothetical 8% annual return. Notice the dramatic impact on the ending value of the portfolio. This may be a great time to reevaluate your financial situation and increase your annual investment to your IRA. Even if you are unable to max out your contribution, any increase you can afford may help you reach your savings goals more easily in the long run.

Call Jim to discuss whether a traditional or Roth IRA makes sense for you.

To The Cliff and Back (continued)

Economist Brian Wesbury, likens our economy to a trusty plow horse; it isn't as glamorous or fast as a thoroughbred, it simply plods forward cultivating our field setting the stage for more productive growth.

Over the next few weeks and months there will be more hand-wringing and consternation about the debt ceiling, entitlement funding and tax reform. I'm not suggesting the answers are easy. In fact, we should expect to see more market volatility as we sort things out.

Nevertheless, perhaps Winston Churchill got it right when he said, "Americans can always be counted on to do the right thing…after they have exhausted all other possibilities."

Here's to a peace-filled and prosperous 2013!

Risk, Not Volatility, Is The Real Enemy

We can help you objectively assess your comfort level.

What would you do if your investments lost 10% in a single day? A) Add more money to my account. B) Hold steady with what I've got. C) Yank my money; I wouldn't be able to stand any more losses.

If you buy the right investments but sell them at the wrong time because you can't handle the price fluctuations, you may have been better off avoiding those investments in the first place. Most people are poor judges of their own risk tolerance, feeling more risk-resilient in up markets and more risk-averse after market losses. However, focusing on your response to short-term losses inappropriately confuses risk and volatility. Understanding the difference between the two and focusing on the former is a potential way to make sure you reach your financial goals.

Volatility encompasses the changes in the price of a security, a portfolio, or a market segment, both on the upside and downside, during a short time period like a day, a month, or a year. Risk, by contrast, is the chance that you won't be able to meet your financial goals or that you'll have to recalibrate your goals because your investment comes up short. So how can investors focus on risk while putting volatility in its place? The first step is to know that volatility is inevitable, and if you have a long enough time horizon, you may be able to harness it for your own benefit. Diversifying your portfolio among different asset classes can also help mute the volatility. It helps to articulate your real risks: your financial goals and the possibility of falling short of them. Finally, plan to keep money you need for near-term expenses out of the volatility mix altogether.

Investing in securities always involves risk of loss. Diversification does not eliminate the risk of experiencing investment losses.

Hallett Advisors
Plan Well • Live Well

James D. Hallett, MSFP, CFP®, ChFC, CLU, CDFA™, AIFA®

321 E First Street

P.O. Box 3050

Port Angeles, WA 98362

RiA STANDS FOR YOU.

Discover the difference with a Registered Investment Advisor.

www.HallettAdvisors.us

jim@hallettadvisors.us