February 4, 2015

Best House on a Troubled Block – Alex II

The United States emerged from 2014 as the best house on a troubled block. Civil war in Ukraine, a slowing Chinese economy, a stagnant Europe teetering on deflation, a potential economic meltdown in Russia triggered by tumbling oil prices – it all made a slowly improving situation at home look even brighter by comparison.

In 2014 the United States was stronger than it has been in years. The labor and housing markets improved, and corporate profits were solid. Congress managed to avert another government shutdown, and so far the Ebola threat had little impact domestically. All in all, it was a Goldilocks economy – not too hot, which could have brought higher interest rates from the Federal Reserve, and not too cold, thereby letting the Federal Reserve end the bond buying program known as QE (Quantitative Easing) without upsetting the bond and stock markets.

U.S. large-cap stocks outperformed U.S. small-cap stocks in 2014. I don't believe that will continue in 2015. The U.S. dollar has been so strong that earnings by our large multi-national companies appear to have been weakened. This has the potential to benefit smaller U.S. companies that have smaller percentages of foreign exports.

The domestic stock indexes continued to outperform their overseas peers. During the past five years the S&P 500 had an annualized return of about 15.45% vs. the MSCI EAFE (international developed stocks) return of 5.71%. I don't believe this trend will continue over the next five years. If the ECB is successful in stimulating the European economy, or if our domestic markets become too rich with high valuations, investors may seek better values overseas.

2014 felt like the mid to late 1990's. In simple terms, it was a year to buy just U.S. large-cap stocks and high quality bonds. Non-U.S. equities lost money and small-cap stocks lagged on the upside, while high-yield bonds, international bonds and alternatives all lagged U.S. large-cap stocks and high-quality bonds.

Morningstar, an independent investment research firm, has 5 Target Risk Indexes. Its Conservative Index has 18% in stocks and most of the rest in bonds and cash, and its 2014 return was 3.4%. Its Aggressive Target Index has 91% in stocks and the rest in bonds and commodities, and its 2014 return was 5.2%. So the difference in returns between these two indices for 2014 was very little, only 1.8% between its least and most aggressive Target Indexes. While a diversified portfolio won't be the best investment in any given year, it should perform well most of the time to help investors reach their goals with a more balanced approach than the higher highs and lower lows that come with lack of diversification.

The bond market gave us a surprise in that the 10-year U.S. Treasury Bond yield fell to around 2.1% from a January 2014 yield of about 3%. That fall in rates gave the Barclays US Agg Bond Index a return of 6% for 2014. Currently the 10-year Treasury is yielding about 1.825%. Could this yield go lower? Yes it could if demand for them increases. Equivalent government bonds in Europe and Japan are near 0%, yes, zero. Consequently, investors looking for yield may continue to shop at the "best house on a troubled block", namely the U.S. Treasury.

Has anything changed that might reverse the bull market in U.S. bonds? Yes, Europe has finally started its own version of QE this year. Mario Draghi, President of the European Central Bank (ECB), announced the launch of its private and public bond-buying program on January 22. That news along with a stronger U.S. economy might prompt the U.S. Federal Reserve to start raising short-term interest rates. If short interest rates are increased, U.S. bonds will be hard pressed to give us the returns we have experienced over the past five years.

What should a bond investor do to protect their bond portfolios? We have made changes to our bond holdings in our model portfolios. In August 2013, we changed a large percentage of our traditional bond holdings to shorter-term maturity bonds. So far those changes did not make a huge difference from what we previously held, but I believe that when interest rates rise, those changes will give us better results than where we were positioned.

2015 Outlook – Alex II

Alex and I never make market predictions like guessing the year-end value the S&P 500. *The Divine Comedy*, written by Dante in the 14th century, said: “Those who attempt to divine the future should have their heads twisted around and be forced to walk backwards for eternity.” Indeed, the past few weeks on the internet you are likely to have seen many headlines screaming for your attention with flashy titles like “Top Analyst Gives 2015 Predictions.”

As one Wall Street pundit stated, “Tapping into our collective desire to believe that the markets can truly be figured out by someone, these reports are like reading the investment equivalent of a person’s horoscope.” We continue to believe that investors should invest in diversified portfolios of high-quality stocks and bonds. The percentage of stocks to bonds and cash should be determined by your risk tolerance and your financial goals and timelines. We also believe your should rebalance your accounts on a regular basis, but at least every 12 to 18 months.

We have a great deal of respect for our broker dealer, Raymond James Financial. Chief Investment Strategist Jeffrey Saut recently made these observations: Though we’ve experienced 38 months of upside without a 10% correction (we’ve come close, but haven’t quite hit the mark), in a typical market cycle, we’d see a pullback of that magnitude every 18 months or so. This particular rally is “long in the tooth” by his reckoning, but isn’t unprecedented. His outlook for 2015 suggests a difficult period in the first quarter, though in a longer-term bull market any pullback could provide an opportunity for rebalancing or starting new positions. Taking the longer view, however, Saut believes this secular bull market has years left to run. (Source: http://raymondjames.com/pointofview/article.aspx?a=2172&l=2015_may_look_a_lot_like_2014)

Alex and I look forward to seeing you in 2015 and will continue to work hard to earn your confidence and respect.

Below are the calendar year 2014 returns and YTD as of January 30, 2015:

Asset Class	Index / Category	2014 Returns	YTD as of 1/30/2015
Cash & Cash Alternatives	Average 1-year CD rate	0.27% (annual yield)	0.28% (annual yield)
U.S. Govt & Corp. Bonds	Barclays US Agg Bond TR Index	6.0	2.1
World Bonds	Morningstar World Bond Category	1.7	0.3
U.S. Large-cap Stocks	S&P 500 TR Index	13.7	-3.0
U.S. Small-cap Stocks	Russell 2000 TR Index	4.9	-3.2
International Developed Stocks	MSCI EAFE NR USD	-4.9	0.5
Emerging Market Stocks	MSCI Emerging Markets PR USD	-2.2	0.6
World Allocation	Morningstar World Allocation Category	1.5	0.0
Diversified Commodities	Morningstar Long-Only Commodity Index	-24.4	-5.0
Multi-Alternatives	Morningstar Multi-Alternative Category	1.8	0.3

Source: Morningstar.com, Bankrate.com

- The S&P 500 is an unmanaged index of 500 widely held stocks that's generally considered representative of the U.S. stock market.
- The Russell 2000 index is an unmanaged index of small cap securities which generally involve greater risks.
- MSCI EAFE Index is an index, with dividends reinvested, representative of the securities markets of 20 developed countries in Europe, Australasia and the Far East.
- MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets.
- Morningstar World-allocation Category includes funds that seek to provide both capital appreciation and income by investing in three major areas: stocks, bonds, and cash. While these portfolios do explore the whole world, most of them focus on the U.S., Canada, Japan, and the larger markets in Europe. It is rare for such portfolios to invest more than 10% of their assets in emerging markets. These portfolios typically have at least 10% of assets in bonds, less than 70% of assets in stocks, and at least 40% of assets in non-U.S. stocks or bonds.
- Morningstar World Bond Category includes funds that invest at least 40% of bonds in foreign markets.
- Barclay's Capital U.S. Aggregate Bond index covers the U.S. investment grade-fixed rate bond market and consists of components for government and corporate, mortgage pass-through and asset-backed securities. Must be rated investment grade or higher by at least two of the following: Moody's, S&P, or Fitch, have at least one year left to maturity and an outstanding par value of at least $250 million. Security representation would be those that are SEC-registered, taxable, dollar denominated, non-convertible and fixed rate.
- Morningstar Long-Only Commodity Index is a fully collateralized commodity futures index that is long all eligible commodities.
- Morningstar Multi-Alternative Category includes both funds with static allocations to alternative strategies and funds tactically allocating among alternative strategies and asset classes. Average gross short exposures are greater than 20%.
- Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Past performance does not guarantee future results.

The information contained in this report does not purport to be a complete description of the securities, markets, or developments referred to in this material. The information has been obtained from sources considered to be reliable, but we do not guarantee that the foregoing material is accurate or complete. Any opinions are those of Alex Petrovic and Alex Petrovic III and not necessarily those of RJFS or Raymond James. Expressions of opinion are as of this date and are subject to change without notice. Any information is not a complete summary or statement of all available data necessary for making an investment decision and does not constitute a recommendation. You should consider any tax or legal manners with the appropriate professional. Past performance may not be indicative of future results. There is no guarantee that any forecasts made will come to pass. Diversification does not ensure a profit or guarantee against a loss.

2014 Tax Season Update – RJ 1099 Mailing Schedule

- February 17 Mailing of original Form 1099s
- March 2 Begin mailing delayed and amended Form 1099s
- March 16 Final mailing of any remaining delayed original Form 1099s

Note: We will notify Raymond James clients who will receive delayed 1099s in mid-February.

Please note the exceptions immediately below:

Delayed Form 1099s

In an effort to capture delayed data on original Form 1099s, the IRS allows us to extend the mailing date until March 16, 2014, for clients who hold particular investments or who have had specific taxable events occur.

Amended Form 1099s

Even after delaying your Form 1099, please be aware that adjustments to your Form 1099 are still possible. Raymond James is required by the IRS to produce an amended Form 1099 if notice of such an adjustment is received after the original Form 1099 has been produced. There is no cutoff or deadline for amended Form 1099 statements.

What can you do?

We will notify Raymond James' clients who will receive delayed 1099s in mid-February. If yours is delayed, your 1099 will be mailed between March 2 – 16, and you might consider talking to your tax advisor about whether it makes sense to file an extension with the IRS to give you additional time to file your tax return. We apologize in advance for this inconvenience. We know some of our clients have experienced delayed 1099s over the years, but unfortunately there is little we can do.

If you receive an amended Form 1099 after you have already filed your tax return, you should consult with your tax advisor about the requirements to re-file based on your individual tax circumstances. Additional information can be found at http://www.raymondjames.com/taxreporting.htm.

Please note, changes in tax laws or regulations may occur at any time and could substantially impact your situation. Raymond James financial advisors do not render advice on tax or legal matters. You should discuss any tax or legal matters with the appropriate professional.

2015 Five Star Wealth Manager^{sm} Award!

In the January issues of KC Magazine and KC Business, Alex Petrovic was recognized as a 2015 Five Star Wealth Manager^{sm}. For the 2015 award, there were 201 recipients out of the 1,572 award candidates considered in the Kansas City metro area.

This is the third time in four years (2012, 2014 and 2015) he has received this award, and he appreciates everyone who took part in the survey.

We want to extend a heartfelt thank you to all of our clients for your loyalty and confidence throughout the years. If you believe we provided you with excellent advice and service over the years, one of the best compliments you can give is to pass our information along to anyone you know who needs financial advice.

The award is bestowed by an independent third party organization not affiliated with Raymond James. The award based on advisor being credentialed as an investment advisory representative (IAR), a FINRA registered representative, a CPA or a licensed attorney, actively employed in the financial services industry for five years, favorable regulatory and complaint history review, fulfillment of firm review based on internal firm standards, and accepting new clients. For additional evaluation criteria considered, thttp://www.fivestarprofessional.com/awards/2014_wealth_manager_research_overview.php

89.3 FM KCUR's *Money Therapy* – Alex II

Last Monday I was on 89.3 FM KCUR's Central Standard show, *Money Therapy*. The show's name was changed to *Money Therapy* from *Ca$h Money Crew* to better reflect our desire to talk about money from a more personal viewpoint. We have now completed 37 since January 2012.

I am one of four CERTIFIED FINANCIAL PLANNER™ professionals from the Greater Kansas City Financial Planning Association who are on the show. The UMKC studio only seats three guests, so one of us skips a show now and then to even out our appearances. Our last show was titled "A Year in Review". Here is a link to the show for those interested. http://kcur.org/post/money-therapy-year-review.

Alex at the mic.

Sometimes I get a little nervous preparing for each show. Last week my wife Peggy sent me this text just before show time, "Good luck on the radio. They won't see the fear in your eyes." Her text made me laugh and settled my nerves enough not to say anything too stupid or make any colossal mistakes on air!

Inside & Outside of PFS – Alex III

Wow, one month into the New Year has already past. Feels like New Year's Eve was just last weekend! We hope you and your family enjoyed the holidays and are still keeping your New Year's resolutions! ☺

Since our last newsletter, our big KC sports teams didn't quite deliver for us, especially given our high expectations at the time. Our Chiefs lost four of the last six games and missed the playoffs as a result.

Of course we are painfully aware the Royals were 90 feet away from tying the game seven. My father was fortunate enough to attend two World Series games. Unfortunately they were games one and seven, both of which we lost primarily due to Madison Bumgarner's phenomenal pitching. Over three World Series, he has the lowest ERA (earned run average) of 0.25 of any pitcher in the history of baseball who threw a minimum of 25 World Series innings. (Source: USA Today) I know this doesn't make losing feel any better, but it took a historic recording-breaking performance to bring us down.

Sporting KC starts its season in March and the Royals in April, so let's hope new seasons, new players and renewed hope can heal our 2014 wounds.

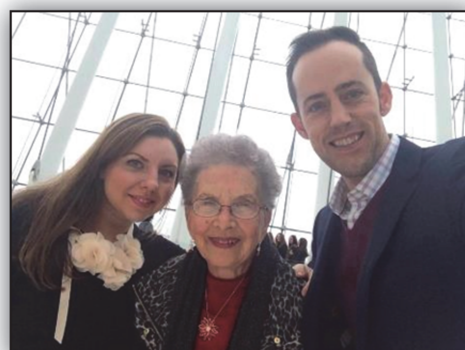
Last November my father attended the Financial Planning Association's (FPA) Chapter Leaders Conference in Denver, Colorado. This conference is conducted every year for directors of all local chapters of the FPA. He is serving his second year as a board member of the Greater Kansas City FPA and as the director of the Public Relations Committee. The Greater Kansas City FPA chapter currently has 402 members, and they meet every month at the Doubletree Hotel in Overland Park.

At the Denver conference, he really enjoyed meeting other public relations directors from about 30 other local chapters in the United States. Their focus was how to better serve their local chapters' public relations efforts. They learned they need to connect with three "publics": the local and national media, the local consumer and their local chapters' members. The information from the conference was extremely useful for his committee, and he is excited to implement some of the tactics he learned at the conference to promote his FPA chapter's efforts in the Greater Kansas City area.

We had a great Thanksgiving around the Petrovic household! On my mother's side of the family, my Cousin Sasika came in from Atlanta, Georgia, and my Aunt Debbie and Cousin Stephen visited from St. Petersburg, Florida. Debbie and Stephen were supposed to attend Thanksgiving in 2013, but on the way to the airport that year they rear-ended a lady in the rain. She was driving backwards on the off ramp, back toward the freeway. Crazy! Thankfully no one was severely injured, but they did sustain injuries and were not able to come in 2013.

We had a great week while they were here. We walked and shopped on the Plaza, had dinner at the newly reopened JJ's Resturant, enjoyed some after dinner drinks at Hotel Sorella on the Plaza and went to see a neo-Soul music group perform in Westport. As always we wished they could have stayed longer, but we made the most of our time together!

On December 7, my wife Dasha and I took my Grandmother Doris to see the Kansas City Ballet Company perform *The Nutcracker* at the Kauffman Center for the Performing Arts. My grandmother is hard to buy gifts for (though she says the same thing about us), so we decided a couple of years ago to give her event-based gifts because we like spending time with her, so this was one of her birthday gifts from a few month earlier.



Dasha, Grandma Doris and Alex III in the Brandmeyer Great Hall before The Nutcracker. This may be my grandma's first selfie! ☺

Before the performance, we went to brunch at Baked in Kansas City in Westport. We enjoyed the piano music, excellent food and copious amounts of java. We left Baked fully caffeinated and prepared for *The Nutcracker* with happy tummies!

As we had hoped, the dancers' performance, Tchaikovsky's music and the beautiful venue of the Muriel Kauffman Theatre combined for a pleasurable afternoon! We enjoyed taking Grandma Doris out for the afternoon, and later she repaid us by giving us a nutcracker doll for Christmas. How very thoughtful, Grandma!

My nephew Aiden and my brother John in front of a very bright Christmas tree after seeing A Christmas Carol.

The evening of December 11, several of us attended the Kansas City Repertory Theatre's performance of "A Christmas Carol." For the past few years, our family has attended this Charles Dickens' classic. This year my brother John decided to take Aiden for the first time. The ghost of Christmas Yet to Come has frightened many a child, but Aiden did a good job. Hopefully, it also helped scare him straight, so he would stay on Santa's Nice List for a couple more weeks.

Our family had a great Christmas! On both sides of my family, we were happy to have out-of-town family celebrate with us in KC. My Uncle Bill, my mother's brother, and his wife Beatriz came in from St. Petersburg, Florida. On my father's side, my Aunt Anastasia traveled from Bend, Oregon. My Aunt Teresa and her husband David came in from Washington D.C. Teresa's three children, Henry, Sophie and Maggie, journeyed from New York City, Washington D.C. and Los Angeles, respectively. It was the first time in many years that her children were back in KC since leaving for college, and it was wonderful to have them back!

Per Petrovic tradition, we spent Christmas Eve at Grandpa Alex's Sugar Creek home. We did our best to break the fire code with the number of attendees this year, and a couple more babies were added to the mix to liven up the party. Given the number of family members, several years ago we switched to a 'white elephant' gift exchange. Usually the gifts are well considered, and occasionally there have been some comical arguments regarding a lack of rule clarity.

On both sides of the family, Christmas Day was full of laughs, wonderful food and relaxation. Oh, and there was the occasional fight amongst nephews for the 'cool toy'. Who would have thought the cash register my mother gave Jack would have caused the ruckus it did. Good job Mom! ☺ Boys will be boys!

Jackson and Aiden starting the Christmas countdown with the help of Santa's cotton-ball beard.

For the remainder of the holidays, we enjoyed spending extra time with our visiting relatives. The KC cousins were able to hang out with Henry, Sophie and Maggie a few times more before they left for the coasts, and Uncle Bill and Aunt Beatriz from Florida came to Dasha and I's small New Year's Eve party. We are thankful to have such a kind, loving family and to be able to share the holidays with them!

Since the holidays ended, as have the excessive amounts of food and goodies, life has returned to normal, which is good since most of my pants do not have elastic waistbands. One of my New Year's resolutions is to exercise more regularly. I made some progress in 2014 after overcoming an iliotibial (IT) band injury from 2013 because of improper running technique. The IT band is a tough group of fibers that run along the outside of the thigh. This year I plan to exercise more via running (properly), yoga and golf. Yes, in my humble opinion golf counts as exercise as long as you walk the course. Exercising more and golfing are also amongst my father's resolutions. Like father, like son, I guess!

My father and I wish you good health and happy surprises in 2015!

Alex Petrovic, CFP®
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P.S. In observance of President's Day, the financial markets and our office will be closed on Monday, February 16, 2015.