



Qtr Notes

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Quotes:

Low growth contributes to political polarization, and that not only limits the tailwinds to our economy but also creates headwinds.

*Mohamed El-Erian,
CEO and co-CIO of Pimco*

These gains were achieved despite substantial fiscal headwinds, which are likely slowing economic growth this year by a percentage point or more. ... Federal fiscal policy continues to be an important restraint on growth and a source of downside risk.

*Ben Bernanke,
Federal Reserve Chairman*

Kamikaze missions rarely turn out well, least of all for the pilots.

Wall Street Journal

"Quantitative easing" sounds like what I do when I put on tight pants.

Paula Poundstone

Political Risks and Shutdown Impede Ongoing Recovery

The third quarter of 2013 ended with many unanswered questions, a spike in volatility, and a sobering reminder of the political risks in Washington. Yet despite the headlines, this has been a year of economic healing and market appreciation. Over the last year, home prices have increased by 12%, demand for housing has accelerated, and residential investment from household goods to new home construction is up. The auto sector is enjoying robust sales and overall corporate profits are hitting all-time highs. JP Morgan's analysts observe that improving housing and stock prices have pushed household net worth up by nearly \$1.7 trillion. Considering that 70% of our national GDP is derived from consumer spending, these measures of the improvement in household wealth are critically important. Despite the drag of political friction, the US economy looks positioned to continue expanding in the fourth quarter and beyond.

2013 marks the first year since the fiscal crisis five years ago that the US budget deficit has been less than a trillion dollars. Though total indebtedness has continued to grow, the deficit has declined in each of the last four years as employment inches up and the economy slowly recovers. In 2013, the deficit will fall by roughly 40%, primarily because of a combination of higher taxes and reduced government spending (the infamous sequester). It speaks to the strength of the US economy that our economic recovery was able to continue despite these austerity measures, a feat Europe has not achieved. But the absence of effective fiscal policy has been a drag on recovery, and continues to hamper the climb back to true prosperity.

Under normal operating conditions, the government has two levers at its disposal to deal with the economy: fiscal policy and monetary policy. The Federal Reserve handles monetary policy by controlling the money supply and interest rates. Congress directs fiscal policy

Index	9/30/2013	YTD
Dow Industrials	15,129.67	15.5%
S&P 500 Index	1,681.55	17.9%
Russell 2000	1,073.79	26.4%
MSCI EAFE	1,818.23	13.4%
Global Bond Index	455.89	-2.2%
10-Year Treasury yld	2.61%	

through its spending and taxing authority. Fed Chairman Bernanke has been quite vocal about his frustration at trying to steer the ship with only one lever.

The markets reacted favorably when Lawrence Summers withdrew his name from consideration as the new Fed Chair, opening the way for the less controversial Janet Yellen, who is expected to continue the Fed's current policies. At its mid-September meeting, concerned that economic recovery was still too fragile, the Fed delayed tapering its Quantitative Easing program. We don't know when the Federal Reserve will ultimately begin tapering, but the political situation in Washington is a major dark cloud hanging over the next stage of recovery. With 800,000 government employees furloughed as a result of the shutdown, Congress' failure has already created another additional obstacle to recovery.

Overseas, Europe appears to be coming out of recession at last. Most of the growth continues to be in France and Germany, while Spain, Portugal, Italy, and Greece are still contracting. Unemployment still plagues the region and governments continue to employ austerity measures, a serious drain on short-term economic growth. On the positive side, consumer and business confidence has picked up and capital is returning to the region. Questions over the long-term stability of the euro remain, but with recent economic improvement and the strong support of the European Central Bank, there remains a strong case for owning European companies.

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Safety in Numbers: The Affordable Care Act

October 1 is the first key date for provisions of the Affordable Care Act. The ACA is a complex and controversial topic, and a great deal of misinformation has been disseminated about it, making informed decisions a challenge. Comprehensive information and assistance can be found at the website healthcare.gov.

Inevitably, the legislation has already given rise to a new wave of scams and fraudulent schemes, from variations on identity theft to sales of fake ID cards and bogus insurance plans. You are not required to purchase an ID card, and any unsolicited phone calls, faxes, or emails should be viewed with skepticism.

Wire Fraud Safeguards

Fraudulent wire requests continue to be a major concern for us at Firestone. We will continue to require verification for all requests. If we receive any wire request by email on any account, we will not be able to act on it without calling you and speaking to you personally.

Risks to Recovery

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In other recent international developments, saber-rattling gave way to diplomacy both in the reduction of an immediate threat of military action regarding Syria and in the first official direct US contact with Iran's head of state in more than 30 years.

At midnight October 1, the government went into partial shutdown, with this impasse likely to be followed by yet another tug-of-war over the nation's debt ceiling. The Affordable Care Act – "ObamaCare" – has drawn most of the political fire, but ultimately, everything is a budget issue. All Americans are concerned about addressing long-term budget problems and entitlement reform, and defining what constitutes a moral and affordable health care system. We do not expect Congress to agree about all of these issues, but we need Congress to begin to work in a civil manner and a reasonable timeframe.

Social Security Strategies

Retirement security used to be a three-legged stool: workers had pensions and personal savings, and everyone had Social Security. For most people today, that stool is teetering on two uneven legs.

Personal savings are often far short of goals and pension plans are nearly extinct. Employees are forced to take the risk of managing their own 401(k) accounts. At the same time, optimizing Social Security benefits has become more complex. Couples are approaching retirement with the work histories of two breadwinners on the one hand, and longer life expectancies on the other. Without the guarantees of employer pensions, planning your Social Security strategy has become essential.

The decisions on how and when to take benefits will have a profound effect on your retirement income. The key elements in Social Security planning include your past and current earnings record, what spousal benefits are available (if applicable), your "Full Retirement Age" (FRA), and the timing for you and your spouse to claim benefits. For couples, a new emphasis has fallen on the "two-life benefit" – that is, maximizing the lifetime total benefits of both spouses.

Social Security benefit strategy is a numbers game. The government actuaries have calculated the odds of how long you will live, adjusting benefits according to when you start taking them. Most workers are entitled to claim benefits at age 62, but

at a steep cost – made even steeper if you're still working and earning income.

Waiting to claim benefits can be richly rewarding. For every year benefits are deferred, your monthly check will increase by a guaranteed 8%. That's a pretty sweet deal in today's 2% inflation climate. In simple numbers, if your full benefit is projected to be \$2000 per month, claiming at 62 cuts your monthly benefit by 25% to \$1500, while waiting till 70 yields a 32% increase in benefit to \$2640.

Spousal benefits need to be factored into the calculation, especially when one spouse has the potential to draw a much higher full benefit than the other. Commit to making a full analysis of your options prior to claiming any benefits: possible strategies include file and suspend, in which the higher earner files for benefits but then suspends the claim, while the lower earner draws a spousal benefit. We encourage you to discuss this with us so we can help you analyze your situation and plan your strategy.

The Social Security Administration no longer sends individual statements to workers. You will need to visit their website at socialsecurity.gov, where you can create a secure login and see your statement at any time. Their site also offers detailed information on your options (including the possible complications of divorce and/or widowhood), calculators for estimating benefits, and instructions on how to file.

The SSA can also be contacted via phone at 800-772-1213. The agency personnel can assist and advise you on your plans, and are knowledgeable, helpful, and effective.

Post-DOMA: A Shifting Landscape

Three months after the Supreme Court voided the Defense of Marriage Act, the financial landscape for affected couples continues to change. The IRS and the Treasury Department have implemented policy changes allowing all married couples in all states to file jointly, but each settled topic raises a new set of questions. Will the IRS allow for amended returns to reflect the changes in legal status? Will other benefits become retroactive? In addition, some federal programs that are administered at the state level, including Social Security, are still in flux. These questions remain unsettled, and we continue to follow the situation as it develops.