

INVESTMENT UPDATE

THE MUNCY BANK & TRUST COMPANY

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Points of interest:

- Big U.S. stock returns have averaged only 0.4 percent per year since 2000.
- The long term average for big stocks is 9.9 percent annually.
- Diversified portfolios, however, delivered 7 percent annual returns in the same period.
- Bank savings rates are down to 0.2 percent.

IT HAS BEEN A DISAPPOINTING 11 YEARS FOR INVESTORS AND SAVERS

Do you feel like you just aren't making money on your investments and savings the way you used to? You aren't alone and your perceptions are not off: since the start of this century, returns on most investment and savings vehicles have been well below their long-term averages, and markedly lower than they were from 1980 through 1999.

Investors and savers have generally earned subpar returns since the first day of 2000 and, with world economic activity chugging along at a glacial pace, it is hard to see a pickup coming in the near term.

The outlook for savers is especially bad: The Federal Reserve's recent pledge to keep short-term rates at nearly zero for the next two years will probably mean that there will be no pickup in rates paid on bank savings, money market funds, or U.S. Treasury securities.

Hope for investors

However, investors with diversified portfolios have plenty to hope for: we have seen slow periods like this in the past and they have always been followed by years with above-average returns.

Investors who own big stocks in the United States or the developed world have had little to cheer about. From the beginning of 2000 through the end of 2010 the Standard & Poor's 500 Stocks Average gained just 0.4% per year on



Investors have not had an easy time of it since the new century began, while savers are earning dismal interest rates.

a compounded basis, compared to its long term average (since 1926) of 9.9 percent per year.

The S&P 500 did even better from 1980 through 1999, when it gained 17.9 percent per year.

The last decade's results are just a hair better than the Great Depression: the S&P 500 lost 1 percent per year from 1930 through 1940.

But each decade from 1940 through 1999 offered positive returns on stocks, until this century, which has suffered so far through two major bear markets (just like the market did in the Depres-

sion, when stocks fell from 1929 through 1932 and again from 1937 through 1942).

Diversification works

The market's behavior since the Depression offers hope to today's investors that stock returns could pick up over the next decade.

Diversified investors can also take heart in the knowledge that they probably did better than the S&P 500 over the last 11 years and have a good chance of doing well going forward. After all, there have been winners since 2000: small U.S. stocks

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INTEREST RATES ON SAVINGS ARE LOWER THAN THE INFLATION RATE

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gained 7.4 percent a year, real estate investment trusts 12.1 percent per year, commodities 8 percent per year, and emerging markets stocks 10.9 percent per year.

A model portfolio tracked by Dimensional Fund Advisors that invests 60 percent in large and small domestic, international and emerging markets stocks, REITs, and 40 percent in short term bonds, returned 7 percent per year from 2000 to 2010.

Unhappy savers

Those who like to sock their money away in the bank probably will not enjoy any return over the next few years. In fact, they may end up losing purchasing power.

Average rates in savings accounts and certificates of deposit currently are less than 0.2 percent per year. The Fed says that's where they will stay into 2013.

Meanwhile, consumer inflation averaged 3.8 percent in the 12 months ended in August. Savers actually lost money by keeping it in the



Savers are earning pennies these days.

bank. To add insult to injury, many paid income taxes on their meager interest.

COLLEGE COSTS ARE GETTING FAMILIES DOWN

The most successful college savers seem to be those using state-sponsored 529 savings plans, found a survey by the College Savings Foundation.

But even those who have built up respectable sums in their savings plans say they are worried "that their best efforts will not keep them and their children out of long term debt," said Roger Michaud, chair of the College Savings Foundation, a non-profit organization.

Fewer families say they believe financial aid or help from grandparents will help them pay for college, the survey also found.

529 plans help

Parents who use 529 savings plans are accumulating larger amounts of money, on average, than parents who do not use the tax advantaged plans, the survey found.

The Foundation said 76 percent of parents with 529 plans had saved at least \$5,000 per child. That compared to just 29 percent of

parents who do not use the plans who said they had saved \$5,000 per child.

About one-quarter of all parents have 529 accounts for college. They save dramatically more than parents without the plans, the survey found.

For instance, almost 21 percent of parents who use the plans had saved between \$25,000 and \$50,000 per child, while only 4 percent of those parents who don't use the plan accumulated that much money.

On the high end, 11 percent of 529 owners had more than \$100,000 per child, vs. only 3 percent of parents who do not use the plans.

Owners of 529 plan accounts say they use them because of the rising costs of college and because plan balances are transferable among children.

A sense of doom

More parents expect to share the costs of college with their children, and some even say rising costs may limit their child's college choices.

Some 38 percent say they expect to receive no financial aid at all, up from 28 percent with that expectation in a year earlier survey. And those who expect aid say it will cover a

smaller portion of overall costs.

Almost two-thirds of parents expect their children to help with financing through assumption of loans and/or employment. Many believe their children will be shouldered with debt for years to come.



As the cost of diplomas rises and financial aid declines, more families are using 529 plans to save and asking children to take out loans.

"Fewer families say they believe financial aid or help from grandparents will help them pay for college."

BOND INVESTORS WIN SINCE 2000, BUT CAN THE STREAK CONTINUE?

Government bonds have been standout investments since 2000 as a combination of falling interest rates and roiled stock markets sent investors fleeing for their perceived safe haven.

But investors hoping for a repeat of this performance in the years ahead may be sorely disappointed: at best, they may underperform stocks and earn returns of a couple of percent a year; at worst, they will lose value if inflation increases, says a report issued by the Research Institute of Credit Suisse, a global banking company.

"Only a raging optimist would believe that, given today's bond yields, the future can resemble the more recent past," the Institute's 2011 Investment Returns Yearbook said. "It is sheer fantasy to expect bond performance to match the period since 1982."

A long bull market

Since 2000, bonds have beaten stocks in 15 of 19 developed countries as interest rates declined over the

period to historic lows, boosting bond prices.

"Government bonds have so far tended to be the asset of choice in the 21st century," Credit Suisse said.

Despite that, stocks have handily outperformed bonds over the past 111 years in the 20 developed markets tracked by the bank.

In the United States, for example, inflation-adjusted annual returns for stocks over that period were 6.3 percent a year, compared to 1.8 percent for government bonds.

Long bear markets

Even though bonds have done very well since 1982, they have gone through several major bear markets since 1900. Credit Suisse put together charts of bond performance in England and the United States over the last 111 years.

"For those who are seek-



Bonds have been great investments in recent years, but have little room to appreciate.

ing safety of real returns, these charts are devastating," it said. "Historically, bond market drawdowns have been larger and/or longer than for equities."

The worst period occurred in the U.S., when bonds hit their peak at the end of 1940, declined by 67 percent, and did not recover until mid 1991.

Inflation governs future bond returns. If higher inflation reappears, Credit Suisse says bonds will become riskier and lose value.

"It is sheer fantasy to expect bond performance to match the period since 1982."

INCOME DROPS, CREDIT FOR FOOD, & MORE

Real median incomes for American family households declined by 1.2 percent in 2010, the U.S. Census Bureau announced in September.

It said family income fell to \$61,544. The biggest declines occurred in western states while the smallest drop came in the northeast.

Meanwhile, fewer Americans had private medical insurance in 2010, with the numbers covered dropping to 169.3 million from almost

171 million in 2009. About 10 percent of children under 18 were not insured.

Credit for food?

American shoppers have increased their use of credit cards to buy non-discretionary goods says First Data Corp., a payment processing firm.

Its survey of payments at retail outlets in June showed a 10.7 percent increase in credit card transaction volume and "consumers are increasingly turning to credit cards to fund

non-discretionary purchases," First Data said.

'Death cross' looms

Does an obscure technical indicator predict a new bear market? Some analysts say the appearance of the "death cross" in August, when the Dow Jones Industrial Average's 50-day moving average crossed below its 200-day moving average, is a bad sign.

Yet newsletter editor Mark Hulbert said his analysis shows that in eight of the last 10 times the death cross appeared, the Dow gained ground over the next 12 months.



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FINANCIAL FRAUDS MULTIPLY DURING ECONOMIC HARD TIMES

Con artists come out of the woodwork during times of economic and market stress, preying on investors looking for better returns or alternatives, says the North American Securities Administrators Association.

State officials who regulate securities have seen a host of new scams aimed at those who are looking for alternatives to low bank interest rates and a volatile stock market, the organization said.

“Con artists follow the news and seek ways to exploit the headlines to their advantage while leaving investors holding an empty bag,” said Association president David Massey.

The current top five financial products designed to trap unwary investors include:

- Distressed real es-



Financial scam artists ply their trade during times of economic distress.

tate schemes that offer investment in foreclosed homes.

- Energy investments like the one that says “wave energy” will eventually power your home.
- Gold and precious metals investments, often linked to promises to mine

gold from dormant claims.

- Promissory notes that “guarantee” high interest rates on privately placed loans.
- Securitized life settlement contracts, where an investor “buys” the death benefit on someone’s life insurance policy and the results are “guaranteed” by bonds.

“Unsuspecting investors can be lured into these schemes, especially if they sound familiar,” Massey said. “These offerings require careful research and a strong reminder that if it sounds too good to be true, it probably is not true, nor will it be profitable to anyone but the promoter.”