Quarterly
BEACON HILL INVESTMENT ADVISORY
Winter 2015

Happy New Year! This is a great time to reflect on past successes and plan for upcoming goals. I find this time of year to be helpful in recalibrating expectations. Check out the last page for an easy tip to a smart start in 2015.

Best Wishes – The Beacon Hill Team

Quarterly Market Review

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 worried about potential deflation, a new recession in Japan, the threat of a new Russian economic meltdown triggered by plummeting oil prices–it all made an improving situation at home look even brighter by comparison.

Even apart from the troubles overseas, the United States by almost any measure was stronger than it's been in years. The labor and housing markets improved, corporate profits were solid, Congress managed to avert another government shutdown, and the Ebola threat had little impact domestically. All in all, it was a Goldilocks economy: not too hot, which could have brought on higher interest rates from the Federal Reserve, and not too cold, which let the Fed end the QE3 bond purchases begun in the wake of the 2008 financial crisis.

That domestic strength fueled more gains for domestic equities than had been envisioned for the fifth year of this bull market. The S&P 500 ended 2014 up more than 200% from its March 2009 low, and the Dow saw its sixth straight yearly gain. However, in the coming year, investors will almost certainly be faced with the start of long anticipated interest rate increases. Though the Fed has promised patience in implementing rate hikes, higher borrowing costs and a strong dollar that makes U.S. goods more expensive overseas could create a headwind for domestic corporations. The question is whether that wind might blow the economy off its current promising course or will merely keep the game interesting.

Market/Index	2013 Close	As of 9/30	As of 12/30	Month Change	Q4 Change	2014 Change
DJIA	16576.66	17042.90	17823.07	-.03%	4.58%	7.52%
NASDAQ	4176.59	4493.39	4736.05	-1.16%	5.40%	13.40%
S&P 500	1848.36	1972.29	2058.90	-.42%	4.39%	11.39%
Russell 2000	1163.64	1101.68	1204.70	2.68%	9.35%	3.53%
Global Dow	2484.10	2534.47	2501.66	-2.71%	-1.29%	.71%
Fed. Funds	.25%	.25%	.25%	0 bps	0 bps	0 bps
10-year Treasuries	3.04%	2.52%	2.17%	-1 bps	-35 bps	-87 bps

**Chart reflects price changes, not total return. Because it does not include dividends or splits, it should not be used to benchmark performance of specific*

Snapshot 2014 – Economy & Markets

The Markets

- **Equities:** After a discouraging start, large-cap domestic equities spent much of the year climbing to new heights. Though they didn't come close to matching last year's fireworks, the S&P 500 and Dow industrials set 53 and 38 new record highs respectively during the year. However, little of that love spilled over to the small caps. The Russell 2000, which had soared in 2013, had trouble scaling the proverbial "wall of worry" and spent much of 2014 either flat or down before a Q4 rally returned it to positive territory. The Nasdaq proved the strongest of the four indices; by December it had come within 242 points of its all-time closing high of 5,048.62, set in March 2000. Beset by weakness worldwide, the Global Dow barely managed a positive return for the year.
- **Bonds:** The bond market confounded those who had feared bond prices would suffer from the unwinding of Federal Reserve support. Challenges overseas lured investors to the safety of U.S. Treasuries; prices rose as the benchmark 10-year yield dropped more than 3/4ths of a percentage point, especially after the threat of an imminent Fed rate hike faded and falling oil prices threatened the economies and currencies of several oil-dependent countries.
- **Currencies:** Falling oil prices coupled with the expectation of higher interest rates helped boost the U.S. dollar, which rose almost 11% over the course of the year. The dollar also benefitted from interest rates abroad, some of which were even lower than those for Treasuries. The strong dollar raised new concerns that countries and foreign corporations hurt by lower oil prices might have trouble repaying debt in currencies that were substantially weaker against the U.S. dollar.
- **Gold:** After plummeting in 2013, gold managed to stabilize a bit last year. The precious metal ended the year at roughly $1,180–not far from where it began in January despite a spring rally prompted in part by the crisis in Ukraine.
- **Oil:** A drop in crude prices that began in July accelerated in Q4 after Saudi Arabia chose market share over profit by deciding not to cut supplies. Prices promptly plummeted to levels not seen since the depths of the financial crisis, falling roughly 45% from the July high of $107 a barrel. The plunge in oil prices helped fatten consumers' wallets but renewed concerns about oil-dependent economies.

The Economy

- **Unemployment:** Improvement in the U.S. job market was slow but steady. The unemployment rate ended the year at 5.8%, its lowest level since July 2008 and better than last December's 6.7%. According to the Bureau of Labor Statistics, the unemployment rate is now down 4.2 percentage points from its October 2009 high of 10%. And after a slow start, job creation accelerated; by December, the number of new jobs added during the previous 12 months was the highest it's been since April 2006.
- **GDP:** After a slump during the first quarter, when the U.S. economy contracted by 2.1%, by Q3 the U.S. economy was growing at its fastest pace in 11 years. The Bureau of Economic Analysis said the 5% annualized growth of gross domestic product outpaced Q2's 4.6% and represented the strongest growth since Q3 2003's 6.9%. After-tax corporate profits also were up, rising 2.8% from Q2 and more than 5% from a year earlier.
- **Inflation:** Inflation remained well under historical averages, which allowed the Fed to postpone any interest rate hike until 2015. By December, the Bureau of Labor Statistics said consumer inflation for the previous 12 months stood at 1.3% while wholesale prices gained 1.4% over the same time. The lower gas prices that kept inflation in check also helped spur retail sales and consumer spending.

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- **Housing:** The most recent home prices measured by the S&P/Case-Shiller 20-City Composite Index were up 4.5% from a year earlier, and the National Association of Realtors® said that by November, new home sales were slowing but still up 2.1% year over year. However, both year-over-year figures were lower than in previous months, and slippage in both housing starts and building permits suggested that the pace of gains may be slowing.
- **Manufacturing:** Manufacturing was a fundamental component of the economy's strength during the year. The Federal Reserve said that by the end of the year, usage of the nation's industrial capacity had finally reached its long-term average. Meanwhile, higher exports helped shrink the U.S. trade deficit to $43.4 billion.
- **International markets:** Economic problems overseas contributed to the Fed's caution with interest rates. Though the European Central Bank cut a key interest rate to -0.1% and continued to say it was prepared to take stronger measures to try to avoid potential deflation, Europe entered the new year still waiting for additional stimulus. In Japan, two consecutive quarters of contraction marked an official recession, calling so-called "Abenomics" into question. Meanwhile, faced with growth that had slowed to 7.3% by Q3, China's central bank cut two key interest rates to try to stimulate domestic consumption; it also agreed to work with the United States to cut greenhouse gases. Finally, President Obama took steps to reestablish diplomatic relations with Cuba, though ending the trade embargo would require congressional action.

Source: Broadridge

Healthy Resolutions Can Pay Off *(Literally)*

If you made a New Year's Resolution to get healthy, you may get more bang for your resolution buck than you bargained for. That's because healthy habits can benefit your wallet as well as your body.

The link between health and money

According to the Centers for Disease Control and Prevention (CDC), chronic conditions–including diabetes, heart disease, and cancer–account for more than 75% of all health-care costs nationwide. Nearly half of all Americans have a chronic disease, which can lead to other problems that are devastating not just to health but also to a family's finances. People with a chronic condition pay five times more for health care each year, on average, as those without a chronic disease.*

Many chronic diseases can be linked to four behaviors: tobacco use, excessive alcohol consumption, poor eating habits, and inactivity.* A closer look at each of these behaviors demonstrates the health-money connection.

Tobacco and alcohol

The American Cancer Society (ACS) reports that the average price of a pack of cigarettes in the United States is $6.36. That means the average annual cost for a pack-a-day smoker is more than $2,300. However, the average health-related cost to a smoker, says the ACS, is $35 per pack–or $12,775 per year for someone who smokes a pack a day.

The National Institute on Alcohol Abuse and Alcoholism defines moderate drinking as one drink per day for women and two for men. Drinking more than that can lead to health problems, including various forms of cancer as well as impairment of your brain, heart, liver, and pancreas. Such outcomes have economic costs. The CDC reports that in 2006, the national cost of excessive alcohol consumption was $223.5 billion, 42% of which was shouldered by excessive drinkers and their families.

Eating habits and activity level

Proper nutrition and regular exercise are vital to staying healthy, but they can also save you money. For example, reducing the amount of high-in-saturated-fat products, processed foods, and red meat in your diet can result in benefits to your heart and wallet. Replacing high-fat ingredients in some recipes with healthier, low-cost options–such as using beans instead of ground beef–can help trim your grocery bills. And replacing high-calorie meals eaten at restaurants with meals made at home using fresh, in-season ingredients can benefit both body and bank account.

Current guidelines from the U.S. Department of Health and Human Services recommend at least 2½ hours of moderate physical activity per week. Many opportunities exist in everyday life to both accumulate active minutes and save money. Instead of driving to your destination, walk or ride a bike. Do your own yard work or house cleaning instead of hiring help. Go for a hike or play ball with your kids rather than going to the movies or visiting an amusement park.

Long-term considerations

Chronic disease also has indirect long-term costs. Leaving the workforce for extended periods–or having to retire early–means fewer paychecks, less chance to benefit from workplace-provided retirement plans and health-care benefits, and lower earnings to apply toward Social Security benefits. In addition, chronic diseases often necessitate home renovations, the hiring of specialized care providers, or even permanent nursing care. When viewed over the long term, taking steps today to reduce your risks of getting sick down the road may make good health and financial sense.

Sources: Centers for Disease Control and Prevention, the Department of Health and Human Services, and the Partnership to Fight Chronic Disease. Broadridge.

Take Twenty and Put it on Paper...

Take 20 minutes of your time over the next week and jot down what you would like to improve about your current situation. By putting it on paper, you tacitly commit and psychologically, it's more powerful than verbalizing. Once on paper, take a few minutes to brainstorm what resources you need to achieve your goal. If it's money, how will you save? If it's time, what can you cut from your already hectic schedule or what efficiencies can you cull to free up more time? If it's emotional (i.e. happiness), what proactive steps can you weave into your daily schedule to set your frame of mind?

All of these scenarios have a multitude of solutions and many tips can be found with a quick Google search. A good way to view your challenge is by way of "cause and effect" - in other words, your challenges are the effect of some cause further upstream. By writing down your goals/ challenges, it helps you to understand the root cause which can then be addressed. For instance, if your goal is to be free from the stresses of debt (business debt, credit card debt, etc.), by acknowledging the problem and writing it down, you're halfway there. Next, you can start looking at your weekly "spend" to see why your putting more onto the card versus paying it down. One clever method is to remove the credit card from your wallet and start paying with cash and/or debit card. If it's your business, remove the ease of access to a commercial line of credit. This will allow you to "feel" the spending in contrast to lines of credit that give you a false sense of money that you don't have. With the new system, expenses that can be cut from your budget will quickly come to light. You also become a better judge of "needs" versus "wants".

Whatever your goal this year, be it weight loss, retirement savings or debt restructuring, write it down so that you can uncover the cause of your desired effect.

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