MALLARD *Money Matters*

April 2014

Expired Tax Breaks

Susan Lehnerd

Congress allowed 55 tax breaks to expire at the end of 2013. There are only six that are likely to have any kind of impact on you.

1) **College Tuition Deductions:** Allowed the deduction of qualified tuition costs from $2,000 up to $4,000.
2) **Deductions for Teachers' Expenses:** Teachers could deduct up to $250 of out-of-pocket expenses for school and classroom related supplies.
3) **Tax-Free Donations Through An IRA:** Known as the Qualified Charitable Distribution, IRA owners 70 ½ or older could make non-taxable charitable donations directly to the charity through an IRA disbursement.
4) **Mortgage Debt Forgiveness:** Homeowners who defaulted on their mortgages and had their bank write off all or part of their loans were not required to claim the unpaid and discharged debt as taxable income.
5) **Energy Efficiency Credits:** A tax credit of up to $500 for specified energy saving home improvements to a primary residence.
6) **Commuter Costs:** Commuters who use mass transit were able to have their employer direct, from their paycheck, $245 a month in tax-free money towards those expenses. In 2014, they will only be able to write off $130 per month.

What kind of tax changes can you expect in 2014 – not many, if any. With Congressional elections in November, you can be sure little focus will be on tax policy change.

What's With the Document Request

Susan Lehnerd

You're my financial advisor. Why do I need to share with you a copy of my will, and my insurance documents, and my tax return, and my…? We get this question all the time. Like a doctor who asks you a lot of questions about factors that can impact your health, we ask you to share information that could impact

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NOTICES

Susan and Ed will be attending the NAPFA conference in Salt Lake City, Utah from May 13-16.

Pam will be vacationing in St. John from April 21—May 20.

Paul will be vacationing in St. John with Pam from April 21—28 and from May 15— 20.

Paul will be in legislative session—Tuesday, Wednes-day and Thursday afternoons, the weeks of April 29, May 6 and 13, and June 3, 10, 17, and 24, and on Monday June 30th.

Ed will be on vacation May 12 - 30, when he is not attending the NAPFA conference.

Diana will be on vacation June 19 & 20th and July 7-10.

Alan will be on vacation May 15—22.

Chris will be on vacation July 7—10.

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What's With the Document Request . . . continued

your financial health. Will your assets be distributed the way you want at your death? Let's review your will or trust document, and take action if necessary to ensure that they will be. Is your income protected should you become disabled? Let's talk about disability insurance. Do you have enough insurance to protect your assets? Your insurance documents will help us determine that.

A tax return can provide a wealth of information. It can help us determine how much your tax withholdings should be in a given year. (We get the tax withholding question often, and can best answer it only if we have the previous year's tax return.) Your return may show that you have charitable inclinations. Maybe we should talk about a charitable gift fund, or ways that can give your donations 'more bang for the buck.' What tax bracket are you in? This answer impacts how your investments are managed. How tax sensitive should investment recommendations be? Maybe you're a perfect candidate for municipal bonds. The answer lies in your tax return.

By being a depository for copies of your important documents, Mallard can provide a 'financial safe deposit box' - a great source for your family when you pass away. Just recently, one of our clients died unexpectedly. The family turned to us for information about the client's will. Because the will had not been shared with us, we felt helpless in assisting the family during such a difficult time.

Why would family turn to the financial advisor for a loved one's will? People have a tendency to mention their financial advisor more than a lawyer or insurance provider. So the name of the advisor may be familiar, thus a starting point for family. Who do you turn to when you need assistance? An advisor!

While initially it may not feel right providing Mallard with documents other than your bank statements and other investment statements, we hope you come to understand and appreciate that doing so provides benefits in addition to documenting your current financial picture.

Buffett on Investing Fundamentals

Paul Baumbach

Every year around this time Berkshire-Hathaway CEO Warren Buffett writes a letter to the company's shareholders, and every year around this time I share some of its highpoints. This year, rather than taking a quote here and there, I am focusing on one section—the one with the most important advice for all investors.

The letter is at http://www.berkshirehathaway.com/letters/letters.html. There is a section on pages 17-19 called "Some Thoughts About Investing." He begins the section with a quote from noted investor and author Benjamin Graham, in his 1949 book The Intelligent Investor: "Investment is most intelligent when it is most businesslike." I would like to really dig into this area, as it provides some great advice for all investors.

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Buffett begins by mentioning two non-stock investments he has made, a 400-acre farm in Nebraska which he purchased in 1986, and a New York City retail property adjacent to NYU he purchased in 1993. Both properties were distressed at the time, and being unloaded by a government agency (FDIC sold the farm, and the RTC, the Resolution Trust Corporation, sold the NYC property). He shares the following six points:

> You don't need to be an expert in order to achieve satisfactory investment returns. But if you aren't, you must recognize your limitations and follow a course certain to work reasonably well. Keep things simple and don't swing for the fences. When promised quick profits, respond with a quick "no."

Keeping it Simple—For close to twenty years now, I have been encouraging investors to focus on the big picture, your stock/bond balance, and to 'plan your play and play your plan.'

> Focus on the future productivity of the asset you are considering. If you don't feel comfortable making a rough estimate of the asset's future earnings, just forget it and move on. No one has the ability to evaluate every investment possibility. But omniscience isn't necessary; you only need to understand the actions you undertake.
>
> If you instead focus on the prospective price change of a contemplated purchase, you are speculating. There is nothing improper about that. I know, however, that I am unable to speculate successfully, and I am skeptical of those who claim sustained success at doing so. Half of all coin-flippers will win their first toss; none of those winners has an expectation of profit if he continues to play the game. And the fact that a given asset has appreciated in the recent past is never a reason to buy it.

Looking Forward and the Pitfalls of Speculating—You don't need to know everything in the investing world, but you should do the work to research the investments you make or advisors you use, ensuring that there is reason to expect good future results. This is related to driving your car by looking out the windshield, not the rear view mirror. Avoid the temptation to assume that (100% known) past results are indicative of (largely unknowable) future results. Be aware of yesterday, but plan for tomorrow.

There are investments without any underlying economic activity (such as gold). Here investors are making their decision purely on the expectation that prices will be higher when they wish to sell than they were when they bought. Most often this is a zero-sum game, with an equal number of losers as winners. For this reason, I strongly prefer investments tied to economic activity (stocks and bonds of companies which are conducting economic activity). These investments most often provide win-win outcomes—you being a 'winner' does not require someone else being a 'loser.'

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> With my two small investments, I thought only of what the properties would produce and cared not at all about their daily valuations. Games are won by players who focus on the playing field – not by those whose eyes are glued to the scoreboard. If you can enjoy Saturdays and Sundays without looking at stock prices, give it a try on weekdays.

Ignore the Noise—Buffett points out that he has made and continued these investments without any valuations. This touches on the distinction between information and knowledge. Our current investing culture is overwhelmed with information—we sometimes hear that we are drinking information out of a fire hose. There are many cable channels with 'news' 24 hours a day, seven days a week. Stock prices flow constantly through the business day. Does that mean that this information is useful?

Recently I have been describing the process of investing for and during retirement as being analogous to a sailor crossing the ocean. They have a destination in mind, and that is their top focus. They monitor the little details, and make appropriate adjustments (of sails, of the rudder), however the current does not change their overall plan, just as current prices of stocks, and stock markets, should not lead you to change your investment plans.

> Forming macro opinions or listening to the macro or market predictions of others is a waste of time. Indeed, it is dangerous because it may blur your vision of the facts that are truly important. (When I hear TV commentators glibly opine on what the market will do next, I am reminded of Mickey Mantle's scathing comment: "You don't know how easy this game is until you get into that broadcasting booth.")

Macro Hocus Pocus—Here I both agree and disagree with Buffett. I agree that individual investors should not need to have a complete market prediction in mind in order to invest, and I agree that most 'market experts' on TV are chosen based on their looks than on their credentials, and are encouraged to share sensational assessments rather than well-reasoned ones. I actually encourage investors to disregard such TV 'market experts.'

However I do believe that Mallard's macro outlook is worthwhile (although limited in its dependability). We are very careful to avoid all tainted market analysis, which is 98% of what is available. We also put much more weight in data than in analysts' spin. One top reason that we provide our macro outlook is to meet our clients' understandable desire for a calm, balanced voice, to help them stick to their investment program in both good times and bad.

A further justification for Mallard's macro outlook is that, unlike Berkshire-Hathaway's investing focus, Mallard's investment focus is on both stocks and bonds. Bonds are necessary for investors to obtain a

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smoother path. More so than stocks, bonds are highly affected by macro-economic events, and our rotation amongst the many subtypes of bonds requires that we make these decisions based on informed, businesslike analysis of the US and global macro-economic outlook.

> My two purchases were made in 1986 and 1993. What the economy, interest rates, or the stock market might do in the years immediately following – 1987 and 1994 – was of no importance to me in making those investments. I can't remember what the headlines or pundits were saying at the time. Whatever the chatter, corn would keep growing in Nebraska and students would flock to NYU.

Timing—Especially when clients (new and existing) bring cash to Mallard, we are asked 'whether now is a good time to invest.' I sometimes share Sir John Templeton's answer: "The answer is the same as when is the best time to plant an oak tree. Twenty years ago is the best answer, and today is the next best answer." If your investment timeframe is a year, there is never a good time to invest. If your investment timeframe is a lifetime, as it is for most of us, now is a great time to invest.

We certainly advocate gradual investment of new dollars, to benefit from dollar cost averaging. More importantly, gradual investment of new dollars helps investors avoid "buyer's remorse," regretting a purchase. One of our top goals as investment advisors to our clients is to reduce the risk of making bad investment decisions. The most common bad decisions that investors make are tied to crowd behavior—selling stocks when they have fallen sharply, and boosting stocks when they have risen sharply. The primary method we use to address this risk is through education (newsletters, reports, and conversations regarding the benefits of long-term investing)—focusing on the destination across the ocean, not on the current waves. A secondary method is to use gradual approaches that are designed to limit the instances where there is substantial financial pain from having made a single investment in what turns out (in hindsight) to have been a poor time/price.

Investing is not for the faint of heart, but need not be only for the brave. Whether you invest on your own, or with the advice of a firm such as Mallard, focus on the forest and not the trees, on your portfolio's path over decades, not hours. In turn, this will help you avoid costly mistakes, and to sleep better. Getting tips from authorities such as Warren Buffett is always a good idea for every investor. Unlike most investing heavyweights, Buffett can always be counted upon to provide useful, extremely readable recommendations and insight.

Market Review and Outlook—April 5, 2014

Largely a sideways quarter. We had Winter Olympics with little controversy, but followed that up with turmoil in the Ukraine. While Janet Yellen was confirmed as our new Fed Chair (the first female chair), replacing Ben Bernanke, she appears to plan to continue the Fed's recent practices, at least initially. Europe is very slowly crawling out of its sovereign debt crisis-led double dip recession. Following a very strong year for stocks, the past quarter brought very modest results, from both stocks and bonds. Bonds, rising 1-2%, kept up with, and in some cases outperformed, stocks this quarter. **The average investor, with a 'moderate allocation' approach, earned 1.6% in the past three months.**

The US economy ended 2013 with solid 2.6% growth, however the 1st quarter will likely come in much lower due to the harsh winter. Fortunately, **solid growth is expected in the US for the rest of 2014**. Vehicle sales continue to run above average levels, as do real capital goods orders. Real estate prices, both residential and commercial, continue to rebound, and inventories of houses on the market are down to, and are remaining at, normal levels. The federal budget deficit is about 3%, at or below where it was for most of 1975-1995, and well below its 10% peak in 2009. Unemployment has fallen to 6.7%, and is approaching its 50-year average level of 6.1%. Inflation fell during the quarter, and is up only 1.1% in the past year, partially due to declines in energy and transportation costs.

Overseas economies in developed markets generally enjoyed steady growth in 2013, from near-zero levels at the start of the year to 2% by the 4th quarter. Emerging market countries also enjoyed fairly steady economic growth in 2013, and while they are expected to see their growth slow slightly this year, this is from an attractive 4% current level. Globally, manufacturing activity/momentum slowed a small amount during the quarter, but continues to be above average. The only notable exceptions are Australia, China, Greece, and Russia.

In the past quarter, precious metals leapt 12%, but are still down over 30% for the past year. Real estate rose 9%, while utility stocks and long-term government bonds returned more than 7%. Healthcare stocks rose over 6%. Latin American stocks were the only notable investment segment which fell more than 1% during the past quarter. Investors continued to buy more stock funds than bonds during the quarter, but the amount of difference declined, compared with late 2013.

As the quarter brought almost equal results from stocks and bonds, **many investors may find that minimal rebalancing is required at this point**. Investors who have not yet rebalanced their portfolios after 2013 should not delay; the benefits are still available to you, for now. We are making some changes within our target bond levels.

Category	3 Months	12 Months	3-Yr Avg	5-Yr Avg	10-Yr Avg
Fidelity Cash Reserves	+0.00%	+0.01%	+0.01%	+0.08%	+1.70%
Intermediate Term Bond	+1.94%	+0.21%	+3.99%	+6.62%	+4.28%
Intermediate Muni Bond	+2.33%	-0.29%	+4.56%	+4.99%	+3.50%
Large-Cap Stock	+1.70%	+21.17%	+13.09%	+20.02%	+6.92%
Mid-Cap Stock	+2.54%	+22.66%	+12.27%	+22.97%	+8.31%
Small-Cap Stock	+1.45%	+24.10%	+12.74%	+24.09%	+8.61%
Foreign Large-Cap Stock	+0.11%	+15.39%	+5.80%	+15.41%	+6.36%
Real Estate	+9.06%	+3.73%	+9.67%	+27.18%	+7.52%
Natural Resources	+2.69%	+8.64%	-1.74%	+14.59%	+9.54%
Technology	+2.39%	+30.00%	+10.58%	+21.68%	+8.08%
Moderate Allocation	+1.64%	+11.86%	+8.40%	+14.55%	+6.01%

The data in this table comes from Morningstar and is as of March 31, 2014.
Information herein should not be construed by any consumer and/or prospective client as a solicitation to effect, or attempt to effect, transactions in securities, or the rendering of personalized investment advice for compensation.

Due to the VERY gradual pace, **the economic recovery in the US appears have plenty of room to continue**, despite completing its 5th year this quarter. Similarly, while the US stock market has been recovering for 5 solid years, current stock prices are not clearly expensive as they have largely merely kept pace with the underlying companies' profits. Certainly stock market profits from this point forward will most likely be much more modest than profits from this time, than from one, two, or five years ago.

Similarly, we have recommended a much higher-than-normal use of 'opportunity bonds' in the past five years, as the recovering economy has favored bonds with more credit risk. In the past five years, high-yield bonds have outperformed intermediate-term bonds by a large margin. Thus future profits in this area will most likely be harder to come by than in the recent few years, so **it is time to start becoming more wary for opportunity bonds**.

The two areas with the best risk:reward characteristics we see at this time are Europe and emerging market stocks. Both are out of favor, largely for good reasons. Europe took less drastic actions in 2008-2009, and thus began to emerge from the financial meltdown later than the US, and then it suffered a double-dip, with the Greece and other peripheral country-led sovereign debt crisis. We appear to be at or just beyond a turnaround point, such that new developments are generally better than expected. As such, we have been establishing positions in European stocks for a few months.

Emerging market stocks have similarly been under a cloud, but for less time, less than a year. China always presents challenges for investors. Other emerging markets have been rejected by investors, due to concerns over their reliance on sale of natural resources (which have been under pressure for the past year or more), and due to concerns with their susceptibility of pressure when the US interest rates rise. Those are good reasons, good concerns. However, at some point investors will likely recognize that those worries are fully reflected in the relatively low prices of emerging market stocks. For these reasons, **we have been stubbornly maintaining a fairly high level of emerging market stocks**.

Overall the past quarter was fairly quiet for investors. As a result, our outlook is largely unchanged. We continue to find cash unappealing. Bonds are OK but uninspiring. Given the alternatives, we like stocks a little more than normal. We like the economics backing up the companies behind the stocks. We also like the tailwind which the continuing shift of investors' dollars from cash into both stocks and bonds (more to stocks for the past nine months).

As contrarians, we like to be early to the party, but to leave before the police arrive. We prefer to purchase investments before they become popular, and thus before they become expensive, and we like to sell investments while they are popular, while they are expensive. This doesn't mean broad SELL THIS, BUY THAT moves, but rather we prune—we cut back areas that have been stronger, and maintain or boost areas which remain out of the spotlight.

At this time, this means that we are ensuring that we are at or below normal levels for utilities and health-care stocks. We are also being more strategic with our high yield bonds, and we are reducing our position in bank loan bond funds, due to their recent popularity (and resultant reduced upside). We remain committed to **emerging markets stocks**, despite their being out of favor for a few quarters. In the second half of 2013 we began establishing a **Europe-only stock position**, and we continue this approach. While the European economy is not out of the woods, the region is doing more good things than bad, and stock prices do not yet reflect the coming recovery. As we saw clearly from 2009 forward, US stocks began strong recoveries well before economic growth was well established, and we expect the same in Europe.

We are taking advantage of two apparent bond opportunities at this time. We are establishing a very small allocation to **long-term bonds**. These were hurt badly in 2013, and have recovered a little in the past quarter. They appear to offer adequate yield and prices, relative to their risks. We are also focusing a small slice of client bond money in **high-yield municipal bonds**, even for tax-deferred accounts and low-tax bracket investors. This is due to the pure potential return, yield and price increase, that they offer, regardless of tax benefits. Here we are trying to take advantage of an out-of-favor sector of the overall bond market.

For the rest of 2014, we currently expect continued modest returns from stocks, led both by profit growth and growing investor confidence. Bonds should continue to have challenges, but could end the year with positive returns. Investors always face risks, however **a well-diversified portfolio, with protections for all likely risks, regularly rebalanced, should shield investors from the most painful challenges around the corner**.

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Working together, building your financial security

Compliance Corner

Pam Baumbach

Form ADV

Mallard Financial must file our annual Form ADV update with the Securities and Exchange Commission (SEC) by March 31st. Form ADV Part 1 is the informational filing we submit annually and when there are significant changes in our business. Part 2 is the "plain English" brochure that is written in a user friendly manner and explains our business operations to the consumer. We will be delivering our annual ADV notice (an update that lists significant changes since our last filing) to our clients by April 30th. The most recent Form ADV Part 1 & 2 are always available on our website at: http://mallardfinancial.com/documents/adv.pdf or by contacting our office.

Mallard makes every effort to employ "best practices" and the procedures often require added efforts on the clients' part. These efforts are employed to safeguard their assets and are reviewed heavily before enacting them. I would like to thank all our clients for their patience with increasing compliance requirements.

As Chief Compliance Officer, I am available to discuss any questions concerning our ADV or any compliance issues.

I can be reached at (302) 737-4546, (888) 737-4546, or pam@mallardfinancial.com

News and Events

Mallard will be offering the following Delaware Money School class:

April 21, 2014 - 6:30 p.m. - 8:30 p.m., "Social Security Benefits" at the Newark Free Library -presented by Ed Mink