

HWM ViewPoint



HENRY

WEALTH MANAGEMENT, LLC

1370 Washington Pike,
Suite 403
Bridgeville, PA 15017
Phone: 412.838.0200
Fax: 412.838.0204
www.HenryWealth.com

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Architects for Wealth

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What Happened to Asset Allocation and Diversification in 2008?

Did you know that the Chinese calendar declared 2008 as the **Year of the Rat**? Investors can certainly relate to that allegorically, yet would prefer 2008 to have been the **Year that Never Existed!**

At Henry Wealth Management, LLC, we preach the following themes, regardless of the "year":

- **Long-term**
- **Buy and Hold**
- **Asset Allocation**
- **Diversification**
- **Rebalancing**, and
- **Patience**

Asset allocation is the systematic approach of dividing your portfolio into stocks and bonds, based on goals, time frames and propensity towards risks.

Diversification goes one step further, dividing stocks into sub-categories, such as U.S., International and Emerging Markets. It also separates bonds into various types, such as Corporate, Government and International. Diversification is a method used to help reduce portfolio volatility. However, the financial unraveling in 2008 pulled down every conceivable sub-asset category except for Treasury securities.

Thus, did asset allocation and diversification fail in 2008? In the sense that most investment portfolios suffered negative returns, it did. Yet the damage could have been far worse were it not for asset allocation and diversification.

Below are returns for major indices for the year ending 2008. Only the Citi I-5 Year Treasury index was positive. Notice, also, that the worst performer over one year, the MSCI Emerging Markets Index, was also the best performer over 10 years.

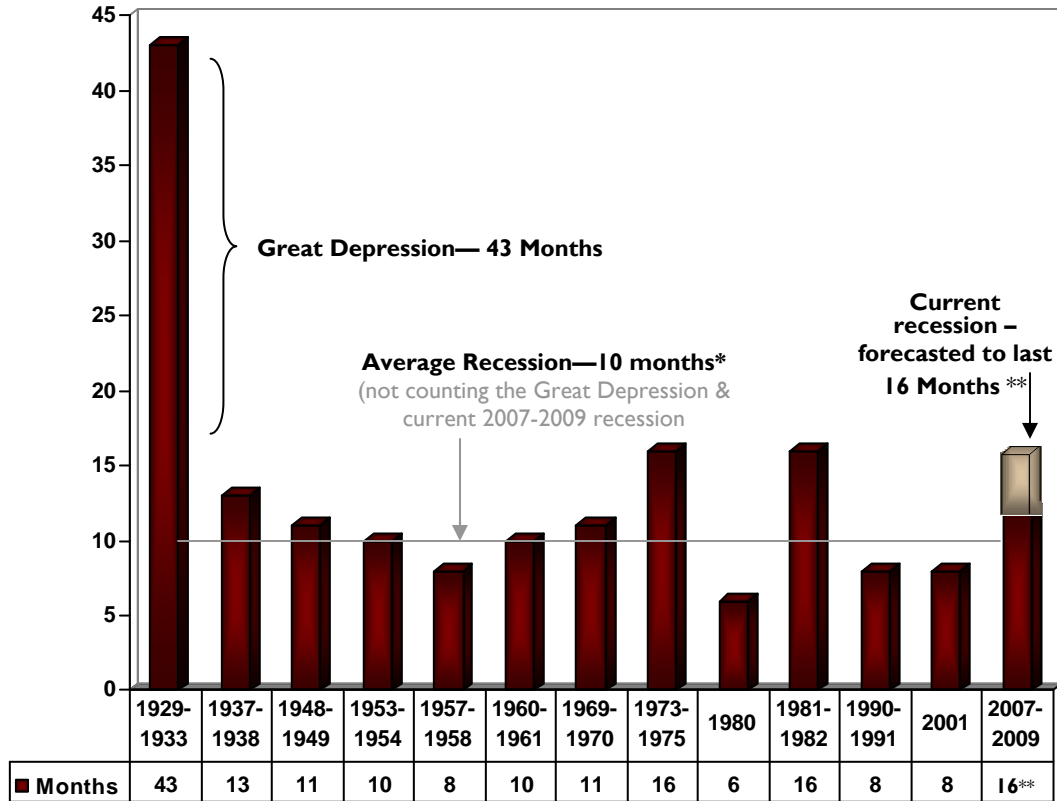
P.S. For what it's worth, 2009 is the **Year of the Ox**...could that be a bullish sign?

Major Indices						
	Citi I-5 Year Treasury Index	Lipper Balanced Index	S&P 500 Index	Russell 2000 Index	MSCI EAFE Index	MSCI Emerging Markets Index
	0% Equity	50-60% Equity	100% Equity	100% Equity	100% Equity	100% Equity
1-Year Return	8.75	-26.19	-37.00	-33.79	-43.06	-53.18
3-Year Return	6.85	-4.25	-8.36	-8.29	-6.92	-4.62
5-Year Return	4.61	-0.04	-2.19	-0.93	2.10	8.02
10-Year Return	5.17	1.45	-1.38	3.02	1.18	9.31

The above information is supplied from the Symmetry Portfolio: Fourth Quarter 2008 review. Statistical data courtesy of Dimensional Fund advisors.

Current Recession vs. Past Ones

World economies are now deep in the grips of a major slowdown. There are still plenty of risks, including additional housing market foreclosures, more credit losses and continued liquidity issues. While this may be the worst economic crisis since the Great Depression, the current recession still pales in comparison. Consider these facts;



*Median value excluding Great Depression and Current recession
 **AllianceBernstein forecast
 Source: Bureau of Economic Analysis and AllianceBernstein

The Great Depression of 1929-1933 saw a crippling contraction in the availability of money for lending and borrowing. Prices plummeted and so did demand, which contributed to a staggering 26.5% total decline in inflation-adjusted GDP!

Today's current recession is much different, featuring deposit insurance (FDIC), much lower unemployment, and more government policy that at least on the surface, seems to be supportive of an eventual recovery. History also provides some comfort in that the average length of previous recessions (excluding the Great Depression) was 10 months, with economic growth falling no more than 4%.

The current environment is more supportive than that of the Great Depression		
	That was Then (Great Depression)	This is Now (Current Recession)
Federal Deposit Insurance Corp (FDIC) to insure Bank deposits	✗	✓
Social Security protect workers	✗	✓
Coordinated global interest-rate cuts to stimulate economies	✗	✓
Good international trade relations	✗	✓
Lower tax rates	✗	✓
Single-digit unemployment	✗	✓

Section 529 Plans Disappoint in 2008



Having just recently taught my son Philip, now a senior in high school, how to drive, and presently teaching Alexander, a junior the same, three common words are oft-repeated... PLEASE SLOW DOWN!

Parents with kids in the same age range as Philip and Alex, those just about to head off to college, who own Section 529 plans, specifically "age-based allocations", were surprised to see large losses in 2008.

Based on losses in 2008, you may be tempted to change your 529 strategy. First of all, until 2009, Section 529 Plan participants were limited to only one investment allocation change per in their plans each calendar year. However, the IRS recently issued a rule that allows plan participants to make two changes in 2009. That means participants could opt out of an age-based plans now, then later this year, opt back in. Should this type of "timing" be pursued? Here are three general points of consideration;

1- Should I reposition my entire 529 portfolio to a "safer" mix?

2- Should I at least change my new contributions into a "safer" mix, and leave my current allocation as is?

3- Can I afford to postpone withdrawals from 529 accounts, opting rather to use other sources of funds to pay the bills during the first year or two of college?

The pro's and con's of making allocation changes certainly needs to be discussed on an individual basis.



2009— Improving Signs?

Today's investors would like to know to know when the stock market and economic recovery may begin. While much of the news remains bleak at this particular time, there are some "signs" of improvement are appearing:

1. LIBOR Rates: A significant decline in the LIBOR (*London Interbank Offered Rate*) has occurred since the original panic in September, 2008. The 3 month rate at that time was over 4%. This has most recently reduced to approximately 1.2%. This indicates a significant reduction in the cost of bowing between banks, which is a reflection of a perceived reduced level of risk. Many new and existing adjustable rate mortgages are based off of

LIBOR, so a lower rate can be viewed as an economic stimulator. (Source: Bankrate.com: <http://www.bankrate.com/brml/ratewatch/3mo-libor.asp>)

2. Commercial Paper: The commercial paper market (*another form of short term corporate debt*), which often provides insight to how companies manage debt and daily operations, has improved dramatically. This "cost" of top-rated commercial paper dropped

from a high of 4.64% on October 10, 2008 to a current yield of 0.73%, and may be viewed as a stimulator. (Source: Advisor Asset Management January 12th Market Commentary by Mike Boyle).

Remember This: Thus, with a bit of good news in the mix, recall also that stocks historically to tend to rally on average, six months prior to economic recoveries. This is due to the expectation that a recession has bottomed out and economic recovery is in sight. For those who have steered out of stocks, or steered away from them with new contributions, waiting for the economy to "recover" before re-deploying a long-term investment strategy may mean missing the next wave of recovery.



Living Benefit Riders: Offering Portfolio Protection at a Cost

Have you sensed a common theme in advertising to “boomers”? Notice attractive, middle-aged couples living in the moment. The pulsating beat of favorite classic rock tunes provides background to deliver a pitch, often times promoting a new car, an anti-aging product, or an insurance company trumpeting a guaranteed lifetime income available through a variable annuity. Let’s briefly overview the latter, its potential application and costs.

What is a variable annuity?

A variable annuity is a contract between the purchaser (you) and an insurance company. You provide them with an amount to invest. They provide you with a lineup of investment options. At some future point, you may liquidate the account or convert it into a stream of income. Unless the contract contains some type of guarantee, receiving an on-going income could result in your principal being exhausted, similar to any other investment.

How does an annuity generate lifetime income?

Of course, many boomers envision long periods in retirement. This naturally lends to the thought, “**I could outlive my assets.**” A variable annuity with a lifetime income option can alleviate the concern of running out of money during a single or even a joint lifetime (husband and wife). Here are examples of how two common annuity riders could work to ensure that assets are not outlived.

RIDER 1: Guaranteed Minimum Accumulation:

An accumulation rider is geared for pre-retirees who are still in the **growth phase**.

Consider Andy and Sandy. Of course, this example is hypothetical and for illustrative purposes only. They are five years away from retirement and are concerned about exhausting their assets in the future. Assume they diversify \$100,000 of their nest egg into a



variable annuity product offering an accumulation rider. Many insurance companies will guarantee them a 7 percent return per year, during the “growth” period. In other words, their \$100,000 deposit would have a guaranteed “benefit base” of \$107,000 after year one, \$114,000 after year two, all the way up to \$135,000 after year five.

The actual value of the annuity may be more or less than this benefit base. If it’s more, Andy and Sandy will have additional options. Let’s concentrate on the example of having less, due to poor investment performance. Assume their account value is only \$125,000 at the end of five years just as they are set to retire. Now what?

RIDER 2: Guaranteed Minimum Withdraw:

Turning to the **income phase**, Andy and Sandy may commence with a lifetime income and use their benefit base of \$135,000, which would generate an income stream guaranteed for life, or for their joint lives if they so choose. The actual amount paid will be dependent on the carrier selected and their provisions, typically in the 4.5% to 5% range.

Once started, what if the actual investment performance exceeds the guaranteed income amount and the benefit base grows? Then the contract would offer a “step-up” so the income could also grow. The security in knowing that they have a “pension” of sorts, in which a percentage of income per year is guaranteed for their joint lives, and may increase with favorable investment

performance, does add a layer of comfort.

So far, so good, but... what if the annuity consistently earns less than the guaranteed income amount? The actual account balance would decrease, maybe to the point where the account could become worthless. If that were to occur, **the guaranteed income would still continue to be paid**, until both were deceased. Their heirs would receive nothing from the annuity in this case.

Costs:

With regard to costs, most variable annuities entail annual internal expenses, including the costs associated to manage assets, of over 2% per year. Tacking on “accumulation” and “withdraw” riders would push total expenses to over 3% per year. Not only is this an expensive proposition, but liquidity may also be limited, as most annuities have liquidity restrictions for the first three to seven years.

Thus, folks like Andy and Sandy need to carefully weigh fees and expenses against benefits derived in making an intelligent decision. Certainly a prospectus should be carefully reviewed and all guarantees mentioned are based on the claims paying ability of the issuing insurer. Those nearing or at retirement that are risk adverse may be the best candidates to utilize a variable annuity with accumulation and withdrawal guarantees. Investors with moderate to aggressive risk tolerances may likely view variable annuities as expensive propositions, offering unnecessary features.

At Henry Wealth Management, we want to review all of your assets and your need for income, to determine if a variable annuity with living benefits provisions may make sense for a portion of your assets. If so we will be able to offer products from a variety of carriers.

Here We Go Steelers... Here We Go Stocks?



With the Pittsburgh Steelers securing their record breaking sixth Vince Lombardi trophy, do investors have reason to be optimistic? History would suggest yes.

In each of the five previous Super Bowl wins by the Steelers, the S&P

500 has produced an average return of 20.48% during that calendar year! It is also noteworthy that the Pittsburgh Steelers have had the best average performance of any of the Super Bowl teams that have won at least three championships.

Of course, this is speculation at best and is not guaranteed. Nonetheless, this may give fans of stocks in general something to cheer about!

	Year	Change
Super Bowl IX	1975	+31.55%
Super Bowl X	1976	+19.15%
Super Bowl XIII	1979	+12.31%
Super Bowl XIV	1980	+25.77%
Super Bowl XL	2006	+13.62%
Super Bowl XLIII	2009	???



Teams with 3 or more Super Bowl victories	Number of Championships	S&P 500's Avg. Performance in Championship Years
Pittsburgh Steelers	6	+20.48% (excludes 2009 YTD)
Green Bay Packers	3	+19.59%
San Francisco 49ers	3	+19.18%
Washington Redskins	3	+11.38%
Dallas Cowboys	5	+8.49%
New York Giants	3	-3.38%
New England Patriots	3	-3.79%
Oakland/L.A. Raiders	3	-6.61%

Source: www.CNBC.com



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WEALTH MANAGEMENT, LLC

1370 Washington Pike,
Suite 403
Bridgeville, PA 15017
Phone: 412.838.0200
Fax: 412.838.0204
www.HenryWealth.com

Philip C. Henry, ChFC, CFS
President
Phil@HenryWealth.com

Daniel L. Henry
Vice President
Dan@HenryWealth.com

Amy Rhoads
Director of Client Services/
Technology
Amy@HenryWealth.com

Lauri Henry
Administrative Assistant
Admin@HenryWealth.com

Beth Henry
Events Coordinator
Beth@HenryWealth.com

Architects for Wealth

Disclaimer

Asset allocation and/or diversification do not guarantee against loss. Rebalancing assets can have tax consequences. If you sell assets in a taxable account you may have to pay tax on any gain resulting from the sale. Please consult your tax advisor. Gross Domestic Product is the total market value of all final goods and services produced in a country in a given year. S&P 500 Index is a market cap weighted index composed of 500 widely held common stocks. Citigroup USBIG Treasury Index 1-5 Yr measures total returns for the current on-the-run Treasuries that have been in existence for the entire month and is used as a proxy for high quality and short duration bond holdings. Lipper Balanced Fund Index is a more suitable benchmark as Index's composition has greater diversification, which is more consistent with the Symmetry's model portfolio. Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index. Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market. MSCI EAFE Index is composed of companies representative of the market structure of 20 developed market countries in Europe, Australia and Far East. MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging market and consists of 25 emerging market country indexes. Past performance is no guarantee of future results. Investors cannot invest directly in an index.

There is no guarantee that the 529 plan will grow to cover college expenses. In addition, depending upon the laws of your home state or designated beneficiary, favorable state tax treatment or other benefits offered by such home state for investing in 529 college savings plans may be available only if you invest in the home state's 529 college savings plan. Any state-based benefit offered with respect to a particular 529 college savings plan should be one of many appropriately weighted factors to be considered in making an investment decision. You should consult with your financial, tax or other adviser to learn more about how state-based benefits (including any limitations) would apply to your specific circumstances and also may wish to contact your home state or any other 529 college savings plan to learn more about the features, benefits and limitations of that state's 529 college savings plan. You may also go to www.collegesavings.org for more information.

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Philip C. Henry, ChFC, CFS is the President of Henry Wealth Management, LLC, an independent financial planning firm located at 1370 Washington Pike, Bridgeville, PA. He may be reached at 412-838-0200 or through email at Phil@HenryWealth.com. The firm's website is www.HenryWealth.com. The opinions expressed in this commentary are those of the author and may not necessarily reflect those held by NFP Securities, Inc. This is for general information only and is not intended to provide specific investment advice or recommendation. NFP Securities, Inc. does not provide legal or tax advice.