GALECKI FINANCIAL MANAGEMENT FINANCIAL SENSE

	LAST MONTH	LAST 3 MONTHS	YTD
S & P 500 Index	-0.25%	4.93%	13.69%
Russell Midcap Index	0.21%	5.94%	13.22%
Russell 2000 Index	2.85%	9.73%	4.89%
Dow Jones Industrial Average	-0.18%	5.05%	12.95%
Morgan Stanley EAFE Index	-3.46%	-3.57%	-4.90%
MSCI US REIT Index	1.93%	14.34%	30.38%
DJ UBS Commodity Index	-7.63%	-12.10%	-17.01%
Barclays Aggregate Bond Index	0.09%	1.79%	5.97%

INDEX RETURNS

The fourth quarter saw domestic stocks and real estate excel, while commodities and international stocks struggled. U.S. Large cap stocks as measured by the S&P 500 were up 13.69% on the year. Small-cap stocks according to the Russell 2000 surged in the fourth quarter by 9.73% to finish positive on the year by 4.89%.

International market returns were decent from a local currency perspective, but due to a strengthening dollar, the US dollar returns were actually quite weak. International Developed markets as measured by EAFE were down 3.57% in the last quarter and finished down 4.90% on the year. Emerging markets were down 4.51% in the fourth quarter and they were down 2.19% on the year. Commodities were crushed by plummeting oil prices and the index declined 17.01% on the year. Real Estate had a great year up more than 30%.

The bond market was a pleasant surprise in the fourth quarter and on the year. The Barclays Aggregate Bond Index rose 1.79% in the fourth quarter and finished the year up 5.97%. Emerging market bonds were down 0.46% in the last quarter but finished the year up 7.60% according to the JPMorgan EM Bond Index.

ECONOMIC REVIEW AND OUTLOOK

The economy continues to show strength. Real Gross Domestic Product (GDP) increased 5.0% in the third quarter following a 4.6% rise in Q2. Roughly 68% of our economy is driven by consumer spending which increased 3.2 percent in the quarter.

The Leading Economic Index increased 0.6% in November to 105.5 following a 0.6% increase in October and a 0.8% increase in September. These numbers suggest continued growth through the winter months assuming no major storm disruptions. Industrial Production increased 1.3% in November and the Capacity Utilization rate rose 0.8 percentage points to 80.1 percent. This is now in line with the historical average over the last forty years. This means that we could eventually see some pricing pressure on goods with factories running at this higher rate.

The U.S. labor market is one of the main reasons for improved sentiment. Total non-farm payrolls increased by 321,000 in November and the unemployment rate remained at 5.8%. Initial weekly unemployment claims were 298,000 for the week ending December 27th. Our economy lost roughly 8.8 million jobs in the 2008-2009 Recession. Since then we have added 10.9 million new jobs. According to JP Morgan, there were roughly 7 unemployed individuals for every available job in 2009. This ratio is down to 1.9 persons per available job.

The ISM manufacturing survey was at 55.5% in December. This shows a manufacturing sector that has expanded for the 19th consecutive month and the overall economy has grown for the 67th consecutive month. The ISM Non-Manufacturing index came in at 56.2% in December which was 3.1 points lower than the November reading. Both numbers show a growing manufacturing sector and a growing service sector for the U.S.

The housing market has started to cool. Housing starts in November were at a seasonally adjusted annual rate of 1,028,000. This is 7.0% lower than the November 2013 rate of 1.015 million. There is now a 5.8 month supply of homes for sale which is in line with historical averages. Look for price increases to be minimal in 2015.

Global growth is still expanding… but slowing. The JP Morgan Global Manufacturing PMI is now at 51.6 in December down from 51.8 in November. The U.S. and Canada both have PMIs at 53.9. The Euro area is at 50.6 with France and Italy both at 47.5. China and Korea are both at 49.6 and Indonesia is down to 47.6. This data suggests that manufacturing is slowing in the U.S. and abroad.

EQUITY AND BOND MARKETS

Does Diversification and Asset Allocation still work? Should I just put all my money in the S&P 500? These are questions that investors are asking given returns for U.S. Large cap stocks over the last few years. In fact, Liz Ann Sonders (Chief Market Strategist for Schwab) addressed this question by stating that "A desire to index to the hottest market is often a sign that discipline is beginning to take a back seat to performance-chasing".

As humans, we become experts about events after they have occurred. The problems that occurred with the economy in 2008 seem easily avoidable now with the benefit of hindsight. We all knew that Ohio State would beat a very good Wisconsin team 59-0 with their third string quarterback (seriously 59-0?) after the game. Just as we now know that U.S. Large Cap stocks would be the best performing asset class (other than REITs) in 2014 and only invested in that one particular asset class. It sounds ridiculous to us to only invest in one asset class, but that is exactly what many retail investors are discussing right now. Which one would you choose?

The truth is that we do not have a crystal ball. We don't know what the best performing asset class will be in 2015 or in 2016. We do know that diversification utilizing an asset allocation approach works over the long-term. Our returns over the last 3-5 years have been very solid and ahead of cash flow projections. Our returns for the first seven months of 2014 were also excellent. So what happened in the last five months?

Early in the year, we were helped by our 3% exposure to commodities and our MLP and energy fund. We were beating virtually every asset class benchmark. The last five months brought a different result. We were right that stocks were still attractive and we stayed fully invested. However, the collapse in oil prices hurt our commodity exposure and our energy funds.

In addition, there were really only two asset classes that did well at the end of the year: U.S. Large Caps (Typically measured by the S&P 500 and the DJIA) and Real Estate. Our real estate fund was up more than 25% on the year, but it is only about 7% of the portfolio. Our US Large Cap funds were in line with the S&P 500, but this is typically only about 30% of the portfolio. We have exposure to small-caps, mid-caps, international developed markets, and international emerging markets… all of which struggled in the last 5 months. In hindsight, it would have been really nice to only own U.S. Large Caps in 2014… but who knew? Is that all we should own in 2015, Domestic Large Caps? Or should we choose a different asset class? The best asset class in 2007 was Emerging Markets and the following year in 2008 it was the worst.

The S&P 500 is trading at a forward P/E ratio of 17. Just slightly above its long-term average of 16. International Developed Markets as measured by EAFE have a P/E ratio of about 14 times earnings and International Emerging Markets have a P/E ratio of about 11 times earnings. Both asset classes are significantly undervalued relative to the S&P 500.

The bond market continues to be a challenging environment. The Barclays Aggregate Bond index climbed nearly 6% in 2014 as the 10 year Treasury yield fell from nearly 3% down to roughly 2%. International investors flocked to the safety and liquidity of the U.S. Dollar in 2014 as global economies slowed during the year. This put downward pressure on the 10 year yield and subsequently saw the U.S. Dollar appreciate versus other currencies.

PORTFOLIO MANAGEMENT

Our diversified approach has served our clients well over the last twenty years. Specifically, returns over the last five years are tracking well ahead of expectations. All planning firms and money managers will have short stretches when their strategy does not work as well as they would like. Last year was one of those years for our firm. We still like our strategy and are confident it will work in 2015, we just feel like we were a bit early.

We hold roughly a third of our portfolio in international investments. The international markets all performed decent in 2014 when measured in local currency terms. However, due to the surge in the U.S. Dollar the return that we saw as U.S. investors was quite different. For example, the EAFE was positive 6.4% on the year in local terms, yet down 4.5% when converted back to dollars. Emerging Markets were up 5.6% in local terms, but down 1.8% in dollars. Japan's market was up 9.8% in local terms yet down 3.7% in dollars.

We believe in our investment philosophy and are worried for investors who choose to just benchmark to the S&P 500 going forward. We believe that your portfolio should look like a pizza with 10 slices of different flavors. In 2014 there were only two good performing slices: U.S. large Caps and Real Estate. Having the other 8 slices hurt performance. But that is not a reason to abandon the approach. It might be more important than ever to make sure you are diversified heading into 2015, as so many retail investors are suddenly only interested in one slice.

FINANCIAL PLANNING

There are a few changes in 2015 that you should be aware of. Some of the changes will allow you to save more while others may cost you more.

- If you have a 401(k) or 403(b) plan, you can now defer up to a maximum of $18,000 per year and the catch-up for those over age 50 is $6,000. This is a maximum $24,000 per year for those over 50!
- Income cutoffs for Roth contributions also increased to $183,000-$193,000 for married filing jointly and $116,000-$131,000 for single taxpayers.
- Contributions for Traditional and Roth IRAs did not change. They remain at $5,500 plus a $1,000 catch-up for those over age 50.
- The income limit for social security taxes has increased to $118,500 from $117,000 which means that an additional $1,500 is subject to the 6.2 percent tax.
- The cost-of-living (COLA) increase for 2015 social security benefits was 1.7% and will be reflected in the January payments. The monthly maximum at retirement increased to $2,663.

In the past, we have shared some popular mobile phone/ tablet apps that we either find beneficial, or simply just enjoy. Here are a few for you to try in 2015:

- **RunKeeper**: Use your iPhone’s GPS capabilites to track your jogging, walking or cycling routes and examine details of your pace and calories burned. This app is free on most platforms.
- **Dropbox:** Dropbox is an easy to use cloud based storage system for files, photos, music, movies and more. Create an account, upload and save the files, then access them from anywhere. This app is free on most platforms.
- **Trivia Crack**: If you enjoy playing trivia against friends, this is the app for you. The app has different categories and gets tougher as you go. The app is free on most platforms.

Company News

Alex Bunyan

Alex joined Galecki Financial Management in September of 2014. She works primarily as a Client Service Specialist. Alex graduated from Indiana University – Purdue University of Fort Wayne (IPFW) in May of 2014. Prior to joining GFM, Alex worked as a Patient Access Services Rep at Parkview Whitley Hospital.

In her spare time, Alex enjoys being outdoors. She likes to play basketball, golf, hunt and fish. Her favorite sports teams are the Dallas Cowboys, Cincinnati Reds and the Indiana Hoosiers.

Alex will be working with many clients over the next few years on their financial plans. We are very excited to have her on the team. Please welcome her when you see her.

- Galecki Financial Management Investment Committee

Special Note: If you would like to receive a color copy of this newsletter, or schedule an appointment with a financial planner, please visit www.galecki.com.