Third Quarter 2012

GALECKI FINANCIAL MANAGEMENT FINANCIAL SENSE

	LAST MONTH	LAST 3 MONTHS	YTD
S & P 500 Index	2.58 %	6.35 %	16.43 %
Russell Midcap Index	2.12 %	5.59 %	14.00 %
Russell 2000 Index	3.28 %	5.25 %	14.23 %
Dow Jones Industrial Average	2.75 %	5.02 %	12.19 %
Morgan Stanley EAFE Index	2.99 %	6.98 %	10.59 %
Barclays Aggregate Bond Index	-0.03 %	0.90 %	2.71 %

INDEX RETURNS

The third quarter of 2012 produced solid equity returns across virtually all asset classes. Following a second quarter slowdown in the markets, equities have pushed up to their highest level in four years. In fact, the S&P 500 is up roughly 113% since early 2009.

The S&P 500 was up 6.35% in the third quarter. Mid-cap stocks as measured by the Russell Midcap Index were up 5.59%. Small-cap stocks as measured by the Russell 2000 Index were up 5.25%. The Dow Jones Industrial Average was up 5.02%. International equities recovered nicely with the MSCI EAFE index up 6.98% and the Emerging Markets Index increasing 6.05%.

Bonds have cooled in the third quarter with the Barclays Aggregate Bond Index declining 0.03% in September. Global bonds performed much better with the Barclays Global Aggregate Bond Index increasing 3.28%.

ECONOMIC REVIEW AND OUTLOOK

The economy grew in the second quarter at an annualized rate of 1.3%. This follows the 2.0% growth rate in the first quarter of the year. The domestic economy continues to expand at a very sluggish pace. We believe that slower economic growth will be our new normal as we deal with significant government debt levels. According to www.usdebtclock.org, the current Debt to GDP ratio is 104.9% or $16.1 Trillion. Typically, countries with debt in excess of 90% see their economic growth slow dramatically.

The Index of Leading Economic Indicators rose 0.6% in September following a 0.4% decline in August and a 0.4% rise in July. This is an indication that the economy should continue to see slow economic growth. Industrial production rose 0.4% in September after having fallen 1.4% in August but remains 2.8% higher from a year ago.

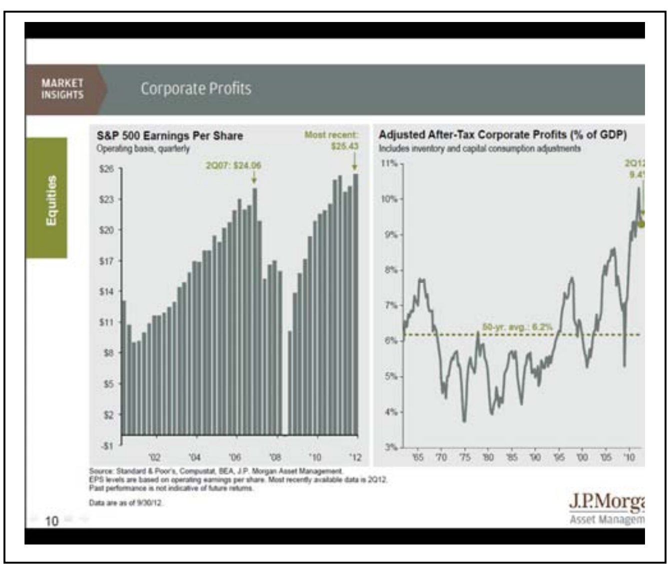
The labor market is improving. Weekly initial unemployment claims are below the key 400,000 level with the four week moving average at 365,500. ADP reported that private payrolls rose by 162,000 in September. The overall unemployment rate has dropped to 7.8%.

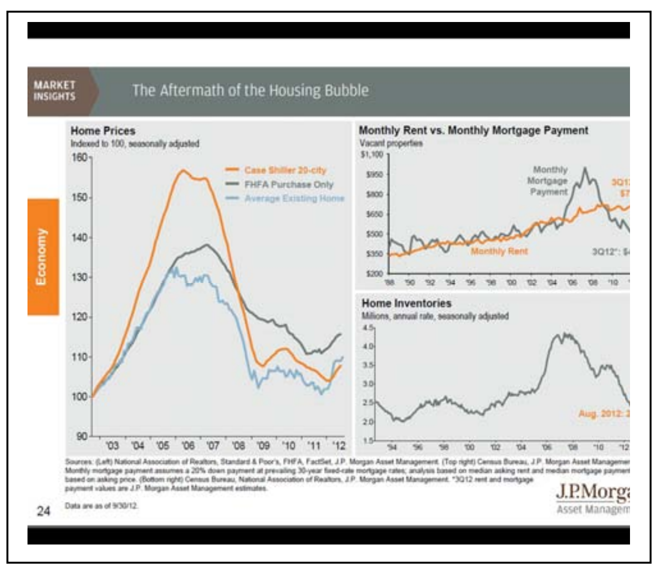
The ISM manufacturing index rose to 51.5 after being below the key 50 level for three months. The new orders component jumped 5.2 points to 52.3. The ISM Non-Manufacturing index came in at 55.1, up from 53.7, while new orders rose to 57.7.

U.S. corporations have been running very lean, and consumer demand has remained strong. Retail sales were up 1.1% in September and are 5.4% higher than a year ago. Second quarter earnings came in at $25.43 for the S&P 500 companies. In addition, corporations are sitting on $2.2 Trillion in cash waiting to be deployed when confidence rises.

Housing has continued its comeback in 2012. Housing starts in the U.S. surged 15 percent in September to the highest level in four years. Housing inventory has dropped dramatically which has caused home prices to increase. With low interest rates and minimal inventories, expect continued strength in this sector.

The fast approaching “Fiscal Cliff” could have a dramatic impact on the domestic economy. The expiring Bush Tax Cuts, AMT, Payroll Tax Cut, and the Automatic Enforcement cuts are expected to drop GDP by an estimated 3.9% at the beginning of 2013. With an economy growing at roughly 1.3%, this would pull our economy into contraction territory.





The European region continues to be a major concern. Most of the region appears to be in contraction territory. Spain is struggling to recover and may still require a bailout. Germany has been one of the few bright spots and yet just lowered their 2013 GDP forecast to 1% from 1.6%.

Emerging economies have shown some recent weakness. Chinaõs GDP in the third quarter dropped to 7.4%. However, their industrial production, retail sales, and fixed-asset investment accelerated in September. This should lead to a rebound in the fourth quarter.

U.S. exports account for roughly 9.8% of our Gross Domestic Product. Of the 9.8%, 1.4% is exported to the European region and 1.4% goes to the BRIC countries (Brazil, Russia, India and China). Although this is not an insignificant amount, it is clearly less than most developed economies and has enabled us to continue expanding while global GDP is slipping.

EQUITY AND BOND MARKETS

Stocks have had a strong run over the last few months. We stated in our second quarter newsletter that equities were ñpoised to move higher.ò Indeed the S&P 500 and EAFE index were both up by more than 6% for the quarter.

Stocks typically like to climb a ñwall of worry.ò With the upcoming Fiscal Cliff, U.S. Debt Ceiling, Eurozone debt crisis, and the U.S. election, there is plenty of uncertainty, if not worry. Although some investor sentiment surveys have moved higher (suggesting that a short-term correction is due since it is a contrarian indicator), the underlying sentiment is still negative. This is evidenced by the fact that $77 Billion has moved out of domestic equity funds and roughly $200 Billion has moved into bond funds through the first three quarters of 2012.

Since 1925, the S&P 500 has risen more than 12% during the first three quarters of the year 31 times according to Ned Davis Research (Oct. 2012). The median gain for the fourth quarter in those instances has been 4.9% and the S&P 500 has finished in positive territory 81% of the time in the fourth quarter. Although there is no guarantee that we will see comparable results in 2012, it is comforting to see this historical trend.

PORTFOLIO MANAGEMENT

Our move to reinvest the cash into mid-cap growth in June turned out to be a well-timed purchase. This new position is up more than 8% in just under four months. Our portfolio remains almost fully invested on the equity side with only a small 2% cash position. At this point, we believe short-term corrections will be met with additional purchases and the overall trend for stocks will remain higher.

The fixed income side of the portfolio has truly lifted overall returns. Our high yield bond funds are up roughly 15% on the year and global bonds are up more than 9%. We believe that our high yield bonds are getting expensive and you could see a reduction in this position in the next few months.

The Alternative portion of the portfolio has also seen impressive results. Specifically, the DFA Global Real Estate fund is up more than 18% year-to-date. We still believe in the long-term benefits of owning real estate in each portfolio.

We recommend that you review your overall equity and fixed income allocation to make sure it is appropriate for you given your risk tolerance and time horizon. Remember to keep a long-term focus and not worry about the short-term fluctuations.

GALECKI
FINANCIAL MANAGEMENT

FINANCIAL SENSE
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FINANCIAL PLANNING

The IRS announced that the maximum deferral amount for retirement plans in 2013 will be $17,500, up from $17,000 this year. However, the catch-up contribution (the additional amount for people over 50) remains unchanged at $5,500. Taxpayers will be able to gift $14,000 tax-free in 2013 up from $13,000 this year. In addition, social security recipients will receive a 1.7% increase in their benefits in 2013.

Donọt forget to take your Required Minimum Distribution from your retirement accounts by the end of the year. The penalty for not satisfying the proper withdrawal amount is 50%.

Remember to make a contribution to your Indiana 529 College Choice Direct Savings Plan before the end of the year to get your tax credit. Currently the state of Indiana offers a 20% state tax credit for contributions made to the plan, up to a maximum annual credit of $1,000 per tax return.

GALECKI NEWS

GFM Staff and family members completed our second annual 5K walk for Making Strides Against Breast Cancer on Team Becky on Saturday October 13. The weather was ideal, the discussions were enjoyable, but our pace was questionable. We might need to do some additional training for next yearọs walk.

There were 5,000 people that participated in the walk including 246 survivors. The walk raised $254,000 that will go to the American Cancer Society to help provide free resources and support to newly diagnosed women. GFM is proud to be a part of this great event and support our strong survivor, Becky.

- Galecki Financial Management Investment Committee