

HARBOR VIEWS

HARBOR ADVISORY QUARTERLY NEWSLETTER

Fall 2012



THOUGHTS ON THE ECONOMY

The economy grew 2.0% in the third quarter of this year which brings the year-to-date rate to 1.7%, the third consecutive year of slowing output. The jobs market continues to tread water, creating about 140,000 non-farm payroll jobs per month which does not keep pace with the expansion in the labor force.

There are however positive economic developments this year including autos and housing which represent over 20% of the economy when including suppliers and ancillary services. Auto sales are running at a rate of 14.5 million units this year, the third year of expansion, allowing our domestic manufacturers to record the best profits in North America in decades. Housing is finally stabilizing which has allowed residential real estate prices to rise in each of the last seven months and new home starts to reach the highest level since early 2008. The improvement in housing is healing banks' balance sheets and banks are recording healthy profits.

The slowing in Europe is beginning to take its toll on our exports which, along with the manufacturing sector, had been leading the economy during this recovery. Europe is now back in a mild recession. The ECB's decision to stand ready to purchase sovereign bonds to eliminate the 'non-credit related spread' in rates between countries in the EU has reduced higher risk sovereign bond yields over 1% since our last letter.

The continued explosion in U.S. energy production is truly a long term benefit to U.S. economic and earnings growth and will last many years.

The Chinese economy seems to have bottomed at 7.5% GDP growth this quarter. New leadership in China has been announced which will be followed by new, stimulative economic policies.

The U.S. will stay with divided government as the President was reelected and Republicans held a majority in the House. The focus has now shifted to dealing with four years worth of deferred and difficult decisions which all hit at the end of this year and are known as the Fiscal Cliff.

A LOOK INSIDE HARBOR VIEWS

- *Thoughts on the Economy* – The continued explosion in U.S. energy production is truly a long term benefit to economic and earnings growth...
- *Our View of the Financial Markets* – Equity prices will be volatile around the posturing but...will benefit from the confidence which would flow from a reasonable compromise.

LATEST NEWS FROM HARBOR ADVISORY

- You can visit us at: www.harboradvisory.com. Take a look and let us know your feedback.
- Jack De Gan continues to make news with his regular guest appearances on CNBC's top rated financial shows "Squawk Box", "The Call", "Closing Bell" and on Bloomberg TV, Fox Business News and National Public Radio.



We believe the country is ready to accept some bad tasting medicine and is ready to pay higher taxes and accept some spending cuts. A grand bargain along the lines of the Simpson-Bowles Agreement would go a long way to improving business and consumer sentiment and strengthen economic growth.

OUR VIEW OF THE FINANCIAL MARKETS

The U.S. equity markets were up nicely into the double digits at the end of October bringing valuations back into line with the last two years of earnings growth. Since the election however we have lost about half that advance as the two political factions again stake out extreme positions on dealing with the budgetary issues called the 'Fiscal Cliff'. We hope the two sides can both give a little and agree on a scheme that would raise taxes, cut spending and help stabilize the national debt. We cannot continue adding \$5 trillion to our national debt every four years!

Equity prices will be volatile around the posturing and negotiating. Ultimately stock prices will benefit from the confidence which would flow from a reasonable compromise.

Stocks remain one of the few places to earn a reasonable return as the 10-year Treasury Note now yields 1.5%. With inflation rates approaching 2% per year, much of the fixed income world provides a guaranteed loss of purchasing power. We remain optimistic that capital will flow back into equities as the bond market deflates, our economy normalizes, and interest rates rise to historically normal levels.

Still, 2013 will be an interesting year for stocks as the first year of the presidential cycle is historically the lowest of the four in terms of share performance.

CHANGE IN THE LINEUP

After 35 years our stalwart leader, Joan Gordon, has decided to relinquish her title as office manager. To many of our clients Joan is the go-to person when you absolutely, positively, need it done and done right. Many of you are known to her just by the sound of your voice on the phone. You have two reasons to rest easy. First, Jan Yeaman who joined Harbor 7 years ago, has assumed this critical role and is excellent at her job. Armed with a CPA, a long history in the investment business pre-Harbor, and supported by longtime employee Cheryl Crowley, Jan is more than up to the task. Second, Joan will be at Harbor on a reduced weekly schedule and will surely keep us all in line. A quick calculation of time in grade for all Harbor employees reveals a startling average of 22 years tenure. However, we remain young at heart.

We provide a safe harbor for individuals and families in New England...

Most of Harbor Advisory's new clients come through referrals from our existing clients or from industry professionals who know us and how we work.

All of us at Harbor Advisory value these referrals as the greatest compliment our small, independent firm could receive.

If you know an individual or family who is seeking counsel and might appreciate sound, personalized investment advice and financial services, we would welcome the opportunity to meet with them.



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REFI AGAIN

Over many years we have recommended clients take advantage of the low interest rates if they have outstanding mortgage debt. At the risk of redundancy...if you, a child, a relative, or a friend have a mortgage...run...do not walk...to determine if you can benefit from locking in today's historically low interest rates. Thorough debt management can be **just as** effective as good asset management to promoting one's financial health.

TAX REPORTING REMINDER

This year again all custodians will supply capital gain and loss information to their clients on Form 1099. They will issue these by February 28th. Don't forget that K-1's may not be mailed until March 15th. These are necessary for filing tax returns so it pays to wait for these before you file.

HOLIDAY GIFT

In lieu of sending Holiday cards this December, Harbor Advisory will be making a gift to The New Hampshire Charitable Foundation. This Foundation has been working to improve the quality of life in New Hampshire communities since 1962. In view of the outpouring of need in our difficult economic times we are proud to help our community.

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Nod to the ubiquitous disclaimer:
While we're not infrequently, and always quite accurately, accused of being of strong opinion – we want to let the reader know we've been wrong before, we will be again, but please don't hold it against us. The forward looking parts of the letter are the best efforts of fallible humans working at Harbor Advisory.