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# HC FINANCIAL ADVISORS, INC.

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## Economic Outlook Presentation to Sons in Retirement

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March 27<sup>th</sup>, 2013

# S&P 500 Index at Inflection Points

Equities



Source: Standard & Poor's, First Call, Compustat, FactSet, J.P. Morgan Asset Management.

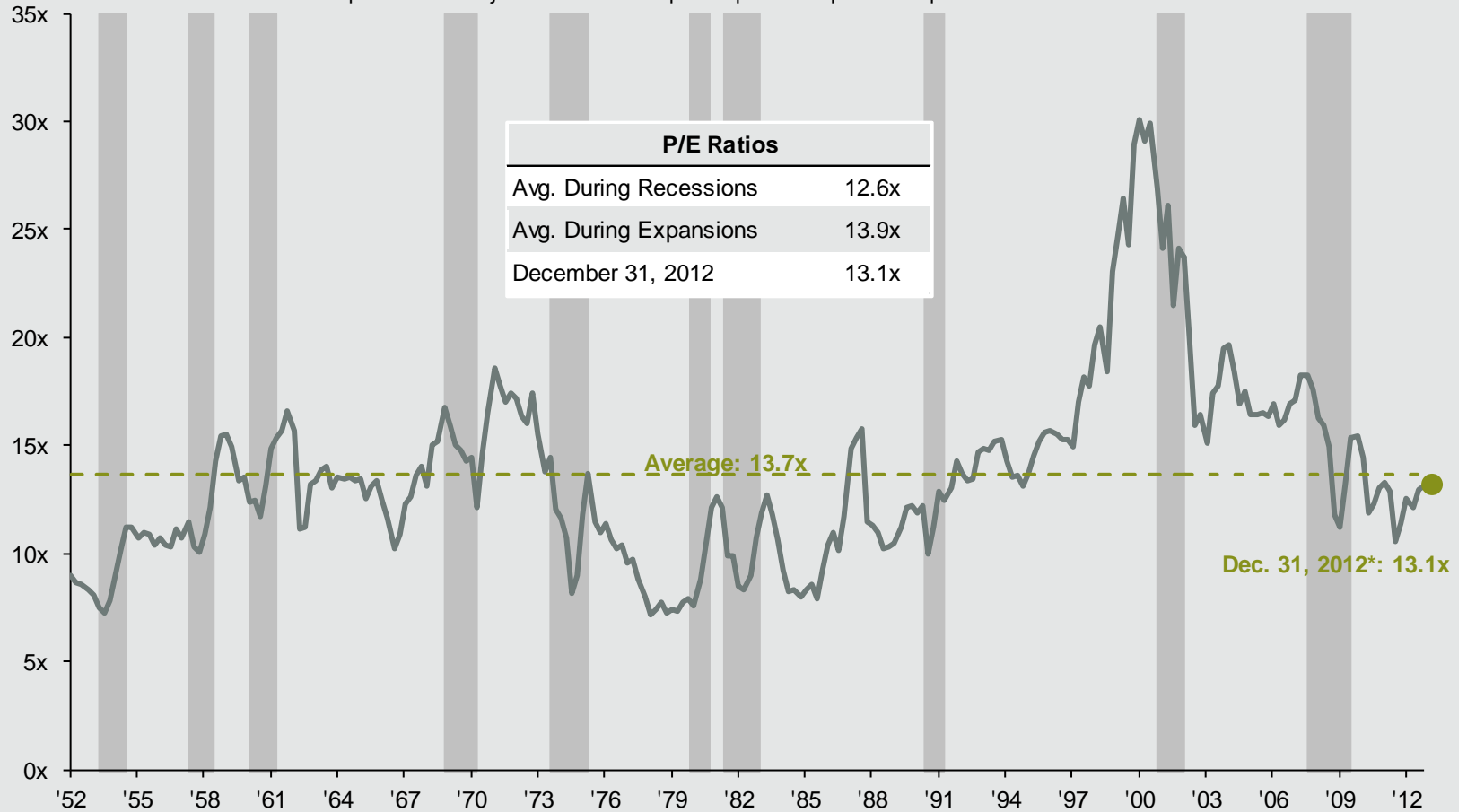
Dividend yield is calculated as the annualized dividend rate divided by price, as provided by Compustat. Forward Price to Earnings Ratio is a bottom-up calculation based on the most recent S&P 500 Index price, divided by consensus estimates for earnings in the next 12 months (NTM), and is provided by FactSet Market Aggregates. Returns are cumulative and based on S&P 500 Index price movement only, and do not include the reinvestment of dividends. Past performance is not indicative of future results.

Data are as of 12/31/12.

# Broad Market Lagged Price to Earnings Ratio

## Lagged P/E Ratio – All U.S. Corporations

Ratio of market value of all U.S. corporations to adjusted after-tax corporate profits for prior four quarters



Source: BEA, Federal Reserve Board, Wilshire Associates, J.P. Morgan Asset Management.

\*The December 31, 2012 price is a J.P. Morgan Asset Management estimated based on the daily value of the Wilshire 5000 Total Market Index.

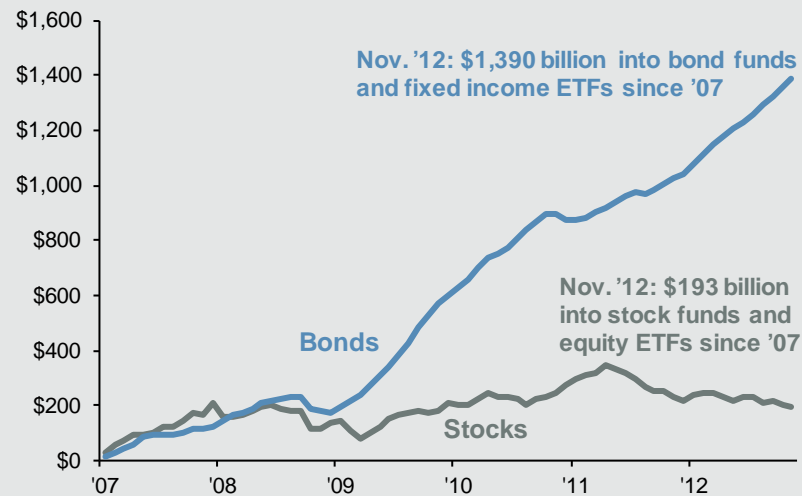
Data are as of 12/31/12.

# Mutual Fund Flows

Billions, USD	AUM	Fund Flows														
		YTD 2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
<b>Domestic Equity</b>	4,290	(130)	(132)	(81)	(28)	(148)	(65)	(0)	18	101	120	(26)	55	261	176	149
<b>World Equity</b>	1,562	7	4	58	28	(80)	139	149	106	71	24	(3)	(22)	53	11	8
<b>Taxable Bond</b>	2,832	244	136	230	311	22	97	45	26	5	40	125	76	(36)	8	59
<b>Tax-exempt Bond</b>	590	53	(12)	11	69	8	11	15	5	(15)	(7)	17	11	(14)	(12)	15
<b>Hybrid</b>	980	46	30	24	10	(26)	42	18	37	49	38	9	9	(36)	(14)	10
<b>Money Market</b>	2,617	(77)	(124)	(525)	(539)	637	654	245	62	(157)	(263)	(46)	375	159	194	235

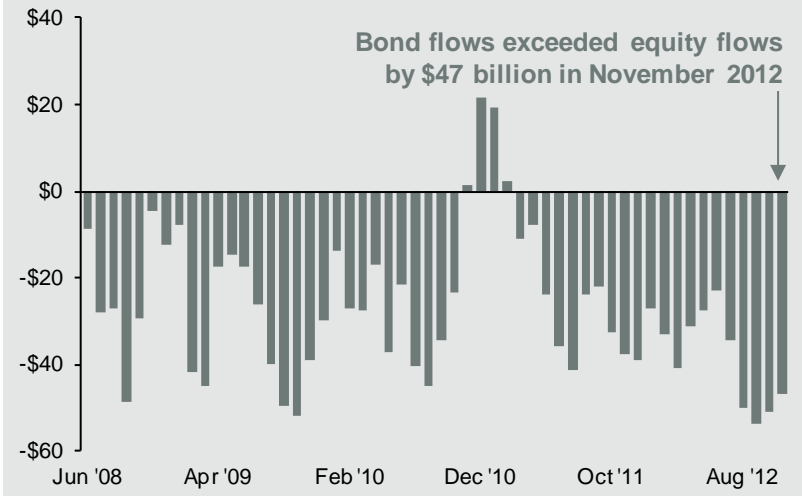
## Cumulative Flows into Stock & Bond Funds

Includes both mutual funds and ETFs, \$ billions



## Difference Between Flows Into Stock and Bond Funds

Billions, USD, U.S. and international funds, monthly



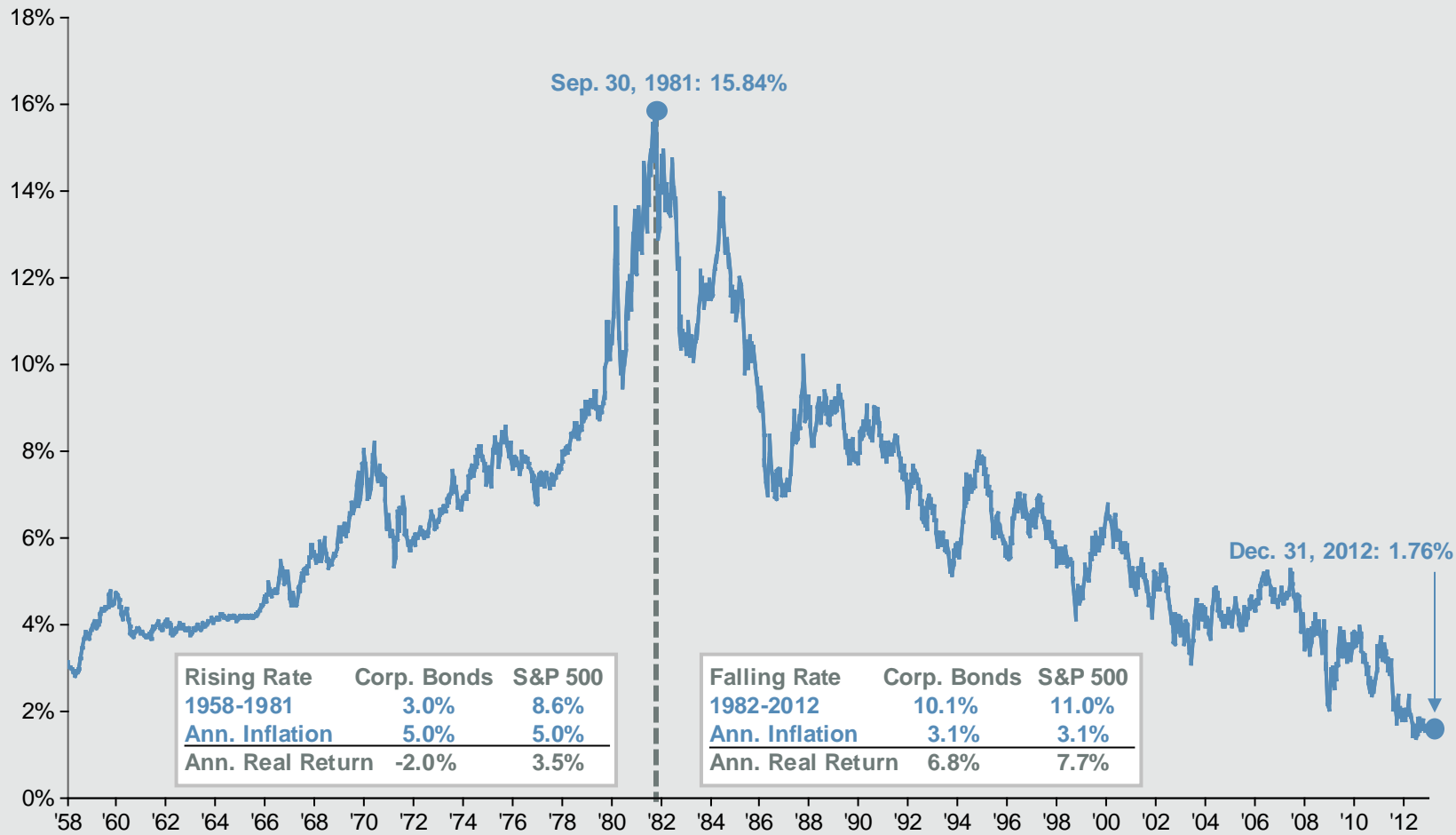
Source: Investment Company Institute, J.P. Morgan Asset Management.

Data include flows through November 2012 and exclude ETFs. ICI data are subject to periodic revisions. World equity flows are inclusive of emerging market, global equity and regional equity flows. Hybrid flows include asset allocation, balanced fund, flexible portfolio and mixed income flows.

Data are as of 12/31/12.

# Interest Rates and Market

10-Year Treasury Yields and Real Capital Market Returns



Source: Federal Reserve, Standard & Poor's, BLS, Strategas, J.P. Morgan Asset Management.

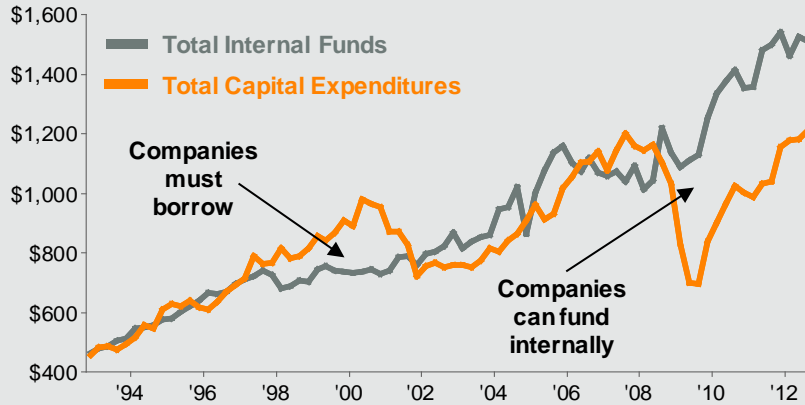
All returns above reflect annualized total returns, which include reinvestment of dividends. Corporate bond returns are based on a composite index of investment grade bond performance.

Data are as of 12/31/12.

# Corporate Finances

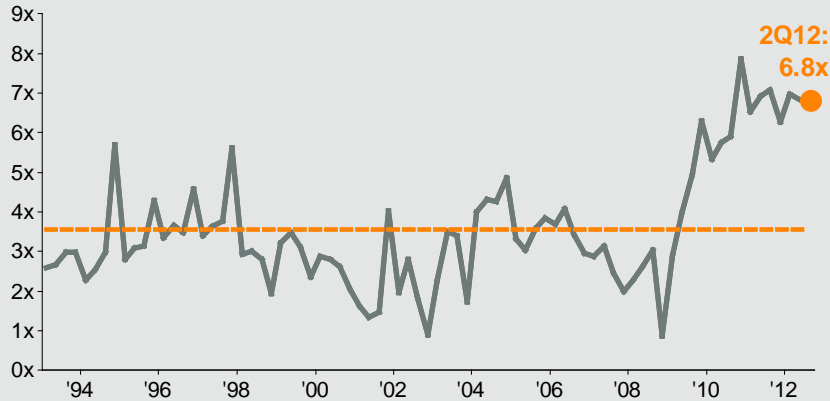
## Corporate Financing Gap

Nonfarm nonfinancial corporate business, billions USD



## Interest Coverage Ratio (EBIT / Net Interest)

S&P 500, quarterly



## Total Leverage

S&P 500, ratio of total debt to total equity, quarterly



Source: Federal Reserve, Compustat, Standard & Poor's, FactSet, J.P. Morgan Asset Management.

(Top Left): All data is from the Fed's Flow of Funds tables report Z.1, F.102 lines 9 and 11. Total internal funds equals retained earnings plus depreciation.

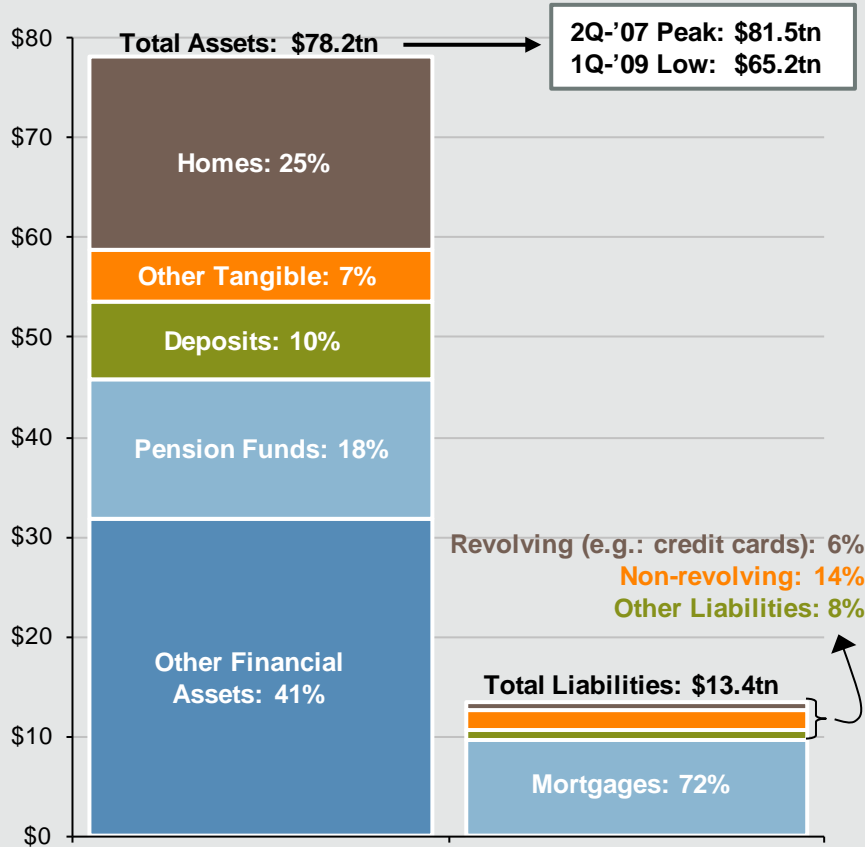
Data are as of 12/31/12.

# Consumer Finances

Economy

## Consumer Balance Sheet

Trillions of dollars outstanding, not seasonally adjusted



## Household Debt Service Ratio

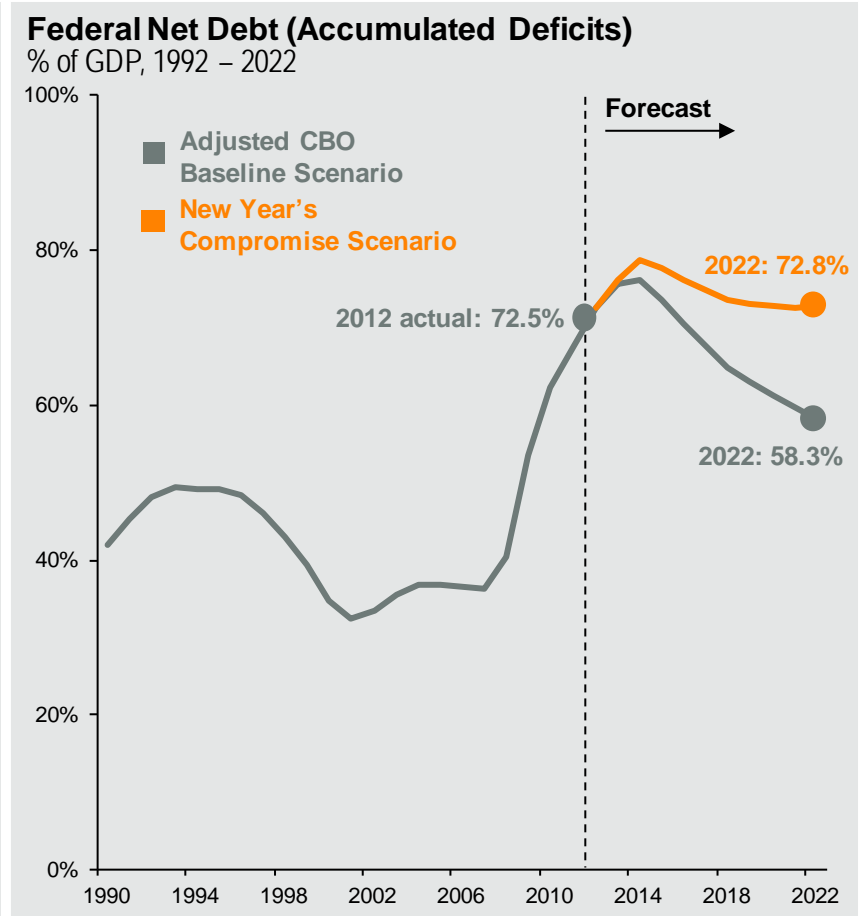
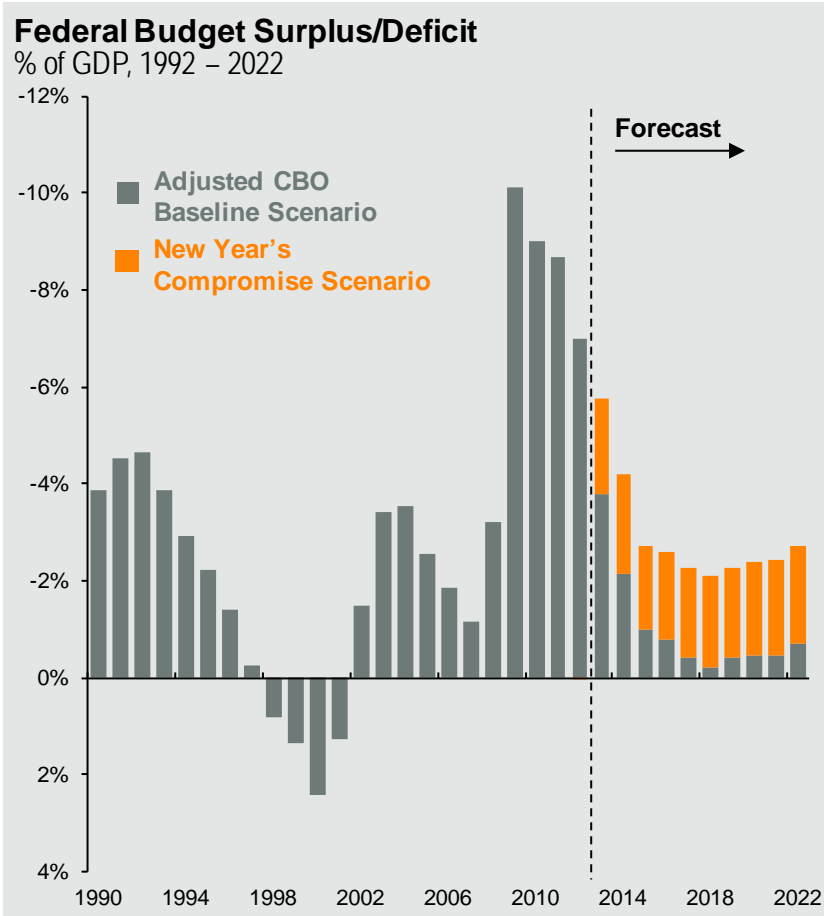
Debt payments as % of disposable personal income, seasonally adjusted



Source: (Left) FRB, J.P. Morgan Asset Management. Data includes households and nonprofit organizations. (Right) BEA, FRB, J.P. Morgan Asset Management. \*4Q12 Household Debt Service Ratio is a J.P. Morgan Asset Management estimate.

Data are as of 12/31/12.

# Federal Finances: Deficits and Debt



Source: U.S. Treasury, BEA, CBO, J.P. Morgan Asset Management.

2012 numbers are actuals. Note: Years shown are fiscal years (Oct. 1 through Sep. 30). Chart on the left displays federal surplus/deficit (revenues – outlays). Federal net debt comprises all financial liabilities of the Federal government (gross debt) minus all intra-government holdings as assets. Deficit and debt scenarios are based on CBO budget forecasts from August 2012 and the CBO cost estimate for the American Taxpayer Relief Act, as passed by the Senate on January 1, 2013.

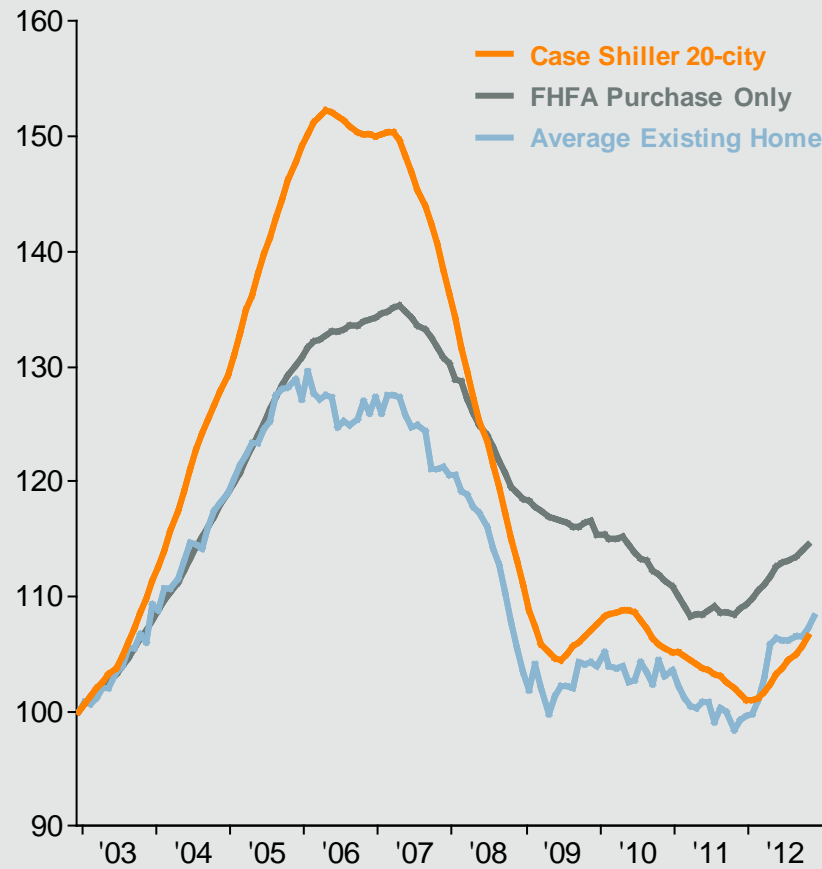
Data are as of 12/31/12.



# The Aftermath of the Housing Bubble

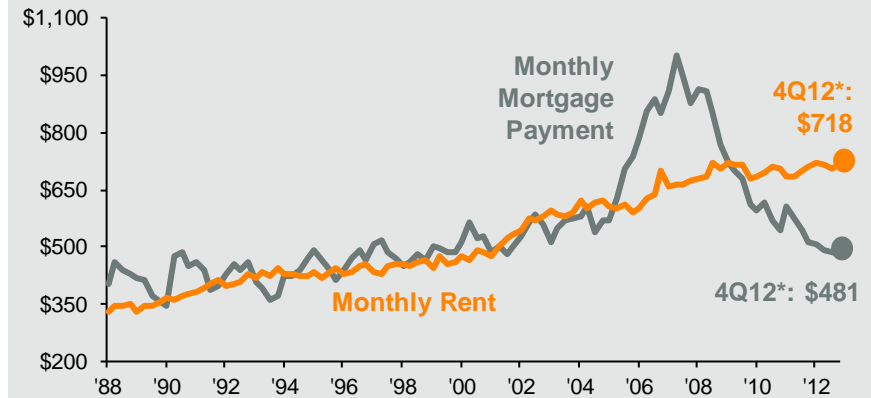
## Home Prices

Indexed to 100, seasonally adjusted



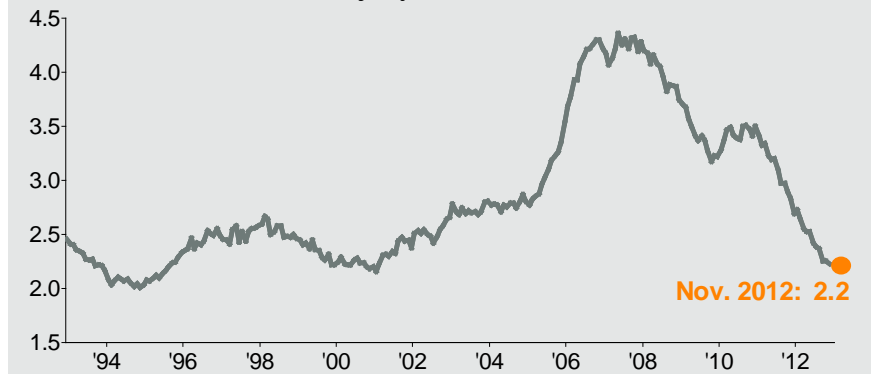
## Monthly Rent vs. Monthly Mortgage Payment

Vacant properties



## Home Inventories

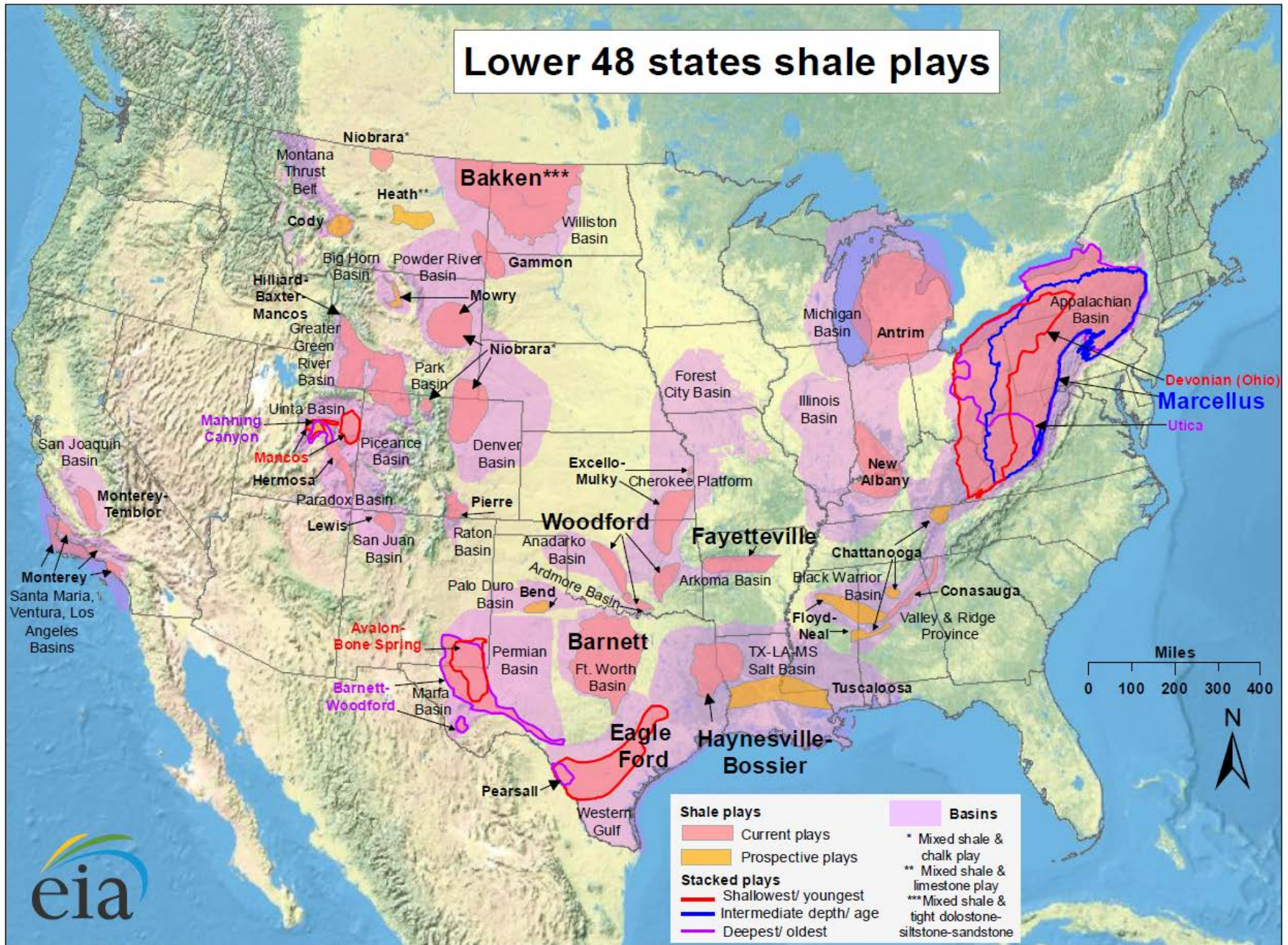
Millions, annual rate, seasonally adjusted



Sources: (Left) National Association of Realtors, Standard & Poor's, FHFA, FactSet, J.P. Morgan Asset Management. (Top right) Census Bureau, J.P. Morgan Asset Management. Monthly mortgage payment assumes a 20% down payment at prevailing 30-year fixed-rate mortgage rates; an analysis based on median asking rent and median mortgage payment based on asking price. (Bottom right) Census Bureau, National Association of Realtors, J.P. Morgan Asset Management. \*4Q12 rent and mortgage payment values are J.P. Morgan Asset Management estimates.

Data are as of 12/31/12.

# Lower 48 states shale plays

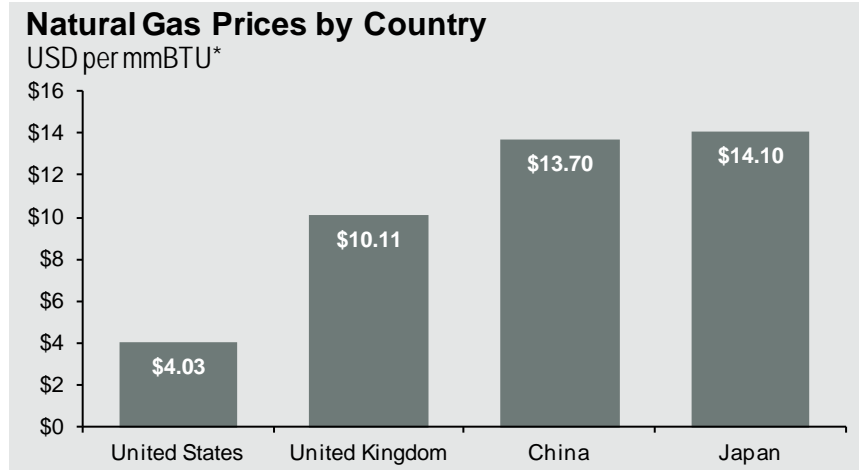
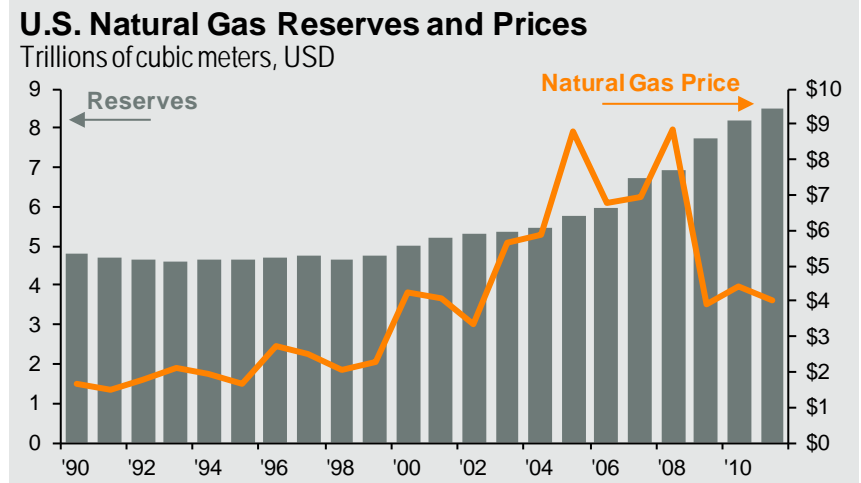
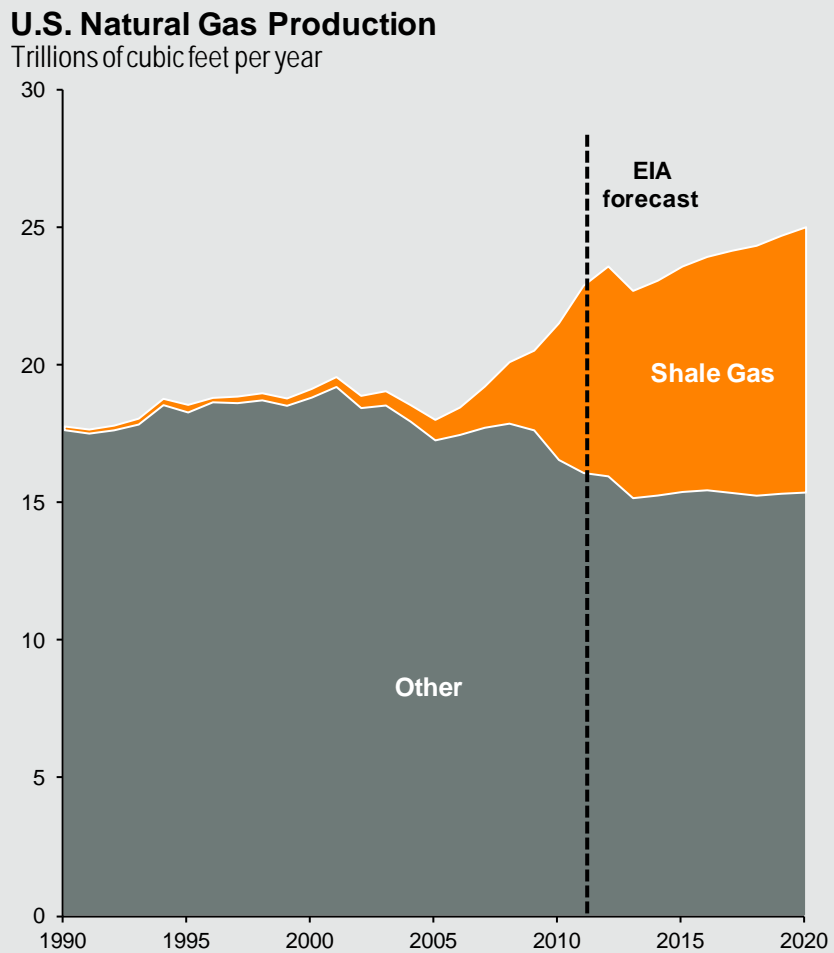


Source: Energy Information Administration based on data from various published studies.  
 Updated: May 9, 2011



# Domestic Natural Gas

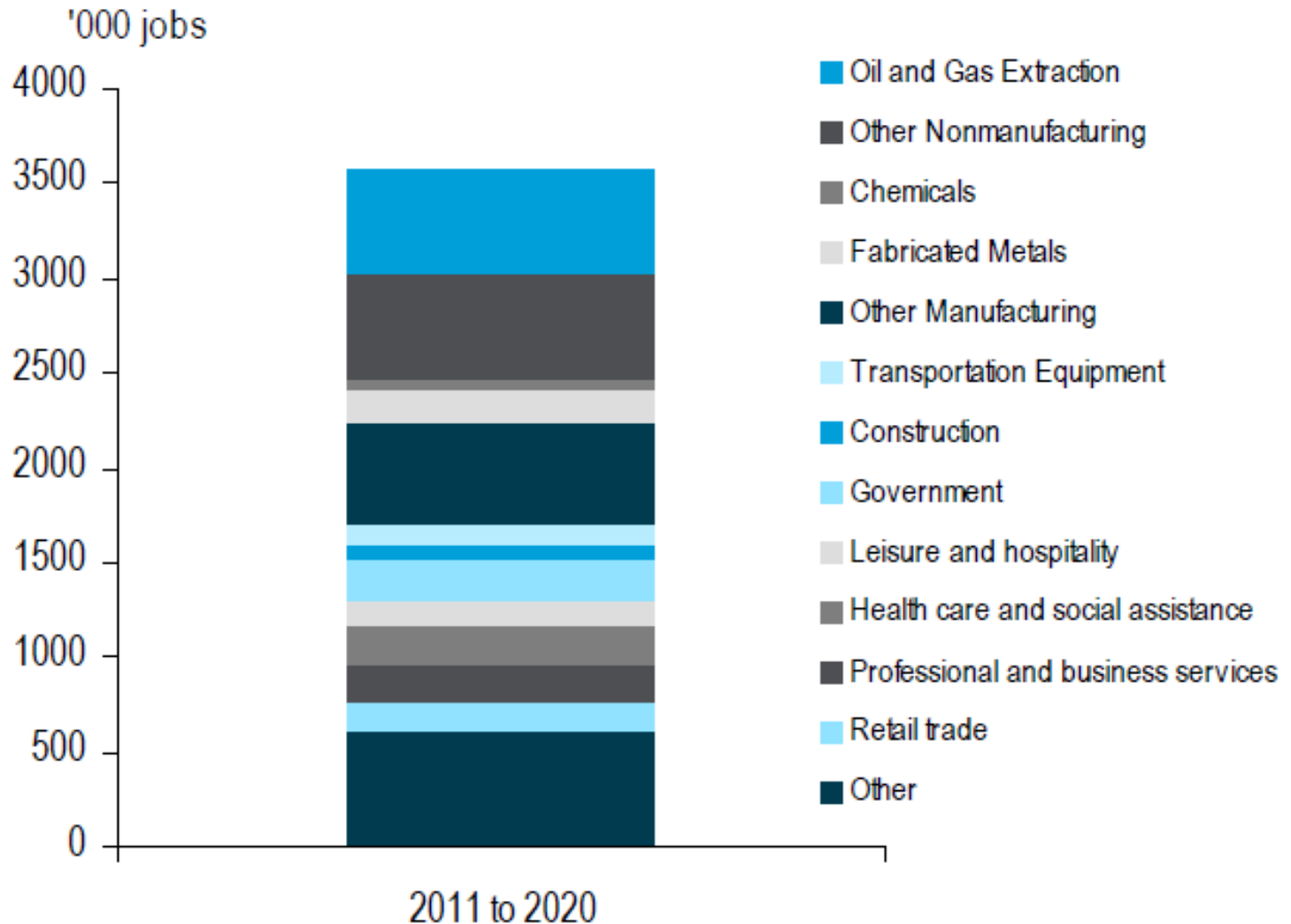
Economy



Source: EIA, BP, Federal Energy Regulatory Commission, J.P. Morgan Asset Management.  
\*mmBTU represents 10,000 million British thermal units.

Data are as of 12/31/12.

Domestic Energy: Impact on U.S. Employment is estimated to be approximately 3.6 million new jobs.



# European Crisis: Sovereign Bond Yields

## European Sovereign Funding Costs

10-year benchmark bond yields, daily



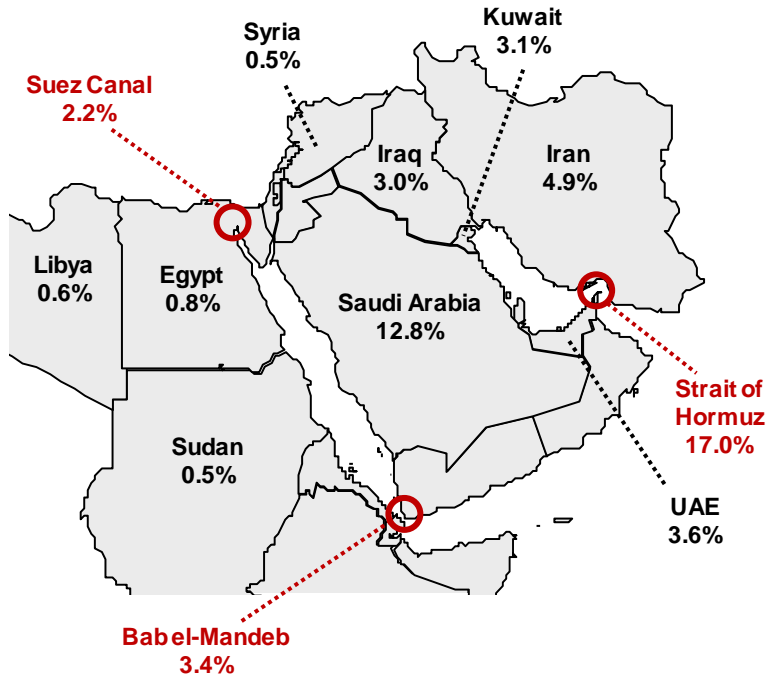
Source: FactSet, ECB, J.P. Morgan Asset Management.

Data are as of 12/31/12.

# Global Oil Supply

## Middle East Energy Production & Chokepoints

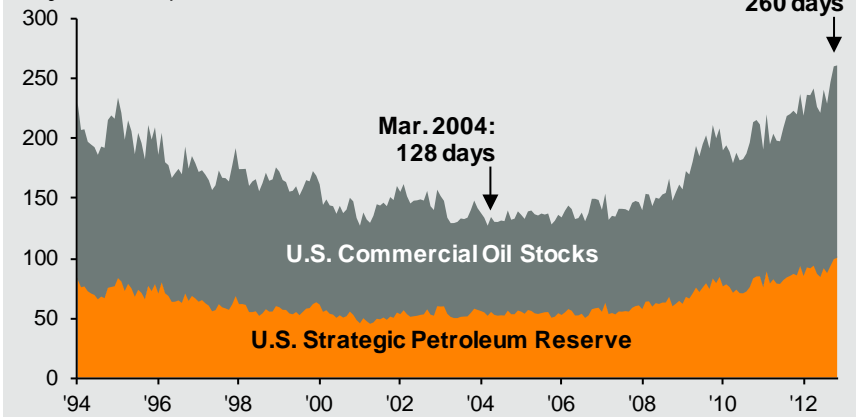
Percent of global liquid fuel production, 2011



Major Producers				Major Consumers			
Percent of global total, 2011				Percent of global total, 2011			
Saudi Arabia	13%	China	5%	United States	22%	India	4%
Russia	12%	Iran	5%	China	10%	Saudi Arabia	3%
United States	12%	Canada	4%	Japan	5%	Brazil	3%

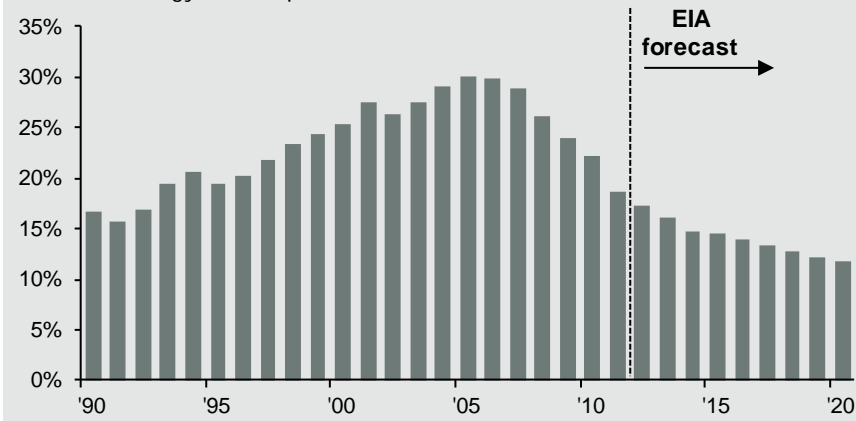
## U.S. Commercial & Strategic Oil Stocks

Days of net imports



## Total U.S. Energy Net Imports

% of total energy consumption



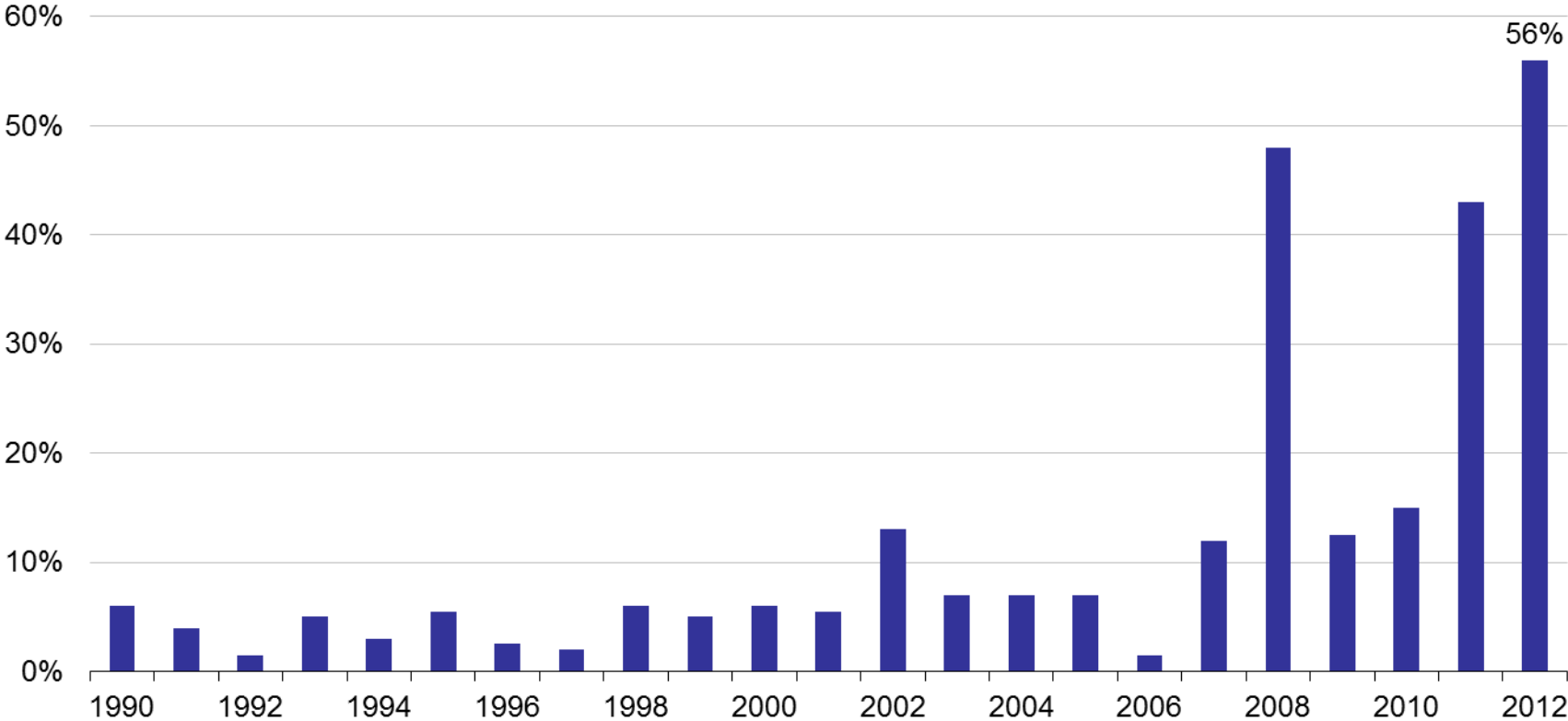
Source: EIA, J.P. Morgan Asset Management.

Forecasts are from the EIA Annual Energy Outlook 2013. Imports are mostly crude oil, petroleum and natural gas while consumption includes oil, gas, coal, nuclear, hydropower and bio-fuels.

Data are as of 12/31/12.

Equities are also an attractive source of income.

**Percentage of S&P 500 Stocks with Dividend Yields Greater than the 10-Year U.S. Treasury Yield**



Past performance is no guarantee of future results. You can not invest directly in an index. Index performance is not meant to represent performance of any Fidelity Advisor fund.

Source: Strategas

# Example: AT&T vs. McDonald's

**March 21, 2003**

## **AT&T**

Stock Price = \$21.64

Dividend = \$1.36

Earnings Per Share = \$2.56

Payout Ratio = 53%

Yield =  $\$1.36/\$21.64 = 6.3\%$

## **McDonald's**

Stock Price = \$14.65

Dividend = \$0.39

Earnings Per Share = \$1.15

Payout Ratio = 34%

Yield =  $\$0.39/\$14.65 = 2.7\%$



# Example: AT&T vs. McDonald's

**2003 - 2013**

## **AT&T**

Ten Year Average EPS Growth = -0.2%

Ten Year Average Dividend Growth = 2.82%

## **McDonalds**

Ten Year Average EPS Growth = 17.5%

Ten Year Average Dividend Growth = 22.8%

# Example: AT&T vs. McDonald's

**March 21, 2013**

## **AT&T**

Stock Price = \$36.15

Estimated 2013 Earnings per Share = \$2.51

Expected 2013 Dividend = \$1.80

Yield =  $\$1.80/\$36.15 = 5.0\%$

## **McDonald's**

Stock Price = \$98.53

Estimated 2013 Earnings per Share = \$5.78

Expected 2013 Dividend = \$3.08

Yield =  $\$3.08/\$98.53 = 3.1\%$

# Example: AT&T vs. McDonald's

## **Yield on 2003 Investment**

$$\text{AT\&T} = \$1.80 / \$21.64 = 8.3\%$$

$$\text{McDonalds} = \$3.08 / \$14.65 = 21.0\%$$

# Example: AT&T vs. McDonald's

## **AT&T**

Dividends \$14.98

Appreciation \$14.51

Return =  $\$29.49 / \$21.64 = 136.3\%$

## **McDonald's**

Dividends \$15.21

Appreciation \$83.88

Return =  $\$99.09 / \$14.65 = 676.4\%$

# Where Are The Next Dividend Growers?

## Technology

Qualcomm

Current Yield = 1.5%

Current Payout = 30%

Trailing 10 Year Dividend Growth = 19.8%

Estimated 5 Year Earnings Growth = 15.0%

Apple – Implemented a dividend last year

Current Yield = 2.3%

Current Payout = 24%

Estimated 5 Year Earnings Growth = 15.1%

# Fixed Income Yields and Returns

U.S. Treasuries	# of issues	Mkt. Value	Avg. Maturity	Yield		Return	
				12/31/2012	12/31/2011	2012	4Q12
2-Year	} # of issues: 169 Total value: \$5.209 tn		2 years	0.25%	0.25%	0.31%	0.05%
5-Year			5	0.72	0.83	2.29	-0.01
10-Year			10	1.78	1.89	4.13	-0.23
30-Year			30	2.95	2.89	2.34	-1.28
<b>Sector</b>							
Broad Market	8,109	\$16,973 bn	7.0 years	1.74%	2.24%	4.22%	0.22%
MBS	805	5,027	4.8	2.22	2.68	2.59	-0.20
Corporates	4,435	3,651	10.6	2.71	3.74	9.82	1.06
Municipals	46,472	1,343	13.6	2.17	2.82	6.78	0.67
Emerging Debt	580	860	11.0	4.34	6.07	17.95	3.29
High Yield	2,013	1,145	6.7	6.13	8.36	15.81	3.29
TIPS	33	861	8.9	1.51	1.69	6.98	0.69

Source: U.S. Treasury, Barclays Capital, FactSet, J.P. Morgan Asset Management.

Fixed income sectors shown above are provided by Barclays Capital and are represented by – Broad Market: U.S. Barclays Capital Index; MBS: Fixed Rate MBS Index; Corporate: U.S. Corporates; Municipals: Muni Bond Index; Emerging Debt: Emerging Markets Index; High Yield: Corporate High Yield Index. TIPS: Treasury Inflation Protection Securities (TIPS). Treasury securities data for # of issues and market value based on U.S. Treasury benchmarks from Barclays Capital. Yield and return information based on Bellwethers for Treasury securities.

Change in bond price is calculated using both duration and convexity according to the following formula:  

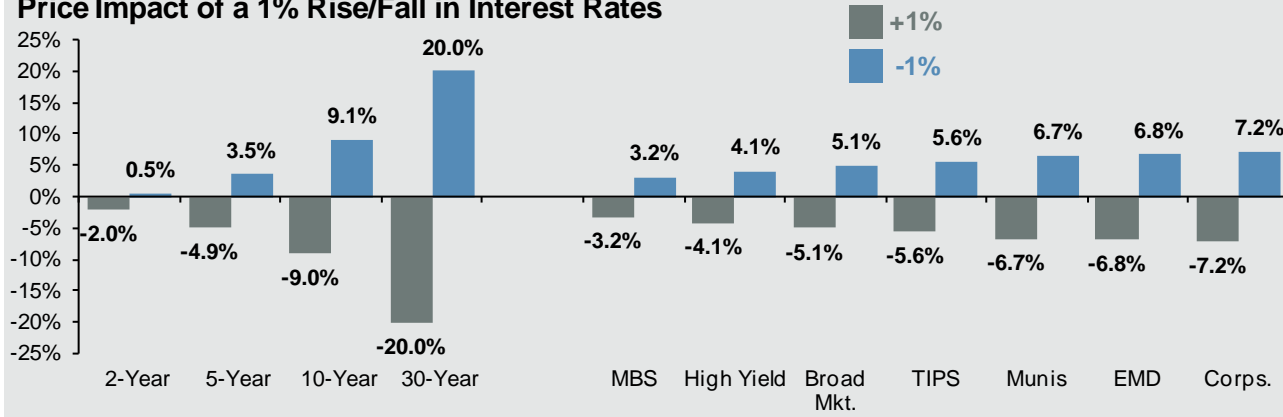
$$\text{New Price} = (\text{Price} + (\text{Price} * \text{-Duration} * \text{Change in Interest Rates})) + (0.5 * \text{Price} * \text{Convexity} * (\text{Change in Interest Rates})^2)$$

\*Calculation assumes 2-year Treasury interest rate falls 0.25% to 0.00% and the 5-year Treasury falls 0.72% to 0.00%, as interest rates can only fall to 0.00%.

Chart is for illustrative purposes only. Past performance is not indicative of comparable future results.

Data are as of 12/31/12.

Price Impact of a 1% Rise/Fall in Interest Rates



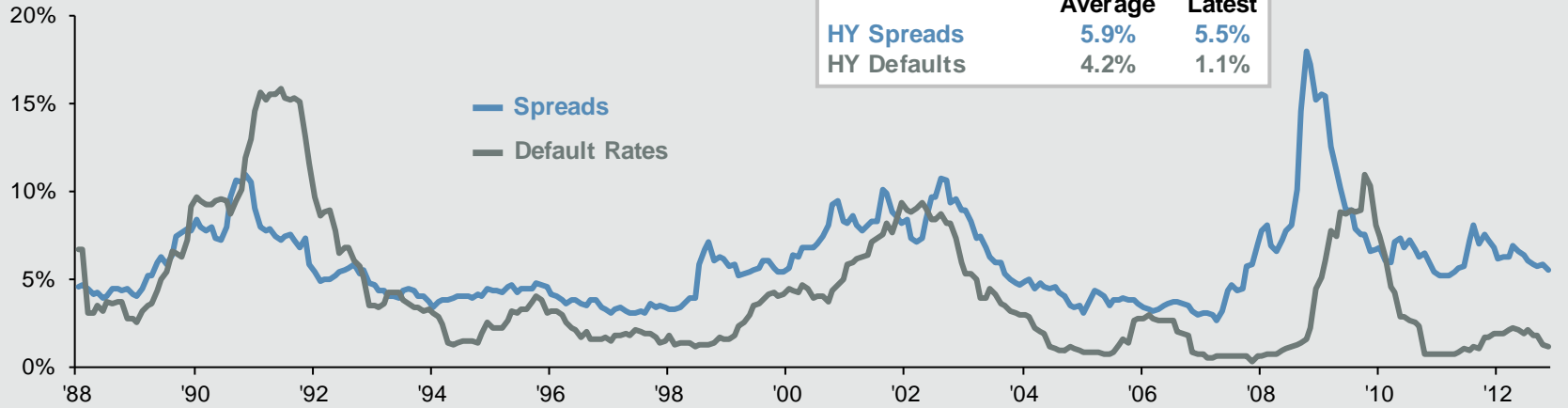
# Bond Ladder

## CORPORATE BONDS

20,000	Comwlth Edison 7.5% 7.500% Due 07-01-13	113.30	22,659.20	101.73	20,345.52	0.5	7.500	1,500.00	7.4
15,000	Verizon New England 4.75% 4.750% Due 10-01-13	105.89	15,883.17	102.24	15,335.67	0.4	4.750	712.50	4.6
15,000	Goldman Sachs Group Inc FFE Use 38 5.250% Due 10-15-13	107.54	16,131.15	102.23	15,335.07	0.4	5.250	787.50	5.1
10,000	Cleveland Electric Note 5.650% Due 12-15-13	97.17	9,717.00	103.48	10,348.09	0.3	5.650	565.00	5.5
10,000	Staples 9.750% Due 01-15-14	110.60	11,060.00	107.00	10,700.00	0.3	9.750	975.00	9.1
15,000	Pepsico Inc 3.750% Due 03-01-14	106.58	15,987.60	103.08	15,461.83	0.4	3.750	562.50	3.6
10,000	Vodafone Group 4.15% 4.150% Due 06-10-14	105.96	10,596.10	104.14	10,414.49	0.3	4.150	415.00	4.0
20,000	JP Morgan Chase 5.125% 5.125% Due 09-15-14	108.24	21,648.80	106.08	21,215.52	0.6	5.125	1,025.00	4.8

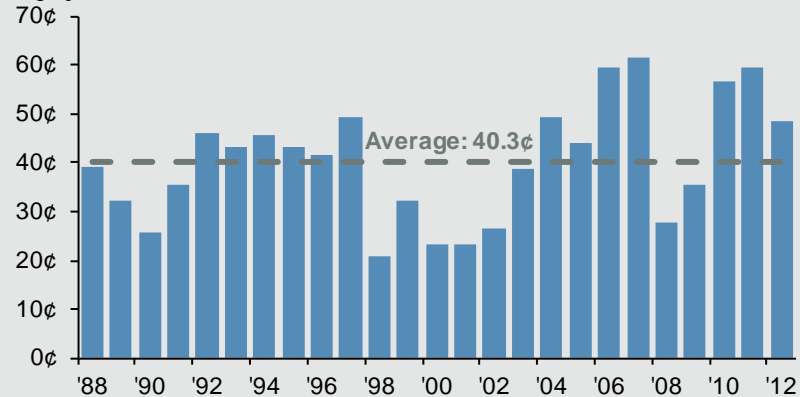
# High Yield Bonds

## High Yield Spreads and Defaults



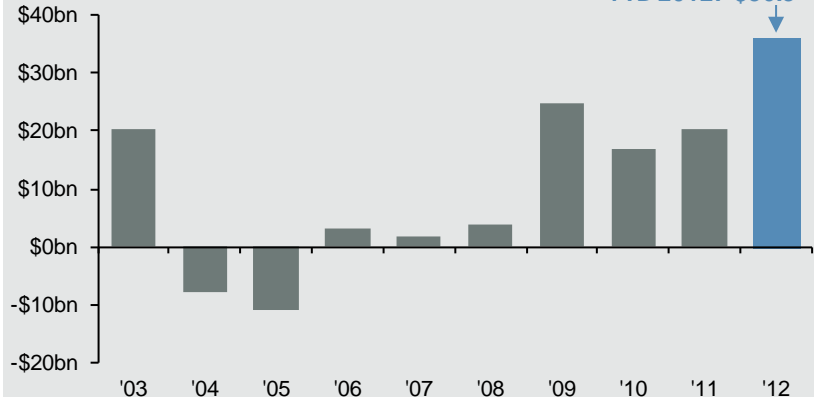
## Historical High Yield Recovery Rates

High yield bonds, cents on the dollar



## Annual Flows into High Yield Mutual Funds & ETFs

Billions USD



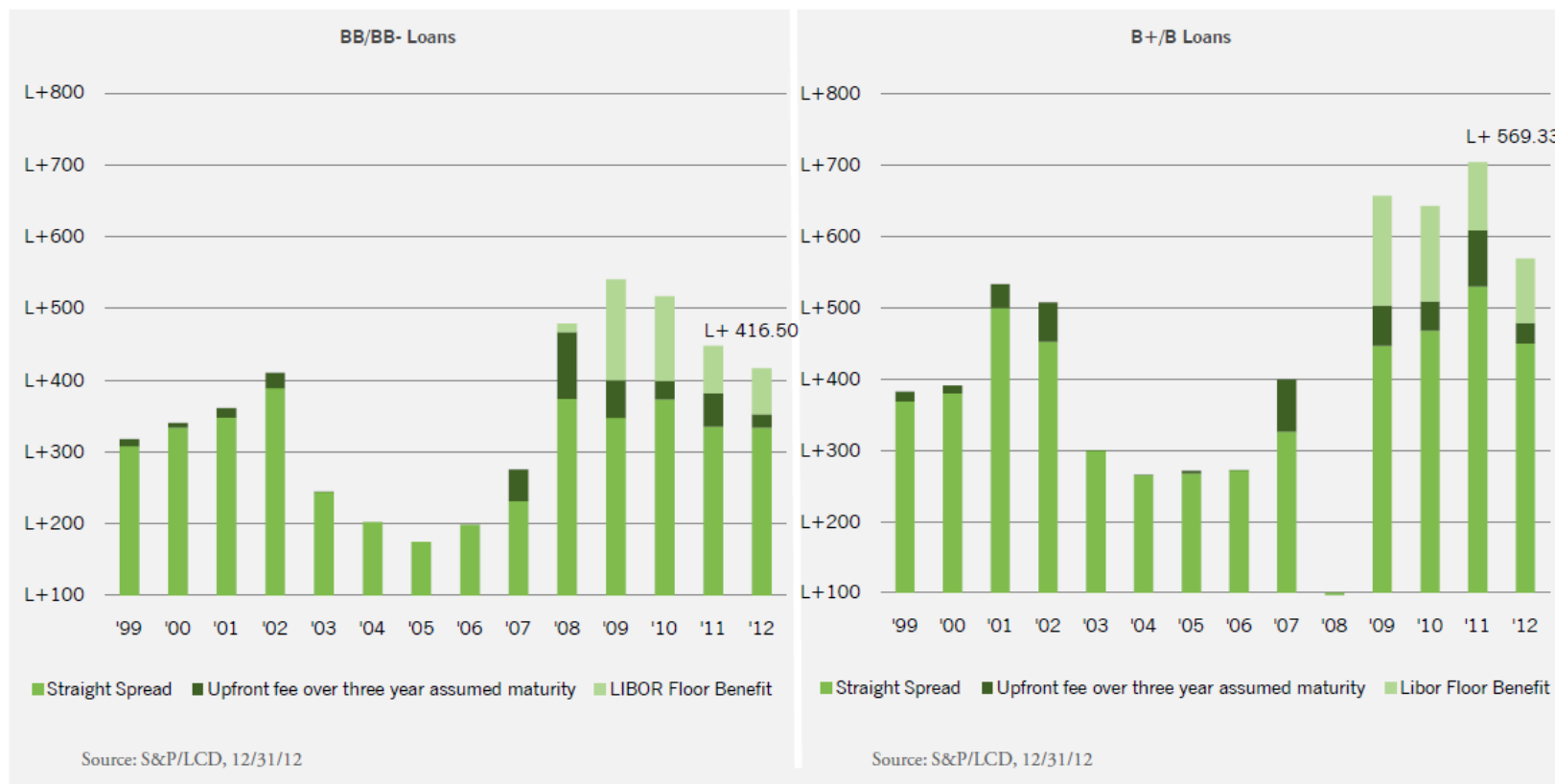
Source (Top chart): U.S. Treasury, J.P. Morgan, J.P. Morgan Asset Management. Default rates are defined as the par value percentage of the total market trading at or below 50% of par value and include any Chapter 11 filing, prepackaged filing or missed interest payments. (Bottom left): J.P. Morgan, J.P. Morgan Asset Management. (Bottom right): Strategic Insight, J.P. Morgan Asset Management. Yield to worst is defined as the lowest potential yield that can be received on a bond without the issuer actually defaulting and reflects the possibility of the bond being called at an unfavorable time for the holder. Spreads indicated are benchmark yield to worst less comparable maturity Treasury yields. 2012 recovery rate is a year to date number as of November 30, 2012. Flows include ETFs and are as of November 30, 2012. Past performance is not indicative of comparable future results. Data are as of 12/31/12.





# All-In Primary Market Spreads

No longer L+250 bps; More than double the historical spread for same fundamental risk



Data provided is for informational use only. Past performance is no guarantee of future results. It is not possible to invest directly in an Index. See end of report for important additional information. Assumes upfront fee is amortized evenly over an assumed three-year life; Upfront fee includes original issue discount. As of 10/5/06 LCD began using Corporate Credit Ratings by S&P and Corporate Family Ratings by Moody's for rated spread and fee calculations. Straight spread is the fixed nominal spread paid by issuers over the floating base rate. Up-front fees generally refer to original issue discounts (OID) paid by the issuer as a form of yield enhancement. LIBOR floor benefit refers to the incremental spread paid above reported LIBOR.