FAIRPORT ASSET MANAGEMENT
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The Compass

Wealth management tips, trends and articles that provide confident navigation for high net worth clients.

December 2014
Happy Holidays! During this season of thanksgiving, we would like to express our gratitude to Fairport's clients and friends. Whether you are a long-time client or you have started working with us this year, it is our privilege and honor to serve as your financial advisor. From the entire Fairport team, thank you for your continued trust, loyalty and generous referrals.

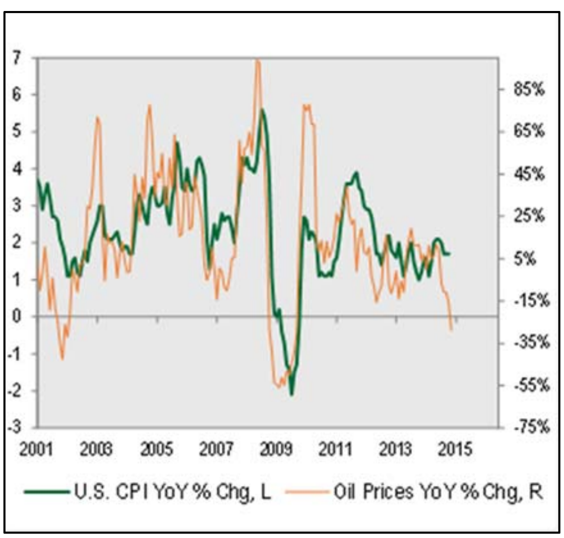
As always, we encourage you to share this newsletter with friends, family members and colleagues.

Mid-Quarter Commentary as of December 3, 2014

By John M. Silvis, CFA
Chief Investment Officer

As we enter the final month of 2014, the equity markets are again poised to finish the year with solid returns, building on the foundation of the previous two years. Through November, the S&P 500 Index has logged a total return of 13.95% while the global benchmark, the MSCI All Country World Index, registered a total return of 6.21% through month end. It wasn't without some recent drama as capital markets reacted to softer economic numbers here in the U.S., slower global growth led by China and what was then a the growing threat of Ebola. From the peak in October to the trough on November 16th, the S&P 500 Index declined -9.8% before rebounding. As we have pointed out over the last few quarters, corrections are to be expected and should be viewed as a normal part of a long term secular bull market.

After a rocky start to the year, the U.S. economy continues to pick up steam with Gross Domestic Product (GDP) growing 3.9% on an annualized basis in the third quarter of the year. This added to the previous growth in the second quarter of 4.6%. The economy should improve as we head into 2015 with the consensus of economists surveyed by Bloomberg forecasting growth of just over 3%. The closely watched unemployment rate continues to decline with the most recent reading falling to 5.8%, indicating that the employment picture is improving and job creation is rising.



The real story of the last few weeks has been the steady drop in oil prices and how that will affect the economy going forward. Oil tends to have a negative effect on inflation (see chart) leading the Consumer Price Index (CPI) by several months. This reinforces our belief that inflation will be well-contained in the coming year and stay below the Federal Reserve's long term target of 2%. With gasoline prices declining, consumers will have more disposable income which should be a positive driver for the economy in 2015.

Global monetary policy will take center stage in the coming months as central banks around the world take steps to shore up their slowing economies. Unlike the U.S. where the Federal Reserve is likely to raise the Federal Funds rates sometime next year (the consensus is at midyear around the June FOMC meeting), the rest of the world is likely to continue down the path of easier monetary policy. Japan continues to expand their monetary policies (increase quantitative easing) to help aid their anemic economic growth while European Central Bank (ECB) is setting the stage to embark on a more aggressive monetary policy that will likely include some fashion of QE. China again cut interest rates and likely will do more in the coming months to try and prop up their own slowing economy. The success of these efforts will likely determine how strong the global economic growth outside the U.S. will be in the next few years.

Earnings of companies within the S&P 500 Index have remained strong throughout the year. The recently completed third quarter reported growth of nearly 10% over the same time last year. Utilities have been the best performing sector as investors flock to the high dividend yield. On the flip side the energy sector, driven by the 35% drop in oil prices, has been the worst performing sector within the benchmark. Energy is an area we have been underweight, as supply in the U.S. coupled with the declining demand in China should put pressure on oil prices for some time. However, multiples remain stretched within Utilities and valuations are rich for the sector. Health Care and Technology have outperformed as well so far this year and valuations are still attractive. We continue to favor cyclical over the more defensive sectors as the economy should continue to improve and the consumer benefits from lower energy prices. We remain biased to the higher end of the capitalization curve favoring large over small cap.

We started the year favoring domestic equity markets over international markets and remain committed to that view as we head into 2015. Europe is struggling with the onset of deflation, China is continuing to cope with slower growth and Russia is feeling the economic effects of the economic sanctions coupled with lower oil prices. Some areas could be bright spots such as Mexico which will benefit from its strong ties to the U.S. markets and India which is adopting more market friendly reforms.

Final Thoughts: Seasonal strength should be a tailwind for the equity markets in the coming months. 2015 will be the third and best year of the 4-year presidential cycle. The third year (2015) has been positive every year since 1948 with a median return of 17.1%. Not to be outdone, years ending in the number “5” have seen positive equity returns every year since 1928 with an average return of 25.3%.

Fixed Income Commentary as of December 5, 2014
By Rick D’Amico, CFA
Manager of Investments

After reaching an intraday low of 1.86% on October 15th, the 10-year Treasury yield seems to have settled into a trading range between 2.20% and 2.50%. At today’s current rate of 2.30%, yields are down some 70 basis points from where we began the year, providing a significant tailwind for most fixed sectors in 2014. The Barclays U.S. Aggregate Index has returned a respectable 5.57% year-to-date. Within the Index, the long Treasury bond sector has returned an impressive 20.73%, while U.S. corporate bonds and agency mortgage backed securities have returned 6.87% and 5.79%, respectively. Looking outside of the Aggregate, the Barclays U.S. High Yield Index has returned a disappointing 3.06% year-to-date. The high yield sector has been negatively impacted by technical factors, such as outflows, along with recent stress in the energy sector. Energy issuers currently comprise 15.2% of the Barclays U.S. High Yield Index.

Looking ahead to 2015, fixed income investors remain focused on both the timing and pace of potential interest rate increases by the Federal Reserve. A gap currently exists between FOMC Fed funds rate projections and market expectations, with the Fed expecting both an earlier lift-off (June vs. September) and a faster pace of tightening (150 bps per year vs. 80 bps per year) than the market. As the lift-off date moves nearer, this gap should narrow and it is our view that market expectations will eventually gravitate higher towards Fed rate forecasts. What does this mean for fixed income performance in 2015? Historically, most bond sectors tend to produce modest negative returns in the 3 months prior to the first rate hike, but typically recover any losses by the following 6 months. Since 1980, high yield and emerging market bonds have provided the most attractive returns in periods of Fed funds rate increases. In our view, we believe we are also likely to see a flattening of the yield curve. Short-term rates tied to economic and policy expectations are likely to move higher, while the longer end of the curve, affected by factors such as low global yields, flight-to-quality flows and foreign demand, stays relatively range-bound.

Building Family Legacies Through Philanthropy
By Janet Havener
Director of Wealth Advisory Services

As a society, we are wealthier than previous generations. Families of wealth expect to pass their assets on to their heirs in an efficient manner while minimizing taxes and hoping for family harmony. How can we at Fairport help our clients prepare themselves and their heirs for transitioning their wealth? Our major role as a wealth planner is to utilize proactive planning for clients who want to employ their wealth as a means to make a lasting impression on society, community and future generations.

The true heart of wealth planning is translating a client's goals and family values into a comprehensive wealth management plan. This is accomplished by taking into consideration such issues as longer life spans, higher rates of divorce, generational differences, rapidly rising health care costs, volatility in the market, uncertainty associated with world affairs, personal security and changing tax laws. Discussions with the clients about their values, principles and virtues will help them focus and obtain a thorough understanding of their goals, objectives and charitable intentions that can be translated into a multi-generational wealth management plan.

Open discussions with younger generations about wealth, legacy issues, goals, objectives, philanthropy, etc. are essential to ensure that they are prepared to eventually take on the responsibility of the family wealth. A strong financial education is the cornerstone of preserving family wealth and it is important that the younger generations understand the framework of the wealth management plan.

Many clients recognize that they have a financial responsibility to themselves as well as their heirs. They feel that their objective is to bequeath to their children sufficient resources for them to pursue their own goals and objectives and to equip them for the responsibility of handling family wealth. But, when asked "How much is enough to pass on to your heirs?" they will often respond, "Well everything, of course." They believe there is no other answer loving parents could give. But is this really what the client wants? Warren Buffet's famous quote "to bestow upon your children enough wealth that they will feel they can do anything, but not so much that they might choose to do nothing" becomes an integral part of the discussion.

Clients can be shown through a comprehensive wealth management plan how they can take care of themselves, their heirs as well as have wealth left over for charitable gifting and feel comfortable about it. As part of the overall plan, the topic of how your charitable giving will affect your future financial security, your non-charitable financial goals and your overall estate plan is addressed. When clients feel completely secure that they are going to be able to maintain their lifestyle and ride out any kind of emergency as well as provide for their heirs, the question is then asked "What do you want to do with what is left?" Generally, the answer is charitable giving. This is the point where philanthropy is discussed and where the fun begins.

It is absolutely critical to spend a substantial amount of time with clients to discover where their passions lie, what is really important to them, help them think through the primary virtues upon which they have built their lives, what core values they might like to transfer to future generations and how they might effectively do so—by showing clients how they can change the world in significant ways by effectively concentrating their remaining time, unique talents and accumulated treasures in areas that are important to them. To accomplish this, discussions about matters beyond financial statements and legal documents are essential—the human side of the equation. Clients are encouraged to speak about their hearts, souls, dreams and desires and to think about the charitable organizations that have touched their lives from earliest childhood until today. Most clients are amazed at just how many charitable organizations have actually had an influence on their lives and their family's lives over the years. They become excited over the possibility of creating something that will remain, prosper, grow and endure.

Next, discussions with clients regarding how to use philanthropy to build/rebuild family unity are incorporated. Often times, clients and their families are scattered throughout the country or the world. How can clients keep their families socially and emotionally together in this dynamic global society? Without some overriding purpose or commonality, family members can and often do go for extended periods of time never visiting or communicating. By introducing a philanthropic mission, families can be brought to higher levels of unity, cooperation and meaningful fellowship.
Also, by concentrating on the lives and needs of others, the entire family is sharing in a philanthropic mission which can be the glue that holds the family together from generation to generation and the lens that keeps them focused on a central,

common family goal. As time passes, senior generations are encouraged to mentor and coach the younger generations to continue with the family legacy.

The joy of giving can only be learned through personal experience; it cannot be learned academically. In order to truly discover the joy of giving, one must make a gift. Giving is addictive and the more a person gives, the more giving one wants to do, and the healthier and happier one becomes.

Practice Group Spotlight on Family Business Owners
By Andrew R. Connors, CFP®, CEPA
Partner & Business Owner Practice Group Leader

Could you be the boss of your relatives? Our survey found that 44% of family businesses have never or rarely do performance reviews for family members. Find out ways to better manage the "family" part of a family business by checking out our thought paper.

It would be our pleasure to present our survey findings to your group. Contact Andrew directly about speaking engagements at andrew.connors@fairportasset.com or (216) 431-2754.

Fairport News
Fairport employees frequently present at and attend conferences, educational seminars and informational webinars on new strategies and industry trends relating to the wealth management needs of our clients. From investment management to client service to technology, read more about the conferences we've recently attended.

Andrew Connors was one of the key presenters at the annual Cleveland Foundation continuing education conference where he presented *Aligning Family Business Values and Value*.

Pete DeVito, **Chris Isabella** and **Emily Shacklett** attended the Ernst & Young conference on Thought Leadership for Private Businesses with Generational Wealth in November.

Pete DeVito, **Chris Isabella**, **Tom Seifert** and **Emily Shacklett** attended the Smith and Condeni Estate Planning Seminar in October.

Heather Ettinger presented to American Heart Association's Circle of Red on the growing influence of women's wealth and philanthropy. **Heather** also attended the annual Schwab Impact conference in Denver in November as well as the Schwab Advisory Services Advisory Board meeting in September.

Janet Havener, with **Heather Ettinger**, presented Solutions for Women™ to the Intown Club in October.

Chris Isabella and **Rachel Margulis** attended the OSCPA Financial Planning Conference at the beginning of October. **Chris** also participated in the OSCPA Ethics Webinar later that month.

John Silvis kept current on investment strategies and trends by attending Schwab Impact and the Midwest Investment Conference.

Newsletter Disclosures
This newsletter represents an assessment of the economic and market environment at a specific moment in time and is not intended to be a forecast of future events or any guarantee of future results. It is for informational purposes only and should not be relied upon as research or investment/financial planning/tax advice. It should not be considered as a solicitation or recommendation by Fairport to buy, sell or continue to hold securities or other investments. Past performance is not a guarantee of future results, and is not indicative of any specific investment. It should not be assumed that the investment process and strategy discussed herein has been or will prove to be profitable. Diversification and strategic asset allocation do not assure profit or protect against loss in declining markets.