

# Third Quarter 2011 Client Newsletter

## Yanni & Associates Investment Advisors, LLC

### Review of the Markets:

	<u>3Q11</u>	<u>2011</u>
S&P 500	-13.87%	-8.68%
S&P Mid-Cap	-19.88%	-13.02%
S&P Small-Cap	-19.83%	-13.79%
Morgan Stanley's EAFE (International Stocks)	-18.95%	-14.62%

**Economy** – Overall, GDP growth during the middle of 2011 has remained anemic. GDP growth for the first quarter had a second consecutive estimate reduction from 1.8% to 0.4%. Recently, second-quarter GDP was revised upwards from 1.0% to a modest 1.3%. The September unemployment rate was flat at 9.1%. However, on an encouraging note, the other employment report featuring Non-Farm payrolls for September rose 103,000 (forecast 65,000), following a revised 65,000 increase in August (originally flat) and a revised 127,000 increase in July (originally 85,000). The private sector has very much led the way. While we are encouraged by these figures, we still believe the employment situation in the U.S. will take many years to get back to more sustainable figures. Inflation continues to remain tame with the CPI being 3.8% year-over-year.

**Equities** –As we stated in our last quarterly report, **YAIA shifted to an underweight stock position for its second time in history on July 8<sup>th</sup> for all of our clients. The timing of our shift indeed turned out to be beneficial as the stock market had a significant drop shortly afterwards. On August 12<sup>th</sup>, we reversed this move, investing into large-cap growth equities whereby also shifting to neutrally weighted positions within growth and value stocks.** Following this July stock market correction, the Dow Jones Industrial Average has hovered between 10,600 – 11,600. We continue to be cautious and believe the stock market may stay in this side-ways volatile “trading-range” for the next few weeks unless the following issues exhibit signs of improvement:

1. Continued concern with Greece's (and other European countries) budgetary issues and the corresponding European banks that hold a large portion of the country's debt. A few weeks ago, we thought it was inevitable that Greece would default on its debt. However, it does appear that other stronger European Union (E.U.) countries are opposed to this happening. Recently, German Chancellor Angela Merkel and French President Nicholas Sarkozy indicated they will deliver a plan to recapitalize European banks and address the Greek debt crisis at the November 3<sup>rd</sup> Group of 20 Summit. With this recent announcement and other related news, we have become much more optimistic that the E.U. will fix the European banking crisis, which may remove the cap on the “trading-range” on the stock market.
2. Domestic unemployment continues to remain at high levels. The Federal Reserve is taking extraordinary measures in order to keep interest rates at low levels attempting to “stimulate” the economy; it appears that few options remain for our government's monetary policy tactics. As we have stated before, higher-skilled work-force's (those with four-year degrees) unemployment remains well below 9%.
3. We are about a year away from the next presidential election. As we get closer to the 2012 presidential election, we are forecasting more political gridlock and additional headline focus on the U.S. economy and unemployment situation. Ultimately, these ongoing debates may place a ceiling on the stock market and may stretch out this “trading-range” scenario for the upcoming months.

**Fixed Income** – The panic in the stock market in the last quarter led to a “flight-to-quality” as investors invested heavily into Treasuries. Bond yields fell to historic levels; the average 30-year mortgage rate is now below 4% for the first time in history. While this may help stimulate the economy a bit, we are just not convinced that lower interest rates alone will bring jobs back to the unemployed. If someone does not have a job, how can they afford to buy a home even during this attractive low interest rate period? At some point, interest rates are going to rise and we are very concerned with this leading to a “bond recession”. We have thus positioned a portion of our fixed-income assets to hedge against this scenario.

## Yanni & Associates Investment Advisors, LLC Firm Update:

Mark has continued to become integrated with YAIA. He has been meeting many of our clients through the charity golf outings we support, as well as those who have come in for recent face-to-face meetings. He met the rest of our clients through email introductions as he coordinated our annual calendar effort. In addition to his contributions at YAIA, Mark has maintained a 4.0 GPA in the M.B.A. program at Robert Morris University.

Compliance updates: Per the new government regulations, we have filed our “new” ADV Part II and will be sending that to clients. The government required that document to be re-written in a “plain English format”. YAIA did not make any significant changes to its ADV Part II. Additionally, as a part of our ongoing compliance commitment, I will be attending two seminars in October (the annual Pittsburgh Compliance Symposium and the PA Securities Commission Symposium in Harrisburg, which occurs every three years)

Yanni & Associates Investment Advisors, LLC recent quotes in various publications:

- *Pittsburgh Post Gazette, Markets Staggering After Day of Huge Losses, Len Boselovic, August 9, 2011*

### Current 2011 Portfolio Recommendations:

- On July 7<sup>th</sup>, we shifted our client’s assets to an **underweight stock position relative to bonds** in relation to their customized portfolio structures. Then, on August 12<sup>th</sup>, we reversed that position moving back into stocks (mainly large cap growth stocks).
- Within equities, we shifted to neutrally-weighted “**value**” stocks relative to “**growth**” stocks.
- Within equities, we remain **overweight** “**small/mid**” capitalization stocks relative to “**large**” capitalization stocks.
- Within equities, we remain **underweight international stocks relative to domestic stocks**.
- Within fixed-income, we maintain our overweight to shorter maturity/duration vehicles, while focusing on high-grade corporate bonds and FDIC insured certificates of deposit. We continue to believe that long-term inflation is going to rise and the Federal Reserve will take actions to tighten monetary policy. We also remain very cautious that a rising interest rate environment could be detrimental to the bond market.
- While we continue to strongly encourage a diversified portfolio of more traditional securities, we do invest in niche areas as well, based on our views of the economy. A few of our “niche” type investments include:
  1. A “Bullish Dollar” exchange-traded fund (ETF) – We believe at some point inflation is going to rise, forcing the government to raise interest rates, which should increase the value of the dollar. We also continue to have concerns with budgetary issues in some European countries, which may put weakness on the Euro. This position performed well acting as a hedge during the third quarter.
  2. High Yield Bond ETF – We do not believe the economy is heading into a double-dip recession; therefore high-yield bonds and their attractive coupons may prosper during the upcoming months.
  3. Treasury Inflation Protected Securities (TIPS) – Our expectations continue to be that inflation will start to rise at some point in the upcoming years.

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