# Pettinga Insights and Outlook

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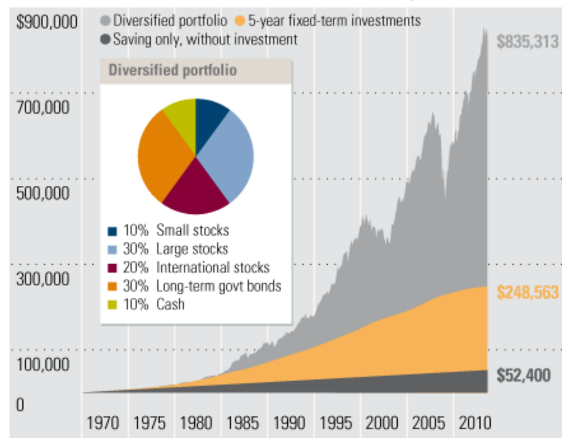
## Saving Is Not Enough

After two financial crises occurring almost back to back during the “lost decade,” investors have every right to be risk-averse, hesitant, angry, or distrustful. The problem with not investing at all, however, is that you may not have sufficient money to achieve your financial goals. An individual saving $100 per month, without investing, would have put away only $52,400 since 1970. By placing that money in five-year fixed-term investments, the investor would have been able to end up with almost five times that amount. And if invested in a diversified portfolio, our investor’s savings would have grown to $835,313. It’s true that any investment involves varying levels of risk. But, as the image illustrates, even if you have low risk tolerance, you can find a suitable investment for your needs that may still be much better than no investment at all.

### Two Types of Investments Versus Saving Without Investment, Jan 1970–Aug 2013




Past performance is no guarantee of future results. This hypothetical example is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Holding a portfolio of securities for the long term does not ensure a profitable outcome and investing in securities always involves risk of loss. The diversified portfolio was created for illustrative purposes only; it is neither a recommendation, nor an actual portfolio. Government bonds are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest, while stocks are not guaranteed and have been more volatile than bonds. International investments involve special risks such as fluctuations in currency, foreign taxation, economic and political risks, and differences in accounting and financial standards. Diversification does not eliminate the risk of experiencing investment losses. The data assumes reinvestment of income and does not account for taxes or transaction costs.

Source: Small stocks—Ibbotson® Small Company Stock Index. Large stocks—Standard & Poor's 500®, an unmanaged group of securities considered to be representative of the U.S. stock market. International stocks—Morgan Stanley Capital International Europe, Australasia, and Far East (EAFE®) index. Long-term government bonds—20-year U.S. government bond. 5-year fixed-term investments—yield on a 5-year U.S. government bond. Cash—30-day U.S. Treasury bill.

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### Our Firm

Pettinga Financial Advisors, LLC is an independent, fee-only financial services firm serving clients across the nation from our office in Evansville, Indiana.

We offer a no-obligation introductory meeting to interested persons and institutions to determine if we can add value to their individual situation.

Because you receive our services on a fee-only basis, you pay no sales commissions for our investment counsel. Nor do you deal with sales people tied to transaction commissions. Instead, you enjoy a personal relationship with a knowledgeable, unbiased advisor.

Your personal financial advisor focuses on the future you envision and commits to helping you Get There.

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# Monthly Market Commentary

News in recent weeks has been all about the government shutdown and the even more worrisome prospect of violating the debt ceiling sometime later this month. A debt-ceiling violation could lead to the deadly combination of higher interest rates and a slower economy. In a world where markets swoon on a 20,000-job miss in monthly employment data (on monthly job growth of about 200,000), losing 800,000 government jobs in one shot is a very big deal. Although the market has been soft lately, it seems to have hardly grasped the potential of a longer-term shutdown. We have reached this crisis point so many times recently with no negative consequences that the market seems almost numbed to the potential pain. Relatively inflexible wage rates and the propensity of most consumers to keep spending despite short-term adversity all contribute to the economy's overall stability and slow growth rate. But a month-long government shutdown would likely cut GDP growth by at least 0.5% in a world of 2.0% growth.

Employment: Another negative consequence of the shutdown is that government agencies have stopped releasing statistics; the Bureau of Labor Statistics' official employment report is missing. The ADP employment report showed more of the slow, unsatisfying growth rates seen for the last several months, with private sector jobs growing by 166,000, up from the 159,000 jobs added in August. The report was a bit of a disappointment, as the consensus estimate was for 180,000 jobs to be added.

Housing: New home sales and housing starts slowed down in the face of higher rates, while existing home sales jumped ahead as homebuyers raced to close quickly before rates moved even higher. Even before the higher rates, housing data had begun to top out as land and labor shortages slowed home construction. This has caused many analysts to scale back their housing growth rate and GDP contribution for both 2013 and 2014.

Consumer spending: Month-to-month consumption data has shown improvement, but the much more reliable year-over-year data suggests more of the same for consumption and the United States economy. Year-over-year three-month averaged consumption growth remained stuck in its slow and unsatisfying rut of 1.9% when adjusted for inflation. That remains well ahead of income growth of just 1.1%, with the higher payroll and income tax rates subtracting close to a full percentage point off of income growth. Income data is beginning to show some improvements that might help fourth-quarter spending data, but initial reports seem to suggest a softer holiday shopping season than last year.

Quarter-end insights: While the overall U.S. economy has been quite stable, the third quarter did bring a number of real surprises, some positive and some negative. In the positive camp, Europe appeared to move from recession into recovery. The U.S., Chinese, and European manufacturing economies appeared to pick up steam in the quarter. Better auto sales and production helped the data, as did some inventory rebuilding and general improvements in consumption from more confident European consumers.

On the negative side, U.S. interest rates continued to climb throughout most of the quarter. The U.S. 10-year Treasury bond approached 3% in the middle of September before settling back a little after the Federal Reserve decided not to taper bond purchases. However, despite this decision, rates are still substantially higher than they were a quarter ago and are unlikely to approach old lows. Although tapering is off the table for another month, it will happen at some point, and the market knows it. Morningstar economists expect the 10-year Treasury bond to reach the 3% to 4% range over the next year or so, and a tapering program of some type to begin in the next three or four months. Projections for the remainder of the year include GDP growth in the 2.00% to 2.25% range, inflation at 1.60% to 1.80%, and the unemployment rate at 7.10%.

# A Brief Overview of ETF Providers

The exchange-traded fund industry has come a long way since the first ETF, SPDR S&P 500, was launched in 1993. U.S. ETFs closed August 2013 with just over $1.49 trillion in total net assets.

An ETF is a passively managed index fund that strives to achieve a return similar to that of a particular market index. There are many factors that contributed to the increase in popularity of ETFs, including trading flexibility, lower expense ratios, tax efficiency with regard to capital gains distributions and, more importantly, potential diversification benefits. By buying a single unit of an ETF, investors can get exposure to all the securities that make up the related index—for example, the S&P 500. Here is a quick look at the three major providers in the industry.

iShares is the largest ETF provider in the world, with a 39.4% current market share and $587 billion in assets as of August 2013. It was acquired by money manager BlackRock in 2009, and the impact of this transaction might have been seen in the recent SEC filing to launch its own actively-managed ETFs. iShares is best known for a varied and large product lineup, with a suite of ETFs that invest in municipal bonds, treasuries, and specific countries. In September 2010, iShares launched three new country-specific emerging-markets ETFs for China, Brazil, and the Philippines.

SPDR State Street Global Advisors manages the SPDRs family of ETFs and is best known for sector funds that track the S&P 500's sectors, including the most heavily traded ETF, SPDR S&P 500, as well as high-yield bond and mortgage ETFs. As of August 2013, it has approximately 22.7% of the total market share of the ETF industry, with $338 billion in assets.

Vanguard is the third-largest provider of ETFs in terms of assets under management. It has aggressively increased its market share in the past few years, with a 1.5% increase during the past year, and it currently has a 19.4% market share as of August 2013. It is best known for having some of the lowest expenses among the industry's major players and has launched ETFs based on Russell indexes, as well as expanded its suite of equity indexes, while offering lower-priced alternatives.

All the major ETF providers have offerings that suit the needs of a variety of investors. When deciding which ETF to invest in, consider important factors like expense ratios and brokerage commissions, since these can reduce the returns on any portfolio. In addition, make sure that your overall investment portfolio is diversified and that ETF investments are only used to complement existing investments, not replace them.

Diversification does not eliminate the risk of experiencing investment losses.

## Top 10 ETF Providers by Market Share August 2013

| Name | Market Share (%) |
|---|---|
| iShares | 39.4 |
| SPDR State Street Global Advisors | 22.7 |
| Vanguard | 19.4 |
| PowerShares | 4.9 |
| WisdomTree | 1.9 |
| ProShares | 1.8 |
| Market Vectors | 1.5 |
| Guggenheim Investments | 1.1 |
| First Trust | 0.9 |
| Schwab ETFs | 0.9 |

Source: Morningstar Fund Flows, Morningstar Direct.

Holding an exchange-traded fund does not ensure a profitable outcome and all investing involves risk, including the loss of the entire principal. Since each ETF is different, investors should read the prospectus and consider this information carefully before investing. The prospectus can be obtained from your financial professional or the ETF provider and contains complete information, including investment objectives, risks, charges and expenses. ETF risks include, but are not limited to, market risk, market trading risk, liquidity risk, imperfect benchmark correlation, leverage, and any other risk associated with the underlying securities. There is no guarantee that any fund will achieve its investment objective. In addition to ETF expenses, brokerage costs apply. Fees are charged regardless of profitability and may result in depletion of assets.

# Five Lessons from the Three-Year Market Rally

…now a four-year market rally, but the lessons are still relevant. 1) The turning point is not always obvious. In hindsight, it seems like it should have been dead obvious that stocks were cheap four years ago. But, because of their inability to clearly identify market bottoms, investors may be better off sticking with a strategic asset-allocation plan. 2) Don't let past performance control your portfolio. To the extent that you can, let your strategic asset-allocation framework be a key driver of where you deploy new cash. 3) To help maximize participation, make a little room for the risky stuff. Even though higher-quality stocks tend to hold up better during downturns, the opposite tends to be true during recoveries. Investors may want to maintain exposure to both types of companies: high-quality, wide-moat dividend payers and economically sensitive small- and mid-caps. 4) But there are also chicken ways to play. You don't need to pile on the risk to generate robust gains in absolute terms. Investors who have shorter time horizons or are simply more comfortable with lower-risk stocks can reasonably allocate more toward such stocks without completely ceding their upside potential. 5) There will be bumps (and buying opportunities) along the way. The movement hasn't always been upward since the market bottomed. If your portfolio is light on stocks at the outset of a rally, periodic sell-offs may provide opportunities even at a later time.

Diversification and asset allocation do not eliminate the risk of investment losses. Stocks are not guaranteed and have been more volatile than other asset classes. Small stocks are more volatile than large stocks, are subject to significant price fluctuations and business risks, and are thinly traded. This should not be considered financial planning advice. Please consult a financial professional for advice specific to your individual circumstances.



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