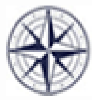


Stein Wealth Advisors, LLC

Newsletter

August 11, 2009 Volume 1, Number 1

In This Issue

Commentary

Did you Know...
Profits, Inflation, and Stock Rallies

Articles of Interest:
Tax Savings Tips

Quick Links

Yahoo Finance

Wall Street Journal

Barron's

Social Security

IRS

Online Money Manager-Mint

Did You Know...

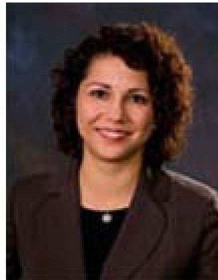
Q: What is the American Recovery and Reinvestment Act of 2009 ("the Act")?

A: It's the $787 billion economic stimulus President Obama signed in February. It includes new tax breaks and improvements on existing tax deductions and credits, all of which add up to about $300 billion in tax relief for middle-class taxpayers.

Q: What are some of the major tax savings opportunities that are available for families?

A: Major tax saving opportunities for families include:

• An improved First-Time Homebuyer Credit-the initial First-Time Homebuyer Credit was rolled out in July 2008, and it included a $7,500 tax credit that worked like a loan. It had to be repaid over 15 years unless the home was sold or became a secondary residence. Now, for homes purchased before December 1, 2009, the credit has been increased to



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Commentary

Over the last several months many people felt like things were never going to get better. The expectation of any economic recovery seemed impossible to imagine, but as we near the end the Summer and hopefully the end of the longest bear market since the 1930's, the S&P 500, finished the month of July up 11% year to date. It's best performance since 2003.

According to the U.S. Federal Reserve Board's Beige Book the rate of economic decline has moderated or stabilized in most parts of the country, and the survey found that although conditions remain weak in many regions there are signs of improvement in key areas, including manufacturing, residential property, and employment. While the Beige Book provided few indications of outright growth, it did suggest a slowed pace of decline since its June 10 report.

I encourage you to remain "cautiously optimistic" about the recent rally we've seen in the equity markets and continue to stick to the strategies we have put in place that have proven viable time and time again. As always, do not hesitate to call me to talk about any questions or concerns that you are having. Have a wonderful and hopefully warm August!

Very Truly Yours,

Melissa J. Stein

Melissa J. Stein

Articles of Interest

Chief Investment Strategist Corner

by James Swanson, CFA
July 30, 2009

Profits, inflation, and

$8,000 and you don't have to repay it after you own your new home for three years. And, speaking of three years, calling it a "First-Time" credit really isn't entirely accurate. For purposes of this bill, the government defines a "first-time" home buyer as someone who hasn't owned a home in the past three years.

• Tax deductions on new cars- if you buy a new car, SUV, light truck or motorcycle anytime after February 17 until the end of the year, you can write off any state or local sales or excise tax as an itemized deduction on your taxes. If a vehicle costs less than $49,500 and weighs less than 8,000 pounds, you can write off the full amount of the sales tax. If you buy a car over $49,500, you can still write off a portion of the sales tax. The deduction is phased-out if adjusted gross income exceeds $125,000 ($250,000 if married filing jointly). The Act also modifies the existing credit for plug-in electric vehicles. The base credit is now between $2,500 and $7,500, depending on battery capacity of the vehicle.

• Increased child tax credit-the 2009-2010 child tax credit which is refundable now has the income threshold at $3,000.

• College savings-the Act contains several items that can help make college more affordable, including a $500 increase in the Pell Grant, for the 2009-10 academic year, an increase in the Hope credit from $1,800 to $2,500 for 2009 and 2010, and additional tax-free distributions for 529 plans. Now, students can use money from a 529 plan to pay for computers, computer technology and even internet services without paying taxes.

stock rallies

The bad news first: Unemployment's rise to almost 10% is a worrisome trend and one that will have to be reversed before the United States can embark on a full economic recovery.

The good news next: However, the fact that companies have been able to increase productivity and keep labor costs low is leading to the upside second-quarter earnings surprise that we have seen over the past couple of weeks. Low labor costs have been a key element in boosting corporate profits and at the same time have helped tame inflation, even as the government increases the money supply to help the economy exit recession. Both strong profits and tame inflation are **key components** behind the current stock market rally.

The components of a stock rally

Profits
Let's look at this phenomenon of low labor costs closely. In the United States, labor and benefits make up about 70% of an average company's costs. So when the crisis began, American companies very quickly cut jobs, capital expenditures, and costs in general. Low-cost competition from China and India gave U.S. companies added incentive to keep expenses down.

Now we are starting to see these companies reap the rewards of their frugality. Their biggest cost element - labor - is not growing very fast and in some instances still shrinking. At the same time, companies are beginning to see some improvement in their unit growth, a trend which could result in margin expansion and better return on equity. So it is thanks to this cost cutting that more than 70% of the Standard & Poor's 500 Stock Index companies that have reported earnings thus far have surprised to the upside. In our view, cost containment is the main story behind the revitalization of corporate earnings and should enable companies to report solid corporate profits for a number of quarters ahead.

Inflation
Now let's look at low labor costs and their effect on consumer inflation. Labor and wages, directly and indirectly, make up about 50% of the U.S. consumer price index. Labor costs are rising slowly because the

average worker has become more productive. That means that at this time inflation is not a big risk. We have been watching the numbers that companies have reported for aggregate hours worked, and these numbers have not been rising because productivity has been increasing. Companies are not likely to begin to hire more workers until the man hours they need to meet their production demands begin to rise. The fact that they have not yet increased payrolls is a positive for the inflation outlook.

Even though the government has been pumping money into the economy, money alone is not inflationary. Excess money growth PLUS running an economy at full capacity are the main risks in creating widespread inflation. Currently, excess capacity exists everywhere in the U.S. economy. Excess factory production and excess workers have become the norm.

In sum, low labor costs are supporting the stock market because earnings are coming in better than expected. Lower inflation expectations are also supportive of the stock market because low inflation has a high long-run correlation with price-to-earnings ratios.

So, what will this current situation mean for some market sectors?

Stocks: In our view, stock prices should continue to find support from the earnings rebound and the near-term favorable outlook on inflation. As I have mentioned, both will likely be sustained by low labor-cost increases.

Bonds: Bond yields are tied to expectations about future inflation. Historically, however, it is not just excess money supply that has spurred inflation here or elsewhere in the world. Rather, it is pressure on resources, such as workers and thus wages, which sparks inflation.

Currently the U.S. has no pressure on resources and is operating well below its potential. We believe that as the U.S. economy continues to grow below trend, excess capacity will be slow to be absorbed. Under those circumstances, substantial money supply growth will not be able to spur inflation. Bond prices and yields therefore will likely stay in a relatively narrow range. Credit-linked bonds, however, are historically cheap; that value suggests possible excess relative return to the Treasury market could continue until conditions normalize.

The views expressed in Chief Investment Strategist Corner are those of James Swanson and are current through July 30, 2009. They do not necessarily reflect the views of individual MFS® portfolio managers or other persons in the MFS organization. These views are subject to change at any time based on market and other conditions, and MFS disclaims any responsibility to update such views. No forecasts can be guaranteed. These views may not be relied upon as investment advice or as an indication of trading intent on behalf of any MFS fund.

The investments you choose should correspond to your financial needs, goals, and risk tolerance. For assistance in determining your financial situation, please consult a financial advisor.

Past performance is no guarantee of future results.

Source: MFS research

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