ASPIRIANT

Insight

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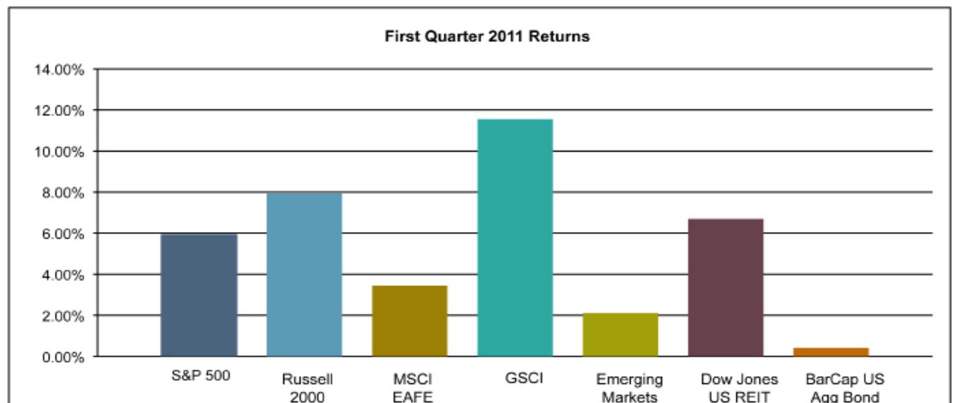
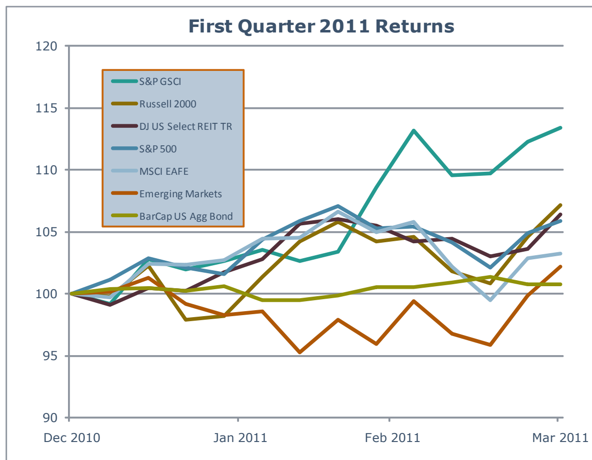
Markets Continue to Advance

Perhaps surprisingly, investment markets continued their strong performance though the first quarter of 2011. Investors' confidence in improving economic fundamentals has outweighed a series of traumatic events that, in a different climate like that of late 2008 or early 2009, could have produced very sharp downturns.

Results, however, were not uniform. Emerging markets were just barely positive while small cap stocks continued their "best in class" equity performance again this quarter, outstripped only by the uniquely strong commodities results.



And, the ride wasn't smooth. Following a relatively flat January, early February saw strong rallies, only to fall sharply as the Japanese earthquake, tsunami, and nuclear reactor disasters rocked markets around the world, but particularly in Japan and elsewhere in Asia. But then March resumed the advance, despite slow resolution to the perceived dangers of nuclear radiation from Japan and the increasing violence in Libya and other areas where regime change is in the air.



So, despite what might be a once in a lifetime political and social transformation now playing out in oil-rich North Africa and the Middle East, despite continuing risks to the stability of the euro as Portugal follows Greece and Ireland to sovereign debt rescues, and despite the considerable uncertainty about the willingness of the US Government to seriously address its own deficit problems…despite all this, markets now seem focused on the accelerating underlying economic recovery. Corporate profits are strong, the job market is improving, and consumer spending is increasing. In some respects then, this first quarter of 2011 may be a microcosm of a lifetime of investment experience: aggregate, long-term performance reflecting what growth does occur in the underlying economy, punctuated by unexpected and sometimes deeply troubling threats along the way. Broadly diversified, global investment strategies continued to serve Aspiriant clients well this quarter. A similarly perseverant approach to very long-term investment strategies should continue those rewards.

In the articles to follow, our Chief Investment Officer, Jason Thomas, and our Director of Real Estate Research, Lauren Pressman, comment in further detail about the current investment climate and the special role that real estate and other "real assets" can play in client portfolios. Brett Gookin shares insights for an increasingly relevant concern that faces our clients as they and their parents age. And Kacy Gott, our Chief Planning Officer, reminds us of the possible second chapter for the Roth conversion activity many Aspiriant clients undertook in 2010.

As we get deeper into 2011, we'll be commenting further on other tax and wealth planning issues, especially regarding taking advantage of the current estate and gift tax allowances.

We look forward to discussing all of these matters, and more, with our clients as the year progresses.

Tim Kochis, JD, MBA, CFP® **Editor**

Director - New Business Lines, Chairman of the Board, Principal

Still Room for More Good Performance

During the first quarter of 2011, a number of US equity market sectors surpassed their October 2007 peaks and a few more have a total return (including dividends) which is now positive. Small- and mid-cap stocks are now at new highs, though large cap value (Russell 1000) and large cap blend (S&P 500) indices, with heavy weighting in financial services, are still below their previous peak. Is there cause for concern that the markets have come too far, too fast? As we discuss below, we don't think so.

Total Return of US Market Sectors Since Market Peak (October 2007-through 3/31/2011)

	Value	Blend	Growth
Large	-14.7%	-8.5%	1.0%
Mid	1.1%	3.9%	5.7%
Small	0.9%	4.8%	8.1%

Source: Russell Investment Group, Standard & Poors, J.P. Morgan Asset Management

For investors looking for reasons to be optimistic, the first quarter started off well. The US economy seemed to have finally put the financial crisis into the past and Europe's sovereign-debt crisis seemed less acute. Investors responded by moving out of money market funds and into equities. Their primary concern was that emerging economies would grow too quickly, pushing up commodity prices and allowing inflation to take hold in their domestic economies.

What a difference a month can make. First, social unrest in North Africa put oil markets on edge. Then an earthquake, tsunami, and a nuclear accident deeply wounded the world's third-largest economy. Finally, a series of setbacks in the European financial system – Ireland uncovered a capital shortfall in a round of "stress tests" on top banks, Portugal reported that it missed its 2010 budget deficit goal and has now just admitted it needs to be bailed-out – led to ratings downgrades and more fears about sovereign default risk.

Social Unrest

In response to social unrest throughout North Africa (which provides around 35% of the world's oil), the price of a barrel of Brent crude oil has increased from around $96 in January to $115 as of this writing (April 12). The fighting in Libya, which itself produces 1.7m of the world's 88m barrels a day, continues.

But so far prices have not been pushed up by actual disruptions to supply. Oil hit a peak even before news emerged that some foreign oil firms operating in Libya would cut production and that the country's ports had temporarily closed. Further, oil is more global than it was during previous crises. In the 1970s, production was concentrated around the Persian Gulf. Since then, the supply of non-OPEC oil has hit markets from fields in Latin America, West Africa, and beyond. Russia overtook Saudi Arabia as the world's biggest crude supplier in 2009; OPEC's share of production has gone from around 51% in the mid-1970s to just over 40% now. The impact of a deeper crisis would depend on how much oil production was lost and for how long, but in the longer term, stable, democratic regimes may improve productivity and reduce the influence of terror groups. There is a rosy potential outcome.

Japan

Concerns regarding the potential impact of the earthquake on Japan's economy and the knock-on effects to the US and global economies took hold in US markets after a muted reaction immediately following the earthquake. While the full extent and duration of the earthquake's effect on Japan's economy isn't yet clear, our initial impression is that the impact to growth in the US and the world will be limited.

US exports of goods and services to Japan represent roughly 4.4% of total goods exports (exports were 12.7% of GDP in Q4), equivalent to roughly 0.4% of GDP. Including services exports brings overall exports to Japan to 0.7% of GDP. It would take a very significant disruption to domestic demand in Japan to have a meaningful effect on US exports.

The disruption in the global supply chain is more problematic, especially for the US auto industry. Some Japanese suppliers, it is now apparent, are critical suppliers of raw materials. For example, the Economist reports that two firms, Mitsubishi Gas Chemical and Hitachi Chemical, control about 90% of the market for a specialty resin used to bond parts of microchips that go in to smartphones and other devices. Both firms' plants were damaged. The compact battery in Apple's iPods relies on a polymer made by Kureha, which holds 70% of the market, and whose factory was also damaged.

It seems clear that industrial firms, having spent years becoming ever leaner in their production techniques (in the process, making themselves more vulnerable to supply shocks), will now have to make adjustments, likely giving up some efficiency gains to become more robust.

Europe

The challenges facing the Eurozone as the result of issues in Greece, Ireland, Portugal and Spain are too numerous and complicated to review here. But the threat of sovereign default and/or the need for a massive bailout is real, and the implications of a collapse of the Spanish financial system are significant.

On the other hand, the European Central Bank, preparing for a policy meeting shortly after this writing, is expected to become the first central bank among the world's large, developed economies to raise interest rates since 2008 (China recently increased rates for the fourth time in less than six months). Higher interest rates could punish Europe's fragile economies in the short run and a stronger euro could hurt German exports by making them more expensive on world markets, but the ECB is betting that a rate increase now will prove its willingness to fight inflation and help it avoid more significant increases in interest rates in the future.

Implications

Across a range of likely scenarios with the three issue areas above, the implications are clear. Unrest and uncertainty in oil producing regions will put upward pressure on oil prices, regardless of the actual impact on production. With the ECB moving toward tighter policy and the US Federal Reserve standing pat, the US dollar would likely continue to decline as investors seek higher-returning bond investments elsewhere. The dollar is down 3% against a broad basket of currencies since the beginning of the year and down 24% from a decade ago, though it has been even weaker in the past – July 2008 and in the early 1990s, according to Fed data.

Many Aspiriant portfolios include commodities, through the publicly-available exchange traded note GSC (which we worked with Goldman Sachs to create), as a hedge against an oil crisis. That vehicle has been very effective.

Total Returns of GSC and the S&P Goldman Sachs Commodities Index (GSCI)

	YTD (through 3/31/11)	YOY (3/31/10-3/31/11)	Since GSC Inception (annualized) 7/31/07-3/31/11
GSC	13.72%	27.96%	0.88%
GSCI	11.56%	22.73%	-3.7%

Source: Bloomberg. Total returns include the reinvestment of dividends and GSC reflects the management fee of Goldman Sachs (the issuer of GSC) while GSCI does not.

Aspiriant portfolios are also well-diversified globally, with currency exposure generally unhedged. So our investments in real estate and public equity markets around the world will benefit from, and act as a hedge against, a weakening dollar.

In summary, we do not believe that the equity markets have come too far, too fast, and anyway think that is the wrong question. The right question is whether, from here, global capital markets offer an attractive future return given the risks. We think so. Our thoughts are more fully spelled out in our March 2011 *Market Viewpoint*, which is available on our website (link).

Jason Thomas, PhD, CFA
Chief Investment Officer, Principal

From the CEO

This was a very strong quarter for the clients of Aspiriant. Despite severe geopolitical unrest in North Africa and the Middle East and an unprecedented sequence of disasters in Japan, the world's underlying economy continued to gain momentum and markets accordingly produced excellent returns for the quarter. While many obvious threats remain and we've been reminded, yet again, that we must "expect" threats that are unexpected, we believe that our clients will continue to be rewarded by perseverance in their long-term investment strategies. It's a much longer perspective than one quarter, of course, but it's gratifying to see clients being rewarded for that perseverance as we move deeper into 2011.

I'm happy to report good news for the firm as well. Integration of our new partners and clients is proceeding rapidly and our new colleagues are all either just moved or are about to move to new quarters, independent of their former Deloitte homes. We remain committed to our partnership with Deloitte in serving our shared clients and are eager to continue to expand our relationships moving forward.

By expanding our talent through this combination, we added a fresh perspective to our investment strategies and planning opportunities, and by successfully integrating our efforts, we will enable even more specialization that will add depth to our capabilities, and ultimately, improved solutions for all clients. As this process unfolds, we will be sure to report on our progress and the benefits we have achieved.

In addition to the more "inorganic" growth we have experienced, I'm also happy to report that we have grown organically as well. Since the start of the year, we've already welcomed 5 new staff to our organization and the pace of new business remains strong thanks to the ongoing support of our existing clients and centers of influence. This robust growth helps us to attract and retain strong talent to serve all of our clients even better.

There were also some important achievements this past quarter as well:

- Lindsey Cornell, of our Los Angeles office, received the CFP® (Certified Financial Planner) designation;
- Nate Wong, of our San Francisco office, became the organization's 9th CFA (Chartered Financial Analyst) charterholder
- Nikki Michelini, a Team Leader in Los Angeles, was added to the AICPA Personal Financial Planning Executive Committee; and
- Kacy Gott, our Chief Planning Officer, has just been appointed Chair of the CFP Board's Council on Education.

In addition, I'm happy to have accepted a position on Schwab's Advisory Board that will give us the opportunity to improve their direct client service efforts.

We are very proud of these very significant professional accomplishments and their continuing demonstration of Aspiriant's leadership within our profession.

With our genuine gratitude for the opportunity to serve our clients and for the foundation that that service provides to us to advance our profession.

Sincerely,

Rob Francais, CPA
Chief Executive Officer, Principal

Real Estate...An Inflation Hedge?

Allocation to real assets can play an important role in a long-term investment portfolio and, in particular, as a hedge against inflation risk.

Assets that are tangible or physical in nature encompass a wide range of investment strategies whose values are sensitive to inflation. Examples of real assets represented in Aspiriant portfolios include real estate and commodities. Commodities were added to Aspiriant portfolios several years ago in particular to provide significant and unique protection against inflation. Similarly, real estate has demonstrated that it is a good, albeit partial hedge against inflation. The reasons why are fairly simple.

First, inflation causes a rise in construction costs, which, in the short run, will limit new supply. Why is this the case? Because real estate developers/investors target a certain return on cost (yield) prior to starting a new development. If the numerator (net operating income derived from rents less expenses), does not rise sufficiently to offset an increase in the denominator (development costs), then ground breaking on new projects will be postponed until projected net operating income rises enough to meet the desired yield.

Inflation, then, fuels rent growth and, as a result, an increase in value of existing properties.

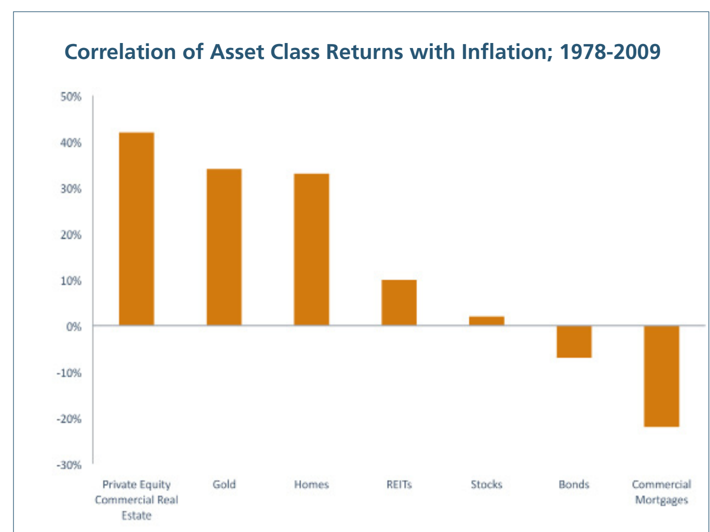
Although inflation will drive up expenses as well, many commercial real estate leases are structured so that the tenants bear all expense increases, insulating property owners from much of the burden of higher expenses.

The combination of these factors translates into higher market rents, which eventually feed higher operating incomes. In some real estate sub-asset classes such as hotels and apartments, which generally have shorter lease terms, the impact can happen relatively quickly. In others, with longer average lease terms such as retail and office properties, it may take longer for the impact to filter through. However, real estate investors will often price in the expectation of future rent increases, and will give existing owners "partial credit" for this expectation in their current valuation of properties, even if the rent increases haven't materialized for that property quite yet. This occurs by a fall in the capitalization rate (or yield, calculated by the net operating income divided by the property value) used to value a property. Essentially, investors lower the discount rate they are using to value existing cash flows, resulting in a higher estimated property value.

Why, then, is commercial real estate considered only a partial hedge against inflation? The reasons are a bit more complicated and have to do with the condition of the space markets, real estate's sensitivity to interest rates, and how real estate is owned (direct private ownership or through a securitized vehicle such as a REIT).

One clear lesson from the early 1990s is that owning real estate is not an effective hedge against inflation if there are large oversupplies of space in property markets. High vacancies inhibit a landlord's ability to lift rents, while expenses might respond more immediately. During this period of time, even though consumer prices rose steadily, commercial property prices collapsed. In contrast, from 1979 to 1982 (a period of high inflation, peaking at 15%, and a relatively healthy space market measured by the vacancy rate), commercial real estate outperformed, returning 17% vs. stocks and bonds, returning approximately 11% and 6%, respectively. Unlike the collapse in the early 1990s caused by massive overbuilding, additions to new supply over the last ten years have been relatively moderate. As a result, today's space markets are not as vastly oversupplied as in the early 1990s. In many cities, landlords have already begun to raise rents as job growth has resumed. If inflation were to rise significantly (which we don't expect), we'd expect this impact to amplify.

A second reason why real estate may act only as a partial hedge is that commercial real estate is impacted by interest rates, as most acquisitions are at least partially financed by debt. Higher interest rates will affect the price a buyer is willing and able to pay to meet its required rate of return, thereby dampening real estate value increases.



Source: S&P; Barclay's Capital; NAREIT; NCREIF: Moody's Economy.com; PPR

Lastly, academic research has indicated that while *privately held* commercial real estate over the period of 1978-2009 provided an excellent hedge for inflation, REITs have not been an effective inflation hedge, especially against unexpected inflation. While theories abound to explain the performance of REITs during inflationary periods, it is important to note that until the mid 1990s, the REIT industry was dominated by *mortgage* REITs, which provide debt financing for commercial or residential properties. Like bonds, mortgage REIT values are negatively impacted by rising interest rates. The rise of *equity* REITs (REITs that own and operate properties) occurred after the passage of the Tax Reform Act of 1986. Today, equity REITs represent over ninety percent of Aspiriant clients' REIT exposure. The research done to date on equity REITs performance during inflationary periods has been inherently limited by the fact that since the mid 1990s, inflation has never exceeded 3.85% in the US. More recent research on equity REITs seems to indicate a positive correlation with inflation, while mortgage REITs have a significant negative correlation with inflation. As we've seen with the extreme price volatility over the last few years, REIT performance can be affected as much or more by general stock market sentiment than underlying property valuations. Nevertheless, although REITs' ability to act as an inflation hedge may be dampened in comparison to privately owned real estate, we do expect equity REITs to exhibit an increasingly positive correlation to inflation particularly in periods of above-average inflation growth.

Consequently, if we do face an inflationary period, we expect commercial real estate owned by our clients, whether privately or through REITs, to provide a valuable inflation hedge in their investment portfolios.

Lauren Pressman
Director - Investment Research, Real Estate

INSIGHT **Publication Change**

To better meet our clients' expectations for in-depth commentary and analysis, we will be changing the timing of *INSIGHT's* **future** publication. Starting with the second quarter of 2011, we will be publishing at the middle of the *following* quarter. This will permit a more thorough analysis of the quarter just past and an opportunity to also comment, at some depth, about the quarter under-way. Consequently, look for the next issues of *INSIGHT* in mid-August (for the quarter ending June 30), mid-November (for the quarter ending September 30); and so forth for the future issues. This timing will also more closely coincide with clients' actual receipt of their portfolios' performance reports.

Roth IRA Recharacterizations

American taxpayers in general (and our clients in particular) have been encouraged to defer tax as long as possible. Since Roth IRAs have the same investment risk as other vehicles, those who chose to convert, and pay tax on, some or all of a traditional IRA are at risk of the value declining by the time tax on the conversion is due, owing tax on values that were higher than now.

To avoid this potential regret, Congress created an escape clause which is known as "recharacterization". Taxpayers can choose to recharacterize, basically undoing the Roth IRA conversion, until mid-October of the year following the conversion (the final deadline to file returns).

2010 was the first opportunity for many of our clients to convert some or all of their traditional IRAs to a Roth IRA. Many did. With the Roth IRA, taxpayers never have to pay tax on qualified distributions and there are no minimum required distributions beginning at age 70-1/2. But when initially "converting" a traditional IRA to Roth, tax must then be paid on the amount being converted.

If a return is filed before the final deadline and it did not include the recharacterization, an amended return is required to recharacterize and the amended return must still be filed by the final deadline (typically October 15th, but October 17th in 2011).

There is very special tax treatment for Roth conversions in 2010 which allows taxpayers to spread the recognition of the income into the two succeeding years (50% each in 2011 and 2012), but this deferral of tax into two installments does not extend the recharacterization period. The deadline is still October 17, 2011.

In view of the substantial market advances throughout 2010 and 2011 thus far, it seems unlikely that a recharacterization will be attractive, but in the event of a significant decline in values later this year, we'll be on alert to help you consider taking advantage of this second look before you actually do file your 2010 tax return.

Kacy Gott, CFP®
Chief Planning Officer, Principal

Making Life Better for Older Adults

As we age, there comes a time when we may need assistance making it safely through the day. Perhaps you have a nagging suspicion that an older adult (a spouse, your parents…) needs that help right now. Of course, you want to avoid being forced to confront a crisis where an older adult has deteriorated, physically and/or mentally, to the point where they are a danger to themselves or others. What can you do to plan ahead?

The first step is to be aware of warning signs rather than waiting for a crisis to occur. The next, and often the most difficult, step is taking action and getting appropriate help.

Early signs that an older adult might need help

The National Association of Professional Geriatric Care Managers has compiled a list of some of the early warning signs that an older adult might need help, including:

1. **Personal hygiene** Is he shaving? Does she shower less frequently, wear dirty clothes, or have neglected teeth? Are there any injuries that you can see? Is there a urine smell?
2. **Forgetfulness** Are there stacks of unopened mail or newspapers, unpaid bills, unfilled prescriptions or missed appointment slips?
3. **Interaction/Behavior** Does she constantly repeat questions? Can he carry on an extended conversation? Does he refuse any suggestion or does he agree with every suggestion? Does he retain what was said? Are there any apparent mood swings? Is he unusually loud or quiet? Is she angry? Does she make phone calls at all hours of the night?
4. **Relationships** Do friends call? Do friends or neighbors express concerns? Has she quit socializing or participating in group activities?
5. **Mobility/Medication** Can she get around? Can he take medications without supervision? What are the medications? Who goes to the doctor with him? Is she going to the doctor at all or does she refuse to go?
6. **Refrigerator/Eating Habits** Does the refrigerator contain adequate food? Is there any spoiled food? Have his eating habits changed? Has she lost weight? Has she missed meals or is she generally not hungry?
7. **Shopping** Does he have any problems making change or writing checks?
8. **Buying things he doesn't need** Is there evidence of excessive shopping, ordering. Is the mail full of charitable letters, a sign that he is giving out money to anyone who asks?
9. **House** Does it look maintained or is it in disrepair? Is dust and/or trash accumulating in what was once an immaculate household?
10. **Driving** Can he drive safely? Is her reaction time adequate on the road? Is there any evidence of automobile accidents?

Taking action at this stage to address problems can forestall a full blown crisis.

Obstacles to securing help

There are significant obstacles to securing help for older adults, however. Just because you have observed warning signs doesn't mean that others will agree with your observations.

One of the biggest obstacles to securing help is denial that a problem even exists. Children are reluctant to acknowledge that their parents, the ones who have been the traditional family caregivers, now need care themselves. A spouse, even the person needing help, is likely to deny the need for additional assistance because of a combination of fear and anger about their declining health. Moreover, how do you arrange and monitor care for someone if they don't live in close proximity to you? Move them into your home?

Taking action

A Geriatric Care Manager (GCM) is an excellent resource to help you avoid an elder care crisis or, in the unfortunate event one occurs, to help you deal with the crisis and, as the name implies, manage the care. A GCM can evaluate an older adult's current living situation, their needs, including physical and mental health, and their resources, including family, community and financial resources and create a comprehensive care plan. As a trained, experienced and objective third-party, the GCM can help overcome the many psychological and family dynamics obstacles to care.

Once the care plan has been recommended, it is up to the older adult and the older adult's family to determine next steps. GCMs can coordinate implementation of the plan, from the simple (having grab bars installed in the bathrooms and other safety measures) to the complex (screening, arranging and monitoring in-home help, identifying institutional care facilities...) Once services have been established, GCMs can

monitor and coordinate them, or leave that up to the family. GCMs can be used on a one-time basis, or they can serve in an on-going role, depending on the situation. At the very least, plan to bring in the GCM periodically to reevaluate the older adult's ongoing needs and revise the care plan as necessary, as continued deterioration is likely.

Unless the older adult suffers from a severe cognitive disability, he should play a significant part in the evaluation and follow-on care. Remember, the GCM works for the older adult and if the older adult does not accept the process and recommendations, nothing is going to change.

Aspiriant maintains a list of helpful resources, including Geriatric Care Managers. Please contact your client service team for a referral or you can go to the website for the National Association of Professional Geriatric Care Manager, Inc. **www.caremanager.org.**

In selecting a GCM, some important things to look for include:

- Length of time as a Geriatric Care Manager
- Degree in a field related to nursing, counseling, mental health, social work, psychology or gerontology
- Previous occupation as an RN, social worker or geriatric nurse practitioner
- Independent from any service providers (no conflict of interest)
- Experience using community based resources
- Available for emergencies
- Member of the National Association of Professional Geriatric Care Managers (GCM)

Fees

GCMs bill by the hour for their services and their fees can range from $150 - $300 per hour depending on location and needs. The initial evaluation could take two to three hours and a written care plan a bit more, so the total initial cost is likely to be about $1,000. This is a very small price for our clients to pay for an objective, competent plan for dealing with such a critical issue, and for the access to an ongoing resource for the older adult and his or her family.

Even if estate tax reduction planning is not currently urgent, families of any wealth should review the effects of the new laws on their existing revocable living trusts. The increase in the exemption to $5,000,000 raises some of the same funding concerns raised in 2009 when the exemption was $3,500,000. Plus, the new portability rules provide additional planning opportunities.

Brett Gookin, CFP®
Director - Wealth Management, Principal

Circular 230 Disclosure: To assure compliance with Treasury Department rules governing tax practice, the Treasury Department now requires that all tax advisors attach the following statement to any and all written communication, except to the extent exhaustive steps are taken to satisfy the new guidelines of the regulation. We hereby inform you that any advice contained herein (including in any attachment) (1) was not written or intended to be used, and cannot be used, by you or any taxpayer for the purpose of avoiding any penalties that may be imposed on you or any taxpayer and (2) may not be used or referred to by you or any other person in connection with promoting, marketing or recommending to another person any transaction or matter addressed herein.