HERITAGE PERSPECTIVE

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Navigating Through the Noise

Noise is everywhere. The mainstream media bombards you with sensationalistic news that jumps from disaster to catastrophe with the grace of a ballerina. Financial news stations are constantly inundating you with buy and sell recommendations from experts who are hoping to gain an edge on the market. Your neighbors, your in-laws and your co-workers all have a hot stock tip for you, and your own human nature conspires with these outside forces to incite you to follow the herd. The seductive influence of all of this noise has the potential to lead you to make poor investment decisions.

> *"Noise has always been there, playing to investors' emotions and tempting them to make unwise decisions."*

If this sounds familiar, you are not alone. Most investors view news events and trading recommendations as the very essence of investing. But basing your investment decisions on the latest headlines is like buying yesterday's winning lottery numbers: The headlines can tell you about yesterday's winners, but with respect to future winners, the headlines are of no help. The market quickly incorporates any relevant news, often before it actually happens, and adjusts prices accordingly. The banter that follows is simply noise.

The truth is that successful investing is often a matter of knowing what not to do. Attempting to predict the short-term moves of financial markets is extremely difficult, if not impossible, and making the wrong decision can be extremely expensive. Consider the following: Over the past 50 years, US stocks have returned over 10.3% per year. Compounded over that 50-year period, this is a total return of over 13,500%[1]. Any investor could have entered the market in 1964, taken a nap for 50 years, and seen his wealth increase by 136 times over that period. The returns were there for the taking by anyone who was able to avoid the nefarious influence of noise. By not reacting to

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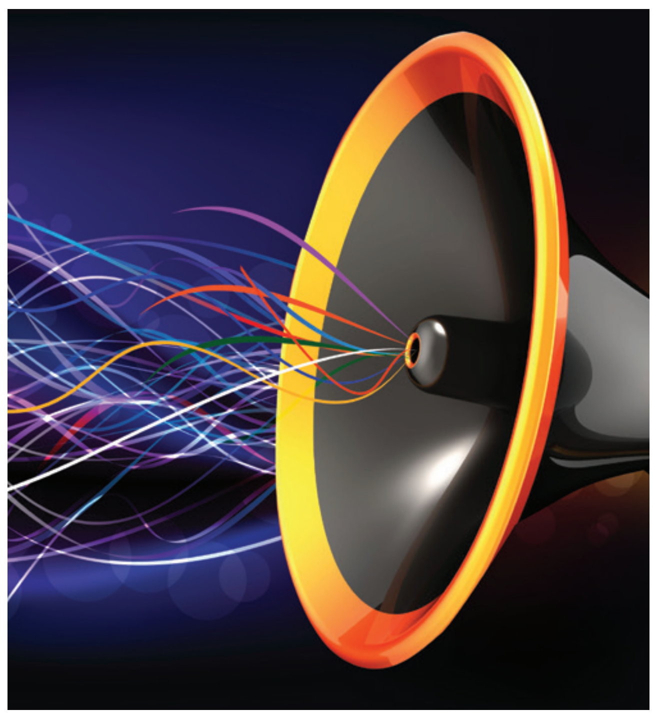

Heritage Investment Group would like to thank all of our clients for their continued support. If you have any friends or family members who could benefit from our disciplined investment process, we would welcome the opportunity to speak with them. Please contact us at (954)785-5400.

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short-term market movements, an investor could have simply sat back and allowed the power of capitalism to do its work. Conversely, investors who jumped in and out of the market because they were provoked by the noise around them had a significant risk of missing out on these spectacular gains.

Noise has always been there, playing to investors' emotions and tempting them to make unwise decisions. Noise was in full force during the dotcom boom of the 1990s, encouraging investors to sell safe assets and go all-in on high-risk technology companies that had no underlying profits or adult supervision. In the mid-2000s noise told investors that real estate prices would go up forever: "Buy a house for a foolish price, then sell it to a bigger fool. Repeat until wealthy." Noise was there during the global financial crisis of 2008, inciting panicked investors to sell stocks right before one of the most dramatic rebounds in the history of the markets. It's a fact; noise is to blame for many investing missteps.

Avoiding the lure of noise is difficult. Emotion often gets the best of investors and makes the noise tough to ignore. The good news is, successful long-term investing is in large part merely a function of paying that noise no mind. At Heritage, our disciplined approach is specifically designed to insulate our clients from the harmful influence of bell-ringing market strategists and overconfident in-laws. The global capital markets have issued you an open invitation to participate in the tremendous wealth generating power of capitalism. The noise is bad for you and your portfolio, so go on… ignore it. Instead of heeding the noise, embrace the sophistication of basic discipline and allow capitalism to work for you. That is a reliable way to generate real wealth.

> ***"The noise is bad for you and your portfolio, so go on…ignore it."***

[1]50-year returns of Dimensional US Market Index as-of December 31, 2013. Source: Dimensional Fund Advisors

A New Tradition: Family Wealth Planning Conversations

Whether it's gathering for an annual reunion, recounting an anecdote about quirky Uncle Jim, or simply being there for one another during difficult times, family traditions are the comfort food that nourishes our most satisfying relationships. As we enter 2014, we would like to suggest that you begin a new and important family tradition: the family wealth planning conversation.

> *"As the word 'tradition' suggests, you should consider this initial meeting to be the first in a recurring conversation."*

What are family wealth planning conversations, and why have them?

At their best, family wealth planning conversations engage every family member, with each of you contributing your talents and interests to achieving your collective and personal lifetime goals. That is not to say everyone must participate equally. As we work with families, one individual often emerges as the spokesperson or steward for the group, and that is fine, if the role is based on a mutual and deliberately planned arrangement. If it is instead based on unspoken assumptions or force of habit, your family wealth planning may benefit from a fresh conversation.

Even if your family is in full agreement on who is best suited to champion its interests, there are always life's many "what ifs." Are others in your family adequately prepared to assume the stewardship role when and if it is required of them? Might they have unexpressed questions or concerns that are best addressed well before that day arrives? Carving out time to hold candid conversations is where it all begins.

Your Investment Advisor should guide your new tradition

To kick off your family wealth planning conversation, you should hold a face-to-face meeting with your advisor. He or she can guide you in exploring key considerations such as:

- How would each of you define your roles in your family wealth planning?
- Are each of you satisfied with your current roles?
- Do all family members have an adequate understanding of the investment goals, estate plan and tax strategy?
- Should anyone be required to increase their participation?
- Are there other questions, suggestions or family wealth dynamics you would like to explore, either immediately or over time?

As the word "tradition" suggests, you should consider this initial meeting to be the first in a recurring conversation. Regardless of who may be "in charge" of your family wealth, the entire family is dependent on the outcome of the efforts. Creating a forum for everyone's voice to be heard is another way your advisor can help you achieve your greatest life goals, keeping your family's wealth strong and meaningful over time.

Is There Some Virtue in Debt?

Politicians and voters in the United States have engaged in heated debate in recent years over the skyrocketing debt owed by the federal government. Over the last decade the debt has ballooned to approximately $17 trillion. Some taxpayers and politicians, understandably angered by the legacy being left to their children, have argued that the U.S. should balance the budget and pay down the debt.

However, we should keep in mind that as recently as the year 2000 we were on track to pay off the entire federal debt by 2012. What we did not know at the time was that the prospect of an end to U.S. debt sent government officials scrambling to put together an emergency plan to deal with the event. That is because the U.S. debt, in the form of Treasury bills, bonds, and notes, is considered the world's risk-free asset and safe haven. It serves as the most important interest rate benchmark, and it is used by the Federal Reserve to implement monetary policy.

A potential crisis

In the last year of the Clinton Administration, economists at the Treasury worked on a secret report speculating on the effects of the debt pay-down and on alternatives that the government and markets could use in place of Treasury securities. That report, titled "Life After Debt," was never publicly issued. It was obtained in 2011 by National Public Radio through a Freedom of Information Act request. It shows how worried some in the Treasury Department were about the projected debt elimination.

U.S. Treasury securities have become a ubiquitous holding for large and small investors, foreign countries, and even the Social Security System, and there is no clear idea how disruptive the absence of such debt would be. For instance, where would the Social Security System stash the billions it collects daily from payroll taxes? It needs to earn interest but it also needs a rock-solid security that will guarantee payout later in this century when the retired population increases.

Fed left high and dry

What would the Federal Reserve use to manage monetary policy? Currently the Fed buys and sells Treasury securities in order to increase or decrease the money supply and interest rates. It needs a large, orderly, and very liquid market to achieve its objectives, and the Treasury security market is made to order.

The report proposed alternatives to using U.S. debt. However, in light of what happened during the financial crisis of 2008, such alternative instruments appear to be a lot riskier today than they did in the year 2000 when the report was written.

For instance, the report identified government-backed agency securities issued by the giant mortgage companies Fannie Mae and Freddie Mac as alternatives. However, even at that time the market for their securities was not big enough. In retrospect we know that the two agencies went bankrupt in 2008 and they continue to limp along today.

The swaps market, where banks and other institutions swap liabilities, was also identified as an alternative because it was "remarkably liquid" and a "vibrant market." However, that market froze solid in 2008 and has not fully recovered since.

The report shows that even though our debt is too big now, it is probably a good idea to always have some amount of federal debt outstanding as a backstop for world markets. There may be some virtue in debt after all.