



INVESTMENTS, INC.

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MarketView

Fourth Quarter 2012

Tis the Season

Soon it will be “Tis the season to be jolly,” but before then, it is the season for political folly. Candidates up for election in November are extending their promises for a better America, and for many who listen, this is a serious time. We hear expressions such as, most important election of our life-time, fiscal cliff, horrendous budget deficit, onerous tax changes, health care upheaval, and high energy prices, etc. There are many uncertainties, many of which are inflated by political rhetoric.

Society, markets, and individual investors are uncomfortable with this uncertainty. We would rather know the “rules of the game” even if we are certain we do not like the outcome (e.g. of the election, tax rates, etc.). Eventually, we adjust to our new situation and move on. While there is plenty of uncertainty now, in the coming months there will be fewer unknowns and that may ultimately lift some clouds currently over the markets.

Barring a hanging chad recount (a.k.a. Florida of 2000) we will at least know the outcome of the election in November. Below is one strategist’s view of the timeline of resolving several of the fiscal cliff issues.



“According to the latest figures, your share of the National Debt is \$47,922.53.”

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Largest Stock Holdings

9/30/2012

<u>Securities</u>	<u>Pct.</u>
Apple Computer Incorporated	2.86%
Exxon Mobil Corporation	2.03%
Wells Fargo and Company	1.95%
AT&T Incorporated	1.86%
International Business Machines	1.82%
US Bancorporation	1.79%
Visa Incorporated	1.78%
Williams Companies	1.64%
Philip Morris International	1.62%
Microsoft Corporation	1.60%

Timeline for Decision-Making

Greg Valliere is the chief political strategist for the Potomac Research Group. In his monthly commentary, dated September 21, 2012, he set forth a possible political timeline for congressional and White House decision making. We found his comments interesting. He points to five elements of the January 1, 2013 “fiscal cliff,” stating that two might be handled, in December, no matter who wins. He thinks the “doc” fix (a 26% reduction in the Medicare reimbursement rate for doctors) will be resolved in December. The cuts are budgeted saves in Medicare, and by extension Obamacare, but believes Congress will not enact them and simply not pay for it. Next, he feels Congress will “kick the can down the road” on the Tax Extenders Bill which keeps tens of millions of middle class taxpayers out of the Alternative Minimum Tax. This is a huge budgeted revenue source, but one that Congress will elect, for the umpteenth time, not to pay for. That’s two down, three to go...sort of.

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ECONOMIC FORECASTS	
↑	GDP Growth 2% in '12, with a slight pickup from first-half slowdown
↑	Interest rates 10-year Treasuries 2% or less at year-end; 2% in '13
↓	Unemployment Around 8% by year-end, despite up-ticks earlier.
↓	Inflation .8% in '12, higher in July-Dec. because of rising food prices
↔	Crude oil Holding steady, trading at \$90 - \$95/bbl. by fall.
↓	Business Spending Unemployment, global slowdown will curb spending well into '13

1 Kiplinger Letter, September 21, 2012.

He feels the debt ceiling issue will be pushed back until February or March due to favorable receipts. Sequestration (automatic spending cuts like defense) may be avoided in January due to cuts in spending elsewhere, and this could last for about six months. Not entirely resolved, but at least some breathing room.

That leaves the Bush tax cuts as the big one to resolve by year-end. If Obama is reelected, he may try for a grand compromise on taxes in December, but it will not be accepted by Congress. Fizzle. No progress. If Romney is elected, no decisions will be made until 2013, when an overhaul/simplification of the tax code will be placed on the table by spring. Either way, Valliere feels, decisions on the Bush tax cuts will be pushed into 2013, so there will be some kind of temporary extension of the current tax code.

Taxation of Dividends

As we have noted in prior newsletters, we have emphasized dividend paying stocks for some time now. A number of our holdings in this space are gas, electric and telephone utilities, most of which provide dividend yields ranging between 4% and 5%. Utilities have been attractive due to low interest rates alternatively offered on most other fixed income investments. Also, the companies in this space have a tendency to increase their dividends each year. Finally, the tax rate for these dividends is currently 15%.

It is no wonder why utilities have been such a good place for the investor to be.

With that said, if the Bush tax cuts are allowed to expire, these dividends could be taxed at a much higher rate, the same rate as earned income. Theoretically, the purpose of a higher tax rate on dividend income would be to cause the wealthy to pay higher taxes. Reality paints a different picture. A recent study by Ernst & Young pointed out that, "68 percent of all tax returns with qualified dividends were filed by taxpayers with annual incomes of \$100,000 or less in 2009, the latest year for which complete IRS data are available." The implication then would be that a higher tax on dividends would hit hard on the middle class, and especially those who are retired.

The Politics of Investment Performance

In every Presidential election each candidate makes the claim that the markets will perform better if his or her party controls the White House. That issue is not as clear when you consider that government power is often shared between parties. The chart to the left shows the results of a different approach looking into the relationship between the composition of the legislative and executive branches of the U. S. government and mar-

Average Annual Returns 1926-2011

	S&P 500	Diversified Portfolio	Number of Years
"Unified" Years	14.8%	9.9%	45
"Partially divided" years	11.1%	9.5%	30
"Completely divided" years	1.1%	7.4%	11

Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Diversification does not eliminate the risk of experiencing investment losses. Government bond funds 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. The time period examined is 1926-2011, and the returns are average annual returns. Stocks-represented by the Standard & Pooors 90 index from 1926 through February 1957 and the S&P 500 index thereafter, which is an unmanaged group of securities and considered to be representative of the U.S. stock market in general. Bonds-20-year U.S. government bond.

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hard to reach resources within North America, most of which involve private land. The question at hand is how much, if any, of the much more abundant resources offshore and on federal lands become available to environmentally acceptable drilling. If this oil and natural gas can be drilled safely and efficiently, it could provide an economic boom providing many needed jobs.

Absentee Ballot Voting

Finally, we find it important to comment on absentee ballot voting. In a recent article in the “Star Tribune” entitled “Mail-in ballots are a new minefield,” it was noted that in a study covering the last presidential election conducted by Charles Stewart III, a political science professor at the Massachusetts Institute of Technology, out of 35.5 million voters requesting absentee ballots, 27.9 million were counted. That’s a difference of 7.6 million ballots or a failure rate of 21%. Our conclusion from this study is, vote at the polls, not by absentee ballot, if you want to be sure your vote is counted.

New Look and Reporting Coming Soon!

We will be deploying a newly-crafted look including company logo, marketing material and reporting software. You should expect to see enhancements to your statements and other changes early next year.

ket performance. The “unified” situation refers to years when the Senate, the U. S. House of Representatives, and the White House were all controlled by the same party. The “partially divided” situation represents years when the House and Senate were controlled by the same party, but the White House was held by a different party. The “completely divided” situation uses data from years in which the two houses were divided. Both the S&P 500 and the diversified portfolio (60% stock/40% bond) averaged the highest returns during unified years, lower returns during partially divided years, and lowest under completely divided years.

The Politics of Oil

With gasoline prices reaching \$4 at the pump (much higher in California), energy costs will probably be a major factor during the 2012 election season. Each candidate has made promises regarding the reduction of our dependence on imported oil. In fact, oil imports (measured in thousands of barrels) have been dropping since 2006. This is due to energy efficiency gains implemented over the last couple decades, a slower economy, and technologies that have made available

Notable Quotes

“A market is the combined behavior of thousands of people responding to information, misinformation and whim.”

Kenneth Chang

“Money will buy a fine dog, only kindness will make him wag his tail.”

Anonymous

“Every day I get up and look through the Forbes list of the richest people in America. If I’m not there, I go to work.”

Robert Orben

“A good time to keep your mouth shut is when you’re in deep water.”

Anonymous

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“My roller derby name is ‘Wall Street’ because it’s thrilling when I jump, scary when I fall, and everyone gets hurt when I crash!”

“Our greatest compliment is your referral.”



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GS Tenets

Who is GSI?

GS Investments, Inc. is an investment management company specializing in individual and institutional asset management. Privately owned and operated, GS Investments, Inc. is run by its owners, Glenn H. Steinke, C.F.A., and John G. Steinke, M.B.A. and Greg Cunningham.

Glenn Steinke, CFA brings over 45 years of investment management experience to the business. Previous capacities include Vice President and Senior Investment Officer with a major pension fund (\$1.8 billion under management) and Senior Vice President with a major Minneapolis-based financial institution (\$3 billion under management). Glenn is a graduate of the University of Minnesota.

John Steinke MBA offers a broad financial services background with 18 years of portfolio management experience and 7 years of banking experience including capacities as a Vice President of a \$50 million bank and as a private banking officer for a large, Minneapolis-based financial institution. John received his BA from Concordia College (Moorhead) and his MBA from the University of Minnesota.

Greg Cunningham comes to us from Minneapolis-based Ameriprise Financial, a national leader in financial planning with over 2 million retail clients and \$300 billion in assets. Greg spent 15 years at Ameriprise, most recently in the asset management group. In this role he worked with the Chief Investment Officer in support of the international and domestic hedge funds and with the President and General Manager of Riversource mutual funds. Greg is a graduate of Gustavus Adolphus College in St. Peter, MN.

Sheri Ritchie brings over 20 years of financial services experience to the business. Previous capacities include client service and support positions with Dean Witter and Kemper brokerage firms and a Minneapolis-based investment management firm. Sheri is a graduate of the University of St. Thomas.

GS Investment Philosophy

GS Investments, Inc. utilizes a balanced approach for the majority of its accounts although each account is tailored to the individual needs of each client. Taxable or tax-exempt bonds are used along with a common stock component. The division between bonds and stocks is determined by the personal objectives of each client. A need for income and a willingness to assume risk are also determinants of an account's bond/stock mix.

GS Investments, Inc. emphasizes the purchase of quality securities and employs a long-term investment style, as market timing, frequent shifts in asset allocation and interest rate forecasting are not consistent with the firm's philosophy. In-depth market analysis and many years of experience support this approach.

GS Fixed Income Strategy

GS Investments, Inc. emphasizes a staggered maturity approach when purchasing bonds. Individual security investment grades and call protection are considered when making these investments. Quality grades of "A" or higher are favored with tax-exempt issues. Government bonds are dominant among taxable securities.

GS Equity Strategy

GS Investments, Inc. favors stocks emphasizing quality and growth. Appropriate cyclical growth stocks and small capitalization growth stocks are used periodically as well. Additionally, GS Investments, Inc. believes that a growth oriented philosophy tends to result in less frequent trading and lower tax payments (for taxable accounts) on realized capital gains. This provides a lower cost approach for the client.

GS Investments, Inc. emphasizes client communication. Written investment objectives as well as periodic oral and written reports are used to heighten the understanding between the client and investment manager. In addition, easy to read, detailed reporting is provided by state-of-the-art investment software in order to inform the client of portfolio progress.