2016 1st Quarter

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PERFORMANCE WEIGHTED ASSET ALLOCATION REPORT

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ADVISORS' THOUGHTS

The first quarter of 2016 was a rocky ride for the stock market, but by the end of March it was more like a round trip to nowhere. For the quarter, the **S&P 500 eked out a 0.77%** gain as noted in the Benchmark Return Table. However, the **path that it took scared some investors to sell** out of the market at just the wrong time.

During this volatile period **we held your portfolio allocations the same**. Based on all available information it **appeared to us** that the market was experiencing **a normal correction** and not the start of a bear market. With this backdrop we are pleased to report that **many of you achieved a small gain for the first 3 months** of the year as reported on your quarterly statement.

The year began with the S&P 500 trading at 2,043.94, but by February 11th when the market closed at 1,829.08 it had fallen 10.5%. Similar patterns occurred in most stock benchmarks around the world with MSCI EAFE (large company international stocks) down 3.74% at the end of the quarter. The turnaround in stocks was most pronounced in the area of emerging markets. The MSCI Emerging Markets benchmark started the year down 13.3% on January 22nd only to end up for the quarter 5.36%.

(Continued on Page 4)

BENCHMARK RETURNS THROUGH 03/31/2016

	3 Mo.	6 Mo.	12 Mo.
DJIA	1.49%	8.60%	-0.51%
S&P 500	0.77%	7.28%	-0.39%
Russell 2000	-2.24%	0.89%	-11.36%
MSCI EAFE	-3.74%	0.46%	-10.67%
MSCI Emerging Markets	5.36%	5.65%	-14.14%
Barclays Inter-term Bond	2.16%	1.26%	4.57%
Barclays Long-term Bond	7.79%	5.82%	3.23%
ML High Yield Bond	3.23%	1.07%	-3.90%

Source: Wall Street Journal and Morningstar Principia
Does not include reinvestment of dividends

DJIA: A price weighted average of 30 stocks.

S & P 500: A market value weighted index of 500 stocks.

Russell 2000: A market value weighted index of 2000 stocks.

MSCI EAFE: A stock market index designed to measure the equity market performance of developed markets outside US and Canada.

MSCI Emerging Markets: A stock market which captures large and mid cap representation across 21 Emerging Market countries..

Barclays Capital Treasury Intermediate-Term Bond Index: An index comprised of US Treasury securities with maturities between 2 and 10 years.

Barclays Capital Treasury Long-Term Bond Index: An index comprised of US Treasury securities with maturities of 10 years or longer.

ML High Yield Bond: An index of non-investment grade corporate bonds.

For many people the looming deadline of April 15th (April 18th this year) is an annual ritual of learning what their tax burden will be and then scrambling to make a retirement plan contribution. This may be to their Individual Retirement Account (IRA) or for business owners their company retirement plan. Either way their immediate goal is to receive a tax deduction and reduce their income tax burden. These plans can be a wonderful way to save for retirement, yet they all have a drawback; eventually income taxes will be due when money is withdrawn from the plan. If only there was an alternative that could provide tax free withdrawals from a retirement account. There actually is such a choice and it is called the Roth IRA.

Established by the Taxpayer Relief Act of 1997, the Roth IRA was named after the late Senator William Roth, Jr. of Delaware, who was its chief legislative supporter. Beginning in 1998, taxpayers were permitted to contribute up to $2,000 of their after-tax earned income to a Roth IRA. Catch up contributions for people age of 50 and over had not yet been established (that began in tax year 2002).

A **Roth IRA is subject to many of the same rules that apply to a traditional IRA** with **some exceptions** as noted here:

- **Contributions made to a Roth IRA** are deemed after-tax money and therefore are **not deductible from your tax return**.
- Contributions can be made to a Roth IRA after you reach age 70 ½ provided you have taxable compensation (earned income).
- **Qualified distributions are tax-free if certain requirements are satisfied**. These requirements are discussed later.
- Minimum distributions (RMD) are not required; you can leave amounts in your Roth IRA as long as you live.
- The account or annuity must be designated as a Roth IRA at the time it is set up.

Like all IRA's, Roth IRA's grow tax deferred. There is no potential tax obligation until money is distributed from the account. Then if certain conditions are met, the withdrawals from the account will be tax free also. This can be a powerful planning tool as you can potentially better control your taxable income by having some of your retirement money free of income tax.

However, **not everyone can contribute to a Roth IRA** because of **limitations based on**

If your filing status is...	And your modified AGI is...	Then you can contribute...
married filing jointly or qualifying widow(er)	< $183,000 or less	up to the limit*
	≥ $183,000 but < $193,000	a reduced amount
	≥ $193,000	zero
married filing separately and you lived with your spouse at any time during the year	< $10,000	a reduced amount
	≥ $10,000	zero
single, head of household, or married filing separately and you did not live with your spouse at any time during the year	< $116,000	up to the limit*
	≥ $116,000 but < $131,000	a reduced amount
	≥ $131,000	zero

***Contribution limit for 2016 is $5,500 ($6,500 if age 50 or older)**

your filing status and income. The same contribution limit that applies to traditional IRAs also applies to Roth IRAs. In 2016, the contribution limit amount is $5,500 ($6,500 if you are age 50 or older).

The **table on the previous page** shows whether your 2016 **contribution to a Roth IRA** is **effected by the amount of your modified adjusted gross income** (AGI).

On its website, the IRS does provide the calculation to determine ones' contribution limit. As with most IRS related topics, it can be a little confusing. Therefore, we suggest contacting your tax preparer before contributing to a Roth IRA.

In addition to Roth IRA's, **many 401(k) retirement plans now offer a Roth salary deferral** option. Contributions made to your retirement account with this provision work in much the same way as a Roth IRA. There is **no tax deduction for the contribution**, but account **balances may grow tax deferred** and **future withdrawals may be tax free**. Furthermore, unlike the Roth IRA there are **no income limits of who can contribute** to their Roth 401(k). If your company retirement plan offers the Roth contribution, you may take advantage of it.

As mentioned earlier in this article, **qualified distributions from a Roth IRA are tax-free**. In order to be defined as a qualified distribution **certain requirements must be satisfied**. **First** one must meet the **Five-Year Rule** plus one other condition. According to IRS Publication 590-B "it **(a qualified distribution) is made after the 5-year period beginning** with the first **taxable year** for which **a contribution was made** to a Roth IRA set up for your benefit, and" one other requirement is met.

A **second requirement** to make a distribution "qualified" is that **you must be at least age 59½**. If both these requirements are met, Five-Year Rule and at least age 59 ½ your Roth IRA withdrawals become tax free. There **are additional conditions that meet the second requirement** for example if one becomes disabled (as defined) withdrawals may be tax free.

What happens if you already have a traditional IRA, but decide after reading this article, a Roth IRA might be a better fit for you? The IRS does allow the **conversion of traditional IRAs to Roth IRAs**. "Fantastic!" you might be thinking. It **might be a great opportunity** for you, but there are a number of things to keep in mind.

The **most important item to think about** when converting to a Roth IRA is the tax consequences involved. That's right. Taxes. When **converting from a traditional IRA to a Roth IRA, you pay income taxes** on the untaxed amount of your IRA that is converted. The amount you convert could put you into a higher tax bracket. If you have a sizeable account, you might be faced with a sizeable tax bill. Do you have enough money set aside to cover a large tax bill?

Still, converting your traditional IRA to a Roth IRA might make a lot of sense. Remember, qualified distributions from a Roth IRA are tax-free. Therefore, if you make the conversion and pay the taxes today, you will not pay taxes on distributions in the future. Note: The Five-Year Rule (mentioned above) applies to Roth conversions also.

Like its cousin the traditional IRA, a Roth IRA can play a significant role in retirement planning. Which one is more suitable for you, depends on your situation. That is why it is so important to come **talk with us at Braziel & Associates, LLC before making any changes with your retirement accounts**. We will work with you and your tax preparer to determine if a Roth IRA is the right choice.

(Source: IRS Publication 590-A and 590-B)

Deep concerns over weak global growth (Europe and China), tumbling oil prices, a strong US dollar and the direction of Federal Reserve interest rate policy weighed on investors. Worry over how these conditions may halt the US expansion led investors to sell stocks early in the year. However, since that time of heightened concern many of these conditions have shown improvement.

Oil which **bottomed on February 11th** for West Texas Intermediate **at $26.21 is now trading near $40 per barrel**. This has translated into **significant improvement in the financial well-being of the energy sector** which had recently been a drag on the US economy.

Also supportive of higher oil prices has been a weakening US dollar. The market for oil globally is priced in US dollars. Therefore when the dollar weakens relative to other major currencies the price of oil, if all other factors remain the same, will tend to rise.

The **declining value of the US dollar** in the past two months has **improved the competitiveness of US multi-nationals**. The Institute for Supply Management's manufacturing purchasing managers index rebounded strongly in March to 51.8. Any reading above 50 is considered expansionary. March was the first month the manufacturing sector expanded in six months.

As the year began, it was believed that the **Federal Reserve was on a path to raise interest rates four times** this year. The health of the global economy did not seem to support that interest rate trajectory as investors feared these rate hikes may cause a recession. **Recent decisions and statements by the Fed** have **reassured investors** that the **path to rate hikes will be much more gradual in 2016**.

Today the health of the US economy appears more in balance. The job market continued to expand throughout the first quarter. Nonfarm payrolls expanded 215,000 jobs in March with more people re-entering the labor force as the participation rate rose to 63%.

With the **immediate fear of a recession dissipated investors are more focused on current and future corporate profits**. When the year began, according to S&P Capital IQ Lookout Report April 15, 2016, "…the consensus for the S&P 500 was 1.2% earnings growth." Near the **start of this earnings season analysts** are now **expecting earnings to decline 8.4%**. These downward revision in estimates we believe were largely driven by the same factors listed above. While it is typical for estimates to come down during the quarter the magnitude of this change is particularly large. However, **early reports** are showing **actual earnings are handily beating analyst estimates**. We are anticipating a year-over-year decline in earnings, but with reason to believe that the **worst of this multi-quarter decline in earnings may be nearing an end**.

It is clear that the US economy hit a soft patch during this economic expansion. However, there are signs that the economy may be gaining strength again. We are continuing to monitor economic and financial conditions and **remain positive about the continuation of this expansion**.