Pacific Crest Financial Advisors, LLC

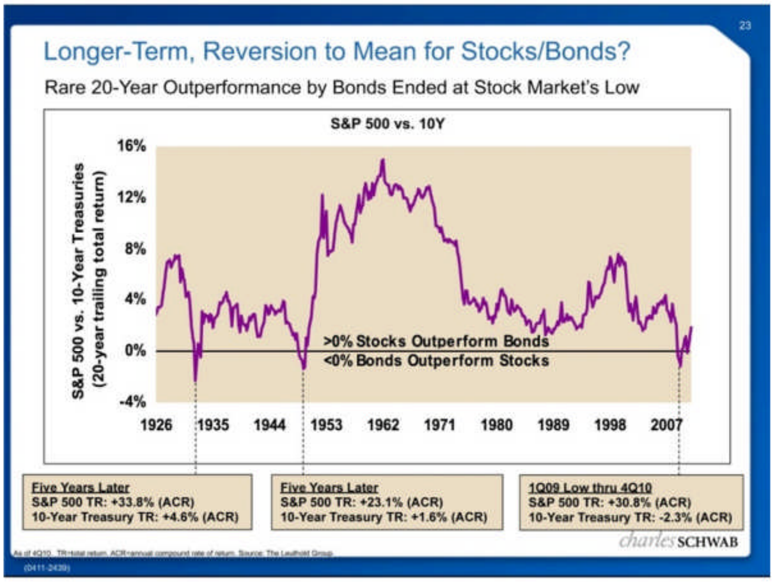
Dear Clients and Friends,

In this first quarter stocks continued to post positive returns, with domestic equities posting returns ranging from roughly 6% to 8% depending on the asset class (smaller-caps and mid-caps generally beat larger-caps), while high-quality bonds were slightly positive. Overseas, returns for both developed and emerging-markets equities were lower, at 3% and .5% respectively.

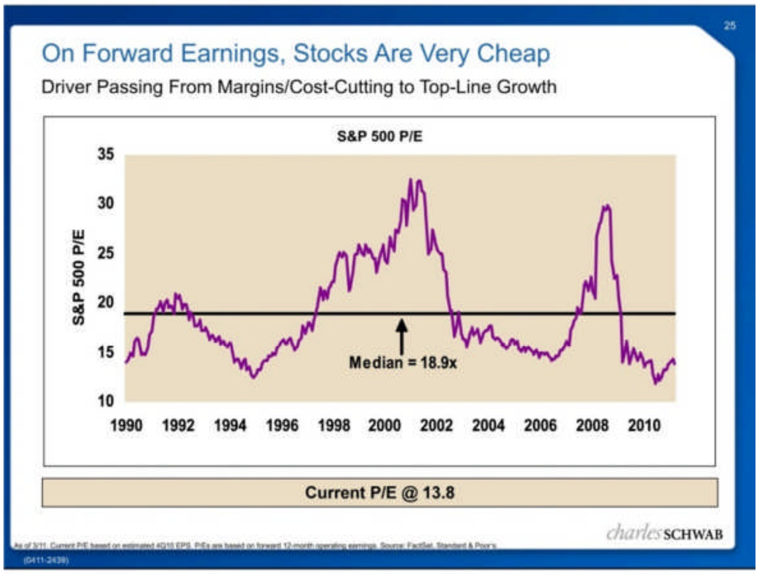
We have had two years of recovering markets. It was so tempting to pull all of ones “risky” investments in those harsh days of early 2009 but you stayed the investment course (against your emotional desires). We heard frequently a suggestion that we should sell off part or all of the equities until the market returns to a more normal state. If we had sold off those equities waiting for a calmer market, we would have likely missed much of the 79% rise in the S&P 500 that occurred from March 2009 to March of 2011. Investing driven by emotion frequently causes us to sell out at the lowest and buy towards the highs.

Along those same lines, we are all hearing lots about the need to invest in gold and if you do not invest you will be left behind. We would argue that gold is now priced at a dear level and to use caution on any allocations of new capital commitments in that area. The long-term (150 year) average return on gold is .7% over inflation. If you exclude the last five years, the long-term return is nearly zero over inflation. Morningstar showed the 30 year return at 2% while the one year return was 30%. Simple reversion to the mean would indicate that the price of gold is bound to go the other way at some point in the future. Gold has little intrinsic value. Its price is simply based on what people are willing to pay for it. Gold on its own does not generate value. Just as it was so tempting to sell off those equities in early 2009 with all the bad news flooding us. It is very easy to buy gold now on the emotional pitch we are frequently hearing.

Below we have a graph showing the pattern of bonds out performing stocks. At the market bottom in 2009 we hit a rare point when 20 year stock performance was out done by the 10 year treasury bonds for the period. This is the third time in the modern US market that bonds have outperformed stocks for an extended period of time. After each of these previous events, stocks have rallied back to outperform US treasury bonds. We believe that pattern will continue to be repeated. We are not arguing that stocks are going to do brilliantly but we support the view they will outperform bonds.



A second data point worth a look is the forward looking price to earnings ratios (P/E). The S&P 500 is priced well below the average P/E ratio over the last 20 years, a good sign of value in the equity market.



We have had two years of recovery from the depths of the early 2009 market bottom to our present market levels. We do not expect these tremendous returns to continue over the next few years. With interest rates currently very low, bonds are generating a low return from yield. Further, with government policies likely to contribute to longer-term inflationary pressure, we are more likely to see rates rise (which pushes bond prices lower) than fall over the next few years. One of our key economic review services that we hire expects only low single- digit returns from core high-quality bonds. In using individual bonds, we do avoid the long-term loss of principal that can occur in a bond fund. With individual bonds we avoid that permanent loss of principal because each bond has a maturity when the original principal is paid back.

Estate Planning

We now have a record high $5,000,000 estate tax exemption that many people are aware of but few have noticed the gift/estate exclusion portion is only certain for 2011 and 2012. Those with potentially taxable estates may want to consider accelerated gifting in 2011 and 2012. The federal gift/estate exclusion will revert back to the one million exclusion level unless Congress takes action. Where many more might get into unexpected estate taxes is at the state level. In Washington State, the estate valuation over $2,000,000 is taxed at a starting level of 10%.

Many of our clients financially support their grandchildren's educational expenses. These educational gifts from grandparents or extended family have no restrictions or limitations if the checks are made directly payable to the educational institution. Among our client base we are seeing more and more gifting in the form of grandparents helping out with grandchildren's educational expenses. We cannot think of a better gift then to help your family pay for educational expenses. However, as some of you know, we remind our clients that part of your children's or grandchildren's education is taking part in choosing and buying the education. If they contribute in some way towards the cost, they will consider their options more carefully. Just as if a young person makes a more careful purchase on their first car if they had to work and save up for part of the cost of the car. Paying all cost of college education takes away one of the most important educational experiences. We argue that when all costs are paid for, the college student is losing out on the opportunity for pride of ownership. Whether it is having an equity stake in purchasing a car or purchasing an education, the supporting adults are depriving the student part of their needed education if the students are not contributing capital to the purchase of education.

CDs

Many clients have a collection of their own CDs (at local banks). Please consider us a resource for those CDs also. We can quickly email you a list of local or national institutions with their CD rate offerings in the maturities you are looking for. We strive to be a financial resource to our client base.

Along those lines of offering additional services, we are available to spend a two hour period with any of our on-going client's adult children to review their 401-K or other financial questions they may have.

Charitable Gifting

If you are taking required minimum distributions (RMD) and accordingly are at 70 ½ or older and do not need the capital for living expenses, you can have the RMD (or portion thereof) made directly payable to the charitable organization of your choice. The direct charitable gift counts towards your RMD. You cannot take a tax deduction for the donations, but the distribution will not show up on your tax return either. The direct charitable gifting allows the donor to lower the deductible threshold to take some Schedule A (tax return) deductions.

State of our office

We have not only made it through the first quarter we have already built a viable business that is sustainable in its present size. We cannot thank you enough for your confidence in us. We continue to strive to build a locally owned high touch personal financial planning business where we know each and every client. The two office locations are working well. We are generally scheduling two days a week in Seattle and two days a week in Everett with Fridays spent at our respective local offices. Thus we are working physically together four days per week and spend much time talking over the phone on Fridays. Our office phones are forwarded to our cell phones and so if you call the office we are not in we will either answer or return your call promptly.

We have spent the past six weeks intensively meeting with clients to ensure all our financial data and long-term cash flow projections are current and have been reviewed both by us and the client. We should be rapping up the initial client meeting schedule in the next few weeks.

Our current client load is such that we have additional room to grow and greatly appreciate those of you who have been sharing our name and the work we do.

Sincerely,

Alec

Darron

Alec Williamson, CFP®
Managing Director

Darron Kuehn
Managing Director