Dear Clients & Friends of Patriot Investment Management

The dog days of summer are here, but where are the down days? It would seem that the perennial pessimistic financial journalism that we all are bombarded with continues to fly in the face of reality. While the gloom-and-doom, world-is-coming-to-an-end stories and headlines sold a lot of papers and magazines during the dark days of the financial crisis, that tag line has gotten pretty stale. So here is a reality check.

First, the quarter's bad news – After setting a new all-time record on May 28th, the Dow shed 700 points over the following month due to Federal Reserve Chairman Ben Bernanke's announcement that the Fed would begin to taper their monthly bond buying later in the year, and plans to end bond purchases by mid-2014, providing the economy and unemployment numbers continue to improve. Fear that this announcement might mean a slowing U.S. economy triggered a worldwide selloff, and was compounded by China's slowing economy, and by the Bank of China's deliberately generated cash-flow crunch to flush out speculative banking. These events in turn squeezed the already hard hit emerging markets and commodities sectors, with gold ending the year to date down almost 30%.

Now, the good news – After Mr. Bernanke reassured markets that 1) this shift was not eminent, 2) it would be gradual, and 3) the Fed has no intention of raising interest rates any time soon, global markets quickly recovered, and the Dow has now recorded new all-time highs. The 10-year bond has absorbed this news and its yield is coming back to more normal levels. Indeed, Bernanke's tapering announcement is excellent news, as it means that GDP is growing at a rate such that less stimulus is needed to promote economic recovery. The effects of Japan's economic restructuring, coined 'Abenomics' after new Prime Minister, Shinzo Abe, look promising to finally pull Japan out of more than two decades of deflation over the next two years. U.S. economic indicators continue to strengthen, from retail and auto sales to housing to an increase in industrial production. Gold is a financial crisis haven; losing its luster means the global economy is moving past crisis mode.

It is a fact that the Great Recession was the worst recession this country has seen since the Great Depression; however, there is no comparison between the severity of the financial crisis of the 1930's and what we have experienced in the last five years. Most Americans today were born after the Great Depression, and have had no direct experience with a financial crisis of this magnitude – for many, especially the millions who found themselves unemployed, this Katrina of recessions embodies the same life changing trauma, and a generation will likely be shaped and influenced by these events just as our parents and grandparents were by the Depression. Many have good reason to feel gun-shy, but for the financial press to prey on fear and continue to promote catastrophic 'news' when the world is beginning to move on is sensationalism, not journalism.

Yes, it has been a weak and jobless recovery, but it has also been a steady one since the market bottom in March 2009. Markets will rise and fall; recessions will come and go. That is a normal part of the business cycle. Far from catastrophic, this quarter's bad news is beginning to look more like business as usual, and that is great news.

S&P 500	2.8%
Dow	2.3%
Russell 2000	4.1%
EM	-10.89%
10 yr Bond	2.48%
Inflation	1.8%
Unemployment	7.6%

What your Index Annuity Salesperson Won't Tell You

Wouldn't we all love an investment that follows the stock market up, but never goes down? Scared of stocks? Worried about outliving your money? Index annuities promise you'll share in the upside of the stock market with no downside. How about an additional guaranteed 6% tax-deferred growth rate? How about another 10% bonus? It sounds like a retiree's dream. The weekend talk-radio hours are filled with "retirement specialists", who tout the safety of these investments that are paired with the guarantee of never outliving your money.

Our clients frequently receive letters in their mailboxes with invitations to seminars at expensive restaurants to learn about these great investments. At the dinner seminar, the sponsors will usually display a 12-year S&P 500 stock market chart that includes the last two recessions that followed the 2001 dot-com bubble and the 2008 financial crisis. Since the index annuity value stayed level during these recessions, the annuity chart finishes higher, proving the superiority of the index annuity over investing directly in the stock market.

Could there be a catch? There are several, many of which you will find if you read through the fine print of the index annuity prospectus.

1. You don't quite get the return of the index. While the annuity may be indexed to the stock market, there are "participation rates", "cap rates" and/or "asset fees" that the insurer imposes. The insurer usually has the option of changing these limits annually. The stock market could rise 20%, but these limitations may only allow the annuity to rise 5% or less.
2. The index does not include dividends. Dividends currently make up around 20% of stock market returns. In 2011, the S&P 500 finished the year with no gain, but investors received 2.1% in stock dividends. An index annuity account saw no gain in 2011.
3. Lack of liquidity. Significant surrender penalties (12% average) usually apply to investors who need access to their money. This lock up period lasts as long as 12 years with the penalty declining over the surrender period. The insurer needs this time to earn back the large commissions that they pay to the salesperson.

4. Most people never annuitize. "To annuitize" is to give your entire account to the insurance company in return for a lifetime income stream. Generally, people prefer to have these funds available for a healthcare or other emergency and to spend this money as they need it.
5. Bonuses and income guarantees can cost you. They always come with tradeoffs such as higher surrender fees or lower caps on returns. Often, these values are held in a separate account and are only available for annuitization, i.e. the bonus and guaranteed income can never be withdrawn in full.
6. Your taxes may be higher. Upon withdrawal, earnings are taxed at ordinary income rates rather than the lower long-term capital gains rates… and earnings must be withdrawn first. There is also a 10% penalty for withdrawal of earnings before age 59 ½.
7. Your insurer may not be around in 30 years. If the insurer goes out of business, these benefits will disappear.

How well do index annuities really perform? Most investors will see their accounts grow much slower than they expect. While the two deep recessions over the last 14 years was a great period to compare an index annuity to the S&P 500, a typical index annuity would have lagged an investment portfolio with equivalent risk – a mix of 85% one-month Treasury bills, and 15% large cap stocks, for example -- by nearly two percentage points annually over the past 44 years. In only two of the past 44 rolling 10-year periods would the most widely sold index annuity have beaten this conservative 85% T-bill/15% stock portfolio.

While other types of annuities may be appropriate for some investors under limited circumstances, index annuities usually fail to live up to the hype.

Patriot News & Community Events

In sporting events...In June, Patriot's Adam Brock and his daughter Berkeley won the 2013 USTA National Father/Daughter Mixed Doubles Hard Court Championship in San Diego. Adam played on the pro tennis circuit after college, and Berkeley was a nationally ranked player in college. This is their third national event they have won together. On June 20th, Kate Moehl led the Patriot sponsored women's softball team to victory in the Oak Ridge Recreational Summer Softball League, winning the first place trophy. Congratulations, Adam and Kate!
Save the Date! This year marks the 20th anniversary for the Buddy's Race Against Cancer 5k Walk 'n Run, to be held on Sunday, November 10, 2013, at World's Fair Park. All funds raised through this event are used locally by the Thompson Cancer Survival Center to provide much needed cancer screenings and education to thousands of medically underserved individuals in the East Tennessee area.

Patriot is a proud sponsor of the Buddy's Race, and we would love to have you join our team this year. If you would like to participate, email our team captain, Laura Bolton (lbolton@patriotinvestment.com) and she will provide you with more information as race preparations are finalized later in the year. You can learn more about this worthy cause at www.buddysrace.org, or click on the link.

Thank You!

We value the confidence and trust you have placed with us, and we welcome your questions and comments. Our goal is to be our clients' trusted resource for all things financial.

Do you know someone who could benefit from our expertise? We appreciate your introductions and the opportunity to help your friends and colleagues meet their financial goals.