



COMPASS
ADVISORS

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Investment Directions

Fall 2012

Keys to Effective Investing

Three Decades of Experience

This year marks thirty years since I finished my university finance courses and entered the investment industry. That is long enough to have seen many changes and to observe both good and bad investment strategies.

Marvelous technological advancements have helped every investor from the sage to the swindler on Wall Street. Not surprisingly both shady schemes and prudent plans have multiplied.

In my experience, successful strategies over the years share four common cornerstones: discipline, patience, purpose and understanding.

Discipline

Discipline starts with investment principles you are committed to observing. Diversification is one such principle. Diversification does not guarantee gains or eliminate losses; it is a means to manage volatility. It may help us avoid the temptation to put all our eggs into an Enron basket or drink the Kool-Aid of an enthusiastic forecaster's projection.

Prudent asset allocation is another such principle; it is purposeful diversification. By carefully combining different types of investments a portfolio can be tailored to your goals. Discipline in asset allocation requires reason prior to change.

Patience

Patience is a virtue in investing as it is in life; a patient investor is wise. Here at Compass Advisors we regularly research money managers by evaluating years of data.

Occasionally after selecting an outstanding manager we see their performance falter for a time. While some may be tempted to immediately fire the

manager, we prefer to be patient. Poor performance is often temporary and a good manager's track record is built over years not months. Patient investors avoid the siren song of last year's hot stock and the expense of rapid-fire trading.

*"It is possible to be busy
– very busy – without
being very effective."*

Steven Covey

Purpose

Purpose addresses the *why* rather than the *how* of investing. Profit alone, making more money, is a weak motivator.

Powerful purpose often involves providing for your family, pursuing your passion or realizing your dreams.

When Alice asked the Cheshire cat if he could help her find her way he wisely responded "That depends on where you want to get to." One of Steven Covey's *7 Habits of Highly Effective People* is to "Begin with the end in mind."

When you know the *why* you can invest with purpose, improve your experience and possibly achieve a better outcome.

Understanding

Finally, successful strategies include only investments you understand.

One of the causes of the now-popped housing bubble was the creation of derivatives. I dare say few, even on Wall Street, understand them. They are risky, complex and nearly unpredictable. Derivatives were a major cause of the housing bubble, banking meltdown and Wall Street losses. Much pain could have been avoided if more investors would have only invested in what they understood.

These are some of the lessons I have learned in the past thirty years. In the decades ahead I believe we could all profit by adopting strategies built on these solid cornerstones. Let's do it.



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Vacation Spots You May Not Want to Miss

Some vacation destinations get overlooked ... perhaps for good reason. The following need no further explanation:

World's largest ball of twine, Darwin, Minnesota



Wallpaper Museum, Akaa, Finland



Outhouse Museum Gregory, South Dakota



Announcements

Josh Nicholls Pursues a Master's Degree

Josh Nicholls, the new Dad highlighted in this space last time has been accepted at the BYU Marriott School of Business into the Masters of Information Systems program (Geek speak for complicated computer stuff). As a result, he and his little family have moved to Provo, Utah where he will be studying.

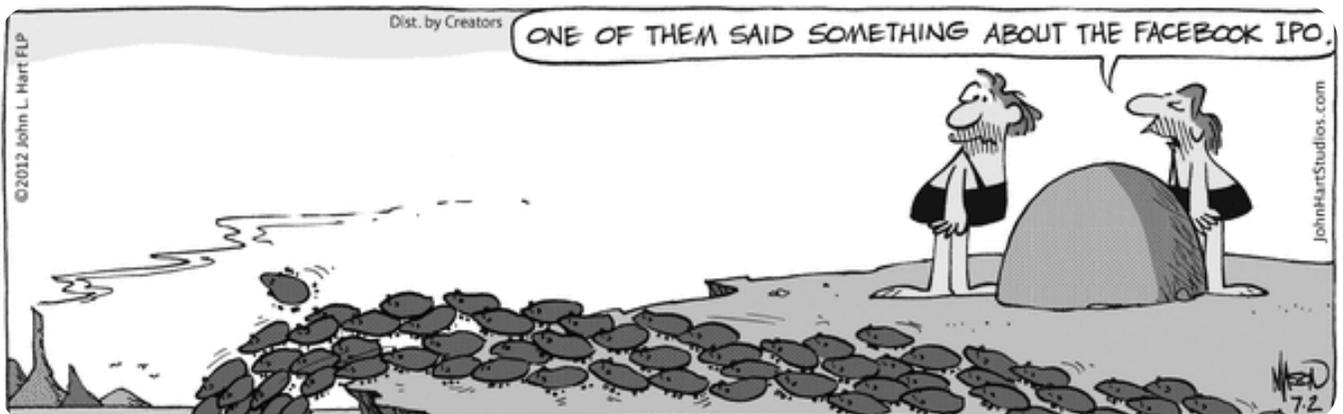
Randy and Kelly Nicholls, while excited for Josh, already miss little Emma and look forward to visiting her soon.

Kell Bjorn Joins Compass Advisors

In related news, Kell Bjorn, a local young man with a degree in Business Marketing has joined Compass as our new Director of Business Development.

Kell is married with one daughter and a son due to arrive in September. He returned to the area to join Compass after running a successful small business in Mesa, Arizona. We are excited to have him join the team; he is a great communicator, a clear thinker and an organizational whiz. Welcome Kell!

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Facing the Music

Let's be frank: Have you ever seen interest rates this low? I have not. So, what does this low interest rate environment mean to you? It depends on your stage in life.

For someone who is saving for retirement it means you will have to save a lot more if you plan to live on interest from good quality American bonds. The chart above illustrates how much more.

Here is why: In August 1992, ten-year Treasury bonds paid 6.72% interest. This year in August, ten-year Treasury bonds paid 1.56%. That means in 1992 you could have invested about \$178,000 and earned about \$12,000 interest or \$1,000 per month. Today to generate the same income you would have to invest over \$769,000. (Data is from the U.S. Treasury Department, available at www.treasury.gov)

For someone in retirement, this means if you are depending on bond interest for your monthly income, it is probably much lower than it once was.

Assessing the Change

Before we can discuss strategies to address this problem, we need to look at how we got here. Clearly, over the last several years interest rates have dropped. Because rates fluctuated every day,

sometimes down and sometimes up, the dramatic trend may not have been obvious at first. When Certificates of Deposit renewed at the bank, most folks noticed the renewal rate was lower than the original rate. For bond fund investors the trend was more subtle.

This is the tricky bit and you need to be careful so you won't get burned. As interest rates fell, bond values tended to go up and that made bond funds look pretty good. If interest rates stay the same or go up, bond funds may not get that benefit and returns may look worse, they could even go negative for a time.

Orchestrating Income

Now that we understand what has been happening we can talk strategies. Perhaps an analogy might be instructive. Music can be made by one instrument or many. Successful investing is a bit like making music.

An orchestra combines strings, woodwinds and brass instruments to provide a rich, full sound. Each plays an important part delivering a unique sound which can complement the others. Similarly, income can be generated using multiple instruments and by combining them may create a full and well-balanced portfolio. Bonds are like trumpets, they are great but other instruments may enrich the experience.



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New Tools for New Times

As a young boy I loved to work with my Grandpa. He had a wonderful old toolbox he kept on his wooden workbench. It seemed he had a hundred different tools, each uniquely designed for a mysterious purpose I could not imagine. When we worked together he would often reach into his toolbox, pull out one I had never seen before and teach me how to use it. He taught me if you want to do the job right you have to use the right tool.



In contrast, Abraham Maslow once said: "If you only have a hammer, you tend to see every problem as a nail."

Consider the manly chainsaw – a loud, powerful and effective tool. I like chainsaws; a friend of mine always carries one in his trunk just in case he needs it. As wonderful as a chainsaw is, few of us would use it to prune a bonsai tree. Good tool but bad for the task.



Over time the challenges we face change. This requires new solutions and often new tools. Fortunately, in the investment world we have many good tools and can choose the right one for the job at hand. When change happens, we would do well to look in the toolbox, put down the hammer and select the right tool.

