First American Trust

WEALTH MANAGEMENT SERVICES

Spring 2014

QUARTERLY UPDATE

First American Trust provides investment advisory and fiduciary services for individuals, families, non-profits and corporations.

My Two Cents

By Kimberly Dwan Bernatz, CFP®, AEP®

The Difference between Men and Women

I doubt many would argue with the statement that men and women are very different. John Gray's bestselling book ***Men are from Mars, Women are from Venus*** provided a practical guide to many of the common relationship problems between men and women that result from fundamental psychological differences between the genders. And when it comes to financial planning, several recent studies have also shown that there is a big difference between how men and women view finances during various life stages.

Having worked with male and female clients ranging from self-made millionaires to those who have inherited family fortunes, I have found that the only similarity is that they are all different. They have different collections of assets, different investment goals, different risk tolerances and different sensibilities.

Even within a household, the financial planning roles are completely different between patriarchs and matriarchs, but gender roles don't tell the whole story themselves. Often, a client's life stage is the most indicative element in their financial planning behavior.

I have worked with many women who have not been particularly active in the family's finances until their husband passed away, suddenly leaving them in charge of the family's financial decisions. Some of my most meaningful accomplishments have come from helping these women grow into the financial leaders their families need them to be. Watching the evolution of these women as they gain financial confidence is incredibly inspiring.

The Confidence Gap

Today, more and more young women are building wealth of their own, and it's a wonderful thing to see. According to Prudential's biennial study on the Financial Experience & Behaviors Among Women, women were increasingly found to be the breadwinners of many households and more likely to be single than a generation ago, either as a result of being widowed or the decision to remain single, marry later or divorce.

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Market Watch

By Jerry Braakman

Economic Outlook

Total Return as of 5/31/2014

Index	Q1-2014	YTD
Dow Industrials	-0.15%	1.92%
S&P 500	1.81%	4.96%
Russell 3000	1.97%	4.32%
All Country World x US	0.51%	4.01%
Barclays Int. Gov't/ Credit	1.00%	2.36%
Merrill Lynch 3-7 Muni	1.20%	2.60%
Gold (SPDR Gold Trust)	6.45%	3.71%

Source: Bloomberg

Equity markets continue to set new highs, but the exuberance we saw last year has been muted. As expected, with a more mature market, we saw divergent trends action in various segments of the market. High flying momentum stocks (think Priceline, Tesla, Chipotle, Twitter, biotech), big winners last year, reversed course and adjusted based on stretched valuations. Meanwhile, defensive sector stocks led the market, with the Utilities sector the largest gainer (+14.7% YTD as of April 30) as investors flocked to value and dividend yielding stocks. As shown in the Russell 2000 vs S&P 500 Relative Performance chart below, we also observed a significant underperformance of small cap versus large cap stocks.

Source: Bloomberg *Russell 2000 vs S&P 500 Relative Performance*

Bond markets have continued to rally as the expected rise in rates has failed to materialize thus far. The 10-year treasury rate has settled into a 2.5 to 3.0 percent range, established since the Bernanke taper fears changed interest rate expectations. Rates have continued to stay subdued without signs of increasing inflation, continued geopolitical concerns (Russia/Ukraine), and slow GDP growth in Q1 due to severe weather. In the precious metals arena, lower treasury rates with stable inflation have helped gold partly recover from last year's painful sell-off.

Fundamentally, U.S. economic activity continues to be stable with gradual improvement continuing. Earnings reported in April for Q1-2014 were solid, supporting valuations. Seventy-five percent of companies reporting exceeded analysts' expectations. Expectations for the remainder of the year are increasing as a cold winter's impact on the economy dissipates.

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Investment Focus

A more challenging market was expected this year as we are extending a very long bull market. But we do not think economic expansion will stall and lead to recession. In contrast, as slack in the economy dissipates, we continue to believe economic expansion will accelerate.

As growth was scarce in a slow growth environment, aided by global weakness, those few companies still exhibiting strong earnings growth were bid higher and higher, creating rich valuations. As economic recovery broadens into mid-cycle, revenue growth will spread to more companies, benefiting value-oriented investment, such as mature large companies. The market signaled this change with outperformance in value and dividend paying stocks since late February, as well as large cap stocks outperforming small caps. Although we think that growth has sold off quite rapidly and provides some near term opportunities, we expect to continue to transition our client portfolios towards more value-based investments in the second half of the year as GDP growth accelerates. Taking a long-term perspective, value does outperform growth with less volatility. The three years prior to February, growth styles did outperform, which helped our performance, but we feel this run is at or near the end.

Mid-cycle economic activity should also impact fixed income expectations. Treasury rates have not skyrocketed as others expected, and this has helped our fixed income return due to our longer duration positions and our exposure to credit (corporate bonds). We are anticipating that rates will eventually move higher, thus, we are shortening the duration of our client portfolios by reinvesting in shorter duration vehicles as existing bonds mature. Our over-allocation to corporate bonds during the last few years have served our clients well as they have performed nicely as credit spreads narrowed. We will bring that allocation in line over the next two years as well. We are not worried about another credit concern cycle in the near term, but do want to work out of our over allocation prior to the next cycle. By reducing our allocation over time, we can gradually implement these changes with maturing cash flows and not have to trade positions or incur trading expenses.

Monetary Policy

The past five years have seen unprecedented monetary policy implementations in the U.S. economy in an attempt to mitigate the effects of recession. We understand some may have different political views on the efficacy of these policies, and while it will take many more years to fully assess, the impact of the policies on our markets is and has been significant. The diatribes of pundits and economic experts are inconclusive. Hence, we continue to focus on economic results more so than Fed actions. Specifically, interest rate changes disproportionally impact variant segments of our economy, and thus an outlook of those changes is important. Although markets can create volatility based on perceptions (exacerbated by hedge fund and computerized trading), our longer term views allows us to disregard short-term fluctuations.

We will continue to focus on what we determine to be drivers of interest rate changes, such as inflation expectations, risk premiums, liquidity premiums and opportunity costs. Looking forward, continued progress on wage growth, unemployment, consumer balance sheets, productivity, factory capacity utilization and other metrics are trending favorable to allow for higher rates. Whether such improvement is attributable to monetary policy, or political party, is not important from an investment perspective. What is important is that these trends continue to be supported and to keep diligent watch for substantial changes in trends to mitigate downside risk.

— Jerry Braakman is Chief Investment Officer
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However, there is an interesting disconnect that studies have found involving younger women who are in relationships. According to one from Fidelity Investments, 24 percent of women from the Baby Boomer Generation identify themselves as the primary household decision maker for day-to-day financial decisions, while only 17 percent of Generation X women and 12 percent of Generation Y women felt the same way. It's a stunning statistic, which implies that women become twice as involved in household finances as they go through different life stages.

Oftentimes, there is a confidence gap between men and women when it comes to financial planning roles, and that gap usually closes over time, as women learn more about wealth management and take on more financial responsibility within the family unit.

Different styles

As women achieve greater financial aptitude, they are more inclined to take the reins from their husbands or other family members; however, that does not mean they are likely to manage money the same way as their male counterparts. The financial styles of men and women can be starkly different from each other no matter what life stage they are experiencing – different concerns, different priorities and different sensibilities.

Consider these findings from the Prudential study:

- When men and women worry about money, they worry in different ways. Women worry most about household expenses, debt and saving for retirement, while men are more focused on broader and more abstract challenges such as the state of the economy.
- Men have a much greater appetite for risk. About 70 percent of women see themselves as savers rather than investors, and they are more likely to put their money in an FDIC-insured product such as a normal savings account. Men, on the other hand, are the exact opposite with 70 percent of them preferring to invest, embracing a certain amount of risk if it could yield a greater financial reward.

- There is also a level of enjoyment that is at play here. About 40 percent of the men in the Prudential survey said they actually enjoy the sport of investing. That's taking confidence to a higher level, and it's very telling about the difference in men and women as it pertains to their financial planning tendencies.

It comes down to confidence, and this conclusion from Prudential could be the most insightful: "Women not involved in financial decisions most often claim a lack of financial knowledge, while uninvolved men say they are too busy with other obligations."

My experience has taught me that no two clients are the same. They each have different financial needs and styles despite what gender or age they happen to be. Yet, these studies can be instructive as they point toward a need for more financial education and empowerment in women.

— Kimberly Dwan Bernatz, CFP® Senior Vice President
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Honors

Gala 2014 Creating Hope

Our own relationship manager, Jody Hudson, was awarded "Alzheimer's Volunteer Partner of the Year" by the Alzheimer's Association, Orange County for her generous volunteer work throughout 2013. Jody, who is a founding member of Alzheimer's Visionary Women 1000, was one of four recipients honored at the event that took place on March 1 at the Balboa Bay Club in Newport Beach. Aside from a splendid gourmet dinner, attendees were treated to a special performance by singer Taylor Hicks, winner of Season 5 American Idol. In addition, the successful event that drew some 300 people raised more than $525,000 for research to battle the Alzheimer's disease, by supporting programs, continuing education and services. Jody requested that any seat purchases and donations be made in honor of her own father, who is currently living with Alzheimer's.

First American "In the News"

Jerry Braakman, Chief Investment Officer, quoted in:

- "Markets were surprised by Citi: Pro." CNBC Europe live on Capital Connection with Caroline Roth, March 27, 2014.
- "For Some Hot Stocks, Trading Winds Blow Cold." The Wall Street Journal, March 25, 2014.
- "Traders Seeking Ukraine Haven Pile Into Treasury Wagers." Bloomberg, March 18, 2014.
- "U.S. Stocks Fluctuate as Investors Watch Ukraine Crisis." Bloomberg, March 14, 2014.
- "Stocks Tumble; Dow Drops Over 200 Points." The Wall Street Journal, March 13, 2014.
- "Stocks rise more than 1% despite weak jobs report." Los Angeles Times, February 7, 2014.
- "ADP Jobs Report Crimps Stocks." The Wall Street Journal, February 5, 2014.
- "U.S. Stocks Rise Amid World Bank Forecast as Banks Rally." Bloomberg, January 15, 2014.
- "U.S. Stocks Bounce Back a Day After big Loss." Associated Press, January 14, 2014.
- "Investors See More Gains for Banks." The Wall Street Journal, January 5, 2014.
- "U.S. Stocks Remain Lower." The Wall Street Journal, January 2, 2014.

Kimberly Bernatz, Director, Wealth Advisory Services, featured in:

- "Lost your job? Here's how to save your retirement." MoneyRates.com, March 25, 2014.
- "Rigorous management principles keep endowments healthy for stability, future stakeholders." Nonprofit Business Advisor, March 20, 2014.

A new look for First American Trust!

We are pleased to announce the launch of our new and improved website! Please visit www.firstamtrust.com to view enhancements that include:

- Overall improvement of the user experience
- More current, streamlined look
- Less clicking, better navigation
- Fly-out navigation and hover effects
- Centralized location for Login links

Events & Happenings

The first quarter of 2014 kept us busy with a variety of mixers and philanthropic events.

February Advisor Mixer

Pre-tax season gave us a reason to thank our trusted advisors with a hosted event in our San Diego region where guests were treated to a special wine tasting with hors d'oeuvres.

Lunch with Beethoven

As a thank you for doing business with us, we held a client event on the afternoon of April 1 at Bowers Museum in Santa Ana. "Beethoven: The Late Great" exhibition included tours and lunch. Docents escorted guests to the Beethoven room to observe rare artifacts with live commentary provided by Dean Corey, Artistic Director and President of the Philharmonic Society of Orange County. Guests also toured the exhibit Soulful Creatures: Animal Mummies in Ancient Egypt. This was followed by the luncheon with a presentation by Mr. Corey, who talked about his recently published book "Beethoven: The Late Great," a curated exploration of the composer. Wealth Management's executive vice president, Eric McMullen, spoke about First American Trust as a client-focused disciplined investment management firm with a history of fiduciary excellence. Some 55 guests attended.

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