

Volume XXI, Issue III

THE HARBOR ADVISOR

What We Know

I frequently ask staff here at Harbor to focus on ‘what we know’ as a starting point for analysis and discussion of topics from investment analysis to client service issues. I coined this phrase to kick-start a process to find a common starting point for creative problem solving. While the strategy has worked well for us, it is also the catalyst for a bigger discussion and I think begs the question of ‘How Do We Know What We Know?’

We derive what we know from life experiences, educational exposure and trial and error, but perhaps most importantly the relationships we form as we progress through our lives. Given some thought, we all can iterate what we know. In thinking about what I know I have come up with a varied and I think interesting list.

I know I value creativity, honesty, kindness, and simplicity. I believe enthusiasm can go a long way toward moving mountains as can a positive attitude. I have learned that if one person cannot do a job, that joined by friends and co-workers, the group can accomplish great things. I know that one person can and does make a difference, every day and that knowledge of this can be life changing for me and for the people I encounter in my daily life. The older I get the more people I have had the opportunity to know and to touch and the more they have affected me. I know that I am devoted to lifelong learning and that teaching what I know is gratifying. I know it is important to treat people I encounter as I would like to be treated; with kindness and respect. I know that listening to others is a great way to learn and distill my own opinions.

I know I don’t know it all and learn every day.

Realization of what we know here at Harbor becomes a springboard for meaningful discussions that are more focused and immediately interactive. We have found that the process also focuses the seemingly unending information and data available to us down to a more manageable set to with which to deal. This in turn simplifies the decision process. It also allows us to pass along a simplified set of information to you focusing on what is pertinent and important in your life. Finding new and creative ways to efficiently provide individualized services to our clients is paramount for us and keeps the process of our business focused on you and our relationship with you. It also allows for more time to add to what we know.

Enjoy your lovely fall.



October 15, 2010

Contents

Main Articles

What We Know	1
Alternative Investments	2
Risk Management (Part 4 of 4)	3
Harbor Happenings	4

Individual Highlights

Investor IQ	1
Q3 2010 Market Recap	2
Fund Focus	2
Living Smart	3
Living Well	3
Market Closures	4

Investor IQ

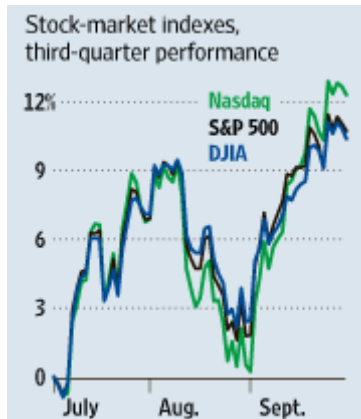
Q: Which European country had the best stock market returns over the past decade?
(A) Spain (B) France (C) Norway (D) Germany

A: c



Third Quarter 2010 Market Recap

Domestic equity performance in the third quarter of 2010 was a bit of a roller coaster with a strong start, plunging middle and a big finish, as seen in the graph below.



Source: WSJ

The strong relative performance came in spite of little visible improvement in the economy. Unemployment stagnated at a stiff 9.6% and consumer spending remained depressed. Global concerns over currency valuations and debt levels have elevated in recent weeks as well.

Positive net flows to fixed income funds continued as investors sought a shelter from the uncertainty of the equity markets and a boost over the minimal yields of money market funds. Corporations have increased cash reserves by taking advantage of low current financing costs. Whether this is a defensive posture or preparation for an expansion is still unclear.

The MSCI EAFE finished 15.79% higher and the Barclays Aggregate was up 2.48%.

"It's what you learn after you know it all that counts" – Harry S. Truman (attributed)

Fund Focus: Ivy Global Natural Resources (IGNAX)

One of our longest held positions is Ivy Global Natural Resources, which satisfies a portion of our tactical overweight to energy and commodities. Portfolio manager Fred Sturm has led the fund for over 13 years and has built a solid track record of choosing a blend of companies to meet near-term needs with an eye on long-range global macro movements. Given the choice over holding physical grain or a grain producer, Fred would prefer the producer because owning the company leverages its human capital and their ingenuity versus pure commodity pricing. The fund's mix of the intangible with the tangible has a strong appeal.

Performance in the sector has been volatile over the past three years with big swings in energy pricing, but the fund has outperformed the S&P 500 by 13.79% annualized over the past ten years and its peers by 4.76% over the same time period.¹ Global demographics imply that natural resources exposure will continue to be a significant portion of our portfolios.

¹ Morningstar data as of 06/30/10

Alternative Investments

In recent newsletter issues, we have been highlighting various investment strategies and ideas primarily focusing on market traded assets such as stocks and bonds. We view these assets as the 'core' of our clients' portfolios. However, there is another segment of our asset allocation model that focuses on more complicated alternative investment strategies. These strategies expand beyond traditional stock, bond and cash ownership. Alternatives have the potential to increase return while reducing the risk associated with a typical stock and bond portfolio. This is observed when looking at historical return, correlation and efficient frontier data including an allocation to alternative investments. We have developed a quality platform of alternative investments with a few examples below:

Non-Traded Real Estate Investment Trust (REIT) – Non-traded REITs raise capital and issue stock similar to any corporation yet focus exclusively on investing in real estate. As opposed to their publically traded counterparts, non-traded REITs attract long term oriented investors seeking to go full cycle on the properties. These properties cover a variety of strategies from core to opportunistic to value added and across multiple sectors from retail, industrial, multi family, assisted living senior housing facilities, self storage facilities, office, lodging and development. Using non-traded REITs to achieve exposure to institutional quality real estate allows the investor to benefit from direct property and hard asset ownership, low correlation, current income and potential gain.

Oil and Natural Gas Drilling Partnerships: These partnerships have a simple mandate - raise capital to drill as many wells as permitted by the capital raise, sell the oil/gas to market and return the profits to shareholders via monthly or quarterly distributions. These partnerships drill in proven natural gas areas primarily in the Eastern US. Due to long-standing tax law, these partnerships have become very valuable for high income earning individuals via intangible drilling cost, depreciation and depletion deductions. In addition to the estate planning advantages (this will be discussed in our Q4 newsletter), an allocation to this asset class provides non-correlation to the equity markets, an inflation hedge, and current income.

Alternative investments are more complicated in nature than traditional assets and require more education on behalf of the investor. Contact your team for more information.

Risk Management (Part 4 of 4)

The most familiar of the risk management strategies that we discussed in the last newsletter is risk sharing or transfer. This involves sharing the burden of loss with another party and the most recognized way of doing this is with insurance. While it is possible to purchase a type of insurance for almost anything (prior to the World Cup last summer, Berkshire Hathaway wrote a policy that would pay out if France should happen to win), the most well known types fall into two categories, life and health-related categories and property and casualty coverage. Insurance can be thought of as a guaranteed and known small loss (premium payments) to prevent a large and possibly devastating loss. This makes obtaining some form of insurance economically prudent and financially efficient regardless of your degree of wealth.

For smaller losses, it may be possible to self insure. Premium dollars may be saved by increasing the deductible on an insurance policy or by dropping the comprehensive insurance on an older automobile. Since insurers prefer not to deal with smaller claims and, in fact, have been known to increase the policy premiums if small amounts are claimed, these strategies can save on multiple levels – lower premiums as well as smaller increases.

In instances with larger losses, insurance can provide compensation, replacement and protection. The determination of whether the possibility of loss is of a value large enough to insure against should be decided based on the net worth of the party purchasing the insurance and more importantly, on the cost of the premiums in relationship to the extent of the risk.

Many people prefer not to think much about their insurance coverages. Policy language is lengthy and complicated and the need for insurance spotlights our fragility, the possibility of something catastrophic happening to us or to those we love. Insurance is, however, a significant and fundamental part of your overall risk management strategy. If you would like, Harbor is prepared to conduct an analysis and review of any of your current coverages to test for adequacy, affordability and comprehensiveness. Please contact your team if you are interested in this service.



Oil and Gas Tax Benefits

As mentioned in the main investment article, our investment strategy utilizes non-market traded assets such as oil and natural gas partnerships. We have received several questions on the tax benefits associated with this investment. Since these benefits constitute a large part of the return, we wanted to revisit the topic.

An investor receives an intangible drilling cost deduction (IDC) in the year after investing in the partnership, which is usually in the range of 80-95% of the original investment amount. This deduction is an ordinary loss, which can offset ordinary income if the investor invested as a general partner. It is considered a passive loss if the investor is a limited partner. The investor also gets to apply depreciation and depletion deductions to the regular cash distributions, making them potentially tax sheltered as well.

We view these partnerships as an integral part of our investment strategy, as not only can they reduce taxable income in any given year, but also provide a long-term, inflation protected, tax advantaged cash flow to investors. In the next newsletter, we will highlight how these partnerships can be a valuable estate planning strategy.

Living Well

Local Volunteer Opportunities

BoulderReads! Literacy Program

Learn to teach the crucial skill of reading. The Boulder Public Library tutors adults and children in one-on-one reading sessions.

www.boulderreads.org

Humane Society of Boulder Valley

Opportunities are open in animal care, community education, fundraising and special events. Volunteer information sessions are held regularly.

www.boulderhumane.org

Volunteer for Outdoor Colorado

Build trails, plant trees, battle invasive species or restore habitat to help preserve our beautiful Colorado, projects available across the Front Range. www.voc.org

Living Smart

DO YOU HAVE A HOME INVENTORY?

If you don't, you should! A record of your belongings is recommended along with your homeowner's insurance to protect yourself in the case of fire, burglary or natural disaster. As well as helping you to purchase enough insurance to replace your belongings, a home inventory will help substantiate any losses for your income tax return and facilitate settling with your insurance company.

The process of creating and maintaining a home inventory involves documenting your assets with receipts, video and photos as well as appraisals and any other information that might be needed to establish replacement value. Along with the larger and more expensive items, smaller items such as toys, CDs and clothing should be noted and photographed. Both the interior and exterior of your home should receive the same treatment. Items in storage, either in the home or in storage lockers, should not be forgotten.

Harbor's staff is always available to help discuss your inventory process.

Harbor Financial Group, Inc.

1909 26th Street, Suite 1A
Boulder, CO 80302

P: 303.939.8788
F: 303.541.1059

info@harborfin.com

Find us on the Web:
www.harborfin.com

Harbor
Financial Group, Inc.

Images: Nat Arnett

Harbor Happenings

CONGRATULATIONS!

- Kevin McCulley has obtained the Certified Financial Planner™ designation. More information on the CFP® Certification process can be found at www.cfp.net.
- Jordan Kunz passed the second of three exams required to receive the CFA® charter and is preparing for next year's final exam in June. More information on the CFA® charter process is available at www.cfainstitute.org.

CLIENT APPRECIATION PARTY

Harbor will be hosting a wine and cheese party for our clients at our office on October 21st. It promises to be a great event and we hope to see you there!

HARBOR IN THE NEWS

Harbor was recognized in the 1st annual NABCAP Premier Advisors list, published in *Denver Magazine's* September 2010 issue. This exclusive group of Colorado firms met an objective standard of excellence, focusing on a wide range of criteria including experience, team dynamics, credentials and customer service.

2010 Closures

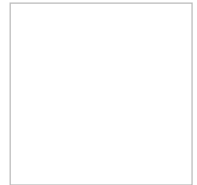
The New York Stock Exchange (and therefore our office) will be closed on the following days in 2010: Thanksgiving Day—November 25, Christmas (observed) —December 24.

Securities offered through Triad Advisors and Schwab Institutional. Members FINRA & SIPC.

Harbor Financial Group, Inc.

1909 26th Street, Suite 1A

Boulder, CO 80302



[Recipient Name]

[Street address]

[Address 2]

[City, ST ZIP Code]