GHP Investment Advisors, Inc.
INVESTMENT INSIGHT
First Quarter 2013

Bubble Tic-Tac-Toe

Carin D. Wagner, CFP®

In the first quarter of 2013 the Dow Jones Industrial Average (DJIA) and S&P 500 surpassed the market peak reached prior to the 2008 financial crisis. **People are now asking if it is time to act and sell out of the market. We do not think so.** Underlying valuations continue to make the stock market seem attractive for two reasons. First the economy (employment and housing) is improving. The second and most important is the equity market, both in an absolute sense compared to historical prices and a relative sense, to fixed income and real estate, appears to be priced appropriately.

The market opportunities in 2013 are not the same as the last two peaks. In 2000, there were unrealistic expectations of the equity market during the internet and telecom bubble which was then followed by a real estate bubble in 2006. The setting in 2013 is considerably different. Bubble Tic-Tac-Toe will guide you through the unique investment environments in 2000, 2006, and now by providing relative yields for three major investment sectors: fixed income, real estate and equities.

Bubble Tic-Tac-Toe Columns

The first column of Bubble Tic-Tac-Toe is the yield of the 10-year U.S. Treasury, the fixed income representative, considered to carry a very low risk of default due to U.S. government backing. In our case, this low risk asset is used as a benchmark against which investments with more risk should outperform.

The second column in the table is the average dividend yield of diversified Real Estate Investment Trusts (REITs). A diversified REIT, as the name suggests, includes various types of real estate ownership such as multi-family, retail, industrial, hospitality, health care, etc. in an investment trust wrapper. A REIT is required to distribute at least 90% of its taxable earnings to investors; therefore, the dividend yield on REITs can be used as an indicator for the valuation of real estate.

The last column is the Price to Cash Flow Ratio for the S&P 500 Growth Index, a ratio used to compare a company's market price to its cash flow. The inverse of the Price to Cash Flow ratio provides the yield an investor would earn at the current price based on the ownership of the business in the most recent fiscal year. As an example, the current Price/Cash Flow ratio of the S&P 500 Growth Index is 12.1 (1/12.1 = 8.2% yield). In other words, for every $1,000 invested in the S&P 500 Growth Index, an owner of these companies would earn $82 for the year.

Investment Landscape in 2000

To understand the investment options in 2000, we will start with the first row of Bubble Tic-Tac-Toe. The peak yields on the three major asset classes in 2000 were as follows:

Bubble Tic-Tac-Toe

	10 year U.S. Treasury	Diversified REIT	P/CF of Equities
2000	**6.3%**	**8.7%**	**3.0%**
2006			
NOW			

At the peak of the bubble in early 2000, the S&P 500 Growth Index had an unprecedented price to cash flow ratio of 30 translating into a 3% cash flow yield. Concurrently, 10-year U.S. Treasuries were yielding 6.3%. In other words, investors were so overly optimistic (or speculative) cash flow would rapidly grow in the future, they were willing to accept a lower yield when investing in stocks than they could gain from ultra-safe bonds. Given these spreads, it was clear investors were not being compensated for the risk they were taking in the equity market and it was not surprising the S&P 500 Growth Index subsequently fell 57% from 2000-2002 when corporate cash flows did not live up to the market's lofty expectations.

Investment Landscape in 2006

After the stock market declined in 2000, money flowed from equities into real estate, which, in conjunction with lenient lending practices, dramatically inflated prices in the real estate market. By 2006, peak yields on fixed income, diversified REITs, and stocks were significantly different than 1999. Below is the second row on Bubble Tic-Tac-Toe:

Bubble Tic-Tac-Toe

	10 year U.S. Treasury	Diversified REIT	P/CF of Equities
2000	6.3%	8.7%	3.0%
2006	5.1%	3.7%	6.9%
NOW			

As illustrated above, yields on REITs declined to 3.7% while investors could earn a risk-free yield of 5.1% on Treasuries or a yield of 6.9% in the equity market. These numbers indicate the real estate market was overvalued – on an absolute basis investors were not being compensated for the risk in the real estate market, and at the same time, lower risk investments were yielding more.

Current Investment Landscape

Over the past decade, yield has not been aligned with risk until now – the last row of Bubble Tic-Tac-Toe and the completion of the Bubble Tic-Tac-Toe board:

Bubble Tic-Tac-Toe

	10 year U.S. Treasury	Diversified REIT	P/CF of Equities
2000	6.3%	8.7%	3.0%
2006	5.1%	3.7%	6.9%
NOW	2.0%	4.2%	8.2%

The S&P 500 Growth Index is priced relative to cash flow to deliver healthy investment returns. After the real estate bubble burst, money flowed from real estate into fixed income securities causing interest rates on most debt securities including the 10-year Treasury bond (used in this example) to significantly decline.

While debt securities are historically not as volatile as equities, they are nevertheless subject to interest rate and inflation risk. With the 10-year Treasury yielding only 2% and the U.S. Federal Reserve targeting inflation at 2.5%, most likely the 10-year Treasury will lose buying power over the next 10 years. Given the inverse relationship between interest rates and bond prices, if interest rates rise, bond prices will decline causing the fixed income bubble to burst.

Unlike the real estate bubble in 2006, we do not believe this potential fixed income bubble will cause an equity market collapse. The near 55% drop of the S&P 500 from 2007 – 2009 was not triggered by unrealistic expectations of growth in the equity market. Instead, it was produced by a bubble in the U.S. real estate market that ultimately threatened the collapse of large financial institutions creating a credit crunch. Rising interest rates are likely to increase the cost of borrowing for the U.S. government and cause bond prices to fall. However, in contrast to past bubbles, because the primary owners of the bonds are not highly leveraged financial institutions, the decreasing bond prices are not likely to create another banking crisis.

Bubble Tic-Tac-Toe was built on the flow of money based on past performance from one bubble creating the next!

Bubble Tic-Tac-Toe

	10 year U.S. Treasury	Diversified REIT	P/CF of Equities
2000	6.3%	8.7%	3.0%
2006	5.1%	3.7%	6.9%
NOW	2.0%	4.2%	8.2%

Ask yourself, based on Bubble Tic-Tac-Toe, would you want to own the S&P 500 companies in 1999? What about a REIT in 2006? Where is the investment opportunity now?

While future prospects for cash flows (profitability) of U.S. companies are never certain, we know stocks are selling for far less than 2000 or 2006. Further, just as relativity is essential to the study of physics, it is likewise crucial to investment analysis. It is our conviction that currently, **stocks, relative to the other major investment sectors, represent the best potential for long term growth** as demonstrated in Bubble Tic-Tac-Toe.

Sources for Bubble Tic-Tac Toe:
www.nareit.com Performance Statistics by Property Type.
www.federalreserve.gov
Bloomberg, L.P.

Market Summary

Key Financial Ratios for Domestic Asset Classes

Asset Class	Price/Earnings 2013:Q1	P/E Benchmark	Over/Under Valuation	Price/Book Value 2013:Q1	P/BV Benchmark	Over/Under Valuation
Large-Cap Growth Stocks	17.3	27.0	-35.9%	3.3	5.7	-42.1%
Large-Cap Value Stocks	13.9	20.2	-31.2%	1.8	2.5	-28.0%
Mid-Cap Growth Stocks	22.8	24.8	-8.1%	3.2	4.5	-28.9%
Mid-Cap Value Stocks	20.2	19.1	5.8%	1.7	2.2	-22.7%
Small-Cap Growth Stocks	23.9	23.2	3.0%	2.8	3.5	-20.0%
Small-Cap Value Stocks	22.3	18.2	22.5%	1.6	2.1	-23.8%

**Please note that the P/E data reported above are based on "as reported" earnings information rather than "operating" earnings. "As reported" earnings include one time write-offs whereas "operating" earnings reflect the profitability of a company as a going concern. We believe P/E's based on operating earnings are a better long-term valuation indicator, but Standard and Poor's does not report this information for the style indexes used in our calculations. To address this issue we have also included Price to Book Value (P/BV) data, another important valuation indicator.*

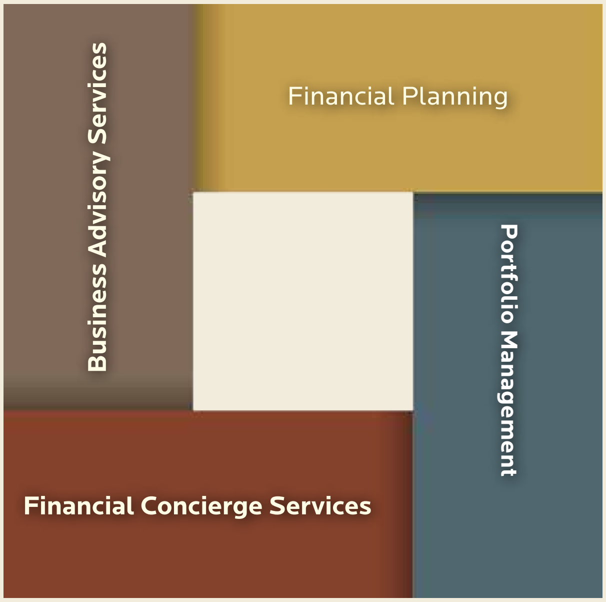
GHP Investment Advisors, Inc. benchmarks are based on proprietary discounted cash flow models. P/E and P/BV data are provided by Bloomberg L.P. as of 4/02/2013.

Returns by Index

Index	YTD*
DJIA Total Return	11.93%
NASDAQ	8.52%
S&P 500	10.61%
S&P 500/Value	11.28%
S&P 500/Growth	8.85%
S&P MidCap 400/Value	14.30%
S&P MidCap 400/Growth	11.87%
S&P SmallCap 600/Value	11.30%
S&P SmallCap 600/Growth	11.70%

DJIA, NASDAQ & S&P Returns: Bloomberg L.P. as of 4/02/2013.

*Dividends Reinvested.



Business Advisory Services
We help you drive your continued success as a business owner, executive or entrepreneur.

Financial Planning
We create a personalized financial plan to help you meet your wealth management goals – and give you peace of mind.

Portfolio Management
We develop and implement an integrated portfolio investment strategy, taking into account your individual investment goals, time horizon and risk tolerance.

Financial Concierge Services
We relieve you of the everyday burden of your financial affairs.

GHP Investment Advisors, Inc.
Registered Investment Advisor

1670 Broadway, Suite 3000
Denver, Colorado 80202
P (303) 831-5000
F (303) 831-5082
Invest@GHPIA.com
www.GHPIA.com

Brian J. Friedman, CFA President
Robert W. Hochstadt, CPA/PFS Senior Principal
Steven I. Levey, CPA/PFS Senior Principal
Carin D. Wagner, CFP® Vice President of Personal Wealth Management
Sommer C. Vincent Client Relations Manager
Mike Sullivan, CFP® Wealth Management Advisor
Deirdre McGuire Client Relations Specialist
Katy Evans Marketing Analyst
Dave Garcia Data and Operations Analyst
Sebrina Ivey, CPA, CIA Operations and Compliance Manager
Brad Engle Research, Trading and Portfolio Analytics
Ed Leone Jr., DMD, MBA, CFP®, RFC Associate