Advisory Notes

DECEMBER 2015

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VALICENTI ADVISORY SERVICES, INC.

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The Year in Review: The Fed Finally Hikes Rates

Following a volatile, negative third quarter, the fourth quarter started just as volatile with the major indexes reporting a four year monthly high return of roughly 8% in October. (See Market Table.) November and December continued to tread water as the holiday season started early with major discounting at retail “brick and mortar” stores and a shift to spending online.

With the exception of two months, 2015 was relatively flat, as the markets anticipated a midyear interest rate hike. Economic signals, however, did not allow for the Federal Reserve to move until December’s meeting, when it raised the current rate 0.25 basis points from the zero interest rate policy of the last seven years. Fed Chairman Janet Yellen’s announcement was highly expected, but her dovish comments indicated slow and steady rate hikes through 2017. This will allow our markets to digest the rate hikes at a reasonable pace without causing too much inflation or a rapid strengthening of the U.S. dollar, which would ultimately hurt U.S. exports.

Due to the global slowdown and commodity price pressures, the U.S. economy has had disappointing manufacturing numbers which represent around 12% of the economic activity, while the service side of the economy, representing roughly 88% of U.S. activity, remained healthy in 2015 and should continue into 2016. While we believe 2016 will present some opportunities in both the equity and the fixed income markets, we see more of a slow sustainable growth within the markets that mirror the slow quarterly interest rate hikes

(See **Year in Review** *on page 2)*

Market Table

Valicenti Advisory Services, Inc.
Comparative Index Period Returns
From 12-31-14 THROUGH 12-13-15

	DJIA	S&P 500	NASDAQ	Russell 2000 Index	Lehman Muni Bond Index	Citi Corp Corporate Bond Index	U.S. Treasury Bill Index (90 day)
12-31-14 to 03-31-15	0.33	0.95	3.48	3.99	1.12	2.22	0.00
03-31-15 to 06-30-15	-0.29	0.28	1.75	0.09	-0.98	-2.91	0.00
06-30-15 to 09-30-15	-6.98	-6.44	-7.35	-12.22	1.82	0.43	0.06
09-30-15 to 12-31-15	7.70	7.04	8.38	3.20	1.66	-0.44	0.06
YTD Returns 12-31-14 to 12-31-15	0.21	1.38	5.73	-5.71	3.64	-0.75	0.12

How a Financial Plan Can Reduce Anxiety and Doubts

We all have financial goals in life. These goals may range from the ability to have a comfortable retirement to saving for holiday gifts. No matter the goal, the primary difference between those that achieve their goals and those that fall short is planning.

For some, the thought of a financial plan may be scary, fearing what the plan may require will be worse than the anxiety of being unprepared. This fear often leads people to delay or ultimately avoid establishing a plan. In reality, once you have a plan, most of the anxiety and uncertainty surrounding your goals disappear.

Retirement is a prime example of where people fail to plan. Most households recognize the need to save for retirement and want to make it a priority. While the majority of households smartly elect to participate in their employer sponsored retirement plan, sadly, this is where their retirement plan ends. Households are left feeling unprepared for retirement. Their common concerns are often summarized by the following questions:

- How much money will we need for retirement and are we saving enough to meet that goal?
- What will our income be in retirement?
- What investments should we select to meet our goals?
- What happens when we retire?

A sound financial plan is a simple plan. It is unlikely you will follow a plan that requires you to save the majority of your income, is based on unrealistic investment returns or involves so many moving parts that it is difficult to understand. You should look for a plan that is unique to your circumstances, timeframe, risk tolerance and financial goals.

While it is never too late to start a financial plan, one of the keys is early planning. Time can be one of the greatest benefits to a financial plan, as it gives a person flexibility. Early planning will also allow you to consider alternatives and to explore other financial goals along the way. In addition, the earlier you outline your plan and its limitations, the more educated you will become in how to achieve your financial goals. As you become more educated and gain a greater appreciation for your plan, your confidence in the ability to achieve your goals will continue to grow.

The best time to start your plan is *today*. You can help yourself by prioritizing your goals and being honest with your ability to meet those goals. Once the goals and the means to reaching your goals have been established, you can begin to develop the road map. You may find for straight forward goals, you can create your own road map. For more complex goals, we are available and willing to help develop a financial plan that will reduce anxiety and doubts and increase confidence in your ability to achieve your goals. Don't let fear and uncertainty rule your decision to plan. Start your financial plan *today*.

Andrew R. Clark, CFP®
Vice President of Investment Research, Portfolio Manager

Year in Review

(Continued from page 1)

that are planned for 2016.

The unemployment picture remains quite healthy, since the year began with a 5.6% unemployment rate and ended around 5%. Automobile sales hovered near new highs and consumers are being smarter with their savings – building those nest eggs consistently with the slow growth environment.

Many foreign central banks are expanding their easing programs, providing attractive investment opportunities in areas that may benefit from expansion. The European Central Bank, the Bank of Japan and the People's Bank of China continue to pursue aggressive stimulus packages for their economies.

If history is an indicator of the future, then this tidbit may be of some importance. From 1928 to 2015, when the beginning of a rate hike cycle began with a slow and steady pace during the fourth year of a presidential term, the equity market outperformed fast pace rate hike cycles over that same period.

As always, our team of investment professionals, consisting of portfolio managers, an economist and a financial strategist, will continue to look for opportunities that match our clients' overall goals and risk tolerance objectives.

From our family here at Valicenti Advisory Services, Inc. to you and your families, we wish you a healthy and prosperous new year in 2016.

Joseph M. Valicenti
President/CEO

Employee Corner

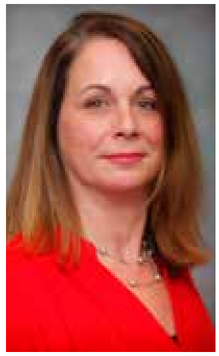
We are pleased to announce that Frances M. Allis, Amy M. Chacho and Molly L. Bartlett have recently joined the firm.

As a member of our affiliate, Valicenti Insurance Services, Inc., Frances is a Licensed Property/Casualty Insurance Agent. She is an honors graduate of SUNY Regents College with a Bachelor of Science degree in Accounting and has completed a number of graduate level business courses. She is a Notary Public and a Certified Instructor for the National Safety Council's 6-Hour Defensive Driving Course.

She has a varied employment background having worked as a Staff Accountant and a Financial Analyst in the manufacturing sector and an Adjunct Accounting Instructor for both Corning Community College and EBI. Most recently she was the Controller/Treasurer for an independent insurance agency.

Amy attended Fairfield University majoring in Business Administration. Prior to joining the Tax and Business Services Department, she was both the office manager and a tax preparer for the local office of a national tax preparation firm. Her experience also includes bookkeeping and special projects for the CFO and the Controller of a small conglomerate in Connecticut.

Frances M. Allis



Amy M. Chacho

Molly L. Bartlett

As a member of the Tax and Business Services Department, Amy is scheduling client meetings, providing tax support, processing and e-filing tax returns, lending client support and doing special projects, as required.

Molly is a graduate of Notre Dame High School and she completed the Travel and Tourism Program at Corning Community College. Upon graduation, she worked as a certified travel agent for several years. Her experience also includes office administration at a local insurance firm and retail management.

As the receptionist for the Tax and Business Services Department and our affiliate, Valicenti Insurance Services, Inc., her responsibilities include answering and directing phone calls, receiving clients and vendors, office supply ordering and distribution and handling of mail and client correspondence.

As you may remember, last year Jeff Naylor was instrumental in re-establishing the cross-country program at Notre Dame High School. Jeff's efforts paid off having both theDaily Review's top female and male newcomers of the fall sports season and three of the athletes, one girl and two boys, went to the state meet. As a result of the season, Jeff was voted all regions girls' cross-country Coach of the Year.

This year, Jeff was named the boys' Coach of the Year based on the team, which included three newcomers, winning a sectional title and a fourth place finish at states. One female runner made the state meet. We know that you join us in congratulating Jeff and his team.

Please join us in welcoming Frances, Amy and Molly to the firm and thanking Jeff for all he does for our firm and the community. We are very pleased to have these employees as a part of our team.

Melissa B. Dixon
Administrative and Marketing Assistant

2015 Notre Dame High School Boys Cross Country Team

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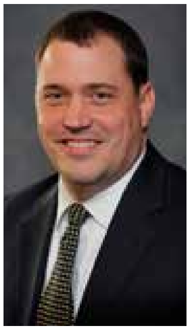
Our Clients Come First

Analyst Corner



Having just concluded the Federal Reserve's December FOMC meeting where policymakers moved to raise the level of short-term interest rates for the first time since the era of "extraordinary policy" began, it is appropriate to take stock of some history in order to begin to think about how certain measures might trend and influence financial asset markets going forward. Taking a look at overall financial conditions, inflation, S&P 500 Index levels and Commodity Index performance over a 15-year period gives us a framework to do this. Financial conditions as measured by the Chicago Fed's National Financial Conditions Index are at a -0.70 level. This is an aggregate measure designed to have an average value of zero. It measures credit, risk and leverage in the system and it currently remains consistent with broad conditions which are still loose relative to the longer term average. The Fed's preferred gauge of inflation is the core Personal Consumption Expenditures (PCE) measure which sits at 1.28% Year over Year and is still below the target of 2.0%. For now, the Fed seems confident that core PCE inflation will move towards the 2.0% level over the next few years and any downward pull on aggregate price levels relating to the energy price environment will pass through. The bottom chart clearly shows an almost 50% decline in the Rogers International Commodity Index from mid-2014 to now and any further significant downside from here could signal, along with a rising dollar, disinflation and poor global growth, a negative feedback to our economy and markets. However, should a stable commodity complex, targeted inflation and average financial conditions reign in 2016, then U.S. growth and market performance could be constructive.

Positive Influence	Negative Influence
U.S. Growth Outperformance	Emerging Markets
Labor Market Conditions	Cost of Capital & Spreads On The Rise
Movement Off of Crisis Era Monetary Policy	Persistently Low Commodity & Energy Prices

From a market symmetry perspective, resilient yet lower growth rates and further continuation of the present business cycle may very well be maintained as we move into the next year. At present, we are certainly driving through an environment experiencing various dynamic changes and adjustments. Influences appear to be balanced, but market watchers, as always, should display good form and be on the watch for downside risks while understanding that for the preponderance of time we are climbing the "wall of worry."

Positive Market Influences:

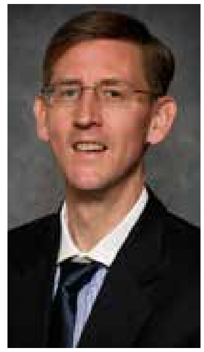
- U.S. Growth Outperformance – The expectation for U.S. growth and future inflation verses that of Japan, the Eurozone and in the developing world is generally viewed as having a relatively more positive outlook.
- Labor Market Conditions – Average monthly gains as of November in non-farm payrolls are running at +237K over the last twelve months and Average Hourly Earnings have risen 2.3% over the same period. Underemployment and labor force participation rate issues are serious concerns, but labor conditions broadly have been positively stable.
- Movement Off Of Crisis Era Monetary Policy – While post Global Financial Crisis rate normalization has been a hotly debated topic, the Fed has reduced a good deal of policy uncertainty having completed the asset purchase taper and recently achieving rate liftoff.

Negative Market Influences:

- Emerging Markets – Major developing economies starting with China and mov-

(See **Analyst Corner** *on page 5)*

Investment Strategy



Led by a continued weakening of commodities, such as oil and natural gas prices, a slowdown in U.S. manufacturing and a stronger dollar which had a negative impact on exporters, 2015 presented many challenges for both the U.S. equity markets and the fixed income markets. In addition, the concerns as to when and how much the Federal Reserve might raise interest rates held the markets hostage. In December, the Federal Reserve, in a highly expected move, raised interest rates 0.25 basis points. This marks the first interest rate increase in over seven years and ended the uncertainty of a rate hike. The U.S. consumer faired reasonably well as the labor markets continued to show improvement throughout the year, led by a strong showing in auto sales.

There will likely be many of the same issues in 2016 and we will see some of the focus shifted to the presidential election. The market outlook appears to remain split with manufacturing and commodities still struggling and consumer and services sectors remaining positive. In addition, if stock valuations remain reasonable, we will use market pullbacks as buying opportunities within the U.S. fixed income and U.S. equity markets. Our focus continues to be on companies with strong balance sheets, strong cash flow and strong earnings growth.

With market volatility likely for the foreseeable future, we will remain flexible with our asset mix. Fixed income will be in a range of 35–45%, equities 35–55% and cash 5-20%. The asset mix will vary based on client income needs, risk levels and client specific directives.

Jeffrey S. Naylor
Executive Vice President/CFO

Analyst Corner

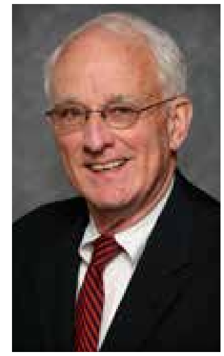
(Continued from page 4)

ing to Brazil, South Africa, Turkey and Russia are all struggling to regain a stronger growth footing. The growth differential in the U.S. combined with foreign currency depreciations vs the U.S. Dollar has complicated the rate normalization process.

- Cost of Capital & Spreads On The Rise – Corporate credit spreads have widened this year with more significant deteriorations seen in the bottom tier of the High Yield space. Short-term funding rates are on the rise and, while this is all taking place in an overall backdrop of growth, the decreased corporate liquidity position could ultimately slow output if firms' capital costs are pushed too far too fast.
- Persistently Low Commodity & Energy Prices – WTI and Brent Crude prices have fallen below $35 and $40 a barrel, respectively. Industrial metals are suffering from weaker demand, oversupply and weakening liquidity positions in the world. While absolutely positive for consumers and anyone working with these cost inputs, the low prices are having the opposite effect on over indebted producing firms and nations.

Daniel P. Burchill
Security Analyst

Thank You!



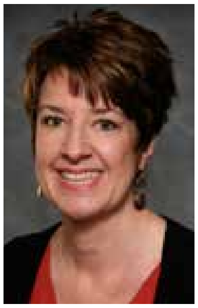
As this is being written on December 15, 2015, our various departments are focused on the usual year end duties and planning for 2016.

It is hard to believe that we are completing our 31st year. We have much for which to be thankful, not the least of which are our diverse and loyal clients who have given us the opportunity to know them, to work with them and to help them along their "financial journey." At the same time, a thank you to our wonderful staff for its dedication and hard work. We continue to use a teamwork approach to our business and we continue to "cultivate relationships," always adhering to our vision of "Our Clients Come First."

From all of us to all of you, a very Happy Holiday Season and a Prosperous New Year.

Ralph H. Roberts, Jr.
Vice President of Client Services

The Importance of Designating and Updating Beneficiaries



Who are your named beneficiaries? This is a question we often answer once while completing an application for a new account and then do not revisit.

Most retirement plans and accounts, annuities and life insurance policies allow you to name primary and contingent beneficiaries and what percentage of the assets you would like distributed to each upon your death. Some investment accounts also offer "transfer on death" (TOD) beneficiary designations. Beneficiaries may be named individuals such as spouses, children and friends or they can be trusts, charities or institutions.

Beneficiary forms now often offer "per stirpes" distribution also. If you elect "per stirpes" distribution and a "per stirpes" beneficiary predeceases you, distribution will usually be made of his or her portion equally to his or her living children, rather than being split between the remaining living beneficiaries. Contingent beneficiaries will inherit assets only if there are no surviving primary beneficiaries or "per stirpes" heirs (if indicated) at the time of death of the account holder.

Spouses can generally inherit assets from one another without generating estate taxes or being forced into taking mandatory taxable retirement distributions, unless they are already over 70½ years, by rolling over the account assets into their own accounts. Other heirs may face some tax consequences.

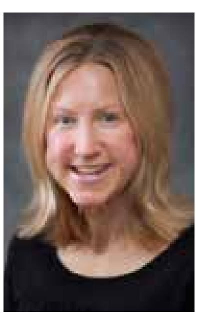
Designating beneficiaries is actually one of the first steps in creating an estate plan. Creating a will is another. A will addresses the treatment of assets that are part of an individual's estate; however, a retirement account does not need to be considered part of an estate. Beneficiary designations override bequests you make in your will. When you name a beneficiary, those assets can pass directly and immediately to whomever you designate – avoiding the probate process, which may be lengthy and costly.

Events in our lives sometimes warrant a change in our wishes for those who are to receive our assets and, at the time of a life changing event, updating our beneficiary designations is not at the forefront of our thoughts. Plan to review your beneficiary designations on a regular basis, especially following marriage, divorce, the birth of a child or the death of a loved one. If you do need to change your named beneficiaries, request the official beneficiary change form from your plan's administrator or your account custodian.

In most cases, beneficiary issues are noticed only after an account holder has passed, causing much frustration, disappointment and unnecessary expense and time. So we ask again, who are your named beneficiaries? Do your beneficiary designations reflect your current wishes?

Kelly S. Diehr, RP®
Administrative Assistant

NEWS FLASH!

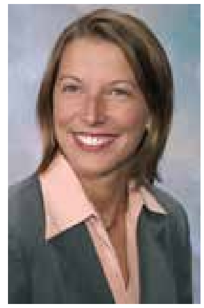


The long awaited tax legislation to renew a series of tax provisions known as "tax extenders" was finally passed by Congress and signed into law by President Obama. The new legislation known as the Protecting Americans from Tax Hikes (PATH) Act of 2015 retroactively reinstates for all of 2015 the "tax extenders" that expired at the end of 2014. However, unlike past "tax extenders" legislation, the PATH Act of 2015 makes many of the provisions permanent, with some of the remainder being extended for more than the normal two year extension. The following provisions have been made permanent:

- **Qualified Charitable Distributions Made Directly From IRAs to a Charity:** Taxpayers who are over age 70 ½ can make a "Qualified Charitable Distribution" of up to $100,000 directly from an IRA to a charity. The distribution from the IRA is not taxable to the taxpayer, but the contribution to the charity cannot be claimed as a tax deduction.
- **State and Local Sales Tax Deduction:** Taxpayers may claim an itemized deduction for either the payment of state income taxes or the payment of state and local sales tax, whichever produces the largest deduction. This permanent extension will primarily benefit those who itemize their deductions and do not pay state income tax.
- **Enhanced Child Tax Credit:** The Child Tax Credit is a $1,000 credit available for each "qualifying child" in the household. For lower-income individuals who do not even have a $1,000 tax liability, the child tax credit becomes a refundable credit for 15% of earned income over a threshold amount. The new PATH legislation sets the threshold at $3,000 permanently.
- **School Teacher Expense Deduction:** Elementary and secondary school teachers are eligible for an above-the-line deduction for schoolteacher expenses up to $250/year. In addition, the PATH Act

(See **News Flash** *on page 7)*

Valicenti Firms Partner with Local Organization to Provide Several Families a Merry Christmas



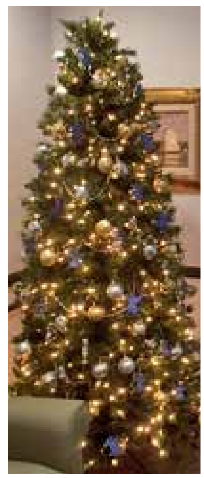
Valicenti Insurance Services, Inc. and Valicenti Advisory Services, Inc. partnered with Heart to Heart of the Southern Tier to provide several families in the Southern Tier clothing, household essentials and gifts for the 2015 holiday season.

In our first year, Valicenti displayed “Giving Wings of Hope” trees at both of our Elmira locations and staff members, clients, vendors and community friends were invited to take a tag and purchase a gift or household need. These generous gifts were delivered to the Heart to Heart organization in late November to distribute to families in need.

Heart to Heart of the Southern Tier partners with local schools, non-profit organizations, Head Start programs and other social service organizations that provide names and wish lists of families in need during the holiday season.

Our firms are blessed to have such caring staff members, clients and friends who went above and beyond to be sure that these families had a Merry Christmas. We look forward to carrying on this tradition for many years to come.

Suzanne M. Valicenti
President/CEO



“Giving Wings of Hope” tree displayed in our Elmira office.

News Flash

(Continued from page 6)

indexes the $250 cap for inflation beginning in 2016.

The following provisions have been extended through 2016:

- **Deductibility of Mortgage Insurance Premiums as Qualified Residence Interest:** Taxpayers who pay mortgage insurance premiums are permitted to deduct the mortgage interest as though it was interest on mortgage debt, as long as the mortgage was taken out after 2006 and was acquisition debt for the primary residence.
- **Exclusion of Discharged Mortgage Debt on Qualified Principal Residence:** When a taxpayer’s debt is discharged, the canceled debt is treated as taxable income. To provide some relief for this situation as the real estate market declined, legislation was passed to stipulate that up to $2,000,000 of canceled debt associated with a mortgage of a primary residence could be discharged without tax consequences.
- **Above-the-Line Deduction for Qualified Tuition and Fees:** This rule provides for the deduction of up to $4,000 of tuition and related fees for an eligible student (generally the taxpayer, spouse, and/or dependents).

Kathleen O’Herron, CPA
Staff Accountant

The highest compliment our clients can give is the referral of their friends and family. Thank you for your trust!

New Health Care Information Reporting Forms

The Affordable Care Act has an implementation plan to put in place the new health care laws, over a number of years. The focus is to make sure that Americans are covered for their health care needs. Several tax focus surveys from the current administration and prior administrations have determined that the most effective form of compliance is third party reporting. In 2016, health coverage providers and certain employers will provide health coverage statements to covered individuals. The Internal Revenue Service (IRS) has issued new health care law information regarding the reporting forms: Form 1095-B, Health Coverage and Form 1095-C, Employer-Provided Health Insurance Offer and Coverage.

While the IRS does not require taxpayers to submit documentation of health coverage with their tax returns, gathering documents in advance will help with return preparation at tax time. Beginning with records for tax year 2014, taxpayers should keep insurance cards, explanation of benefits statements from their insurer, Forms W-2 or payroll statements reflecting health insurance deductions, records of advance payments of the premium tax credit and other statements indicating that they or a family member had and maintained health care coverage.

Form 1095-B is used to report certain information to the IRS about individuals who are covered by minimum essential coverage and, therefore, are not liable for the individual shared responsibility payment. By January 31, 2016, health coverage providers should furnish you a copy of Form 1095-B, if you are identified as the "responsible individual" on the form.

Form 1095-C is used to report information to the IRS and employees about individuals who have minimum essential coverage under the employer's plan and; therefore, are not liable for the individual shared responsibility payment for the months that they are covered under the plan. Employers with 50 or more full-time employees in the previous year use Form 1095-C to report the information required about offers of health coverage and enrollment in health coverage for their employees. An employer must furnish a Form 1095-C to each of its full-time employees by January 31 of the year following the year to which the Form 1095-C relates.

Like last year, the Health Insurance Marketplace will issue Form 1095-A, Health Insurance Marketplace Statement, in January 2016, to individuals enrolled in Marketplace coverage during 2015. If claiming the premium tax credit, taxpayers will need information about any advance credit payments received through the Health Insurance Marketplace, the type of coverage obtained at the Marketplace, the premiums paid and the months covered. If you did receive a premium tax credit, be aware that changes in your reported income on your 2015 tax return will have an effect on the ultimate refund or amount due.

Paul H. Hornbuckle, CPA
Vice President of Tax and Business Services

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