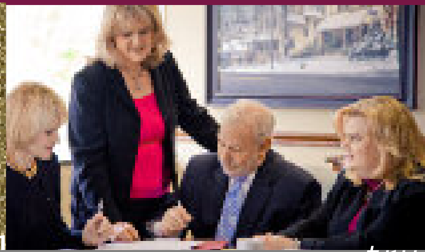
PENNSYLVANIA TRUST
25 YEARS



SUMMER 2011

trust & investment
perspectives

# Deeper in Debt

**by Willard N. Woolbert**

Entering the summer, there are two structural issues that are weighing on global markets. They are beyond the ebb and flow of economic numbers or judgments about relative value in the markets, and speak to longer-term issues impacting the financial health of the developed economies. Resolved, they could provide dramatic stimulus to markets. Allowed to continue, they have the ability to bring down not just markets but governments and currencies. One is the Greek budget crisis; the other is our own struggle to address structural budget problems in the debate around raising the government's debt ceiling.

In Greece, the debt to GDP ratio has reached 150%. Years of budget deficits, combined with anemic growth, have created a situation in which the markets will no longer freely fund the deficit. Two-year Greek government yields have reached 25%. In 2010, the International Monetary Fund (IMF), European Central Bank (ECB), and European Union collaborated on a bail-out that was intended to fund Greek debt needs until the country could return, unsupported, to the debt markets, hopefully by 2013. For this to happen, the Greek government was required to reduce spending and increase taxes to close their budget deficit. A year later, the austerity demanded of the Greeks has resulted in an economy that is falling, unemployment that is accelerating, and a budget deficit that is worse than originally projected. The medicine required by the ECB, IMF, and others, for additional support, is more austerity — and the Greeks are rioting. This has begun to look like an impossible situation to investors and is why there is an increasing discussion of the possibility of a Greek default. The words used are extension of maturity, restructuring, and private participation, but the outcome must be the same. The Greek economy appears to have passed the point of being able to service its debt.

Why is a default by Greece, a relatively small economy, important to global markets? The fear is contagion. The debt is widely held by government and financial institutions in Europe. A default would require a write-down of this debt, creating capital adequacy problems. A default could also encourage other wounded European economies, such as Portugal and Ireland, to consider similar action. The Irish situation is different from the Greek one in that their increase in debt was largely caused by having to bail out their banks. In Ireland, there has already been pressure to force bank debt holders to suffer some form of default to relieve pressure on the government. Any or all of these events would bring crisis to the European financial system, cause the

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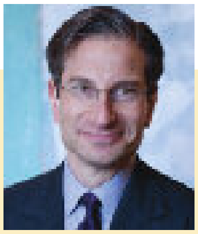


## Investor Seminar Features Media Expert Jeffrey F. Rayport

"How Digital, Mobile, and Social Media Are Changing Our World" will be the topic of our annual Investor Seminar this October. Mr. Rayport is well known for his thought provoking commentary on contemporary business practices and introduced the now familiar term "viral marketing" when he was on the faculty at Harvard Business School. Currently, he leads a consulting firm that specializes in publishing and information and marketing services while continuing to write a column for BusinessWeek Online as well as commentary for numerous other publications. His most recent book on the topic of reinventing service businesses is titled *Best Face Forward: Why Companies Must Improve Their Service Interfaces With Customers.*

# President's Message: Summer Nostalgia

Hot, humid Philadelphia weather reminds me that mid-July is upon us, the thick of the summer. Our beloved Phillies are halfway through the season, school is out, flags are flying and I find myself waxing nostalgic about the routines and traditions that are synonymous with summer.

The pace of the days magically seems to slow. Extended daylight finds us perhaps enjoying the company of family and friends at an outdoor barbecue. The golf course or tennis courts beckon. Colleagues head off to favorite vacation spots, the coast of Maine, the Outer Banks, the "Shore," international destinations. Celebrations across the country mark our nation's history. It is the rhythm of the season.

Pennsylvania Trust observes a milestone in our own history this year, 25 years of providing investment management and trust administration for individuals, families, foundations, and endowments. And what better place to come together with colleagues and their families than Valley Forge National Park, where we recently gathered for an official celebration of the hard work and dedication that has contributed to a quarter century of excellence. We were joined by two luminaries from the past, General George Washington and the Marquis de Lafayette, who shared history lessons with us, reminding me that many of the issues confronted and overcome in the past resonate even today. The spirit of joy and camaraderie that our colleagues share was evident, and I am certain that it is a key ingredient to the success we continue to enjoy.

Summer however, finds the U.S. economy anything but routine as it continues to confound models and predictions, slowing considerably after a quarter of modest growth. Economist David Hale notes that we have entered a "soft patch" and concerns over a recurring recession are aired. Consumers are worried about slow growth, high structural unemployment, and inflation. On a more positive note, the auto industry, despite ongoing disruptions from the Japanese earthquake, continues to grow. Equipment and software sales are satisfactory, but the housing market remains weak. International economic news is unsettling. In this issue, Bill Woolbert expands on two looming global economic questions, the Greek debt crisis and the ongoing debate over the U.S. government debt ceiling. The intersection of politics and monetary policy is an issue that we will closely follow as time progresses.

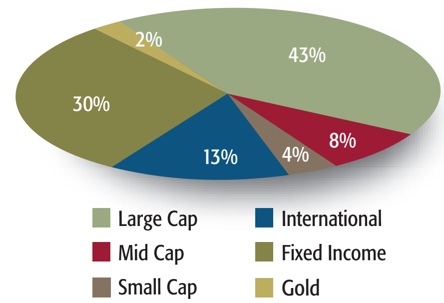
While summer offers all of us at Pennsylvania Trust a chance to relax and reflect, know that we are no less diligent in our attention to the daily business of providing you, our valued clients, with the highest level of service, one that will never be compromised. Mediocrity is not in the Pennsylvania Trust vocabulary. For 25 years, we have remained committed to our core values of excellence, respect, community, confidentiality, compassion, and service, a tradition that is just as true today as it has ever been. I hope that this summer affords you and your family opportunities to savor the season.

**Richardson T. Merriman**
*Chairman, President,*
*and Chief Executive Officer*

## Pennsylvania Trust Celebrates 25 Years


Valley Forge National Park was the setting for the celebration of the 25th anniversary of the founding of Pennsylvania Trust. Members of the Pennsylvania Trust team and their families enjoyed an evening of history, including a chance to interact with General George Washington, pictured here discussing the Winter Encampment with Adam Rogers, Portfolio Manager, as colleagues look on.

## Balanced Asset Allocation



## Trust Talk

# Estate Planning for Families with Special Needs

by Peter J. Johnson, Esq.

Many families are impacted by children with special needs. Although parents go to extraordinary lengths during their lifetimes to ensure their children with special needs are physically and financially provided for and protected, parents should also consider the disposition of their assets at death to ensure that their children with special needs are not adversely impacted. By working with a team of estate planning professionals to clarify long-term goals for the care of their children, parents can be confident they have an appropriate plan in place that will benefit their families and not unwittingly sabotage the long-term health and well-being of children with special needs.

**Disinheritance is rarely the best approach.** Some improperly prepared estate plans assume incorrectly that access to money, either outright or in trust, automatically disqualifies disabled individuals from eligibility for governmental benefits. While it is true that disabled individuals may be eligible for government benefits that are "means-tested" (supplemental security income and Medicaid), a properly drafted special needs trust—a stand-alone document, or one created within a parent's will (a "testamentary" special needs trust)—can allow disabled individuals' inheritances to supplement, and not supplant, such benefits.

This does not mean estate planners can disregard benefits that are based on an individual's work history (Social Security disability income and Medicare). Rather, the trustee of a special needs trust must consider the availability of, and a disabled individual's eligibility for, such benefits, to ensure that the administration of a special needs trust does not jeopardize eligibility for such benefits. For example, although a disabled individual may not rely on Medicaid for day-to-day health benefits, that individual may need to qualify for Medicaid for life skills or work training programs.

**Consider division of assets among heirs.** When planning their estates, parents frequently divide their assets equally among their children. In the case of a child with special needs, this approach may result in an inappropriate amount of assets held in trust for the benefit of that child. There is no "one size fits all" approach to structuring the forms of descendants' inheritances, and parents should give careful consideration to the amounts of descendants' inheritances, and—in the case of a child with special needs—consider engaging a life care planner to understand the amount of assets the child is likely to need, or find beneficial, for the rest of his or her life.

**Do not forget beneficiary designation forms.** High net worth individuals often hold significant wealth in beneficiary-designated assets, such as individual retirement accounts. A carefully designed estate plan will ensure that beneficiary designation forms are completed properly and coordinate with the overall goals of the estate plan. As discussed above, outright receipt of such assets by a special needs child could have negative consequences for that child's eligibility for benefits.

**Trustee selection is crucial.** Administration of a special needs trust is not for the faint of heart. It may be tempting to name a trusted individual or family member as the trustee due to the individual's familiarity with the family, but legal compliance and documentation requirements are extensive. The appointment of a professional trustee with specific knowledge of the subject area provides assurance that the goals of the trust will be carried out in compliance with applicable law.

Many complex considerations face families of children with special needs. Our Trust Administration team offers considerable expertise gained from years of experience in the Special Needs and Guardianship arena, as well as a measure of sensitivity and compassion that affords clients and families peace of mind in knowing that their family member's care has been provided for. We look forward to working with you to design an appropriate and effective estate plan that includes all your wealth management needs.

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*Mr. Johnson is Senior Vice President, Trust and Account Administration, at Pennsylvania Trust.*

continued from page 1 Euro to fall, and certainly shake the U.S. financial system. We believe the strategy of European authorities is to avoid any default by providing funding to again push the problems forward in the hope that the impact of default can be better managed in the future. This will ensure periodic crises until the tolerance for austerity among the Greeks ends and the inevitable write-down of debt occurs.

There is some irony in that the debate over extension of the U.S. debt ceiling is taking place as we see the chaos in Greece unfold. Like Scrooge in "A Christmas Carol," we are being shown our future. What has been in most instances a routine vote to extend the borrowing capacity of the government, has become a debate over how to best control current and future deficits. In January, the Congressional Budget Office produced a report on the outlook for the budget and economy for the next ten years. Under the baseline assumptions (current law), annual deficits will decline but stabilize at about 3% of GDP over the period. The cumulative effect would result in debt to GDP rising to 77% in 2021, up from 40% in 2008. However, this outcome depends heavily on spending and tax outcomes that, while part of current law, do not reflect current circumstances. An alternative outcome, and a more likely one to us, shows debt to GDP rising to 97%. Beyond 2021 the situation deteriorates further. As we know, the primary agents for increased spending will be the surge in "baby boom" retirements and the impact on Social Security and Medicare spending; structural as opposed to discretionary spending. While not yet "Greek-like" in severity, the structural nature of the coming deficits has, and will, create problems with the value of the dollar, the level of interest rates, and eventually with inflation.

Beyond earning a continuance, we do not see much that the European authorities can do to fix the problem of Greek and perhaps other sovereign debt, thereby ensuring a future crisis. In contrast, we see some movement in the U.S. towards resolving our structural issues. First, there is an effort among the states to address their budget problems. It is bipartisan in that not just Wisconsin, with its well-publicized changes, but states such as New York and Massachusetts, have begun to deal with long-term budget imbalances. On the national level, in a dramatic change, AARP's leadership has accepted the need for reform in the Social Security System. Lastly, central to the debate going on now about extension of the debt ceiling, is the need to establish a framework for dealing with the long-term deficit problem. Justifiably, there is little expectation among investors for any progress of this sort. But a compromise on the debt ceiling that includes a credible outline for change would provide a significant boost to a deficit-weary market.

We must deal with the daily ebb and flow of the markets. But the evolution of these structural issues will provide the backdrop for market action in the immediate future.

*Mr. Woolbert is Senior Vice President and Chief Investment Officer at Pennsylvania Trust.*

## Guardianship and Special Needs Experts Join Trust Administration Team

Pennsylvania Trust has long been committed to the area of Special Needs and Guardianships. Adding further strength and expertise to this important practice are Peter J. Johnson, Esq. who joins us as Senior Vice President, and Sheila Gibson, Vice President.

Peter will serve as unit head, administering estate, trust and guardianship accounts with a focus on special needs individuals. He comes to us from Heckscher, Teillon, Terrill & Sager where he specialized in special needs trust and guardianship planning; estate planning for high net worth individuals; trust and estate administration; and fiduciary litigation and counseling.

Sheila's primary responsibilities will include the administration of special needs trusts and guardianship accounts for minors and incapacitated persons. Prior to joining Pennsylvania Trust, she spent over nine years with PNC's Wealth Management group as a special needs trust and guardianship advisor.

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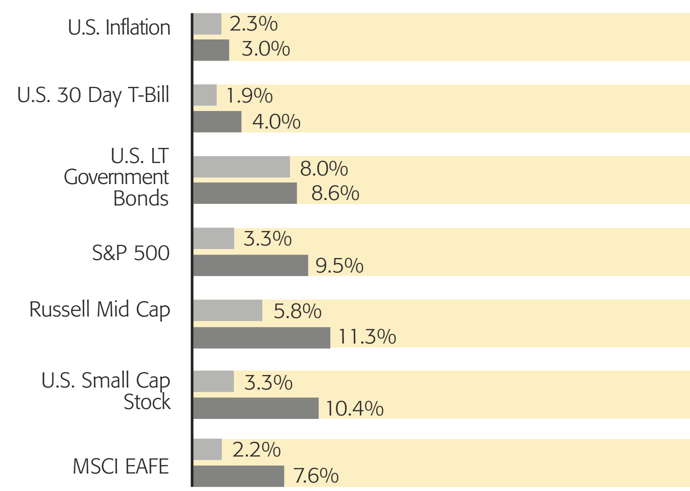
Pennsylvania Trust is committed to conduct all our relationships with integrity and to maintain the highest ethical standards; provide outstanding professional and personalized services; produce superior investment results consistent with client objectives; and retain exceptionally skilled individuals, empowering them with state-of-the-art technology.

# Market Indicators

| | Current | Three Months Ago | One Year Ago |
|---|---|---|---|
| Stock Indices | 6/30/11 | 3/31/11 | 6/30/10 |
| Dow Jones Industrial Average | 12,414 | 12,320 | 9,774 |
| Standard & Poor's | 1,321 | 1,326 | 1,030 |
| U.S. Treasury Yields | | | |
| 2 Year | 0.5% | 0.8% | 0.6% |
| 5 Year | 1.8% | 2.3% | 1.8% |
| 10 Year | 3.2% | 3.5% | 2.9% |
| 30 Year | 4.4% | 4.5% | 3.9% |

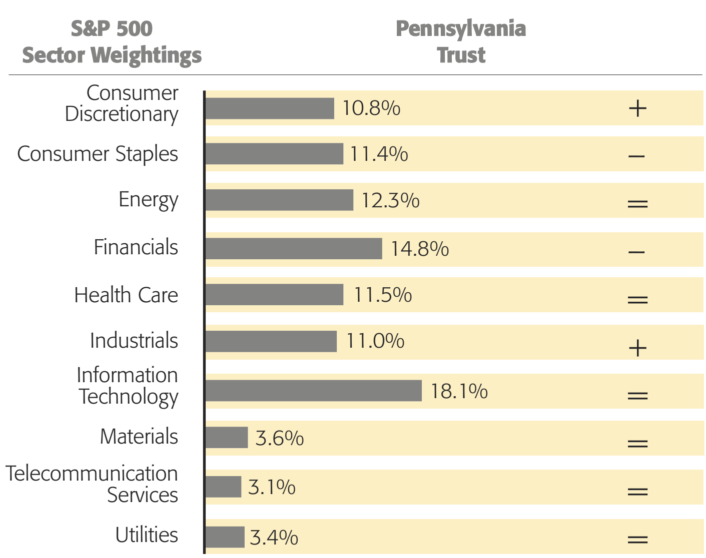
## ANNUALIZED RETURNS OF SELECT ASSET CLASSES




*Source: Ibbotson Associates*

## CORE LARGE CAP DIVERSIFICATION

*In order to maintain a well diversified large cap common stock portfolio, we recommend the following relative sector weightings within the Standard & Poor's 500:*

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25 YEARS

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