MacMillan Financial
John MacMillan, CRFA, CLTC, CSA
P.O. Box 66
Annandale, NJ, 08801
T: (908) 236-7500
F: (908) 236-7511
WWW.MACMILLANFINANCIAL.COM

SENIORS/BOOMERS NEWSLETTER

"THE RETIREMENT EXPERTS"

July 2010

BE CAREFUL WHAT YOU WISH FOR!

Happy 4th of July.

There's so much going on as we enter the second half of the year, that it's hard to know where to start this month's newsletter. To begin with, thankfully the market has taken the time to shake off some of the blues that it had for the month of May and most of June. If you went into a deep sleep on January 1st and woke up at the end of June, you'd be quite justified in thinking that the market was pretty quiet & tame for 6 months. Ha, tell that to your frazzled nerves and queasy stomach. We ended up the first half just about where we started the year.

Hopefully, we should have a pretty decent summer (market-wise) until we get to earnings season in the fall. I still believe the July earnings numbers should be good. Analysts are expecting a 27% rise in the 2nd quarter year-over-year earnings. October's, however, are going to be more of a challenge. (More on this in a few minutes).

For now, the market is attractively priced and is trading at 12.5 times forward 12 month earnings estimates. The fact that there are 34 S&P 500 stocks yielding more than 5% dividends tells you stock prices are fairly cheap. When you look at Earnings/Price (instead of Price/Earnings) we come up with a calculation showing stock prices are yielding 7.2%. That's a heck of a lot better than 10 Year Treasuries yielding 3.2%.

As the caption for this month's newsletter cautions, getting what you want may not always be what you need. For many months now the Treasury Secretary and the White House have been rattling chains at China to 'un-peg' their currency from the U.S. dollar and let it float in the world currency markets. This had to be done sooner or later. The ramifications however, could prove to be a little disappointing.

A stronger Chinese renminbi will mean a weaker U.S. dollar. The Chinese will gain significant purchasing power for everything their central government buys. Because most commodities are priced in dollars (think gold, iron ore, steel, aluminum, coal, grains, natural gas and oh yes, oil, etc, etc) the likelihood of price increases are pretty well baked into the cake.

Higher prices lead to inflation. Inflation leads to higher interest rates. Higher interest rates will mean servicing the $13 trillion of debt the country is shouldering will get **much more expensive.** This is going to be a very tricky maneuver even for Treasury and the Federal Reserve. According to Table S-4, ***interest payments*** on our national debt are on course to explode from $164 billion/year today to more than $1 trillion per year by the end of this decade.

Financing further debt is also going to be a little challenging. This year alone Treasury has to refinance $2.4 trillion of debt and the Chinese aren't showing up at the party in their usual numbers. In 2006 the Chinese bought up 47% of our debt notes. In 2008, that number was down to 20%. Last year…only 5%. It may come down to the only entity willing to purchase our debt will be us through the Federal Reserve.

What caught my eye in June was a report issued by the Treasury Department which debunked the theory that we would hit $20 trillion of debt by 2020. They have now changed that estimate to $19.6 trillion by... 2015.

Where is all this money going to come from? I have several interesting tidbits which you should find interesting:

• According to the Tax Policy Center 47% of U.S. households will pay no federal income tax for 2009.

• The Taxpayers Foundation has found that 36% of the 142 million people who filed tax returns in 2009 had no tax liability, and in fact through 'tax credits' many of them actually got money back from the government.

• The U.S. population is 307,000,000. This means that we have 90 million people supporting 217,000,000 (and of course, the government).

From an investment point of view, these facts should help us with structuring our portfolios. Bill Gross, famed bond investor guru had this to say: 'High fiscal deficits and higher outstanding debt lead to higher real interest rates and ultimately higher inflation. Both trends are bond market unfriendly'.

This is going to be particularly true for long-term maturity bondholders and bond fund holders. According to Erik Jacobson, director of fixed income research at Morningstar, for every 1% rise in interest rates in the economy, Intermediate Term bond funds will suffer a decline of 4.4%. **The lesson here is to keep your <u>investment grade bonds</u> ultra-short, like no more than 3-4 years.**

How are we doing on the state level? Actually, not much better.

• New York & New Jersey are running $18 billion & $7 billion budget deficits respectively. In fact, as you know, New York has been on the verge of shutting down most of this year.

• California's budget deficit is projected to be $37 billion in 2010.

• San Diego is being urged to consider bankruptcy by the Grand Jury which examines local governments in addition to indicting suspected criminals. The city has unfunded pension obligations of $2.2 billion and unfunded retiree healthcare liabilities of $1.3 billion.

• The Illinois Department of Corrections was forced to make an emergency purchase of ammunition last month when their regular supplier refused to ship the bullets due to unpaid invoices. The state budget deficit is $13 billion and its unfunded liabilities are about $78 billion.

• U.S. states reportedly face a funding gap of more than $1 trillion for the retirement benefits promised their public sector employees. Orin Kramer, chairman of the New Jersey retirement system has stated that if assets were recorded at market value and not what's on the books, the actual number is at least $2 trillion. If the states default who do you think gets to pay the tab??? Right! Us. The people who pay the taxes.

• The state capital of Pennsylvania, Harrisburg is on the brink of declaring bankruptcy. Vallejo, California already has.

Why am I telling you this? For an investment reason, of course. **Stay away from municipal bonds**. Many people have been flocking to them in search of safety (???) and tax free yield. Even Warren Buffett has been warning of a municipal debt meltdown and has said, 'insuring muni bonds has the look today of a dangerous business'. This coming from an insurance man who also owns a ratings agency.

MISCELLANY ☺

• Want to know which hospitals are considered the best in town? Well, you can. Patient outcomes from hospitals are measured and recorded at the government website, www.data.medicare.gov

• If you are looking for a way to create a document that any computer can read, download ***free*** software to create PDF files at, www.primopdf.com

• You suspect that your computer has a file containing a virus, or Trojan or other malware. You can have it analyzed for free at www.virustotal.com

• Have you ever wondered when it's the best time of year to buy certain products? There really is a best time.

>Small appliances & electronics are on sale in April.

>Refrigerators, in May.

>Computers are priced lowest in August.

>Televisions heavily discounted in January.

>Cameras in February.

>You'll get great deals on lawn mowers, BBQs & snow blowers at the end of season.

What Happens to Bondholders When a Company Goes Bankrupt?

Seniors like bonds because they can provide a steady income, diversify a stock portfolio, and are backed by the insurer's financial strength. But things don't always go as planned. Companies occasionally have financial problems and must file for bankruptcy.

Investors holding bonds in bankrupt companies can at least have the comfort in knowing that as unsecured creditors they are second in line for payment. Secured creditors, those with claims backed by collateral, such as equipment or real estate, are paid first. Stockholders come last, and that is only if there is any money left after the creditors have been paid.

There are two general forms of bankruptcy: Chapter 7 and Chapter 11. With Chapter 7, the company is liquidated and bondholders should file a claim to receive a portion of the value of their bonds. In Chapter 11 proceedings, however, the process is quite different.

Chapter 11 allows the corporation to reorganize. Its bonds might continue to trade, but holders will not receive principal and interest payments. As a result, a default could occur, and the value of the bonds might decline significantly, or the court may approve an exchange of the old bonds for new ones (which could have a lower value).

How can you find out if a company that you lent money to (by purchasing their bond) has filed for bankruptcy? TV reports, newspapers, and financial magazines often give an account of companies that recently declared bankruptcy. The company will also send you information on the reorganization plan and ask you to vote on it. If a financial institution holds the bond for you, it should forward everything from the company.

If you would like a free credit report on bonds you currently own, include the CUSIP numbers and issuers' names on the enclosed coupon and mail it to my office. Along with the report, I will provide a list of investment-grade bonds that I am currently recommending.

TIPS to Fight Inflation During Retirement

Perhaps no word is scarier to a fixed income investor than inflation – especially for those who depend on the yields from bond investments for their retirement income needs. For example, inflation can reduce the payout rate of bonds over the long-term, as the higher costs of living can often erode the purchasing power of bond's return.

You can however, help protect your portfolio and your cash flow from inflation by adding Treasury inflation-protected securities (or TIPS) to the bond portion of a diversified investment portfolio.

TIPS were introduced several years ago by the U.S. Treasury to offer investors a means to protect assets from inflation. TIPS help to protect against inflation by adjusting the principal amount invested by a rate equal to the Consumer Price Index (CPI) – the primary barometer of inflation on the consumer level. Because the principal amount of the TIPS bond rises over time, this helps to protect the purchasing power of the bond.

TIPS can also be a suitable choice for a diversified portfolio, because they have a low correlation with stocks and other bond securities. That means they often react differently than stocks and other bonds to market and interest rate risks and can potentially reduce the volatility of your overall portfolio.

However, TIPS are not a risk-proof investment. To receive the full inflation-protection potential of a TIPS, it must be held for the term of the bond. Also, TIPS may underperform regular Treasury bonds, should inflation remain low. In a deflationary environment, TIPS could also lose value, although investors would be guaranteed to receive at least the par value of the security upon maturity.

TIPS may also provide you with some tax benefits. Like other Treasury notes & bonds, TIPS are exempt from state and local taxes, but interest payments are subject to federal income tax. A very important point is that gains from inflation adjustments to the value of the principal are taxable in the year they occur, even though you won't get the money until maturity.

A complete evaluation of your current investment portfolio and income needs can help you determine whether TIPS would be appropriate for you. Call my office to schedule an appointment to learn more, or simply complete the enclosed reply coupon to have information on TIPS mailed to you.

IF YOU HAVE FAMILY OR FRIENDS THAT MIGHT ENJOY MY ARTICLES, FEEL FREE TO PASS THEM ON.

IF THEY WOULD LIKE TO RECEIVE THEIR OWN COPY OF MY MONTHLY NEWSLETTER, THEY SHOULD SIMPLY E-MAIL ME AT

JRM@MACMILLANFINANCIAL.COM

FOR MORE INFO:

Mail or Fax back to:
John MacMillan
P.O. Box 66
Annandale, NJ, 08801
T: (908)236-7500 F: (908) 236-7511
www.seniorsboomers.com

Please send me information on these items:

*Corporate Bonds.
*Municipal Bonds.
*TIPS

I would like to order a copy of these booklets (enclose $1 for each)

- ❑ Avoid Mistakes in Buying Long-Term Care Insurance
- ❑ Annuity Owner Opportunities: Tips and Ideas That Could Save Thousands
- ❑ Understanding Mutual Funds
- ❑ Six Strategies to Help Retirees Reduce Taxes and Preserve Their Assets
- ❑ Helping You Avoid IRA Distribution Mistakes (And Reduce Your Taxes)
- ❑ CD Shoppers' Guide
- ❑ Creating a Retirement Income You Cannot Outlive
- ❑ Keep the IRS out of Your IRA
- ❑ Leaving a Legacy
- ❑ Protect your Investments (a guide to investing without losing a penny)
- ❑ Law Points for Senior Citizens (78 page guide)

I think these people would like to receive your newsletter and an invitation to your next public presentation:

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