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"

August 2011

I hate to spoil a good argument by throwing in a few facts.....

The debt ceiling debate continues to rage on as I write this piece. Regardless of how this event turns out, and how close we get to the brink (or fall into the abyss), getting our fiscal house in order has to be the priority of the day.

It is abundantly clear that the majority of Americans believe that our current spending addiction has to be curbed. Neither you nor I could run our respective households on borrowed money. As I mentioned last month, our government borrows, **from strangers**…40 cents…of every dollar we spend. This cannot continue.

The facts are pretty much straight forward. We sent a lot of new people to Washington last November with a clear mandate. Fix this problem because it will not go away by itself. All the current political one-upmanship and theatrics is not doing the "people's business". Our message to Congress (and to our local representatives) has to make this clear. *If you can't afford a Cadillac…but a Chevy*. Ladies & gentlemen in Washington – DO YOUR JOB!

Although I am <u>highly doubtful</u> that the United States would ever default on its debt obligations, its credit rating is another subject. At this point a credit downgrade looks to be unavoidable. If/when that happens let's take a look at some of the consequences of going from a AAA rating to a AA:

•According to the American Institute for Economic Research, the 'most immediate impact of a downgrade would be an increase in interest rates on Treasuries of at least half a percent'. They go on to say that that would cost the economy at least half a million jobs.

•JP Morgan Chase has come out and said the interest rate increase will immediately cost the American taxpayer $100 billion. This is absurd in the face of Congress trying to reduce an already ballooned budget deficit. Adding a $100B to our growing list of bills is going in the wrong direction.

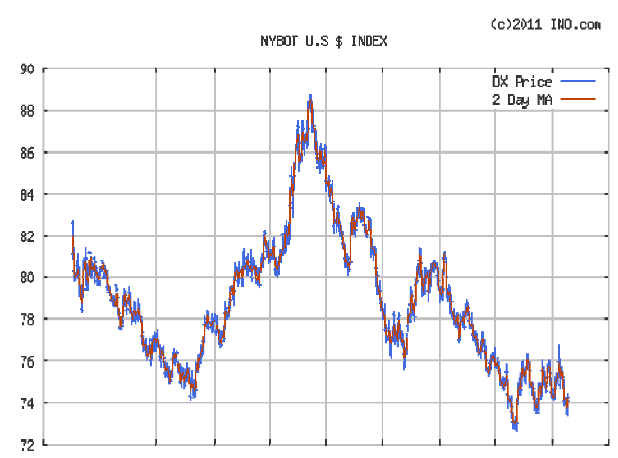
•Interest rates on variable rate mortgages, credit cards, car loans, etc. would rise.

•State and municipal governments would see higher costs to borrow money…if indeed they could find willing lenders.

•Many companies would see borrowing costs rise which would negatively affect employment as well as spending on capital expenditures.

•All financial institutions would have to hold more capital (rather than lending it) to secure short term loans.

•The role of the U.S. dollar as the world currency would be in serious jeopardy. When the day comes that our $$ is no longer considered the world currency, our days of printing money come to a screeching halt...and our reckless spending along with it.



The preceding chart illustrates how much our currency has depreciated since last summer. In June 2010 the US$ index (which compares the US$ against a basket of world currencies) sat at almost 89. Now in July 2011, we are at 74. That is a decrease of $17%!

Now let me ask a rhetorical question. If you were a Central banker in China and holding, what many analysts believe to be, $2 trillion of US debt, what would you do about losing $340 billion on currency exchange alone in 12 months? How much longer would you want to own US Treasuries or US dollars?

If we go back further in time to 1934 when the FDR administration repudiated the national contract to pay debts in gold and, instead paid debt in dollars, this is the equation:

Prior to this de-facto default, the US dollar was defined as being the equivalent of 1/20th of an ounce of gold. Said another way, $20 US dollars purchased one ounce of gold. Today, it takes $1600 to buy one ounce of gold. That is how much our currency has devalued over the last 80 years.

Come August 3rd, or close to that day, Treasury is going to have to decide who gets a check. The US government is supplying about 20% of American's personal income through social security, jobless benefits, food stamps, disability payments, etc. Who will get money, and who won't? The following chart is a list of our bills due to be paid in August.

Making Priorities

If Treasury can't issue new debt, it must choose what bills to pay

Item	Cost	Running Total
Interest on Treasury Securities	$29 b	
Social Security Benefits	+ $49.2 b	$78.2 b
Medicare/Medicaid	+ $50 b	$128.2 b
Defense Vendor Payments	+ $31.7 b	$159.9 b
Unemployment Insurance Benefits	+ $12.8 b	$172.7 b
Military Active Duty Pay	+ $2.9 b	$175.6 b
Veterans Affairs Programs	+ $2.9 b	$178.5 b
IRS Refunds	+ $3.9 b	$182.4 b
Food/Nutrition Services & TANF	+ $9.3 b	$191.7 b
Federal Salaries & Benefits	+ $14.2 b	$205.9 b
Small Business Administration	+ $0.3 b	$206.2 b
Education Department	+ $20.2 b	$226.4 b
Housing & Urban Development Programs	+ $6.7 b	$233.1 b
Other Spending*	+ $73.6 b	306.7 b

e.g., Justice, Labor, General Services Administration, Commerce, NASA, Health and Human Services, Energy, EPA, Interior, Federal Transit Administration, Federal Highway Administration, AID, etc.

Source: Bipartisan Policy Center WWW.AGORAFINANCIAL.COM

WHAT TO DO NOW?

1. Believe it or not, the stock market is quite strong in the face of all these problems. More than ¾ of the S&P 500 companies have beaten 2nd quarter estimates…and the 200 day moving average is still sloping upwards. Don't forsake the market…but put off to the side, in cash, money needed for immediate or near future needs.
2. According to David Rosenberg, (former head of investments for Merrill Lynch) he recommends income generating stocks and precious metals.
3. A good bet is a basket of blue-chip companies getting a large portion of their earnings from overseas markets…that pay dividends. These companies actually benefit from a falling dollar.
4. There are 947 companies (many of which are solid American companies) paying dividends at a higher rate than the current yield on US 10 year Treasury notes.
5. Did you know that all DOW 30 industrials and 76% of S&P 500 companies generate substantial earnings from overseas? The key is to pick those with growing earnings and dividends and a clean balance sheet.
6. As a point of interest, there is $1.4 trillion in undistributed profits sitting in overseas units of American companies…most of which is in the pharmaceutical & oil industries.
7. If the US government does get a downgrade, there are several American companies which will have a higher rating. Guess where new money will go?
8. Money continues to pour into bond funds. Morningstar has estimated that 2011 will be the 3rd straight year where taxable bond fund inflows will exceed $200 billion. Remember, as interest rates rise the NAV of these funds will fall like a stone. Caveat emptor.
9. Bank stocks are getting a lot of attention recently. The big story is that some are

now selling below book value. I'm not in the camp of jumping in the water yet. At such time as the full extent of their bad/toxic mortgage loans are fully accounted for, we may see that they are not quite the bargains some are proposing.

10. David Rosenberg mentioned precious metals as a good investment in this market environment. Silver, in particular, has attracted a lot of attention. But, be careful here. Many investors have flocked to one particular Exchange Traded Fund in the belief that they physically possess all the silver they have sold through their shares. This is NOT the case. According to recent research, this particular ETF is actually 37 million ounces short of what their prospectus says that ought to have. Choose carefully.

Now, talk about liking silver. This is a sign posted outside the Long Bridge Grill in Sandpoint, Idaho. This may seem like quite a deal, 50 cents for a burger & fries. BUT, because silver coins, pre 1964, were real silver this may not work out in your favor. When you do the math with silver at $40/oz, this equates to about $15 for a pretty cheap meal.

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☺You can live forever by recording family stories for preservation at the American Folklife Center at the Library of Congress. Go to www.storycorps.com

☺Looking for the best local deals on gas. Try www.gasbuddy.com

☺There is a movement afoot which effectively will limit forever social security benefit increases for seniors. It's called 'chained CPI'. What it basically does is this: If you eat steak, but cannot afford it anymore and therefore switch to hamburger, the government says that your standard of living hasn't changed because you're still buying beef. Therefore on those grounds you don't get a CPI increase. So what happens when you can no longer afford hamburger but instead buy baked beans. Well, once again the government doesn't count this as a reduced standard of living because you can still afford to get your protein. Hard to believe, ain't it? See a couple of videos on YouTube.

http://www.youtube.com/watch?v=MZVeXGf0fS4

http://www.youtube.com/watch?v=rWiSJVtTZ8Q

Understanding the difference between Exchange Traded Funds (ETF) and Exchange Traded Notes (ETN)

Many investors tend to group both ETF's and ETN's in the same category. Both are tied to an index or basket of homogeneous companies and/or industries. Both offer lower fees than mutual funds and both trade like stocks throughout the day.

Some of the dissimilarities are:

1) **ETF's actually own the underlying securities that go into their mix. ETN's do not.**

2) **Dividends are paid out in cash for ETF holders. ETN's retain dividends in the total return of the note. This makes The ETN's more tax friendly.**

3) **ETN's give the investor their promise to pay their NAV value and is backed only by the good faith of the issuer. Think Lehman Brothers. They can go out of business without any assets for you to get your hands on.**
4) **ETF's focus on stocks & bonds. ETN's focus on asset classes more difficult to access, commodities and sometimes unusual strategies.**

If you would like free information on any of the subjects discussed in this month's newsletter, please fax the enclosed reply coupon or call my office for a free consultation.

Mail or Fax back to:
John MacMillan
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- ☐ Dividend paying stocks
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