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# SENIORS/BOOMERS NEWSLETTER

***"THE RETIREMENT EXPERTS"***

**August/September 2013**

**"Even turkeys can fly if the wind blows hard enough"…………….old stock market maxim**

(The stock market has been range bound all summer with not a lot of exciting news to report. For that reason I'm combining the August & September newsletter so that I don't get too boring with, what up till now, have been relatively tame events). Take a look!


As you can see the S&P 500 has been in a narrow trading range since early March: between about 1550 to where we are now – just below 1700. The same thing goes for the Dow Jones. The chart below shows a very tight range since March of 14,500 to 15,500.


Nonetheless, that hasn't stopped some stocks from getting 'silly expensive'. Without naming names, one electric car company that is not profitable is selling at 28x its book value; 12x sales with a price/earnings of 312 (that means it would take you 312 years to recoup your stock investment).

Another company making just one product – a medical device- has yet to turn a profit in 13 years; has annual sales of about $250M but is valued at almost $2B; trades at 13x book value and just had their most recent quarterly report which showed another loss, and yet the stock went up more than 10%. Go figure.

My last example is a leading company in product fulfillment. I've wanted to buy shares for ages but just cannot pull the trigger when its P/E ratio is 104. This is just too rich for a value investor.

These examples are far from exceptions. The market right now is fairly expensive and it's becoming harder and harder to find cheap stocks...by that I don't mean lousy companies…I mean companies selling below their true value. If you buy great companies for less than their worth, you will never get burned for long in market declines.

This past earnings season saw, once again, earnings rise but the top line (sales growth) stay put. This is not how markets gain value. Wall Street is looking for significant acceleration in 3rd and 4th quarter earnings – up from $26.71 in the 2nd quarter to $27.72 in the 3rd, then $29.32 by year end. These are lofty numbers.

Currently the stock market is being fueled by monetary stimulus without strong underlying economic activity. This has got traders a little jumpy. For the first half of the year, we have seen volatility on a scale with 2008/2009.


These numbers are through June and indicate investors having a hair trigger and an itchy finger.

## OPPORTUNITIES AND DANGERS

When is market sentiment getting frothy? When investors are borrowing a lot of money for margin purchases. Currently, margin debt has reached $408.7 billion. That number tops the July 2006 former peak of $381.4 billion by $27 billion. That's a lot of money. That's a lot of speculation.

I mentioned earlier that you should try to buy stocks selling below their intrinsic values. Conversely, you should keep a close eye on stocks selling above their fair value.

These two factors – sentiment and valuation – blow the 'buy & hold' crowd out of the water. If sentiment is running high, it is setting the trend. If valuations are going to the moon, it's probably time to take profits.

Benjamin Graham, one of the most famous investors of all time, and mentor to Warren Buffet, had three simple rules to his investing success.

#1. Buy stocks with a price-to-earnings ratio below 10 and a debt to equity ratio below 50.

#2. Hold a minimum of 30 stocks.

#3. Either sell once you're up 50% or in two years, whichever comes first.

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Investors everywhere are looking for yield in this no-yield environment. But, be careful. Interest rates are rising and interest sensitive stocks could be adversely affected.

REIT's for example, have to borrow money on a regular basis in order to finance their operations. (Remember, they are required by law to distribute 90% of their income). Check their balance sheets to be certain that their credit quality and earnings power are both strong.

The ability to maintain REIT status is also often directly related to the credit quality of the portfolio, since the majority of the REIT's income and assets must also be derived from "real estate sources". To the extent that a REIT portfolio deteriorates, income and assets from real estate sources will decline as "real estate" assets are written down in value and income from "real estate sources" evaporates.

Bonds are another area of concern. Bond yields are so low it looks like they are competing in an ugly contest. Again, as investors go out further on the risk curve in search of making a few bucks on their fixed income investments, they have ventured into 'junk bonds'.

It used to be that junk bonds paid double digit returns to compensate investors for their higher risk of default. Today, however, they pay meager returns like a blue-chip! It's all about supply and demand, and demand is high, so yield is low.

Never pay over par (100) for any junk bond. It's a recipe for disaster. In fact I try never to pay more than par for any bond – investment grade or otherwise. At least when the bond matures you'll get all your money back…providing they're still in business.

A key point to remember in prudent investing is to ensure that you have a balanced and asset allocated portfolio. Also, CASH is an asset class. Don't be uneasy if your every last cent is not invested. It's great in a rising market, but it's not so great a strategy in a market correction.

I'm sure this comes as no surprise to you, (I've been preaching this forever) but dividend paying stocks put money in your account every quarter. They account for over 40% of stock returns and they are 70% less volatile than corporate earnings.

Finally, one last area to look for improved returns is in the realm of companies buying back their own shares. These are dividends of a different nature. Rather than sending you a check, the reduced number of shares outstanding mean higher earnings per share, which in turn usually means a higher share price. Also, you don't pay taxes on gains until you sell.

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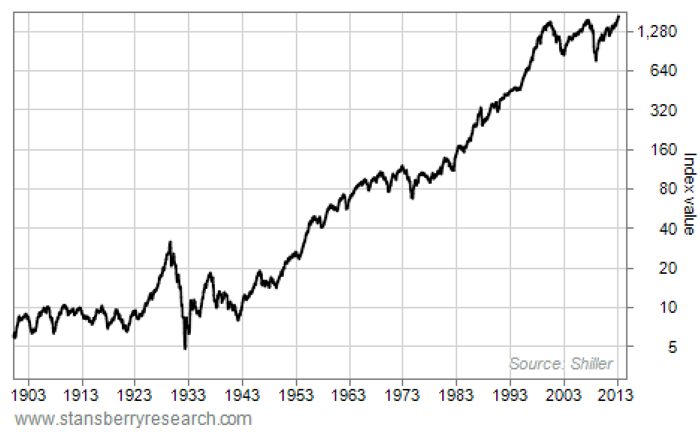
## CHARTS CAN BE DECEIVING….

Charts can be a useful resource when looking at stocks and markets…but the same data can tell, supposedly two different stories. In viewing the chart at the top of the page you would suppose that the stock market was basically flat from 1900 until the mid-80's. Then, it took off till the crash of 2000 and 2007; we also see extreme volatility in this period.


This next chart has the same data, but a different scale which allows for percentage changes rather than using straight numbers. After all, 50 point change in a market having a value of 100 is a lot different than a 50 point change in a market having a value of 1600.

This chart correctly depicts the effects of the stock market crash of 1929; whereas the first chart barely shows a ripple of a change The lesson here is to be careful when viewing charts!




## CLEAR ANSWERS TO YOUR QUESTIONS ABOUT THE NEW HEALTH INSURANCE PLANS

After years of discussion and amid continuing controversy, some of the most important parts of the Affordable Care Act will take effect in the next six months (see "ObamaCare Basics" below). Yet many people still aren't clear on how these elements of "ObamaCare" will affect them.

To help make clear what is happening, *Bottom Line/Personal* asked Kathleen D. Stoll, JD, director of health policy for Families USA, to answer 12 key questions…

## ELIGIBILITY

**Q:** *I read that my state decided not to set up a health insurance marketplace. Will there be any marketplace available to me?*

**A:** Yes. Every state and Washington, DC, will have a marketplace (also called an "exchange") of insurance plans from private insurers. Some marketplaces will be run by the states themselves…others by the federal government…and still others by a state/federal partnership. All of the marketplaces will help consumers compare plans and find financial assistance, if they are eligible, to help pay for coverage.

However, it is possible that differences in funding will result in less in-person support for consumers in states where the marketplaces are run by the federal government.

**Q:** *I have Medicare. How will these health marketplaces affect me?*

**A:** They won't affect your coverage. Medicare recipients are not eligible for coverage through the marketplaces.

**Q:** *I obtain health insurance through my employer. Will I have to shop for insurance through these marketplaces?*

**A:** No. You can continue with your employer's coverage. But if it offers limited benefits and/or little help with premiums, you might have the option of buying coverage through a marketplace instead. Once the marketplaces are up and running, they will provide details about what to ask your employer to determine if its group health coverage is so limited that you qualify for this option.

**Q:** *I heard that some small businesses will drop their current insurance plans and leave it up to their employees to shop for their own plans in the marketplace. Is that true?*

**A:** Many small-business owners are unsure whether they will drop coverage. However, employers with more than 50 employees that do not provide insurance plans will face penalties.

Instead of dropping coverage, some employers may switch plans, using the marketplaces to compare small group plans. To help pay for the cost of insurance, tax credits will be available to some small businesses.

## COVERAGE

**Q:** *What will the plans in the new marketplaces include?*

**A:** Health insurance plans sold to individuals and small businesses both inside and outside the new marketplaces will have to provide at least "essential benefits." This means that all policies will include prescription drug coverage, preventive services, maternity care, mental health services and other components currently missing from many individual insurance plans. And plans won't be able to arbitrarily limit or cap the coverage received. Also, plans will have to meet rules about providing adequate networks of medical providers.

**Q:** *Is it true that there will be only four health insurance plans?*

**A:** That's not true in most states, if any. All the health marketplaces will divide plans into *four tiers*—bronze, silver, gold and platinum—but that's just to make it easy for consumers to determine quality of coverage. In most states, there will be a number of different plans within each of these tiers, likely from multiple insurers.

Plans must meet a certain actuarial value to qualify for a given ranking—that is, they must pay a predetermined percentage of total average costs for covered benefits—but even within a tier, plans could have different costs and benefits. For example, one plan might have relatively high deductibles and low co-pays, while another might offer the reverse.

The online marketplaces are supposed to list each plan's costs and benefits in a consistent format and clear language to make the plans easy to compare.

**Q:** *My son is 20. Why should he have to pay for a plan meant for older people?*

**A:** He won't have to. There will be certain low-cost, high-deductible plans available only to people under age 30. These are likely to be much less expensive than more comprehensive plans. But with high deductibles and less financial protection, these plans will be appropriate only for people who have sufficient financial resources to pay hefty medical bills out-of-pocket. Also keep in mind that under the new law, children are now allowed to remain on their parents' health plans until age 26.

**Q:** *If I use a marketplace, do I have to shop online for coverage?*

A: Not necessarily. The marketplaces will offer shopping assistance through toll-free phone numbers and in person in many communities starting in October.

**Q:** *I looked for the marketplace online but couldn't find it. Where is it?*

**A:** It won't be available until October 1. Until then, visit www.Healthcare.gov/ Marketplace for updates.

**TAX CREDITS**

Nearly 26 million Americans will be eligible for tax credits to help them pay the cost of health insurance.

**Q:** *Do I have to be poor to qualify for these health insurance tax credits?*

**A:** Many middle-class families will qualify. The limit has been set at 400% of the federal poverty level (FPL). This year, that's an annual income of $45,960 for an individual…$62,040 for a couple…or $94,200 for a family of four. However, your tax credit will decrease the closer you get to these limits.

*Example:* Because of the tax credit, a family of four with income of $35,325 (that's 150% of the FPL) would be able to buy a typical silver-tier plan for $1,413 per year out-of-pocket, which equals 4% of the family's income. If that family had an income of $94,200 (400% of the FPL), however, it would have to pay 9.5% of its income out-of-pocket—a much heftier $8,949 bill.

The tax credits will be based on the price of a typical silver-tier plan in the state. Families receiving tax credits can opt for pricier gold or platinum plans…or pay even less in premiums if they are willing to accept the more limited benefits of a bronze plan.

People won't have to do this math on their own. Once the marketplaces are up and running in October, they'll guide users through the process. A family of four earning $50,000 would be entitled to a subsidy of around $6,500.

**Q***: The subsidy is in the form of a tax credit. Does that mean I won't receive it until I file my tax return?*

**A:** No. People can elect to get credits in advance, but in that case, the government will pay the amount of the credit directly to the insurer and you will pay only the remaining portion of your premiums.

**Q:** *If I sign up for 2014 coverage in late 2013, I won't yet know my exact 2013 income. What should I do?*

**A:** Your 2014 subsidy will be based on 2014 income. You will be asked to estimate your 2014 income when you apply. If your estimate proves too high, you can return to the marketplace, update your income and receive the credit you're due. If your estimate is too low, you might have to pay back part of your subsidy. There's no penalty for getting income estimates wrong.

**OBAMACARE BASICS**

Starting October 1, 2013, individuals and small businesses will be able to compare and sign up for health insurance policies through new online marketplaces. These policies take effect January 1, 2014.

Among the people who benefit the most will be those who have health problems but lack access to group coverage. Insurers will no longer be allowed to deny coverage or charge higher premiums based on preexisting conditions.

Also benefiting will be people ages 50 to 64 who lack group coverage, including early retirees. Insurers still will be allowed to charge older applicants more than younger ones, but they no longer will be able to charge older applicants the prohibitively high rates that they often imposed in the past.

Americans who choose not to obtain health insurance will have to pay a penalty starting in 2014. That penalty will be $95 or 1% of income, whichever is greater, in 2014, but the penalty will climb in future years, to $695 or 2.5% of income by 2016.

**Source:** Kathleen D. Stoll, JD, director of health policy for Families USA, a nonprofit organization that advocates for affordable health care in Washington. She previously served as special assistant for health & welfare issues for House Ways and Means Committee.

## ENERGY ANSWERS THE CALL

We all know that we have problems here at home with federal & state budgets, deficits and of course, spending. When we look at our national debts, it can be a little nerve wracking and begs the question: How on earth are we ever going to pay off these $70 trillion of accumulated debts?

Table 5. Treasury debt held by the public and combined federal off-balance sheet liabilities

| | 2006 | 2008 | 2010 | 2012 |
|---|---|---|---|---|
| 1. Treasury debt held by public | 4,867 | 5,837 | 9,052 | 11,299 |
| | | | | |
| 2. Housing-related commitments | 6,386 | 8,036 | 7,594 | 7,520 |
| 3. Student and other loan guarantees | 468 | 547 | 419 | 325 |
| 4. FDIC | 4,154 | 4,975 | 6,575 | 7,406 |
| 5. Federal Reserve | (773) | 360 | (1,136) | (1,128) |
| 6. Social security | 16,500 | 18,700 | 21,400 | 26,500 |
| 7. Medicare | 28,500 | 33,200 | 24,900 | 27,600 |
| 8. Other government trust funds | 1,308 | 1,487 | 1,646 | 1,862 |
| **9. Total off-balance-sheet commitments** | **56,544** | **67,305** | **61,398** | **70,085** |



**Source: National Bureau of Economic Research**

Being a great believer in American ingenuity (we always figure it out) and our ability to solve problems, and to quote Winston Churchill when referring to our Congress

"The Americans will always do the right thing… after they've exhausted all the alternatives",

I believe we have before us one of the most exciting periods ever, and a potential 'game-changer' for our Finances and National Security….**ENERGY!!!**

Since peaking in 2004 at 20.7 million barrels of oil consumption/day, the United States has been steadily reducing how much oil we use to about 18.7 million barrels/day in 2013. In 2012 we imported 40% of the oil we consumed compared with 60% in 2005. And, according to the US Energy Information Administration (EIA) we'll only need to import about 30% in 2014.

This is going on because we have been steadily increasing our domestic oil production from 5 million barrels/day three years ago to 8.5 million by next year. According to experts, if these trends continue the United States will be able to supply all of its own energy needs by 2030.

Experts are also confident that within **seven years** the U.S.A. will not need to import any oil from outside the Americas.

The Canadian tar sands alone, in Alberta, are estimated to hold proven reserves of 174 billion barrels of oil. That places this one area of North America, in third place only behind Saudi Arabia and Venezuela. It's safe to say that the West is no longer susceptible to oil blackmail.

How about natural gas?' We've got plenty. According to the EIA, they estimate that we have 2,203 trillion cubic feet of currently recoverable natural gas in this country. We consume approximately 24 Tcf/year; therefore, we have enough to last us 92 years. In fact, we are building liquefied natural gas facilities right now that will be operational by 2015…when we will begin to exporting this commodity.

Back to oil: Here's how our oil stacks up:

**<u>OUTER CONTINENTAL SHELF</u>**

Gulf of Mexico 44.9 billion barrels
Alaska 38.8 billion barrels

**<u>ONSHORE</u>**

Prudhoe Bay (AK) 13.0 billion barrels
Arctic National Wildlife Refuge 10.6 billion barrels
National Petroleum Reserve (AK) 10.6 billion barrels
Bakken Formation (ND & SD) 7.4 billion barrels
Eagle Ford (TX) 3.0 billion barrels

Now comes news that drillers in Utah and Colorado are poking into a massive shale deposit trying to find a way to unlock oil reserves that are so vast they would swamp OPEC.

A recent report by the U.S. Government Accountability Office estimated that if half of the oil bound up in the rock of the Green River Formation could be recovered it would be "equal to the entire world's proven oil reserves." Both the GAO and private industry estimate the amount of oil recoverable to be 3 trillion barrels.

A recent report by the American Petroleum Institute affirms that "each direct job in the oil and natural gas industry supported approximately 2.7 jobs elsewhere in the U.S. economy in 2011,".

Daniel Yergin, a leading energy expert and author of award-winning "The Prize," estimates the U.S. energy boom has generated 1.7 million new jobs, including direct and "induced" employment. He expects the number to double by 2020, the year when the U.S. is expected to surpass Saudi Arabia in oil output and Russia in gas.

**HAVE A GREAT LABOR DAY**

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