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## Democracy in Action

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I am a firm believer in democracy. In this great country, we have a duty to vote to elect our officials. Now, we may not be overjoyed at the candidates we have or the outcome, but in the end it is our responsibility to cast our vote. For president, congress, governor, state legislature, mayor, boards of directors on our investments, etc.

10 days ago, on a Friday night, I came home from work late and found an empty house. No wife and no kids. Rather than looking a gift horse in the mouth, I quickly ate dinner and buried myself on the house for the Yankee game. By 10pm, I became concerned that there was no sign of my family, but that's no unusual as they often hang out with my in-laws.

Just as I dozed off, like Sherman through Atlanta came the wife and kids and little fury thing wagging its tail and jumping all around. For 6 years, I have voted against adopting a dog. We are too busy, too much on the run, love going away. Over the past few years and now months, the kids' cries for a dog have become louder and more persistent. So much so that I had them sign a contract whereby I agreed to a good faith discussion on adopting a dog if they could go 30 consecutive nights without any trouble during the bedtime routine.

What I didn't plan on was my wife jumping ship!

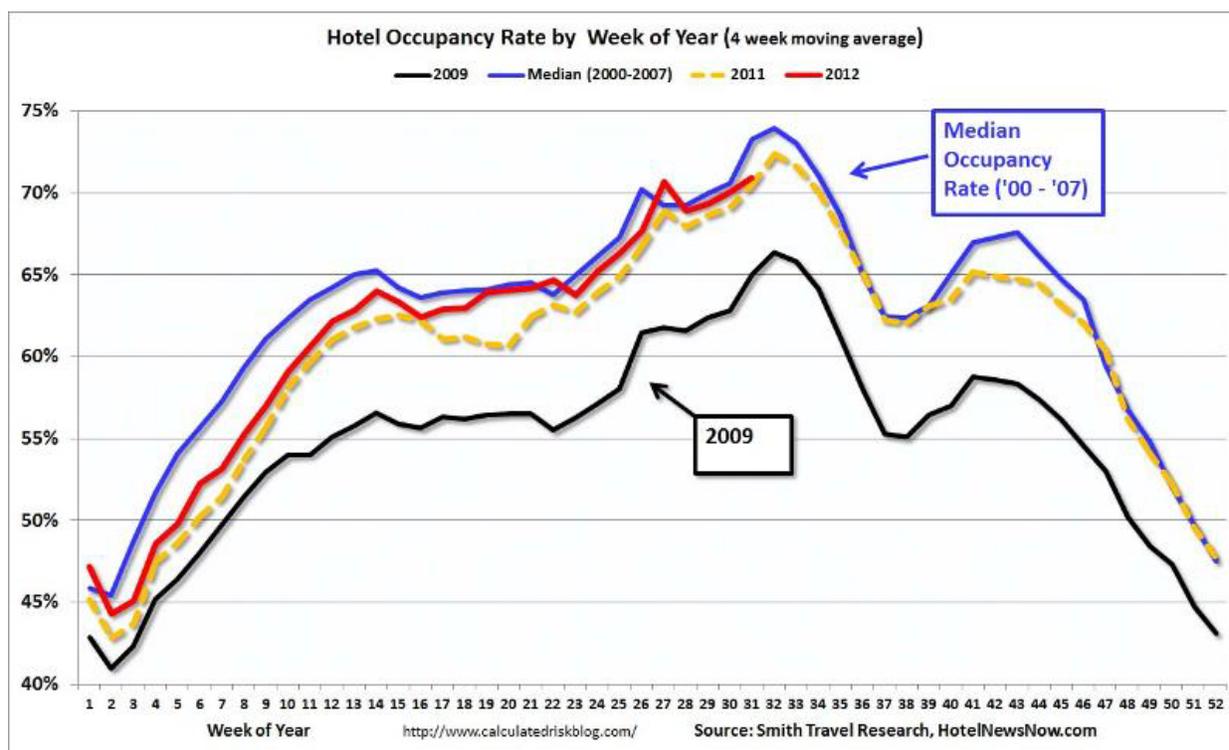
When I asked them why they disobeyed me, they said they took a vote and it was 4-1 with mom in the majority. So now we have this very cute, energetic and lovable puppy named Annie Bailey or Bailey Annie. We're still not sure. And of course, as the lone dissenter, the dog won't leave me alone! So here is the newest member of our family.



Turning to the economy and my love of the non mainstream indicators, below you can see the Hotel Occupancy Rate published by the good folks at Calculated Risk Blog. There are several colored lines, but take a look at the red line, which is 2012. Note how much stronger it is than the black and yellow lines, 2009 and 2011, respectively. In fact, 2012 is close to matching the blue line, which shows a compilation of 2000 - 2007 occupancy rates.

The takeaway from this is that the hotel industry, which is dominated by the business traveler, meetings and conventions, is not showing signs of

cracking beneath the surface. I think part of this is the lack of new construction since 2008 and another part is the reemergence of the business, albeit in a more cost effective manner perhaps.

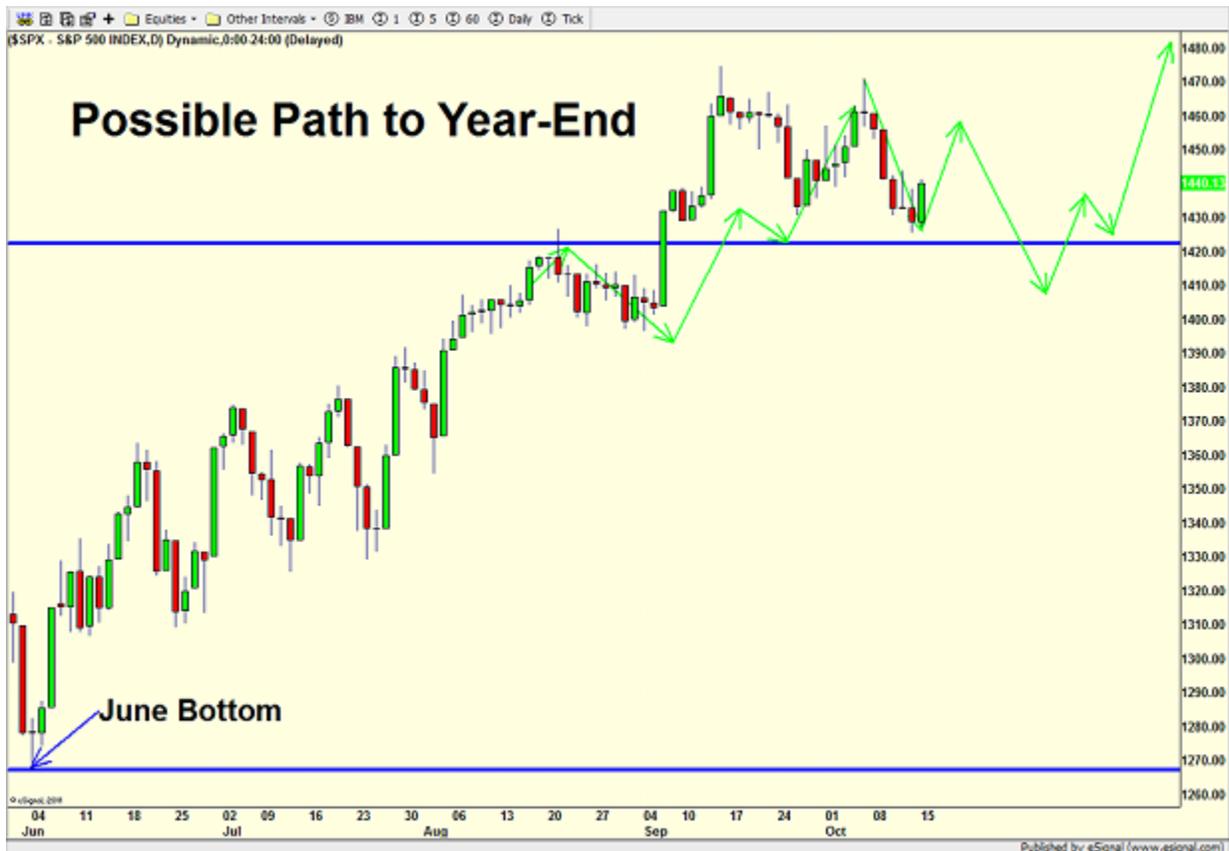


## Election Equals Opportunity

Is the [previous issue](#) of Street\$mart's, I spoke about the intermediate-term positives for the stock market with the S&P 400, Russell 2000, junk bonds and NYSE advance decline line. That article ended with my comment that I expected a 2-8% short-term pullback to shortly. So far, the market has cooperated with a 3.3% decline that does not appear to be over.

However, I do believe that over the coming few days or week, the bulls should make some noise but not exceed the highs we saw in September. From there, we should see stocks decline once again below the levels seen last week into what would be a good bottom and trading opportunity before the election. That all sounds very nice and clean, but the markets have a funny way of teasing and tantalizing us.

I think so few people are prepared to see the stock market establish a low before the election and even fewer would actually buy before knowing the outcome. And that's one of the reasons I think it can happen. We shall see. Below you can graphically see what I just described with a rally, decline and much stronger rally in November into December. IF this is even remotely accurate, the second rally into year-end could be a big one!



Regarding the canaries I wrote about in the previous issue, nothing has changed. The semiconductors and transports continue to behave poorly while high yield bonds and the number of stocks on the NYSE advancing and declining act very, very well.

If you haven't had a good portfolio check up in a while, now is an excellent time! Please call me at 203.389.3553 or reply to this email.

## Conspiracy in the Jobs Report

On October 5, the government released its monthly employment report. Net new jobs came in at a less than stellar 114,000 which doesn't even keep up with the pace of population growth. The previous two anemic reports were revised upwards to show a little better progress, but nothing to write home about.

The shocker came in the actual unemployment number which is the most widely and heavily watched single statistic of the month. It fell from 8.1% to 7.8%. That's a rather large and "curious" drop right in front of the

election. Jack Welch, former CEO of GE during its glory years who knew a thing or two about manipulating numbers, immediately Tweeted "Unbelievable jobs numbers! These Chicago guys will do anything. can't debate so change numbers."

Welch isn't the only one who have questioned the government's accuracy here. There has been all kinds of talk about an Obama conspiracy here to "massage" the numbers in the president's favor. Although I absolutely LOVE conspiracy theories and books and movies, I completely and utterly dismiss this one as nonsense, just like I do that magical clandestine government operation that supposedly covertly manipulates the stock market.

Employment data is incredibly volatile to begin with. That's a fact. There is the business survey and the household survey. That's a fact. The two surveys sometimes diverge for a month or so. That's a fact. There is a formula called the "birth death ratio" (<http://www.investopedia.com/terms/b/birth-death-ratio.asp#axzz28pPjrRev>) that estimates the number of businesses starting and closing. This number is extremely volatile and can even be unreliable as the economy rolls from/to recession. That's also a fact.

The data released on October 5 were an outlier. (and now supposedly confirmed as a technicality that will be averaged out next month) But I fully expect the next two employment reports in November and December to smooth out the rough edges of this report and perhaps give back some of the gains. If this report was released one, two or three quarters or years ago, few would have really questioned it. But since it was so close to the election and the election is all about jobs and the economy, the conspiracy theory sells very well. I just don't buy it...

## **The High Cost of Low Interest Rates**

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With the Federal Reserve now indicating that its policy of low interest rates will continue into 2014, collateral damage is expanding. The impact of low rates is particularly painful for older investors who rely largely on bank deposits and individuals living on fixed income, reducing their purchasing power and eating away at financial security. And it is also contributing to serious underfunding of long-term liabilities.

With interest rates no longer keeping up with inflation, older investors are tapping into their savings at an increasing rate. As savings fall, these investors are reducing consumption, affecting employment at businesses the older savers may once have patronized.

One rationale for low interest rates is to force investors to turn to riskier investments such as funding expansion of the economy. But the pursuit of higher earnings is also resulting in higher levels of fraud. Top 10 lists of investment scams are everywhere including the North American Securities Administrators Association "Top 10" list of investment scams shown below:

1. Investment pools targeting distressed property.
2. Fraudulent energy investments.
3. Fraudulent gold and precious metals offers.
4. Unregistered or fraudulent promissory notes.
5. Securitized life-settlement contracts marketed under the implication of less risk and guaranteed returns.
6. Affinity fraud, i.e. marketing a Ponzi scheme to members of a particular group.
7. Increased use of bogus or exaggerated credentials.
8. Claims of mirror trading investment transactions placed or executed by a skilled and knowledgeable third party.
9. Fraudulent private placements.
10. Advice from unlicensed agents.

Defined benefit pensions plans, such as public employee benefit plans, are particularly vulnerable to underfunding in periods of low interest rates, which undermine the performance of the plan's bond investments. Pension plans base current contributions from the employer on future return expectations. In 2011, California pension fund CalPERS decided to keep its assumed investment return rate at 7.75% to avoid requiring more funding from cash short governments. In March 2012, the pension fund admitted its expectations were a little high and recommended lowering return expectations to 7.25%.

According to the *Sacramento Business Journal*, CalPERS earned 1.1% in the 2011 calendar year and an average annual 5% in the past decade, and 7.5% over the past 20 years.<sup>1</sup> CalPERS isn't alone in failing to meet its return expectations. Without internal earnings, public pension funds will have to turn to government and ultimately taxpayers to meet their obligations to public employees under current contracts. Underfunded corporate pension plans tend to fall on the Pension Benefit Guaranty Corporation, which is also underfunded. According to Credit Suisse, of the 341 companies in the S&P 500 index with defined benefit pension plans, 97% are underfunded today, the *Wall Street Journal* reports.

Underfunding is also reflected in defined contribution plans, such as 401(k) plans. When asked if they felt their employees were saving sufficiently for retirement, only 5% of U.S. businesses replied yes when surveyed in 2011.

Low short-term rates are also encouraging increased borrowing at short maturities, raising the risk that when it comes time to refinance, increased

interest rate costs may prove beyond the borrower's capability. The U.S. government is squarely in this crowd. The U.S. Treasury currently has \$10.7 trillion in outstanding publicly-held debt on which it pays an average interest rate of 2.24%. More than \$5 trillion falls due within the next 36 months. If this debt is refinanced at the historical average of 5%, interest costs will more than double to in excess of \$535 billion, twice CBO's projection for total federal spending on Medicaid this year, reports the Wall Street Journal.<sup>2</sup>

And lastly, the tools used by the Federal Reserve to keep interest rates artificially low have the potential to increase inflation, further eroding investment portfolios and increasing costs across the board.

The unintended consequences of the Federal Reserve's focus on stimulating the economy through record low interest rates may be imposing a long term costs far greater than any short term benefits. Time will tell.

1 "CalPERS may lower assumed rate of return," *Sacramento Business Journal* by Mark Anderson, Wednesday, March 7, 2012.  
[http://www.bizjournals.com/sacramento/news/2012/03/07/calpers-may-lower-assumed-rate-of-return.html?ed=2012-03-07&s=article\\_du&ana=e\\_du\\_pub](http://www.bizjournals.com/sacramento/news/2012/03/07/calpers-may-lower-assumed-rate-of-return.html?ed=2012-03-07&s=article_du&ana=e_du_pub)

2 "Uncle Sam's Teaser Rate - Low interest rates disguise the federal debt bomb." *Wall Street Journal*, March 12, 2012.

## Upcoming Appearances

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Yahoo Finance's Breakout - [Bull Markets Die Hard](#)

Real Life Survival Guide - October 28 at 4:30pm WNPR Radio

Fox Business' Markets Now - October 12th at 1:30pm

Global Market Summit - November 29 in New York

You can view most of the past segments by clicking below.

## [Media Appearances](#)

(<http://www.investfortomorrow.com/InMedia.asp>)

## Investment Quotes/Adages To Live By

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"The only easy day was yesterday."

- The U.S. Marines

"When in doubt, get out!"

"If it's obvious, it's obviously wrong."

-Joe Granville

"It's ok to be wrong, but it's not ok to stay wrong."

"This time is different."

"The markets require the patience of a dozen men."

-Robert Rhea

"Luck is the residue of effort."

"The most bullish thing a market can do is go up in the face of bad news."

"The most bearish thing a market can do is go down in the face of good news."

"The market can stay irrational longer than you can stay solvent."

-John Maynard Keynes

"Government is best which governs least" - Thomas Jefferson

Inflation is the one form of taxation that can be imposed without legislation.

-Milton Friedman

"You cannot legislate the poor into freedom by legislating the wealthy out of freedom. What one person receives without working for, another person must work for without receiving. The government cannot give to anybody anything that the government does not first take from somebody else. When half of the people get the idea that they do not have to work because the other half is going to take care of them, and when the other half gets the idea that it does no good to work because somebody else is going to get what they work for, that my dear friend, is about the end of any nation. You cannot multiply wealth by dividing it." -

Dr. Adrian Rogers, 1931

"Bear markets seem to be divided into three phases: the first being the abandonment of hopes upon which the final uprush of the preceding bull market was predicted; the second, the reflection of decreased earnings power and reduction of dividends, and the third representing distressed liquidation of securities which must be sold to meet living expenses. Each of these phases seems to be divided by a secondary reaction which is often erroneously assumed to be the beginning of a bull market."

- Robert Rhea via Tim Woods

"Free enterprise is a rough and competitive game. Nobody too big to fail. Nobody too small to succeed. It is a hell of a lot better than government control." - Ronald Reagan via Dan Kennedy

"A government big enough to give you everything you want is big enough to take everything you have." - Gerald Ford via Dan Kennedy

"The problem with socialism is that, sooner or later, you run out of other people's money." - Margaret Thatcher

"Diversification alone is no longer sufficient to temper risk... You need something more to manage risk well."

- Mohamed El-Erian

## **Friends And Family Plan**

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Finally, as you know, our firm and this newsletter continues to grow mostly from your referrals. If you know anyone who is interested in securing their retirement, planning for it or just plain worried about it, please send them here. As always, thanks for thinking of us with your circle of family and friends.

**[Sign Up Here](#)**

You can also forward this email to family and friends by hitting the "forward email" hotlink at the bottom of this email.

## To Your Financial Success,



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