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**MONEY PLANS  
ECONOMIC  
REPORT  
(Summer 2010)**

**ECONOMIC OVERVIEW**

**U.S. Economy**

The year started on a positive note, as stocks turned in one of the strongest first quarter increases on record. And then the second quarter came and everything changed. Our last newsletter pointed out that the VIX (an index which measures investor fear) was extremely low, indicating little fear in the market. Since the market tries to fool investors into complacency, we suspected a correction was nearing. In just weeks, the market lost over 10%.

For the 6 months of 2010, the DJIA lost (6.3%), the NASDAQ lost (7%), the S&P lost (7.6%), gold gained 13.4%, and international markets measured by MSCI EAFE lost (15.9%). CD's and money market yields averaged .25% and bonds measured by the Barclays Capital Aggregate Bond Index gained 3.9%. A diversified portfolio's return is a blend of these numbers, depending on how risk adverse or how aggressive the portfolio. These numbers are gross returns (enclosed statements are net returns) and assume that all monies remained invested for the full twelve months of the year.

After 2008's sharp decline and last year's recovery in stock markets, many had hoped that 2010 would see a return to relative normalcy and stability: The year started off strong-- helping investors feel secure. Investment statements were showing improvement-- and investors were once again willing to put money into the market. Then, from almost nowhere and in rapid succession-- came five major events that were just too much for the market to handle:

- The intensification of the budget crisis in Greece that arose in February, with the risk of contagion across Europe;
- Concerns that European budget cuts would slow down economies, with spillover effects globally; especially problematic in light of the need to compete with a devalued euro;
- Growing fears about a housing bubble in China;
- The April 22 sinking of a BP oil drilling rig in the Gulf of Mexico; and
- The May 6 "flash crash" in which US markets plummeted in a matter of minutes without explanation.

Within three months from when the above occurred, the market, which had regained nearly 80% of what was lost during the great recession of 2008, gave nearly half back.

Looking at these events, it's tempting to ask what the next catastrophe will be. History books are referring to this last decade for stock returns as the "the lost decade" and "the calamitous decade" as stock market returns

haven't been able to get out of negative territory over the last ten years. With the government running huge deficits, we believe the stock market will continue to face huge hurdles for years to come.

When we look at GDP to US entitlement spending we can easily see where the problems lie on the horizon. US commitment to entitlements (mainly to Medicare and Social Security) is around \$62.3 trillion while GDP (Gross Domestic Product) is around \$14 trillion dollars. In other words, our commitments well exceed the value of our economy's output. To further illustrate this imbalance: in less than ten years entitlements have grown by 138% while GDP grew at 30%. At this rate, in about ten years, the US will be insolvent – yes, just like Greece!

This alone is inflationary, but—ironically-- the timing for this explosive imbalance couldn't be better. The huge debt crisis came at the same time economies around the world had entered into a recession. This has enabled the US to keep interest rates low as investors around the world fled to the safety of US Treasuries. And with the Euro in trouble, China, the largest borrower of US debt could no longer threaten to sell its stake in US Treasuries. In essence, China had no where to run. So, everyone fleeing to US Treasuries has kept interest rates at rock bottom levels. Rest assured though, at some point, the winds will change and the US will need to get out of its debt problems.

Jeff Gundlach, chief investment officer of DoubleLine, an investment firm for mortgage backed securities, commented in his keynote speech at a recent Morningstar Investor Conference that the US will need to

print more dollars but nonetheless at some point he expects the US to renege on some of its debt or entitlement obligations. He sees that happening by the US imposing higher taxes and also cutting back on entitlements. "That would be a way of engineering a default in a creative way," he said. We agree with him completely. And we also agree with his concluding remarks:

**"At some points something bad could happen relative to risk, causing the dollar to drop and Treasury yields to rise. You need to sell immediately, because you don't have much time, you have to sell very, very quickly."**

In other words, once US Treasuries are no longer considered a safe haven, investors will flee.

### **What We Are Doing**

Our top priority is to make sure your investment portfolios are managed according to your needs. We are adjusting asset allocation as your cash and income needs change, we are helping you make sound financial decisions, we are assuring that your retirement account distributions are up to date, we are employing tax advantaged strategies, and we are using cost effective investments to minimize overall investment expenses.

We are currently buying short to medium term lower end investor grade bonds. The yields on these bonds are nearly three times that of US Treasuries and carry less risk on a valuation basis. As everyone rushed to buy US Treasuries, the value of those bonds reached extraordinary prices when compared to corporate bonds.

We continue to buy dividend paying stocks as yields have reached 3 to 7% on high quality companies. We are concerned that dividends may be taxed as high as 40% for higher income taxpayers when, as the current administration stated that it will allow, the Bush tax cuts to expire at the end of this year. Nevertheless, we still think dividend paying stocks offer value. As retirees look for ways to supplement income, we believe that dividend paying stocks will be in demand, causing these stocks to appreciate faster than non-dividend paying stocks.

We continue to buy gold and silver as a hedge against market and political uncertainty. While we are buyers, we are being cautious as these metals have risen very fast.

We are also investing for short term gains by using the VIX as our guide. When the VIX gets as high as 35-- indicating fear in the market, we will buy an index fund that represents the overall market. When the VIX gets below 20, we will sell that index in anticipation that the market will go down. The VIX is a good index to determine entry and exit points. We will use a similar strategy using inverse funds.

While all the above strategies help to reduce volatility and limit losses, no strategy is perfect in an imperfect world. Investments are only one strategy for getting to a secured future. In addition, it's necessary to have adequate insurance coverage, such as appropriate life and disability coverage and long term care insurance.

**When the market is as rough as it is, having the right amount and types of insurance policies becomes even more necessary.**

## **Receiving Social Security Benefits While Working**

Just because you reached your full retirement age (which is now 66) doesn't mean you have to retire. If you enjoy your work but wish you had extra income to enjoy life while your health is still good, you can work and still receive your full Social Security benefit payment without regard to your earnings. Or, if you are divorced, then in some cases it makes sense to draw on your ex-husband's account, but wait to take your own benefit until you are older.

Now let's say you are 62 and just retired from your job and started taking Social Security benefits. You decide to pick up some part time work for extra income. Now let's say you enjoy the part time work and want to work more hours, but the extra earnings will exceed the exempt amount (the amount you can receive before your benefits are reduced—by \$1 for every \$3 above \$14,160 for 2010). If Social Security withholds some of your benefits because you continue to work, then after you reach full retirement age, Social Security will recalculate your benefit amount to give you credit for any months in which you did not receive some benefit because of your earnings. Of course, this benefit will not be as high as it would have been if you had waited until 66 to start receiving your Social Security benefit.

**Speaking of Social Security**—did you know that you can apply for your benefits on line? It is a very efficient and user-friendly process. But should you apply on line? Yes—but...as the above discussion has illustrated, the questions to be considered—about when to apply and on what account-- are not nearly as straight forward. In fact, these decisions require focused thought and analysis.

## **Watch Out Taxes Are Going Up!**

The Obama Administration has stated that it will allow the Bush Tax Cuts to expire the end of this year. What this means is that EVERYONE will pay higher income taxes, not just the tiny percentage of rich folks. The current six brackets of 10%, 15%, 25% 28%, 33% and 35% will be replaced with five higher brackets: 15%, 28%, 31%, 36% and 39.6%. And taxes will be still higher because there will be higher taxes on dividends and capital gains, return of phase-out for itemized deductions regarding mortgage interest and charitable donations and personal exemptions, and the return of the marriage penalty. Higher taxes will make saving a bit harder for everyone.

## **Money Plans is Recognized**

Money Plans has been included in the 2010 **Financial Advisor** Top RIA Ranking! (RIA - Registered Investment Advisor)

**Financial Advisor** states that "This is a coveted honor and a true testament to your firm's accomplishment and success this past year."

"Being a part of this ranking further establishes your firm's credibility and heightens your presence as an RIA firm".

## **EMAIL ADDRESSES**

We ask that all clients provide an email address so we can get out timely information. Send your email address to [deniseleish@moneyplans.com](mailto:deniseleish@moneyplans.com). **Please visit us at [www.moneyplans.com](http://www.moneyplans.com).**

## **Quarterly Statements**

If we are managing your investments, you will find a personalized report:

The "Position Performance Summary Report" which shows your performance for the period 12/31/09 through 06/30/10 (six months of 2010). The net flow column when positive shows monies used to purchase new investments after 12/31/2009 and a negative means monies flowing from the investment into the money market account either from the sale of an investment after 12/31/2009 or from a dividend payment.

A positive or negative in the net flow column for cash/money market means that money flowed in or out of your money market, i.e., money flowing in from the sale of a security, money flowing out for investment purchases, management fees, etc.

**The Actual IRR Column is a percentage change net of fees (after Money Plans fees and all trading costs) and discounts all cash flows.**

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Our ADV Part II and Code of Ethics are available upon request.

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