2013 FEBRUARY NEWSLETTER

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Happy New Year

In the last newsletter in September 2013 I characterized the Economy as the …

‘THE GREAT STALLED RECOVERY’

And soberly forecast a very slow to flat National economy for the second half of 2012. And unfortunately, I was accurate in that forecast.

So what happens now ??

Well, the bottom line, the next six months, slow, slow, slow improvement. Improving but way below normal.

The word that comes to mind is **'SLUMP'**

- ✓ A slump for a baseball player is a 'bad batting average' for a season.
- ✓ A slump for a person is a bad and drooping posture.

BUT

For an Economy … a 'SLUMP' is an extended period of below normal performance.

THE 'RECOVERY' IS OVER … AND …
THE GOOD NEWS IS … we are in a slump … AND …
THE BAD NEWS IS … we are in a slump

The Economy may not be growing at a normal pace, but (and this is a big **but**) it is **<u>not</u>** getting worse !! This is the best news !!

The general Economy is slowly getting stronger as the natural business cycle marches on. Eventually, shoes wear out and cars break down.

People and companies, over time, pay down debt, spend less, save and invest and generally improve their financial situation.

More people with more 'wants' promote the need for more productivity. It is a time of change. Inventing and re-inventing … new opportunities.
Hence, the Economy gets better by itself over time.

In the meantime, settle in for a **slowly** improving world and think about how to adapt … to the SLUMP.

What do the 'crystal ball indicators' indicate ??

The 20 common indicators used to measure the Economy, indicate the Economy is slightly improving Slow and frustrating.

In the last six months of the 20 indicators used the indicators indicated:

ROUGHLY POSITIVE … 7 … 35%

ROUGHLY NEGATIVE … 3 … 15%

BASICALLY NO CHANGE … 10 … 50%

TOTAL INDICATORS: 20

<u>Some indicators have slightly improved</u>:

✓ The unemployment rate has thankfully dropped from 8.2% to 7.8% … not much of an improvement … but we will take it

✓ Consumer confidence improved from a measure of 63 to 72 … not bad

✓ The inflation rate has stayed around 2% … fairly benign … this is good

✓ And auto sales have been steadily improving … go Ford Motor !

Some indicators have become slightly worse:

- ✓ The Dow Jones Stock Average dropped from 13,008 to 12,938 … not much of a decrease … but more importantly … NO increase.

- ✓ The number of people getting jobs has averaged 130,000 to 160,000 per month … this is good … (but don't get too excited … at that pace it will take roughly 8 years to get jobs for today's 12.2 million unemployed).

- ✓ The 10 year Treasury Bond … a major factor in determining interest rates … has been slowly trending a little higher in the last six months ...

Some indicators seem to stay about the same:

- ✓ Oil prices went up … went down … went up … went down …

- ✓ The business confidence index has been flat at about 50 for the last seven months … no change.

- ✓ Retail sales went up a little but seem to be leveling off at about $412 billion … not very encouraging for the retail industry.

Why do we think we are in a slump?

Well, here's the math.

In the 70 years, from 1930 to 2000 the average annual growth rate was **3.9%.**

Average Annual Growth Rate

1930 to 1969 4.4% … For 40 years
1970 to 1999 3.3% … For 30 years
2000 to 2011 1.8% … For the last 10 years ? Huh ?

the long-term math does not look good …

Fact 1

The long-term average growth rate in America has been steadily decreasing since 1930!

IF WE USE A 10 YEAR AVERAGE

SINCE 1945, THE END OF WW II, THE GROWTH RATE HAS BEEN CONSISTENTLY GOING DOWN !!

- ☛ From 6% in 1945
- ☛ to 4.4% (by the end of the 60s)
- ☛ to 3.4%.(by the end of the 90s)
- ☛ to 1.6% !! FOR THE TEN YEARS ENDED IN 2010 !!

WHAT !?!?!?!

This is **significantly** less than the **70 YEAR** historical average of **3.9%**. In fact, it is **60%** less.

Decade	**Growth Rate**
1950 to 1959	Slowed by 27%
1960 to 1969	basically was flat - no change
1970 to 1979	slowed by 24%
1980 to 1989	slowed by 8%
1990 to 1999	improved by 8%
2000 to 2009	**slowed by 53%**

AND WHY IS THIS HAPPENING ?

WHAT FACTORS IN OUR LIFETIME ARE CAUSING THIS LONG TERM DECLINE IN THE GROWTH RATE OF AMERICA ??

What do you think ?

? Change in the demographics of America i.e. the 'BOOMER GENERATION' and its effect on the Economy.

? Increase in the size of government spending and debt (as an amount of our total productivity on all levels Local, State and Federal).

? The long-term increase in government regulations in America and its effect on private sector productivity.

? The effect of 'globalization' on the competitiveness of America and its ability to sell its products to the World.

? The decline in the educational standards of America and it's consequent effect on our productivity.

? The change in our cultural values. Breakdown of the family unit, children out-of-wedlock, hard work not so appreciated, increased drug use, just plain laziness, entitlement mentality, et cetera.

WHY DOES THIS MATTER TO YOU ??

BECAUSE YOU MAY BE LIVING IN A WORLD OF DECLINING STANDARD OF LIVING.

HOW WILL THIS IMPACT YOUR LIFE ?

HOW ABOUT:

- Higher taxes.
- Higher crime rates.
- Increased societal stress including violent street demonstrations.
- More governmental involvement in your life.
- More threats on the World stage as America's economic power is reduced.
- Etc.

AND now the big question ??

If we do enter a slump. How long will it last? When is it over ?
When do we get to grow again ?

WELL, THE GOOD NEWS IS THE ECONOMY IS CYCLICAL.

YES … history does repeat, and historical and financial cycles do happen.

For example, WOULD YOU BELIEVE 250 YEARS AGO?

After spending six years in London, a man returned to Philadelphia and was shocked at the housing prices. "The expense of living has greatly advanced in my absence,' he commented. "Rents of old houses and value of lands have trebled in the past six years". The man who said this in 1762 was Benjamin Franklin. He had come home to a real estate bubble, which collapsed in 1763, bringing on a credit crunch and a deep recession that was the economic backdrop to the American Revolution.

Will 'THE GREAT STALLED RECOVERY' become

'THE GREAT SLUMP' ?

THE GOOD NEWS

Ta …ta … ta *drum roll* here is the good news (you know, glass half-full stuff).

In the Manufacturing Sector

→ 27 months of modest, but steady expansion
→ In the last year added $1.7 trillion to the U.S. Economy. Up 6.6% over the previous year (the rest of the economy grew by 2.2%)
→ The U.S. continues to lead the world in manufacturing, commanding 20% of global manufacturing
→ Boeing unveiled the future of aviation with the 787 Dreamliner and announced the largest orders ever.
→ The auto industry, the largest manufacturing sector, is rapidly recovering with a sales pace above 15 million vehicles. (not seen since 2007)
→ The U.S. makes great products with some of the greatest manufacturers; Ford Auto, Caterpillar, Intel, Harley Davidson, Hewlett Packard, Google, Apple … etc … etc …

In the Housing Sector

→ Prices in most markets are now rising
→ New home sales volume up 20%+ from last year
→ There is only 4.5 months of inventory on the market (the lowest level in 7 years)
→ The median price of a new home in September 2012 … $242,400. The median price of a new home in September 2011 … $217,000. Up 10.3%

In the Financial Sector

→ Interest rates continue to stay at historically low levels
→ The Federal Reserve has confirmed its commitment to a zero-rate policy through mid-2015 … keeping interest rates low

In the Corporate Sector

→ Corporate balance sheets are very strong with cash of $1.5 trillion
→ This is the largest amount of available cash in history
→ More than half of the companies in the S&P 500 met their earnings estimates … corporations are still maintaining their profit levels

In the Energy Sector

→ The U.S. is experiencing an energy boom on private lands
→ Domestic oil and gas production has increased dramatically which has lowered energy prices
→ The new hydraulic fracturing technology has opened up vast new sources of natural gas

production (driving down prices)
→ We now have the lowest energy costs in the developed world … which is helping to lead to the steady expansion and resurgence of U.S. manufacturing
→ The International Energy Agency reported the U.S. oil output is poised to surpass Saudi Arabia in the next decade. This year the U.S. produced the most oil since 1991 while crude oil imports have fallen 11% this year

In the Governmental Sector

→ The fiscal health of 48 of the 50 Sate's has improved dramatically as steps were taken to address budget deficits
→ State tax revenues increased 3.2% from a year ago and have been rising steadily for 2.5 years

(I am sorry to say that California and Illinois are the only two States that have not got their act together … still)

In the Miscellaneous Sector

→ We have not yet been invaded by Martians and
→ Christmas came again this year … HO HO HO !!!

RENTER NATION

In 2004 America reached the historical peak of home ownership

- ✓ 69.4% of Americans owned a home
- ✓ 30.6% of Americans were renters

By 2012 America had reached the lowest level of home ownership since 1997

- ✓ 65.5% of Americans owned a home
- ✓ 34.5% of Americans were renters

In the 8 years since 2004

- ✓ Home ownership dropped by 5.6%
- ✓ And 6.5 million more households are renting

*At the current pace by **2015**, the home ownership rate is likely to fall to the **1993** level of **64%***

And the future ??

Will more Americans be renting ??

What do you think ? Well here's the facts ...

(A) The current economic **'SLUMP'** will bring slow growth in jobs and wages and hence less ability for households to purchase homes.

(B) Continued tight lending standards by the banks, Fannie Mae and Freddie Mac will make loan qualifying for home ownership difficult … to impossible for many people (especially for young adults).

(C) A dramatic increase in the number of Americans in some form of long- term assistance from the government; unemployment benefits, disability payments, Section 8 housing assistance, food stamps, college Pell grants etcetera. This does not encourage productivity. Keeping standard of living low and hence more renting, less ownership.

(D) And the <u>demographic trend</u> is working against home ownership and is working in favor of Renter Nation.

Demographics ?

Here is a general breakdown of our American population for 60 years.

Generation	Years Born	Population	Duration
The Baby Boomers	1941 to 1957	75 million	17 years
The Bay Bust - Gen X	1958 to 1977	74 million	20 years
Echo Boomers - Gen Y	1978 to 2001	80 million	24 years

Imbalances will be created with the expanding and contracting of the size of different populations through different generations and years. This expanding and contracting, combined with generational cultural differences, will determine the ratio between renting and home ownership during a specific period of time in history.

So here is what is going on now …

There are now more people aged 15 to 29 … than 30 to 44.

There are now less people aged 30 to 44 … than 45 to 59.

In other words, the 30 to 44 age group is the small guy on the scale.

And young people under 30 have the lowest percentage of home ownership and this group is getting bigger.

Makes sense. They're just getting started in life. Getting their first jobs. Out on their own for the first time. Developing a credit history. You know, not quite ready to buy a house.

A key factor in home ownership is household formation; getting married, having kids, dogs and cats, kitchen table etc.

BUT, between 1960 to 2010, the share of young adults (18-29) who got married fell from 59% to 20% … AND … not surprisingly … the decade from 2000-2010 saw the slowest household growth in U.S. history.

And a decline in marriage means less household formation which means less home ownership and renting for a longer period of time.

And this ECHO BOOMER generation is handicapped (by high student debt), fewer job opportunities and lower pay and an unusual slow growth economy which all leads to delaying marriage, delaying children and delaying home purchases.

And again, this leads to longer periods of renting for today's young adults.

THIS YEAR 100 YEARS AGO - 1913

A REALLY BIG financial and economic YEAR !!

Could the people in January of 1913 have imagined the huge financial and economic changes to come in the next year ??

Only **100** years ago, during that year of **1913** …

☛ **Henry Ford established the first moving assembly line.** Amazingly, it allowed an automobile to be built in three hours !!!! And he astounded the business world by announcing that he will pay his employees a minimum wage of $5 a day ! Not bad (considering New Jersey just set the minimum wage for women at $9 per week !)

☛ **The Panama Canal was opened**. Joining the waters of the Atlantic and Pacific Oceans and opening the two oceans to new commerce and shipping possibilities (and of course cruise ships).

☛ **Hollywood becomes the world film center !!** Cecil B. DeMille founded a film mecca in Hollywood, joined by film producers fleeing New York and New Jersey and Charlie Chaplin made his film debut in 'Making a Living'.

☛ **The New York Grand Central Terminal** opened connecting trains for daily commuters to New York City and trains throughout the East Coast.

☛ And on June 5, **China opens a bank in New York City**.

BUT THE BIG FINANCIAL NEWS FOR 1913 Was ...

On December 23, 1913, the Federal Reserve Banking System was signed into law by Woodrow Wilson. The first Democrat president, with the consent of the first democratically controlled Senate and House. America now had a Centralized banking system … Merry Christmas ##!?

AND THE BIGGEST FINANCIAL NEWS THIS WAS THE YEAR

ON OCTOBER 31, 1913

THE INCOME TAX CODE OF THE UNITED STATES COMES INTO EFFECT

THE INTERNAL REVENUE SERVICE BEGINS !!!!

Would you believe the original IRS Form was 1 … yes … 1 page?
Today there are 1,000 forms ?? (What the hell for ??)
And back then there was 14 pages of law.
Today, the IRS Code regulations, tax court cases etc. is **72,000** pages.
WOW now that's a growth business.

Let's see that's …

- **7,200** new pages of tax bull a year !
- **20** new pages **a day** every day for 100 years !!
- And **10** new forms a year

Unfortunately, we the people, have to keep up on this reading !!!! Unfortunately, we the people are on the receiving end of this growth ##!!

So WHAT IS GOING TO HAPPEN TO OUR FINANCIAL HISTORY IN 2013 ??

And how silly has our Income Tax System become ?

280E – No deduction is allowed for expenses incurred in trafficking in controlled substances. (i.e. selling drugs, duh)

276 – Indirect Contributions to Political Parties. No deduction is allowed for the cost of admission to an Inaugural Ball (Aww, now that's too bad).

276(b) – But, to help clear things up and I quote specifically from the Code;

276(b) Definitions

For purposes of this section – (1) Political Party – The term "political party" means –

(A) a political party:
(B) a National, State, or local committee of a political party.

(Now wasn't that helpful ? What ? You have to wonder who writes this stuff).

And if you were wondering and confused about how to go about 'living', well do not fret the IRS has defined how to live.

Section 7702B (c)(2)(B) Activities of Daily Living –

Each of the following is an activity of daily living:

(i) Eating.

(ii)Toileting.

(iv) Bathing.

(v) Dressing.

(Now don't you feel better that you have that cleared up !)

25A(f)(1)(B) – if part of a degree program under Section 25A, 'Hope and Lifetime Earnings Credits' expenses for sports, games or hobbies are deductible as 'qualified tuition and related expenses' (No Comment)

And don't fool with the IRS.
Section 6702 … charges a $5000 penalty for a 'frivolous tax submission'

And on the other extreme see if you can get through this definition (dare you to read it twice). In fact let's see if you can get through it once.

Per Regulation Section 1.704;

Member Nonrecourse Debt Minimum Gain Chargeback. If there is a net decrease in Member Nonrecourse Debt Minimum Gain during a fiscal year, any Member with a share of the Member Nonrecourse Debt Minimum Gain attributable to such Member Nonrecourse Debt as of the beginning of such fiscal year shall be allocated items of Company income and gain for such year and if necessary, subsequent years, equal to that Member's share of the net decrease in Member Nonrecourse Debt Minimum Gain. A Member's share of net decrease in Member Nonrecourse Debt Minimum Gain shall be determined pursuant to Reg Section 1.704-2(g)(2). A Member shall not be subject to the foregoing chargeback to the extent permitted under Reg Section 1.704-2(i)(4).

Now is **that** clear? Of course not. How did we get a tax system this complicated? And consequently expensive !!!! It's expensive to be complicated and we the people do it to ourselves ?