MIKE CHADWICK'S

MONEY MATTERS

ADVISING, EDUCATING & INSPIRING YOU TO A BETTER LIFE

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Lower Returns are Better?

Most folks would have to ask if you were feeling alright if you advocated lower returns on your investment portfolio. In our society of quick fixes, everyone is searching for the magic pill that you can swallow and eliminate all of your worries. As we all know, no such pill exists, but the media has been pushing hard that the simple answer is to simply buy a "low-cost" index fund or target maturity date account and blindly and let it go to work.

If you are looking for long-term total returns and don't plan on touching your capital for a long time, then the highest return is indeed the best way to go. If you need to use your money systematically – to pay for college, retirement or any other periodic payments - then consistency in returns is much more important than actual total overall returns.

Let's think about the math of gains and losses. If you invest $1,000,000 and lose half, you now have $500,000. That's a 50% loss. ☹ I hope that never happens to you, but unfortunately I've met hundreds of families that experienced this degree of decimation in their portfolios from 1999 – 2002. If you are going to need your money soon or are using it now, that is a deal breaker – life as you know it just evaporated.

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INSIDE THIS ISSUE

China Shop Bulls

Bull markets are considered good – asset values are going up and investors feel warm and fuzzy as the confident bull rushes upward and onward. Bear markets are considered bad – wealth quickly dissipates as values are struck down as the bear conquers his opponent.

Bulls and Bears are neither good nor bad – yes let me repeat that – neither market is good nor bad, it just is what it is. We can make money in either market environment and the market itself isn't what is at issue. The issue is what investments are available for purchase and how much you are you required to pay to own them. In China we've clearly had a lot of Bulls on the trading floors for the past few years.

In the late 1990's and early 2000's the valuations of stocks in American stock exchanges were out of control. Federal Reserve Chairman Alan Greenspan pleaded with investors to watch out for what he called "irrational exuberance" quickly driving equity prices unsustainably higher.

In China today we see a very similar situation. On February 27th the Chinese stock market lost almost 10% of its value overnight, sending shock waves to stock markets around the world. Investors were without question very nervous of the day's events and worried about things to come. A few days later most countries' markets regained that day's losses and have since made a lot of new record highs.

The China thing happened again on June 4th. Shanghai lost about 8% that night and 15% in the four trading days leading up to it, but the reaction around the world was very different this time. In Europe the markets were up or down less than 1% on the China news, Asian markets were all up except India & Sri Lanka, both

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Lower is Better *Continued from page 1,*

There are circumstances where lower returns actually provide you with more money over the long-term as you consume the asset. We're going to illustrate one of those scenarios here. I am going to compare the performance of a mutual fund called the American Mutual Fund (AMF) to the performance of the S&P 500 index from 1/1/70 – 12/31/99 (before the stock market meltdown). AMF had an annualized return of 13.43% and the S&P 500 had an annualized return of 13.72% in this period. My 5 year old knows bigger is better, right? Not always and not this time! Here is the compounding of the money over time in the two investments assuming you never touched the money.

Year End	AMF	S&P500
1970	$ 105,083	$ 103,948
1971	$ 119,485	$ 118,813
1972	$ 132,851	$ 141,382
1973	$ 118,643	$ 120,614
1974	$ 99,743	$ 88,691
1975	$ 134,796	$ 121,709
1976	$ 180,957	$ 150,830
1977	$ 184,488	$ 140,035
1978	$ 207,888	$ 149,236
1979	$ 252,676	$ 177,008
1980	$ 316,743	$ 234,451
1981	$ 341,491	$ 222,909
1982	$ 444,076	$ 270,938
1983	$ 551,283	$ 332,049
1984	$ 568,298	$ 352,880
1985	$ 765,640	$ 464,838
1986	$ 907,651	$ 551,600
1987	$ 947,779	$ 580,562
1988	$1,069,566	$ 676,718
1989	$1,339,674	$ 890,774
1990	$1,317,939	$ 863,082
1991	$1,604,215	$1,125,458
1992	$1,729,888	$1,211,086
1993	$1,976,945	$1,332,883
1994	$1,983,557	$1,350,412
1995	$2,606,024	$1,857,272
1996	$3,028,648	$2,283,406
1997	$3,828,002	$3,044,946
1998	$4,393,133	$3,915,053
1999	$4,387,983	$4,738,717

It appears to be a no-brainer: the higher return wins hands down, right! Not so quickly. Notice I stopped this comparison in 1999. If we continued to today the results would have flip-flopped: there would be much more money in AMF because the S&P 500 lost 45% during 2000-2002. Let's keep it here, when the market was at its strongest point at the end of the best bull market in recent memory to stack the deck in favor of the index. Now let's take the same exact portfolio over the same exact time frame and make withdrawals to spend in retirement. We'll start by taking 5% of the portfolio value as withdrawals and increase those withdrawals by 5% annually. Here is the cash flow and growth of the capital as the annual withdrawals take place:

Year	Withdrawal	AMF	S&P 500
1970	$ 5,000	$ 99,327	$ 98,240
1971	$ 5,250	$ 107,444	$ 196,744
1972	$ 5,513	$ 113,545	$ 120,955
1973	$ 5,788	$ 95,633	$ 97,812
1974	$ 6,978	$ 74,825	$ 66,669
1975	$ 6,381	$ 94,219	$ 84,658
1976	$ 6,700	$ 118,973	$ 97,663
1977	$ 7,036	$ 114,058	$ 83,705
1978	$ 7,387	$ 120,822	$ 81,588
1979	$ 7,757	$ 138,360	$ 88,390
1980	$ 8,144	$ 164,118	$ 107,436
1981	$ 8,552	$ 168,159	$ 93,734
1982	$ 8,979	$ 207,604	$ 102,902
1983	$ 9,428	$ 247,591	$ 116,167
1984	$ 9,900	$ 252,575	$ 112,831
1985	$10,395	$ 317,806	$ 136,551
1986	$10,914	$ 365,252	$ 150,576
1987	$11,460	$ 370,644	$ 148,400
1988	$12,033	$ 405,723	$ 160,111
1989	$12,635	$ 494,291	$ 196,536
1990	$13,266	$ 472,883	$ 177,119
1991	$13,930	$ 560,211	$ 215,148
1992	$14,626	$ 588,743	$ 215,954
1993	$15,358	$ 656,693	$ 221,569
1994	$16,126	$ 642,785	$ 208,190
1995	$16,932	$ 825,154	$ 266,700
1996	$17,778	$ 939,513	$ 307,847
1997	$18,667	$1,166,541	$ 389,384
1998	$19,601	$1,317,600	$ 478,077
1999	$20,581	$1,296,113	$ 555,551

Think about it. For this comparison we've 'stacked the deck' in favor of the S&P500 index because we stopped the comparison before the 2000-2002 market meltdown. So even while this example shows withdrawals of principal and interest, the consistency of returns of AMF year over year was indeed much more important to your bottom line than the overall return posted by the S&P500. Similarly, as we illustrated in last month's newsletter, the very order of returns year to year has a mind-boggling effect on overall financial security (or insecurity depending on what side of the fence you reside). So it is critical that you avoid substantial losses in any year.

Many of you with relatively conservative portfolios are currently feeling frustrated that your portfolios are not 'beating' the stock indexes which have recently set record highs. Please understand these portfolios are not meant to beat the indexes in any one year: they are meant to provide you with a reliable source of asset growth and long-term income without you having to worry about outliving your money.

When, not if, but when the markets cool off you will be reminded why you have your safe and steady portfolios. Call the office anytime with questions. ☺ ☺ ☺

Noteworthy News! ! !

Congratulations to Dan Albanese on the purchase of his new business, Maletta Pfeiffer & Associates Physical Therapists. ☺

Congratulations to Maletta Pfeiffer on her recent retirement. ☺

Congratulations to Ben & Jen Hotchkiss on the birth of their son, Jacob Liam. Their first boy, but their third rugrat! Can you ever have too many? ☺

Congratulations to Ben Camerota on his new position with Johnson & Johnson! ☺

Who Makes It?

A serious risk most of us have faced over the past few months is the pet food poisoning issue. Something thought to be initially tied to just one company turned out to be an industry wide issue. This brings us to the question of who makes it? In many products you can tell things are different and clearly made by different companies – you'll never confuse a Chevy Suburban for a Honda CRV! In pet food it's much more difficult and quite surprising to find out that one company, Menu Foods, Inc of Ontario, Canada is the maker of dozens of competing brands of pet foods. Menu Foods has created over 100 different brands of pet food under the names of Procter & Gamble's Iams & Eukanuba to Hills Pet Nutrition Science Diet owned by Colgate-Palmolive and Ol' Roy's pet food – Wal-Mart's own name brand. If the stuff is all being made by the same company – and being sold for grossly different prices – are you getting what you are paying for? NO! Often times the manufacturer of a brand name label will also manufacture the private label versions. Kimberly Clark makes Huggies diapers as well as Wal-Mart's private label diapers. Kellwood Corp. sews clothes for all levels of consumers – from Calvin Klein to Sag Harbor! Marketing is often the difference. Marketing drives price and companies work very hard at hiding whom is actually making what. If consumers knew many of the things they pay a lot more for were to be had in cheaper, different packages the companies would lose pricing power and consumers would view the product as a commodity. Marketing isn't always the only difference. Do the research on the things you buy often! ☺☺☺

Bulls in the China Shop *Continued from page 1*

down less than 0.60%. The Philippines PSE Composite Index was up over 2% on the news. In America all the market indexes were up slightly. Why the big difference in reactions across the world on seemingly identical news?

The first piece of the puzzle is simply information – the general public didn't really know prior to February 27th that the Chinese markets have been on an amazing tear for years.

Secondly, the Chinese government is actively trying to get rid of its version of "irrational exuberance" by recently imposing a trading tax. The goal of the trading tax and its subsequent increases is to curb speculative trading while allowing the long-term investor to buy and hold. The Chinese stock exchanges also have circuit breakers just like our markets do but with different triggers and limits: the effect is to control the amount a security's price can rise or fall within a trading day. Since May 30th the new trading tax has tripled to $2.00 for every $1,000 worth of stock traded. The Chinese Government has also been running ads in the state-controlled newspapers asking people to "think rationally in the markets."

It's interesting to see how the emotion of investing plays on the human psyche! Is there a Chinese bubble coming? Probably. In the past 2 years the major index values have quadrupled: this is clearly not sustainable. Despite the 15% drop in prices in just four trading days, these markets are still up 37% year-to-date, and we're not even half-way through 2007! In May on a single day, more than 450,000 new trading accounts were opened on a single day!

The Chinese markets are very different from ours in that they lack mechanisms investors can use to limit their risk. Here we have futures, options and other derivative-type contracts that allow savvy investors to profit from prices going up or down. In China it's a one-way street: if it goes up you win and if it falls you lose. Most U.S. investors utilize f*undamental analysis* to assess what a company is actually worth on paper, and compare to the market price of the security. But in China, because of tight government controls on capital, fundamental valuation plays a very small role in the investor's ability to judge stocks based on fundamentals. ☺☺☺

Money Quiz

Last month's quiz was won by Linda St. Pierre, she and Rodney will enjoy dinner on us at the Outback. The average household savings rate is in China is 25%. This month's challenge is to tell me what the average wedding costs! (There are 165 guests at the average wedding, what is the price tag?) The winner is going to dinner on us at any one of a few select fine dining establishments. BTN 060407

Killing the Planet!

Let's face it, human beings are doing a number on the planet by forcing our lifestyle upon it. We can leave a lighter footprint by just paying attention to what we are doing. So many things are recyclable today. Junk mail is a big waste, but if recycled would keep getting reborn into new junk mail or other paper products instead of landfill. You just need to put it with your newspapers and it'll become reborn. If you don't want any more junk mail you can opt out by writing to the following:

Direct Marketing Association Mail Preference
P.O. Box 9008
Farmingdale, NY 11735-9008

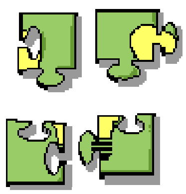
Ask to be removed from all junk mailing lists! Most of us recycle aluminum cans because there is financial incentive for us to do so. What about other things that can be recycled but perhaps are not being recycled: cardboard; glass; appliances; wood; leaves; grass clippings (composting will get rid of all of this stuff as well as your food scraps and create black gold for your garden ☺). Try not to buy things packaged with 20 layers of stuff to make it look big to justify a higher price (software, toys, games, medical supplies). Whoever designed childrens' toy packaging should be wrapped in that stuff themselves! ☺

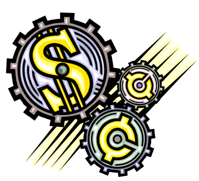
Going Private

People often talk about the IPO (Initial Public Offering) when a stock is first sold to the public and investors have a chance to make or lose a lot of money in the transaction depending on how well the company performs. Buying Berkshire Hathaway at its IPO would have been brilliant, buying Enron would have been painful. ☺ Public stocks are those that trade on stock exchanges and can be bought and sold by anyone, not just company founders or specifically named employees, friends or family members. Lately there has been a slew of the opposite – public companies going private – taking the shares of stock off the exchanges so nobody can trade them. When this happens the investors of the public companies are essentially "cashed out" and given a check for a specified amount for each share of stock they held. This is a very popular strategy today in almost all industries – automotive, electronics, medical, media, its everywhere. Here are a few companies either talking about going private or actually doing it: Avaya, Palm, Cadence, Dominion Resources, Dow Jones, Warner Music, Alliant Insurance. Why has this been happening? There are many reasons this has been happening: if a company goes private it no longer has to deal with disclosing it's financial information to the public for dissemination as to whether or not it makes sense to invest in it; the company doesn't have to gain shareholder approval to make decisions, hire directors, set pay rates, etc. The term "private equity" has been slung around a lot lately and that refers to wealthy individuals, trusts or businesses looking at buying companies and doing whatever they see fit with them – splitting them up and selling the pieces, expanding, growing, whatever the new owners see fit. The private equity players are not your average consumer, they're very savvy business people looking to profit. As this happens more and more investment opportunity is evaporating, leaving billions of dollars that used to be invested in public companies looking for new places to go to work. There was a feeling on Wall Street over the past few years that private equity wouldn't touch technology stocks, but since their prices have come back down to reality and below, the blackballing of technology companies has been removed from the private equity pocketbooks. ☺ ☺ ☺

Inspirational Quotes

- If you do not hope, you will not find what is beyond your hopes, *St. Clement of Alexandra.*
- The only way of finding the limits of the possible is by going beyond them into the impossible, *Arthur C. Clarke*.
- Work spares us from thee evils: boredom, vice and need, *Voltaire*.
- Experience is the child of thought, and thought is the child of action, *Benjamin Disraeli*.
- Do not wait til the iron is hot to strike; but make it hot by striking, *William B. Sprague*.





We can piece the puzzle together and make your money work for you. ☺

Kids Korner

Tips to teach our youth about money

The opportunity cost of waiting. Tell your teenager, who likely knows everything and wonders why you even exist, about this financial concept. If a 16 year old takes $1,000 out of her bank account and buys a mutual fund that earns 10% until age 65 that mere $1,000 investment will have grown to be $106,718.96. Since the teenager knows absolutely everything at this point and your only reason for existence is to provide food, money, a livery service and shelter, ask why they didn't do it already! If they saved their money and put the same $1,000 into an investment account earning the same 10% starting at age 10, they would have $189,059.14. Five years of waiting cost them $82,340.18, or $16,468.04 per year – much more than they earn! They can't afford to wait! Perhaps now you'll have more reason to be hanging around their world! ☺

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If anyone you care about would benefit from receiving this newsletter, tell us who they are and they will be included on our mailing list. They'll certainly appreciate you thinking about them and having their best interests at heart.

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