MIKE CHADWICK'S

MONEY MATTERS

ADVISING, EDUCATING & INSPIRING YOU TO A BETTER LIFE

Volume 7, Issue 5 Advising, educating and inspiring you to a better life May 2009

Rewriting the Rules

Historically there has been a clearly defined method by which creditors were "in line" for corporate assets if anything went wrong with a business. In the investment world we commonly refer to this as the capital structure. The historical method of legal rights to a company's assets is first secured bondholders, then unsecured bondholders, then preferred stockholders, then common stockholders. Bankruptcy courts have defined a very distinct pecking order that has been around for decades and has been upheld by countless legal attacks, until now depending on how the Chrysler deal unfolds.

With our society as it is run by the bureaucracy of law with all of the good, bad and the inefficiencies that inherently come with it, one would think the law would hold up and do what it is intended to do. This massive auto bankruptcy is attempting to completely rewrite legal and investment law by force of the White House as it's providing the funding to keep the company alive. The auto task force that's been pushing everyone involved with Chrysler to get concessions to make the firm viable (the term 'concessions' kills me, in our entitlement society, everyone seems entitled to everything, whatever happened to putting your head down, working hard and just making it happen, not looking for or expecting handouts). The negotiations failed and it forced Chrysler into bankruptcy court protection.

The main issue at hand holding up the negotiations prior to the bankruptcy are about half of the bondholders, who are currently refusing to take 33 cents on the dollar as senior bondholders. The beef they have isn't with taking a loss, it's clear they're taking a big loss, just how much is the question. The beef the bond firms have is how the law defines secured

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INSIDE THIS ISSUE

Innovation

There is a lot of good happening today, unfortunately we don't hear too much about it. Smart firms have always innovated, especially in trying times. We have a history of coming up with incredible ideas and products when there seems to be absolutely no light at the end of the tunnel. Let's look at some of the things that have changed our world in a positive way in the past and a few that may in the future.

Following the Great Depression we were introduced to Kraft Macaroni & Cheese – what would kids do without this? My rugrats wouldn't have had 20% of the meals in their life had this not been invented. ☺ The depression also introduced us to Butacite, a shatterproof glass created by DuPont that is now in windshields and all types of safety glass, as well as other applications requiring strength and clarity. Kraft hit another home run in the 30's with Miracle Whip – the mayonnaise alternative. DuPont also had another killer invention – Nylon in the 1930s that clearly changed our world forever. The GPS & the Sony Walkman came out in the 70's and 30 years later Apple introduced the iPod in 2001 just after the terrorist attacks.

Now we live in a world that has so much, that produces and consumes so much, we threaten to change the planet. Traditional garbage companies are no more, the new firms are both garbage companies, recyclers and energy firms. Yes, energy firms. Today's modern garbage plants recycle anything that can be recycled from metal, aluminum, plastic to wood and paper to compost. Then anything that cannot be recycled is incinerated to generate electricity that is sold back to the grid. If they don't incinerate they plop it in a landfill – which today is generating energy from the extraction of the methane gas and covered with solar tarps, giving double duty to the horrific landfill. Not a bad business model – get paid to pick up your raw materials, separate them and sell some off again, get paid again to generate power from the incineration or storage of what's left.

Energy is so hot today, innovation is everywhere with the goal to reduce carbon emissions and global warming. I'm not sure

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bondholders. When the firms lent Chrysler the money, the agreements they signed gave them a legal right to the first lien on assets. This right is superior legally to unsecured creditors or employees. The plan as it sits now is to make the secured bondholders take a 67% loss, and give up on how the original agreements were written. On the back side of the agreement, infuriating everyone involved is that the bondholders will be taking a bath but the unions (United Auto Workers) will essentially be made whole by having their health care trust own 55% of the stock in the company that emerges from bankruptcy. Stockholders get wiped out, mainly Cerberus Capital Management, the hedge fund that bought the struggling automaker in 2007.

With the state of things today, few people on the planet have any pity for hedge funds, which are getting most of the blame here and likely were a main contributor to the meltdown of the financial sector. If more hedge funds take a bath, many people will likely party in their sorrow. Don't get hung up on that point, realize it's not just hedge funds objecting to the proposed government deal, it's also many other money management firms, some working on behalf of regular folks like you, fighting for what is legally theirs. 20 of the 46 lenders are opposed to the proposed government deal, which is what ultimately forced Chrysler into bankruptcy.

When a firm goes bankrupt through a chapter 11, the presiding judge must approve any negotiated deals with lenders, unions and other interested parties. This case is being presided over by Judge Arthur J. Gonzalez, a well known expert in big bankruptcy. He presided over the Enron and WorldCom deals earlier in the decade. The biggest difference is the goal here is to keep Chrysler alive to fight another day, where the Enron's and WorldCom's of the world are ancient history.

This deal is so different from any other because in trying to make Chrysler a viable concern to eventually merge with Fiat, there are so many parties that must be satisfied. If the lenders end up taking a bath and unsecured creditors go above them in the capital structure, it will permanently change the way loans are made and risk is viewed. Lending costs will go through the roof; banks and other firms will constantly be worried that their supposedly secured right to an asset can be overturned in a heartbeat, if it's for the greater good (who decides the definition of 'the greater good' ?).

The administration's viewpoint on the deal is that the company must be preserved to merge with Fiat and it'll take workers, suppliers and warranty holders intact, all of whom are key to making the company a long-term success. Is that at all possible, a long-term success? I feel the pain of anyone currently in the new car auto sales business, especially those at Chrysler – the customer asks about the warranty and they are told the U.S. Government is guaranteeing all warranties in the event Chrysler doesn't make it, now that's a tough job.

The U.S. Treasury will be wiped out on the "loans" it already provided and will provide another $8 billion along with the $2.4 billion from the Canadian government. In exchange they'll get 10% of the equity of the new company. What's going to happen to the state and local governments, who face the same fate as the big auto companies with manpower legacy costs that are equally unaffordable? It'll be interesting to see the next few years unfold. ☺

News Blast

This is not a "normal" time in the world with the upheaval we are all living through with the global recession. The globe is awash with issues and the media is hitting all things financial on all cylinders. People are terrified as a result. It's perfectly normal to be concerned, but real fear and pure terror are simply unacceptable.

If something bad hits you or a loved on, you'll deal with it when the time comes. Don't worry about losing your job until you do. If you fear that it may happen, hedge your position and start looking around and spreading the word that you're in the market for a change. This way if you're downsized or outsized you'll have a head start on finding a new position.

The media isn't doing anyone any favors, from an entertainment perspective the media is cashing in on the economic chaos because people cannot turn it off. CNBC has a host of hot hitting shows, mostly of an entertainment tool and not a financial tool for decision making. Most of us in the investment business don't tune into CNBC at all as it's targeted to the consumer, not the institutional investor. It's often put on in waiting rooms of financial firms and in any financial lobby to play the part, but don't get the wrong impression, Cramer is an entertainer, not a financial or investment advisor.

Many people in the past few weeks have said that after meeting or speaking with us, they just feel better, as if a load has been taken off their shoulders. Some folks said they're sleeping better at night with a new found confidence following a meeting with us.

If you're stressing about money, finances, investments, etc. please don't hesitate to contact us. Financial issues can be hard hitting, and if you cannot find answers or comfort with what you're currently doing it's time to talk with someone. I recently ran into a client in the grocery store one evening following a meeting we had a few weeks back, and after we said our pleasantries, the husbands comment was "Mike, thanks for the meeting, we feel a lot better now but how much do you charge for the psychiatric counseling portion of the meeting?" As comical as it seems, this isn't all about money and numbers. I tell folks all time there is a continuum in the financial advisory world we must fit into. On the far right it is a viewpoint of purely economic ramifications, a place I comfortably sit and view the world to make all of my economic decisions from. On the far left is a place viewpoint of emotional/societal/psychological ramifications, a place most of the population sits and makes their economic decisions from.

My goal is to get most people to the economic place, where they're not jaded or swayed by emotional/societal and psychological issues that inhibit their ability to make sound financial decisions. Most people cannot get to the exact place I am, but if we can slide you toward that direction until you feel a place of comfort, you'll substantially improve your outcomes over continuing to reside where you do. You must always consider all sides of any decision, but the intellectual side of the equation must rule. If this prescription is followed, the financial stress level should fall through the floor. ☺☺

Noteworthy News! ! !

- Congratulations Kevin & Michele Gaffney on the birth of baby Caraline Alise! ☺
- Our deepest condolences to the Demsey family on the passing of Kathy's father, a wonderful man, husband, father, grandfather and friend.
- Our deepest condolences to the DeFiore/Russ families on the passing of Armand's brother Robert DeFiore, a wonderful man, husband, father, grandfather and friend.

I Bond = O Bond

The I Bond, or Inflation bond has been a great tool for investors, until now. The Treasury announced that the I bonds purchased between May & October will have a yield of 0%, that's right, zero. This is the first time the bonds have hit 0% since their inception in 1998. The rates of I bonds are set every May 1st & November 1st. The inflation adjustment component, typically added to the fixed rate of return on the I bond, has recently been calculated to be -5.64%. Add this to the new fixed component, which will be a paltry 0.10% and you have a security that yields nothing. It may make more sense to put your money under your mattress than to lend it to Uncle Sam in the form of an I bond. You can't lose any money on these instruments, the rate cannot fall below 0%, but 0% isn't an investment, and it's a loss after taxes and inflation, the very thing these tools were designed to offset.

In this day inflation hedged tools seem like a smart bet, since the rate that the Treasury is printing money seems like it will lead to inflation, eventually. Amazingly in recent times we've had a system where the governments of the world are printing money like mad and simultaneously prices are falling. Food and certain items are more costly today vs. a few years ago, but that's more sticky pricing (prices stay high for long periods of time after the underlying items that it takes to make the goods goes down) than actual supply and demand. Big ticket items are much less than they were a few years ago – homes, cars, commodities, fuel, etc.

If you're looking to hedge inflation, this I bond isn't the way to do it right now. When they had a fixed rate of 2% + the inflation component, these tools made a lot of sense. Today they don't make any sense unless you're really bad at math. If you buy lotto tickets it may make sense to buy some I bonds too! ☺

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how much of an impact man is playing on these issues, but we all would welcome a world where we are energy independent and the petro-dictators stop pounding their chests. With oil at $55/barrel the petro-dictators have been very quiet lately! ☺

Windmills are the rage today just because you can see them, but there are alternative energies everywhere coming around the corner. Underwater turbines are now all over – in the Manhattan harbor juicing up Wall Street cleanly and in many other rivers and oceans. Ocean buoys are being used today to generate electricity – there are firms that put very large buoys a few miles offshore, tether part of it to the ocean bottom and each time the currents do their thing and the buoy bobs, it generates juice that is then returned to the grid. Once installed, these buoys have the capacity to generate clean power forever. You'll of course need to maintain them and scrub off the barnacles from time to time, but the oceans won't stop bobbing anytime soon.

Rooftop solar collectors today can do double duty, providing electricity and three hundred degree hot water, with the ability to give your home or building heating and electricity. If this goes large scale in the coming years every building with adequate sun exposure will have the potential to become a self-generating power plant, not consuming any public power and supplying local utilities with clean power to resell after the buildings needs have been met.

Not all plastic is created equal. Most people assume plastic is an oil byproduct, pollutes the planet and takes thousands of years to break down. Firms today are making plastics from plant material where you can dispose of the plastic in salt water or in a compost pile where it turns into dirt in 30 days. Think of the water bottles floating around in the ocean – an island of them the size of Texas that will take thousands of years to decompose. If this technology takes hold, we'll all be using it for our water bottles, computers and every other application for plastics in our world.

A few recent additions in the past few months and years to the cool innovation category is the Nintendo's Wii and Wii fit, Amazon's Kindle and Uconnect Web (amazingly a Chrysler innovation ☺).

Companies that continue to spend on research and development (R&D) in tough times like today will reap big rewards in the coming years and decades. If firms cut their R&D budgets they'll likely have a lot of painful years ahead of them as they will not be able to spool up in time when new products and technologies come online. Detroit is the mess it is because instead of innovation, it was big fat and stupid, laboring along with unaffordable legacy costs and spineless executives who were unwilling to make the tough decisions.

Money Quiz

Last month's quiz went unanswered. Americans added $246 billion to savings accounts from 1/1/09 – 3/09/09 a time when the markets were 50% off their highs. This is another example of the average Joe doing the wrong thing at the wrong time. ☹

This month's challenge is to tell me what positive return is as likely for the S&P 500 for a calendar year as a negative for the last 75 years, from 1934 - 2008? The winner will enjoy lunch/dinner on us at Chili's. 050409:3☺

Banking Redefined

Banks are getting a lot tougher on company credit these days. The transition from an easy money environment to a more critical approach is difficult to live through, but the outcomes will be good for everyone involved. This process is going to make it a tad more expensive for businesses that commonly rely on lines of credit to live when cash flow is tight on a seasonal or periodic basis, as most businesses live through.

The good news here is the banking sector that wasn't really functioning well is now thawing out and lending is again happening, if you've got the credit and financial ratios to justify the loans. Most banks today are raising rates a little bit or tying the interest rate of the loan to the company's credit rating and shortening the length of the line of credit available to businesses. They're also coming up with other creative rate strategies, the most recent is to tie the interest rate of the loan to the cost of the credit default swap of the company. A credit default swap is an insurance policy tied to a company's bonds, which cost raises exponentially as a company is feared to have financial trouble. This will automatically make the loan more costly if a firm taps it when it's in trouble.

These strategies all make sense to make the world a less leveraged, more conservative place to work and live.

Shortening the loans means companies will need to renegotiate their loans more frequently, giving bankers more time with a company's books and financial teams. This will lead to better relationships and better understanding of a firm's assets, risks and liabilities. The banks win too because with shorter term loans they don't have to hold as much in reserves as they do with long term loans, taking some of the pressure off of their reserve blocks today. ☺

Beware Insurance

Insurance purveyors are out in full force trying to play on people's fears and emotions today. Many sophisticated insurance products are available today to investor that offer "guarantees" as well as stock market like returns. Remember the old adage, if something is sounding too good to be true, it probably is.

There are various insurance products out there that offer guarantees on your principal investment. These products are often low, fixed rate contracts that ensure you 2-3% in today's climate. This guarantees you a loss against inflation and taxes on a long term basis. When insurance products offer you guaranteed interest, plus stock market like returns your guard as well as the hair on the back of your neck needs to stand at attention.

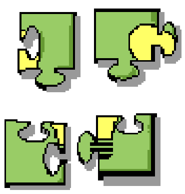
We've seen countless new clients in recent months that have been talked into such products thinking they now get a guaranteed 5, 6 or even 7% return, plus all appreciation that can be had in the stock market. Nothing is further from the truth because these guarantees just don't exist. Bernie Madoff's guaranteed 11% forever sounded real slick too and look where that landed people. Stay away from such offers.

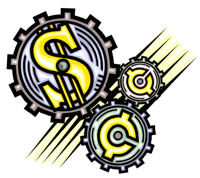
The way these variable annuity contracts work is your money is invested in "subaccounts" within the variable annuity. These subaccounts are very much like retail mutual funds, with a different name because they're wedged inside the annuity. You are guaranteed a certain return upon death, but the living benefits require you to take an income stream of no less than 4, 5, 6 or 7% depending on the details of the insurer's contract. These annuity contracts are always written by insurers, not investment firms. Investment firms may be available within as choices, but they're not inking the contracts.

It all sounds great, especially in an environment like we've had lately where most people have lost money. The guarantees are not like you think they are, you cannot just walk away with a big pile of cash unless you die, and sometimes there are even strings attached to death benefits. To get the living benefits you must agree to leave the money with the insurer essentially forever, withdrawing only the amount they deem you can. To that end, you're only guaranteed to get your money back over time, an awful lot of time when you factor in they only allow you take out 5% annually on average. This will take 20 years just to get back what you put in. When you apply lost opportunity costs to this equation the 3-4% in total fee's you're paying the insurer, plus the lost opportunity costs make this a real raw deal for the consumer. Don't let people or firms pray on your fears, make intelligent decisions that are fact based, not emotionally charged. If you're already been talking into such a contract, it's very hard to leave it but we're happy to provide a review for you to be sure you do the right thing to improve your outcomes. ☺

Inspirational Quotes

- *Nothing in life is to be feared, it is only to be understood. Now is the time to understand more, so that we may fear less.* Marie Curie
- *Every time we choose safety, we reinforce fear.* Cheri Huber
- *Only when we are no longer afraid do we begin to live.* Dorothy Thompson
- *You must do the things you think you cannot do.* Eleanor Roosevelt
- *Don't be afraid to go out on a limb, that's where the fruit is.* H. Jackson Browne





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

Kids Korner

Financial Candy Land – that's where many of our youth live today. It's imperative that the children understand money from an early age. My rugrats are 7 & 8, have their own ATM cards and checking accounts and pay their own bills from the allowance we give them. We're providing all of the money, but they are making the decisions. Even school lunches, we provide enough loot to buy one a week and if they buy the lunch great, but if they don't they can pocket the cash. I see many kids today who don't have a clue financially even when they graduate from college. The kids will make very different financial decisions if they have skin in the game. Everything from buying clothes to books to cars to college educations – they have to know the costs, know where the money is coming from, and use some of their own in the process. It's always easier to spend your money, so make them spend some of their own too. ☺ ☺ ☺

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