The 'Fiscal Cliff' is Just Another Y2K

-J. Kevin Meaders, J.D, CFP®, ChFC, CLU

December, 2012- In eighteen years of advising retirees I have discovered two rules to be absolutely true:

1. Never let your kids move back into the house, and
2. Never get up on the roof—for any reason.

Though these rules have nothing to do with investing, I hope they brought you a little smile, because sometimes I get blamed for only reporting doom and gloom scenarios. ☺

I've discovered there are two types of people reading this right now: those who want the down and dirty truth; and those who only want the truth if it's pleasant. I'll let you be the judge of what category you fall into, but if it's the latter, you might want to just skip to the last page now.

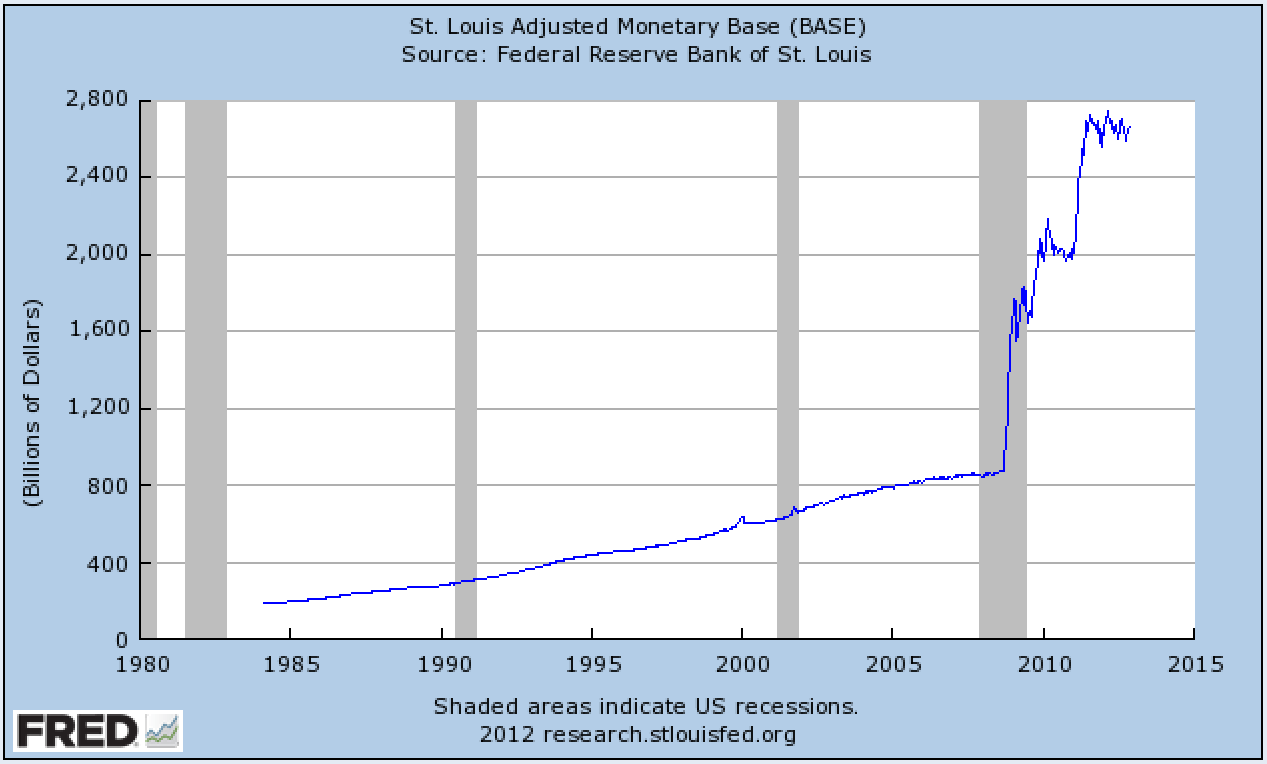
For you brave, hard-core truth types, the recent election brings to mind an insightful quote by Ben Franklin: *"When people find that they can vote themselves money, that will herald the end of the republic."*[1]

Franklin knew that the only way to provide the money "voted to the people" is through higher taxation and/or currency debasement, both of which are detrimental to liberty and can undermine social stability. This was all too evident to the founding fathers as they witnessed the French Revolution unfold in all its terror.

For us today, it would seem we are in for higher taxation in addition to more massive currency debasement. So with the election over, it's back to the business of destroying the dollar—a job the Fed has done in earnest since the 2008 crash.

The chart on the next page represents America's monetary base. In dollar terms, the base has increased from about $850 billion to now roughly $2.6 trillion. The number itself is not as important as the obvious percentage increase that has occurred since 2009—an increase of over 300%! These numbers are so big they start to lose meaning to the average person. And what most people don't even realize is that this increase in the money supply has been simply electronic—created, as the saying goes, from thin air. Nice gig.

[1] *Franklin: Writings.* Benjamin Franklin, J.A. Leo Lemay, Editor.



The money that you and I own was not obtained electronically, but by working, saving, and investing. All of these things require real capital (yours) and real work and effort (also yours) to acquire, increase and preserve your money. Thus, essentially, the Fed has just reduced the value of your money and the value of your work and investment by two-thirds.

Another way to think of the value of your dollar is to use the price of one ounce of gold as a benchmark. For instance, in 1971, the value of a dollar was 1/35th an ounce of gold. Today, the value of your dollar has fallen to roughly 1/1700th an ounce of gold.

Why has this happened? The “Powers That Be” have convinced Congress and the American public that our economy *needs* "stimulus"—TARP, QE1, QE2, Operation Twist, and now an additional $40 billion per month (remember, that’s forty thousand million) until further notice, which I call QE infinity. (In case you missed it, "QE" doesn't stand for Queen Elizabeth, but for "Quantitative Easing," which means "printing money.")

They just don't get it: no matter how hard you try, you can't create something real from something phony. This is the reason the price of gold and silver continue to rise, even though we still harvest tons of these metals from the earth every year.

My greatest mentor, a German-born economist named Ludwig von Mises, wrote:

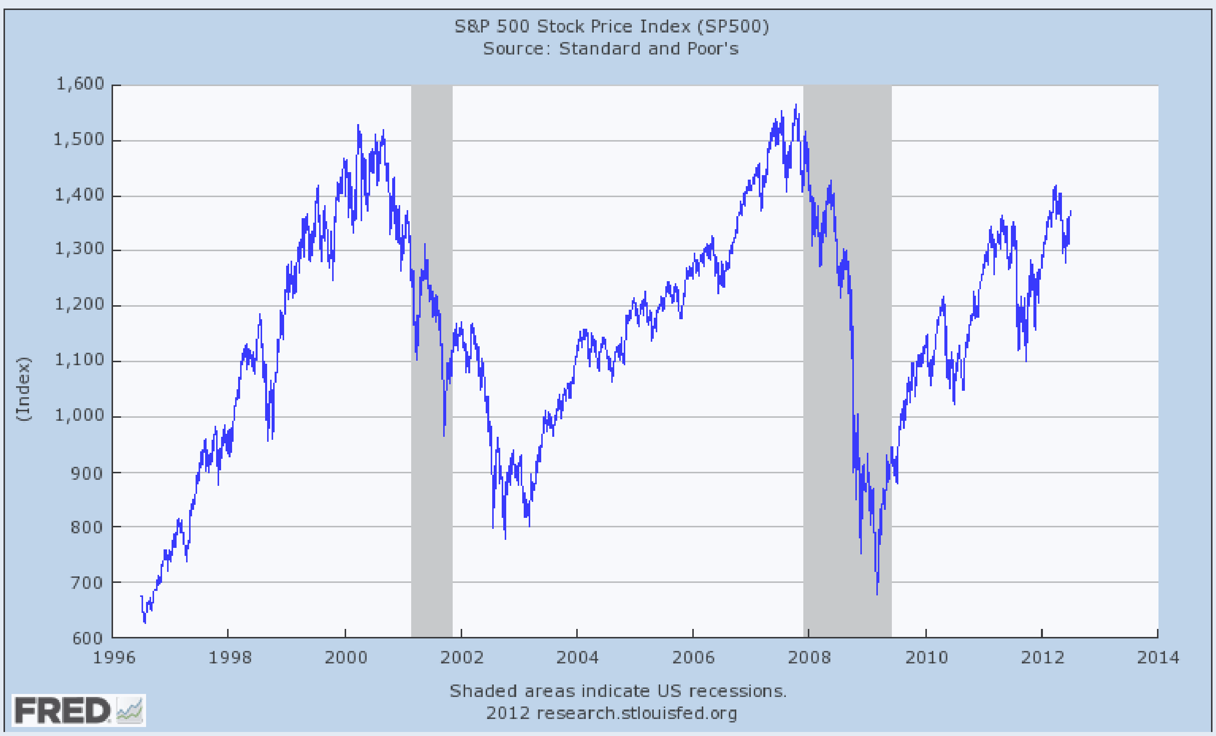
“True, governments can reduce the rate of interest in the short run. They can issue additional paper money. They can open the way to credit expansion by the banks. They can thus create an artificial boom and the appearance of prosperity. But such a boom is bound to collapse soon or late and to bring about a depression.” (1944, *Omnipotent Government* p.139)

Ludwig von Mises
1881-1973

"The wavelike movement effecting the economic system, the recurrence of periods of boom which are followed by periods of depression is the unavoidable outcome of the attempts, repeated again and again, to lower the gross market rate of interest by means of credit expansion." (1940, *Human Action* p. *570)*

"The ultimate cause, therefore, of the phenomenon of wave after wave of economic ups and downs is ideological in character. The cycles will not disappear so long as people believe that the rate of interest may be reduced, not through the accumulation of capital, but by banking policy." (1978, *On the Manipulation of Money and Credit.* p. 39)

I've always wondered if Professor Mises knew how right he was. Take a look at this chart of the S&P 500® since the 1996 Atlanta Olympics. You can clearly see the "wavelike movement" of which Professor Mises speaks. Recent massive addition to the money supply could be expected to exacerbate these waves. Understanding these waves is critical to managing your nest egg.



Alas, this is the economy in which we live and there is very little we can do to change it. We, therefore, are forced to deal with it. But at Magellan Planning Group, we have an advantage: we have the teachings of Professor Mises and the Austrian School of Economics to help us identify the real underlying causes of market trends, and booms and busts. As a consequence, we were not caught unawares when the markets crashed in 2000 and 2008, but were rather expecting it.

The Austrians teach us that the economy, through artificial monetary manipulation, essentially goes through two repetitive phases: an expansion phase and a contraction phase. It is during the contraction phase that depressions and recessions occur, and during the expansion phase that money is misallocated into artificial booms.

Through these lenses, we can clearly see that our economy—and indeed the entire world—is in a monetary expansion phase. History has taught that no matter the immediate cause of market pullbacks—Y2K, the U.S. losing its AAA rating, the budget deficit crisis, Libya, Syria, Obama's re-election, the Fiscal Cliff, the Aztec Calendar, the coming Israel-Iran confrontation—the market will continue its general trend of expansion and inflation.

This is not to say that the rules of supply and demand do not apply. Quite the contrary. The $10 Trillion in cash tells us that the demand for safety is great because people are willing to pay financial institutions a high price (by accepting minimal interest) to keep their money in cash.

Likewise, we can tell that the demand for stocks is weak because the price of stocks is lower than their earnings suggest they should be. This is good news for us because we can sit around in these stocks earning dividends while waiting for the stock prices to rise. This has already occurred in the bond market quite significantly.

Thanks to Professor Mises and the Austrian School, we know what to expect: an artificial boom followed by a bust of roughly equal magnitude. So, knowing a boom is coming, along with its imminent accompanying bust, we are much better equipped to deal with the uncertain future. As the saying goes, “History doesn’t repeat itself, but it often rhymes.”

And so, in simple terms, while everyone’s objectives, risk tolerance and financial situation is unique, our general strategy hasn’t changed and is three-fold:

1. Seek dividend and interest yield in the 3-6% range while we wait for equities to rise.
2. To capture as much growth as possible when stock prices finally do increase.
3. To begin reversing our exposure to stocks when the Fed starts to raise interest rates.

As always, I encourage you to call or visit so we may review your specific situation in light of your circumstances and today’s economic environment. From all of us at Magellan Planning Group, I want to wish you a heartfelt “Safe and Happy Holidays” and the very best for the New Year.

About J. Kevin Meaders

kevin@magellanplanning.com

Kevin Meaders graduated from Oglethorpe University in Atlanta with a double B.A. in Philosophy and Political Science, and then obtained a law degree from Georgia State University College of Law, focusing on estate planning and trust law. He has earned the designations of Certified Financial Planner (CFP®), Chartered Financial Consultant (ChFC) and Chartered Life Underwriter (CLU). He holds a General Securities Principal and Registered Representative registration and Investment Advisor Representative registration through ING Financial Partners (member SIPC).

About Magellan Planning Group

www.magellanplanning.com

Magellan Planning Group was established in 2000 to provide a service uniquely tailored to the needs of our affluent Atlanta community. We concentrate on *personalized* retirement planning through tri-disciplinary coordination:

- Financial planning with our Certified Financial Planner™ to prepare a retirement plan that takes into account your needs and expectations. We are a fee only asset management firm with a $500,000 minimum relationship.

- Estate planning with our in-house Attorney-at-Law to determine and prepare the documents needed to minimize family liability and maximize privacy. (www.magellanlegal.com)

- Tax planning through a relationship with our in-house CPA to manage tax obligations throughout the year and prepare a tax return that takes into account current tax laws. (www.magellantax.com)

Our relationship doesn't begin and end with the preparation of a plan and the appropriate documents. We establish close personal relationships with our clients and their families and maintain those relationships through regular 'check-ups', market commentaries and educational Lunch & Learns.

4170 Ashford Dunwoody Rd. NE, Suite 480
Atlanta, GA 30319
404-257-8811