

Banking Blunders

In New England most banks work as banks should, responsible and fiscally conservative, never taking undue risks with precious capital. They borrow money from depositors and pay a low rate of compensation to them, and immediately reinvest that money at higher rates of return, capturing the difference or 'spread' in the process.

The banks' investment could be in the form of loans to your neighbors, credit cards, car loans, bonds, stocks or mutual funds: whatever the bank's investment committee determines is a good fit for the bank's return on capital objectives while complying with its internal investment policy guidelines. A well-run bank can easily earn mid-double digit returns on its investment, or about 13% on an average basis. If they're paying depositors an average of 1-2% for deposits, that's a lot of money to be made. The term 'Old Yankee' exists because many local, relatively small-time bankers still operate according to those sound economic principals.

That is the furthest thing from the truth on a national basis as many banks sought to exploit the real estate gravy train, expecting that by hopping on board they would grow to become even bigger, badder, more profitable financial institutions. Many of those banks now wish they had stuck to the fundamentals of sound banking. A great example of such poor stewardship is National City Corp., a Cleveland bank that went full steam into sub-prime mortgages that

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Adrenaline, Emotion & Media

The news is something that from the dawn of time was meant to inform people about what's going on in other areas. The word "news" is actually an acronym. In an era devoid of ubiquitous print and electronic media, people from different geographic regions would gather together and share the information they possessed that was related to their home in the North, East, West or South. When you take the first letter from each of these words, you get NEWS. Coming from every direction and sharing news gave everyone a more informed, big picture view. News was exchanged relatively infrequently, perhaps weekly, monthly or even less frequently. It certainly didn't happen in the manner it does today, with an update virtually every second of the day or night.

The media today mostly sells sad, scary and bad things, because that's what interests most people, and it is ultimately what creates viewership ratings. Television attempted to produce an all-positive news channel years ago and it failed – go figure.

I've been so turned off by the television news that I have another acronym I use to explain it to my rugrats: NEWS = Nothing Educational or Worth Seeing – with the notable exceptions of weather and traffic. Both the weather and traffic can be had on the web without being forced to absorb the rest of the negative minutia associated with the news, so I rarely consume television news media. I simply don't want to surround myself with negative noise. You become part of your environment and I keep my environment as optimistic as possible at all times. If you allow yourself to be exposed to negativity it will affect you in a negative way. I can tell you by guesstimate what's on the news any given day: fire destroys home, six homeless (duh, if a fire destroyed their home could they be anything else!); man arrested for raping a woman; mother

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are now turning sour. The bank had a reputation for mid-western common sense; many are now thinking they had no sense at all. I cannot disagree with that conclusion. In 1999 National City began acquiring sub-prime firms and eventually expanded into Florida communities to which many of its successful Mid-western clients had chosen as their retirement destination. National City decided to expand its presence rapidly in Florida by buying several smaller banks—one as recently as January of 2007.

When the expansion was complete, they had 94 branches along Florida's southwestern "gold" coast. Think about these two strategic decisions – focus on subprime loans (this really means making adjustable rate or other non-standard loans to people who don't qualify for "normal" mortgages, and so inherently represent a higher risk for default), and do so at a time when the real estate market is at a frenzied pitch and valuations realistically are due for a 'correction.' These decisions were clearly influenced by greed, not common sense. That is not the thinking I expect out of a banker. I'd expect such thinking out of a hedge fund manager.

Fast forward the clock to January 2008 and what has happened – we now know real estate prices are melting down, banks are foreclosing on consumers in record numbers, and the values banks said their portfolios of loans are worth are far from the truth. The medicine = many banks will go out of business, get bought or perhaps barely survive. National City is trying to cope by slashing its dividend payment to shareholders by 50%, ceasing sub-prime lending, and halting its stock repurchase program. National City bank was happy to buy its shares back a few months ago at \$38 per share. The stock is now priced around \$14, the bank has no money to repurchase shares and is struggling to find enough capital to operate day to day. Is National City worth \$14 per share? Perhaps. Or maybe its shares are nothing but toilet paper at this juncture.

National City no longer makes sub-prime loans and they no longer allow outside brokers to originate its loans. That's great, but management should have implemented sensible policies from its inception, or at least about five years ago: this may have left National City in a position today to buy a troubled bank or mortgage company at a substantial discount to book value. Instead it's on the ropes and may be going down for the count.

Common sense goes a long way and is usually all that it takes to avoid calamities. Don't get greedy and emotional about money! ©

Social Security Retirement

The Social Security system is designed to be a supplemental retirement system and is indeed a great one. There are many misconceptions as to when and how you can collect so we'll dispel some of those myths now. To qualify for Social Security payments in retirement you must have 40 quarters of credits if you were born after 1929. In 2008 one credit is earned for every \$1,050 in wages earned each year, with a maximum of 4 credits earned per year. If you worked for 10 years and made even a small part-time income, you're insured for Social Security retirement purposes. If you never worked and are married, you're also entitled to benefits based on your spouse's record as long as you've been married for ten years and are over 62. Social Security benefits are calculated using three different pieces: the first piece is to index your earnings for inflation – what you earned in the 50's doesn't seem like much today but it was good back then; the second piece is your lifetime average earnings, which is your 35 highest years of earnings in which you paid into Social Security – this is called your Average Indexed Monthly Earnings (AIME) and is the basis for the calculation; the last step is to run these two components through a formula to determine your monthly benefit. The system is designed to provide a larger percentage of earnings replacement for those who earned less. If your average monthly earnings were \$455, Social Security would pay \$409/month, replacing 90% of your income. If your average monthly income was \$4,273/month, it'll pay \$1,570/month, replacing only 33% of your income. For young people today, it'll likely replace a smaller and smaller percentage of your true earnings. *When* you are eligible to collect is another issue – you can begin collecting full retirement benefits based on when you were born:

Year of birth	"normal retirement age"
1937 or earlier	65
1938	65 & 2 months
1939	65 & 4 months
1940	65 & 6 months
1941	65 & 8 months
1942	65 & 10 months
1943-1954	66
1955	66 & 2 months
1956	66 & 4 months
1957	66 & 6 months
1958	66 & 8 months
1959	66 & 10 months
1960 and later	67

At full retirement age you're entitled to 100% of your "credits" but you don't have to wait until that age to begin receiving Social Security. You can begin collecting a reduced benefit at age 62, or at 60 if you're a qualifying widow or widower.

People often wonder when to collect and it's based on your life expectancy and family history, which we never know exactly and I wouldn't want to know. We do have a calculator to help you determine this, if you'd like us to run your numbers just call us and we'll be happy to do that for you. ©

Noteworthy News! ! !

- Our deepest condolences to the Keywan & Reid families on the passing of Fred Keywan, a wonderful man, father, grandfather, friend and person.
- Congratulations to the Staves family on the birth of baby Katherine, she joins big brother Ben! ☺
- Congratulations to Richard & Laura Alleyne on the birth of baby Derek Emmanuel, joining big sister Olivia! ☺
- Congratulations to Margaret Leicach on the birth of Derek Emmanuel, another grandbaby! Can you ever have too many grandbabies? Spoil them, fill them with sugar, wind them up and give them back to their parents. ☺
- Congratulations to Gert Conroy on the birth of her third grandbaby – Julia Claire Conroy on November 29th. This is the best holiday present there is! ☺
- Congratulations to Gail & Mike Melanson on the purchase of their new home! ☺
- Congratulations to Mike & Michele Sanford on the completion of the building of their new home! ☺
- Congratulations to Dana & Rebecca Andrews on the recent birth of baby David Joseph, he joins big sister Isabel! ☺

Benevolence Continues

In the past few years we've witnessed some of the wealthiest people on the planet donate the vast majority of their fortunes to charity. Hotel magnate Barron Hilton just announced he'll donate 97% of his \$2.3 Billion fortune to charity to help the homeless, mentally ill, those addicted to drugs, those without clean water and the Catholic sisters! This is a great sign and hopefully the trend will continue. We have so many in this world who are in need.

Barron Hilton is the grandfather of the foolish socialite Paris Hilton, and he is reportedly so embarrassed by her antics that he has decided to leave her nothing of his fortune when he dies. That's a decision that makes most of us well-adjusted "normal" people very happy.

Hopefully this will get some press in younger people's publications and serve to stop the glorification of idiotic celebrity behavior ☺

Adrenaline Emotion *Continued from page 1*

arrested for child neglect; local politician indicted for doing something really dumb; Blumenthal (CT Attorney General) suing some company for not being a mind reader and preventing an idiot from doing something stupid with a product that wasn't intended for said use and hurting self or someone else; there is traffic on Interstate 84; accident on I-91, three teens driving a Subaru WRX Sti (300 hp race car that no 16 year old should own – Blumenthal should talk to the parents for allowing kid to buy and own it) dead; snowstorm coming (remember when a storm comes you'll never have the chance again to buy milk, eggs or basic household supplies so rush out tonight and stock up!). That is the typical headline lineup in any local evening "news" broadcast.

I'm not telling you anything you don't know, but people continue to tune into this noise and let it adversely impact their attitudes--stop doing it immediately if you're guilty of this! On a monthly basis there may be something worthwhile to share and learn from, but by the minute? Minute by minute, day by day it's just noise in the world and your life. Instead of watching the news spend that time exposing yourself to something positive or learning a new skill or doing what you enjoy – perhaps nothing. That will make your life better at the end of the day.

Now let's think about how this affects the average investor. Financial news stories over the past year focused on: real estate slowing; bank write-down of bad loans; sub-prime loans go bad; home foreclosures are up; new home permits down to lowest levels since 1988; consumers walking away from homes in record numbers; blue chip financial company seeks \$10Billion capital infusion by a foreign investment fund. These stories are in the news wherever you turn, over and over again. It's not news anymore. It's really nothing new to anyone, but it's highly emotional and it's something that the media can use to drive people into a frenzy, which drives ratings: in the end it's all about the money. We or any other institutional investment firm obviously don't spend any time listening to the media for financial information – you shouldn't either. When there is new financial news that will impact your future or the future of those you love, we'll communicate it to you when we speak or in this newsletter.

If anything happens suddenly that warrants your attention, we'll call. Until then, enjoy yourself and let us worry about the \$. ☺

Foreign Capital

As the headlines crush many banks and mortgage companies you constantly read about this influx of foreign capital. What is foreign capital and why is flowing to the U.S.? Foreign capital is money owned by foreign governments, wealthy individuals or investment funds. Owners of capital always seek to put it to the most profitable use. Lately we've seen a lot of foreigners make large investments in U.S. companies such as Citibank, Merrill Lynch, and Morgan Stanley. These U.S. financial firms are looking for capital to offset recent losses on loans, and the declining value of the U.S. dollar renders the cost of a U.S. asset relatively cheap from a foreigner's perspective. The stability of our government and the resiliency of our economy are also attractive characteristics.

The average American consumer is fearful today – but super wealthy and intelligent foreign investors are investing heavily in these financial companies today. Do you think they're doing this out of their charitable hearts or as a business decision? It's not charitable intents, but a business decision. These investors recognize a rare opportunity to buy into good businesses at a cheap price: they expect to make some real money over the long haul. Many foreign investments today are grossly overpriced. The same crisis we're having here with an out of control housing market is also happening in Europe and Asia. For many investors the U.S.A. presents the best investment opportunity available. Perhaps we should think differently about what's really going on in the markets today. We clearly have a real estate market in turmoil. A healthy washout is painful but necessary. It will likely take a few more years to bottom out, then another four or five to begin to grow appreciably again. By then those who have been renting or are in good financial shape can then buy again through traditional mortgages without the relaxed lending standards.

The economy is cooling off, whether we have a recession or not is moot, that's just a number on a page. Either way it's a slowdown from the prior pace. If it were all really indeed bad and Armageddon was around the corner, wouldn't these wealthy foreigners be putting their money to work elsewhere? Of course, but despite all the bad 'news' they are choosing the relative safety and potential returns offered by the American economy! ☺



Money Quiz

Last month's quiz wasn't won! ☹ 8% of people are saving at least 15% of their income for retirement! Our prescription is to save 20% so get saving! Nobody has ever said "I saved too much" ☺☺☺

This month's challenge is to tell me how many times in the last 50 years (1958-2007) has the S&P 500 produced at least a 15% return? The winner will enjoy dinner on us at Chili's Restaurant. BTN 112607

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Valuations

Valuations are simply what things are selling for – what willing buyer and seller come to as a price at a certain point in time. Today's valuations in our stock market seem fair, not too high or not too low. There aren't any particular areas where we find smoking deals nor are there any areas that are scary. Even real estate is coming down to reality now slowly but surely. But we're nowhere near the bottom – that'll likely take a few more years. Stock market valuations are something completely different. For 2007 the DOW was up 3.8%, nothing special but valuations remain fair. In early 2008 the S&P 500 index is trading at 13.8 times forward earnings (that means an investor is willing to pay \$13.80 today for each \$1.00 of estimated earnings for the year). This is just a bit below its historical high of 16 times but nothing to get too excited about. I wouldn't consider it a killer deal, but a slight bargain. In 2000 when the internet bubble broke, technology stocks were trading at over 50 times earnings – truly scary values. In China, their market index was up 167% in 2007! Now that level of appreciation simply isn't sustainable and China isn't a small economy anymore so the old argument of it's an emerging market is out the window. They've got some real issues they're wrestling with: inflation; pollution; explosive growth; outrageous housing costs; energy (the Three Gorges Dam project is the largest building project in the world and when completed will be the largest generator of electricity on the planet). Today the Chinese stock market is trading at 70 times earnings – do you see some writing on the walls here? When valuations get that out of control a drop in valuations is imminent and will be dramatic. We had it here with stocks and housing recently and its part of the economic world – don't buy when valuations are out of control! Call to discuss anytime!

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Inspirational Quotes

- Reality leaves a lot to the imagination, *John Lennon*
- Genius is one percent inspiration and ninety nine percent perspiration, *Thomas Edison*
- In order to succeed, your desire for success should be greater than your fear of failure, *Bill Cosby*
- Knowledge comes, but wisdom lingers, *Alfred Lord Tennyson*
- All leaders must face some crisis where their own strength of character is the enemy, *Richard Reeves*
- Few men have virtue to withstand the highest bidder, *George Washington*



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

Kids Korner

Easter Egg Hunt

Yes it's that time of year again – the Easter Egg Hunt will be upon us in just a few months. Last year we held it on Easter weekend and there were too many conflicts so this year we're having it on March 8th. There will be over 7,500 Easter eggs hiding in my yard and the kids will have a blast scrambling to find them. Bring your child, grandchild or temporarily adopted child to our house at 2:00 for fun galore! Dress the kids to be warm and plan to get dirty – real dirty - as that's part of the fun for kids. We need adults at the hunt too. There will be a few dozen eggs hidden that can only be found through solving our live riddles – and kids just can't handle that. You're welcome to bring your know-it-all teenagers too to see if they can solve the riddles, if they're not too chicken! Here is our address:

615 Plymouth Road, Harwinton CT 06791

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