

Rewriting Regulation

The leaders today don't think ahead and lead, they simply worry about their political positioning for reelections and they write laws by reacting to what is going on. What they should be doing is the right things for the countries they run. We've recently witnessed many instances of insane new regulations attacking every aspect of society from financial markets (this is necessary) to daycare centers to healthcare. The financial industry needs to have rules to keep things safe and corporate executives shouldn't be allowed to take excessive risks and walk away with mind boggling wealth after ruining a company. The rules keep on coming, piling on top of an already excessive gamut of rules that have been piling up for decades.

To show just how ridiculous lawmaking has become, look at a few of the new rules in place in Colorado regulating day care facilities. We all want our babies to be in a nice, warm loving safe place with healthy surroundings. Let's look at just a few of the insane new laws that are now the rule of land in Colorado: Each daycare facility will have at least 2 block sets, with a minimum of ten blocks per set, children must play with said blocks on a flat building surface that is not in the main traffic area. I applaud the attempt to make the daycares safe but in reality regulators simply cannot foresee every possible scenario and at the end of the day, human discretion is what has to be in control. Common sense and personal responsibility is the only way we can have a society that is not burden by regulatory nonsense. Taking responsibility is essentially illegal in the modern regulatory state.

Let's move onto the new healthcare law. For all of the great people in the medical field we will not have a bit of complication on the billing side of the equation. We now have 18,000 various forms of billing codes that can be had for insurance reimbursement. This will increase to 140,000 if the new health care law isn't found illegal or is repealed. Let's hope both happen soon, the insanity must end somewhere. Of the new 140,000

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Unemployment

The numbers for people out of work have seemed to look real good as of late. I question the integrity of these numbers and the supposed drop in unemployment rate from 9.1% to 8.5% in a soft economy at best where the global headwinds are blowing in our collective faces.

The first and most obvious conclusion is that since the numbers are reported around Christmas season, we need to adjust for seasonal workers. Retailers and shippers are big seasonal hiring spots as they garner a large percentage of their business during the holidays. There were 42,000 couriers/delivery people added in the month. This is a monster number that will come off in January. We'll see a similar impact in retail.

What is more concerning than the seasonal situation is the way the actual unemployment numbers are being calculated from a total workforce perspective. The chart below shows the participation rate of the population that is in the workforce. Notice to the far left we have about 64% of the population that is the workforce. Fast forward a few years to 2000 and we're at 67.25% of the workforce. Since then we've digressed, losing 3% of the population that was once working and is no longer and we're back to where we were in 1984. The population is now much larger and the economy is much bigger, we should have a lot more people employed today, not less. 3% sounds like a very small number, but when applied against the American population it's a big deal.



Chart courtesy of zenbodge.com

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codes for medical reimbursements, we have 21 categories for “spacecraft accidents.” This is no joke, it is true, and we’re paying an army of administrative people in this administration to think of every way we can possibly take humans out of the equation of life. There are only 12 categories for bee stings so apparently the spacecraft accidents are a higher probability event than a bee sting. Is it me or is government in a complete alternate reality today? Welcome to the twilight zone.

The intent is to create a state where we avoid human discretion and have a regulatory code that is self-executing. The problem with it is that it’s far too complex for most people to follow and it precludes good judgment, it precludes virtually any judgment. How ironic that the court of law is all about judgment, but the law is written in such a way as to prevent it. A teacher cannot maintain order in the classroom without having to worry about paperwork, forms, lawsuits and judges. Towns and states cannot conduct business without having to worry about legal proceedings for volunteer boards and committees. Judges allow nonsensical suits to go anywhere today. Regulators shut down lemonade stands because a law is a law and the kids shouldn’t raise money for cancer.

Instead of regulatory micromanagement, what we need is outcomes based regulation with simpler rule sets tied to the outcomes they produce. Common sense and personal responsibility need to be the hallmarks of this new approach. All regulations should be up for review and expiration periodically as any good thing can eventually become out of control. A perfect example of a great thing that has spiraled out of control is special education. We need to help the kids who are disadvantaged, disabled, or struggling. Since the 1970’s introduction of special education laws, we’re no longer providing special programs for struggling students we are mainstreaming them with all of our kids. Whether it’s right or wrong can be debated for eons, but now we’re spending 20% of the total K-12 educational budget on Special Ed while we’re spending less than 1% on programs for the smartest and gifted kids. This is a big problem in the cities and less so in the country, but where do you think most of your state income taxes are spent? They’re funneled from the rural areas to the cities.

Does this really make sense? I don’t think anyone would argue it doesn’t, but the problem is that nobody is asking the question if what we’re doing makes any sense. It is time we start to think differently about how we’re doing business in government. There is a plethora of ways to improve our outcomes! ☺

Stimulus

Stimulus is when the government pours a lot of money into something to stimulate it and get it moving. In 2007 when the banking crisis boiled over, our government stimulated the economy big time because people pulled back on spending at all levels. China did the same in a big way. That was okay on a certain level and it did stop a bigger bleed, the government in America made a fortune on that. The thought is that when people stop spending, the government can spend temporarily to keep the economy running at the current clip and then when people get back to “normal” the government can pull back.

In theory this is fine and for short bursts it works well. The problem we have today is our government keeps spending more, five years later. The states are doing the same, spending more and taxing more. This is no joke, it’s become very serious. The debt problem of the governments of the world is huge and a main ingredient in the insanity in the global markets.

Just recently it seemed like Europe was about to meltdown, and the central banks of the world joined and poured another round of stimulus into Europe. In early January China is making it very well known that they’ll stimulate their economy if it slows too much. The problem is now with this entire stimulus we’ve got too much money floating around and government spending taking up north of 25% of global GDP in the developed world. This isn’t even close to sustainable and we’re in for it at some point.

The markets have become like crack addicts, addicted to evermore spending. This is just fine if it’s not borrowed money and a healthy expansion of the world, but at this level it’s the government credit cards gone awry and some countries have no chance of paying it back. There is a great YouTube clip on this very concept that can be viewed at <http://www.youtube.com/watch?v=Li0no7O9zmE>

This is a symptom of the underlying problem in the world today, fiscal accountability and living within your means from individuals all the way to governments. Governments are soon going to have no choice but to live within their means as they’re turned off from the capital markets. I’m not a big fan of lack of discipline but as time unfolds people and governments are moving away from reality financially. Much of what I was taught about economics 20 years ago in college no longer applies. Government debt was supposed to be treated as guaranteed. Now we’ve got a situation where many governments are not sustainable. Despite the general news, I’m hunkering down for the imminent storm. This is not a bad thing, it must happen, but money will be made in the shorts, not in the longs. It’ll also be very much a traders market as we will see risk on and risk off come back to a theater near you very shortly.

Noteworthy News!!!

- Congratulations to the Cassidy family on the purchase of their new home! ☺
- Our condolences to the DeFiore/Russ/Quinn families on the passing of Armand, a wonderful man, husband, father, grandfather, great grandfather, uncle and friend.
- Our condolences to the Rzegocki family on the passing of Steve, a wonderful man, husband, father, grandfather and friend.
- Our condolences to the Matava family on the passing of Robert, a wonderful man, husband, father, grandfather, uncle and friend.
- Our condolences to the Danaher family on the passing of Margaret (Peg), a wonderful woman, aunt, great aunt and friend with an amazingly benevolent charitable heart.
- Our condolences to the Sgaglione Family on the passing of Anthony, a wonderful man, husband, father, brother, grandfather, uncle and friend.
- Our condolences to the Rivera family on the passing of John's father, a wonderful man, husband, father, brother, grandfather, great grandfather, uncle and friend.

Question & Answer

Ask any financial question you have and we'll address it here.

Q: What is risk on and risk off that they've been talking about lately?

This is a general mood or feeling of the global stock markets as a whole. Risk on means people are willing to buy stocks and risk off means people are selling stocks. In the past six months we've seen a risk on risk off mood like never before. This isn't normal to see on a day to day basis as we've had lately, but the story isn't over just yet. The real drivers of what is going on are the absolute insanity in Europe, massive government debt in the entire developed world, and a general slowdown in the global economy. Political folly is much to blame as most of these issues could have been avoided if the elected dimwits stopped kicking the can down the road years ago and dealt with the real issues. My suspicion is Europe faces its day of reckoning this year and it's not going to end well. The Eurozone is the largest portion of the global economy and its getting hit hard with governments finally waking up to address some issues. The current path they're on is to try and cut spending and raise taxes. It won't work, they need structural changes in making work rules more flexible and making it easier for businesses, not government, to drive the economy. I would have hoped the dim bulb politicians here in America would see the end result of a socialist state as Europe is so clearly displaying and we'd move in the opposite direction. So far we've actually been leaning towards that model. Hopefully that ends and we tilt back to fiscal reality in the very near term or we'll be Europe in the future. ☺

Unemployment

(Cont'd. from page 1)

In 1984, the total population of the country was 235 million people. We now have 307 million people living in our great nation. The real thing pushing the unemployment number down is the people in the workforce. This is a scary piece of data as it's artificially showing a better picture than what is actually happening. In the past two months, 371,000 people have supposedly left the workforce. This number is highly suspect at best. There is no hard data on this, its survey based each month and shows overall trends. My concern is that as we're heading into an election year if we just continue to remove people from the workforce, we can get unemployment down to 5% in no time flat. This is convenient as it's all about the economy and with ours being painfully weak, a seated president has zero chance of winning. If it can be artificially "boosted" or at least appear to be so, it will give the incumbent a chance. Games that shouldn't be possible.

Since 2007, we've had over 7.5 million people leave the workforce. It's fair to say that many are retiring in this tough job environment. That will contribute somewhat to the numbers, but the youth unemployment scenario is pathetic. Combined, the overall number isn't good, nor is the overall economic picture moving forward. If consumer spending is 70% of GDP and 7.5 million people are not working that were 5 years ago, how can that be a positive factor in consumer consumption? It can't!

Corporations have been running lean and mean for a long time. They have shed employees, cut costs and moved facilities and operations all around the globe to gain a competitive edge and cut expenses. There isn't much more that can be gained in terms of efficiency and inventory levels are historically low. When inventory is low, profits look huge because sales are there and you're not replenishing inventory. Moving forward, companies will either replenish inventory if sales remain or they'll keep them low if sales decline, but either way the bottom line profit figures will go down.

The Bureau of labor statistics says we have 13.1 million people currently unemployed in America. If we factor in some of the 7.5 million who aren't working since the great recession, with 2.5 million out of work in the construction field alone. This is a huge driver of our economy and it's a structural change, it's not coming back anytime soon. Housing isn't done with the bleed five years after the climax. We're probably a year or two away from a bottom and then we'll see a reversal of trend, but a very slow one.

If we factor in the more accurate reflection of the workforce, we have a current unemployment rate in excess of 11% and one trending up, not down as the government would like you to believe. You can peruse the document online that I'm deriving this data from at the following address: <http://www.bls.gov/news.release/pdf/empsit.pdf>



Money Quiz

What is the amount (expressed as a %) bond investors typically recover if a sovereign entity (Government) goes bust and you lent them money by buying their bonds? Last month's winner was Bob Johnson, if the unemployment rate goes down 1%, 1,542,000 people go back to work. The winner will enjoy a meal on us at Ruby Tuesday. © 12/12/11:6

The States are Boxed In

High cost states such as CA, CT, NY, IL, etc. are all in a box that they've painted themselves into. They're very tax and handout heavy. In the past few years they've taxed everything imaginable and people are irate. Many people move with their feet and relocate to different states where the tax climate is friendlier. You cannot blame them; it's become insane at these levels today with what government thinks it is owed and deserves.

The most recent rub is an expansive increase in the earned income tax credit (a fancy name for a welfare system that gives tax free money to certain people from the state who pay zero income taxes – the feds already do this but it's just not enough of a handout) while confiscating more and more from the productive class. This is wealth redistribution at its finest and the working people are pissed off. Now monster corporations are moving out of these states to get away from government stupidity. Governments are responding with sweetheart deals for huge employers because their policies are so bad big business leaves without them. Illinois has granted over 200 million in tax breaks to the Chicago Mercantile Exchange, Sears, Caterpillar and Motorola. Connecticut has done the exact same thing for Cigna, ESPN, NBC, etc.

The box the states have put themselves in is this. We'll tax and spend you to death unless you have the capacity to leave, then we'll give you a sweetheart deal to stay. Sadly, those getting the deals don't need them, they can comfortably afford to pay, but why should they when they can just move their headquarters to another place and keep the loot! The states attitude is that for everyone else, you're just out of luck. They fail to see how many people are moving out of taxation insane places to more tax friendly destinations.

Taxes kill jobs, they don't create them. Taxes make it more expensive to hire and build businesses. The dim bulb running CT has recently signed a bill so daycare centers can unionize in this state. As if the cost of taking care of your little prince or princess isn't high enough, it's going to get a lot higher after this act of genius. Taxifornia is proposing a 7% increase in spending this year when they've already got a 10 billion dollar budget hole. Is it just me or is there a serious failure of simple mathematics going rampant in government?

Crossroads

People focus too much on the negatives in the world and it brings their spirit down. You cannot control the world; you can simply see where you fit into it and impact it as best you can. We've reached an economic and political tipping point and people are quite sad lately. There is no need to be this way. There are certainly plenty of problems to focus on with the state of affairs in the world today, but don't be fooled, these big problems also create big opportunities. We're in a unique place in the world right now in that we can capitalize on things either way. Many people think we need constant good news to do well in the world. Nothing can be further from the truth. In investing, we just need to know the general direction of things and from there it's an easy process to make money. We can make money going long when things appreciate. This has been the focus of our investment thesis for many years, we've never had much trouble finding something that was really cheap and giving it ample time to appreciate was a relatively simple thing to do.

Now with the downward economic, political and debt pressure on the world we've become much more focused on the shorts. The shorts are opportunities to make money from a decline in prices. There is little doubt prices of many things will decline this year. The decoupling of price and reality that has hit in the past few months will come back in line; it's just a matter of when. Our indicators have been giving us mixed signals for some time so we continue to be defensive, waiting for the best opportunity to capitalize on the coming shifts. This short position period will come and go in the coming months, and in the aftermath of it we'll have another great period where things are healthy and we build sustainable prosperity from there.

As we assess the situation of the globe and our spot on it, most of us should be thankful for where we are and what we have. If our biggest worry is the economics of the world we're blessed in many ways. Many struggle with family, health or other much more important issues. I thank God every day for where I am, despite this being a very tough economic period in the world for anyone in the financial business. I had a conversation with a buddy at Bloomberg recently and he said he's getting a fax each and every day of over 200 people who are being laid off in the investment business. These people use his system and part of his responsibility is to keep the subscription base up for his employer. It's a shrinking business for sure in finance as the world adjusts to a lower risk, higher regulated model. Most people I know think I'm insane for being in this business and I probably am, but I love it. The more complicated it gets the better. It's just a matter of getting a feel for the systems, knowing values and seeing where you can safely pick your spots. The game is certainly changing recently, but with that change also comes great opportunity. We must be patient and not get fooled by the mood of the world, but there is much to look forward to in the world. We're all on the planet together, so let's work for one another and make life better for everyone.

Inspirational Quotes

- There is nothing either good or bad, but thinking makes it so, William Shakespeare
- A man sees in the world what he carries in his heart, Johann Wolfgang Goethe
- No one can make you feel inferior without your consent, Eleanor Roosevelt
- Who do nothing at all make no mistakes....but that would be a mistake, author unknown
- Failure is only the opportunity to begin again ,this time more wisely, anonymous
- The only job where you start at the top, is digging a hole, anonymous
- We are confronted with insurmountable opportunities, Pogo
- If your ship doesn't come in, swim out to it, Jonathan Winters



**We can piece the puzzle together
and make your money work for you!**



Who's in Charge?

Kids are kids of course but at what level do we have to draw the line in the sand? I recently had a conversation with a lifelong friend who is a police detective and we discussed how many children today have effectively gained control of the household they reside in. They manipulate the parents, wear them down and keep begging and pleading to get their way. After enough of this, parents let things go. Little things at first, but then it evolves into bigger and bigger problems as time unfolds and the kids grow up. The parents are buried with work, house and family obligations so it's easy to let seemingly small things slide. It's always easy to look the other way, but at what price will that ultimately come? We need the kids to be respectful of the parents, especially the grandparents if they're around. The earlier the kids get the message that they must listen and do what they're told and be responsible for themselves and their actions, the better. It's sad for me to hear that today a large percentage of police work is nonsense with kids that won't listen, are incorrigible or otherwise disruptive. This all comes down to personal responsibility and the breakdown of the family unit. I hope and pray this trend reverses itself.

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