

the **BENEDICT** REPORT

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OUR COUNTRY NEEDS TIME TO HEAL...!

THE CRASH OF THE CENTURY!

Cars of all shapes and sizes are zooming down the freeway. Among the throng are a few idiots who don't seem to know what to do and a group of jerks who seem to care little that they are endangering everyone else.

The speed of the traffic is just too dangerous and something bad is bound to happen. Those who may have at least some power to slow the insanity to a more realistic pace seem too self absorbed.

Then the nightmare happens. An idiot and a jerk collide and cars and trucks are ramming each other, some are flipping over, broken glass fills the air. The accident of the century just happened! The freeway will be shutdown and the mess will have to be cleaned up. It will take some time and create massive stress for everyone involved.

It seems to me our economy (the freeway) has been devastated by the accident of the century. Everyone was driving way too fast (too much debt) and then some idiot (think Fannie Mae) and some jerk (think Wall Street) collide and create a collision that causes massive personal injuries (think job loss) and enormous wreckage (think foreclosures). It is the mess of all messes!

If you were in this accident (I think we all were), but were lucky enough to not be critically injured, do you think you may still be a little gun-shy about driving again on the freeway for a few months? Do you think when you started to venture back on the highway you would stay in the slow-lane for a few more months?

I believe our leaders, with all good intentions, are trying to stimulate our economy (increase speeds on the freeway) a few months before we are over the trauma of the accident, thus we are not ready to be stimulated.

At this point, we need our injured taken care of and our cars repaired.

GET READY FOR MORE REALLY UGLY NEWS!

I believe we are going to encounter even more bad news over the next three months, especially the cover story news. Corporate bankruptcies (retail stores, home builders, auto dealerships and more bank closures) and more massive layoffs will dominate followed very closely by home foreclosures and personal bankruptcies. And, possibly, the bankruptcy of a few cities. I expect it to portray an ugly story of what has happened.

It also appears that, buried deeper in the news, we will start hearing or reading about some good things. I think this news will be more accurate in portraying what is likely to happen in the future, but it will not be good enough to crowd the what-has-happened off the front page. In some areas, housing prices will stabilize and some companies will start selectively hiring again...time will tell.

It is difficult for most of us to understand, but recessions are critical to a strong, vibrant economy. Assets, including money and people, are re-allocated from weak companies to strong companies. From companies focused on yesterday to those who are creating tomorrow. From companies that were run for the benefit of upper level employees to companies focused on their customers, employees and shareholders. Like the former athlete, who needs to

lose fifty pounds of fat created by *the good life*, the process of leaning down and getting in shape again is painful...but necessary to thrive in the future.

The impact of this needed recession has been amplified many times over by the mortgage/banking/ brokerage/credit crisis. It is not pretty and many, many families are really suffering. I wish it had not turned this brutal, but it has. Please be empathetic and provide what support you can to those who are struggling..

They Still Don't Get "IT" - Do They?

I open the paper and see a full-page ad in the *Financial Times* by the largest bank in the country telling how ***"We're taking the trust and faith that America has put in us and getting to work..."*** (Whatever that means, I have no idea.) Later the ad offers, ***"But, at its core is this simple fact: families in America trust more of their hard-earned money with us than any other bank."*** Besides, why is the bank spending money advertising how much good they are doing...just go do it. (And, please don't just spend it on lobbyists or bonuses for executives or traders.)

In late 2007, after losing almost \$10 billion, Merrill Lynch paid its employees bonuses totaling \$14 billion. Said its CEO: "I want to reiterate how strong most of the businesses have done this year, and we are very optimistic as we look out to 2008." Just a few weeks later, Merrill announced additional losses, totaling \$16 billion. The combined write-off for losses taken on investments made between 2004 and 2008 equaled more money than Merrill Lynch had ever earned – in total.

On top of all these losses in 2007 and 2008, and after telling investors half a dozen times that it sold all of its toxic assets, today... incredibly... Merrill announced yet another enormous loss – \$15 billion – an amount beyond what Bank of America could afford after acquiring the company for \$50 billion.

At the end of 2007, the five largest U.S. securities firms paid their employees \$66 billion in bonuses. All of it came from "profits" that we've since learned were horrendous losses..."

[Source: S&A Digest, January 16, 2009]

P.S. Why would anyone continue to do business with them?

Here are two more stories and they don't get any better. "One bonus beneficiary started at Merrill in mid-September and quit December 18th. He walked away with a \$24.9 million bonus..." [Source: New York Daily News, February 11, 2009]

"The top four bonus recipients received a total of \$121 million..." [Source: New York Times, February 12, 2009]

A reporter for *Investment News* [January 26, 2009] asked one Merrill Lynch broker what he felt like knowing the bonus he was receiving just to stay with the firm (retention bonuses they call them) may have come from taxpayer funds. "We are also victims; we suffered huge losses on our Merrill Lynch stock."

P.S. The brokers/banks are paying millions of dollars of retention bonuses to keep their sales people with them. Maybe, if they had run a good operation, everyone would not be in a hurry to leave.

"The fall of Boaz Weinstein, once one of Wall Street's hottest traders, speaks volumes about why financial firms still are reeling from the shattered global markets.

"As a chess master, poker and blackjack devotee and top trader, Mr. Weinstein made big bets, using complex financial instruments with borrowed money, generating large returns for the bank, and about \$40 million in annual pay for himself. But in 2008, he saddled the bank with \$1.8 billion in losses..." [Source: Wall Street Journal, February 6, 2009]

P. S. Sometimes I think I have drifted to another planet. This guy was making \$40 million a year doing something that closely resembles video games. He didn't discover a cure for cancer, he wasn't in poor neighborhoods trying to save some residents from a life in prison, he didn't invent the Internet or a car that creates its own fuel...he traded some financial "things" that few people can understand or care to understand with borrowed money. I know, I know...movie stars and professional basketball players may make this kind of money and what do they contribute to society other than juicy news tidbits? But, sometimes I still think I must be on the loony side of Mars.

P.S.S. Don't feel too sorry for Mr. Weinstein, he is now unemployed but is in the process of starting his own hedge fund. (A hedge fund is basically an un-regulated investment fund that is available only to investors who meet certain net worth and income requirements.)

[As I was writing this, a solution to the whole problem came to me out of the blue...but I think it's a good solution, so here it is:

- ◆ These Wall Street brokers/bankers seem to think they have to be paid outlandish bonuses.
- ◆ Their employers have a big load of mortgage backed bonds (pesky black bags for our readers) that they are now trying to "sell" to the government to get them off their books.

The solution: Simply give the employees their bonuses in "bonds" instead of "cash."

While I'm on this topic, I hinted at this in an earlier *Report*, but I do believe you are witnessing the end of Wall Street as we have known it. It killed itself due to obesity and arrogance - just like the steel industry killed itself in the mid-70's. The auto industry followed and killed itself in a more slow and agonizing way, but death, at least, as they see themselves, seems imminent.

The fat and arrogant steel companies and their workers thought they were too strong to fall. Then, as they started falling, they headed to the government to impose quotas and tariffs. By the late '70's, the auto industry was feeling the heat of Japanese imports, so what did they do...go to the government for some quotas and tariffs. But, neither of the industries really changed anything, especially their attitudes. About that time, power started switching from the manufacturing sector to the Wall Street financiers.

Twenty-some years later, we are witnessing an industry that considers themselves the *chosen few* and can do no wrong and are worth more for one year than most Americans will ever make in a lifetime.

The power is leaving Wall Street. Not because our elected officials no longer want their lavish campaign

contributions, but because the people are fed up and their representatives are learning this or will learn this or will find it much more difficult to be re-elected.

The power is coming to Main Street!]

HOW CAN YOU BE SO POSITIVE?

Written: February 7, 2009

"The world seems to be falling apart and yet you seem to be so positive. Is that how you really feel?"

Recently, we have had a few people question our positive outlook or, maybe, question our sanity. We are positive about the future, but please do not think we are totally unaware of the problems that are out there.

First of all, there are always problems and, if it doesn't seem as though there are big problems, then there will soon be big problems. It is the nature of life. We, as individuals and as a group of people, are constantly enduring the challenges of life; our finances, our eating habits, our family, etc.

But, rather than getting too philosophical about all of this, let's go back to investing in the stock market...which, in case you haven't paid any attention, has been providing plenty of challenges over the last year or so. Is the stock market real? Let's look:

You read the headlines that the share price of XXX Company is down 25%. Wow, you think, that company is in trouble. You hear that YYY Company is laying off 2,000 employees. Wow, you think, that company must be in trouble.

Let's look at two companies that have seen their revenues slow down and have reduced their work force and see how they seem to be doing.

Company A - Global industrial company that just announced they are laying off 14,000 employees, which is almost 10% of their total workforce. It is well diversified, but primarily known as a manufacturer of backup power equipment for telecom, climate control components and electric motors. This is not an exciting company and one that we would think is quite sensitive to the global economic conditions. Let's look at how this company has done recently.

Stock share price since the 2007 peak	-41%
Stock share price since January 2002	-18%
Dividends change since 2002	+71%
Total revenues change since 2002	+60%
Net Income change since 2002	+137%
Cash on hand change since 2002	+399%

Source: Standard & Poor's Advisor Insight

It is pretty easy for us to think positively about **Company A** if we focus on its operations, even if we accept that this economic slowdown will slow their revenue growth. It is not easy to think well of the company if we merely focus on the change in the share price...down 41% since last year. But, do remember that public confidence and attitudes, frequently, have more to do with the short-term share price of a stock than a company's operations.

There are hundreds of companies with strong cash positions, growing revenues and bright futures just like there are way too many financial companies that are now hollow shells being held together with government band-aids. Learn to tell the difference.

Company B - Diversified global company in electronics, health care, consumer, office, safety and security markets. Let's look at how this company has done since January 2002:

Stock share price since the 2007 peak	-46%
Stock share price since January 2001	-6%
Dividends change since 2001	+67%
Total revenues change since 2001	+55%
Net Income change since 2001	+75%
Cash on hand change since 2001	+266%

Source: Standard & Poor's Advisor Insight

Company B seems to be hitting on all cylinders, but its share price is 46% lower than it was last year and below where it was eight years ago. We believe this company has the ability to generate good cash-flow and profits in the future; we also believe that someday the market will more accurately reflect this. You may notice that both **Company A** and **Company B** make real things. They do not spend their energies trading incomprehensible financial gimmicks. Watching companies like this make us optimistic about the future.

We mentioned in January's *Benedict Report* that the really big economic problems are centered on the industries that were relying on very easy credit...namely: housing, automotive, banking and retail. Outside of those industries, there are a lot of powerful companies that are making money, have low amounts of debt and look as though they will continue to make money for many years in the future rewarding shareholders with rising dividends and, probably, increased share prices along the way. See, it's quite easy to be optimistic!

WHAT SHOULD WE DO?

Written: February 8, 2009

I'm writing this before the stimulus plan has been formally approved, but it really doesn't have anything to do with that. And, I'm not writing this to be critical of our leaders in Washington, D.C. as it certainly seems as though they are trying to help us. I'm just sharing some of my thoughts with the hope they will help you understand what I think is happening in our world today and, maybe, inspire you to think outside the box a little yourself.

This economic wreck left almost all of us emotionally bruised if not battered, even if we have not been physically hurt. We need a little time to get over that...almost like the grief of losing someone close to us. We don't need our taxes cut by \$500 or someone to send us a stimulus check of \$500 to spend on crap. Right now we are just not in the mood to buy the things we were buying a few months ago. I realize this doesn't help Panasonic or J.C. Penney, but that's the way it is. We will change, we

will put the accident behind us and, in a few months, we will resume buying a bunch of stuff we don't really need, but you have to give us a little time.

Once our emotional state starts to heal, then we will need to feel confident about the future. Here, I fear our government may be giving the wrong signals.

I believe we can help the less privileged without pulling down the financially successful and productive part of our society. We have to or it won't work. And, we have been giving the wrong signals to the financially successful. Let me explain:

The financially successful are worried not about eating tonight, but about tomorrow, next year, next decade and beyond. They realize that much of the mess we are in was the result of uncontrolled spending by governments and households. They also know that it is they, the financially successful, on which the burden of solving the problems created by others will fall. To help restore their

confidence in the future, we don't need more uncontrolled spending, which is likely to result in higher taxes and inflation...taxes which will be paid by the financially successful and inflation which will erode their savings while it benefits the debtors of our society.

Fear of higher taxes will cause the financially successful to spend less. Talk of using their wealth to help the poor makes them save more because of fear their social security benefits and pensions will be reduced. What are the financially successful thinking?

- ◆ I don't think the financially successful are asking for reduced taxes.
- ◆ I don't think the financially successful are asking for special privileges.
- ◆ I don't think the financially successful like what happened at Wall Street or Fannie Mae or the Rating Agencies, etc. any more than the rest of the population.
- ◆ **I do think** the financially successful want the government to take control...not control of private industry, but control of their own spending. The confidence of the financially successful in the future is critical to the success of our economy and our government needs to formulate not a plan to stimulate a dazed economy but the steps towards fiscal prudence.

I do believe we need to provide assistance to those who need it; however, we must remember that it is unlikely that a poor person is going to give you a job.

Who do I consider *financially successful*? It may be the millionaires and the multi-millionaires, but not all millionaires, because if they don't have their spending and debt under control, they aren't financially successful. A retired couple living modestly, but comfortably, may be considered successful as would the couple down the street who lives a much higher lifestyle but one they can easily afford. The financially successful are all of us who have taken personal responsibility for our financial future.

And, I think many people in our society who are struggling right now due to something within their personal control or due to outside circumstances will resume being financially successful after they work through their current dilemma. The wreck-of-the-century was really rough on them and they need time to rehabilitate their lives, but many of them will come back stronger than ever.

I mentioned in the freeway story that we need **care** now more than **stimulus**. Instead of complicated

government programs, I would offer three steps that could be implemented quickly and easily that I believe would provide us a little time to heal.

The 50% Off Mortgage Program: During the year 2009, every mortgage holder in the country can elect to pay only 50% of her/his mortgage payment each month and not fear the mortgage holder will initiate foreclosure proceedings. This would give the system some time to work out the bigger problems. It would also be more "fair" to the mortgage holders who are making their payments, because they get the same offer. (It is not a free lunch because it doesn't change the overall mortgage, but it offers lower payments for twelve months. (This program should not cost the government anything.) And, if someone can't pay 50% of their mortgage payment, it is unlikely they are going to be able to keep the house anyway.

Extend and increase the Unemployment Benefits: This is simple and probably part of the stimulus plan. There is a cost to this, but it seems to me this money would help those who need it the most and would also be used to stimulate the economy.

Modify the Mark-To-Market rules regarding the assets held by the banks as reserve capital. This says each bank must value their assets at the close of market price for that day. This sounds wholesome and, in general, I agree with it; however, let's give them a little slack for twelve months and give us time to examine alternatives. This was previously required in the 1930's and many claim that strict adherence to this concept exacerbated the economic problems of that era. (There would be no governmental cost to this change.)

Beyond that, Mr. Government, we as a people promise to get our financial affairs in better order and we need you to do likewise. It will assure us a prosperous future and assure you of being re-elected.

Thanks for reading...!

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