MICHAEL COLEMAN, PH.D.
Registered Investment Advisor
RETIREMENT INCOME SPECIALIST

2124 Main St., Suite 170
Huntington Beach, CA 92648
Tel 714.960.2316
800.660.8727
Fax 714.960.0589
mdcoleman@unitedplanners.com
www.michaelcolemanphd.com

Searching For The "New Normal"

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Many financial experts radically disagree about the general direction of the economy in the near and distant future. Their debates include the following questions: Will we have deflation or inflation? Is the current stock market recovery the beginning of a new bull market or just an episode in a continuing bear market? How bad will unemployment get? How long will it last? When will the Real Estate market recover? Above all, how soon will we get back to "normal?"

Alternative answers to these questions frame dramatically different economic futures. John Maudlin has coined the term "the new normal" to capture the essence of what is going on, namely, that we will not be getting back to an economic situation any time soon that looks like financial markets of the past 10 years. We can now see that as a nation we have been living beyond our means on borrowed money. Our national government has run enormous deficits for decades, our state government has used accounting tricks for years to conceal its overspending, and the majority of our population has borrowed against their homes and their credit cards to sustain lifestyles they otherwise could not afford. A recovery will not allow the same level of unsustainable spending that we were used to. Rather, the future will have to be reset at a "new normal."

Some features of the "new normal" are already becoming apparent, and others are yet to be revealed. Many changes are healthy and welcome, such as a new interest in sustainability and conservation for economic reasons, not just environmental concerns. Conspicuous consumption is out, and frugality is in. According to the Wall Street Journal household debt actually decreased for the first time since 1953![1] The Bureau of Economic Analysis reported that the personal savings rate reached a 15-year high of 6.9% in May which is the highest savings rate since 1993.[2] This compares to 2004-2007 when people tapped their home equity and credit cards in order to live beyond their incomes, and the saving rate averaged only 0.6%.[3]

The transition to the "new normal" will be extremely painful for many people. I believe high unemployment rates, work furloughs, and foreclosures will continue for some time. Lower wages for many people will bring lower standards of living, and some elderly will be working longer due to portfolio losses in retirement accounts. Certain jobs may be lost forever resulting in dislocations for many families. There are also important implications for our investment strategies as business earnings remain uncertain and high market volatility is likely.

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As you know, we have insisted on building safety features into your accounts by using income guarantees, fixed annuities, and money managers who employ tactical allocation strategies. More recently I rolled out my new Risk Management System to better protect you during volatile times, and to be nimble enough to take advantage of occasional short-term opportunities. So far I feel these systems are demonstrating their value even though past performance is no guarantee of future results.

Update on High Yield Bonds

At I wrote to you last quarter, my analysis judged that high yield bonds were dramatically undervalued. In light of that judgment, I made significant allocations to high yield bonds in your investment programs with a high yield bond option. In my opinion, this has been a very profitable move so far. High Yield bonds as an asset class were up 23.19% for the quarter and 29.37% for the first half of this year.[4] This compares favorably with S&P 500 which had a lot of excitement but little in the way of profits year-to-date. In spite of a dramatic 2nd quarter recovery, the S&P 500 was up only 3.16%, and the Dow Jones Industrials were still down -2.01% as of June 30![5]

For now we are staying with our nimble strategies and we hope to adapt ever more to the "new normal" as it reveals itself. Please contact me with any questions or if you have life changes with investment implications. Thank you for your referrals; we are still accepting a few new clients.

Michael Coleman, Ph.D.
Registered Investment Advisor

The views expressed are those of the author as of the date noted, and are subject to change based on market & other various conditions. They may not reflect the views of United Planners Financial Services of America.

Certain risks exist with any type of investment & should be considered carefully before making any investment decisions. Keep in mind that current & historical facts may not necessarily be indicative of future results.

[1] *Wall Street Journal*, January 6, 2009
[2] *New York Times,* June 26, 2009
[3] *Wall Street Journal*, January 6, 2009
[4] Merrill Lynch US High Yield Master II Index
[5] Morningstar