



July 29, 2011

Your Future Part II – The Debt Ceiling Debate

In my last letter, I gave you a brief history of the United States Constitution and the clause referring to balancing the budget and the need to borrow money through the US Treasury. I held up sending that letter in the hope that some significant headway would have been made by our “elected” officials in Washington, DC, but alas that was not to be. Well, I have once again held up writing the July letter in hopes that an agreement would be forged, but it has become very clear that the powers to be in the nation’s capitol have differences far wider than the Potomac River.

If you recall, I stressed the need for agreeing on the debt ceiling and trimming the budget by more than \$2 trillion, but I also noted that to do so required strong medicine in the form of tax increases and elimination of some entitlement programs. Tentatively agreed upon or proposed are; slashing \$400 billion in tax cuts for oil companies, a cap on deductions for families earning over \$250,000, trims to farm subsidies, the Pentagon and increased contributions from federal workers. Of course, cuts to Medicare and Medicaid are also being pushed. Hold that thought as we’ll come back to it.

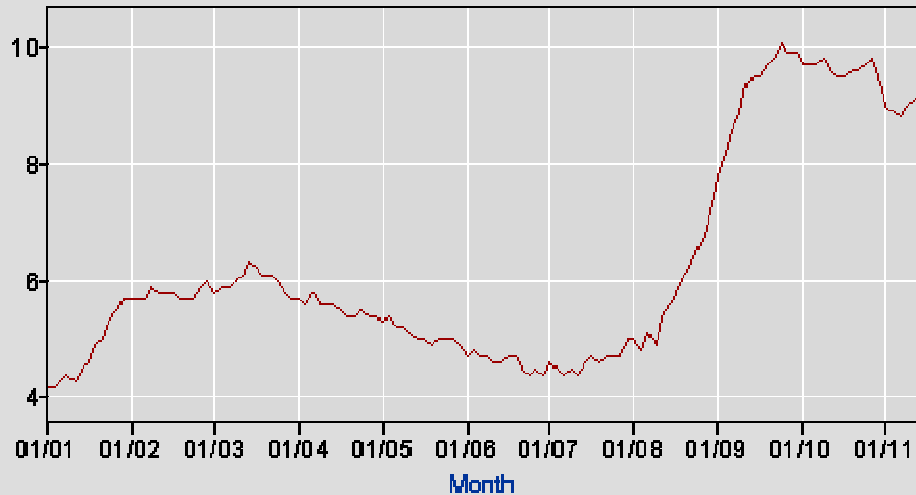
On July 8, the Bureau of Labor Statistics (BLS) released its monthly figures on employment. While the media seems to pay more attention to the unemployment rate (9.2% up from 8.9%) the key number to watch is the number of new jobs created, which rose by a meager 18,200. The markets, having expected a number closer to 200,000, were aptly disappointed and this reflected in the S&P Index and Dow Jones Average that day and the next three days. Coupled with the debt issues in the European Community - namely Portugal, Ireland, Italy, Greece, and Spain (PIIGS) again as high-lighted in an earlier letter - investors are mired in a trading range.

This is further complicated by the apparent slowing of growth in the US, although Federal Reserve Chairman Ben Bernanke did state unequivocally that the Fed would take immediate steps to assure domestic growth. Said steps would most likely come in the form of added stimulus, i.e. a third round of quantitative easing or better known as “QE3.” What takes place here is that the Fed acting in its role as the Central Bank would purchase debt (US Government Securities) directly from the Treasury (issuer of ALL US debt) and thereby decrease the flow in the public’s hands and, as a result, temporarily cap US debt.

But the big story here is the employment picture. History tells us that no sitting president has ever been re-elected with an unemployment rate greater than 7%. The one exception was Ronald Reagan, but the rate had been falling for four consecutive months and continued to do so after the election. Clearly the battle lines are drawn, but more importantly is that the focus be on resolving the debt issue, spurring the economy and job creation. If we can get the unemployment rate down, that would be a major component in the overall economic growth picture.

Labor Force Statistics from the Current Population Survey

Series Id: LNS14000000
 Seasonally Adjusted
Series title: (Seas) Unemployment Rate
Labor force status: Unemployment rate
Type of data: Percent or rate
Age: 16 years and over



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Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
2001	4.2	4.2	4.3	4.4	4.3	4.5	4.6	4.9	5.0	5.3	5.5	5.7	
2002	5.7	5.7	5.7	5.9	5.8	5.8	5.8	5.7	5.7	5.7	5.9	6.0	
2003	5.8	5.9	5.9	6.0	6.1	6.3	6.2	6.1	6.1	6.0	5.8	5.7	
2004	5.7	5.6	5.8	5.6	5.6	5.6	5.5	5.4	5.4	5.5	5.4	5.4	
2005	5.3	5.4	5.2	5.2	5.1	5.0	5.0	4.9	5.0	5.0	5.0	4.9	
2006	4.7	4.8	4.7	4.7	4.6	4.6	4.7	4.7	4.5	4.4	4.5	4.4	
2007	4.6	4.5	4.4	4.5	4.4	4.6	4.7	4.6	4.7	4.7	4.7	5.0	
2008	5.0	4.8	5.1	4.9	5.4	5.6	5.8	6.1	6.2	6.6	6.8	7.3	
2009	7.8	8.2	8.6	8.9	9.4	9.5	9.5	9.7	9.8	10.1	9.9	9.9	
2010	9.7	9.7	9.7	9.8	9.6	9.5	9.5	9.6	9.6	9.7	9.8	9.4	
2011	9.0	8.9	8.8	9.0	9.1	9.2							

You will note from the previous chart how this statistic is a lagging indicator as the unemployment rate was still below 6% at this time in July 2008, three months “after” Bear Stearns was forced to close and well into Lehman Bros. and AIG’s demise.

Just this morning (July 29) President Obama urged a bipartisan agreement on raising the debt ceiling saying that the plan now under consideration in the House is the uncompromising view of a single faction and “has no chance of becoming law.” It is our belief that the gap between the two parties is so wide that the odds are against them reaching a resolution beyond merely

agreeing upon raising the debt ceiling, or in real terms, simply tabling the issue to allow for more debate.

One thing is certain as to the ongoing battle over the debt ceiling and budget; the global (remember this is NOT just about the United States) markets will remain nervous and volatile as long as this conundrum remains unresolved and it will become emphasized as the deadline* of August 2 draws near.

We truly respect and are happy to hear and read client interaction about our economic forecasts and investment methodology. The entire premise of CIG's model is based upon diversification and thusly to insulate assets from market volatility and the catastrophic events witnessed and endured through 2007-2009. As always, we are here to answer your questions and provide you 'white glove' service for all your financial needs.

Sincerely,

A handwritten signature in black ink, appearing to read 'Richard Gonzales', written in a cursive style.

Richard Gonzales
Chief Operating Officer

*The "deadline" repeatedly discussed by the media is, in actuality, as of today's date as the flows of funds (mainly tax receipts) into the US Treasury is nearly impossible to precisely predict. What we do know is that there is presently enough money to cover US debts at least up to August 2, 2011, but it could actually be pushed back as far as August 15.