



Volume 4, Issue 9

The (not so) Almighty Dollar

September 16, 2010

Monthly Newsletter and Update

Dear Friends, Clients and Others,

Next month in these pages we will begin to discuss the conclusions of our review of our allocation decision process incorporating what was learned from the financial meltdown of 2007-2009.

Starting next week Johnelle and I will be reviewing all client portfolios, so those paying for our services get the benefit of our thought before those of you picking up free advice via newsletter have a shot at the conclusions.

One of the by products of our review is what may be a permanent state of low grade depression in your faithful servant and scribe. It is hard for me to be optimistic about the future of our country. I doubt that I will ever recover from the shock and disappointment caused by the greed and stupidity of those running large banks, brokerage firms and insurance companies or the depths of the fecklessness of federal bureaucrats and politicians.

On the other hand, as one of my favorite clients said to me some years ago when I was fretting about climate change, "We always seem to find a way to muddle through these crises."

Johnelle, my strong right arm for three years, has moved to Florida. She will continue to be an important part of my practice. Unfortunately her presence at client meetings will be less frequent or via Skype.

Best regards,

Jeff Sprowles, CFP®



Late Quarter Update

- S&P 500 – domestic large cap
 - 6/30/ to 9/15 9.06%
 - Trailing 1 year 9.65%
- BarCap Intermediate Gov Bonds
 - 6/30/ to 9/15 1.51%
 - Trailing 1 year 6.36%
- 90 Day U.S. Treasury Bills
 - 6/30/ to 9/15 0.04%
 - Trailing 1 year 0.12%
- MSCI Emerging Markets
 - 6/30/ to 9/15 16.05%
 - Trailing 1 year 15.14%
- Jeff's Current Stock Outlook:
87.5% of Target*

* "Target" refers to the percentage of a client's overall portfolio that should be in stocks. If a portfolio has a 60% target, at 75% our goal would be to have 45% in stocks at the moment.

WHAT'S NEW?

ELD — WisdomTree Emerging Markets Local Debt ETF

In spite of my long term dislike of pooled fixed income securities I am beginning to buy ELD.

It owns a basket of bonds issued by governments of emerging market nations.

This ETF is not without risk. It is only a few months old and the ratings of the holdings are similar to a domestic junk bond fund.

I like it anyway. It has more than \$200M in it so I am not concerned about it being orphaned. Apart from 5% in Russian bonds, I am comfortable with the soundness of the governments whose bonds it owns.

Finally, it has a yield of over 4% and potential for gains from currency changes.



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MARKET COMMENTS

The market has been up since Labor Day. There is a significant difference in the P/E of the S&P 500 between TTM (trailing twelve months) at over 18 and forecast 2011 earnings at under 14. Using either ratio, the implied yield compared to that of 5 year Treasury bonds is in the 10th decile of my fifty year data base.

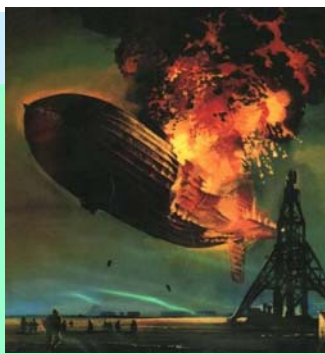
I have been concerned about interest rates for at least 18 months. Even a broken clock shows the right time twice a day. Inevitably, my concern will be justified. In the meantime clients and readers of this newsletter who sold their junk and long bonds missed some yield. That said, I think we are close to the point that rates will go up and when they do staying short in fixed income funds and portfolios will be the place to be.

My 100% evaluation of investment allocation is almost complete. My conclusions are not positive for our country. It is likely that exposure to domestic stocks will be reduced in favor of other developed countries such as Germany and Korea.

I am cautiously optimistic about stocks and am moving new money toward the current 87.5% target with alacrity.



FINANCIAL FABLE



History is open to different interpretations. These financial fables are based on two historical events. We welcome comments via e-mail if any readers care to offer differing accounts of what happened.

FABLE 1 – A Monopoly on a Natural Resource

In the 1930s the United States had a near monopoly on helium. For political, economic, military or other reasons we refused to sell enough helium to Germany for them to use in dirigibles. Therefore, they used hydrogen even though it is more inflammable than helium. This contributed in no small part to the disaster of the Hindenburg at Lakehurst and the subsequent demise of lighter than air transportation.

FABLE 2 – Currency, Reserves and Debt as Weapons

At the end of World War II Great Britain was financially strapped. To stave off a ruinous inflation or bankruptcy the U.S. loaned Great Britain \$3.75 billion. At 1946 rates this was £930 million.

In 1956 Israel, backed and encouraged by Great Britain and France, invaded Egypt to take control of the Suez Canal. This had Cold War implications that President Eisenhower and his advisors thought were contrary to the best interests of America.

President Eisenhower urged Great Britain and France to back off. According to one interpretation, when they resisted, President Eisenhower threatened to destabilize the British pound by dumping the U.S. held British debt and reserves of hard currency. Anthony Eden felt it prudent to submit to the U.S. wishes and the subsequent withdrawal from the Suez Canal was interpreted as a humiliation to Great Britain and hastened the end of Eden's career.

Some say that the Suez crisis of 1956 was the final note of the great British Empire. This decline may have been triggered by Britain's entry in World War I, which at least some historians believe was unnecessary. World War I destroyed the bulk of the Royal Army. The political poison of World War I lingered for two decades and erupted again in World War II which further impoverished Britain economically and militarily. Suez may have been the final act as a major power.



LESSONS

Recently there have been reports that the U.S. military has concerns because China has a monopoly on certain types of minerals known as rare earths. These materials are vital to the manufacture of certain weapons systems.

As of June, 2010 China owns \$843.7 billion of U.S. Treasury securities. Ironically, United Kingdom owns \$362.2 billion of U.S. debt..

At the end of World War II the British national debt was £24.7 billion which was 250% of GDP. The amount owed the U.S. at the time was approximately \$4.34 billion which at \$4.03/£ was £1.08 billion. This was 4.4% of the debt.

China owns about 6.4% of U.S. government debt as of 6/30/2010.

If I were Aesop I suspect some aphorism about having to pay for our mistakes would be the conclusion of these fables. I am not Aesop. I will content myself with wallowing in depression.



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