The CJ Investment Newsletter

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Trust, Society, Government, Investing & Gold

Purpose

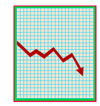
This is a reissue of previously disseminated information.

The *CJ* Investment Newsletter deals with the entire spectrum of securities investing, including cash (money market funds), bonds, equities and options. It will evaluate the overall investing environment and then discuss the relative allocations of these asset types, as well as strategies to implement within them. Essentially, it reflects what I'm actually doing with my clients.

These letters are not sent "cold." Either I know you or someone you know gave me your name. Yes, this letter *is* a sales tool. It communicates how I apply my investment strategies, so that you can decide, without any sales pressure, if my thinking is compatible with how you want your money invested. If you're not already a client, I would like to discuss your *becoming* a client. Please call me for more information.

However, that's not its only purpose. Even if you never become a client, if you want this information, I want you to have it – for a while, anyway. My hope is that providing this information and teaching you what I think is important when investing may help you. Please contact me if you have any questions or comments. I'd love to hear your reaction to my letter.

Quick Look

Market	**Next Expected Move**
?	

- Society, including government, is based upon trust. What happens when societal trust breaks down?
- What role do gold and silver play now?

Trust & Society

Society is based upon trust. Perhaps not 100% trust, but trust nonetheless. Don't believe me? Drive down any street until you encounter another car. Are you not trusting the other driver to stay on her side of the street and otherwise drive responsibly so you can both survive to reach your destinations? Further, are you not trusting the car manufacturer to provide a safe, well-manufactured car for your money? Are you not trusting the oil company to provide clean, uncontaminated oil and gas so your car can operate properly? Are you not trusting the government to assess responsibly the road upon which you're driving and post proper traffic control signs and/or devices, including speed limits? That's just one example. A citizen trusts other people to do the "right thing" hundreds of times a day. Otherwise, society breaks down.

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What happens when significant sectors of society violate the trust of the rest of the society? I guess it depends upon whether the society has been "free" recently enough that some of its citizens would become outraged over the transgressions. It also matters if the press were currently "free" enough to report the transgressions in the first place. I think the United States fits into that category. Certainly, the long-term socialist states in Europe and communist China do not. Their citizens know their governments "own" them and just accept government actions, if they even find out what they are, as something they have no control over.

Unlike most of the rest of the world, we can still hold our government(s) accountable in this country. At least for now. But, I digress. I thought it needed to be said.

One of the answers to the question above is the introduction of moral hazard into the citizenry from the offending societal sector, particularly, the government.

Moral Hazard

Excerpted from Wikipedia: "**Moral hazard** is the prospect that a party insulated from risk may behave differently from the way it would behave if it were fully exposed to the risk. …Moral hazard arises because an individual or institution does not take the full consequences and responsibilities of its doings, and therefore has a tendency to act less carefully than it alternately would, leaving another party to hold some responsibility for the consequences of those actions…"

Obviously, all governments, to a greater or lesser degree, are subject to moral hazard. If they were not, no one would serve in the government. If someone did, she would not make any decisions related to the citizenry for which she would have to suffer the consequences instead of the citizenry. By necessity, to some degree all government personnel are subject to moral hazard.

It would also seem reasonable that the longer one works in government instead of the private sector, the more moral hazard would be incorporated into their actions. Do you think our founders thought of that when they intended all elected representatives to be part-time positions and, most certainly, NOT full-time careers? Eureka!

Let's look at an example. Much of the citizenry believes that insurance companies have been taking advantage of insured's for decades now. They were fine with taking premiums, not so good about fulfilling what was thought to be their obligations. Making insurance contracts unreadable documents of legalese did not help bridge the understanding gap with insured's either. Therefore, the insurance companies exhibit moral hazard themselves through failure to cover (under a mountain of legalese) or outright denial of proper claims.

The result? Many or most citizens do not trust insurance companies to look out for their insured's. Therefore, they start looking out for themselves – even if that involves dishonest behavior they would never exhibit in the rest of their otherwise honest lives. Moral hazard has been passed on to their insured's.

The Wall Street/Government Betrayals

Greenspan made his "irrational exuberance" comment in the mid-1990's. Since then, Wall Street has been up to its elbows in moral hazard. While not expressly stated, the Greenspan Fed made it clear that they didn't like the economic implications of a market crash. He implied that the Fed would do pretty much anything within its power to prevent such an occurrence. *Also known as the "Greenspan Put," investors, especially Wall Street insiders, began taking abnormally large risks because it was clear the Fed would use its monetary and interest rate tools to mitigate market downturns.*

Of course, the government, including the Fed, already dealt with moral hazard constantly, as outlined above. Comments about the "PPT," (plunge protection team – run by the Fed) became commonplace in investing literature. Although the existence of the PPT has never been proven, many suspect it is as real as, well, "climate change."

Do you think investor behavior may have been changed by the knowledge the Fed would act to mitigate downside risk? Me, too.

Additionally, the government, and in particular, Rep. Barney Frank and Sen. Chris Dodd, through Fannie Mae and Freddie Mac have been forcing banks (generally through threats) to write home loans to unqualified applicants since at least the late-1990's. This helped to fulfill their sense of "fairness" concerning home ownership, not to mention buying a few votes and looking good to the liberal media.

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Asset Allocation Percentages
CJ Current Suggested Ranges

Dow Theory Market Phase: **BEAR**
Appropriate Current Allocation: **DEFENSIVE**

Asset Class	**Conservative**	**Aggressive**
Money Market Funds	70-10%	55- 5%
Long Positions:		
Bonds & Bond Funds	30-60%	40-60%
RD Stocks	0-10%	0-10%
Growth Stocks	0%	0%
Gold Equities/Funds	0-20%	10-30%
Bear Market Funds	0- 10%	5-20%
Aggressive Positions:		
Shorts and/or Options	0%	0- 5%

Notes:
Income generating portfolios may not conform to the above guidelines. If income is the primary purpose of a portfolio, income needs are met *first*, then other allocations are made.

Up to 50% of bond/bond fund positions should be in international (non-US) bonds. Such bonds will provide higher interest paid on the face due to the additional *perceived* risk of foreign bonds, as well as providing hedging gains as the dollar declines against foreign currencies due to Fed monetary policies.

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FOR THE RECORD: Not all US media is liberal. Certainly, Fox News and Fox Business are more centrist. Fox, by comparison, is called "right-wing" by liberals and the liberal media. Our local newspaper, the *Kansas City Star*, while left leaning, is certainly moderate in comparison to most other big city newspapers, especially her cross-state rival the *St. Louis Post-Dispatch*. I know this personally from traveling to Seattle, San Francisco, LA, Chicago, Atlanta, Denver, Washington, DC, and Boston.

After the banks would make the loans, Fannie Mae and Freddie Mac would purchase their bundled loan packages, securitize them and resell them out into the securities markets. Since Fannie Mae and Freddie Mac had the implicit, if not express, guarantee of the US government behind these securities, they were viewed as virtually risk-free. This was the genesis of the housing meltdown, the subprime and Alt-A crisis, the destruction of Fannie Mae and Freddie Mac as investments and the credit crisis. It certainly helped enhance the stock market crash since 2007, also. The late 2008 and early 2009 Wall Street bailouts of major banks and insurance companies further perpetuates the moral hazard problem by allowing those firms engaging in the most risky behavior to survive.

While the government was mitigating the risks to themselves and these other parties, who was shouldering these risks without even having a say in the matter? Taxpayers. In a supposedly capitalistic economy, the government has shifted the risk from the proper, risk-taking parties to innocent taxpayers (*aka* stealing). What we are seeing today is not a failure of capitalism, as the liberal media so often and wrongly decry; we are witnessing the failure of government.

Is it any wonder thinking citizens may be fed up with governmental power grabs and might be suspicious of new government programs like health care reform and Cap-and-Trade legislation? The government would like the citizenry to "give up" and let the government take over the rest of their lives (for their own good, of course, Comrade). Instead, the repeated government failures of the last two decades (since Reagan left office) has riled up some of our people. These folks remember fondly their proud, independent, capitalistic heritage and believe we should return more closely to that society and economic system. It's not President Obama, but what he represents – the repeated failure of the government to improve our lives by taking over larger portions of them – that citizens are fighting.

We have not seen enough of the behavioral change of investors to determine if they will fully adopt the moral hazard of the government or if they will rebel and not participate until they know the game is no longer rigged in favor of government and Wall Street insiders. If they adopt moral hazard, the system may collapse. If they rebel, commodities, especially gold and silver, with no counterparty risk, may emerge as investments of safety and choice.