



# Napa Wealth Management's The Sensible Investor

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## Prechter Say's Dow 1000 - I Say "Not Possible"

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Excerpt from Tim's article on Seeking Alpha



Robert Prechter of Elliot Wave International came on CNBC on September 27 and talked about the Dow eventually hitting 1,000 before this was all said and done. For disclosure purposes, I subscribe to his newsletter, as I do many others in both the bull and bear camp. I like to keep my finger on the pulse of what each camp is thinking.

This prediction though, seems to be one set on selling more subscriptions, having less to do with reality. Dow 1,000 is a headline grabber and sure to put some people on edge. What if? What if we did see 1,000 on the Dow? I have talked to a prospective client recently who is scared to invest any money with our firm, even though he agrees with the way we invest, because of Prechter's call the past few months of Dow 1,000. I wonder how many others are staying on the sidelines in cash awaiting the potential end of the U.S. market as we know it. While I agree with a more cautious stance at the moment, Dow 1,000 is out of the realm of possibilities based on my research. Let's take a look.

First, 1,000 on the Dow will literally wipe out 90% of the market cap of the greatest businesses in America, and arguably the world. Let's look at Coca-Cola ([KO](#)) for example. Currently Coke has a market cap of \$135 billion. If we wipe out 90% of that market cap, at the Prechter bottom, the entire franchise will sell at a market cap of about \$13.5 billion. Coke made \$6 billion in free cash flow last year. If their business stayed flat, they would be making 50% returns per year on their "Prechter bottom" market cap. Does Prechter think the world will be drinking 90% less Coke as well? Hopefully, you can see the absurdity of this Dow 1,000 call.

What is more likely to happen?

If (and it's a big if) the Dow were to reach 1,000, it would get there in real terms from the proliferate printing of Ben Bernanke and the Federal Reserve, not in nominal terms. (Real terms are based on real money – gold. Nominal is the number you see printed when view

-ing the stock market index e.g. Dow. It is adjusted for inflation and compound interest/dividends.) We are seeing this happen already.

From the March 2009 lows, the Dow is up about 64%. Seems like a nice little "gain" in wealth for those who were lucky enough to buy in March of 2009. Due to the theft of middle class investors through the printing press, the Dow stocks priced in a basket of 17 commodities that are used by most humans, in "reality", have only gained about 8.8% from the March 2009 lows. That is to say, stocks have barely beat inflating prices since the depths of the crisis over a year ago. Ben Bernanke has done a great Houdini act in making things appear like they have gotten better.

The Dow priced in honest money (gold) is even more worrisome when viewed over the last decade. The Dow in real money (gold) terms is about 82% lower since 1999 before the tech bubble burst. It is up 19% from the March 2009 lows in real terms. In nominal terms, it seems like the Dow is "only" about 24% below its all time highs, but in real money terms (gold), the Dow is already almost 90% lower than it was a decade ago. Will we drop another 90% from here, or is Prechter's 90% drop almost complete in real terms over the past decade?

While I still think there is some pain to be had in the markets, and believe investors should do some focused things to protect them from a Japan-style lost two decades, Dow 1,000, in nominal terms, is absurd in my opinion.

Caution makes sense at the moment, but hiding in a bunker waiting for Dow 1,000 while holding cash is about as risky as the other option, investing 100% in stocks. If the drop happens in real terms and not nominal, holders of "cash only" could stand to lose yet another 50%+ of their purchasing power over the next decade like they would have over the recent past decade, even while stocks lost money.

Read the entire article with graphs on line at [www.seekingalpha.com](http://www.seekingalpha.com). Search for Tim Ayles.



That's right. I love life insurance. I know I'm some sort of übernerd. I have my reasons, however, which I'll be imparting to you this month and next. But, before I begin, I need to point out the barebones basics of life insurance.

There are two types of life insurance – term and whole life. Term insurance, generally the more inexpensive of the two, will only be in effect for a set period of time e.g. 5, 10, or 20 years (though the term can often be extended). Whole life, on the other hand, will be in effect until the insured dies (for your whole life-hence the name). This month we're going to discuss term life and next month we'll look at whole. So why do I love term life insurance?

Cost – Life insurance rates are based largely on life expectancy. The longer you're expected to live, the lower the cost of the insurance. Life expectancy is expressed statistically in what are called mortality tables. Before the beginning of the 21<sup>st</sup> century the last major revision of the mortality tables had taken place in 1980. Around the year 2000 the tables were revised and the changes were quite large. For example, a male child born in 1980 was expected to live to age 70. According to the revised figures a male child born in 2000 was expected to live to age 76. That is almost a 9% increase in a mere 20 years. For most of recorded history a change of that magnitude would have taken centuries. Due to increased longevity, term insurance rates have plummeted. Term insurance is no longer geared primarily for the young. Members of the baby boom generation and older can take advantage of the drops in premiums. According to the Insurance Information Institute, term insurance rates dropped 4% each year from 2000 to 2007. This followed a 15% drop in prices between 1994 and 1999. The net effect is that term rates are about **half** of what they were 15 years ago. How many products of any kind actually decline in price?

Insuring and Protecting the "Mature" – In 1960 a couple, both age 60, would probably own their home outright (or be close). Their children would be out of the house, finished college, and have started families of their own. Most likely, a 60 year old couple wouldn't have a need

for term life. But, as we all know, times have changed. Couples are starting families much, much later in life. The goal of owning a home outright has dropped in priority for many especially amid the low mortgage interest rate environment of the last few decades. As a result our baby boomer couple might have a substantial mortgage as well as pre-college age children at home. They might also consider term insurance to be too costly at their age.

**Absolutely not so.** Let's say Todd and Tanya, both 60 decide to take out a policy on Todd. If Todd is in very good health he might pay as little as \$125 per month for \$500,000 of 20 year term. In average health, the monthly premium will likely be higher. If Todd were to die unexpectedly, \$500,000 could be a life saver for the survivors. Paying for a college education, protecting a mortgage, or adding to Tanya's financial security are the first benefits that come to mind.

Protect a business – Let's say Todd is a CPA and has built a successful solo practice. If he should die unexpectedly what is Tanya supposed to do? Sell and get what she can? An emergency sale of a successful business could have drastic consequences. After all, what is Tanya supposed to do? Spend the next five years becoming a CPA so she can take over? Or, if Todd should die, she could receive insurance proceeds of \$500,000, hire a CPA to take over and then have time to decide what she wants to do with the practice.

As a fantastic gift – I've had individuals ask me, "I'd like to help my children but I'm not crazy about just giving them cash". Offer to buy a life insurance policy. What might be even more important than the monetary gift would be the gift of a parent's experience. You could succeed in helping to insure a young parent where a financial planner might fail. As we all know, young people feel indestructible and often don't take things like insurance seriously or don't consider insurance a high priority. But those of us who are a little longer in the tooth have seen the tragedy of an early or unexpected death. We know that losing a loved one is extremely difficult. We know that being solvent during a difficult time is invaluable.

Frankly speaking,  
Jim

