



FINANCIAL CONNECTIONS

G R O U P I N C O R P O R A T E D

For Clients and Friends of Financial Connections

Your reports for the first half of 2011 are enclosed. During the first four months of the year, the market seemed enthusiastic about global growth. But in May and June, with the debt crisis in Greece and other European nations, the continued high unemployment numbers, and the depressed housing market, it reversed course. Stocks were down during the second quarter.

The balancing act in Europe now is to resolve the debt crisis without creating a banking crisis. The hope is that the latest bailout of Greece will buy enough time for the country to realign its finances.

Amid the media's negative predictions about the economic consequences of the current U.S. budget deficit, we hear no voice of reason. It has taken years to reverse the surplus from the Clinton era into deficits. The current recession only added to the deficits when stimulus programs were initiated. No one should expect this trend to reverse itself in one budget year.

Jeremy J. Siegel, professor at the University of Pennsylvania's Wharton School of Business, says "a big budget deficit should result in higher interest rates because government debt competes with other debt such as corporate bonds and mortgage securities."

But companies with record-size cash balances can still issue debt at low interest rates. Inflation has not arrived—yet.

Please let us know if you would like to get together to review your investments and update your financial plan.

Client Portal/Vault

We have begun to set up portals for clients. This service includes:

- Ability to store your important documents on a secure server
- Download them if needed from any Internet connection
- Receive your quarterly reports and newsletter from us electronically instead of on paper

Quarterly Newsletter, 2nd Quarter 2011 7/20/2011

Our first priority at Financial Connections is to provide the highest quality service to our existing clients. To continue doing so, it's necessary that we raise the minimum assets for new clients of Financial Connections to \$750,000. Also, we are raising our financial planning rate to \$240 per hour.



FACING THE INEVITABLE

You've probably heard the adage "No one is exempt from taxes and death." Given these facts, what can you do? Work with Financial Connections Group, Inc. and your tax professional to look for opportunities to ease the impact of taxes. Your estate attorney can help review your estate tax consequences. But what about death?

Obvious steps to take include having an up-to-date trust, advance directive, and living will. Other things you can do:

It is a forgone conclusion that death will be stressful to a surviving spouse, partner, and/or heirs. A few practical decisions—such as burial or cremation—cannot wait. We can make it easier on our loved ones by making these decisions while we are alive.

Bonnie and Jill decided to do just this. Below is a synopsis of their decision and the thought process behind it.

- ◆ Cremation or burial: They chose a burial site and paid for plots in a cemetery in Mendocino (friends can wave to them as they drive by on Highway 1 ☺). They also wanted to be buried together.
- ◆ Bonnie and Jill also picked out headstones (each wanted to make sure her headstone was something she liked), again with payment now instead of later. In fact, the stones are already installed. Only the ending date is vacant!
- ◆ Last, they searched for a mortuary. They interviewed one in the Mendocino area and one in Marin. After talking with the personnel and reviewing the costs, they decided on Keaton's in San Rafael (part of Dignity Memorial).

Part of their decision to act now was to lock in the cost. They were surprised at the significant amount of paperwork. Here are some of the details to be settled:

- ◆ Authorization to dispose of the body
- ◆ Embalming—yes/no
- ◆ Casket or urn?
- ◆ Obituary? If so, in what newspaper(s)?

We know many people may be uncomfortable planning this way in advance of the need. But isn't it a gift you are offering to those you leave behind?

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THE DOLLAR: STILL A RESERVE CURRENCY?

A reserve currency serves as currency for international transactions and denominates commodities—such as oil, gold—worldwide. Countries other than the one issuing currency hold it in large quantities, to pay for these goods.

Since World War II, the dollar has been the world's reserve currency, accounting for 65% of all global reserves.

Advantages to a reserve country

The dominance of dollar-denominated assets around the globe ensures that liquidity is always available (there is little risk that someone wanting to sell in dollars can't find a buyer). U.S. Treasury securities are the single most important asset bought and sold by global investors. The high demand for Treasuries keeps our interest rates low and makes growth cheaper to finance. A study by McKinsey estimated the savings to the U.S. because of lower interest rates was \$90 billion annually.

Another important benefit to the reserve country is flexibility. As a net lender, it permits a larger trade imbalance for goods and services than for a non-reserve country.

The dollar declined approximately 20% over the last couple of years. Several factors underlie the shift:

- ◆ Government debt is increasing
- ◆ Economic power is shifting from developed countries to emerging markets countries

Alternatives

The call for a reserve currency other than the dollar has been growing. Emerging countries believe the Fed's Quantitative Easing (QE) 1 and 2 policies held interest rates artificially low. The International Monetary Fund (IMF) is calling for a global reserve currency made from a basket of currencies—the euro, the dollar, the pound, and the yen.

This is not the first time there has been a call for an alternative to the dollar but as in the past, there isn't any valid competition, at least for the foreseeable future. Some interesting statistics help underscore why it would be difficult to move away from the dollar as the world's reserve currency.

- ◆ \$5 trillion is the approximate amount foreign central banks hold in U.S. Treasury and Agency-backed bonds
- ◆ 89 countries peg their currency to the dollar
- ◆ 39% of *world* debt is denominated in dollars
- ◆ 85% of foreign exchange transactions are in dollars
- ◆ 70% of U.S. \$100 bills are held overseas

This sets a high barrier to entry for another currency. Should the world move to another reserve currency such as the IMF's recommended basket, a transition will take decades to effect.

Source: Payden&Rygel: Point of View Second Quarter 2011

COMPANY GROWTH OUTSIDE THE UNITED STATES

To illustrate the fact that the majority of growth is outside the United States, we offer the following information.

- ◆ Down 43%—stocks listed on U.S. stock exchanges since its peak in 1997
- ◆ Doubled—the number of stock listings outside the U.S. over that same period
- ◆ 3,800—fewer companies listed on the exchanges since 1997
- ◆ Eight times—more company listings outside the U.S.
- ◆ Down 71%—the number of IPOs (Initial Public Offerings) in an average year since 2000

Here are some of the reasons for the decline:

- ◆ Company mergers
- ◆ Lower fees on overseas exchanges
- ◆ Fewer compliance requirements than Sarbanes-Oxley requires
- ◆ Competition between the two remaining U.S. stock exchanges

Many private companies sell themselves to larger ones—134 companies were purchased by five corporations last year. With low interest rates, private companies can borrow money to fund growth instead of going public and selling shares.

According to Jay Ritter, professor of finance at the University of Florida, "The prolonged drought in IPOs [in this country] raises concerns about whether an important engine of growth in the U.S. economy has come to an end."

With fewer stocks available to the American investor on our stock exchanges, the importance of looking globally for investments increases. There is more supply outside the U.S.

A good example is Seattle-based HaloSource, Inc., a water-purification company. Instead of going public on a U.S. exchange, it selected the London Exchange. Its chief financial officer, James Thompson, said "the savings are pretty significant."



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