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What Does The Debt Ceiling Crisis Mean For FSA Clients?
Market Review From Your Portfolio Management Team—July 28, 2011

There has been considerable posturing among the politicians recently as the August 2nd deadline for the debt ceiling nears. If you've been watching the news, you no doubt are concerned about the potential impact to your portfolio if the debt ceiling is not raised. According to the Treasury Department, the debt ceiling has been raised over 100 times since it was first instituted during World War I. It has been raised 10 times in just the past ten years. Keep in mind that this is a political issue, not an economic one. There is no question that the U.S. can pay its obligations; it is merely a question of Congress and the President coming to terms with how much and under what conditions. The fiscally conservative members of Congress want the U.S. to end its free-spending ways, and are using this vote to force some spending restraint on the federal government.

Most experts believe that Congress will pass a new debt limit. If for some political reason, the ceiling is not raised by August 2nd, the government will technically be in default. We would advise that you not be too worried about that prospect. Imagine if you do not make a payment on your house. The mortgage company will get upset and may charge you a penalty, but once you send in your payment, things will eventually get back to normal. There is no danger that theU.S. will actually default on its obligations. It is really just a timing issue.

Stocks and bonds have stalled out because Congress and the President have not reached any compromise over the past several months. There has been much hand wringing over the prospect of the U.S. losing its AAA credit status and the impact on interest rates, mortgage rates, and what that might mean for holders of Treasury bills and bonds. While many of the fears may be overblown, it has created a good deal of uncertainty which investors loathe.

As you know, we take the prudent approach in managing your money, so we have maintained a pretty conservative stance all year. Across all five strategies, we have less than 30% invested in stock funds, with the majority of that money in more conservative dividend-oriented funds. We have over 50% of our assets in bond funds, but these are primarily corporate bond funds (not Treasury funds), and they are short-term and intermediate-term funds, so they are not as affected by rising interest rates. In addition, we have added some inverse bond funds to the portfolios in case interest rates do rise. So, even though the money market position is not very large, the portfolios are well protected if the debt ceiling is not raised before August 2nd (and the stock and bond markets react badly to that event). As always, we have our safety nets in place to trigger further sales if our current holdings turn down in early August.

Regardless of the outcome, know that we are diligently monitoring your accounts and stand ready to protect your portfolios from harm, while looking for opportunities to participate in the long-term growth from stocks and bonds. Please don't hesitate to call or email us if you have any specific questions.

Your Portfolio Management Team