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July 13, 2009

A Very Few Examples of Today's Challenges

July 10, 2009: This day is one for the history books as General Motors, for many years the world's largest industrial company, emerged from its Detroit ashes as America's new Phoenix bird for the purpose of once again becoming a power in the automobile industry. The largest stockholder of this now private company is the US Government, which owns 61% of the company's stock along with other major stockholders --- the UAW (the United Auto Workers Union) and Canada. It has been renamed Motors Liquidation Company.

In April 2000 the original GM, the world's largest automaker and one of the world's largest corporations – a company without which we probably could not have won World War II - traded at an all-time high of $94 per share. Today its stock is worthless, shedding light on the validity of the "Buy and Hold" strategy of investing. At least we have learned one more axiom about investing that we should put away for another day.

On www.motorsliquidation.com there is an Important Notice stating "Management continues to remind investors of its strong belief that there will be no value for the common stockholders in the bankruptcy liquidation process, even under the most optimistic of scenarios."

The former GM shares, renamed as mentioned above, Motors Liquidation Company, are unlisted and have been declared worthless. Today, July 10th, old GM's shares (GMGMQ) are trading up almost 40% at $1.15 a share in the over-the-counter market, on volume of 74,814,700 shares. We admit that we just don't get it. (Very shortly after writing the above, trading in the worthless Old GM stock was halted. There is no trading in the securities of the reborn/Phoenix company as it is entirely privately held. GM stock is now gone forever.)

We are curious to see if the government will be able to show its prowess in managing the new GM powerhouse back to its former Michael Jackson-like stardom. This will be necessary in order for the company to repay $50 billion of debt to the US government – us - which the company said it will do by 2015. This exercise undertaken by Washington will show how accurate those are who say big government cannot run big business. Actually, it is beginning to look like Washington will have many opportunities to show us how numerous businesses should be properly run.

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On July 9, Bloomberg reported: "American International Group Inc. [AIG], the insurer bailed out four times by the government, will likely have no value left for private shareholders after repaying the US…. Our valuation includes a 70% chance that the equity at AIG is zero," said Joshua Shanker,

an analyst at Citigroup. "Shareholders may have no value left if AIG is forced to sell its assets and can't command prices that exceed the insurer's liabilities, a scenario that has a 60% chance of occurring, according to Shanker. He said there is also a 10% chance of insolvency, which may also wipe out investors."

Bloomberg goes on to report: "the government's rescue includes a $60 billion credit line, $52.5 billion to buy mortgage-linked assets owned or insured by the company, and an investment of as much as $70 billion. You may recall that several years ago AIG was the largest insurance company in the world. Now it is in large part owned by the US government, and analyst Shanker has declared that its shares may well be worthless. It is of interest that several days ago AIG declared millions of dollars of bonuses for executives for 2008. New bonus proposals will be forthcoming in a few more months. This is another opportunity for big government to show the world how to run a big company.

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Oh by the way, one of many other companies where the US government now owns a substantial percentage of the stock is <u>Citigroup</u>. The US will own 34% of Citigroup's shares, and while we do not have exact figures as to how much money Citigroup has borrowed from the government, we believe it's liabilities to the US taxpayer exceed $300 billion. In the last few days Citigroup has undergone its third major executive shakeup in 2009 which leads to some confusion as to when Citigroup's debts will be repaid, if ever.

It is also noteworthy that Citigroup raised its interest rates on its credit cards before the new federal rules become effective. The *Financial Times* (July 1st) reported "Citigroup has sharply increased interest rates on up to 15,000,000 US credit card accounts. Just months before curbs on such rises come into effect, in a move that could fuel political anger at the treatment of consumers by bailed-out banks." The article continued. "People close to the situation said that City, which is about to cede a 34% stake to the US government as part of its latest rescue, had upped rates on between 13,000,000 and 15,000,000 credit cards. It co-brands with retailers such as Sears and Macy's. Citi's rate increases emerged on the day the government proposed legislation to create a new regulator with sweeping powers on consumer protection."

The rate increases were retroactive, and Carolyn Maloney, Democratic representative for New York, told the *Financial Times* . "It's hard to tell if rate hikes on existing balances being put in place now are the result of prior bad business decisions or getting in under the wire of the new law. Regardless, retroactive rate hikes are 'unfair' and deceptive - and that's the Federal Reserve talking, not just Congress." We add "Nice going City. At least you don't deviate from your former business standards and ethics. How much do you owe now, and when will it be paid back to the US taxpayer?" If you hear Citigroup's answer before we do, please let us know. We have a continuing interest!

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Finally, don't overlook <u>California</u>: The state that would be the world's eighth largest economy if it stood alone. California began its fiscal year last week without a budget. California is now paying its employees with IOUs since it has run out of money. On July 10th it was reported that, among others, Bank of America, Wells Fargo and JP Morgan were not accepting the state's IOUs printed because of its $26.3 billion deficit. The California economy continues to suffer an economic slump due to a collapse in housing, unemployment exceeding 11% and welfare and social service spending well in excess of its income. Why wouldn't a bank, accept a California IOU? When we last

checked, we noticed that most banks still aren't accepting Confederate money either.

Our friends in California are far from alone as they continue to spend more money than they are taking in. Apparently another 30 or more states are getting ready to follow California's example. A few that have been mentioned include Massachusetts, New Jersey, Pennsylvania, Ohio, Michigan, Nevada, Arizona and on and on. These disasters have snowballing effects with regard to their citizens and businesses that immediately affect the stock and bond markets in the country as a whole.

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All of the above and volumes more are true. We could not make it up. The relevance to the financial markets is the fact that the Credit Crisis is nowhere near being solved, and as a result, the economy continues to flounder. In our opinion, the economy continues to deteriorate with no end in sight. The Administration seems to be on the edge of announcing a second Stimulus Package as the first has obviously not worked. One of the many small problems with such a proposal is the fact that the US government, like California and her sister states, simply does not have the money. Other proposed major programs with which we are all familiar will require untold sums of money for implementation. There is a great deal of agreement that some of the goals could significantly benefit our society, but the problem continues to be their funding. What will they ultimately cost and how will they ultimately be paid for? Again, if you hear the answers to those questions before we do, please let us know

The average citizen is aware that economic and financial conditions are worsening. He is sitting back watching the parade go by. He realizes that his borrowing power is extremely limited and has long been aware that he can no longer use his home as an ATM machine. Could he be one of those to push the unemployment rate to 10%, 11% or higher? Perhaps worse, he has begun to realize that not even the inspirational politicians he formerly believed in have the solutions. He has simply stopped spending "Until things get better."

When the markets can figure out when things will get better, they will get better.

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