



THE FOXHALL GLOBAL OUTLOOK



AUGUST 8, 2011

PAGE - 1 -



HOW WILL THE S&P CREDIT RATING DOWNGRADE AFFECT INVESTORS & CONSUMERS?

On Friday evening, two hours after STANDARD & POORS downgraded the AAA credit rating of the United States, I gave an interview to FORBES magazine.

SUMMARY OF THE INTERVIEW

*To summarize that FORBES interview, the S&P credit downgrade most likely will be a **NON-EVENT** and, based on the history of similar downgrades in Japan, Australia and Canada, will not raise U.S. borrowing rates and consequently, I do not believe it will raise rates for mortgages, credit cards or auto loans. It is also unlikely to affect corporate earnings.*

However, this credit downgrade may shake markets this week and investors should expect some volatility.

*But, I believe by later this week or next week, when the market realizes this is a **non-event**, the markets will quickly recover, given its largely political nature.*

HERE IS WHAT I SAID IN THE FORBES INTERVIEW:

This downgrade will have more political consequences than any effect on government borrowing or on consumers.

From a practical point of view, this downgrade will have almost no noticeable effect on the U.S. Government's ability to borrow and it will have little to no effect on consumers. I do not believe there will be any change in rates. Also, there will be little or no institutional pressure to sell U.S. treasuries. Here's why:

When the credit ratings agencies downgraded Japan, it had no noticeable effect on either the Japanese government or consumers. The same was true of similar credit downgrades in Australia and Canada. They were "NON

-EVENTS." I believe we will see a similar result here in the U.S.

Because this was a "split decision", with Moody's and Fitch reaffirming the U.S.'s AAA rating, it does not have the same effect as if it were a unanimous decision.

Banks, pension funds, money market funds, etc. usually have to sell any bond that is downgraded from its AAA rating. But U.S. Treasury bonds are a unique asset class in themselves and no institution is required to sell them because of a downgrade. When these rules were written, a downgrade of the AAA credit rating of the U.S. was unthinkable. This historical "accident of good luck" makes it highly unlikely that any institution will feel any contractual pressure to sell U.S. Treasuries. The Federal Reserve, on Friday, reconfirmed this in a directive to all banks in the U.S.

However, from a political perspective this may be a great long-term blessing for this country. S&P has fired a 'warning shot across the bow' of the new Joint Congressional Committee that it now has to tackle the big entitlements of Medicare, Medicaid and Social Security, even though we are entering an election year. Tackling these entitlements are the only way Congress will come up with the long-term cuts that need to be made in order to get America's finances back in balance and to meet S&P's criteria for re-awarding the United States its AAA rating.

From an historical perspective, when Canada lost its AAA rating in April 1993, for instance, the country's stocks gained more than 15% in the subsequent year. The Tokyo stock market climbed more than 25% in the 12 months after Moody's downgraded Japan in November 1998 and the Australian market saw big gains the twelve months after its credit downgrade.

WHAT DOES CONGRESS NEED TO DO TO RESTORE THE AAA CREDIT RATING

Everyone in Washington knows what needs to be done. It was all outlined in the SIMPSON BOWLES COM-



THE FOXHALL GLOBAL OUTLOOK

AUGUST 8, 2011

PAGE - 2 -

MISSION. But, we seem to have no politicians in Washington, including the president, who are willing to tackle true long-term entitlement reform.

The SIMPSON BOWLES COMMISSION basically recommended that everyone over the age of 50 or 55 would continue to get all the benefits that are currently offered in Medicare and Social Security. But people under the age of 50 or 55 would have to work a little longer before they could claim these entitlements. One of the proposals was to tie the retirement age to 85% of the Average Life Expectancy here in America. The current Average Life Expectancy tables, published by the National Center for Health Statistics, is 79.9 years of age. That means that people over 50 or 55 would now have to work to the age of about 68 in order to receive their benefits.

In 1950 the Average Life Expectancy of an American man was 68 years of age. Well if you work your entire life and pay your social security taxes, and retire at 65, and then die at 68, the government has a very actuarially sound entitlement system. But when people are now living into their 80's and will be living, on average, into their 90's within the next 20 years, the system is bankrupt. We will eventually be paying out more than most people paid in.

Everyone understands that the only viable and long-term reforms of Medicare and Social Security will require tying future entitlement recipients to a formula similar to 85% of life expectancy.

THE BIG QUESTION IS, WILL POLITICIANS PUT POLITICS FIRST OR COUNTRY FIRST?

We always have to come back to our country's major problem, which is our dysfunctional government. Both Republicans and Democrats, and all the presidential candidates, know there is a high likelihood that they will not get re-elected if they do the right thing in reforming entitlements. Medicare and Social Security are the most popular programs in America for both Republicans and Democrats.

Even Paul Ryan, who came up with a creative alternative to reform Medicare, did not politically dare to touch Social Security in his proposed budget. Even he could not bring himself to discuss reforming Social Security before a major election. Remember, old people tend to be conservative; they tend to lean Republican; and they all vote!

That is the political reality of America today! But God knows this country is craving for a major politician who is willing to stand up and say, "I know this will cost me my job, but I am going to put the country first and politics second."

Where are the "modern day" George Washington's and Abraham Lincoln's???

That's the politician I want to send a campaign contribution to.



THE FOXHALL GLOBAL OUTLOOK

AUGUST 8, 2011

PAGE - 3 -

Maybe in this time of crisis we will find a new "modern day" Mr. Smith in Washington. I just wish he would stand up and let us know he is there.

Until this passes over the next few weeks.....

Patience!

—Paul Dietrich

pdietrich@foxhallcapital.com

Disclosures: The opinions and portfolio information provided in the Foxhall Global Outlook are subject to change at any time, and are not to be construed as advice for any individual nor as an offer or solicitation of an offer for purchase or sale of any security. Client accounts may differ from model allocations due to many reasons. All investment strategies offer the potential for loss as well as gain. Individuals should consult with their financial professional to determine an investment strategy appropriate for their objectives, risk level, and time horizon prior to investing. Past performance is not a guarantee of future performance.

Foxhall Capital Management, Inc. is a registered investment adviser with the U.S. Securities and Exchange Commission (SEC) under the Investment Advisers Act of 1940. The firm is defined as the Foxhall Capital Global ETF, 401(k) and Stock Series divisions, which manage a variety of ETF, 401(k) and Stock strategies in bundled fee and non-bundled fee accounts for primarily U.S. clients. The firm was redefined as of 12/1/08 due to the creation of the 401(k) Series division. A complete list and description of all firm composites and their compliant presentations are available upon request.

Foxhall Capital Management, Inc. claims compliance with the Global Investment Performance Standards (GIPS®). Foxhall Capital Management has been GIPS verified for the periods 12/31/99 – 12/31/08 by Beacon Verification Services. The ETF Series composites have received a performance examination for the period since inception through December 31, 2008. A copy of the verification report is available upon request.