Falcon Financial Management, Inc.

July 26, 2012

Dear Friends,

I recently unearthed a cartoon (and now it is missing again!) that I wanted to share. The gist of the cartoon was a picture of three people sitting in a row on an airplane, calmly reading, napping. The pilot comes on to advise them that they are entering some choppy air and asks them to keep their seat belt on. The man at the end of the row begins to scream hysterically "We are all going to die!". The folks seated next to him look at each other and the woman says "he's a financial reporter".

I sense from talking to people in and out of our review meetings that there is an enormous of uncertainty today. This uncertainty has created anxiety and a loss of confidence in the future for many. I say this to say that I remain extremely confident in the long term future of our country and our economy.

Let me give you an example of why I am confident; today the 10 year Treasury bill rate closed at 1.48%. The rate for the 10 year Treasury bill is determined by an auction. In an auction that we are most familiar with the bids go up until no one will bid higher. In an auction for the 10 year Treasury bill the opposite happens. The rates go down until no one will buy them.

This is the lowest interest rate we have ever paid for borrowing money for 10 years. Why will people lend us their money at these incredibly low rates? Because they believe that this is the safest economy in the world to store your money. When the world's money is seeking safety they are coming to the USA. The credit rating of the US is irrelevant. As Bill Gross, the head of PIMCO's investments famously opined last summer "there are not enough A's in the Scrabble box to describe the credit quality of the US." This great country of ours is going through a rough patch. We are in an underperformance cycle, a severe underperformance cycle. What is important to understand is that it is a cycle and under performance cycles are followed by over performance cycles. These cycles run approximately 15-17 years. I like to think that we are in the 4th quarter of this under performance cycle.

All of this makes me excited about the future of our economy over the next 10 to 20 years.

That being said, I am uncomfortable with the circumstances that we are facing for the next 6-18 months. So much is going to be determined by the decisions made by Americans in the coming election.

Here are some of my concerns about our domestic economy; the fiscal cliff, this seems insane to me but we are again being put in a position where we do not know what the taxes we will pay next year are. I believe that tax rates are going to change, perhaps not immediately but soon. Based on the last year that tax data is available, 2009, the IRS has said that to rank in the top 1% of all taxpayers required an adjusted gross income (AGI) of at least $343, 927. This group of tax payers paid 37% of all federal income taxes. If every taxpayer in this group paid income tax equal to 100% of their AGI (they paid federal income taxes equal to an average of 24% of their AGI) an additional $1.007 trillion dollars of federal income tax would be raised. The government estimates that there will be a $1.327 trillion budget deficit for fiscal year 2012. In other words, if we took all of the money

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from the top 1% we would still spend more than we bring in. So where do we get the income? Can we continue to spend money regardless of the effect it is having on our ever expanding National debt? It just seems to my simple mind that we must curtail the growth of the government expenses as well as create a tax system that we all think is fair. Right now that seems like a pipe dream.

While doing research for the letter I visited the Tax Foundation web site (taxfoundation.org) on the advice of my good friend Mark Greenberg, one of the West Coasts top planners. On the front page of the web site is a calculator that will allow you to look at what your taxes may be in 2013, based on the three most discussed scenarios.

There was also this interesting chart that can give you an idea of what the folks in Washington are talking about when they are discussing the different tax rates.

It is important to remember that if nothing is done all the tax cuts will expire and rates will go back to what they were in 2001 and 2003 when the Bush tax cuts were originally implemented. In 2010 the partisans came together in mid December, after the congressional elections, to extend the Bush tax cuts until today. Obviously the easiest decision (without being too cynical) is to kick the can down the road again.

	Tax Cuts Expire (2013 projected parameters)		Current Policy (2013 projected parameters)		Obama Proposal (2013 projected parameters)	
Single	$0 to $36,250:	15%	$0 to $8,950:	10%	$0 to $8,950:	10%
			$8,950 to $36,250:	15%	$8,950 to $36,250:	15%
	$36,250 to $87,850:	28%	$36,250 to $87,850:	25%	$36,250 to $87,850:	25%
	$87,850 to $183,200:	31%	$87,850 to $138,200:	28%	$87,850 to $138,200:	28%
	$183,200 to $398,350:	36%	$183,200 to $398,350:	33%	$183,200 to $203,600:	33%
					$203,600 to $398,350:	36%
	$398,350+:	39.6%	$398,350+:	35%	$398,350+:	39.6%
MFJ	$0 to $60,550:	15%	$0 to $17,900:	10%	$0 to $17,900:	10%
			$17,900 to $72,500:	15%	$17,900 to $72,500:	15%
	$60,550 to $146,350:	28%				
			$72,500 to $146,350:	25%	$72,500 to $146,350:	25%
	$146,350 to $223,050:	31%	$146,350 to $223,050:	28%	$146,350 to $223,050:	28%
	$223,050 to $398,350:	36%	$233,050 to $398,350:	33%	$223,050 to $247,000:	33%
					$247,000 to $398,350:	36%
	$398,350+:	39.6%	$398,350+:	35%	$398,350+	39.6%

I would like some long term certainty in the tax code as well as the rules for Estates. Perhaps that is nothing more than wishful thinking. It makes it difficult for us to plan for the next 10 -20 years much less doing any planning for generational gifting and legacy planning.

Coupling our domestic issues with the significant problems that we saw in Europe as they digested the problems of Greece led to a very volatile 2nd Quarter.

The increased uncertainty about the domestic issues and the renewed concerns about Europe triggered a 10% correction in April/May that was followed by a modest rally that has brought us back to a DJIA in the 12,500 range. That is higher than we began the year but still lagging the market peak of 14,700 in October of 2007.

Here is what the Scoreboard looks like:0

The Scoreboard

(www.investmentadvisor.com)

	3rd Q 2010	4thQ 2010	2010	1stQ 2011	2ndQ 2011	3rd Q 2011	4thQ 2011	2011	1stQ 2012	2ndQ 2012
DJIA	**10.4%**	**7.3%**	**11.0%**	**7.1%**	**2.5%**	**-5.9%**	**12.8%**	**8.4%**	**8.8%**	**0.2%**
S&P 500	**10.8%**	**10.2%**	**12.8%**	**5.9%**	**1.8%**	**-7.4%**	**11.8%**	**2.1%**	**12.6%**	**-0.6%**
NASDAQ	**12.3%**	**12.0%**	**16.9%**	**5.0%**	**2.1%**	**-6.8%**	**8.2%**	**-0.8%**	**19.0%**	**-1.4%**
LBAB	**2.5%**	**-1.3%**	**6.5%**	**0.4%**	**2.6%**	**3.1%**	**1.1%**	**7.8%**	**0.3%**	**1.1%**

(Investors cannot invest directly in indexes)

You should expect continued volatility in the stock market as well as a low interest rate environment. The Fed has already said that they will be keeping their rates where they are (0 to .25%) through 2014.

That continues to be bad news for those who are saving money in CD's or Money Market accts. I was at one of our local Credit Unions recently and they were advertising a CD rate .01% for a $10,000, 90 day CD. There are alternatives to these low CD rates and if you are seeking safety of principal with modestly higher rates give us a call and we can discuss alternative strategies for your "safe" money.

I would be remiss if I didn't discuss the most current Institute of Supply Managers (ISM) index. We believe this index is one of the best indicators of the economy. Manufacturing contracted in June as the ISM index registered 49.7 percent, a decrease of 3.8 percentage points when compared to May's reading of 53.5 percent. A reading above 50 percent indicates that the manufacturing economy is generally expanding; below 50 percent indicates that it is generally contracting.

An ISM index in excess of 42.6 percent, over a period of time, generally indicates an expansion of the overall economy. Therefore, the June ISM index indicates growth for the 37th consecutive month in the overall economy, but indicates contraction in the manufacturing sector for the first time since July 2009, when the ISM index registered 49.2 percent.

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THE LAST 12 MONTHS

Month	*PMI*		*Month*	*PMI*
Jun 2012	49.7		Dec 2011	53.1
May 2012	53.5		Nov 2011	52.2
Apr 2012	54.8		Oct 2011	51.8
Mar 2012	53.4		Sep 2011	52.5
Feb 2012	52.4		Aug 2011	52.5
Jan 2012	54.1		Jul 2011	51.4

I have been interested in Social Media and how to use it to better inform our friends and clients. I recently experimented with using a Facebook page to share some articles that I thought would be of interest and to stimulate some reasoned discussion about these issues. I was determined to not censor anyone who was contributing their thoughts; I believe free speech is vital to the freedoms and rights we have. Many times I may not like or approve of some things said or protected under the flag of free speech but I do believe that the right is so fundamental that I have to swallow hard and say that is their right and in most of the world they wouldn't be allowed to say it.

It makes us great.

That said, I was very disappointed in the results. I am responsible for it, some of the articles were more partisan than I realized and they stirred up some conversations that turned ugly and personal. I think of myself as socially liberal and fiscally conservative and try and evaluate each issue on its merit. I don't think I accomplished that and I want to apologize to any of you who may have been offended by the posts. I have elected to walk away from that experiment. If you want to read about the drums, wrestling or my kids the page is still alive and kicking.

Here is the post I used to close the conversations: *I have been experimenting with Social Media the last few months and I have lost control of the page. I am saddened by how deeply people are divided; maybe I should have expected it to turn out as it has. I think friends from both points of view are so entrenched that we do not hear each other, we think that the other point of view is mean spirited, stupid, intolerant and evil.*

Much of what I have read from others has been from a "prove that" or "you are wrong" perspective. I hoped to just stimulate some give and take between some smart people. Some give and take that wasn't personal and mean spirited.

I'm not sure we can do that anymore.

Many of my thoughts and feelings are just intuitive or instinctual. Just as my belief in God, I can't prove there is a God, I just know that for me there is a Higher Power I choose to call God.

I originally believed that I could just devote one hour a day to Social Media, if I let it this experiment will take all my time and I just don't have it.

So if any of my posts have been insulting I apologize. If they have stimulated some thinking about our joint future good, regardless of what you think, thinking is good.

I will end with this, we have a great country, we have survived many crisis that are worse than today, we will survive and prosper as a country. We will not ignore those truly in need and regardless of who becomes President we will wake up the next morning and there will not be tanks in the street, we will get on with things.

It may be more of a challenge than we hoped. Challenges are not bad and have historically stoked the fires of greatness in this country.

So with that, keep love in your heart. Peace

We are here to solve problems. That's what we do. Even though on the whole I am not recommending changes, your individual situations may change and as they do we may need to make individual changes for you.

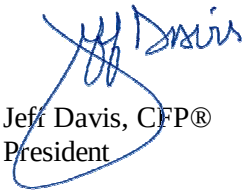
Do not hesitate to let Darla or me know if there is anything you need from us. When we can assist, we will.

I would also like to once again invite all of you to join Chris and me on Saturday mornings at 8:30 where we will continue to be hosting our popular radio call-in show; Dollars and Sense, on 97.3 FM. If you are not in Gainesville our show is also available via the Internet. So check us out on Saturday mornings. If you have questions or topics that you would like us to discuss then please give Chris a phone call or drop him a line at chris@ffmonline.com.

I want to take this opportunity to ask you to remember us when friends and family are struggling with these same questions going forward. Many folks are in retirement plans that don't offer them the kind of investment and planning advice that we provided for you. We have built this business on referrals, on the idea of working with a lot of people just like you. We appreciate you and would like to help those around you.

Thank you for your continued friendship and support.

Best wishes,



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