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The
High Income Factor®

Unlocking Powerful Strategies to Achieve Superior Returns

Tom Hutchinson, Editor

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Two High-Yielding Havens for the Great Central Bank Unraveling

What would happen if you went back in time and killed your grandfather?

Yes, it's a morbid thought experiment, and purely theoretical, but hear me out. Let's say you had a functioning time machine, and went back to a moment when your grandfather was a young man, before he produced any children. If you killed him, what would happen?

It seems the premature death of your grandfather, negating the birth of your father or mother, would consequently erase your own birth. Eliminating your grandfather would simultaneously exterminate your own existence. Upon his death, would you immediately disappear?

Of course, no one can be sure what really would happen. By traveling through time, you would bend it and distort one of nature's fundamental properties, the fourth dimension. Who knows how this distorted dimension would react with the rest of nature's balance? You might just blow up the universe.

When the natural order of things is changed and disrupted, it results in a myriad of bizarre and far-reaching consequences that are impossible to predict, especially if the disruption is without precedent. It's best not to mess with Mother Nature.

Such is the quandary of the current investment environment.

Unprecedented central bank intervention in the markets on such a massive scale has messed with the natural order in the investment world. Central banks, rather than market forces, have controlled interest rates, money supply, and to a large extent stock and bond prices ever since the 2008 financial crisis.

Unencumbered markets work. Sure, they might go up and down more than we would like, but market forces compel money to gravitate to where it is most needed and efficient. Assets in a true capitalist system get properly allocated.

However, this central bank system allocates assets in all sorts of screwy directions. The normal free market checks and balances have been skewed — and in some cases they've been destroyed.

"Without the Fed's ability to maintain this artificial economic universe, the dam could burst."

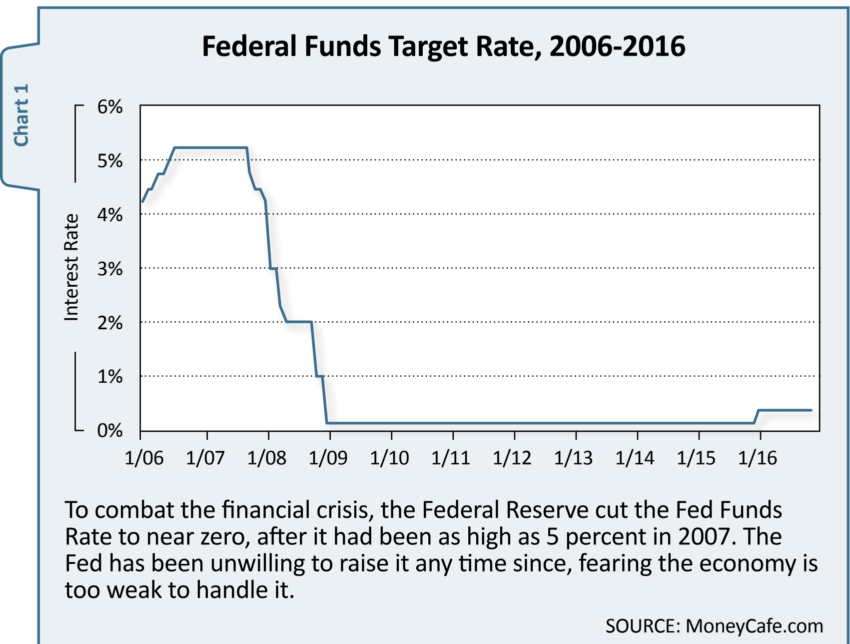
Now we have markets that depend on these central banks ... and these banks are running out of juice. Their ability to lower interest rates and stimulate markets and the economy is waning.

Without the Fed's ability to maintain this artificial economic universe, the dam could burst. Who knows where interest rates and markets should really be priced? We might be about to find out.

Longer term, we could see large-scale inflation or massive debt defaults. In the foreseeable future, the disruptions should be less severe, although we're already seeing a reversal of some of the major foundations that have supported the market over the last five years — the ultra low interest

rates, low commodity prices, and falling inflation environment.

In this issue, I will highlight several current High Income Factor Portfolio positions that should be ideally suited for the changing environment and are an important way to diversify. Let's first delve into the shifting tides we're up against.



To combat the financial crisis, the Federal Reserve cut the Fed Funds Rate to near zero, after it had been as high as 5 percent in 2007. The Fed has been unwilling to raise it any time since, fearing the economy is too weak to handle it.

SOURCE: MoneyCafe.com

Central Bank Distortions

I talk about the Fed a lot in this newsletter. You may think I'm picking on them, but I'm really not. I blame the politicians in Washington. Let me explain.

The financial crisis was serious stuff. There was a very legitimate possibility of financial collapse. Amid the panic, the government had to step in with extraordinary measures. The government instituted massive bailouts of financial firms (Fannie Mae, Freddie Mac, and American International Group) and the major banks.

The Treasury Department then instituted TARP (Troubled Asset Relief Program) to purchase toxic bonds and stocks from financial institutions in order to create markets that didn't exist and keep the banks in business. The Federal Reserve lowered the Fed Funds Rate to near zero (roughly 0.25 percent) from over 2 percent the previous spring and over 5 percent the previous year.

The Fed went on from 2009 through 2013 to institute three rounds of quantitative easing (QE for short) — where the Fed buys mortgage-backed securities, agency bonds, and Treasury bonds from banks — as well as Operation Twist, in order to hold longer-term rates down and inject liquidity into the banking system. In all, the Fed injected about $4 trillion into the banks.

Here's the thing. The Fed's actions were designed to be temporary emergency measures to stave off collapse and jump-start the economy. The idea was to hold up the economy until the government could enact fiscal reforms to generate real and sustainable economic growth.

Unfortunately, the politicians did nothing, and needed reforms never came. Today, we can only wait and see what president-elect Donald Trump and a Republican-controlled Congress will accomplish on this front.

Yet meanwhile, with limited tools — basically interest rates and money supply — the Fed has been left all alone to do all the heavy lifting. But make no mistake about it: The Fed never was designed to be this involved in the economy.

The Fed has so far raised the Fed Funds Rate just 0.25 percent above the Armageddon pricing of the financial crisis, eight years into the recovery.

That's just our own Federal Reserve Bank. Central banks all over the world have joined in the party and gone even crazier.

▶ About Tom Hutchinson

I've worked in finance my entire career, from the back office of a Wall Street firm to the floor of the New York Mercantile Exchange learning how markets work. Eventually, I became a financial adviser where I met with thousands of investors and managed the portfolios of hundreds over the course of about 15 years. I left my career as a financial adviser, writing for The Motley Fool as well as StreetAuthority LLC, researching companies, industries, and markets. In The High Income Factor, I can bring you the full benefit of my years of investing experience.

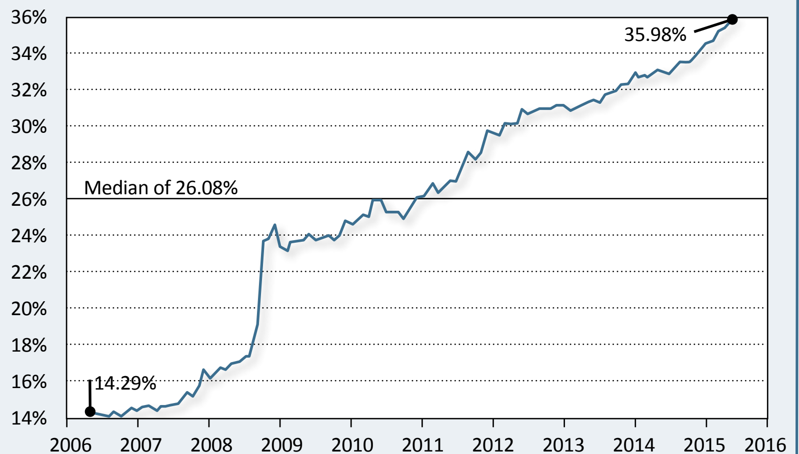
Massive bond buying programs are still underway in Europe and Japan. Rates in many countries are so low that they actually are paying negative yields (see the June 2016 issue for more on that). In fact, it is estimated that over $8 trillion (as of September) of sovereign bonds, mostly from Japan and Europe, currently are yielding negative interest.

While our own Fed has injected $4 trillion into the banking system, central banks globally have collectively increased balance sheets by over $17 trillion. Governments are incredibly indebted now — it is becoming a "new normal."

The global scale of unprecedented central bank intervention takes the risk to a far greater level. Even if our own Fed knows what it's doing, it will be hard-pressed to offset mistakes made globally. Artificial market manipulations on a global scale have made economic management a game of six-level chess.

Chart 2

Total Central Bank Balance Sheet/GDP Ratio, 2006-2016



This chart represents the ratio between central bank balance sheets and GDP for the U.S., eurozone, China, the U.K., Switzerland, and Japan from just before the financial crisis to present. The total assets of those six major central banks are at a new all-time high of 35.98 percent, versus 14.29 percent in May 2006. As central bank debts skyrocket, reflecting more and more of global GDP, it's a situation that could lead to an economic disaster unless the central bank interventions are curbed and traditional market forces are allowed to resume.

SOURCE: National Inflation Association

The U.S. is not an island, and accounting for the collective influence of all these banks seems impossible. And the chances that all these central banks are manipulating economic forces correctly and there will ultimately be no unfortunate and far-reaching consequences are slim indeed.

Inflation-Induced Growth

Interest rates and inflation are moving higher. U.S. core inflation (excluding food and energy) came in at 1.7 percent for the third quarter, with the Consumer Price Index over 2 percent for the same period. It may not seem like much, but these were the highest readings in two years.

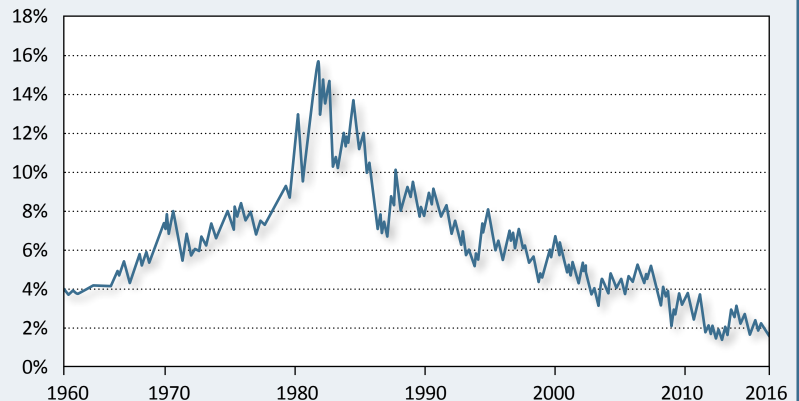
Renewed inflation also has driven longer-term interest rates higher. The 10-year Treasury yield has moved from 1.37 percent in July — an all-time low — to 2.1 percent in November.

Inflation-protected securities are pricing in an inflation rate of 1.7 percent over the next 10 years, up from 1.4 percent in July. There also has been an investor rush into Treasury inflation-protected securities (TIPS) in the past several months.

Let me step back a minute and address some well-justified skepticism. Those of us who remember the double-digit inflation of the '70s laugh at such numbers. The current 1.7 percent or 2 percent inflation numbers still are well below historical averages and not even above the Fed's

Chart 3

10-Year Treasury Rate, 1960-2016



10-Year Treasury rates were at an all-time low of 1.37 percent in July 2016, but inflation now is pressuring the rates higher. We are just at the beginning stages of this reversion to more historically normal levels.

SOURCE: Macrotrends.net

target inflation rate of 2 percent. Besides, many have been warning about the risks of inflation ever since the Fed first got aggressive. Not only has there never been any significant inflation, but inflation became so low that more economists were worried about *deflation*.

Low interest rates and loose money policies under normal circumstances can cause inflation. But inflationary pressures were offset by slow global growth and the ensuing commodity glut and price crash. Warnings of inflation have become so boy-who-cried-wolf that people have stopped making them. It has become perceived as an embarrassing and empty threat.

It reminds me of when my mother used to tell us not to sit around the house in a wet bathing suit or we'd get polio like Franklin Roosevelt. Even as a little kid I never believed Roosevelt became crippled from sitting around in a wet bathing suit. Besides, didn't I already endure that polio vaccine shot?

That said, I believe things very well might be different this time for a few reasons:

• **Commodity prices.** Commodity prices have crashed over the past several years. The Goldman Sachs Commodity Index (a sector benchmark with 24 commodities, including energy, agricultural products, metals, livestock, and lumber) fell from a post-recession high of over 750 in 2011 to 270 early this year. That's a 64 percent crash and burn across the whole sector.

The tumble was precipitated by a huge increase in production following shortages and high prices. The increased supply met with weak demand in a sputtering global economy.

Such a downward trend in the price of hard assets, combined with slow growth in Europe and significantly slower growth in China, offset any inflationary pressures. Indeed, deflation became more relevant.

The index recovered from 270 in February to 390 by midyear, and is currently at about 350. Prices have recovered at least somewhat from the lows and stabilized. The index may not soar any time soon, but it seems to have stopped falling.

That's big. Without falling commodity prices, the inflationary offset of the last five years will no longer exist.

• **Employment and wages.** The official unemployment rate is 4.9 percent, down from 10 percent after the recession. Wages, a key driver of inflation, are moving higher. In the third quarter, average hourly wages (as measured by the Department of Labor) rose 2.4 percent. While that is still below pre-crisis levels, it is the strongest wage growth since 2009.

• **Austerity is out.** Efforts to control spending seem to have gone out of style in much of the world. U.S. president elect Trump promised ambitious infrastructure programs.

Such a spike in public spending would drive more inflation. There seems to be a similar penchant for spending projects in the U.K. and other parts of Europe.

• **New central bank policy.** Rather quietly, central banks are changing long-standing policy with regard to inflation. The European Central Bank (ECB), the Bank of Japan (BoJ), and Fed Chair Janet Yellen all have either said or insinuated that the 2 percent inflation target may no longer apply. This is significant.

The level of 2 percent had been the desired level of inflation, above which they would consider and likely implement safeguards against too much inflation, like raising interest rates. Now they have expressed a willingness to let prices rise beyond the prior limits. They will welcome higher inflation rather than combat it.

The ECB and possibly the Fed appear to be targeting inflation-driven growth. The negative rate regime in Europe failed to deliver the desired growth by attempting to make people spend and invest money rather than earn negative interest. The very fact of negative rates spooked their confidence in the state of the economy and made them reluctant to spend.

Rising rates and prices can induce growth by creating urgency. If mortgage rates are rising, people will feel compelled to buy a house now instead of later when the rates are higher. By the same token, purchases won't be delayed because they will cost more in the future. Such is the theory.

Rates have started to rise, albeit slowly, with rising inflation expectations and a possible ending of the ECB's current bond buying program in the next year. The amount of

sovereign debt globally now has shrunk to $8.3 trillion from a high of about $10 trillion to $13 trillion this past summer.

Fed's Exit, Stage Left

The Fed has driven the current recovery by keeping interest rates at historic lows and flooding the system with liquidity. The low rates have served to buoy stock prices, as money has no place else to go to earn a decent return.

But rising rates and higher inflation will remove the Fed's main tool that propped up the market.

Without the low and falling interest rates, the Fed influence of the past eight years will be removed — and market forces will be unleashed. We will see just how much the Fed's meddling has retarded the natural market.

This is an example of one of the ways the Fed's policies may have misallocated resources. If interest rates were higher, many people would leave more money in safer assets. However, safe money has been forced by the Federal Reserve's actions into the stock market. Rising rates, a return to more natural forces, could cause an exodus of that reluctant money back out of the market and cause share prices to plummet.

Then there's inflation. A little more inflation from current levels might help the economy. Stronger inflation-induced economic growth may lift earnings and stock prices. Such a benefit may offset the risk of somewhat higher interest rates. Yet, once that inflation genie is out of the bottle, it is a herculean task to get it back in. (See the May 2012 issue for an in-depth discussion about inflation.)

More inflation could lead to more growth, and more growth could cause more inflation. Inflation can get out of hand rather quickly, especially if the money the Fed injected gets out of the banks and into the economy.

If the Fed falls behind and inflation rises too quickly, it may have to raise rates rather dramatically to combat it. A world of inflation and rapidly rising rates would be a big departure from the current environment. And it may well occur if the Fed loses its grip on the markets.

It's important to note that rising rates and inflation are not certain to occur in the near future. It is possible that an event disrupts the global economy and thrusts it into recession. China could fall apart, a huge terrorist attack could take place, or the Middle East could erupt, to name just three examples. The U.S., along with the world, seems to have avoided an impending recession for now. But that can change.

Yet, rising rates and more inflation are certainly a strong possibility . . . one that many investors have not prepared for. A diversification into assets that can perform in a different environment is a prudent step to take at this point.

There are two positions already in the High Income Factor Portfolio that are ideal for the current situation. Not only that, but these picks also should be solid income-producing investments even if their prices stay at current levels.

Agrium (AGU)

Food is a commodity, but it's unlike other core commodities. You can cut down on the clothes you buy and the energy you use, but people have to eat no matter what. So demand for the product is remarkably steady.

The supply side of the equation is a different story. The price of crops can be greatly affected by unpredictable factors like weather. Agricultural nutrients and fertilizers are impacted by global supply and natural gas prices.

Along with just about every other commodity in recent years, agricultural commodity prices have plunged. Performance of the stocks of these companies also has been abysmal. Some sellers of crop nutrients are down as much as 60 percent from recent highs.

But if we step back and take a wider look, it's clear that long-term demand will be strong. The world population continues to grow while per capita food consumption also rises.

The World Bank estimates that global food demand will rise 50 percent between 2010 and 2030. At the same time, the supply of fresh water (for irrigation) and arable land (for farming) is decreasing. The world will have to produce more crops on less land, and companies that deal in agricultural commodities will be front and center in that effort.

Agrium is a global supplier of agricultural products and services. The company operates state-of-the-art, direct-to-grower retail stores selling a wide variety of farm services like soil and pest testing, crop inputs (fertilizers and pesticides), and seeds for some 50 different kinds of crops. It is the largest retailer of its kind in the world, with 1,400 facilities throughout the U.S., Canada, Australia, and much of South America.

The retail stores account for most of the revenue. The rest comes from wholesale crop nutrients, primarily the big three: nitrogen, potash, and phosphate fertilizers. These are the essential nutrients that enhance crop yield.

The fact that Agrium not only offers all three major fertilizers instead of just one, but also has the huge retail business, makes the stock less susceptible to downturns. As a result, AGU has held up much better through the sector troubles than its peers.

The thing that makes AGU a great stock is this: Because of recent expansions and acquisitions and lower capital spending, the company is in a position to grow earnings and the dividend even if conditions in the industry stay lousy for a while. When commodity prices actually recover, the stock should kill it.

In the meantime, the stock pays a 3.67 percent yield. There is a big dividend growth story here. Here are the annual per share payouts from recent years.

YEAR	DIVIDEND
2011	$0.11
2012	$0.725
2013	$2.25
2014	$3.00
Current	**$3.50**

The company obviously has been intent on growing the dividend. It's also worth noting that the environment for agriculture has been terrible since 2012. From 2012 to 2015, revenues have fallen from $16.7 billion to $14.8 billion.

However, even amid declining revenues, the company was able to grow free cash flow per share by a compound annual growth rate (CAGR) of 41 percent since 2013. **Agrium (AGU) is a buy at or under $95 per share for the Wealth Builder Portfolio.**

Covanta (CVA)

Covanta is the largest U.S. producer of energy-from-waste (EfW). The company accounts for about two thirds of U.S. EfW production and processes roughly 5 percent of all waste in the country.

The formula is simple. Municipalities and businesses pay Covanta to take waste away. It then incinerates the waste.

The steam produced from the high temperature combustion is used to produce electricity, and the metal recovered is sold to recyclers. The company essentially recycles what is left over after recycling.

It's a particularly good business because Covanta doesn't have any input costs. In fact, the company is paid for its input source and those payments make up about two thirds of revenues. Other companies that produce electricity have to pay for the coal or natural gas necessary to generate it.

The electricity sold accounts for 26 percent of revenues, and metal and other materials separated in the process account for another 7 percent. While metal that is produced and sold to recyclers seems like an afterthought, it actually is significant. Covanta produces 500,000 gross tons of metal per year, enough steel to construct five Golden Gate Bridges and enough aluminum to make 2 billion soda cans.

Waste is a huge problem globally. The world is producing more waste than ever before and certain areas are running out of landfills to put it.

As well, landfills are toxic to the environment, producing more toxic greenhouse gas emissions than just about anything else. The total of the waste we are producing and the accumulated waste over the years is causing major environmental problems.

Covanta is considered very environmentally friendly because modern filtration systems enable the company to burn waste without sending the toxins into the air. It also saves the environment

Continued on page 8

The High Income Factor Portfolio

THE HIGH INCOME PORTFOLIO

Recommendation	Ticker	Entry Date	Entry Price	Recent Price	Buy at or Under	Current Yield	Effective Yield	Dividend Pay Date	Total Return
Terra Nitrogen	TNH	01-Apr-12	$249.75	$107.25	$150.00	9.62%	4.13%	12/6/16	-32.59%
Riocan REIT	REI-UN.TO	20-Mar-13	$26.97	$19.90	$29.00	7.12%	5.25%	11/15/16	19.14%
Brookfield Infrastr Ptnrs	BIP	03-Jun-13	$24.00	$33.71	$30.00	6.76%	9.50%	12/9/16	64.94%
Main Street Capital	MAIN	21-Aug-13	$29.21	$33.99	$32.00	6.53%	7.60%	12/1/16	46.47%
Western Refining, Inc.	WNR	26-Mar-14	$20.25	$26.43	$28.00	5.75%	7.51%	2/2/17	39.73%
Blackstone Group	BX	07-Jul-15	$40.00	$24.04	$35.00	6.91%	4.15%	2/6/17	-33.75%
Care Capital Properties	CCP	18-Aug-15	$34.97	$24.28	$32.00	9.39%	6.52%	12/2/16	-23.17%
AmeriGas Partners LP	APU	10-Jun-16	$43.00	$45.39	$43.00	8.28%	8.74%	11/18/16	5.65%
Cedar Fair, L.P.	FUN	23-Jun-16	$57.70	$59.99	$58.00	5.50%	5.72%	12/15/16	5.46%
Covanta Holding Corp.	CVA	27-Oct-16	$14.70	$14.50	$16.00	6.90%	6.80%	1/9/17	-1.36%

THE WEALTH BUILDER PORTFOLIO

Recommendation	Ticker	Entry Date	Entry Price	Recent Price	Buy at or Under	Current Yield	Effective Yield	Dividend Pay Date	Total Return
PepsiCo	PEP	01-Apr-12	$66.74	$108.72	$90.00	2.77%	4.51%	2/2/17	84.08%
Eli Lilly	LLY	01-Apr-12	$40.48	$74.02	$75.00	2.76%	5.04%	1/11/17	113.72%
Vodafone	VOD	27-Sep-12	$28.72	$27.28	$34.00	6.20%	5.88%	2/6/17	5.40%
Altria Group	MO	26-Mar-15	$50.00	$65.84	$50.00	3.71%	4.88%	1/12/17	35.51%
Seagate Technology	STX	23-Jun-15	$53.80	$34.49	$45.00	7.31%	4.68%	11/23/16	-29.34%
Agrium	AGU	25-Apr-16	$86.40	$95.47	$95.00	3.67%	4.05%	1/23/17	11.59%
Amgen Inc.	AMGN	25-Aug-16	$169.92	$138.45	$170.00	2.89%	2.35%	12/9/16	-18.38%
Magellan Midstream Ptnrs	MMP	22-Sep-16	$69.80	$66.40	$70.00	4.89%	4.65%	11/14/16	-3.67%
Digital Realty Trust#	DLR	—	—	$94.88	$80.00	3.58%	—	—	—
Merck & Co.#	MRK	—	—	$60.51	$45.00	2.97%	—	—	—

INCOME STRATEGIES PORTFOLIO

Recommendation	Ticker	Entry Date	Entry Price	Recent Price	Buy at or Under	Current Yield	Effective Yield	Dividend Pay Date	Total Return
BlackRock Enhanced Cap Fund	CII	01-Jan-12	$12.50	$12.95	$14.00	9.27%	9.60%	11/10/16	50.25%
PowerShares Sr Loan Port	BKLN	25-Sep-13	$24.77	$23.07	$25.00	4.32%	4.02%	12/27/16	6.54%
People's United Financial	PBCT	25-Aug-14	$14.90	$16.65	$16.00	4.08%	4.56%	11/18/16	23.60%
Duke Energy	DUK	06-Mar-15	$75.00	$79.65	$75.00	4.29%	4.56%	12/16/16	13.41%
iShs Int Rte Hdgd Corp Bnd	LQDH	17-Dec-15	$91.65	$92.14	$94.00	1.60%	1.61%	11/15/16	1.44%
Pshares Ins Nat'l Muni Bond	PZA	23-Feb-16	$25.58	$25.74	$26.50	2.84%	2.86%	12/1/16	2.33%

Notes on all portfolios: In order to receive the dividend payment, you will need to own the stock several weeks before the pay date. The "Total Return" column includes all reinvested dividends at concurrent recommended buy prices. Returns calculated based on a purchase of $1,000 of the security on the listed entry date and price. The "Effective Yield" column reflects the yield investors receive assuming they bought at the entry price and followed all subsequent recommendations. #Denotes recommendation not yet purchased. To see the chart of previous "sold" positions, subscribers can log onto www.highincomefactor.com (under the "Portfolio" tab). All chart data is as of close November 8, 2016.

Continued from page 6

from the burning of the coal or natural gas necessary to produce the same electricity. It also saves metal resources and the energy necessary to produce products from scratch.

The environmentally friendly aspect should make Covanta a desirable option for municipalities going forward. The company already won the contract for New York City, and other cities should follow. The EfW solution is much more widely used in Europe than it is here, and wider adaptation in the U.S. is likely.

However, recent times have been tough for Covanta. It has been negatively impacted by the commodities crash, as prices for metals and electricity have fallen and hurt profitability.

The price of CVA has fallen from over $20 per share in the summer of 2015 to $14.50 today. I believe this creates an opportunity.

The company has been able to keep revenues relatively steady by improving margins and expanding. The current dividend yield is a whopping 6.90 percent, and should be secure even if commodity prices stay at current levels. But like Agrium, Covanta will benefit mightily when commodity prices rise.

Covanta offers a fantastic solution to one of society's major problems. The recent commodity sell-off has clouded the picture of what a great business this is, but the current environment won't last. **Covanta Holding Corp. (CVA) is a buy at or under $16 per share for the High Income Portfolio.**

Actions to Take Now

Action No. 1: If you don't own it yet, look for an opportunity to buy **Agrium (AGU)** at or under $95 for the Wealth Builder Portfolio.

Action No. 2: If you don't already hold the stock, watch for a chance to buy **Covanta Holding Corp. (CVA)** at or under $16 per share for the High Income Portfolio.

Action No. 3: Be sure to visit our website, www.highincomefactor.com, to find past monthly issues and weekly updates. For password assistance, you can contact my team at 800-485-4350 or customerservice@newsmax.com.

Sincerely,

Tom Hutchinson
Editor, The High Income Factor

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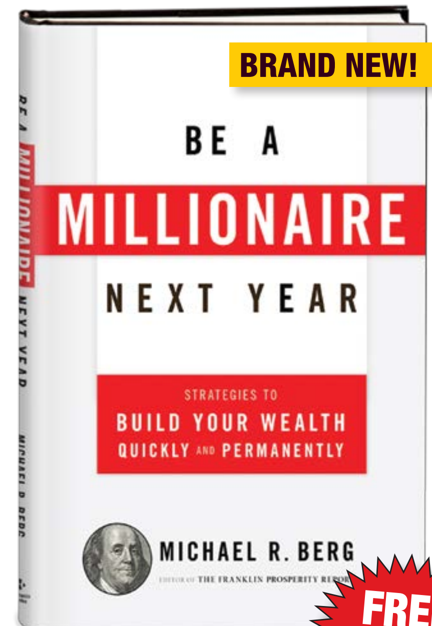

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- How to dramatically lower your risk of losing money in the stock market. Ridiculously simple yet so few people do it!
- **How a bull market can cause you to lose a fortune.** Little-known trap revealed on page 58.
- Type of investment that could earn you more than 6 times the return of other stocks with far less risk!
- **6 ways to use other people's money to become a millionaire**
- How to get "dividends" out of a non-dividend paying stock
- **The trick wealthy people use to generate big returns even when stock prices don't move.** Page 81 shows you how to make money in the market whether a stock price rises, falls, or stays flat.
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