Weekly Commentary
May 17, 2010

The Markets

"Hot potato" is a favorite children's game. Unfortunately, as adults, we're playing an economic version that has the potential for much more serious consequences.

It started with consumers going into debt over their heads to help fund an ever-increasing lifestyle.

For example, total household debt rose from $1.1 trillion in 1978 to $13.5 trillion at the end of 2009, according to the Federal Reserve. That's more than a *12-fold* increase over the past 31 years. By contrast, our economy, as measured by gross domestic product, grew from $5.3 trillion to $13.3 trillion during that same period--a more modest 2.5-fold increase, according to the Department of Commerce.

Then it moved to the financial sector racking up huge liabilities on the back of newfangled derivative securities.

Total financial sector debt, which includes various government-related enterprises and private financial institutions, rose from $0.4 trillion in 1978 to $15.6 trillion at the end of 2009, according to the Federal Reserve. That's a *39-fold* increase over the past 31 years. With this high leverage, is it any surprise that our banking system nearly went kaput in 2008?

Then it moved to the local, state, and federal governments incurring unsustainable debt to keep the world economy from collapsing.

Total U.S. local, state, and federal governmental debt rose by a *factor of 11* from 1978 to 2009, according to the Federal Reserve. Overseas, the picture looks bleak, too, as many of the European Union countries are sitting on huge piles of IOUs that look increasingly less likely to be paid back in full. Not surprisingly, gold prices hit a record high last week as people turn to the perceived safety of the yellow metal in times of doubt, according to the *Financial Times.*

With the potato of debt having passed from party to party over the past three decades, the financial markets are now saying the potato stops here. As John Mauldin, president of Millennium Wave Advisors, LLC, says, "You don't cure a debt problem with more debt unless you have a clear path to grow your way out of the debt." In the U.S., we can grow through population growth and productivity gains. That, coupled with higher taxes and significantly lower spending, may do the trick. In Europe, structural headwinds make the growth story much more difficult and that's partly why the value of the euro is declining and street protests are rising.

How this unwinding of debt plays out with the world populace will likely affect the financial markets for years to come.

Data as of 5/14/10	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	2.2%	1.9%	28.6%	-8.9%	-0.5%	-2.4%
DJ Global ex US (Foreign Stocks)	2.6	-6.4	23.6	-10.6	3.0	0.8
10-year Treasury Note (Yield Only)	3.4	N/A	3.1	4.7	4.1	6.5
Gold (per ounce)	2.8	12.0	33.6	22.6	24.1	16.2
DJ-UBS Commodity Index	-0.6	-8.1	6.4	-9.5	-2.7	2.2
DJ Equity All REIT TR Index	3.7	14.3	70.5	-9.0	3.4	11.2

Notes: S&P 500, DJ Global ex US, Gold, DJ-UBS Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT TR Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.
Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association.
Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not applicable or not available.

WHAT IS ONE OF THE BEST INVESTMENTS you can ever make? No, we're not talking about the stock market, commodities, or gold. Instead, we're talking about investing in your own education. As the chart below shows, there is currently a direct correlation between the level of formal education and the unemployment rate. The more educated you are, the less likely you are to be unemployed.

Educational Attainment	Unemployment Rate April 2010
Less than high school diploma	14.7%
High school graduate, no college	10.6
Some college or associate degree	8.3
Bachelor's degree and higher	4.9

Source: Bureau of Labor Statistics

The fact that the most highly educated people in our population have a relatively low unemployment rate of 4.9% may help explain why consumer spending hit an all-time high in March, according to MarketWatch. People with a higher education tend to earn more and since 95% of that demographic is employed, that has helped reinvigorate consumer spending.

The overall unemployment rate of 9.9% is unacceptably high and understandably grabs the headlines, but looking at the composition of that number suggests the damage to the economy might not be as bad as first thought. Digging beneath the headlines like this helps us make better assessments of the current economic and investing environment.

Weekly Focus – Think About It

It's a shallow life that doesn't give a person a few scars."
--Garrison Keillor

Best regards,

Tony Hartman

P.S. Please feel free to forward this commentary to family, friends, or colleagues. If you would like us to add them to the list, please reply to this e-mail with their e-mail address and we will ask for their permission to be added.

* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.
* The DJ Global ex US is an unmanaged group of non-U.S. securities designed to reflect the performance of the global equity securities that have readily available prices.
* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.
* Gold represents the London afternoon gold price fix as reported by the London Bullion Market Association.
* The DJ Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.
* The DJ Equity All REIT TR Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.
* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.
* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.
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