

Interim Market Update



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May 2007

A WORD TO THE WISE

Chairman Bernanke proclaims that the world is awash with savings. He likewise believes that as the U.S. is the most attractive country in the world for investors, we have become the beneficiaries of those savings. We ask you, where in the world did he come up with such an idea? Savings can be obtained only through income creation coupled with the denial of current consumption. We wonder how much of the investment money from those abroad comes from savings, and how much from borrowed funds. What we do know, is that in 2006 the U.S. consumer had no savings; he did, however, have cash flow due to depreciation and other non-cash items. Note the following 2006 numbers:

Personal Savings	(\$102.1 B)
Non-cash Items	<u>\$304.8 B</u>
Cash Available	\$202.7 B
Net Borrowing	<u>\$1,012.0 B</u>
Available to Spend on Investments	\$1,214.7 B

As you can see, only through borrowing does the U.S. consumer have any money for investment. He has already consumed all of his income, plus reduced savings by \$102.1 billion. The question then becomes how long can this continue? We are frank to admit that never in our wildest dreams did we believe borrowing could accelerate as it has. What we do know is that we are “eating our seed corn,” which means our future harvests will become less and less. Debt does not go away, and when the music stops, only income will retire debts. With income in short supply, the major source of debt payment must come from selling assets. In our opinion, all markets—except government bonds—are vastly overvalued. Please be extremely careful as we are in perilous times. You may want to exit the party before it’s too late. The door is not large enough for all of us to leave at one time.



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