



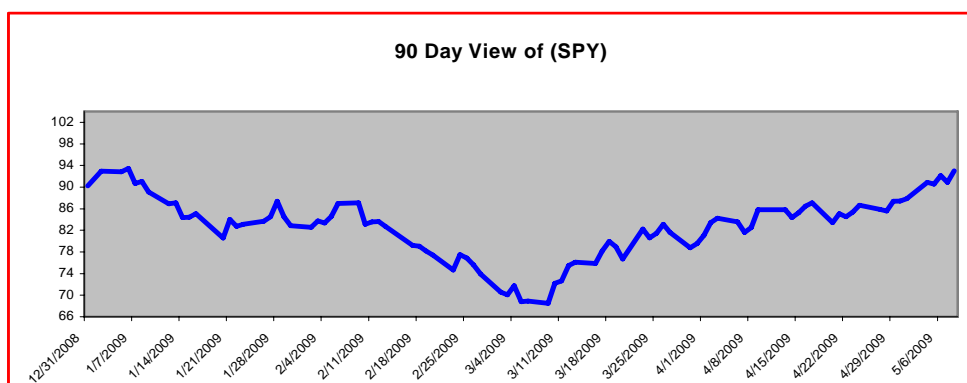
FINANCIAL INSIGHTS

WATCHING THE
MARKETS CLOSLEY.
SO YOU DON'T
HAVE TO.

A newsletter from James Horton Private Money Management

Market Review for Week Ending 5-8-09

Last week the market advanced 5.79%. This was certainly a nice advance but most of the gains came exclusively from the financial sector. Driving financial stocks up was the results of the bank stress test (a failed public relations ploy in my opinion).



The more I learn about the ideas and thinking of this administration the less confidence I have.

For example, the government wants banks to make more loans but at the same time they want them to improve their financial ratios. How do you do both at the same time? It defies logic. On top of that if banks focus on hoarding cash and improving capital ratios the economy cannot grow. Banks are learning quickly that having the government involved in your business sucks so many banks want out of TARP as quick as possible. However there is an important catch in giving back the TARP money. If you pay the TARP money back you immediately lose the FDIC guarantee you currently enjoy when you issue short-term debt. This will be an interesting issue to follow and a great way to take the temperature of the banking industry. Banks will not be giving TARP money back until they are convinced the credit crisis is behind us.

What is bothersome to me is the fact we still have not embraced that the days of high levels of borrowed money is gone for quite a while. It won't happen again until enough time has passed that we have forgotten the devastation it ultimately causes. In many ways it is like watching a professional sport where every athlete is taking steroids and then in one day you decide that steroids will no longer be allowed. The sport will no longer be the same to watch. An economy coming off high levels of leverage will not be the same for many decades and you must adapt your thinking to accept the new reality. I see no such "recognition" yet.

Another disturbing act by the current administration involves Chrysler. It seems to me that their actions are corrupting the constitution and contract law. There are rumors that the parties involved in this deal that did not want to cooperate were threatened with IRS and SEC audits. Is the very branch of government that enforces our constitution trying to circumvent it to fulfill a political agenda? And ironic

enough the ten billion dollars we the taxpayer have given to Chrysler to save them is the exact amount of money that has gone out the back door and paid to fund union benefits like VEBA health trusts and pension plans. If all of this is true then we are seeing a redistribution of wealth from bondholders to unions. Oddly enough, few have noticed that all we hear about is that we must save the American Auto Industry yet we are giving Chrysler to an Italian car company (Fiat).

On Friday we learned that the unemployment rate is now at a 26 year high of 8.9%. Like most government statistics when you look at how it is actually calculated it makes very little sense. For example, this level of unemployment excludes someone who is unemployed but did not actively look for a job in the past four weeks. Only to our government would these people no longer be counted as unemployed! So who knows how high the rate really is but I do believe it sheds light on what I said last week, which was using a level of unemployment of 10% and calling it a stress test is silly.

If General Motors has there way auto dealers will soon be adding to the level of unemployment. General Motors intends on dramatically reducing the number of dealers they have. The goal is to eliminate poor performing car brands and poor performing car dealers. This will have a devastating impact on many states and communities for it will increase unemployment and reduce state and local taxes. I continue to believe that the full impact of the demise of the auto industry is not understood nor properly priced into the stock market.

On a much brighter note we received another meaningful increase in income from one of our companies last week. This is one of the clear advantages of owning a company that sells consumable products in two hundred countries. In difficult times like these were you have to worry about issues such as a companies cash flow, ability to refinance its debt, and reduction in profits, an increase in the annual dividend is one of the strongest statements a company can be making about its future.

Looking toward the market I mentioned last week that I would be watching the technology sector closely. Despite the positive performance in the S&P 500 index the technology sector went nowhere. A respite at this point is to be expected. If stocks can simply just hover at these levels, without incurring a large decline in prices, it will be a great sign and a signal to me that it is time to start buying again. A useful metaphor for the market at this stage is that of a marathon runner. About halfway thru a marathon a runner is often physically challenged and success or fail is determined by the ability to catch a “second wind”. If the market can catch its second wind here that will be good news. If not, it will be sucking wind, and this rally will fail and the gains will go as quickly as they came.

With that in mind, I will continue to watch the markets closely **so you don't have to.**

