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NEWSLETTER

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# The Case for Optimism

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We try to be optimistic in our outlook provided the circumstances warrant such an attitude. Noted British historian Paul Johnson has written that at every given point in time, you can always point to good news and bad news – the only difference is the balance between the two and what gets the media's attention.

Despite the recovery in the global economy and markets since the early part of this year, the general sentiment and confidence level among many people today remains negative. Much of that is driven by concerns about our economy – still the engine of global growth. These concerns are justified given the stubbornly high unemployment rate, a depressed housing market, and rapidly rising government deficits. Without dismissing these challenges, it's important to recognize that many of the previous challenges we have discussed in this newsletter have been corrected and we view this as positive.

On more than one occasion, we discussed the rapid growth within the hedge fund and private equity industries as being overdone. Fueled by low interest rates and high fees, many of these firms took on evermore risk and leverage to achieve their returns. As often occurs, too much money flooded into these asset classes and the party ended with disappointment. As Warren Buffett is fond of saying, you only find out who is swimming naked when the tide goes out. Many of these funds have closed their doors and we believe the industry has declined to a more appropriate level within the overall financial markets.


As far back as April of 2007 we highlighted the risks we thought existed in real estate given the constant repeating of the now infamous cliché: "No one ever lost money in real estate". Of course, the last three years have proven that real estate is not a special asset class and it is possible to pay too much for a property. Fortunately, real estate appears to be stabilizing though has not yet entered a new growth phase. Investors willing to take advantage of distressed prices are emerging and the historically low level of interest rates should help clear the market of excess inventory.

In 2006 we reviewed *The Future for Investors*, the then newly published work by Dr. Jeremy Siegel of the Wharton School at the University of Pennsylvania. Dr. Siegel remains one of the best known researchers of long-term returns in the stock market and his book *Stocks for the Long Run* is often cited as one of the all-time ten most influential books on investing. Though the stock market has rallied since Dr. Siegel's presentation in September of last year, we find his current outlook that market valuations present excellent valuations for long-term investors both exciting and comforting. Professor Siegel also noted in September that historically when then market declines 50%, not only do you achieve a 25-30% return in the following year but also very strong returns over the following three to five years.

To sum up our case for maintaining an optimistic outlook, we feel markets are continuing to work off much of the excess capacity created over the past decade and the curative process of capitalism is working. As always, challenges exist, but over time, the positives outweigh the negatives and the dire predictions about America's decline are probably overstated. We may not see the rapid growth of the past but we will see solid growth and are currently able to invest at valuations that have historically provided attractive returns.