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Greetings,

Very little has changed with the economy over the last three months. The U.S. economy continues with its gradual improvement, but at a snail's pace. The economy is simply a little less bad than it was late last year. The same goes with Europe. Most of Europe is likely in a recession. What has changed is the perception of what is happening. Six months ago, there was a fear that Europe was falling off a cliff. There was also a fear that a European contagion would spread to the U.S. economy, thus causing another recession. One of the reasons why I didn't think that the domestic economy would be adversely affected by Europe is that our economy doesn't rely heavily on exports to Europe. This of course is rarely chatted about on the financial news shows because, as I expect we also know, the financial news shows prefer to focus on all the negative things that could happen, as opposed to objective financial data. All of those fears have not materialized. The market moves in the short term are caused by emotion, fear and greed. Since the fear has been taken out of the market, at least for now, the market indices have risen on less volatility.

The bull market is now three years old. What I find astounding (for lack of a better word) is that the vast majority of individual (retail) investors have basically missed a very strong bull market. There is statistical data that is gathered from both mutual fund inflows and the discount brokers such as Charles Schwab & co., T.D. Ameritrade and E*TRADE which tracks how individual (retail) investors trade. The data still show that the retail investor remains on the sidelines, sitting out this bull market. What is even more remarkable is that in the first two years of the bull market, there were net outflows from domestic equity mutual funds and net inflows into bond funds. That is one of the reasons why bonds are so expensive and long term interest rates are so low. Over the last six months, there has been a trickle of new cash coming into the market. That is one of the reasons why I am optimistic as far as the stock market, at least for the next two years. My reasoning is that if the market can do well with virtually no new cash coming in, then the market should do even better if or when new cash does find its way in. One other reason I am optimistic is because of stock buybacks. I wrote in a previous letter that corporations were flush with cash and as a result of that, would be putting that cash to work with both dividend increases and increases in their stock buyback programs and this is coming true. Technology companies are especially cash rich and they are continuing to put that cash to work by purchasing their own stock. I expect this to continue for at least the next two years.

I do not get any kind of perverse pleasure from the fact that so many individual investors have missed out on this bull market. What I do, on occasion, is to think back to the time that I saw a speaker at the 92nd St. Y in NYC back in 2002. That was during the worst part of bear market #1. He was a legendary money manager. I would say that he was in his 70's at the time. I do not recall his name. What impressed me at the time about him and the event was that he didn't just spout like many like to do. He made the event interactive. He challenged the attendees with provocative, intelligent questions. Most of

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the answers were also intelligent. What has stayed with me for ten years was that at the conclusion of the event, this speaker said that most importantly, with your clients, "be right". So while I get no satisfaction with the fact that so many people (including professionals) were wrong over the last three years because they either stayed in cash or went into the perceived safety of fixed income, I do pride myself in the fact that I was right three years ago in my call that when things were so bleak, the market would quickly recover. The result being that we have made a nice recovery from the most brutal bear market since the early 1930's.

While listening and watching CNBC for much of the day, there is something that I still find fascinating. These pundits have been stating that there is now too much optimism in the market with the recent strong performance by the indices. I am not sure whether these people who like to chat on TV either don't realize or just perhaps never knew that the market climbs a wall of worry. Just because the market has had one of its best quarters in 15 years doesn't mean that all of a sudden there is a lot of optimism out there. Far from it. How many people do you know who are optimistic about the stock market?? I know very few who are, that is for sure! If people were optimistic, then there would be new cash coming into the market. Actions tend to speak louder than words. If there was optimism in the investor community, stocks would be expensive relative to fixed income and relative to historical valuations. Even with the recent run up in the market, stocks are still cheap, based on historical valuations and are mispriced compared to the expensive bond market. That is because historically, when interest rates are low, stocks tend to be expensive because you can't get the return necessary in fixed income for there to be competition to equities. This has not been the case over the last couple of years. For the dividend yield on the S&P 500 to be comparable to that of the 10 year Treasury bond is absurd, at least in my view.

There has been much chatter lately about the slowdown in the China economy, especially during the last week. Without a doubt, the China economy is slowing down. No one can deny that. I have also heard that the Chinese real estate market is overheated and could be in a bubble. Paul Krugman (the award winning columnist for the NY Times) not long ago wrote that the bursting of the China real estate bubble will lead to a world wide recession. While I have become much more informed about the global economy over the last couple of years than I ever thought I would be, I humbly admit that Mr. Krugman knows a heck of a lot more about China's real estate market than I do. While I don't question Mr. Krugman's knowledge in this area, I do question his motives as well as many others in the print media. Negative headlines sell papers. I would like to think that we all realize that. I do believe that the real estate situation in China poses a potential problem. Here is where I differ with many of these naysayers. Unlike the incompetent people who run our country and who fiddled as the domestic economy burned in 2008 (ignoring the warning signs in 2006 and 2007), I have confidence that the Chinese government will do what it takes to avoid the same collapse that happened with our economy. As far as the China economy now; it is growing at an 8 ½% clip. This year going forward, it is expected to "slow" to a 7 ½% growth rate. While a 7 ½% growth rate is slower than it has been, it is still nearly three times the 3% growth rate of the U.S economy. The last time the U.S. economy had a growth rate even resembling the

Chinese economy; I was still living with my parents, I had a full head of hair and the N.Y Mets were the best baseball team in New York.

If you have any questions or if you have anything that you would like to discuss, then please either email me or give me a phone call.