ECONOMIC PICTURE NEEDS MORE PAINT.

For the last two months, the U.S. equity markets have continued to dodge the negative bullets. As the markets continue the recovery, the "what goes up must come down" mantra continues to increase in volume. In addition, we had the "Everyone knows that September is the worst month for the market" diatribe being chanted. Both of these sentiments have resulted in a month were our portfolios were up over 7%. Some fail to learn that the only truly reliable source for a downturn is the equity market itself, not the calendar or what happened in the past. Similar to the months leading up to the sharp downturn in 2008, the market will begin to give indications of weakness before a sizable drop. In the meantime, we will continue to analyze the economic and fundamental data for guidance.

The baffled negative pundits still discount the 3+ trillion dollars of "scared" cash sitting on the sidelines. Investment dollars in cash are earning almost nothing, while bonds are earning 3-5%. Meanwhile the stock market has earned over 15% in the third quarter and is up almost 50% since March. With lack of inflationary pressures, the Federal Reserve Banks do not see the need for a meaningful increase in interest rates for some time. Consequently, investors who need their assets to grow are slowly putting the money to work in equities along with bonds.

The third quarter earnings season will be helpful in giving a clearer indication of the strength in the market. As with the second quarter, we believe our stocks in the portfolio will continue to outperform the expectations. Of course, the market is extremely fickle during earnings seasons that follow quick run ups in stock prices. The skittishness can give us tremendous insight to the underlying strength and validity to a stock's current price versus its perceived value.

Much has been made of the lack of volatility in the recent months which is a sign that short term traders that ruled the market in late 2008 and early 2009 are having a difficult time. We expect volatility to increase as more information is provided by the third quarter numbers.

WALL STREET JUST DOES NOT LEARN.

One year later the "too big to fail" institutions have only gotten bigger but continue to scream for no increase in regulations. Make no mistake about the fact that the financial system MUST have an increase in regulation. However, only regulating the U.S. based financial institutions would not solve the problem. A global financial regulating body is necessary for progress in cleaning up the oft-maligned industry. Like it or not we have a truly global banking sector.

Merrill Lynch's inadequacies finally brought them down, but Bank of America bought the mismanaged assets. Wachovia's "grow at all costs" philosophy ended up costing them the company and is now owned by Wells Fargo. Citigroup's train wreck, Smith Barney, was banished to Morgan Stanley by the perpetually inept Citigroup. Brokerage firm UBS, headquartered in Switzerland, was forced to turn over a list of U.S. clients that were using strategies to elude paying Federal taxes. Hiding behind strict privacy laws, Swiss financial institutions have long enjoyed foreign deposits that were being "hidden" from taxes. Ever since the three pillars of our financial system, insurance firms, banking institutions, and investment houses were allowed to merge, our financial system has become increasingly unstable. The bigger is better attitude must be curtailed for a stronger financial system to emerge.

However, if we only burden U.S. based financial institutions with more regulation, then the money simply moves overseas with a click of a mouse. So any meaningful regulation MUST have global buy in to have the teeth to be effective.

HEALTH CARE DEBATE.

The United States provides the best health care in the world. People come from all over the world to take advantage of our expertise of our doctors. We do not have a health care crisis in America. We have a problem paying for the services. Somehow, U.S. culture has turned into our inalienable right to “live forever, free”. When we do finally give in to the inevitable death, our loved ones can always sue the hospital and doctors to pay for our death! Only in America!!

The United States takes the rare stance that anyone who is sick must be treated regardless of their ability to pay. If they have no insurance and no money, the government will pay. About 59 million people are on Medicaid today—which means that a decade from now about a quarter of the total population would be on a program originally sold as help for low-income women, children and the disabled.

An op-ed piece in The Wall Street Journal on September 11, 2009 makes some interesting points to the current situation. The following are some of the article:

Mr. Obama depicts a financial crisis in the entitlement state, noting that "our health-care system is placing an unsustainable burden on taxpayers," especially Medicare. Unless we find a way to cauterize this fiscal hemorrhage, "we will eventually be spending more on Medicare than every other government program combined. Put simply, our health-care program is our deficit problem. Nothing else even comes close."

On this score he's right. Medicare's unfunded liability—the gap between revenues and promised benefits—is currently some $37 trillion over the next 75 years. Yet the President uses this insolvency as an argument to justify the creation of another health-care entitlement, this time for most everyone under age 65.

As astonishing, Mr. Obama claimed he can finance universal health care without adding "one dime to the deficit, now or in the future, period," in large part by pumping money out of Medicare. The $880 billion Senate plan he all but blessed this week would cut Medicare by as much as $500 billion, mainly by cutting what Mr. Obama called "waste and abuse." Perhaps this is related to the "waste and abuse" that Congresses of both parties have targeted dozens of times without ever cutting it.

Apparently this time Mr. Obama means it, though he said this doesn't mean seniors should listen to "demagoguery and distortion" about Medicare cuts. That's because Medicare is a "sacred trust," and the President swore to "ensure that you—America's seniors—get the benefits you've been promised."

So no cuts, for anyone—except, that is, for the 24% of senior beneficiaries who are enrolled in the Medicare Advantage program, which Democrats want to slash by $177 billion or more because it is run by private companies. Mr. Obama called that money "unwarranted subsidies in Medicare that go to insurance companies—subsidies that do everything to pad their profits but don't improve the care of seniors."

In fact, Advantage does provide better care, which is one reason that enrollment has doubled since 2003. It's true that the program could be better designed, with more competitive bidding and quality bonuses. But Advantage's private insurers today provide the kind of care that Mr. Obama said he would mandate that private insurers provide for the nonelderly—"to cover, with no extra charge, routine checkups and preventative care."

Advantage plans have excelled at filling in the gaps of the a la carte medicine of traditional Medicare, contracting with doctors and hospitals to coordinate care and improve quality and covering items such as vision, hearing and management of chronic illness. If seniors in Advantage lose this coverage because of the 14% or 15% budget cut that Mr. Obama favors, well, that's "waste and abuse."

Mr. Obama did also promise to create "an independent commission of doctors and medical experts charged with identifying more waste in the years ahead." That kind of board is precisely what has many of the elderly worried about government rationing of treatment: As ever-more health costs are financed by taxpayers, something will eventually have to give on care the way it has in every other state-run system.

But Mr. Obama told seniors not to pay attention to "those scary stories about how your benefits will be cut, especially since some of the folks who are spreading these tall tales have fought against Medicare in the past and just this year supported a budget that would essentially have turned Medicare into a privatized voucher program."

This is a partisan swipe at one of the best GOP ideas to rationalize the federal budget, despite Mr. Obama's accusations that his opponents want to do "nothing." This reform would get Medicare out of the business of spending one out of five U.S. health dollars, and instead give the money directly to seniors to buy insurance to encourage them to be more conscious of cost and value within a limited budget. Democrats would rather have seniors dance to decisions made by his unelected "commission of doctors and medical experts."

Mr. Obama also called for "civility" in debate even as he calls the arguments of his critics "lies." So in the spirit of civility, we won't accuse the President of lying about Medicare. We'll just say his claims bear little relation to anything true.

Thankfully, efforts to cram ObamaCare through Congress have been met with strong opposition. If finding a solution to this problem is so critical, why is taking the time to construct a plausible plan so wrong?

As always, thanks for your trust.

Davis Green