

Observations

- ❑ If an investor pulled a Rip Van Winkle on September 1, 2008 and awoke September 1, 2009, where would you begin to bring them up to date? The Dow Jones Industrial average starting at 11,543 then falling to 6,440 and now at 9,500 would highlight the rollercoaster ride of the economy. Our investor might just lapse back to sleep.
- ❑ The Federal Reserve's case as to why it should not be subject to an audit is not passing the smell taste. Why should any government agency not be subject to an audit and accountable to taxpayers? Just three years ago, the Fed was supplying reserve funds of \$880 billion. Today, that figure has grown to \$2.1 trillion. International securities held during the same time period have swelled from \$1.6 to \$2.8 trillion. No reason not to audit them

Facts & Figures of Importance

Economic

US Gross Domestic Product has been negative five out of the past six quarters. The US still remains the world's most predominant economy. The table below shows the world's top ten country GDPs at purchasing power parity exchange rates. The last column shows the growth rate for each economy. These figures are 2008 estimates from the CIA World Factbook (in billions).

1. European Union	\$14,820	1.0%
2. United States	\$14,290	1.3%
3. China	\$7,800	9.8%
4. Japan	\$4,348	-0.4%
5. India	\$3,267	6.6%
6. Germany	\$2,863	1.3%
7. United Kingdom	\$2,225	0.7%
8. Russia	\$2,097	6.0%
9. France	\$2,097	0.7%
10. Brazil	\$1,990	5.2%

Despite the decline in US economic activity, it would take a combination of the GDP's of China, Japan, and UK to equal that of the US. The federal budget for the current fiscal year is projected to be \$1.75 trillion by the White House. If the president's 2010 spending figures are correct, the US is essentially overspending by almost the entire GDP of Brazil. Imagine if the budget deficits of state and local governments were included and the picture gets uglier.

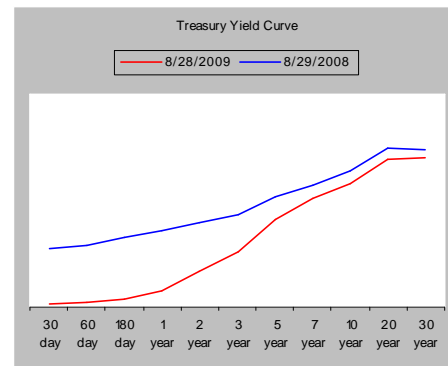
Economic Outlook

- Short-term, better news should be ahead as more federal stimulus money will be spent. Medium and longer term, big problems are staring us in the face. There is no quick fix as the rebuild must use bricks and mortar, not sand.
- Lack of political leadership, financial headlines, tighter credit standards, more foreclosures, new credit card rules, and job security worries are realities that are recognized by the consumer and should stave off a repeat of the excess spending of the past decade. In the long-run, stronger household finances are good for America.

Financial

	Treasury Yields		Equity Markets	
	5 Year	10 Year	S&P 500	DJWilshire 5000
2005	4.35%	4.39%	1,248	12,518
2006	4.70%	4.71%	1,336	14,257
2007	3.45%	4.04%	1,468	14,819
2008	1.94%	2.96%	896	8,945
8/31/09	2.39%	3.40%	1,021	10,512
YTD Return			14.97%	15.68%

The graph below shows the impact of the massive amount of liquidity injected into the financial system and how short-term rates have been pushed to almost zero. This is a true investor's conundrum. Safety/Risk vs. Return



Investment Outlook

- Pay attention to not only third quarter earnings, but revenue also. Costs can only be cut so much. Companies must make tough decisions on pricing, margins, and market share. There is no bottom line without top line sales first.
- Valuations are extremely important. We too often see the pendulum swing too far in both directions. The stock market anticipates future earnings therefore it is forward looking. It is not unusual to see market strength in periods of economic weakness or market declines in times of economic prosperity.

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Insightful Thoughts of Others

U.S. markets have rebounded roughly 51 percent in five months from March lows but the median bear market rebound is 70 percent over 17 months.

-- Frank Holmes, U.S. Global Investors

The sole reason why TAVF Management does not pay any attention to general market factors, is that we are no good at making such prognostications. We don't think anybody else – perhaps with the exception of a few geniuses who are unknown to us – is any good at it either. It seems as if the actions of the general market are truly a random walk.

-- Marty Whitman, Third Avenue Management

When they call the roll in the Senate, the Senators do not know whether to answer "Present" or "Not guilty."

-- President Theodore Roosevelt



A Few More Things

- ❑ Summer is over and Congress will soon be reconvening. The rhetoric over the healthcare bill will become even uglier. Just how many members of Congress spent their vacation reading all 1,018 pages of H.R. 3200, better known as the bill to "To provide affordable, quality health care for all Americans and reduce the growth in health care spending, and for other purposes"? It's available for free on-line if you have not had your opportunity to read it yet. Oh, and just what are "other purposes"? It would be a surprise if anyone thought this would be an improvement over the current system.
- ❑ It is unfortunate that politicians are attempting to exert an even heavier hand, both directly and indirectly, in controlling and dipping their hands into the pockets of the American public. The challenge is to determine whether this is just usual political rhetoric gone a bit to the extremes or if this is real. While the stock market has for the time being stopped back from the abyss and is gaining ground, short-term fixes for the economy are going to cause greater future pain. Hope a better informed American public will push back against government.
- ❑ Much thought has been put into a longer-term scenario where we have low to moderate inflation with economic growth. The Federal Reserve has pumped a tremendous amount of money into the banking system to firm-up capital levels; however banks are not lending those funds. If banks can somehow earn profits and repay the Federal Reserve without making loans, that will allow the Fed to contract its balance sheet. Next, the Treasury has to repay all the holders of US debt. Increasing tax rates usually leads to reduced revenues. The economy could improve and more tax dollars could be collected. How does that happen near term with unemployment approaching 10%, more government spending, and rising tax rates? Spending reductions? How does that happen given the mounting unfunded liabilities and politicians love to spend other people's money? Will the rest of the world keep buying our debt at low interest rates? Remember interest on the debt must be paid. Will foreign debt holders forgive a portion of our debt (not likely)? The remaining answer is for the Treasury to keep printing more money, which in turn will likely devalue the US dollar and lead to inflation. It is a difficult puzzle.
- ❑ Enjoy your Labor Day weekend. Beware of those in politics, executives, and the media returning from vacations all energized with "new ideas". New ideas and grandiose plans are to be funded from your wallet.

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