

Observations

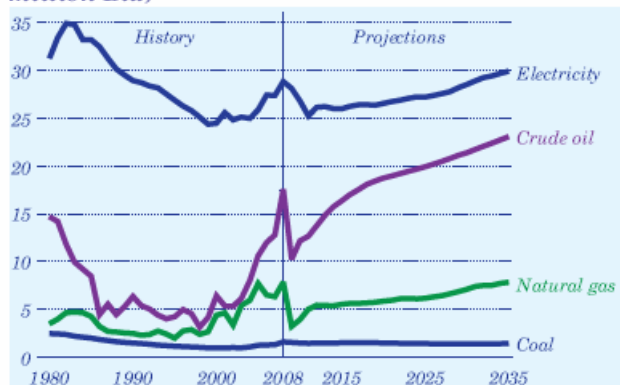
- Get ready for the winter of **healthcare legislation debate discontent**. Whether it is the Senate or the House version, this is a complete disaster for the American public. If one reads the Congressional Budget Office or General Accounting Office work on the proposed healthcare reforms and it is clear that neither better care nor reduced expenses will be the result of the proposed legislation.
- Keep an eye out for the **impact of payroll withholding tax increases which combined with lower income tax rebates** later this year. This could further dampen consumer spending as lower paychecks and expected rebates being less than what they were in the past has folks thinking twice before opening their wallet. Remember, consumer spending comprises almost 70% of the US economy. Add increased healthcare expenses, especially insurance premiums and uncertain future tax increases and the path back to recovery becomes a bit rockier.

Facts & Figures of Importance

Economic

From the Energy Information Administration/Annual Energy Outlook 2010

Figure 1. Energy prices, 1980-2035 (2008 dollars per million Btu)



Not surprising that prices are forecast to rise (coal anyone?). What is interesting are the assumptions used in the forecast. Real GDP grows at 2.5% between 2010 and 2035. During that same period, US population, labor force, and productivity grow at annual rates of 0.9%, 0.6%, and 2% respectively. Not exactly a "robust" recovery.

Economic Outlook

- The economy is slowly healing in spite of government action. It is an election year and the party in power is under pressure to improve the economy. Watch for more stimulus if unemployment does not fall back to the 8-9% levels.
- Repayment of TARP funds to reduce the national debt would do wonders for the economy and investment markets worldwide. If the money is "reinvested" in other programs, (i.e. let's spend taxpayer money) expect negative consequences for the dollar and economy.

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
12/31/09	2.69%	3.85%	1,115	11,549
YTD Return			26.46%	27.09%

Why the Above Four Measures?

Many other important indices should be reviewed in addition to those shown above. The two Treasury yields offer a simple way to compare trends and a relationship between a mid-term and longer term rate. Rates have shown an increasing trend in 2009. Notice also the difference between the two rates has increased.

The S&P 500 is a market weighted measurement that reflects approximately 80% of the value of US equities. The DJ Wilshire 5000 includes more firms, especially small and mid-size cap companies which is a better measure of the entire US stock market. Some investors miss the additional long-term benefits that may be realized by including small and mid-size equities in their portfolios.

Investment Outlook

- The low hanging fruit in the equity market has been picked. While earnings are a fundamental driver of stock valuations, there needs to be signs of top line and volume growth to help propel earnings.
- If interest rates rise with a healing economy, that is good. If interest rates rise amid fears of inflation, be concerned.
- At some point the stock market will be thumped when investors realize tax rates, including capital gains rates, will increase in 2011. Think long-term, not short.

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Insightful Thoughts of Others

From now on, ending a sentence with a preposition is something up with which I shall not put.

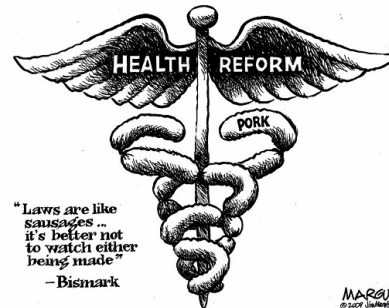
– Winston Churchill

In my sentences I go where no man has gone before...I am a boon to the English language.

– George W. Bush

Give me ambiguity, or give me something else.

– bumper sticker



A Few More Things

- Please do not put much faith in all the predictions you are seeing for 2010, especially when it comes to investing decisions. If there is a need for funds this year, leave that amount in cash as markets are too unpredictable. If you have a time horizon longer than one-year, carefully evaluate your goals and portfolio allocation.
- We make every effort to find reliable sources of information for advising clients. It can be difficult at times to find organizations that are both non-partisan and attempting to do good work. Common Good (www.commongood.org) is on a mission to restore common sense to America. The books of founder Philip K. Howard are easy reads that layout both problems and common sense solutions in a straight-forward manner.
- The Peter G. Peterson Foundation (www.pgpf.org) is another non-partisan organization that is calling attention to America's financial problems. The president of PGPF, David Walker was the seventh Comptroller General of the United States and head of the U.S. Government Accountability Office (GAO) for almost ten years. It is nearly impossible to find anyone with more knowledge of the financial situation of America than David Walker.
- It is very early in the election cycle, however there are very few incumbent politicians at the Federal, state, and local levels that truly understand the frustration of the American public. The push back in the election booth that started with the presidential election of 2008 will spread to Congress and more local levels. The difference is the vast majority of Americans understand that we cannot spend our way out of problems and are rejecting the free spending ways of Washington DC as evidenced by the gubernatorial elections in Virginia and New Jersey. Unless fiscal responsibility is enacted, the politician who is not doing the right thing can expect to be looking for a new line of work a year from now.
- The Government Accounting Office (GAO) reports that in a review of the retirement plans of all 50 states and 39 large local governments, approximately \$530 billion of benefits are not funded. Go beyond the 39 local governments and imagine how high this figure will go. Since only the Federal government can print money and raising taxes will not do much to help, expect state and local governments to slash spending by significant amounts over the coming years.
- It's 2010 and while technology has advanced us far, the saying that no matter how much something is built to be idiot proof, someone will make a better idiot has never been more true. Have a Happy New Year.