

Observations

- How did citizens of the “developed” world and their leaders get so far off-course? The US is supposed to set the standard for liberty and what mankind should strive for as a nation. At the national, state, and local levels, we as citizens have failed to hold our executive, legislative, and judicial branches accountable for their actions. Until hard sacrifices are made by everyone, the problems will worsen and **Americans will see their standard of living erode.**
- **Thank your for flying with USA Inc.** Instead of piloting the plane, Democrats and Republicans are in the cockpit fighting about how and where to land the plane. We'll leave alone any jokes about sleeping air traffic controllers. In the cabin, the citizens are being distracted by entitlements and entertained by a mostly complicit media as the plane is running out of fuel (money, which makes the world go round). The math is simple and this will not end pretty.

Facts & Figures of Importance

Economic

Let'em Eat Hamburger

There are three kinds of lies: lies, damned lies, and statistics. The government tells us that inflation is low and any inflation is likely to be “transitory”. Any of us who eaten food or consumed energy this year and have seen the rise in prices think government math is fuzzy. So Chairman Bernanke, does this mean prices have gone up and will stay higher or will prices retreat? And just how does the government calculate inflation? The primary source for measuring inflation comes from the Bureau of Labor Statistics which publishes Consumer Price Indexes (CPI). There are various reports that are adjusted for things such as seasonality (think more retail spending at year-end) or changes in consumer preferences.

Astute critics of the CPI point out flaws in the calculations that can mislead readers. Do not doubt that political considerations are used in calculating and reporting inflation results. For example, core inflation excludes energy and food prices, which the BLS believes are too volatile on a month-to-month or annual basis. Try selling that to those of us who power our homes and cars or eat. The indexes also can make adjustments like substituting hamburger for steak if steak becomes too expensive for consumers. Adjustments for quality, especially in technology are not easily quantifiable. How does one value items that are purchased every few years such as a computer, cell phone, refrigerator, or TV with today's additional features versus one from ten years ago? It's deeper than the headline.

Economic Outlook

- It's not a question of if, but when at least one country exits the EU as their debt problems linger. Count on political solutions creating greater problems for Europe.
- The frog in the pot metaphor is happening before our eyes as Congress and the Administration are playing an ultimate game of moral hazard with the budget and debt ceiling. Unfortunately, many Americans do not understand the issues and what is at stake, or simply do not care.

Financial

	Treasury Yields		Equity Markets	
	5 Year	10 Year	S&P 500	DJWilshire 5000
2006	4.70%	4.71%	1,336	14,257
2007	3.45%	4.04%	1,468	14,819
2008	1.94%	2.96%	896	9,087
2009	2.69%	3.85%	1,115	11,562
2010	2.06%	3.38%	1,258	13,360
5/31/11	1.68%	3.05%	1,345	14,287
YTD Return			7.82%	6.94%

You Looking for Some TIPS?

Treasury Inflation Protected Securities (TIPS) are bonds issued by the US Treasury that are designed to protect investors against inflation. The principal of a TIPS increases with inflation and decreases with deflation, as measured by the Bureau of Labor Statistics Consumer Price Index (CPI). When a TIPS matures, the investor is paid the inflation-adjusted principal or original principal, whichever is greater. Popular media fawns all over TIPS and gold when advising readers how to guard against inflation.

An eye should be kept on the CPI and its calculation. Investors should also understand how TIPS are taxed and the investment risks associated with zero change or a reduction in the CPI. Be careful with all investments in your portfolio, but heads-up to what the media or some advisors do not reveal. Don't suppose the US Government would tinker with the CPI to understate inflation so as to avoid further running up the deficit? Since Social Security payments are also tied to the CPI...never-mind.

Investment Outlook

- Risk abounds in the three major asset categories, cash, fixed income, and equities. More than ever, diversification is important for all portfolios. There are no easy softballs to hit in the current market.
- With the Fed's Quantitative Easing II ending this month, an economic slowdown becomes a more likely possibility. While they have had a nice run be careful with high yield bonds as the return for additional risk becomes thinner.

Insightful Thoughts of Others

As late as 1980, the US had 14,000 commercial banks and the five largest controlled, in assets, the equivalent of 14% of GDP. Today...we have fewer than 7,000 banks...[with] the five largest institutions controlling the equivalent of almost 60% of GDP.

- Tom Hoening, Kansas City Federal Reserve Bank President

Criminal justice, as it pertains to the Goldmans [Sachs] and Morgan Stanleys of the world, is not adversarial combat, with cops and crooks duking it out in interrogation rooms and courthouses. Instead, it's a cocktail party between friends and colleagues who from month to month and year to year are constantly switching sides and trading hats.

- Matt Taibbi



A Few More Things

- ❑ **What should be happening and what is happening are diametrically opposite.** Governments are artificially keeping interest rates low and attempting to monetize their debt. Talk of nations preferring a strong currency is hot air as their actions show preference for a weaker currency in order to grow exports. Inflation has yet to show in full force as economic fear has kept wages from rising and pricing power is limited. However the spring tightens and inflation will appear in more than energy and food prices. CD rates lower than the inflation rate is a temporary anomaly.
- ❑ **Do not count on the residential real estate market to bounce back anytime soon.** Consider the following: 1) tighter lending standards, 2) an aging population, 3) foreclosed homes that have yet to be put on the market, 4) high delinquency rates that will become homes that will be foreclosed upon, 5) an excess supply of inventory, 6) number of "underwater" mortgages; and 7) public distrust of the market. Even if mortgage rates drop from their current record lows, only lower prices will spur the residential real estate market ahead. Municipalities that count on property tax revenue better get to work PDQ on their budgets or face resident and bond holder backlash.
- ❑ **Wall Street and Madison Avenue find out where the money is and then create products** (usually without real regard as to the benefit to customers). As a financial and investment advisory firm, QRS receives sales pitches each day as to why we should invest client money in the salespersons product. Many a pitch is smooth with charts, bells, and whistles. We poke hard at these pitches to try to understand the benefit and risks to clients. They vast majority of pitches end up in the circular file. Be careful when someone is pitching you. The pigs these days not only have lipstick and earrings, but are now wearing a dress, hat, and heels as they are more desperate to make a sale.
- ❑ **Notice the language and how words can be re-defined.** Target Corp. often tells its suppliers to come up with unique things to surprise guests "so you walk out and you are going to have \$100 of stuff in your cart you didn't plan on buying," says Lindsay Backer, an associated marketing manager at General Mills. Guests? Do you have "guests" come to your home who you are trying to surprise into spending money? When they're spending their money, they are customers, not guests.

Another fuzzy term. The US attack in Libya was described as a "kinetic military action". What is that? Sounds like a drive by bombing to us. Should the 9/11 attacks be re-defined as a "kinetic terrorist action"? Just wondering was it a "kinetic financial transactions" when the Federal Reserve made \$35 billion in loans to the Arab Banking Corporation of Bahrain? The Central Bank of Libya owns 59% of the Bahrain bank which also has a special exemption from having its assets frozen in the US. So the **US funnels money to Libya** at low interest rates and then bombs them. It appears the Federal Reserve's guest/customer (Libya) received kinetic military action for not *stuffing* the cart with *stuff* they did not plan on buying. If you believe our government is competent, there is a bridge in Brooklyn for sale with your name on it.

- ❑ **Happy Father's Day to all the Dads and Congratulations to all the new College and High School Grads.**

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