HAWK 100

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Market Wrap

In case you haven't already heard or read about the precipitous decline in financial markets during February, trust us. The month was ugly in virtually every corner of the world.

Small U.S. equities dropped over 12% as measured by the S&P Small Cap 600 Index. Large U.S. equities nearly matched the decline by losing 11%. U.S. investors are wary of the continued financial crisis and are worried to learn what the Fed and Obama Administration plan for continued intervention into the finance sector.

Even stocks overseas lost 10.4% according to the MSCI EAFE index of developed markets in Europe, Australasia and the Far East. The ripples of the financial crisis are crashing into far off shores. The year-ago theory of decoupling foreign markets from the U.S. appears to still be missing the mark.

A relative bright spot is that the S&P sector index for technology stocks only lost 3.8%. Implied distance from the financial crisis helps perpetuate the isolation from much of the lost market cap this year to date.

Like last September, correlation increased when markets dropped most significantly. Corporate bonds lost 5.2%, and the long treasury lost 1.5%. The 10-year treasury note ended February yielding 3.04%.s

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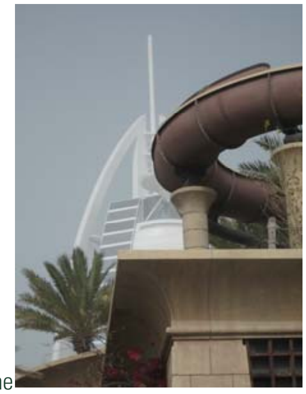
Why, oh why, Dubai?



As Hawk members know, I have the pleasure to lead the investment profession as CFA Institute Presidents Council Representative for the U.S. Midwest Region. In February, that role took me to Dubai, United Arab Emirates for a strategic planning retreat with the CFA Institute Board of Governors to consider globalisation.

Dubai has become emblematic of the global real estate bubble. Since the 1959 discovery of oil under the sands of the Arab desert, Dubai has exploded onto the scene in parabolic fashion. With extremely opulent buildings, such as the Burj Al Arab hotel pictured at right behind the Wild Wadi Waterpark, Dubai hoped to become the distinguished center of commerce and leisure between Europe and Asia.

Now, Dubai is in an economic freefall as construction has virtually stopped on innumerable projects, and its famous cranes stand idle. Dubai authorities estimate that 1500 expatriates flee the emirate every day. Some 300,000 left since population peaked in 2008 and another 300,000 are expected to depart before the 2009 summer heat.

So, why did Dubai grow so rapidly? Why is it now collapsing, and what lessons should we take from the experience?

Aside from effective marketing and natural resources, Dubai's success can be attributed to several factors. The spirited Sheikh Mohammad bin Rashid al Maktoum, the Emirate city-state's leader, has aggressively expanded Dubai to compete with the much larger Emirate, Abu Dhabi. Dubai has introduced a free-zone concept to attract specialty industries (e.g., healthcare, biotech, media, and finance). In 18 zones, expats are free to own property, corporate and personal income is free from tax, and each zone is free to write laws that suit their specific purpose. A one-time English colony, Dubai's legal system has English common law influence which lowered the commercial barrier to entry. Dubai's geographic location places it at the proximate midpoint between Europe's and Asia's financial centers. Dubai is ideally situated to settle transcontinental trade and finance. Additionally, its predictably warm climate, relatively liberal culture, and sandy beaches attract those travelling for leisure and style.

Nonetheless, Dubai has felt the full force of the global collapse for at least as many reasons. Emirates were literally nomadic desert Bedouins little more than a generation ago. They have little experience and insufficient economic systems to handle a crisis of today's magnitude. Their building exuberance extended leverage beyond any sustainable measure. Now, the glass towers sit half empty.

The much larger Emirate neighbor, Abu Dhabi, appears intent on repeating Dubai's mistakes. Preparing to embark on outlandish projects that make Dubai look like a neighborhood park next to Disney World. For example, Sheikh Zayed bin Sultan al Nahyan Mosque pictured at left, is the world's largest mosque by many measures. Visit the museum contained in the multi billion dollar, golden gilded Emirates Palace to view plans for Abu Dhabi to construct its own Louvre, Guggenheim, New York University, and Sorbonne University, among other grandiose visions. Costing trillions of petro-dollars, only time will tell whether these glass towers will ever fill.

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