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Dubai World Defaults.

In February, I wrote of my trip to Dubai to meet with the CFA Institute Board of Governors. The Emirate city-state set on the southern coast of the Persian Gulf is known for its opulence and grandiosity. Idle construction projects served as visual evidence that Dubai had already plunged the depths of the financial crunch. Yet since February, it appeared to be on the mend as the world economy stabilized.

Evidently, the green shoots, to which economists ascribe sanguine forecasts, wither in the desert sands. Dubai World, the finance and investment arm of the Dubai government effectively defaulted on its debt commitments this month.

We will watch Dubai like a Hawk to gauge the risks of its default on financial markets — particularly emerging market stocks and bonds. No investor wants to underestimate systemic risk from an otherwise isolated event. Investors mistakenly understated risk in 2007 when New Century Finance failed and signaled the pending doom of the financial crisis.

Dubai holds lessons for governments too. Dubai was recently a shining symbol of economic dreams. Though it borrowed from afar to build those dreams on sand. When financiers lessened their appetite for Dubai lending, the dreams crumbled. Will this lesson become systemic?

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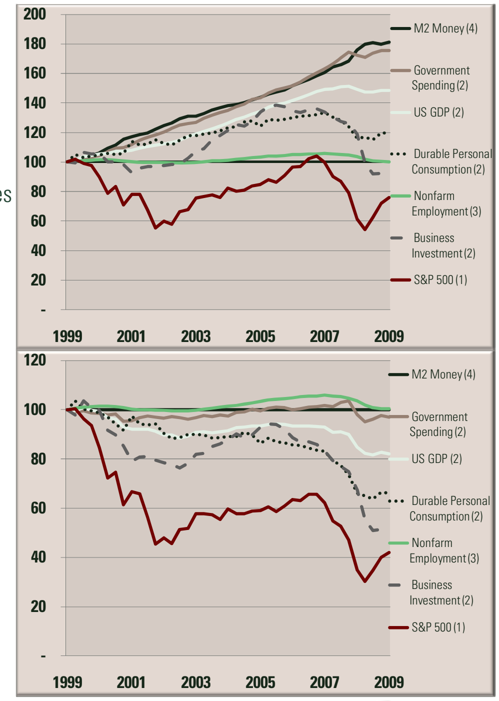
Lost Decadence.

Much ink has been spilled to describe the last ten years as a lost decade. By some measures, the U.S. indeed frittered its wealth during the decade. In our opinion, the policies held by the Federal Reserve during the 2000s eventually led businesses and consumers to cinch their belts and forego decadence.

Hawk100 routinely monitors financial and economic data to create and evaluate its investment strategies. We view this information from multiple vantages in order to gain a deeper understanding of their aggregate effect on the alignment of your wealth with your life. We bring your attention to the charts at right presenting information from two perspectives.

The top chart show trends in certain economic measures over the decade where each indicator was assigned a 1999 base value of 100. During the 10-years hence, money supply and government expenditures nearly doubled; nominal GDP rose 48% and durable consumption rose 20%. While employment was flat, business investment and the S&P 500 price index declined. In all, the numbers hardly describe a lost decade.



Hawk100 computations based on data provided from: (1) Comstock, (2) Bureau of Economic Analysis, (3) Department of Labor, and (4) Federal Reserve Board

Hawk100 has expressed concern, however, that U.S. monetary policy is silently eroding domestic and global wealth. If we reevaluate the same information from the top chart and graph each series relative to money supply, we observe shrinkage in virtually every area of the economy. By loosely defining each item in real terms, relative to the monetary base of money supply, we draw a stark picture of the 2000s.

The bottom chart redraws each series (except employment, a nonmonetary measure) after adjusting the series by dividing it by the corresponding level of the money supply. Here, we depict erosion of 58% from the S&P 500...far worse than the index price level suggests. Business investment, the base for future economic growth, shrank 49% and durable consumption declined 34%. Only government spending came close to matching the money supply expansion.

Emirate Dreams Crumbling

Among the implications, this means the Federal Reserve is indeed monetizing the Federal budget, despite protests to the contrary- from both the Bush and Obama administrations. Given the rapid pace of government expansion, that likely leads to a devalued green-back which would increase the risk of inflation.

More importantly, by largely foregoing investment in the economic engines that drive future success, American businesses will likely suffer diminished industrial might, and American consumers place their famed resiliency in doubt.

By Richard Clemens, CFA, President