April 5, 2010

Client
Address
City

Dear Client;

Continued economic and market supports by all parts of the U.S. Government kept asset prices on the rise during the recently completed first quarter. Current public policy is to have the government prop up the economy and markets until the excesses that developed over the last decade in the private sector abate. While there is some evidence these efforts are bearing fruit and some supports are being reduced, government intervention, however well intentioned, is slowing the abatement process and creating an increasingly weak foundation for asset prices.

In effect, the excesses are being shifted from the private sector to the government. If temporary, this is a reasonable approach; however, it is possible these efforts will become unsustainable. A strong economy and growing asset prices are built on increased worker productivity, increased wages and expanding end-user markets. While private company worker productivity has increased, wages have been stagnant for the last decade and markets have only expanded as a result of decreased saving rates. And as more jobs are shifted to the government, worker productivity will suffer. This creates a tenuous situation.

That preamble explains why I continue to be cautious in my investment approach. During the quarter I found opportunities to put funds to work in high-quality, large-capitalization, dividend-paying companies, starting new positions in Qualcomm and Western Union, while adding to holdings of J.P. Morgan, Exxon Mobil and Time Warner. I also made substantial purchases of three-year U.S. Treasury bonds yielding 1.5 percent to absorb funds until better alternatives develop. I expressly did not add to corporate and municipal bond holdings and I believe that a large number of investors, in an attempt to escape 0 percent money market funds and avoid the stock market, are making a big mistake by deploying additional funds to these asset classes. I took advantage of market strength to sell some small holdings and liquidate mutual funds that have proved to be disappointing performers.

I am always on the lookout for situations not seen before in the economy or markets as a sign that possible imbalances exist that could cause problems or create opportunities later. Two such instances were observed during the first quarter, and they are probably related. The Social Security Administration paid out more in benefits than it took in as receipts, an occurrence that was not projected to develop before 2017. The earlier onset was no doubt a result of lower payroll tax receipts due to high unemployment rates, while the effect is still more borrowing by the U.S. Government. It appears market participants took notice, as there are now AAA-rated corporate bonds that are trading with a lower yield than U.S. Government Treasury bonds. This implies that investors are more comfortable with the safety of the highest rated corporate debt than bonds issued by the U.S. Government, even though corporate bonds are less liquid and have a tax disadvantage for some holders.

Enclosed please find your portfolio report that covers periods through the first quarter of 2010. The results during this quarter were positive as a result of the economic and market supports referenced above. Please call if you have questions about your portfolio or if you have some financial issues that need review.

Best regards,

Peter V. Hedberg