

Weekly Commentary

December 7, 2009

The Markets

Could November go down in history as a major turning point in the U.S. economy?

The shocking (in a positive way) unemployment report released last Friday by the Labor Department showed the economy lost only 11,000 jobs in November. The markets were bracing for a number well in excess of 100,000, according to CNBC. On top of that, revisions to the previous two months showed 159,000 *fewer* jobs were lost than initially reported. And, to complete the trifecta, the unemployment rate dropped to 10.0% in November, down from 10.2% in October 2009 according to a Yahoo! Article written on December 4, 2009. On the surface, this is extremely good news for the economy as it suggests the economy is healing nicely.

Initially, the stock market roared higher on the news. However, as the day wore on, prices started to fade as investors realized that if the economy is too strong, it will cause interest rates to rise sooner than expected. As interest rates rise, it may cause the economy to slow down. So, in the (almost) comical way that Wall Street works, investors like good news – but not too good of news!

Gold prices plunged on the unemployment report and interest rates and the U.S. dollar soared. True to form, whenever there is major market moving news, we tend to see some asset classes that benefit and some that lose out. This complex and ever-shifting interrelationship among various asset classes was on full display after the unemployment news broke. Of course, we do our best to stay on top of these relationships.

Data as of 12/4/09	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	1.3%	22.4%	26.2%	-7.8%	-1.5%	-2.5%
DJ Global ex US (Foreign Stocks)	3.2	40.4	55.6	-5.0	4.1	1.2
10-year Treasury Note (Yield Only)	3.5	N/A	2.6	4.4	4.2	6.1
Gold (per ounce)	2.0	36.9	53.9	22.6	21.3	15.7
DJ-UBS Commodity Index	-0.4	15.0	21.9	-7.7	-1.5	3.9
DJ Equity All REIT TR Index	9.0	25.6	56.8	-13.6	0.4	11.1

Notes: S&P 500, DJ Global ex US, Gold, DJ-UBS Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT TR Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.

Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association.

Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not applicable or not available.

THERE IS A DIFFERENCE BETWEEN LUCK AND SKILL and knowing when you are just lucky and when you are successful due to skill is of paramount importance as an investor. Let's say you correctly called the flip of a coin five times in a row. What are the odds that you will correctly call the next flip? Correctly calling five flips in a row might be considered a "hot streak" and lead you to believe that chances are high you can correctly call the next flip. Well, assuming it is a fair flip, there is, of course, only a 50/50 chance that you will be correct because flipping a coin is a game of known probability. The fact is the coin flip has no memory of your hot streak.

An investor who is on a “hot streak” may or may not be lucky. Let’s take John Paulson as an example. He was a faceless hedge fund manager toiling in obscurity until he came upon an idea. He became convinced several years ago that the housing market was a bubble ready to burst. He put his money where his thesis was and he made billions of dollars for himself and his clients, according to a new book, *The Greatest Trade Ever*, by Gregory Zuckerman.

Today, Paulson is the toast of the hedge fund world and his latest “big bet” is that gold prices will continue to rise. This is not a recommendation from us to either buy or sell gold; rather, we want to make a point.

With millions of investors, odds are that some of them will make winning investments numerous times in a row. If these winning investors were, in reality, just lucky, *but they think they were actually skillful*, then that is when the situation turns problematic. The lucky investor may start to think they are infallible and get stubborn when the market turns against them. Eventually, when the lucky streak ends, it will likely mean serious losses for the investor. Only time will tell whether John Paulson got lucky or whether he has substantial investment skill.

The best antidote we know of to the danger of confusing luck and skill is to remain humble. When our investment strategy performs well, we are very thankful. When it doesn’t perform well, we try to learn from it. The investment business has an uncanny way of turning hubris into painful losses. We think humility is a safer route.

Weekly Focus – Think About It

“If we become increasingly humble about how little we know, we may be more eager to search.”
-- John Templeton

Best regards,

Jim

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