



Five Waves to Surf *Predictions & Reflections at Mid- Decade*

Good news! 2005 ended with most accounts up 13% to 15% versus the Dow which lost a little (down 0.6%) and the S&P 500 which gained a little (up 3%). This was another very good year for our Globalist Strategies as our large holdings in commodities, natural resources and emerging markets all excelled.

In the blink of an eye, half a decade has slipped thru the hourglass. If we look back on our performance over this period of time, we're pleased to say we've outperformed the S&P 500 by about 40% over this stretch. But upon reflection, our greatest mistake has been in underestimating the speed of gale force winds of globalization. These winds continue to roar around us and show no signs of letting up at this time. With our current strategies very **heavily tilted** towards natural resources, energy, commodities and emerging markets (over 60% in most accounts) we're positioned for global expansion outside of the United States. Over the second half of the decade, we will maintain this orientation.

The core concept of our investment philosophy has been that with the globalization of the world's economies in the 90's thru NAFTA, GATT and the internet/telecomm revolution, there has been a significant shift in the single most crucial beam of Capitalism: **Supply and Demand**. Unlocking the productive capacity and vast labor markets of

Eastern Europe, Asia and Latin America has **increased the Supply** of "stuff" faster than we've created new Demand. The basics of Econ 101 tells us this will set off a **vicious spiral of price competition and cost cutting** even when the world's economies are expanding. Recognizing the potential disconnect between a booming economy and falling profits forced us to **rethink the logic** of all the "tried and true" rules of investing in a world faced with a global supply glut of just about everything. Most importantly, it also forced us to seek **new opportunities** rather than simply spout off like an academic on a pending economic crisis.

Some of these pro-active opportunities have been obvious, others more counter-intuitive. Excess Supply means **inflation will be lower** than expected and interest rates will fall. So, we called for a bond market rally in 1999 when the rest of the world was still looking for inflation to re-appear. Our Globalist thinking also helped us foresee the sharp rally in commodities prices after they had hibernated in a bear market for over 18 years. Why? Washington's attempts to rebalance supply and demand by hyper stimulating domestic consumption thru tax cuts and low interest rates would create a squeeze on commodity supplies. We said then and we say again now, this is an **economic policy doomed to failure**.

The ultimate impact of Globalization is very hard to envision, but one impact is also very easy to predict. **With a newly leveled global playing field, we are in the midst of a massive transfer of wealth out of the United States.** A massive balance of trade deficit, new jobs and factories being built in China, India and Brazil, all point to this flow of capital. This is not something that might happen tomorrow, it is in full swing today. To deny this is simply wishful thinking. Our job is not only to recognize this, but also to take positive steps to ride this tide. We won't confuse patriotism with our commitment to make profits for our clients!

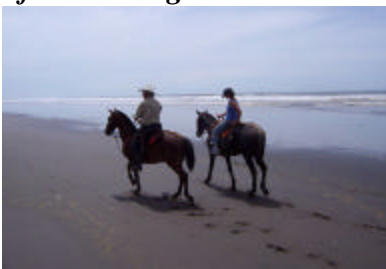
But looking at this a little closer, perhaps we can glimpse where we see profit potential. So along with all the other New Year's pundits, we'll don our finest swami garb, and share with you "**Five**

Random Thought # 103

In a globalized world with mobile factors of production and capital, exactly just what is America's competitive advantage?

Waves to Surf" for the remainder of the decade!

- 1) **Energy Demand** will continue to **increase** and **Energy Supply** from fossil fuels will continue to **decline**. This seems pretty obvious, but to believe it also means energy prices will not only remain high, but will likely climb. \$50 a barrel oil is not an aberration. Oil at \$65 a barrel is only 10 cents a cup or less than what the Beautiful People pay for bottled water. This price could go much higher. Even though the Wall Street Journal and New York Times told us to sell last March when oil topped \$50, **overweighting energy and commodity positions will remain a core part of our strategies.**



- 2) **Manufacturing Supply** will continue to grow and will exceed **Consumer Demand** on a global basis. Again, a very simple but important observation. This means **Price Competition** will continue to get worse, not better, which in turn is **bad news for the U.S. stock market and U.S. workers.** Now that "outsourcing" has run its course, look for the next painful spiral of cost cutting to unfold in the area of **employee benefits** for the remaining workers. This

goose will squeal when plucked! Anticipate growing "**anti-globalism**" sentiments (job protection) in the next presidential election cycle. Also look for a major bankruptcy (GM? Ford?) to spook the psyche of Main Street workers, making them susceptible to the Sirens' call of Protectionism. Since politicians play to the emotions of nervous voters, look for the Democratic party to seize this as a galvanizing force. As investors, since wages are by far the biggest factor of production, we'll continue to **favor emerging market stocks** over the Blue Chips of Wall Street in this environment. Today's voters are very concerned about how their children and grandchildren will compete in a global economy. Heck, so am I, and for that matter, who isn't?

Bring the kids to Costa Rica for

"The Family Gathering and Surf Camp"

Join us for a family oriented weekend at Del Pacifico.

Activities include:

Rainforest Tours & Zipline

Surfing Lessons

Horseback Riding

Beach BBQ

And much more!

June 22nd – June 26th

Please contact Leslie for the "all inclusive" details. She can be reached at (410) 727-6444 or Leslie@noload.com. Help your children experience the flat world!

- 3) Over the next 5 years, look for continued **weakness in the Dollar** to be the catalyst for a **global currency crisis**. Yes, the dollar rallied slightly in '05 but only after falling 50% in the prior 3 years. This can be reversed by a small interest

rate increase in Japan and Europe. The Alfred E. Newman “*What me Worry?*” approach will remain prevalent in Washington until absolutely necessary. Understand a Democratic White House could result in a radically different (protectionist) approach to the problem which might involve currency restrictions. We could see this forming the rationalization for restrictions to shore up a very leaky tax system which can’t function in an age of digital currency. Currency is very boring to talk about, but important never the less. Hard assets are the way to play a currency crisis. **Commodities and precious metals** are all ways to hedge against the economic side. Setting up an international bank account with a **debit card** is a prudent hedge against the political side.

- 4) The Boomer market is 76 million strong and graying! This is 27 % of our population. Already 32 million are over age 50. In another 5 years, we can say with absolute certainty that they will all be 10 years older than they were at the start of the decade, but not necessarily any better off financially. Japan's stock market is still down 40% from its peak 18 years ago. A stagnant stock market could have **severe political implications** in the second half of the decade. What are they going to retire on? Social Security ain't the answer. Nearly 50% of all U.S. workers do not have a job sponsored retirement plan. What about health care? A growing number of people who can retire outside of the U.S. will. Investing in **international resort real estate** is a logical play here.
- 5) If we're talking about riding waves, why not pick the wettest one of all, **Water!** All the geo-political hub-bub aside, water is becoming a scarcer resource and presents investment potential. This is the ultimate **recession proof commodity**, so even if we're faced with a global recession,

people will still be needing clean water. We'll be building our water positions over the next several years.

On the surface, none of these are earth shaking predictions. In fact, most people will agree with almost all of them on some level. However, **accepting the conclusions** they foretell is very difficult. This is even more difficult for an experienced investor who is less prone to impulsive swings because it requires acknowledging the long term inter-relationships between stocks, bonds, currencies and interest rates have been severely twisted. But why else would we have the disconnect between a booming economy and a weak stock market? How else do you **explain the disconnect** between 5 years of economic expansion and low interest rates?



In other words, the bed rock assumptions of “asset allocation” are **no longer stable**. Most professional advisors, even after acknowledging the changed world, have not been able to break free and formulate new strategies. It's easier and less subject to criticism to continue to using a “pre-globalization” asset allocation. Acting proactively to changing conditions is even more difficult. Sure, perhaps they'll add a small 2% commodities or 5% emerging market position **after the sectors have moved 50%**, but anticipating the next dot to connect is beyond their comfort zone. And this is exactly why the average investor is doing so poorly right now. In this changing time, you need not only the ability to recognize the changes and their implications ...but most importantly ...**act upon them proactively**.

Reflections at Mid-Decade

When Smilin' Dan and I re-established ourselves down on Eager Street in January of 2000, one of the things we decided at the time was that it should be just as easy to have "fun" working and investing as it would be grinding away like grim faced gnomes. With a fresh start we also recognized the importance of breaking from the Herd and not only thinking more independently, but also taking concrete actions on our convictions. To achieve this we set a goal of coming up with 5 "new" investment ideas over the next 5 years. These would be ideas where we felt we could truly "add value" to the client relationship and which could not be easily duplicated by just any other advisor. The first of these was a commitment to aggressively pursuing the implications of globalization on the logic of investing. This started with our "**Ten Thoughts for the New Age**" which eventually grew to over 125 published observations. This has been the core of our investment strategy and we've had a heck of a run. We've outperformed the S&P 500 by more than 40% and we've more than doubled our client base.

Our **second idea** was called "**The Last Great Tax Shelter**" where we tested the concept of using the internet to "leverage our intellectual property". To our surprise, this ended up being a "best seller" on *The Motley Fools* website and opened our eyes to the ability of using the internet and email to break the geographic constraints of explaining a sophisticated idea to potential clients. We now have clients spread out around the world.

The **third "new idea"** was a strategy we originally used to help a client hold Alaskan oil wells in an IRA account called **The Omni Asset IRA**. From this we recognized a special niche of using IRA assets to own international real estate. I still remember telling Dan "*I don't know what it is, but we're onto something here!*". What we were tapping into was the **alienation of the average investor** from Wall Street and their desire to own "hard assets", especially outside the U.S. Little did we suspect at the time this would lead to over

50 trips to Costa Rica and Central America in the past 4 years.

This also led to our **fourth "value added idea"** of forming **private equity partnerships** for our clients. Our partnerships now own over 2,000

Random Thought # 104

Rebalancing Supply & Demand

Eventually consumer demand will emerge in China & India, but the real question is whether the stock markets can wait for the growth in international demand as the domestic engine consumer is fizzling out.

acres in Costa Rica. It was through our working on these projects we recognized a shift occurring in the psyche of the Baby Boomers which we called "**The New Three R's – Reflect, Recharge and Rewire**". As retirement approaches, we noticed that more Boomers were seeking a qualitative element in their investments. Sure, the numbers have to work, but not everything in life has to be exclusively about the bottom line.

This led us to our **fifth idea** which was a couple of "**fun**" **investments**, such as our **movie partnership** last year "**The Curse of the Maya**" and this year's movie venture "**Costa Chica**". We're pleased to say both of these are making solid progress with "**Maya**" having just received recognition at "**ShockerFest**" and "**Chica**" is getting set to move into production shortly. Certainly making a zombie movie meet our criteria of not being easily duplicated! While we won't likely see any Spielberg-esque returns, we also had some fun at the same time.

Some of you might recall the old closing line of our radio show **Mutual Perspectives** was "**Innovation Equals Opportunity!**" We set out to discover 5 new ideas and created a whole world of opportunity! Who knows where the next 5 years will take us, but we hope to make

some money for our clients and also have a good time. If you have some friends that would like to join us for the adventure, we'd sure appreciate the introduction!

Now with this 5 years of ancient history taken care of, let's focus on *the last 12 months* more carefully. Here are our most recent thoughts on our *Globalization Strategies*. As always, I've tried to put the most important observations nearer the top and the more esoteric down lower.

- 1) Most of our accounts ended the year *up in the 13% to 16% range* with some aggressive internationally oriented accounts up over 33%. This compares to the old "blue chip" Dow Jones which ended up the year with a little bit of red ink and the S&P 500 which was up only about 3%.
- 2) Our core strategy continues to remain heavily *tilted away from both the U.S. stock market and the U.S. economy* and tilted towards commodities, natural resources and emerging markets. Our U.S. stock market exposure remains below 25% of our total strategies with virtually no "blue chip" exposure.
- 3) We remain *very pessimistic about the U.S. stock market*. GM and Ford have both faced the indignity of being lowered to the lowest rung of the junk bond status and are seriously on the verge of bankruptcy. 75 % of our airline industry is flying under bankruptcy protection. Where are the Blue Chips of yesteryear? AT&T? AIG? Merck? Delta? GM? Ford? And the beat goes on
- 4) ***Frightening Factoid:*** In 2005, 15 of the 20 most widely held stocks in Merrill Lynch's retail accounts lost money. In the old math, that's 75% of the 20 largest holdings at the largest retail brokerage firm lost money last year. Does this speak to the "value" of stock research? Small wonder the little guy is gun shy!

- 5) We just can't bring ourselves to get enthusiastic about investing in a *national consumption orgy* fueled by the empty economic calories of consuming home equity. It's like watching a bon fire at a fraternity party where the revelers keep warm by burning the furniture. Last year over \$1 trillion of new home equity loans were essentially squandered as Americans did their patriotic duty of household deficit spending. How does this make economic sense? Isn't this the opposite of wealth creation?
- 6) At the other end of the spectrum, as we hollow out our national wealth and spend it on non productive consumption, we see the economies of *the emerging markets of Asia and Latin America* flexing their muscles. We have approximately 15% of our portfolios in these markets. This is a very heavy weighting as a typical Wall Street research portfolio might have about 2% in these sectors. We have been rewarded handsomely for taking this risk. Our positions in the broader emerging markets were up about 31% and more focused plays like India (up 50%) and Latin America (up 56%) did even better.



- 7) While great believers in the *emerging markets* long term, we also believe this sector is susceptible to the very fickle finger of Wall Street fad-ism. We took some profits here earlier in the year to rebalance to about a 15% holding as we felt the Wall Street band wagon effect did outpace the economic realities. Again, its supply and demand. Since they are relatively few ways to play the market, even a small shift of stockbrokers onto the band wagon can cause

these stocks to spike ahead of real earnings. Over the past 15 or 20 years we have seen the emerging markets race ahead of reality only to suffer humiliating crashes quite suddenly when fickle brokers change courses. Don't be surprised if we decrease holdings in a strong rally or buy more in a collapse.

- 8) Earlier in the year we initiated our first **gold** positions in over 10 years. They have responded very well with returns of about 24%. We differentiate this holding from our natural resources holdings as a hedge for a potential international currency crisis that we have been watching emerge in slow motion over the past several years. We will likely gradually increase these holdings over time.
- 9) To further tilt our natural resources holdings we are adding a **Water Resources** position which focuses on stocks of companies who provide potable water. Over the next 2 decades we view water as becoming a more important and valuable resource. Over the past 5 years, the index of water stocks has returned about 18% annually versus a 3% loss for the S&P 500.
- 10) The **Erosion of the dollar** is a **silent tax** on your wealth if you allow it to be! However, by diversifying a significant portion of your assets into "Hard Assets" such as real estate, you can protect your purchasing power. Looked at this way, perhaps as much as **50% of the current real estate bubble** isn't "inflated value" prone to a bubble burst at all, but rather simply reflects the falling global purchasing power of the greenback!

Random Thought # 105

Smart Money & Smart People...

Are both highly mobile in a global economy and will always flow to the highest after tax return. If the flow of capital is away from the U.S., so are tomorrow's investment opportunities.

- 11) Think about this for a second. Imagine a dream house in Mayberry USA which has a true value of \$100,000. And since nobody ever comes or goes from Mayberry, supply and demand have remained exactly the same. Now imagine a globalized world economy with a Wal-Mart down the road in Hooterville. Since we no longer have a "closed" economy, if the dollar drops by 25% in global purchasing power, what happens to the market price of the house? It would increase by 33%! But has the "value" increased? No, of course not. Is this a bubble? Or simply a store of value? The good news is that a significant portion of the current real estate "bubble" is simply the impact of a falling currency. ***This won't likely "burst" but it's not "wealth" either.***
- 12) The bad news is that Middle America is spending this phantom home equity money like it's a wind fall, which it is not. This means the country is going further into debt much faster than most people acknowledge.
- 13) This being said, we remain very concerned about the safety of **real estate** at this time. We think the time is coming very shortly to "short" the U.S. real estate market. How can you do this? It's actually now very simple to do. One benefit of the exchange traded index funds or ETF's is that they can be sold short just like any other stock. While historically we have been a "long only" equity player, we will be giving this active consideration over the next years as to whether it would be appropriate for some of our clients. If you would like to discuss this with us, please give me a call directly.
- 14) While overall U.S. real estate appears overvalued, we believe the 76 million strong and graying Baby Boomers make a compelling argument for **retirement resort real estate**. Especially international resort real estate. Here we see sound fundamentals

for increasing demand and limited supply plus the turbo charger of a falling currency.

- 15) With no attempts at humor, a **Hillary** candidacy makes for a Bull market argument for owning resort property outside of the United States. You'll want to invest at least 1 year ahead of this curve, not behind it. Contact us if you want to discuss this further.
- 16) Over the past 3 years we have steadily increased our exposure to **commodities** from about 10% of most accounts to about 35%. This has been a major contributor to our success as our positions here have gained about 65% over the past three years. The logic here is very simple. Like real estate, commodities are hard assets and hedge against a falling currency. As or more importantly, as Western Governments try to stimulate the Demand side of the global economic equation, this creates an intermediate term supply /demand squeeze, driving commodity prices upward. Look for this to continue over the short term.
- 17) Here's the short version of why: when China's demand for iron ore increased by 20% in the last several years, **bottlenecks** appeared in the supply chain which cannot be increased as quickly as the spike in demand. For example, to get ore out of Australia you need to ship it by boats. This means you need larger ports and more freighters. When you take the planning, permitting and financing involved in getting a port expansion approved, you're talking about at least 10 years and perhaps as long as 20 years to get a port expanded. Until then, demand outstrips supply causing prices to spike.



- 18) While the spike in oil prices this year certainly got people talking about the commodity prices, surprisingly the biggest returns in our portfolios came from our **emerging market** positions with typical returns of 30 to 35% for the sector. Again our top performers were not the ones you might have expected. Sure our holdings in **India** were up an eyepopping 50% But even stronger were our returns in **Latin America** with our holdings up 56%.
- 19) **Bonds and the inverted yield curve**...is this a harbinger of a recession? Not really, we suspect that it really means the global bond markets are signaling that worldwide inflation is lower than the bogey man that the Fed is fighting. This is why the Fed controlled "short rates" are slightly higher than the Market controlled "long rates" causing the inversion. The "inflation" we're seeing is not classic manufacturing inflation but rather more of a currency issue being reflected in commodities and in real estate. What will cause a recession here is not if but when the home equity engine sputters.
- 20) Since we're **negative on the U.S. dollar** and short term rates are equal to or higher than long term rates, we remain very negative on the U.S. bond markets. The risk return ratio just isn't here. At the end of 1999, the DJIA was at 10,500 and closed 2005 at 10,700 for a 5 year total gain of 2%. During the same period GDP has grown by 20%. Wouldn't we have expected the stock market to actually have gained even more than the economy? Since it didn't, isn't this concrete evidence of a fundamental disconnect between an expanding U.S. economy as measured by consumption and the lack of new wealth being created by the stock market? What is this telling us?
- 21) Concurrent with this phenomena of a 5 year stagnant stock market, we're also

experiencing a **massive wealth transfer between generations**. We suspect the narcotic effect of this is masking a good deal of the pain many people would ordinarily be experiencing right now. Perhaps this helps to explain another portion of the real estate boom as the Boomers are putting a larger portion of their new found inheritances into real estate and not the stock market.

- 22) Something that we strongly suspect is lurking in the shadows is the possibility of some form of **currency restrictions** in the next 5 years. While the press will spin the reasons here a hundred ways to Sunday, the simple reality here is that our tax system has about 200 million fiber optic holes and is leaking. You may have seen limited examples of this with cyber casinos and international credit and debit cards where e-commerce is already being transacted regularly “offshore” by Middle America. Now add to this global virtual companies conducting business over the internet but outside the U.S. tax system. This might be a computer consulting firm, an

Random Thought # 106

On the same day the Dow broke 11,000 for the first time in 5 years, gold broke \$538 for the first time in 25 years! Which one is right? We'll bet on the gold as the Dow isn't adjusted for a depreciated dollar

internet music download service or even an online book seller or auction site. How about internet phone companies? Are they going to be paying local and federal taxes? Now grow this exponentially over the next 10 years. With virtually every person in the country now able to move funds freely around the world (outside of the U.S. banking system) with the simple click of a mouse from their kitchen table, people will vote with their mouse. The Washington bureaucracy will fight this and will restrict your ability to move funds globally. Naturally the reason cited here will be “in the interest of national security” and

we'll have something along the lines of a Patriot Act II.

- 23) The real underlying problem here is that Washington relies on “reported income” for taxes. The real solution is to move away from an income tax system to a VAT or consumption tax basis, but this will take time. The easier solution will be to restrict **our personal freedoms** in the name of national security. While this might seem extreme thinking, ponder it for just a moment. **Has the internet made our tax collection system obsolete?** If so, what are the logical conclusions? First and foremost, Washington needs to keep the flow of funds going to feed the bureaucracy. How do you do this? Well, first you try to plug the holes as quickly as possible. The best way to do this is to wave the Flag.

The ultimate impact of Globalization over the next 5 years is impossible to predict, but at a basic level it is also very easy to predict. **Based on everything listed above, right now it appears we're in the midst of a massive transfer of wealth out of the United States.** As the international playing field is leveled, our job over the next 5 years will be to keep you in front of this mega trend. As we uncover new ways to do this, we'll share them with you.

Barry Strudwick

December 31, 2005

For more information, please call

410-727-6444 or email us:

invest@noload.com

ABOUT BARRY STRUDWICK...

Barry Strudwick has served an international client base of individuals, investors and entrepreneurs for over 25 years. For private consultations Barry Strudwick & Dan Somerville are available to meet or talk with you. Please contact them by calling (410) 727-6444 or via e-mail at invest@noload.com



“Don Barry” calling in from our Central American office. The world is flat!

Do you think like us?

If so you might want to take advantage of our investment services. New accounts start at \$250,000 and we only will add 12 new accounts this year. Contact Dan at dan@noload.com to arrange an initial conversation.

Contents of this special report may not be reproduced without the expressed written consent of Barry Strudwick.

**Are you ready for your own
Getaway Weekend in Costa Rica?**



Come and join “Don Barry” at our upcoming “Family Gathering” weekend in Costa Rica. The weekend will include:

- ***A tour of Del Pacifico at Esterillos.***
- ***Sun Rise Yoga*** daily on the beach.
- ***Massage and Spa*** treatments.
- ***Aerial photography*** over the Rainforest by piloted ultra-lite.
- ***Horseback riding*** at sunset on the beach.
- Succulent ***Costa Rican “Pig Roast”***
- Poolside ***“World Problem Solving 101”***
- Surfing lessons

Everything is included in our all inclusive Family Gathering week end. Contact Leslie toll free for more details at 866-466-5623 or 866-4-Noload!