THE FOXHALL GLOBAL OUTLOOK

QUESTION:

Dear Paul,

Why is the price of oil continuing to go up?

ANSWER:

There are a number of reasons for high oil prices. The most important is "SUPPLY AND DEMAND" created by the growing consumption of newly developed countries in Asia and Latin America, like China, India, Mexico and Brazil. China is now the second largest car market in the world.

Another reason is that oil is priced in "DOLLARS PER BARREL" and when the dollar drops in value, the price of oil automatically goes up, because it takes more dollars to buy the same barrel of oil.

But, if you consider inflation and other factors, is oil really higher now than in the past? Michael Lewis of DEUTSCHE BANK has come out with an interesting new report on how to value the price of oil.

AS REPORTED BY THE ECONOMIST MAGAZINE

"The price of oil has soared to a new high, hasn't it?

A casual observer might be forgiven for thinking that the oil price reached a new record, of $120 a barrel recently. And so it did, in nominal terms. But by other measures, oil is not quite as expensive as it seems. That, in turn, may go some way towards explaining why demand for oil continues to rise in many countries, despite prices that would have been unimaginable just a few years ago.

> "IF YOU CONSIDER INFLATION AND OTHER FACTORS, IS OIL REALLY HIGHER NOW THAN IN THE PAST? MICHAEL LEWIS OF DEUTSCHE BANK HAS COME OUT WITH AN INTERESTING NEW REPORT ON HOW TO VALUE THE PRICE OF OIL ."

INFLATION

Michael Lewis of DEUTSCHE BANK has come up with several different ways of comparing past and present oil prices. The first step is to account for inflation. But what measure of inflation is most suitable? If historic prices are inflated in line with America's producer-price index, the previous record, struck in the early 1980s, would be the equivalent of $94 in today's money—a level exceeded some months ago. But if the consumer-price index were used instead, oil would need to climb to $118 to hit a record.

But an adjustment for inflation, however it is measured, takes no account of the growth in Western consumers' incomes over the years. Back in 1981, the annual average income within the GROUP OF SEVEN countries would have been enough to buy only 318 barrels of oil. To set back Western consumers by the equivalent today, DEUTSCHE BANK calculates, the price of oil would have to rise to $134 a barrel.

SHARE OF AMERICAN'S DISPOSABLE INCOME

By the same token, the American government reckons that energy ate up its biggest share of Americans' disposable income in 1980: 8% compared with about 6.6% now. To drive spending on energy to the same level again, says DEUTSCHE, the price of crude would have to rise to $145.

Spending on oil as a share of global output, which is about 3.5%, also peaked in 1980, at 5.9%. Other things being equal, oil will not swallow as big a share of the world's GDP unless the price reaches $150 a barrel."

THIS STUDY DOESN'T MAKE THE PRICE OF GAS ANY EASIER TO SWALLOW!

While this is an interesting study, this won't make many people feel better about the current record high gasoline prices.

This is why FOXHALL CAPITAL continues to invest our client's portfolios in global energy funds and in gold and foreign currency funds that make money when the U.S. dollar falls. We hope that these oil, gold and foreign currency funds investments will make up for a little of our client's higher fees at the gas pump.

UNTIL NEXT WEEK...

—Paul Dietrich
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PORTFOLIO COMMENTARY AND ALLOCATIONS

THE FOXHALL WAY: SOUND, REPEATABLE INVESTMENT PROCESS WITH DISCIPLINE

Last week we reviewed our existing portfolio allocations, noting that while we remain in a broadly defensive strategy regarding global stock markets, we are constantly watching for major shifts in the global economy and financial markets that might indicate stronger markets ahead. As much as our clients have appreciated, and benefited, from our conservative approach during the market decline, no one wants to miss 'the next bull market' either!

This week, as we prepare to repeat our portfolio review and reallocation process, I thought it would be informative for our readers to listen in to some dialogue that Paul Dietrich and I recently had with a financial advisor, who entrusts many of his client accounts to FOXHALL CAPITAL, on just this topic.

Advisor: I have a client who would like to put a large sum with FOXHALL. She likes the concept of owning non-US currencies if the dollar continues to weaken. Could you please email me your latest marketing info on the different strategies.

On another note. Your picks are making me really nervous because you are 100% contrarian. You did great yesterday when the market was down and then got beat up today when the market was up. Why don't you at least put 20% in some strong areas of the market, in something that isn't completely contrarian, so that if the market goes on a run our clients don't loose money and get upset with us. The dollar won't stay weak forever, and multinationals are poised to do fine. I would advise a little more diversification in such an uncertain market, but you're the manager, not me.

Paul Dietrich: I am not sure I agree with your assessment. The market will have up days, but I believe the long term trend is down. That would mean that any stock holdings will go down in the long run and your clients will lose money.

I believe the dollar will continue to go down for the foreseeable future. I don't see an upside here over the next few years. We have fewer tax revenues because of the recession; we have wars in Iraq and Afghanistan; we have democrats and republicans busting the budget in DC; and we have the Fed lowering interest rates, which puts pressure on the dollar. I do not know a single economist who thinks the dollar is going to go up over the next few years. Again, it will correct up for a few days or months over the next few years but the long-term trend line is down.

With regard to multinationals, GE is the greatest multi-national and it has been decimated lately.

This is a time for caution and prudence. Dave and I believe that we need to be very defensive at this time. We have not seen any indication that this is the wrong strategy at the moment.

Dave Morton: Let me agree with Paul's assessment and add in one key consideration as well.

Paul's analysis and explanation, reflect what we - and many other top analysts and economists - believe will happen based on all the information available today - this is our current opinion. The very important additional point is that FOXHALL uses objective trend-following and quantitative ranking methodologies and tools. These tools do not have a belief or an opinion, they report changes in supply and demand as they unfold day by day in front of us. Those objective tools will inform, modify, and even override the opinions and beliefs that Paul and I have today. New data, and objective methods, make sure that our beliefs and opinions never stray far from the market reality. You will find that our opinions and beliefs will modify along with the reality of what actually occurs. As Paul's wife says "It is best to ride the horse in the direction it is already going"!

Rest assured, that if some of the possible market changes you list were to occur, our methodologies would quickly pick them up and would guide us to participate in the 'next bull market, wherever in the world it occurs'. That said, Paul has a very deep insight into the world economy that is continuing to give him a strongly bearish outlook, our long term trend-following signals are negative, and very few investments are able to meet our criteria as good risk-reward opportunities. Our portfolios are closely reflecting the defensive themes the market and global economy are depicting. I think a truly contrarian approach would be to continue to invest heavily in equities in spite of these clear bearish themes. Remember, we are trend-followers not trend-predictors!

I hope this gives you a deeper insight into our current defensive posture, and will help you explain to your clients that we won't invest their serious money based on what 'might' happen (even if the market sometimes goes against us for short periods of time), but that we will quickly recognize persistent trend changes and modify our portfolios accordingly.

Thanks for your probing question. Paul and I enjoy working with you and we value the clients you entrust to FOXHALL's care.

Next week we will review just what changes FOXHALL's sound, objective, repeatable, disciplined process has brought to client portfolios!

Dave Morton

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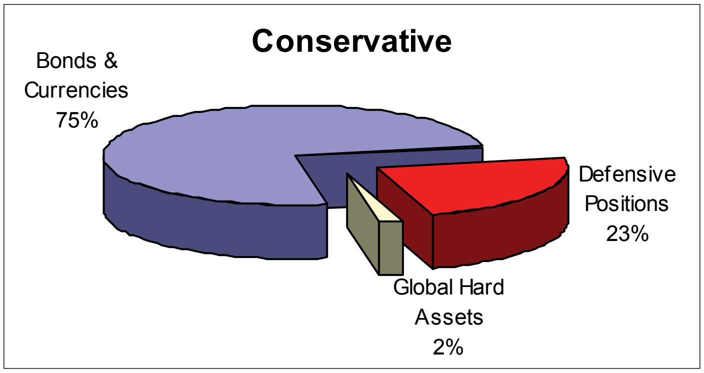
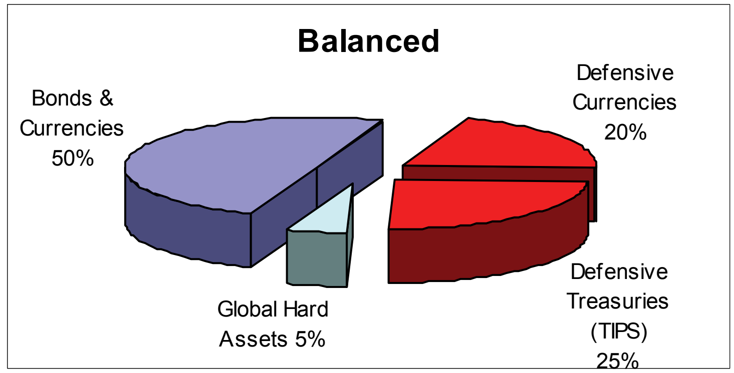
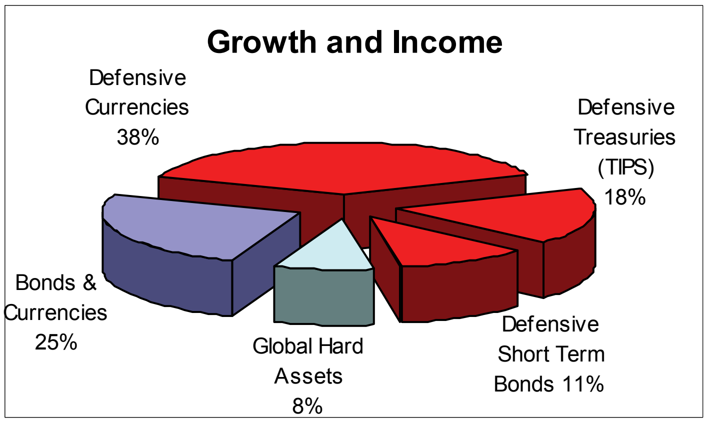
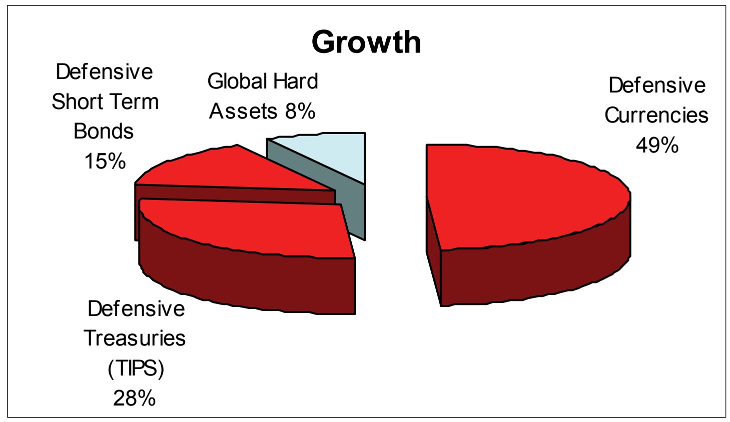
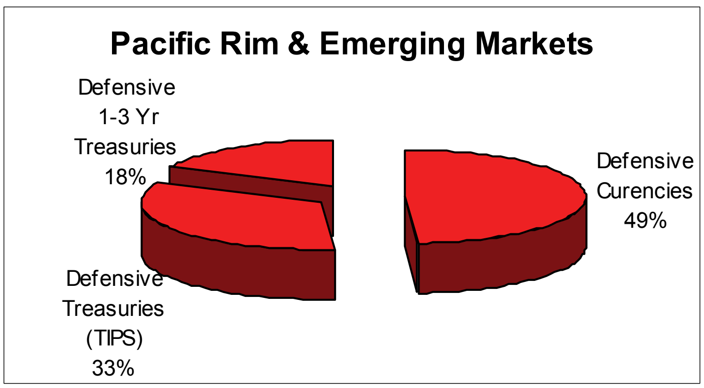
THE FOXHALL GLOBAL OUTLOOK
GLOBAL MARKET ROTATION PORTFOLIOS

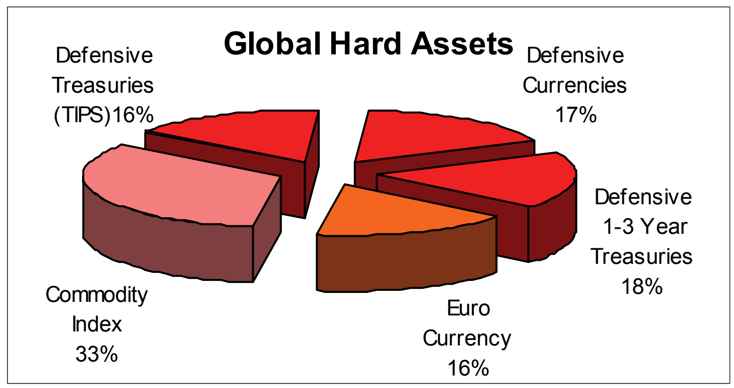




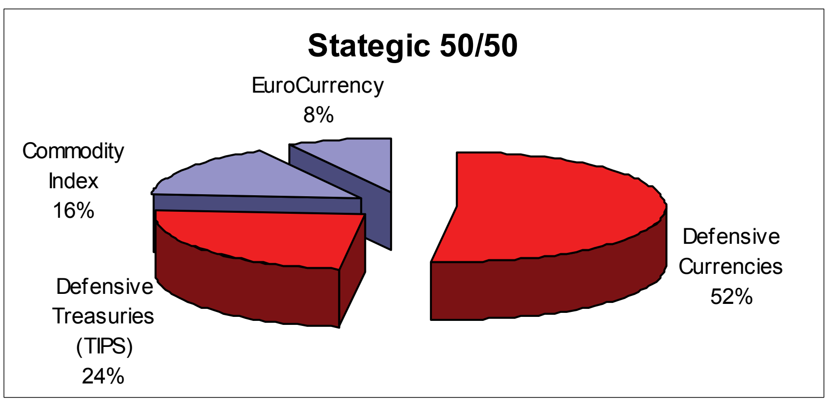








Emerging Markets
Hard Assets
Defensive Position



The allocations illustrated are model allocations, actual client accounts could vary due to many factors. Variable annuity/ variable life accounts will vary significantly due to the availability of investment options in each contract. All allocations may change without notice.