



Is the United States in Decline?

**Let's Diversify our Investments
Outside the U.S.**

October 2012



Executive Summary

Excellence. Experience. Ethics.

- The purpose of this newsletter is to try to remove some of the home country bias that many of us living in the United States may have. Our goal is to help our clients understand why a portion of their portfolios is invested in international financial markets (20% to 50% of the equities may be allocated in Europe, Asia, and Emerging Markets). Not only do Emerging Markets have much lower debt levels and a younger population, international stocks also seem to be currently cheaper than U.S. stocks.
- You have seen in the last newsletter ([Let's Go Global!](#)) why diversifying a portfolio with international securities helps increase returns and decrease risks in the long-term. We would like to share some data which may create some long-term concerns for the U.S. if the situation does not improve in the future.
- The U.S. may be on a declining performance trajectory in the areas of Health, Education, and Safety.
- Let's achieve new greatness for America, but until then,
let's diversify our investments globally!



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Introduction

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The U.S. economy has improved and the U.S. stock market is up more than 110% since March 2009, and has been up 8 of the last 9 calendar years. While the U.S. will still be the largest economy for a few years, some raise the question - is the U.S. in decline? Is it still number 1?

The U.S. is the leader in many areas, but lags behind in several others. In September, I had the opportunity to meet with Professor Friedman (Columbia University), a leading statistician and health economist for the United Nations, and previously, for the World Bank. His research is one of the sources of the data for this newsletter.

Even if the U.S. is one of the wealthiest countries, the data shows it is poor in many areas (Health, Education, and Safety). There seems to be a large disconnect between perception and data reality.

A handwritten signature in black ink, appearing to read 'Blm', with a horizontal line underneath.

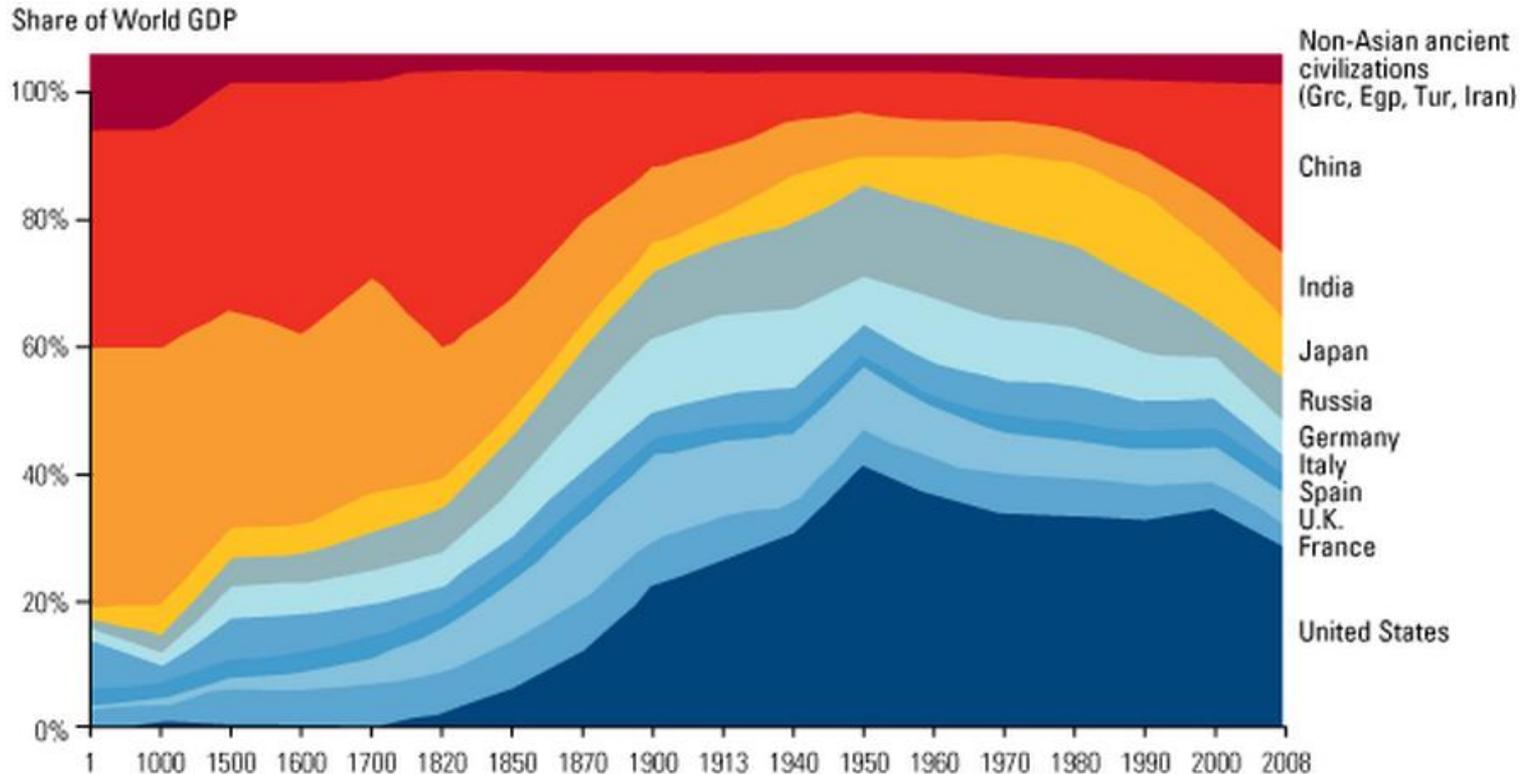
Patrick Bourbon, CFA





Economic History of Major Powers: China is Returning to Historical Norms?

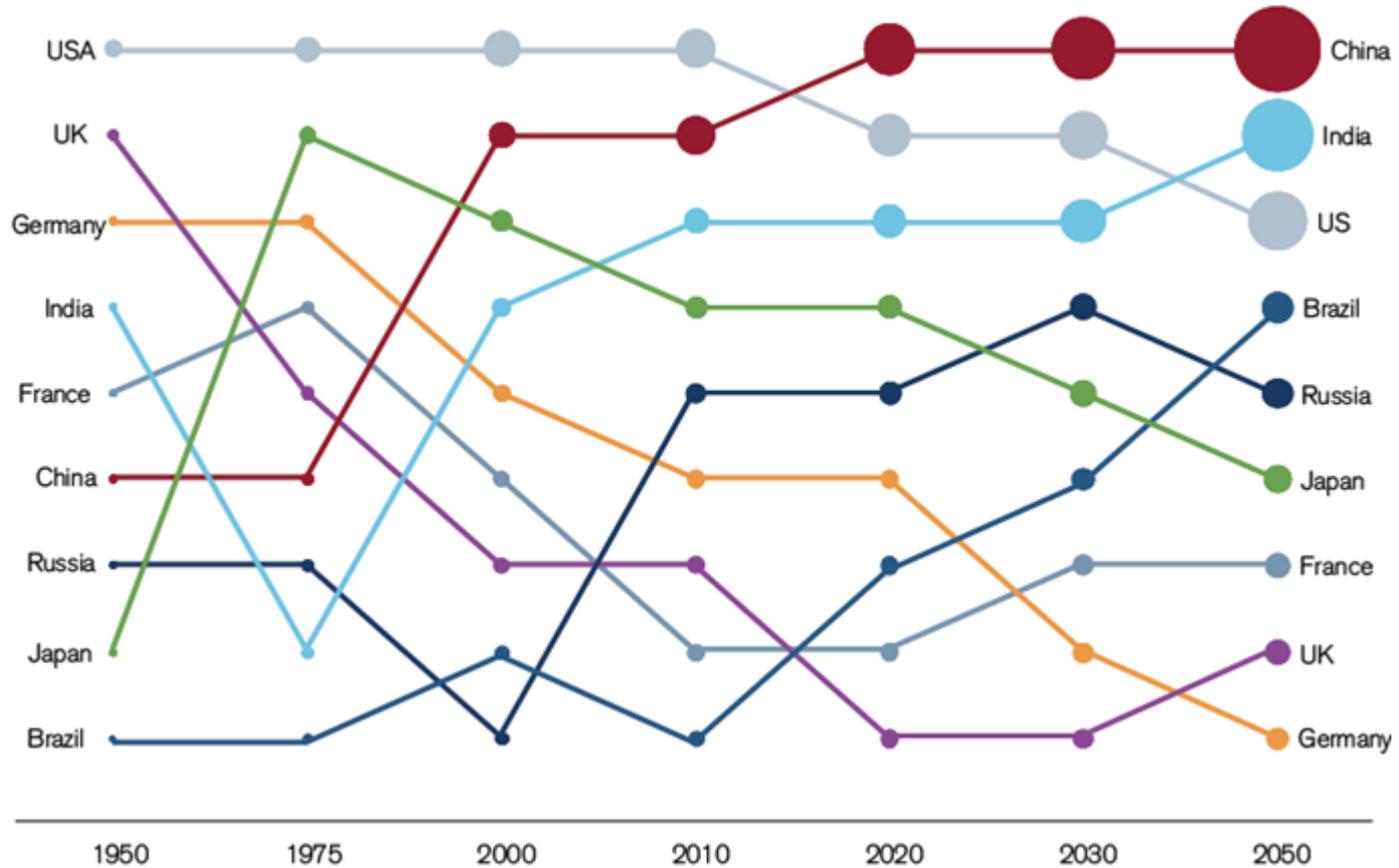
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Source: Statistics on World Population, GDP and Per Capita GDP, 1-2008 AD, Angus Maddison, University of Groningen

GDP, 1950-2050

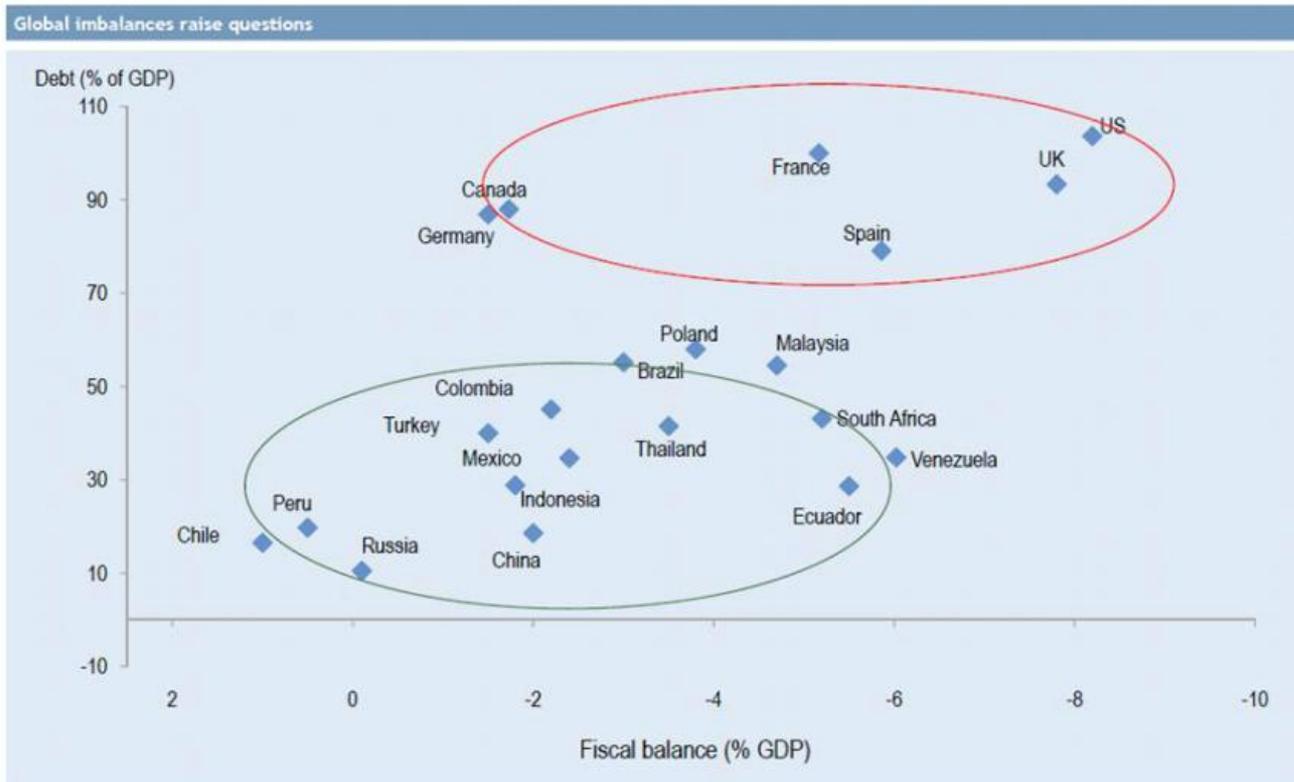
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Source: Data from World Bank and The World in 2050, PricewaterhouseCoopers 2008; updates from John Hawksworth and Gordon Cookson; authors' analysis

U.S. Has Too Much Public Debt and a Very Negative Fiscal Balance

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Source: J.P. Morgan

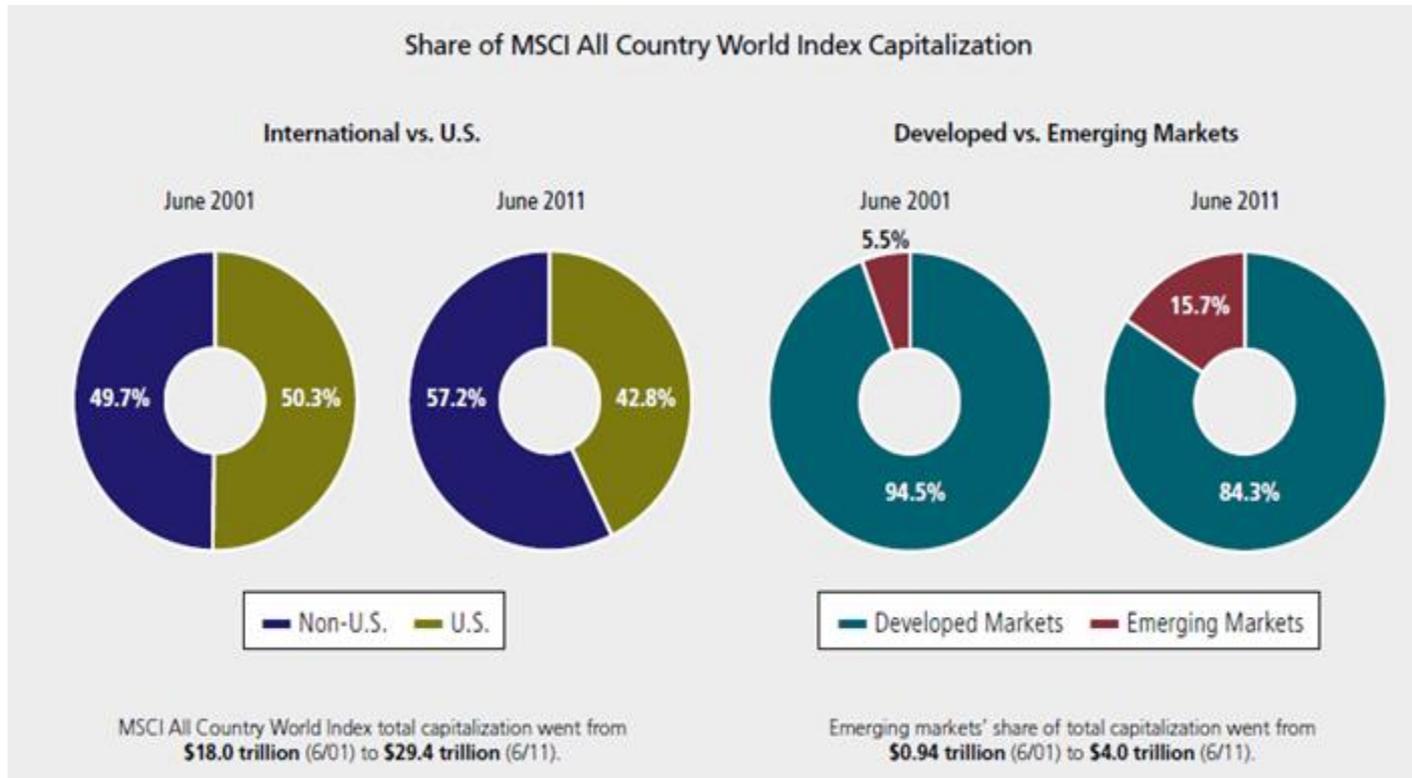
Note: Debt is general government debt, including state and local municipalities, as a % of nominal GDP, data as of April 2012

The fiscal imbalance is the difference between the present value of all future debt and the present value of all income streams.



International and Emerging Markets Stocks Have a Growing Share

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Source: FactSet



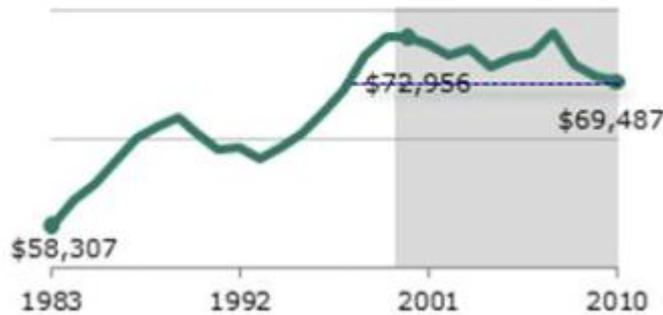
U.S. Median Income is Back to 1999 and Net Worth is Back to 1983

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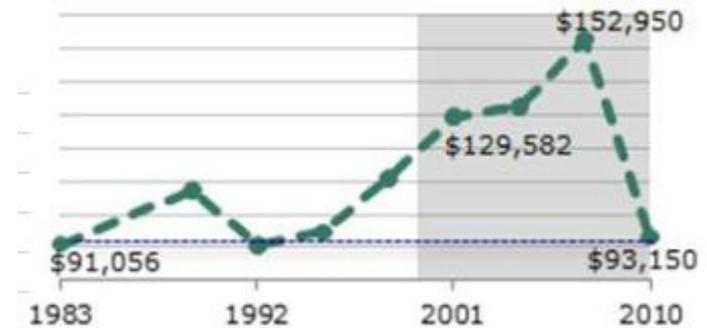
A Decade of Decline

Middle-Tier Median Household Income Falls ...

Incomes are scaled to reflect a three-person household (in 2011 dollars)



Median Net Worth Plummets ... (in 2011 dollars)



<http://globaleconomicanalysis.blogspot.com/2012/09/who-do-you-blame-for-woes-of-middle.html>

"Middle class" in the slide that contains the below charts is based on adults who describe themselves as middle class. It's not based on an income tier.



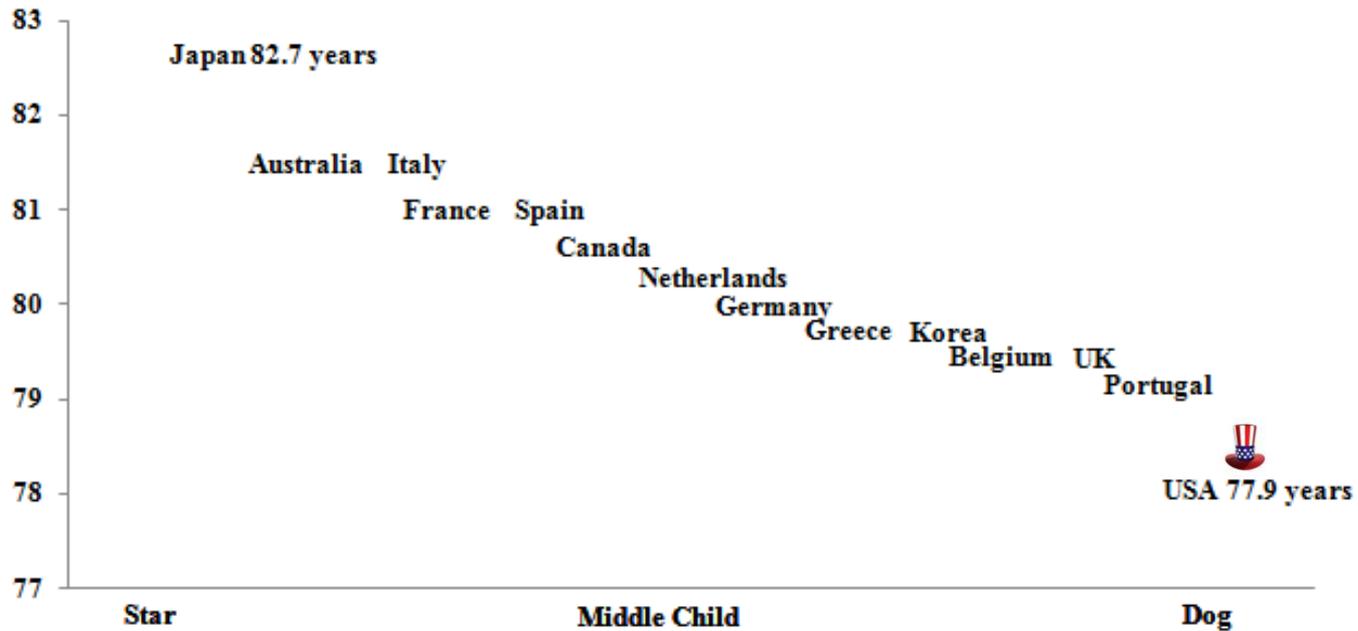
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HEALTH

U.S. Has a Lower Life Expectancy

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Life Expectancy: Total Population



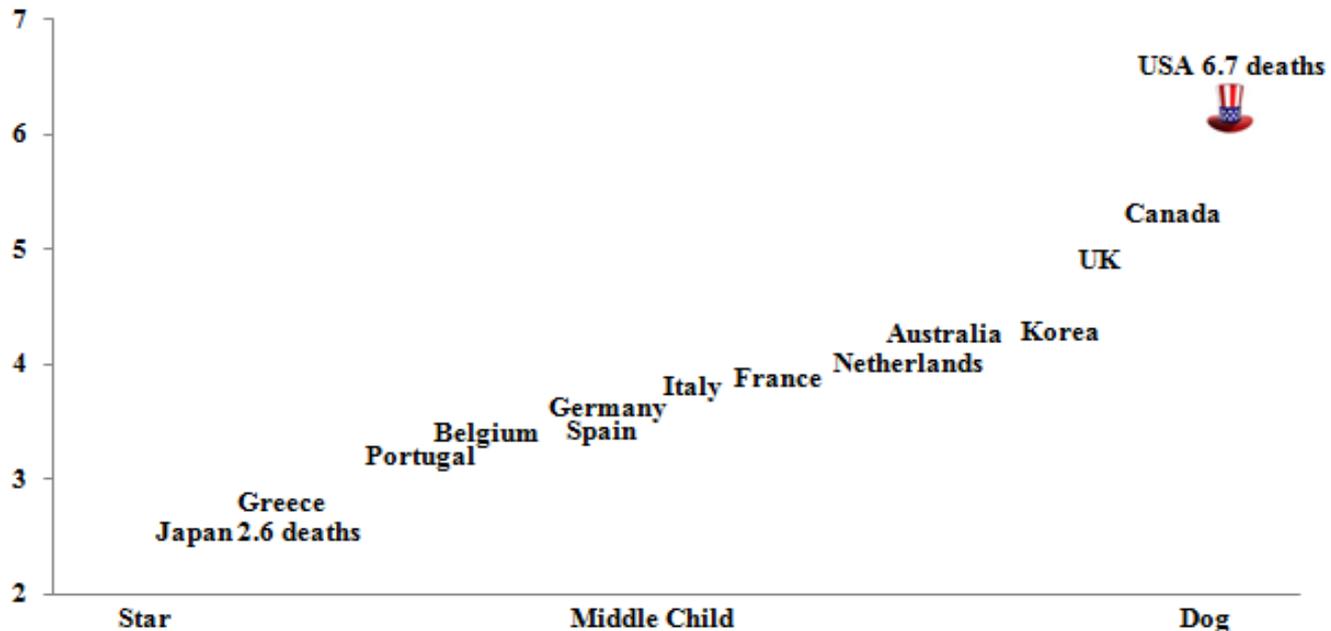
Source: The Measure of a Nation. The countries used for comparison all meet a minimum level of wealth and population size.



U.S. Has a Higher Infant Mortality Rate

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Infant Mortality: Deaths per 1,000 Live Births



In 1960, the U.S. had the 12th lowest infant mortality rate in the world. In 2008, the rank was 23rd.

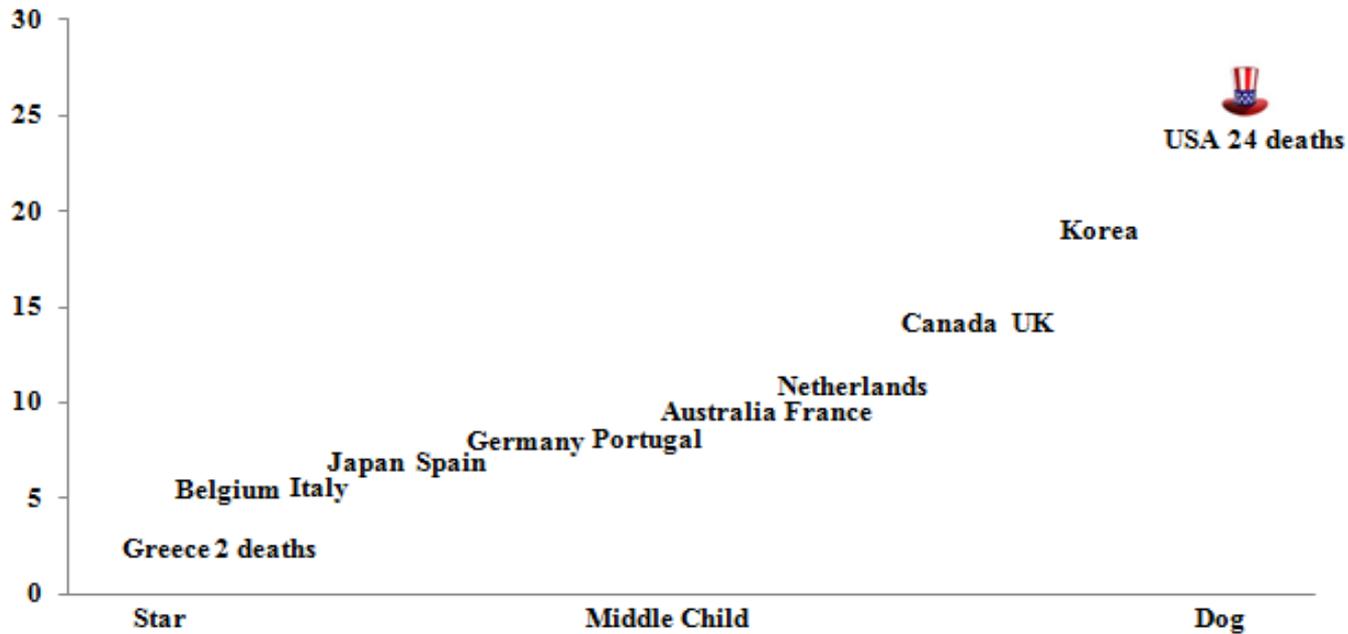
Source: The Measure of a Nation



U.S. Has a Higher Maternal Mortality Ratio

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Maternal Mortality Ratio: Deaths per 100,000 Live Births



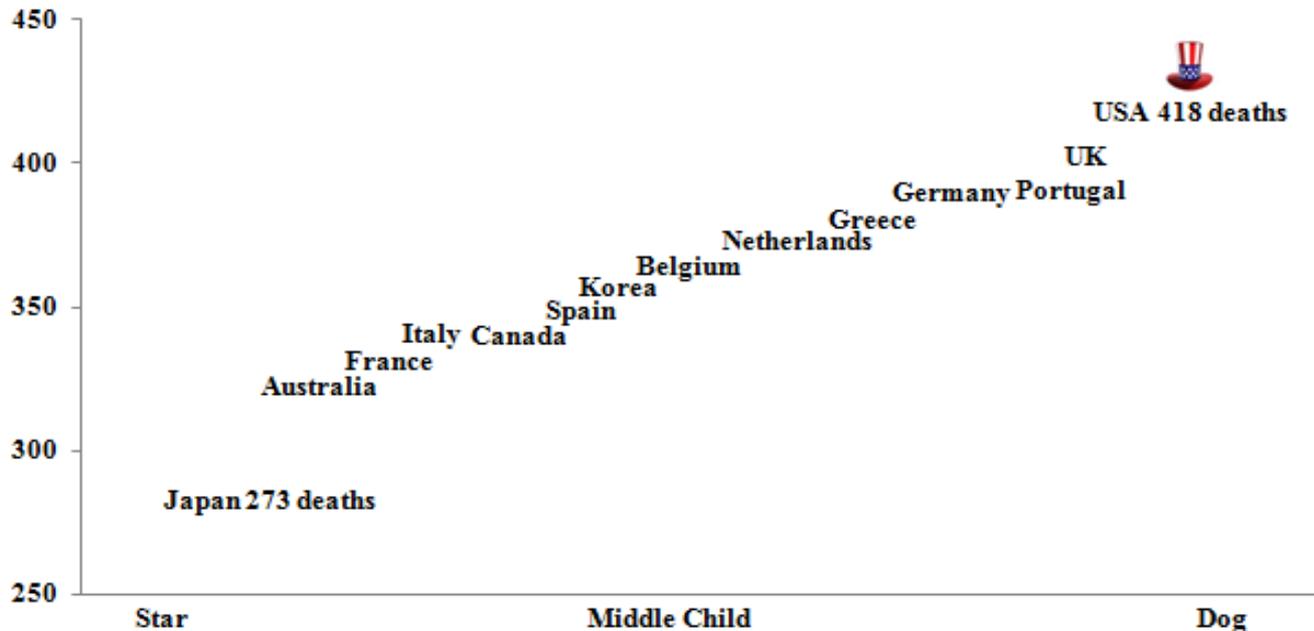
Source: The Measure of a Nation



U.S. Has a Higher Deaths Rate of Cancer And Cardiovascular Disease

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Noncommunicable Diseases: Deaths per 100,000 People

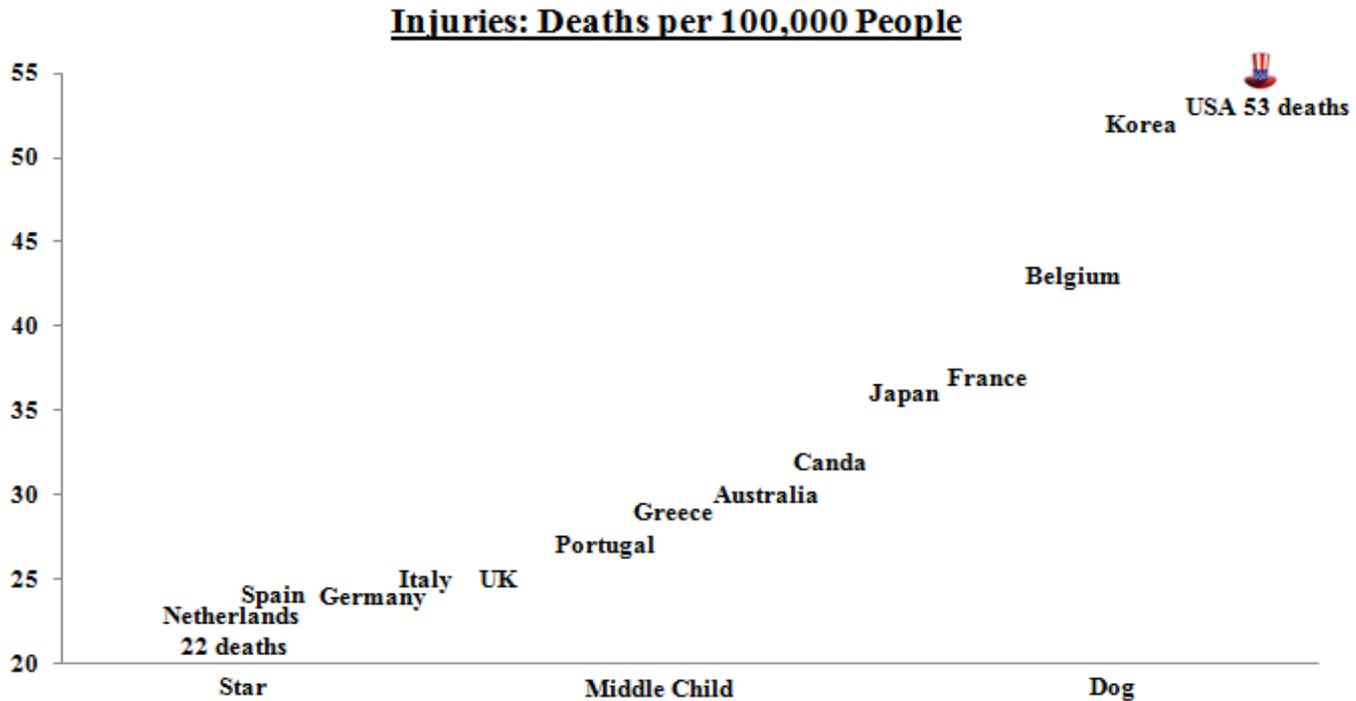


Source: The Measure of a Nation



U.S. Has a Higher Injury Mortality Rate

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Source: The Measure of a Nation



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EDUCATION

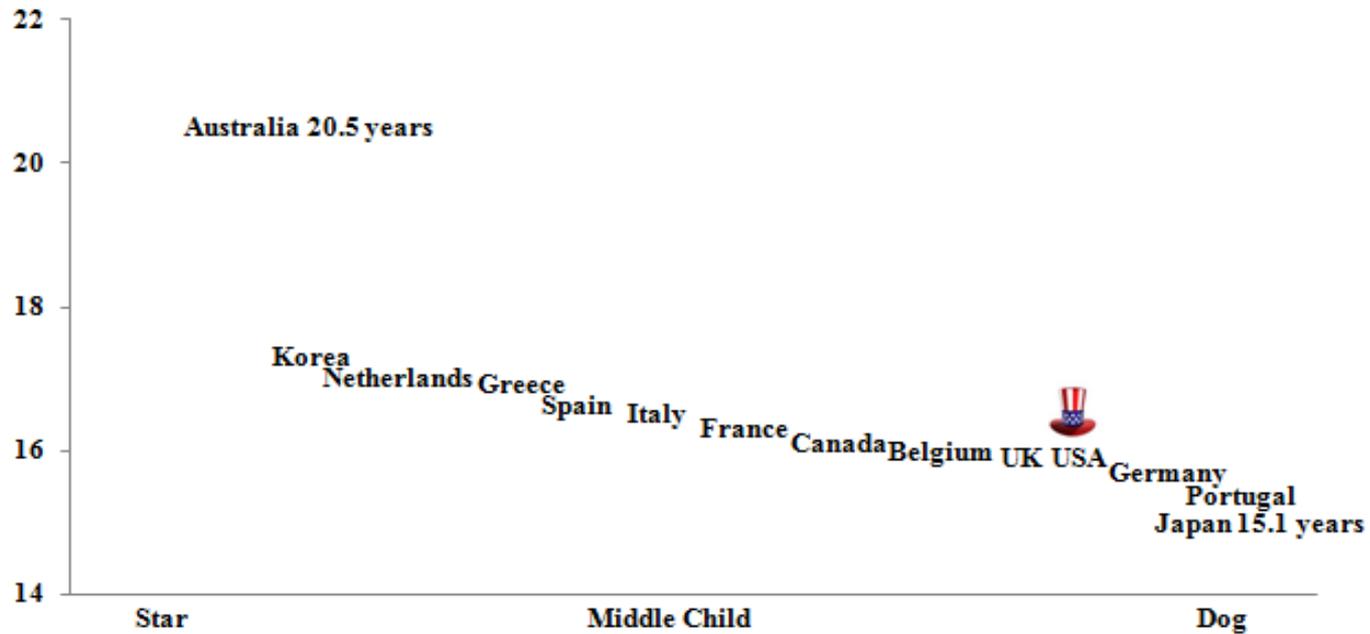
If a nation expects to be ignorant and free, in a state of civilization, it expects what never was and never will be. (Thomas Jefferson)



U.S. Has a Lower Expected Years of Schooling

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Expected Years of Schooling

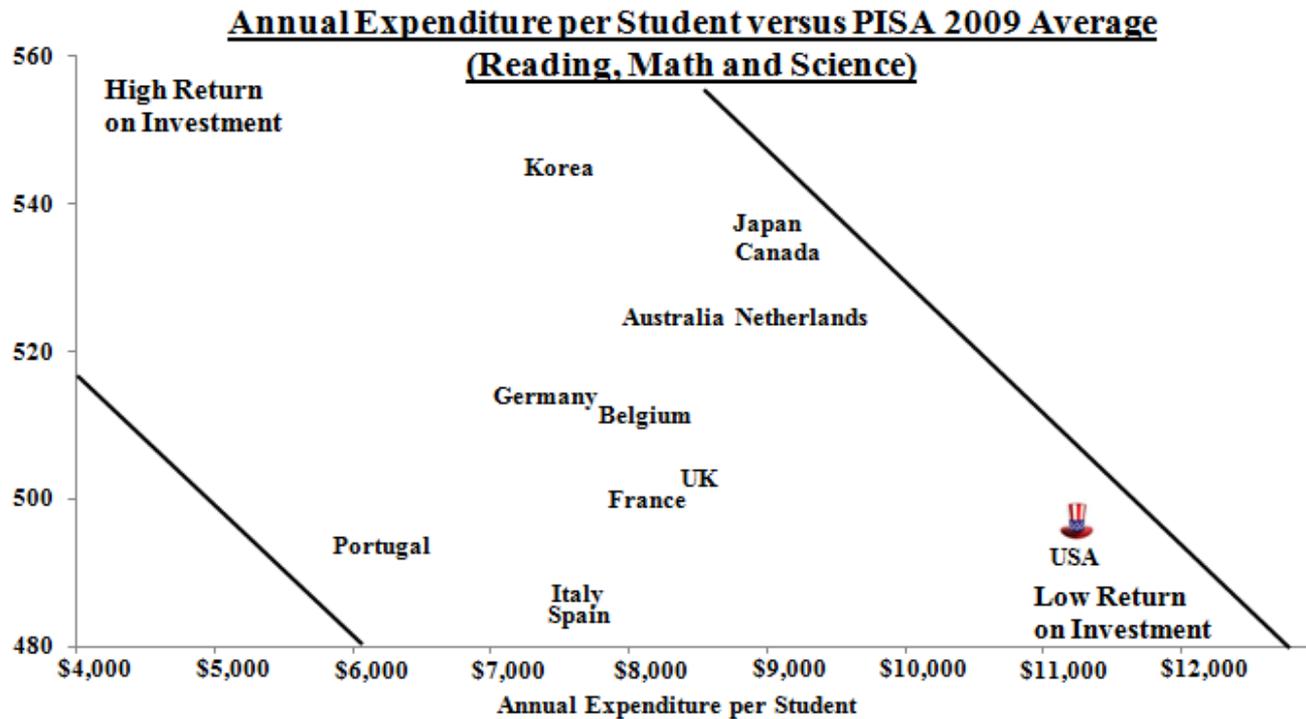


Source: The Measure of a Nation



U.S. Has a Lower Return on Investment on Education

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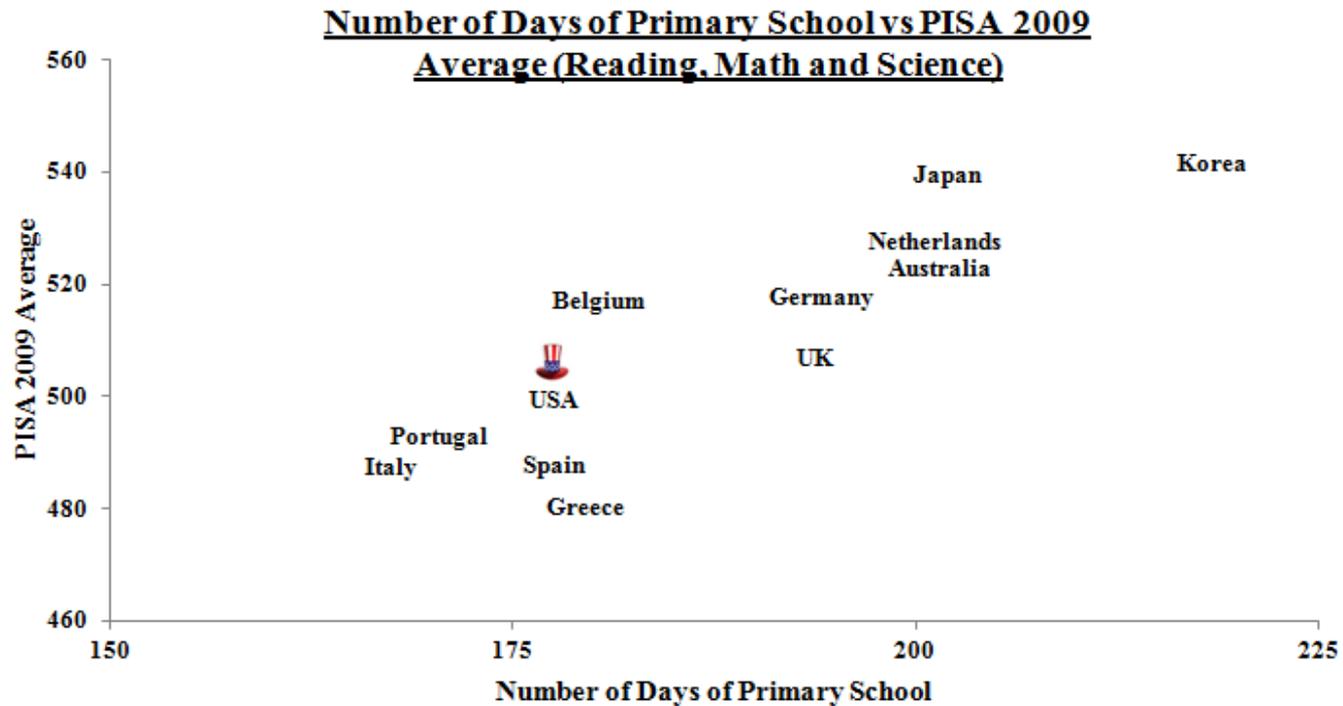


Source: The Measure of a Nation



U.S. Has a Lower Number of Days of Primary School

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Source: The Measure of a Nation



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SAFETY

They who can give up essential liberty to obtain a little temporary safety deserve neither liberty nor safety. (Benjamin Franklin)

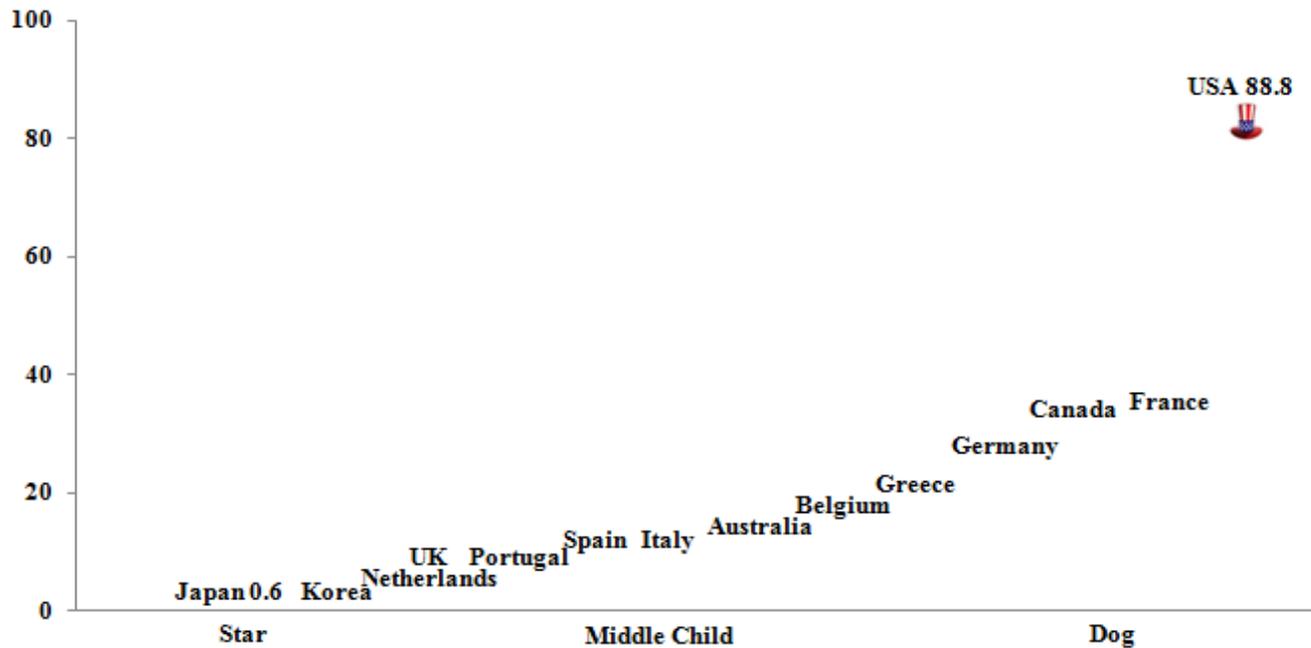




U.S. Has a Higher Firearms Ownership Rate

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Civilian Firearms Ownership Rate (per 100 citizens)



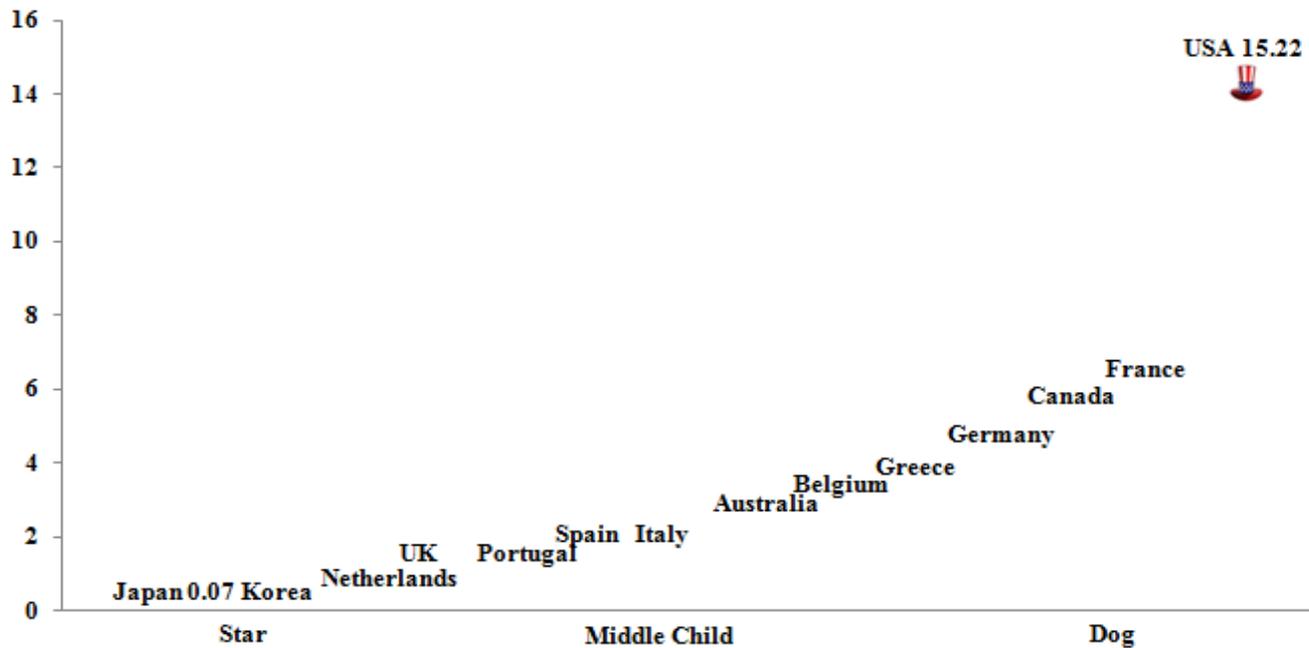
Source: The Measure of a Nation



U.S. Has a Higher Firearms Death Rate

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Firearms Related Deaths per 100,000 Citizens



If the U.S. becomes less safe, is still going to attract entrepreneurs and capital?

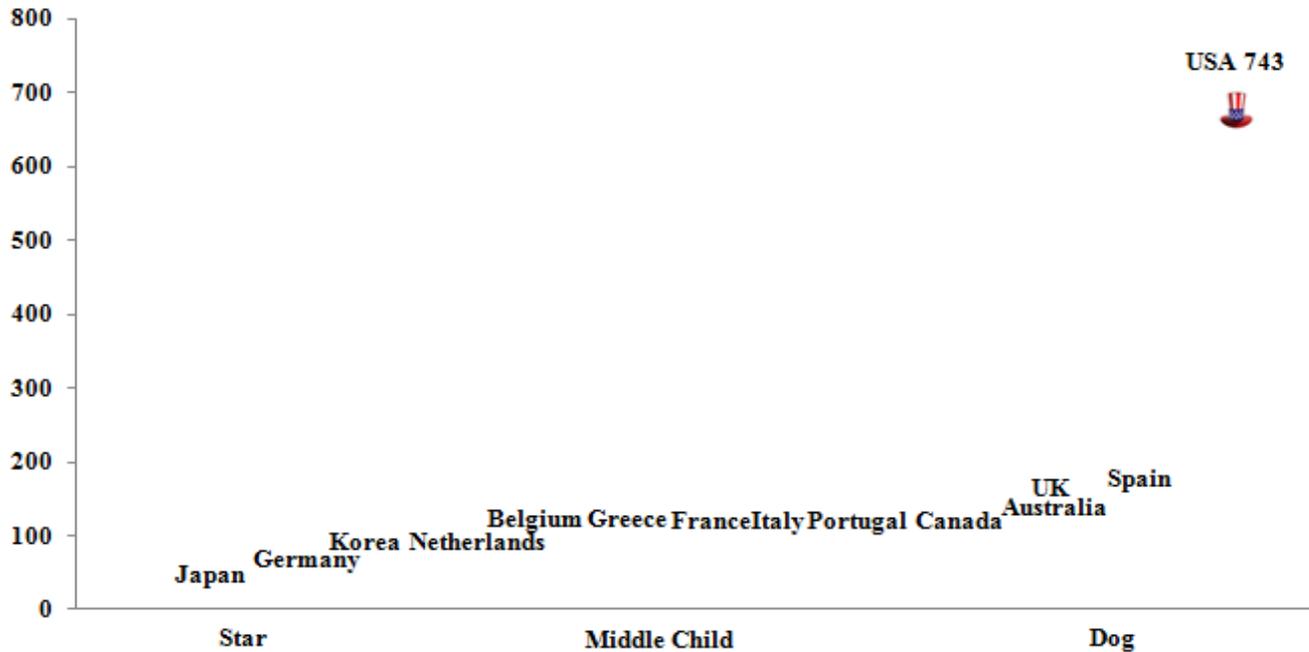
Source: The Measure of a Nation



U.S. Has a Higher Incarceration Rate

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Incarceration Rate per 100,000 Population



Source: The Measure of a Nation



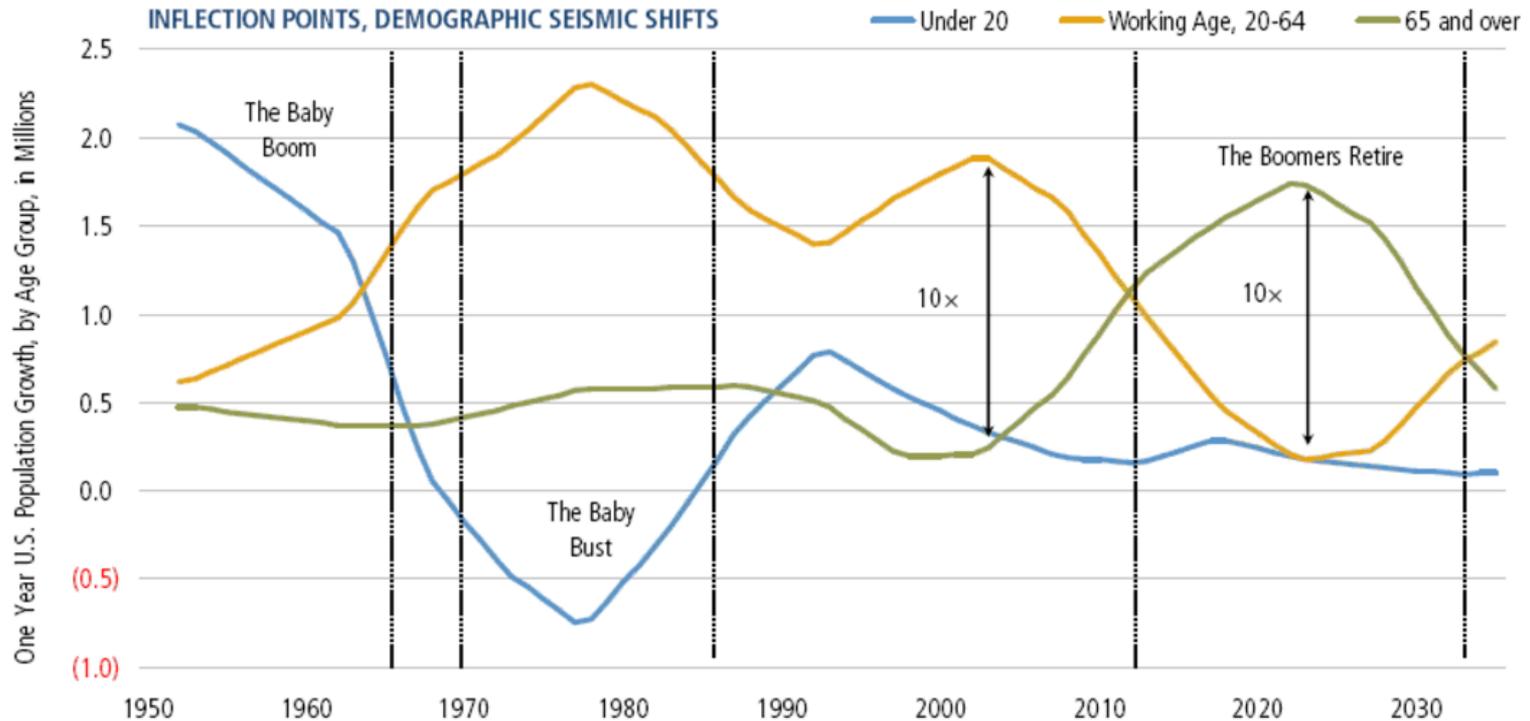
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Appendix



The U.S. Boomers are Retiring and May Become 10 Times Larger than Workers

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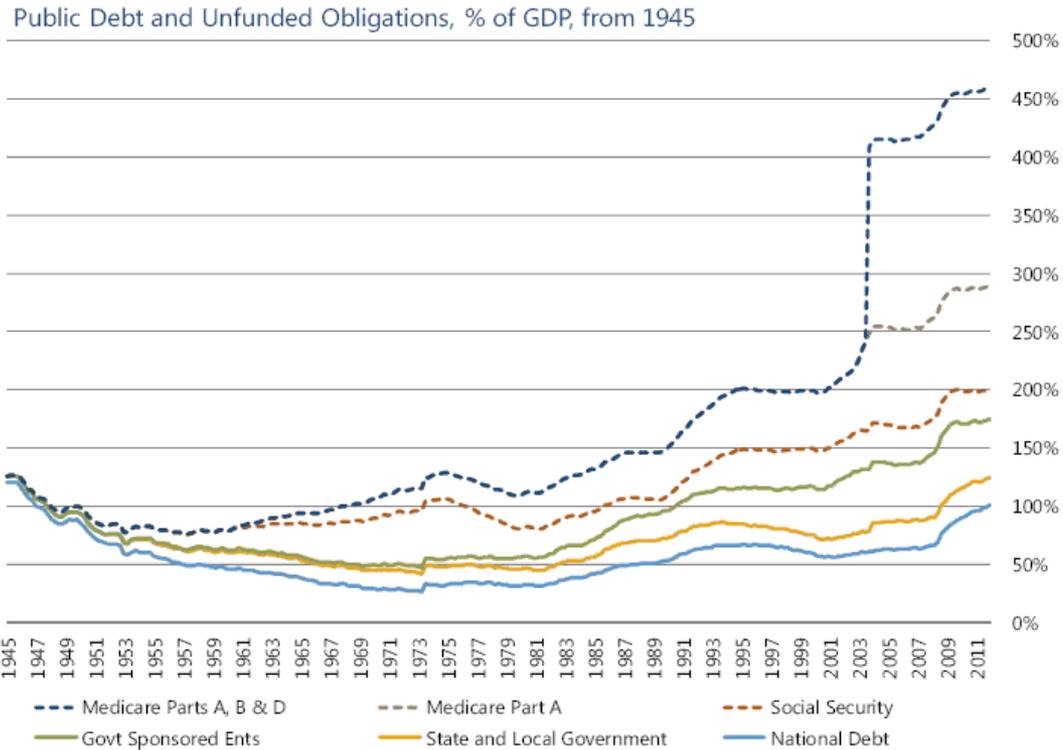


Source: Population data and projections from the U.S. Social Security Administration.



The Future Cost of Medicare has Increased to 450% of GDP

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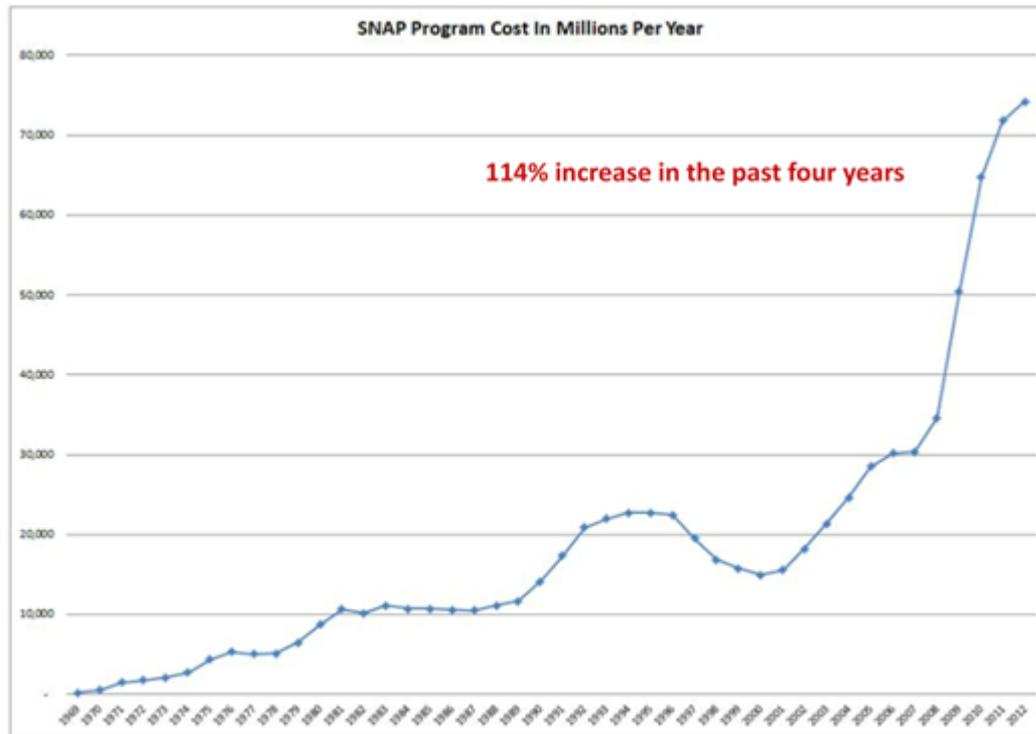


Source: Research Affiliates, LLC, based on data from the U.S. Federal Reserve Flow of Funds database and the U.S. Social Security Administration. Through 2012 Q1.



U.S. Food Stamp Program Costs Have Increased by 114% Since 2008

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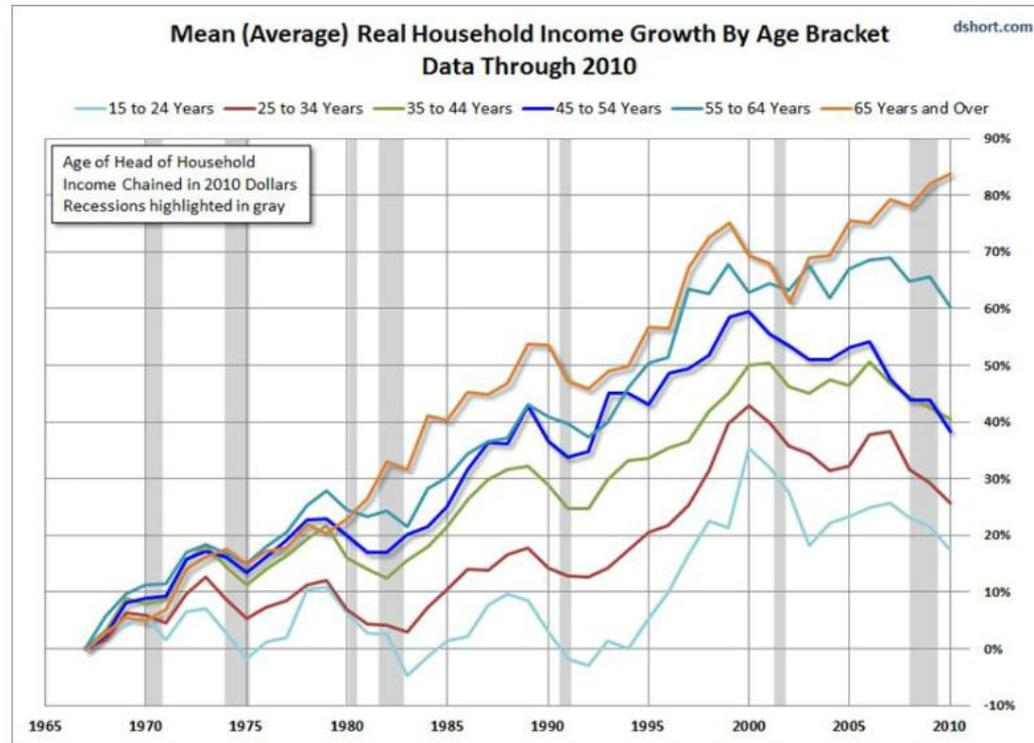


SNAP = Supplemental Nutritional Assistance Program
<http://globaleconomicanalysis.blogspot.com/2012/08/food-stamp-usage-up-64-in-last-four.html>



U.S. Real Income Growth Have Decreased

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Source: Advisors Perspective, <http://advisorperspectives.com/dshort/>



Where are the Millionaires?

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Pockets of wealth

	MILLIONAIRE* HOUSEHOLDS (% OF TOTAL HOUSEHOLDS)	SHARE OF WEALTH HELD BY MILLIONAIRE* HOUSEHOLDS (%)
1 Singapore	11.4	52
2 Hong Kong	8.8	74
3 Switzerland	8.4	44
4 Kuwait	8.2	67
5 Qatar	7.4	63
6 UAE	6.2	63
7 United States	4.1	55
8 Belguim	3.5	36
9 Israel	3.3	36
10 Taiwan	3.0	38
Global average	0.8	38

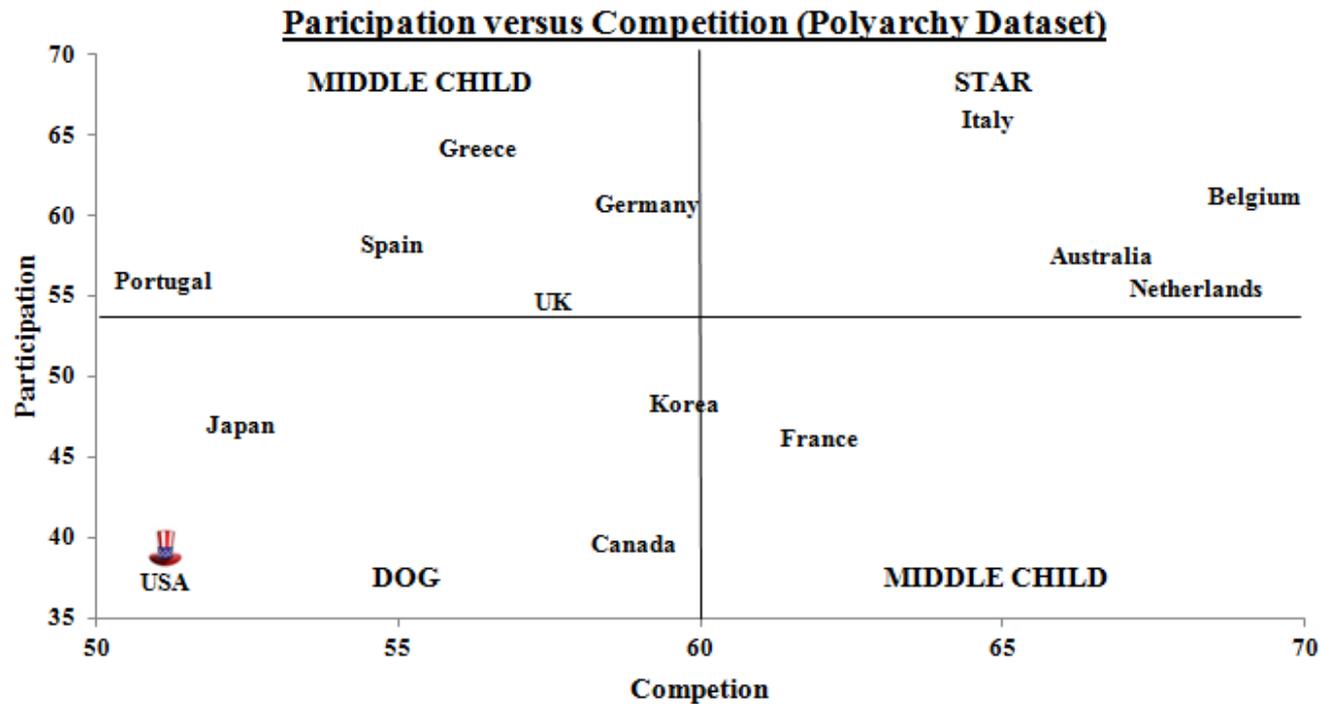
* Millionaire households are those with more than US\$1m in assets under management

Source: BCG



U.S. Has a Lower Political Competition (Many Political Parties) and a Lower Participation

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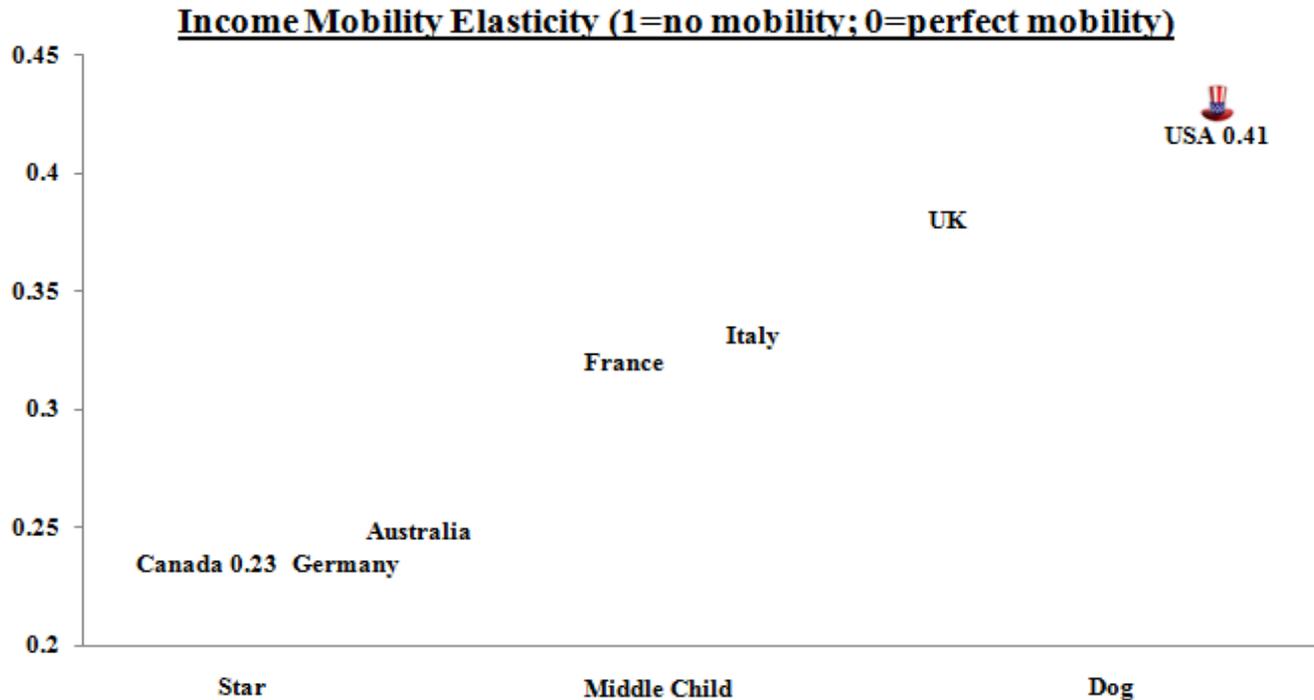


Source: The Measure of a Nation



U.S. Has a Lower Income Mobility Elasticity (Increase in Son's Income Vs. Dad's Increase)

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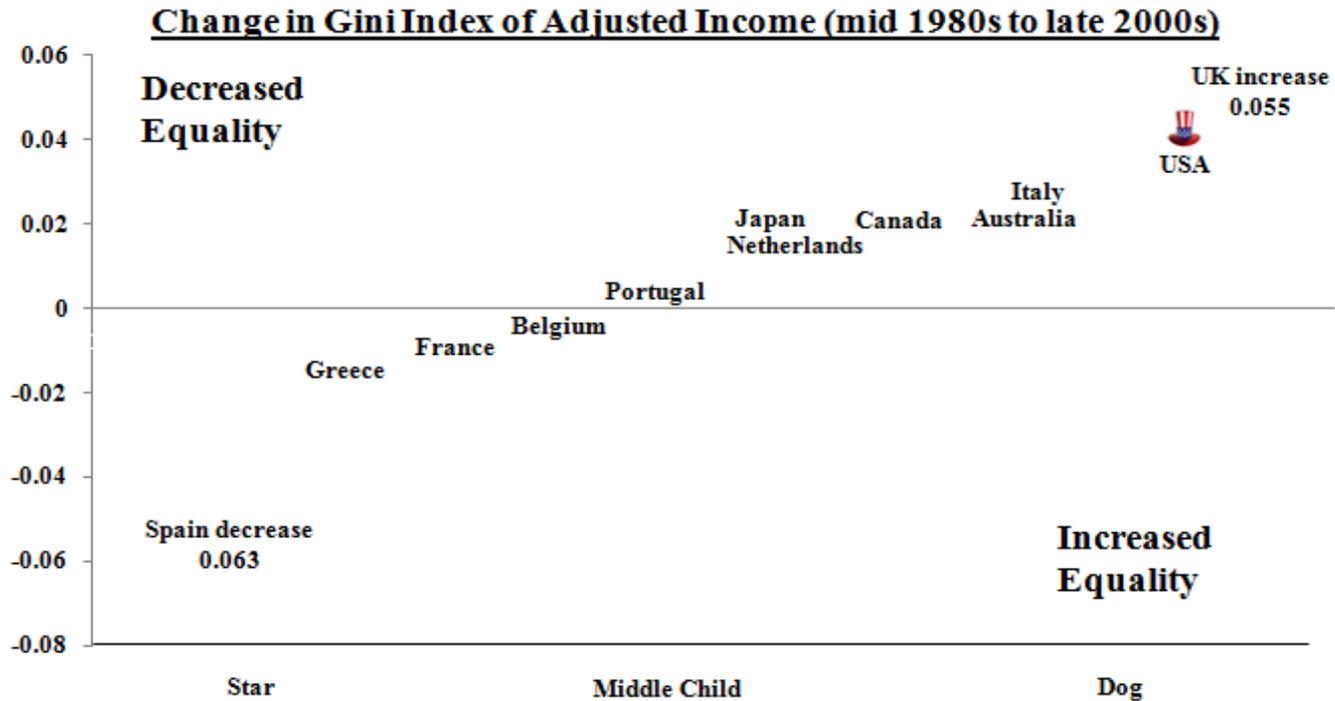


Source: The Measure of a Nation



U.S. Inequality Has Increased Since 1980

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Source: The Measure of a Nation



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Our core investment belief is that asset allocation (equities, fixed income, cash, real estate...) is the single most important determinant of success in any investment plan. The dominant amount of risk and return comes not from your choice of individual investments but from your asset class mix. Bourbon Financial Management focuses our resources on risk management, asset allocation, and securities selection.

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