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MANAGEMENT
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Ellumination Newsletter

"Separating fact from fiction since 1998. The antidote to Wall Street."

What the Heck Happened?

May 7, 2010

Given the magnitude of the sell-off in global equity markets we would normally write an Ellumination to offer our perspective. But we read an excellent piece from Fidelity this afternoon and we are forwarding it to you. We think the report provides great perspective on the forces that are impacting the markets.

Please see the attached report "Fidelity's Monthly Market Perspectives Report for May 2010".

In addition we'd like to take this opportunity to remind our clients that yesterday's conference call and slides are archived on the 5T Wealth website.

All the best,

Paul Krsek

MANAGING MEMBER & CHIEF INVESTMENT OFFICER

5T Wealth Management

(707) 603-2672 Office

(707) 486-7333 Cell

paul@5twealth.com

www.5twealth.com

5T Wealth Management, LLC

Registered Investment Advisors

702 Trancas St, Ste 200, Napa, CA 94558

(707) 224-1340 www.5TWealth.com

Disclosure and Disclaimer - Updated last on August 13, 2007 by Paul Krsek:

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5T WEALTH MANAGEMENT manages accounts with various histories and investment objectives. Various accounts may be managed differently from time to time.

Krsek makes frequent reference to the model portfolios called Hatteras, Mendocino, Halifax, Bonavista, Fresnel and The New World. During 2005 Paul Krsek was appointed Chief Investment Officer of 5T WEALTH MANAGEMENT, and as such is responsible to make all trading and management decisions for all client accounts which are being managed according to a specific portfolio model. A description of each of our models can be found on our website at <http://www.kaassets.com/choices.htm>.

Not all accounts managed by 5T WEALTH MANAGEMENT are "modeled" accounts. We strongly urge our clients to understand which model, if any, are being used to manage their accounts.

As of July 3, 2007 Lee O'Dwyer joined 5T WEALTH MANAGEMENT as a portfolio manager. Paul Krsek and Lee O'Dwyer frequently discuss investment ideas, model portfolio strategies and the investment policies of 5T WEALTH MANAGEMENT. But when it comes to the implementation of those policies Krsek is primarily responsible to manage the accounts that fit into each model portfolio description. He generally makes all final investment and trading decisions relative to those accounts that are considered to be "modeled." However, in Krsek's absence O'Dwyer does have the authority to trade all client accounts. He has been actively trading accounts in the various models since joining 5T WEALTH MANAGEMENT.

From time to time 5T WEALTH MANAGEMENT receives requests from clients to purchase securities that are not included in the model portfolio to which they are assigned. Effective May 24, 2006, 5T WEALTH MANAGEMENT has encouraged clients to hold such securities in a separate account for the client. Because 5T WEALTH MANAGEMENT is a "fee only" registered investment advisor" it charges its normal management fee for monitoring such securities in the separate accounts in which they are held.

5T WEALTH MANAGEMENT makes every effort to exclude securities that are 'requested by the client' from the modeled portfolio accounts.

The investment objectives of various accounts and models may be substantially different from one another. Therefore topics or investments mentioned in E-ELLUMINATION may or may not apply to specific managed accounts and/or models.

Trades or adjustments to accounts mentioned in ELLUMINATION may or may not happen in every account managed by portfolio managers at 5T WEALTH MANAGEMENT.

If you are not satisfied with the investment results in your account it is your responsibility to inform Krsek or O'Dwyer and to discuss possible changes that can be made to the account to accommodate and satisfy your needs.

The assets held in managed accounts at 5T WEALTH MANAGEMENT may include stocks, bonds, cash, commodities, foreign exchange or mutual funds or exchange traded funds (ETF's), money market accounts or limited partnerships that represent the same. They are subject to market fluctuation and the potential for losses. The assets are not insured. The value and income produced by these investment products may fluctuate, so that an investor may get back less than they initially invested.

The portfolio managers at 5T WEALTH MANAGEMENT do not guarantee results.

Past performance should not be considered an indicator of potential future performance. If you do not consider yourself suitable, either emotionally or financially, to experience volatility and/or losses in financial markets, you should not invest.

From time to time Krsek lists the simple annual returns of the six model accounts in this newsletter. These accounts are "models" and do not represent the actual results accruing to individual accounts. Simple annual return does not represent "time weighted return" as reported individually to clients in their quarterly reports prepared using Centerpiece.

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Fidelity Investments Institutional Services

Market Perspectives

May – 2010

Market Perspectives

Jurrien Timmer

Director of Market Research & co-pm of Fidelity Advisor Dynamic Strategies Fund & Fidelity Dynamic Strategies Fund

May 6, 2010

Greek Contagion or Fat Fingers? How About Both?

What Happens in Greece Doesn't Stay in Greece!

Wow, what a day. At around 2:30 pm today, the markets went into a free fall, with the DJIA losing about 700 points in a matter of minutes, for an overall intra-day loss of a thousand points.



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Fri May 07 2010 04:14:38

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Market Perspectives

What was behind this mini-crash? It all started with the ongoing contagion in peripheral Europe, which has been causing massive pressures on the bond yields of the PIIGS* and a commensurate fall in the Euro against not only the dollar but also the Yen and other currencies (including gold).

Why are the problems in Greece et al lingering? Because the only solution that the market seems to find credible is for the ECB to do what the Fed did in 2008-09, which is to expand its balance sheet and engage in Quantitative Easing. In other words, what the market wants is for the ECB to buy the debt of the PIIGS and put that debt on its balance sheet. That is what the Fed did with mortgages, agencies and treasuries in 2009, and this what many investors believe will be the only way out of the European debt crisis. Indeed, this is why the euro has been selling off and the dollar and gold rallying. Whenever a central bank engages in quantitative easing, it is essentially trying to print its way out of trouble, and that tends to devalue the currency. This is what the Fed did back in 2008-2009 and now it's the ECB's turn.

However, this is not happening, at least not yet. The ECB met today, and according to Jean-Claude Trichet, the topic of buying debt was not even discussed. What a joke! Needless to say, as soon as this came out the market sold off in a big way. It seems amazing that the ECB would not even discuss this, but perhaps it has to do with the fact that Germany is loath to go along with any plan to inflate.

Germany has a long and painful history with inflation dating back to the Weimar Republic hyper-inflation of the 1920's, and it is Germany who is standing in the way of the ECB going into full-fledged QE mode. Instead, Germany wants to enforce austerity in Greece. But as we have been seeing from the news these past few days, the Greeks are in no mood to tighten their belts.

So, that leaves Europe with two bad choices: kiss good-bye to the single currency concept, or support the lowest common denominator by guaranteeing or buying the sovereign debt of Greece et al. Either way, it is bad for the Euro, although with sentiment in the low single digits this has been well discounted by now.

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Market Perspectives

So far, the northern European countries have resisted QE, but my guess is that the meltdown in the Euro and asset markets will force their hand. Sort of like the first round of TARP being voted down by Congress in the fall of 2008, only to have the subsequent sell-off scaring them all straight.

So, this is what set the stage this morning. Compared to the U.S. where the Fed, Treasury, Congress and President all acted in a relatively swift and decisive way during the credit crisis (the TARP vote notwithstanding), the Europeans seem to be horribly disorganized.

This is what the critics of the Euro have always pointed to: how can you have a single central bank and a single currency when you have all these different countries with their own unique governments and social structures? This is make or break time for the Euro, which is why gold is now soaring in Euros.

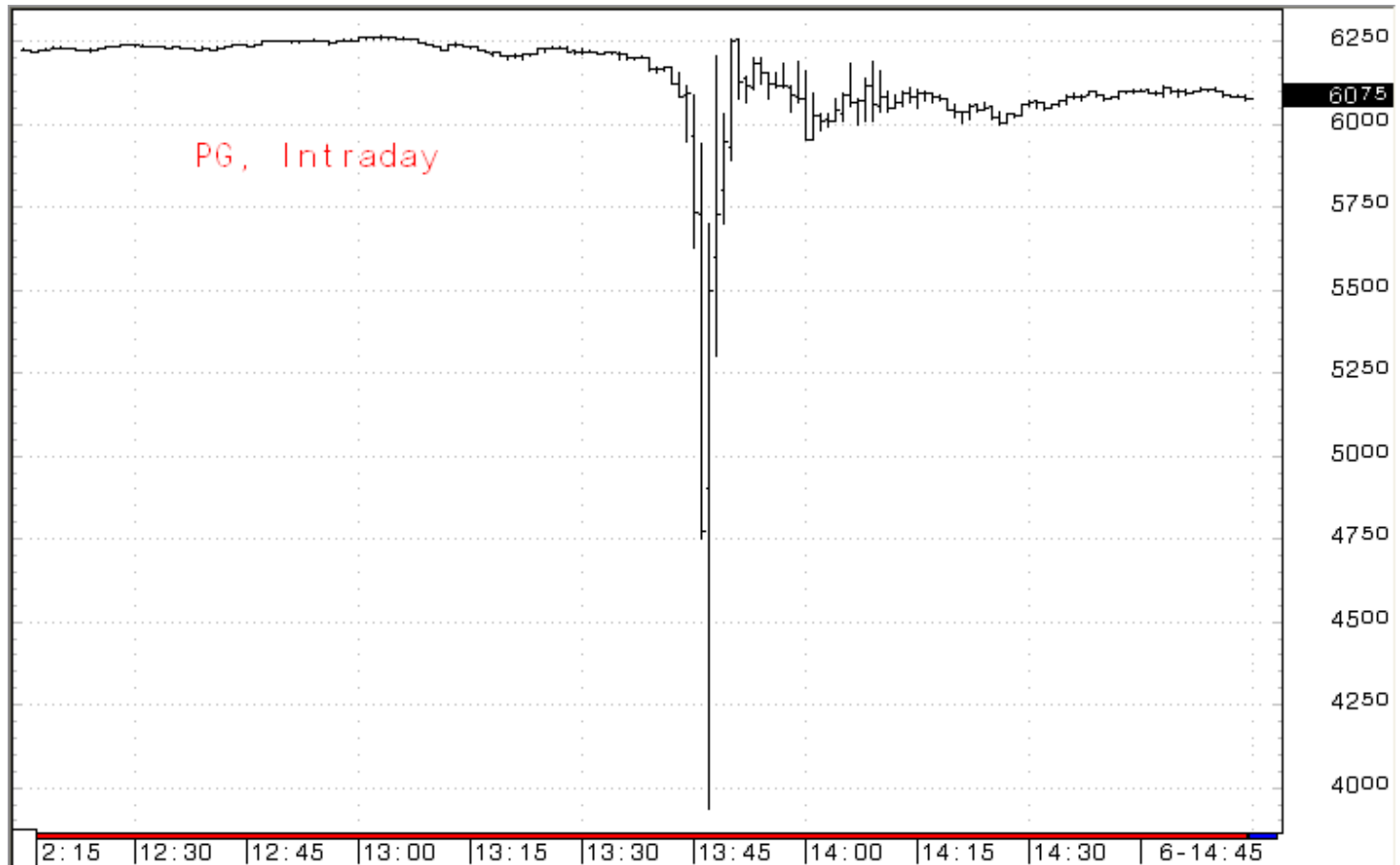
Fat Fingers

Then came the “fat fingers” trade. Apparently, somebody entered a program trade and put in a few too many zeros. What happened next was nothing short of surreal. The Dow lost almost 700 points in a matter of minutes, and by 2:45 pm the Dow was down a thousand points. When you look at where some stocks traded, you can immediately see that this was not normal. For instance, P&G lost \$20 in seconds, Apple was down \$50, and several stocks traded down to a penny! I was just sitting there staring at my screen in disbelief. Then the markets came roaring back, and by the end of the day the market had closed down hard but well off the lows of the day.

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Market Perspectives



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A Game of Chicken with the ECB

Where does that leave us? At this point, the markets are staring down the ECB and it's my guess that the market will continue to sell off until the ECB "blinks" by going the QE route. A classic game of chicken. But blink they will, and when they do, it will be a matter of selling the rumor and buying the news. There is no doubt in my mind that Fed Chairman

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Market Perspectives

Bernanke is on the phone with Trichet right now saying something like “what the \$&#@ are you thinking? Don’t you realize that our QE saved the system for us? What are you waiting for?”

At the end of the day, we have to ask ourselves how contagious the European debt crisis really is for the U.S. As far as I can tell, US banks do not have a meaningful exposure to peripheral European countries, so the contagion should be limited. The real contagion in my opinion is that if the US can’t grow and inflate its way out of its own debt burden, then what is happening in Greece right now could be happening in America down the road (social unrest included).

But if that is the contagion the market was worried about today, then why did Treasuries rally? They should have been at the center of the storm. So, I don’t think it’s that. Instead, I suspect it was an overall sense of fear, some upside down hedge funds or prop desks getting out of bad trades, and all of that compounded by the sharp rise in the dollar. After all, a strengthening dollar is a form of tightening, and tightening is the opposite of reflation which is what the risk markets crave. A strengthening dollar means more expensive exports and a flight to quality and away from risk. Other than a debt crisis, the markets probably fear tightening more than anything else right now.

The good news is that the action today will likely put the Fed on hold even longer than it was planning to be, so this “tightening” will actually prolong the reflation in the long run, which is good. So, nobody has to worry about the Fed raising rates or shrinking its balance sheet anytime soon. In fact, if there are any renewed strains in our credit markets I would expect a new round of QE by the Fed. This is another reason why gold has been strong. Gold is the ultimately hedge against too many governments printing too much money.

As for the charts, we have now had our second major correction of close to 10% this year, with the S&P 500 trading down to 1070 or so today, exactly at four units down from the small head 7 shoulders top at the high. Looks like a capitulation low to me.

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Market Perspectives

The DSI (Daily Sentiment Index) for the Euro is 2% bulls today. That's what the DSI was for stocks at the March 2009 low. The DSI for the S&P 500 was 43% today, a far cry from that 2% 14 months ago but well below the 92% reading a few weeks ago. The DSI for gold is 95% today, the opposite of the Euro.

Given the dramatic capitulation, I would suspect the markets to recover in the days ahead. But Europe needs to come to a resolution and Greek austerity alone is not going to cut it. Europe needs to either cut Greece loose or the ECB needs to expand its balance sheet by buying Greek debt. Make a decision, and make it fast.

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* The acronym PIIGS refers to the following countries in Europe: Portugal, Ireland, Italy, Greece, and Spain.

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