



# THE *Tri Pillar Investments Presents...* MONTHLY ECONOMIC UPDATE

February 2012

## MONTHLY QUOTE

“When we recall the past, we usually find that it is the simplest things - not the great occasions - that in retrospect give off the greatest glow of happiness.”

– *Bob Hope*

## MONTHLY TIP

If you are thinking about a reverse mortgage, you might consider an interfamily loan as a friendlier, lower-cost alternative. Either way, it may be wise to speak with a financial professional before making this kind of decision.

## MONTHLY RIDDLE

Sometimes you pass me slowly, yet other times I just fly by. Sometimes I simply slip away. Regardless of how slow or fast I am, one thing's for sure: when I'm gone, I'm gone for good. So what am I?

### Last month's riddle:

What can you fill with empty hands?

### Last month's answer:

Gloves.

## THE MONTH IN BRIEF

In recent stock market history, there have been many peaks and valleys. January 2012 represented a peak; it was the best January for U.S. stocks since 1997, with the S&P 500 rising 4.36%. It was also the S&P's best month overall since October. Wall Street seemed to worry a little less about Europe during the month and a little more about subpar stateside indicators like consumer spending and home sales. Still, the mood was definitely bullish.<sup>1,2</sup>

## DOMESTIC ECONOMIC HEALTH

Consumers were earning more – and apparently saving more of what they earned. Personal incomes rose 0.5% in December, and so did the personal saving rate, yet personal spending was flat for the month. After consumer spending increases of only 0.1% in October and November, this seemed to hint at a slowing economy in the last quarter of 2011. However, the jobless rate was at 8.3% in January, the lowest level in three years, thanks to the addition of 243,000 jobs.<sup>3, 24</sup>

Was consumer confidence wavering? It depended on which barometer you checked. The Conference Board's January survey fell to 61.1 from December's 64.8 final revised mark, in the previous month, according to the Conference Board. Economists polled by Reuters had thought it would climb to 68.0. The University of Michigan's consumer sentiment survey made a major advance in January, going to 75.0 from the year-end mark of 69.9.<sup>2,4</sup>

The initial estimate of Q4 2011 GDP arrived in late January; a growth of 2.8%, the best in six quarters, was still below the expectations of some analysts. Speaking of growth, our manufacturing sector grew for a thirtieth straight month in January, according the PMI index of the Institute for Supply Management, rising a full percentage point to 54.1. ISM's service sector index had also posted a December advance to 52.6 from 52.0. Not surprisingly, durable goods orders improved 3.0% in December, the third consecutive monthly gain for the indicator; orders for hard goods increased 10.0% across 2011.<sup>4,5,6,7</sup>

As for consumer and wholesale inflation, the threat was mild to say the least. In fact, the Consumer Price Index didn't budge in December and the Producer Price Index retreated 0.1% (with import prices falling for the fourth month in five). So, 2011 goes in the books with 3.0% consumer inflation and 2.2% core inflation; the most since 2007, but hardly remarkable.<sup>8</sup>

## GLOBAL ECONOMIC HEALTH

Efforts to restructure Greece's debt fell apart at mid-month, but picked up some momentum. At the end of January, a deal looked imminent, but in the eyes of some analysts, investors would have to accept as much as a 70% haircut on Greek bonds to take Greece's debt-to-GDP ratio down to a sustainable 120% or so. Last month, Standard & Poor's downgraded credit ratings of nine EU nations: it cut ratings for France, Austria, Slovakia, Slovenia and Malta by a notch and Italy, Portugal, Spain and Cyprus by two notches, commenting that the European Union's debt reduction plan was not of “sufficient size or scope”.<sup>9,10</sup>

Manufacturing did pick up in some key economies in January. Our key PMI (the ISM survey) improved for the seventh straight month, and China's official PMI improved 0.2% to 50.5 with new orders at a three-month peak. The U.K.'s PMI

climbed above 50 again to 52.1. Germany's manufacturing index advanced for the first time since September, and that helped the EU's Markit PMI rise to 48.8 last month, but the Markit PMI has been below 50 (read: contraction) since last July. Overall, JPMorgan's global manufacturing index rose to 51.2 last month.<sup>11</sup>

## WORLD MARKETS

Broadly speaking, it was a very good month for equities. Three of the BRICs posted outstanding gains: Sensex, +11.2%; RTSI, +14.1%, Bovespa, +11.1%. (The Shanghai Composite went +4.2% last month.) Argentina's Merval pulled off a 13.2% gain and the Hang Seng rose 10.6%; the MSCI Emerging Markets Index climbed 11.2%. Other notable indices and their January performances: Dow Jones Asia Pacific Index, +8.1%; MSCI World Index, +4.9%; Nikkei 225, +4.1%; DAX, +9.5%; CAC 40, +4.4%; FTSE 100, +2.0%; KOSPI, +7.1%; All Ordinaries, +5.2%; TSX Composite, +4.2%. At the back of the pack among indices of consequence: Spain's IBEX (-0.7%) and Malaysia's Kuala Lumpur Composite (-0.6%).<sup>12,13</sup>

## COMMODITIES MARKETS

Metals set the pace in the sector last month. Gold fully rebounded from a poor December with a 10.91% monthly gain. Copper futures gained 10.30% and silver futures soared 19.15%. RBOB gasoline futures rose 8.79% on the NYMEX last month; retail pump prices went up 5.32%. Oil (-0.35%) and natural gas (-16.26%) retreated thanks to lessening demand and warmer weather. Key crop futures rose and fell, with coffee going -5.07% on the month, corn going -1.16%, cotton +3.09% and wheat +2.03%. The U.S. Dollar Index fell 1.37%.<sup>14</sup>

## REAL ESTATE

The bad news seemed to outweigh the good news in this sector. The National Association of Realtors said that existing home sales improved 5.0% in December; in mid-January, Freddie Mac reported another record-low average interest rate for the 30-year FRM (3.88%, and a new record low would be set in early February). On the other hand, NAR reported a 3.5% dip in pending home sales in December and the November Case-Shiller Home Price Index slipped for October, its third straight monthly descent. While the Commerce Department noted that single-family home starts hit their highest level since April 2010 in December, overall housing starts dropped 4.1% for the month and new home sales slipped 2.2% to an annual rate of just 307,000. The annual new home sales pace is around 750,000 in a decent year.<sup>8,14,15,16</sup>

Here was the change in average home loan interest rates between Freddie Mac's December 29 and February 2 Primary Mortgage Market Surveys: 30-year FRMs, 3.95% down to 3.87%, 15-year FRMs, 3.24% down to 3.14%; 5/1-year ARMs, 2.88% down to 2.80%; 1-year ARMs, 2.78% down to 2.76%.<sup>17,18</sup>

## LOOKING BACK...LOOKING FORWARD

January was the best month for all three headline U.S. stock indices since October. The DJIA ended January at 12,632.91, the S&P 500 at 1,312.41 and the NASDAQ at 2,813.84. The CBOE VIX (the so-called "fear index") was near 19 at month's end.<sup>1,2,19</sup>

% CHANGE	Y-T-D	1-MO CHG	1-YR CHG	10-YR AVG
DJIA	+3.40	+3.40	+6.23	+2.73
NASDAQ	+8.01	+8.01	+4.21	+4.55
S&P 500	+4.36	+4.36	+2.04	+1.61
REAL YIELD	1/31 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	-0.28%	1.08%	2.40%	3.48%

We had a very nice January, and while you can't gauge tomorrow's market behavior off history, it is encouraging to note that the S&P 500 advanced an average of 23%

during the last five years in which it gained 4% or more for January. Another nice tidbit: when the Dow has had a positive January, it has finished that year in the black 82% of the time.<sup>1,2</sup>

Manufacturing seems to have picked up around the globe, and our manufacturing sector might be among the world's healthiest. We still seem to be in a slow recovery, and the chance of a recession in the European Union (along with its sovereign debt morass) may exert a drag on our markets in February and beyond. Still, it looks like Greece is in line for a second IMF bailout and an actual "solution" toward its debt problem, so institutional investors might be less troubled by the EU debt crisis. If our economy goes to stall speed, the Fed could even opt for a QE3 in the coming months (a possibility in the opinion of some Wall Street analysts). February holds a lot of promise; for the first month in many, world markets may turn on headlines from America instead of Europe.

**UPCOMING ECONOMIC RELEASES:** Here is the schedule for the rest of the month: the initial University of Michigan consumer sentiment survey for February (2/10), January retail sales and December business inventories (2/14), January industrial output and the January 25 FOMC minutes (2/15), the January PPI and January housing starts and building permits (2/16), the January CPI and the Conference Board's Leading Economic Indicators index for February (2/17), January existing home sales (2/22), January new home sales and the final University of Michigan consumer sentiment survey for the month (2/24), January pending home sales (2/27), January durable goods orders, the December Case-Shiller home price index and the Conference Board's February consumer confidence poll (2/28), and the second estimate of Q4 GDP plus a new Beige Book from the Fed (2/29). The January consumer spending numbers come out on March 1.

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## **The TPI Perspective: By Dr. Barry D. Kendell**

### **THE MARKET IN REVIEW**

Stocks recorded a week of strong gains. The S&P 500 was up 2.2 per cent with its best weekly gain in six weeks. The Nasdaq Composite jumped up 3.2 per cent with its best week in the last nine. Even those were trumped by the small-cap Russell 2000, which shot up 4.0 per cent. The markets started the week off declining when Greece sparred with European leaders over a second rescue package. Markets saw good gains on Wednesday, in response to an encouraging estimate of job gains from payroll processing firm ADP. The real surge followed Friday's official jobs report.

The Labor Department reported that nonfarm payrolls had increased by 243,000 in January, the second-straight month of better-than-expected gains and the most since April. The unemployment rate also declined two-tenths of a point to 8.3 per cent- its lowest since February 2009. The industries with the largest employment gains were Manufacturing, Professional & Business Services, and Leisure & Hospitality. While job creation appeared to be gaining traction, the number of layoffs also showed signs of slowing, as fewer people filed claims for unemployment benefits. Federal Reserve Board Chairman Ben Bernanke told a congressional committee that while the pace of the economy would increase modestly this year, the economy faced considerable headwinds, including the weak housing sector and continuing challenges stemming from the sovereign debt crisis in Europe. He urged lawmakers to reduce the federal debt but cautioned against cutting spending or raising taxes too quickly, which could undermine the recovery.

### **EUROPEAN NEWS**

Greek Prime Minister Lucas Papademos struck a tentative deal with political parties on austerity measures demanded by international creditors, as European leaders maintained pressure to complete terms for a 130 billion-euro rescue package. Chiefs of the three parties supporting Papademos's interim government were due to meet midday Monday to hammer out details, after setting a framework for recapitalizing

banks, ensuring the viability of pension funds, and reducing wages and non-wage costs to boost competitiveness. They agreed in a five hour meeting on Sunday to make additional reductions this year equal to 1.5 per cent of gross domestic product. Antonis Samaras, the head of the second-biggest party, New Democracy, indicated he would oppose some measures that the so-called troika of international creditors have put forward. The troika is comprised of the European Commission, the European Central Bank, and the International Monetary Fund. They want assurances that whoever wins the next election, which could be held in April, will stick to pledges made now to receive financing. Greece's biggest public-sector and private-sector union groups called a 24 hour general strike for Tuesday to protest austerity measures.

German Chancellor Angela Merkel and French President Nicolas Sarkozy have proposed setting up a separate account for Greek debt payments to reassure creditors. Merkel said sequestering aid in such an account would give the Greek government guaranteed access to funds to finance interest obligations. Sarkozy said it will "allow us to assure the Greek debt is dealt with," as both urged Greek leaders to agree to conditions set out by international creditors. Merkel went on to say, "We want Greece to stay in the euro. I want to make clear once again that there can be no deal if the troika proposals are not implemented. They are on the table, time is of the essence. Something needs to happen quickly."

### **SUPREME COURT'S HEALTH-CARE LAW NEWS**

The U.S. Supreme Court will hear arguments on President Barak Obama's health-care law over three days, from March 26 to March 28. The high court generally hears arguments for a single hour. However in an unprecedented move, they have left room to expand to 5 and one half hours. The first day will center on the Anti-Injunction Act, also known as the individual mandate that Americans either buy insurance or pay a penalty. On the second day of the hearings, they will consider the central issue of the constitutionality of the individual mandate. On the final day, the court will hear arguments on whether other parts of the law should be invalidated along with the individual mandate. The justices will also consider challenges to a provision expanding the Medicaid program for the poor.

### **LOOKING AHEAD**

Next week, Coca-Cola, Emerson Electric, Walt Disney, Visa, Pepsico and Cisco are scheduled for reports. Major economic reports for next week include December Wholesale Inventories, December Trade Balance, February University of Michigan Consumer Confidence and January Monthly Budget Statement. A busy earnings week and news out of Europe will likely drive markets in the coming week.

Investors are often guilty of focusing on the short-term to intermediate-term action in the markets. TPI likes to step back and look at the "big picture" or "mega trends" from time to time. The market's so-called "secular" trends are those lasting a decade or two, which is in contrast to the "cyclical" trends usually persisting for periods lasting from a few months up to a couple of years. Since 2000, almost all investors, including TPI, would agree that we've been in the midst of another secular bear phase. The Dow has made some progress, but the S&P 500 and the Nasdaq have not. That means we are over 11 years into the current secular bear phase. TPI believes it may take another two to four years before a secular bull market begins. It is important to remember that we have already gone through two of the worst bear markets in history, as well as a mini-bear market in 2011. So the next secular trend is likely to be up!

Congratulations to the New York Giants for winning a remarkable Super Bowl. There is no doubt, both teams are extremely talented, and they provided a thrilling experience for all football fans. If you have any questions or comments, please do not hesitate to call or email.