401KVentures

OVERVIEW

Economic Analysis and Market Review

Q1 — 2011

This is a Recovery...?

AAAHHH, nothing like the smell of “recovery” in the morning. Government figures for the first quarter would have us believe that economic growth in the United States continues to show signs of improvement. Certainly business confidence measures have moved to multi-year highs, sales levels are rising, profits are improving and business investment remains robust. The economy does give the appearance of transitioning to a self-sustaining phase based on improvements in demand from the consumer sector as well as on corporate top-line growth. But the consumer may not be in a position to contribute much to the recovery in the months ahead. In March, government figures showed that 216,000 new jobs were created; however, another set of figures showed that 290,000 part-time jobs were created. Does that mean that 74,000 full-time jobs were lost? There seems to be a trend in corporate America of going towards more part-time jobs and contractor jobs and fewer full-time jobs due to all the regulations and benefits that must be provided to the full-time employee. This would certainly help the profitability of corporations to the detriment of employees. With part-time work, there is no health care, no paid vacations, no sick leave and perhaps, no raises since there are so many looking for some type of work waiting in the wings. There are 8 million Americans working part-time jobs for “economic reasons”. And the pay is minimal, as well. If 70% of our economy is driven by the consumer, how does this trend translate to a robust economy? And when you couple this with the double digit increases in oil, gas and food prices in the first quarter, the consumer is going to be squeezed pretty hard. A year ago, gasoline prices at the pump were around $2.85 per gallon. Today they are over $3.75 a gallon, a 32% increase. Whereas it used to cost me $45 to fill my tank, it now costs over $65. Food prices have increased at the fastest rate in 36 years. Wal-Mart has already cautioned shoppers to “expect to pay substantially more for food and clothing this year” due to increases in producer costs for commodities such as wheat, sugar, soy and cotton.

Not only is the consumer being squeezed, but the Government, another large part of our economy, is looking to squeeze even more. Congress is currently embroiled in a funding fight over how much to spend on less than one fifth of the Federal budget for the next six months. Whether we cut $33 billion or $61 billion — that is whether we shave 2% or 4% off of this year’s deficit — is important. It’ a sign that the debate has changed in Washington from how much we should spend to how much spending we should cut. As of this writing the House Republican majority has introduced a budget that moves the debate from billions in spending cuts to trillions. If, or when passed, this too will put a crimp in the recovery effort.

The markets are taking a lot of this with ease. The proverbial "wall of worry" has been climbed with seemingly little effort. As the news provided investors with stories of rising oil prices, rising interest rates, rising commodity prices, revolutions in the oil producing regions of North Africa and the Middle East, earthquakes, tsunamis and nuclear fallout, the S&P 500 gained 5.4%. The Russell 2000, an index of small cap stocks, gained almost 8% and the Dow Jones REIT index, an index that tracks the commercial real estate markets, gained 6.7%. And given a scenario of impending rise in inflation, bonds should have fared poorly, but they too gained -.42%. An easy answer to all of this is the Fed's Quantitative Easing or QE2 as it's called. The Fed is pushing roughly $6 billion into the markets every week to fuel the recovery. But this too is expected to end in June. Will the recovery, such as it is, be sustainable in the second half of the year? That remains to be seen. All over the world, central banks are raising interest rates to combat inflation and at some point, our Fed will too. Many believe that the Fed has created every recession in the post WWII years by raising interest rates. Will this happen again? Who knows? We are navigating in one of the most uncertain periods in modern global history.

INDEX	Q1'11	YTD
S&P 500	5.92%	5.92%
Russell 2000	7.94%	7.94%
Europe, Aust., Far East	3.36%	3.36%
Barclays Agg. Bond	0.42%	0.42%
Wilshire Real Estate	6.70%	6.70%
Treasury Bills	0.05%	0.05%

- The S&P 500 is an index of 500 large, well-established companies
- The Russell 2000 is an index of 2000 small companies
- The Europe, Australasia, Far East Index (EAFE) is an index of the developed countries around the world
- Barclays Aggregate Bond Index is an index composed of investment grade bonds
- Wilshire Real Estate Index is an index of commercial real estate properties

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