New Albany
Investment Management

MARKET INSIGHT…

- Performance
- Economic Update
- Charts* of Interest

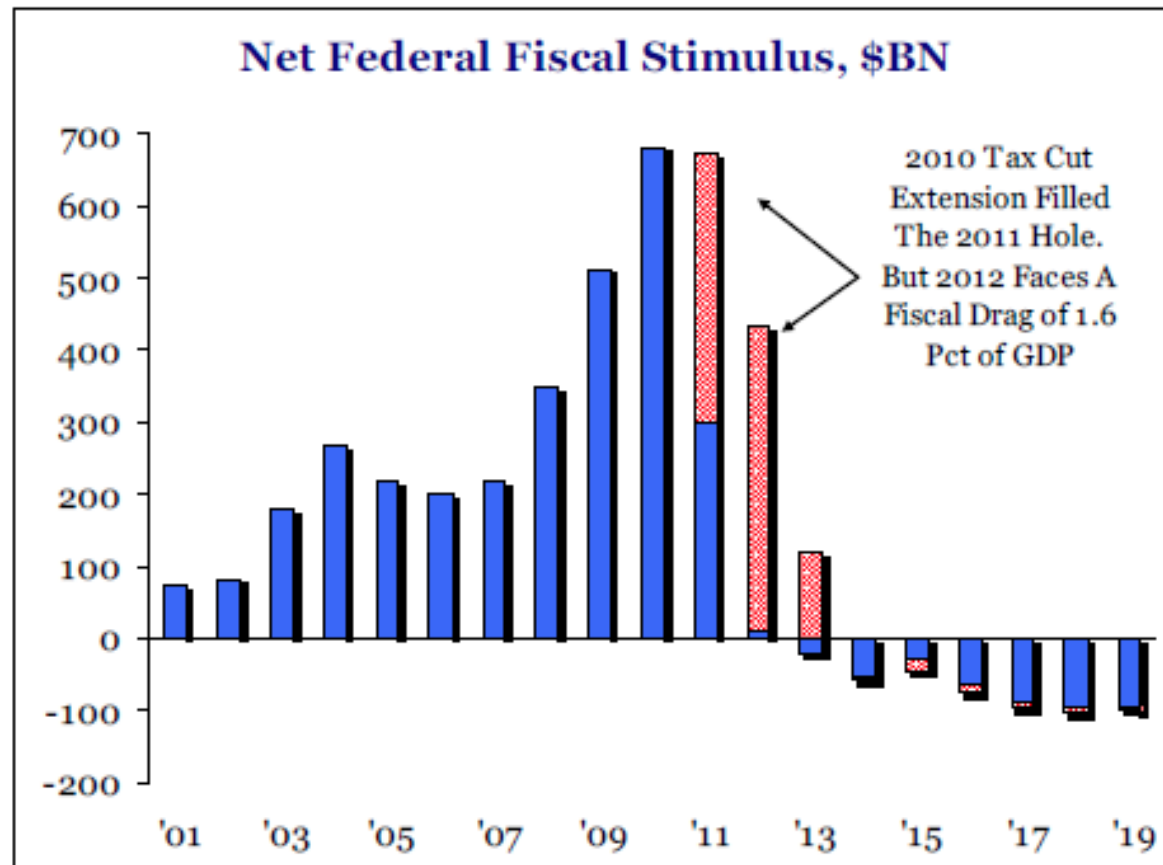*Provided by Strategas Research Partners LLC

August 26, 2011

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# PERFORMANCE: as of 8-25-2011

N A I M

Sector	Week	3Mo	YTD
S&P 500	1.6%	-11.7%	-6.6%
Russell 2000 (small/mid Cap)	1.8%	-17.6%	-13.3%
MSCI EAFE (Eurp. Asia, Far East)	0.0	-18.0%	-9.6%
MSCI Emerging Mkt	4.0%	-9.6%	-11.0%
US Bonds (Barclay's agg. Index)	-0.7%	2.9%	5.6%
High Yield Bonds (US)	-1.0%	-4.7%	0.9%
GLD (Net asset value)	-1.1%	15.8%	25.3%
Real Estate	-0.2%	-10.5%	-1.2%
Energy	1.0%	-3.7%	-14.2%

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Net Federal Fiscal Stimulus, $BN

2010 Tax Cut
Extension Filled
The 2011 Hole.
But 2012 Faces A
Fiscal Drag of 1.6
Pct of GDP

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There's clearly a problem of confidence now not liquidity. The Fed has effectively infinite money because they can print money by creating excess bank reserves. If the economy is lacking confidence and risk taking, it's Congress (after a vote) that we need to look to. **Fiscal policy rather than monetary policy should be in focus.**

Reserve Bank Credit Outstanding

EOP, Mil.$


Source: Federal Reserve Board
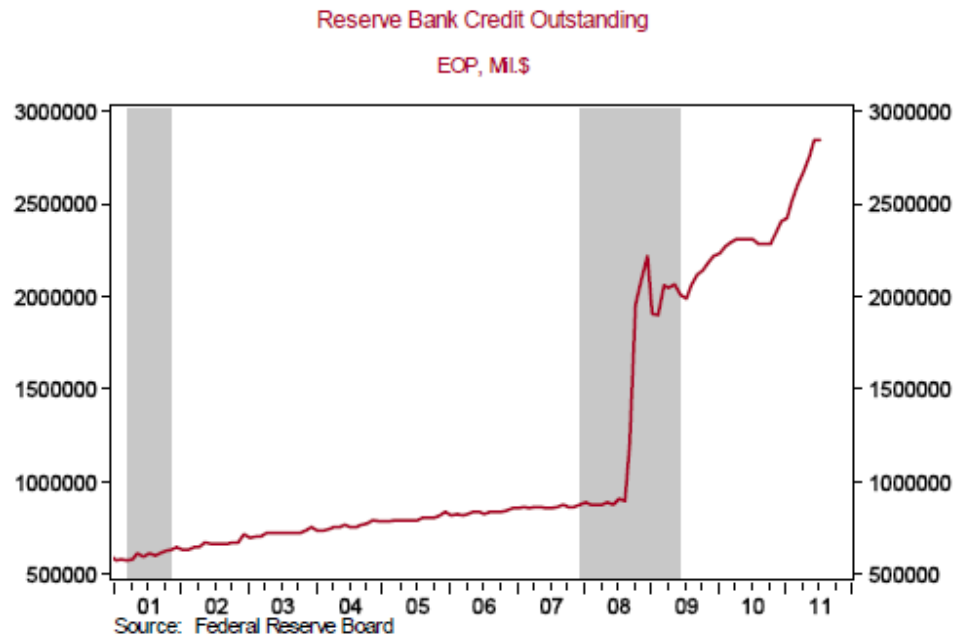
Four Sectors of Economy: 1) households, 2) business, 3) foreign, and 4) government. The past 30 years of the U.S. economy as household-led – that is, real interest rates came down every time the economy weakened (eg, 1985 and 1995) and the household sector leveraged up (mainly using their homes as collateral), supporting growth. **This story is over**, "financial repression" (low real interest rates for a long time) is now the base case.
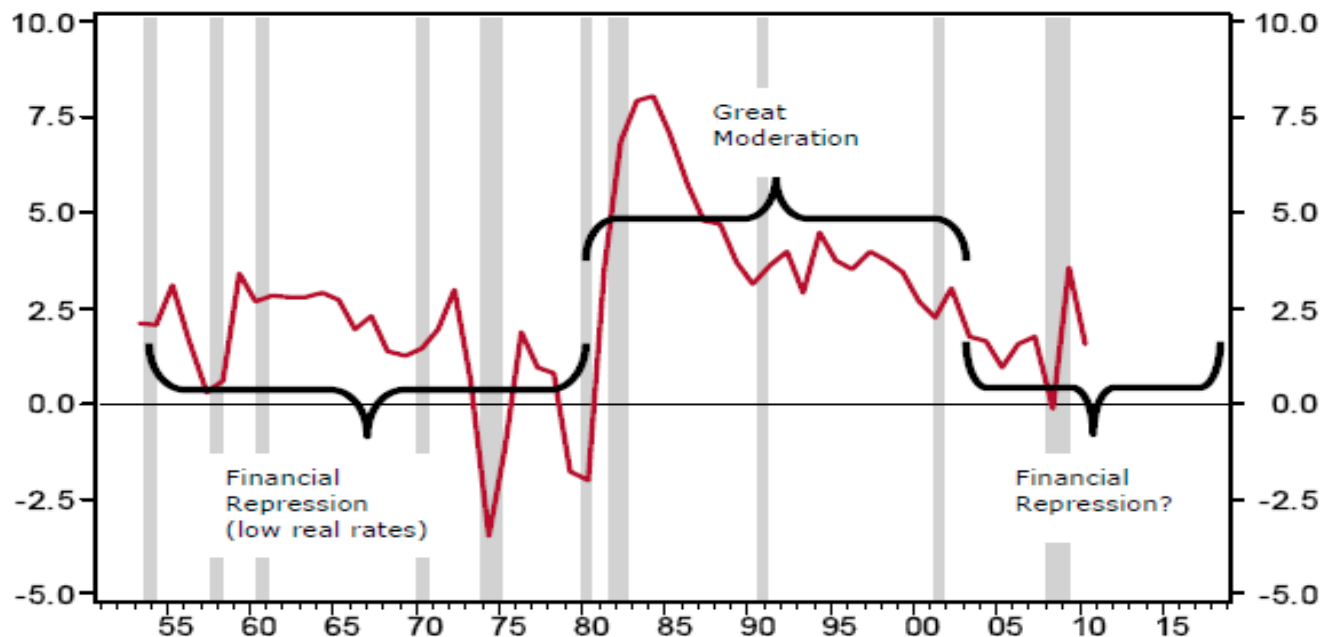
Financial Repression (low real interest rates) should mean that the investment environment going forward may be more similar to the (more volatile) investing environment of the 1950s or 1970s, rather than the "Great Moderation" of the 1980s and 1990s.
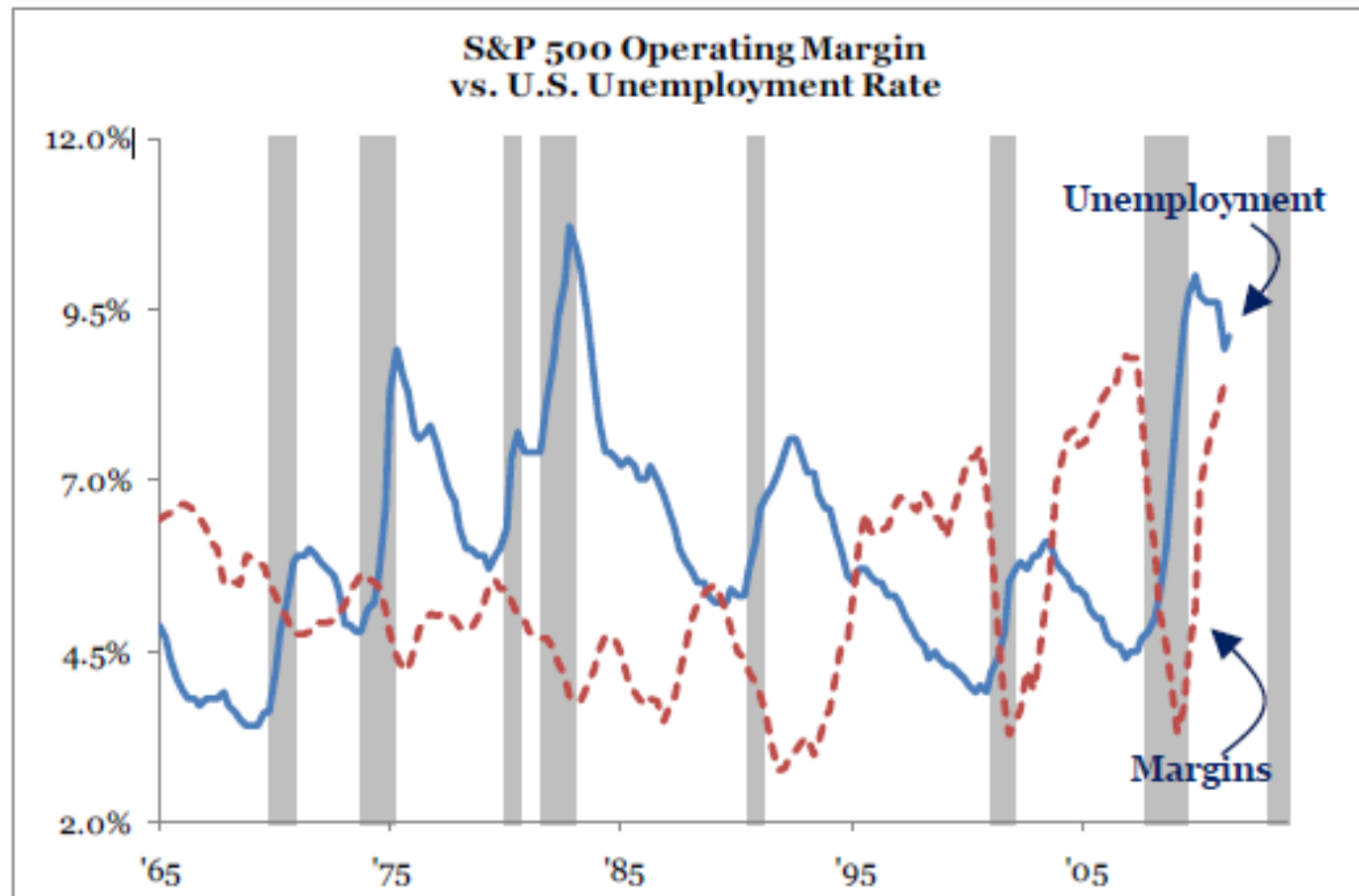
2H '11 earnings will be 'OK', but level of profit expectations for S&P in '12 = $113 and '13 =$126 is very high. Strategas Economic team places a 35% probability on the U.S. moving into recession in 2012 and a 60% likelihood that recession occurs in 2013. One bright spot; there are few credit and inventory excesses to work off, implying a mild recession. Currently, estimating $97 in S&P Operating Earnings for 2012 and $88 for 2013. This -9% drop in profits would be more mild than any recession in the postwar period. Stress-testing for a "normal" recession of a -25% decline would bring the number closer to $73.
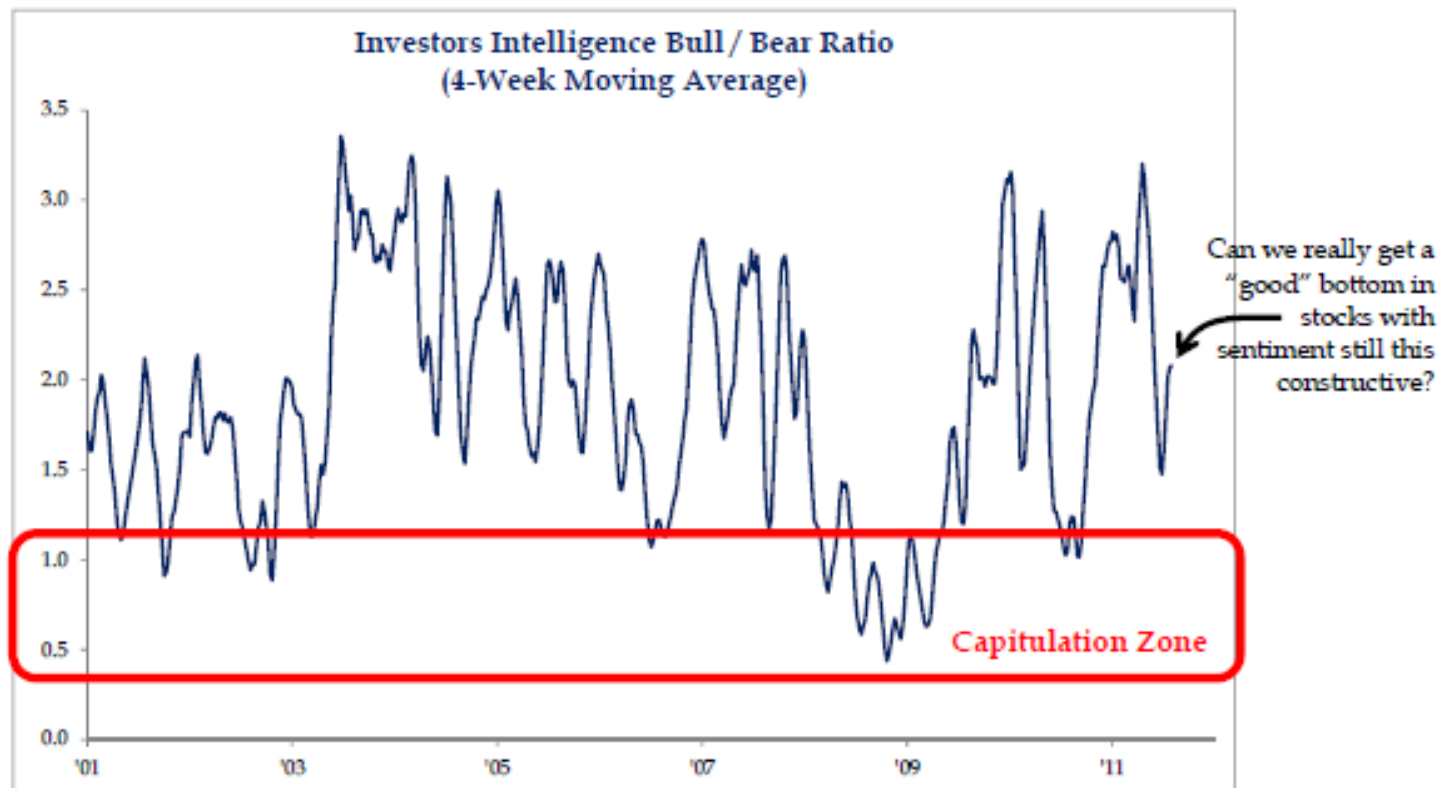

S&P 500 Earnings Per Share
(TTM vs. Historical NTM Est.; CY'12 & '13)
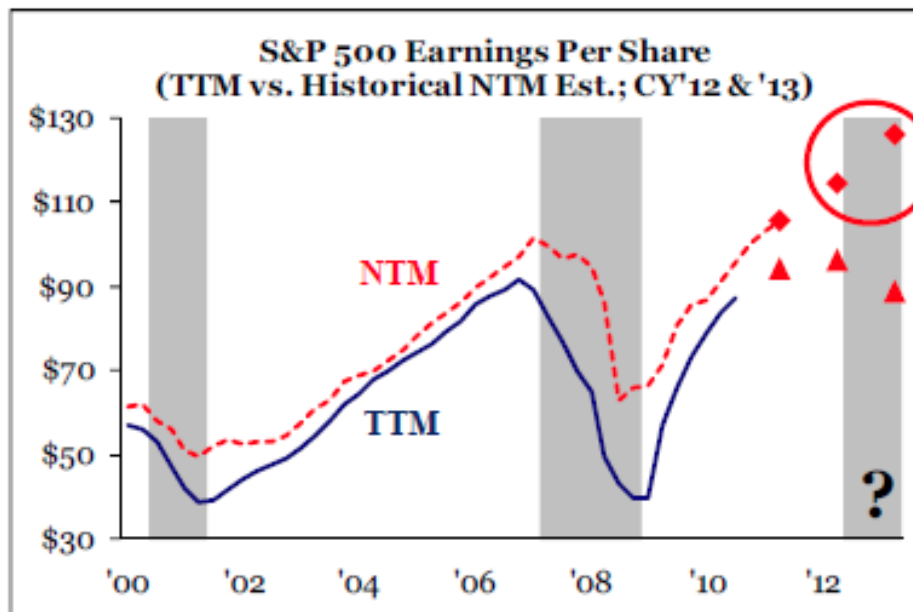
The Street is estimating $113 for '12 and nearly $126 in '13 – those are big numbers.

S&P 500 Operating Margin vs. U.S. Unemployment Rate

WE WOULDN'T CHARACTERIZE SENTIMENT AS CAPITULATIVE, BULLS STILL OUT NUMBER THE BEARS 2 TO 1

Investors Intelligence Bull / Bear Ratio (4-Week Moving Average)

Can we really get a "good" bottom in stocks with sentiment still this constructive?

Capitulation Zone

HIGHER GROWTH WOULD ALLOW 30 YEAR YIELD TO RISE, WITH MORE VOLATILITY FOR 5 AND 10 YEAR YIELDS

Potential Treasury Term Structure Shapes Over Next 12-18 Months

4%+ nominal GDP growth likely leads to a steeper curve.

Lower growth environment of sub 3% nominal GDP growth would likely lead to a flatter curve, with overall rates not much lower than existing rates.
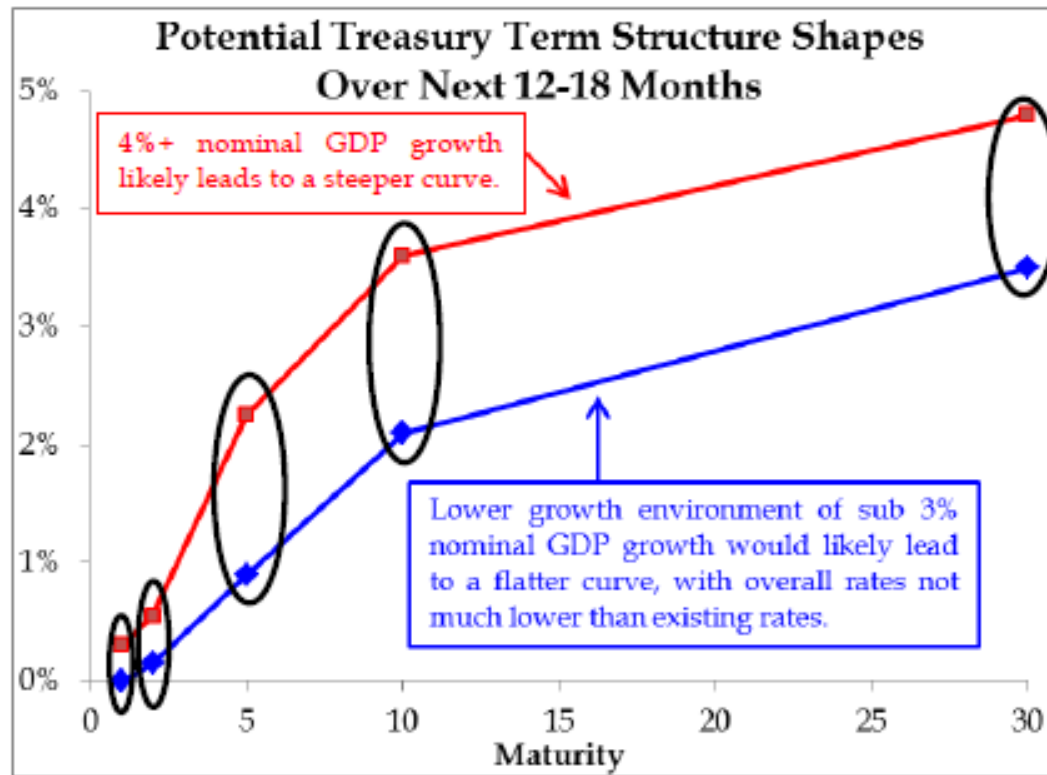
Any uptick in growth would likely have a limited impact on short rates over the next 12-18 months, though 5 year and 10 year yields could swing around violently while 30 year rates edge higher.

Potential Yield Ranges		
Maturity	Low Rate	High Rate
1	0.00%	0.30%
2	0.15%	0.55%
5	0.90%	2.25%
10	2.10%	3.60%
30	3.50%	4.80%

MARKET STRATEGY: Sell Equity Rallies

1) Equities now viewed as source of yield, not appreciation. Look for dividend growers
2) Technology remain relatively strong.
3) Avoid Discretionary and Stocks dependent on Government Spending.
4) Long Precious Metals; Gold & Silver
5) Avoid Energy, Financials, Small caps, Real Estate
6) Bonds: High Quality Corporates should hold up well
7) US Dollar strong against Euro, weak against Asian currencies
8) Global Operators can continue to be profitable
9) Long Volatility