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monthly investment overview.

February 2009

The Economy

US Real Gross Domestic Product for 2008: +1.1%
US Real Gross Domestic Product for 4Q'08: -3.8%
Consumer Price Index Y/Y: +0.0%
Consumer Price Index Dec. 2009: +0.3%

Evidence of worsening economic conditions grew during February. Real GDP in 4Q'08 was revised down to a negative 6.2% annualized rate due to contracting inventory levels, lower consumer spending, and a decline in global trade. Manufacturing activity in the U.S. is contracting at a dramatic pace as evidenced by industrial production declining 12% yr/yr annualized in 4Q'08, the most since 1980. Durable goods orders fell 5.2% in January which will likely lead to another meaningful decline in manufacturing activity during 1Q'09. Consumer confidence plunged to a record low reading of 25.0 in February from 37.4 in January. Unemployment claims pushed higher through mid month, climbing for a 6th consecutive week to a record 5.1 million. Housing continues to search for a bottom as existing home sales fell 5.3% in January to an annualized 4.49 million pace while home prices as measured by the Case-Shiller index declined 18.5% yr/yr through the end of December. Foreign economies have not been immune to the global economic downturn. The Euro zone economy posted a 4Q'08 decline in annualized GDP of 5.9% while Japan's economy shrank at an annualized pace of 12.7% for the same period. The Obama Administration has so far focused on three main initiatives for reigniting economic growth – a $787 billion stimulus bill (passed into law mid-month), a bank rescue plan, and new legislation aimed at stabilizing the housing market. Investors have been critical of these new initiatives mainly due to a lack of details and continued uncertainty over the ultimate magnitude and duration of the ongoing economic decline. The Federal Reserve revised down its forecast for 2009 GDP to a 1.3% decline and also projected that unemployment could rise to 8.8% later this year (up from 7.6% in January). Economists are now pushing out their prior expectations of a 2H GDP recovery into 2010.

The Stock Market

Dow Jones Industrial Average YTD Total Return: -18.9%
Standard & Poor's 500 Index YTD Total Return: -18.2%

News of the government's stimulus package and its proposals aimed at fixing housing and the financial system were greeted by fresh declines in the stock market. Stock market weakness was also fueled by talks of potentially nationalizing large U.S. banks and renewed bailout negotiations with the Detroit auto companies. During February the S&P 500 reached a 50% decline from its October 2007 peak. Financials were the worst performing sector for the month followed closely by industrials. The telecom services and information technology sectors were both down but outperformed relative to the broader index. Investors continue to struggle with an appropriate valuation for the market, as companies cut dividends by a record amount and 2009 GAAP earnings estimates for S&P 500 companies have plunged to $32 from $65 just 6 months ago.

The Bond Market

Federal Funds Rate: Target 0% - ¼%
10-Yr US Treasury Yield: 3.02%
Barclays Intermediate-Term US Gov't Bond Index: YTD -1.4%

Corporate issuers rushed to access the debt market during February. Non-financial investment grade offerings reached a record $63 billion for the month, more than double the $27 billion monthly average for 2008. Treasury yields advanced slightly from last month. Near-term inflation pressures should remain muted due to contracting global economic activity. However, the need to finance the Obama Administration's proposed $3.6 trillion budget for fiscal 2010 (and corresponding $1.75 trillion deficit) is starting to worry bond investors that inflation risks will pick up and interest rates will move higher.