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monthly investment overview.

May 2009

The Economy

US Real Gross Domestic Product for 2008: +1.1%
US Real Gross Domestic Product for 1Q'09: -5.7%
Consumer Price Index Y/Y: -0.7%
Consumer Price Index April 2009: +0.0%

The impact of massive global stimulus efforts has continued to produce signs that the worst of the economic downturn is behind us. Emerging economies have been some of the first areas to see growth return. Retail sales in China jumped 14.8% in April while fixed asset investment rose 33.9% yr/yr, the fastest pace in five years, as government and state banks funded more stimulus projects. In the U.S., progress is clearly being made to stabilize the financial system while many indicators of economic activity are showing a slower rate of decline. Despite these efforts, other indicators, such as the Federal Reserve revising higher its unemployment expectations for 2009 to between 9.2% and 9.6%, are worsening. The U.S. government released the long-awaited stress test results for the 19 U.S. banks with assets of more than $100 billion. 10 banks were ordered to raise $75 billion in new capital and projections found that these banks are susceptible to almost $600 billion in loses if economic conditions worsen. The government also appears to be making good progress with its bankruptcy restructuring of Chrysler. Observers hope the just announced bankruptcy of General Motors will proceed with similar expediency. The latest reading of money borrowed by U.S. consumers showed a much greater than expected $11.1 billion drop, helping the savings rate move back up to 5.7%. With an estimated 22% of homeowners carrying a mortgage balance that is greater than their homes are worth, consumer deleveraging should be a lengthy process. Commodities have surged as economic conditions have stabilized in developed markets and have started to reaccelerate in emerging markets. For example, the price of crude oil has risen 21% this year to $66 a barrel. Higher commodity prices, combined with a sharp rise in interest rates, could ignite inflation and risk tempering the economic recovery. However, the core personal consumption expenditures price index rose just 1.9% yr/yr in April, remaining within the Federal Reserve's comfort zone. Still, the U.S. dollar appears headed lower after a 6.5% decline in May. While a declining U.S. dollar could also lead to inflation, it should be a welcome boost for U.S. multinational companies and export manufacturers.

The Stock Market

Dow Jones Industrial Average YTD Total Return: -1.6%
Standard & Poor's 500 Index YTD Total Return: -3.0%

Taking advantage of the strong advance in the stock market, companies rushed to raise fresh capital, making May the busiest month ever for secondary equity offerings. During the 1Q earnings reporting season, analysts significantly lowered their forecasts, taking estimates for 2009 and 2010 S&P 500 earnings down by roughly 26% and 20%, respectively. The strong market advance indicates that investors have already discounted these downward earnings revisions and are now looking for an improvement in economic conditions later in 2009. Energy stocks joined financial stocks to lead the market (S&P 500) higher by 5.6% in May. Industrial, information technology, and consumer discretionary stocks underperformed during the month.

The Bond Market

Federal Funds Rate: Target 0% - ¼%
10-Yr US Treasury Yield: 3.46%
Barclays Intermediate-Term US Gov't Bond Index: YTD +1.2%

U.S. Treasuries staged a sharp decline in the last week of May, with yields shooting up to 3.74% before settling back to end the month at 3.46%. It is still too early to tell if the move in the Treasury market is in response to improving growth prospects or worries over ballooning government debt / deficits. Finally, in a setback for the housing market, the national average rate on 30 year mortgages jumped to near 5.30% at the end of May from 4.90% a month earlier.