

# BEACON INVESTMENT MANAGEMENT

## THE FRIDAY BRIEF

*Distributed to our clients and friends weekly*

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### Dare to Believe?

For markets, the worst of the credit crisis may be over. Investors' uncertainty over the size of financial institutions' losses took stock prices below reasonable valuations as is typical when information is scarce. While the effects will last considerably longer for people directly impacted and for the economy as a whole, markets are indicating that knowledge is sufficiently filling the void. Citigroup, Merrill Lynch, JP Morgan, Washington Mutual, and Wachovia's shares are all moving significantly higher after reporting huge losses due to credit write downs. The S&P is up 10% since its low on March 17<sup>th</sup> and the dollar rose the most against the euro in more than two weeks on Citigroup's news. Perhaps investors are saying that the nearly \$250 billion in financial losses reported so far represent the majority of the ultimate total.

Bloomberg's Professional Global Confidence Index rose from 13.1 to 14.5 in March indicating a renewed confidence in the world economy. The index which consists of the collated responses of 5,900 business professionals all over the world who use the business data service provides a unique mix of global investors who invest their own money and that of clients. Their views are at least as important as the opinions of economists and strategists delivering projections for pay.

Earnings outside of the financial industry are coming in much stronger than anticipated. Earlier in the week Intel set the tone for a technology rally followed by IBM which posted a 26% jump in first-quarter. As the largest information services provider their results boost confidence that corporate spending, especially overseas, may support a deteriorating U.S. economic picture. And Google today quieted fears that the economy has hurt its business.

The dollar's drop has also helped. Companies like Coca-Cola Co., IBM and Google which do considerable business outside the US are helped as their goods and services, priced in dollars become cheaper. The dollar declined 6.4% against a basket of currencies in the first quarter of this year.

Caterpillar, the world's largest maker of bulldozers and excavators, reported that its first quarter profit rose 13%, beating estimates. Asia and other overseas markets more than compensated for slower growth at home.

Amdocs, the world's largest billing and customer service software company gained 10% on their earnings report which exceeded analysts' estimates. Manpower, the world's second largest employment services provider climbed the most since October 2002, gaining 14% on analyst-beating earnings.

Tom Lauricella in today's Wall Street Journal highlights the dichotomy evident in first quarter earnings reports. He notes the obvious impact of falling home prices and

tightening credit on banks and companies selling directly to consumers. But in stark comparison, many big businesses, especially those that sell to other US companies or to abroad, are proving resilient.

So far this reporting season, about 20% of S&P 500 companies have reported. Those earnings are down 22.1%, according to Brown Brothers Harriman. Excluding financials though, earnings are up by 8.2%. The Wall Street Journal notes that if the actual reported earnings are combined with estimates for the remaining companies, the results are slightly ahead of analysts' expectations, which is for a 12.9% decline. Excluding financials, actual plus projected earnings are up a healthy 9.5%.

While the current earnings trend is good, suggesting a shallow and short recession, the question remains whether the housing market slowdown will further drag down the broader economy. Consumer spending at two thirds of the economy remains the biggest of unknowns. There are no actual signs that the consumer is going to pull away completely. But, given record gasoline prices, tight credit, and falling home prices, the possibility certainly exists. We are keeping a close eye on how the US consumer reacts to today's challenges as a primary indicator for our tactical decisions and allocations.

Have a good weekend.