



Friday, January 29, 2010

**“Steady! Helmsman, Steady. Nay, Nay! Up helm again!”** Captain Ahab in *Moby Dick*

Approaching President Obama’s Wednesday state of the union address, many expected he would steer a new direction, away from a decidedly liberal agenda toward the center. He obliged with more than a few promises on how he would do just that. He took a clearly more populist/centrist tone, berating bankers, rebuking congressmen and senators for partisan bickering, reminding critics of his many “tax cuts,” and doing it all in his own version of “I feel your pain.” He even nodded to the right on initiatives such as nuclear power and offshore drilling. He urged Congress to pass a new jobs bill, called for the extension of a big business tax break, and the creation of a small business tax credit. In a follow-through today, it is reported that the president plans to propose tripling loan guarantees for new nuclear reactors to more than \$54 billion.

Dare we hope our president has indeed changed course? It can be done. Bill Clinton did so very effectively after his/Hillary’s health care reform failed to gain traction and as a result he governed more effectively. But based on the evidence of the past year, it is difficult to envision such a course change is likely for this administration and congress.

At the core of Barack Obama’s message is an undeniable ideology. He made it clear Wednesday night that he still has the intention of passing major healthcare and clean air reforms, despite political warnings. During closed-door congressional sessions with the president secretly hammering out a bill that could pass, I was reminded of a monomaniacal sea captain who sailed from New Bedford, Massachusetts. He was bent on an epic quest, without regard to cost; to kill the great white whale. Along his journey captain Ahab received dire warnings from three ships, the *Samuel Enderby*, the *Rachel*, and the *Delight* to discourage him, but alas he could not and would not be turned. Is the president really undaunted by the political warnings of New Jersey, Virginia, and Massachusetts or will he turn?

While ideology stirs passions, pragmatism gets the job done. Americans want Washington to work for them; to cooperate and to fix the significant problems facing this nation’s economy. Mr. Obama said “we have more than a deficit of dollars right now we face a deficit of trust.” Much will happen between now and November when voters will answer the political question of ‘trust,’ but more pressing right now is how business owners, managers, investors, and bankers ‘trust’ his message. We have an economy in recovery.

The president’s tongue-lashing of bankers, while appealing to Main Street, only adds to the uncertainty on Wall Street. The Administration’s thinking out loud regarding regulatory issues, taxes and levies, equity, and reserve and capital requirements breeds uncertainty and potentially a retreat of risk-taking. We don’t need for bankers to rein in their lending any further as this economy struggles to recover. Everyone expects tighter regulations as a result of 2008, but they should be responsible, appropriate, and globally coordinated in order to avoid crippling this fledgling expansion.

Today the government announced that the US economy expanded in the fourth quarter at 5.7%, the fastest pace in six years. According to the Commerce Department it marked the best performance since the third quarter of 2003. The report showed that 3.4% of the growth came from the rebuild of depleted inventories. While the news is good, inventory rebuilds do not guarantee sustained growth, nor do they suggest that companies are more confident in the recovery. The best indicators of rising company confidence will come in the form of meaningful declines in unemployment.

Following their meeting this week, Fed policy makers said that "the deterioration in the labor market is abating" but that consumer spending is still being "constrained" by an absence of job creation. They repeated their pledge to keep the benchmark interest rate low for an "extended period" with one dissenting vote on that part of their statement.

The president said he wanted a jobs bill on his desk as soon as possible, but gave few specifics on what he was looking for. His offer to keep tax breaks of \$38 billion in place was a nice gesture, but his promise to raise taxes on those making more than \$250,000 sounds more like Ahab as it espouses ideology when we need pragmatic solutions.

Of the people who make more than \$250,000 in this country, a full 60% of them are small business owners, operators, and investors, according to a 2007 US Treasury study. The study found that almost half of the income taxed at the highest rate is small business income representing more than 500,000 sole proprietorships and subchapter S corporations whose owners pay at the individual tax rate. Please Mr. President, let that whale go.

The senate voted 70 to 30 yesterday to confirm Ben Bernanke as Chairman of the Federal Reserve. Stocks rallied as it became clear he would be confirmed. In response to the vote and a growing congressional desire to rein in the Fed's powers, Senator Charles Schumer (D) of New York today criticized efforts to control Fed, saying: "If you don't like monetary policy when the Fed does it just wait until the politicians get their hands on it." Now, there's a pragmatic voice of reason from the left.

The housing market took a decidedly negative turn in December as existing home sales plunged 16.7%, the largest monthly decline since 1968. With the expiration of November's first-round buyer credits, new home sales fell 7.6% to an annual sales rate of 342,000 units. Supply on the market rose to 8.1 months vs. November's 7.6 months.

The Mortgage Bankers Association's refinancing index fell 15.1% in the Jan. 22 week, leading the MBA to issue a rare comment in their text: "Although rates remain low, there appears to be a smaller pool of borrowers who are willing to refinance at today's rates." The average 30-year mortgage rate edged 2 basis points higher in the week to 5.02%. MBA's purchase index fell 3.3%.

But there was good news in home prices. The Federal Housing Finance Agency's monthly House Price Index showed a .7% increase in November. The Case-Shiller Index showed a .2% increase

in November. The new home sales report further confirmed the trend by reporting that the median price of new homes rose 5.2% to \$231,000 while the average price rose 7.6% to \$290,600. The year-on-year rate for the average price is actually up 10.5%.

Consumer confidence bounced in January to 55.9 from 53.6 in December, and the assessment of current conditions remains near historic lows though improving a considerable 5 points. But, consumers have a brighter outlook of the future as expectations jumped another 7 tenths to 76.5. A reading of 80 is widely considered to be a signal of economic health, according to Bloomberg.

The report also shows that the consumers assess the present jobs market as very weak but the reading has improved for three straight months. Those saying jobs are hard to get fell 7 tenths to 47.4% vs. 48.1% in December and 49.2% in November. The reading hit a cycle peak of 49.4% in October as reported by Bloomberg.

The stock market is off its peak by almost 6% on continuing high unemployment and few signs of reversal, bad news on housing, a downgrade of Greece's credit rating, the failure of corporate earnings to surprise big on the upside, and some creeping concern over the health of the recovery.

But despite recent stock declines, sentiment among institutional investors remains little changed in January, according to State Street's sentiment index. The index shows North American investors are the most confident, with a marginal willingness to take risk. European and Asian investors are slightly less confident, tilting toward safety. The index measures confidence directly by assessing the changes in investor holdings of equities. The more investors place in equities, the greater their confidence.

Of course, we point out that the only *confidence* that matters most in investing is the *confidence* that *you* have in meeting *your* goals. Are you confident? We can help.

Captain Ahab and all the souls aboard, save one to tell the tale, perished when the mighty white whale did violently sink the *Pequod*.

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