

## Weekly Update: Talk is cheap

As of 09-09-2011

**There was a lot of talk about jobs and the economy Thursday** In a speech to Congress Thursday night, President Obama unveiled his \$477 billion job creation package. Obama urged congress to pass his new American jobs act 17 times his 30-minute speech. The plan proposes to halve the payroll taxes (on the first \$5 million in wages) for 98% of businesses and extend the payroll tax holiday, increasing it from 2% to 3.1%. Unfortunately, Obama's plan is similar to the 2009 stimulus, with more than half of the stimulus coming from spending increases, making the prospects of passage in a GOP House unlikely. Also, the 2009 plan passed in the context of a deep recession and with a Democratic majority in both houses of Congress; no House Republicans voted for that plan. This new plan also has an additional feature that is repugnant to Republicans: the deficit increase in the near term is offset by future tax increases. Most of these proposals have been raised before, and increasing taxes on the wealthy is a non-starter. Hmm.

**Fed chairman Ben Bernanke had words of his own** In Minnesota on Thursday, Bernanke's speech offered no specifics on future stimulus. Bernanke's speech was essentially a carbon copy of the one he gave in Jackson Hole and the last FOMC statement. He sees weak growth, moderating inflation and is worried about fiscal tightening. He said that the Fed is prepared to employ "tools as appropriate to promote a stronger economic recovery in a context of price stability." Equities expected a more explicit list of policy options or an indication of monetary accommodation beyond duration extension. They got neither. Miller-Tabak notes that since Bernanke took office in February 2006, the purchasing power of the U.S. dollar is down 12%. And since his predecessor Alan Greenspan began his term in June 1987, it's down by 50%. Yet in questioning Thursday, Bernanke said the Fed "has achieved and maintained a very good record of low and stable inflation, which means stable purchasing power of the U.S. dollar." Hmm.

**Jean-Claude Trichet is not amused** The European Central Bank President, also on Thursday, was irritated when asked whether Germany should return to the Deutsche Mark, the official currency of Germany prior to the Euro. Trichet's response: "I would very much like to hear congratulations for an institution which has delivered price stability in Germany over almost 13 years at 1.55 percent approximately...which is better than has been obtained in this country in the last 50 years." Ouch! As we mark the 10-year anniversary of the 9/11 tragedy, our thoughts are with family and friends of those who perished, not to mention those who, in the response to the attack, demonstrated resolve and a resiliency of the human spirit. Do you remember the infamous words of Flight 93 passenger and hero Todd Beamer, who encouraged his fellow patriots, "Let's Roll!?" Now there was some talk that really mattered.

### Positives

**Manufacturing surprises to upside** The ISM non-manufacturing index rose in August, compared to consensus expectations of a decline. This is consistent with modest activity growth and far from the alarming weakness in the Philly fed and some measures of consumer confidence. Unfortunately, the employment index within the report was the weakest since September 2010. Still, most non-sentiment indicators in the economy have not significantly tumbled following the financial turmoil in late July and early August. Additionally, the Fed's Beige Book showed that growth slowed in several districts, but overall economic growth continued "at a modest pace."

**Trade deficit narrows** Ned David Research tells us that in July, the trade deficit narrowed by the most since February 2009, beating expectations, as exports saw the sixth-largest gain on record, led by fuel and autos. Real goods exports surged the most since August 1994. If the deficit remains consistent for the rest of the quarter, trade could contribute positively to third quarter growth.

**Credit expands** Barclays says U.S. consumer credit increased more than expected in July. Gains were concentrated in the non-revolving component, likely reflecting improvements in auto sales following the mid-summer disruptions stemming from the Japanese earthquake. The gain was the largest, in dollar terms, in more than six years. The report was positive, and suggests that the rebound in the auto sector is continuing as expected.

### Negatives

**Consumer sentiment plummets** The Conference Board Consumer Confidence Index currently sits at just under 60. (By the way, no president has been reelected with confidence below 90). After a tumultuous summer, consumer spending on big-ticket items like homes, autos and durable goods is at one of the lowest points ever, and very little borrowing has occurred in more than three years. Additionally, the weekly Bloomberg consumer comfort index fell to its second lowest level this year last week. Confidence worsened across all income groups, reaching a record low among low-income consumers.

**Signals of a global slowdown** We're seeing indicators of global slowdown worldwide. Also, Australia's manufacturing index fell in August to the lowest level since July 2009. Manufacturing indices in the euro area, Korea, the U.K. , Sweden and Taiwan are all indicating contraction. And Canada's GDP dropped in the second quarter for the first time in two years. The good news is that the weakness is leading more central banks to ease, including Brazil's and Turkey's. Mexico indicated that it may lower its rate. The Bank of England held off raising rates, even though inflation is running at twice the 2% target. And the European Central Bank appears ready to halt its policy tightening.

**No appetite for risk** Stocks continue to be sold indiscriminately as evidenced by the record-high reading in 60-day correlation, which is a bear market trait. Credit Suisse says the current divergence between global industrial production growth and risk appetite is the widest ever recorded. Their measure of global risk appetite is only marginally above all-time lows. The market seems to fear another Lehman-like collapse in output. We expect the S&P to test its early August low.

## What else

**Equity valuations in historical context** The 12-session plunge from S&P 1350 on July 22 to 1101 on Aug. 9 (-18%) was capitulatory in nature and the market achieved "price discovery" during that plunge. The price-to-earnings ratio of the market (11 times the latest quarter's earnings annualized) is now six points lower than the 10-year average. The real trailing earnings yield exceeds 6% (exceeding that seen in the spring of 2009 and close to that in July 1982), a level that has more often than not, preceded strong equity returns.

**Gold sparkles in September** Historically, the month of September has had extremely high volatility with equities suffering their worst returns of the year, while gold witnesses its best average monthly return. In a Gallup poll conducted in mid-August, 34% of those surveyed rated gold as the best long-term investment, double the confidence in stocks, and more than triple the sentiment for bonds. And given current valuations, the price of gold could correct to \$1450 and still be in a sustained advance.

**Someone has read that healthcare bill** The Obama health care bill contains a provision that instructs the Health and Human Services secretary to standardize chain restaurant menus, recipes, serving sizes, methods of preparation and training of food service workers. By 2014, there will be a food police division.



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## Recent Global Equity

### **Orlando's Outlook: Hunker down until conditions improve**

Sep 06, 2011 :: Philip J. Orlando

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### **Orlando's Outlook: It was a terrible, horrible, no good, very bad jobs report**

Sep 02, 2011 :: Philip J. Orlando

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### **Weekly Update: Were you planning to watch the GOP debate or the football game?**

Sep 02, 2011 :: Linda A. Duessel

Views are as of the date above and are subject to change based on market conditions and other factors. These views should not be construed as a recommendation for any specific security or sector.

The Institute of Supply Management (ISM) nonmanufacturing index is a composite, forward-looking index derived from a monthly survey of U.S. businesses.

The Conference Board's Consumer Confidence Index measures how optimistic or pessimistic consumers are about the economy.

S&P 500 Index: An unmanaged capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Indexes are unmanaged and investments cannot be made in an index.

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