

**March 30 2011 Steven F. Mosshart AIF® Chief Investment Strategist**

## ***There are times to just let things happen***

### ***2011 Year to Date Market Performance\****

***S&P 500  
4.64%***

***Dow Jones  
5.99%***

***NASDAQ  
3.13%***

***MSCI EAFE  
2.49%***

***BarCap US  
Aggregate Bond  
0.38%***

***Morningstar  
Large Cap Core  
3.86%***

***Morningstar Mid  
Cap Core  
6.74%***

***Morningstar  
Small Cap Core  
6.98%***

*\*Market Data supplied  
by Morningstar  
3/28/11. All returns  
are with dividends  
reinvested.*

I think this is the first time in the last eight years of writing these newsletters that my advice will be to just sit back and enjoy the weather that will (hopefully) arrive very soon and also just let the portfolios we have constructed do their jobs. Those of us that are a bit longer in the tooth already understand that seasons go by more quickly every year and that the greatest or most relaxing moments are those where we get the chance to enjoy what we have worked so hard to prepare for – it doesn't happen very often it seems.

### **Japan, Middle East, and QE3**

**Japan** - The stock market declines subsequent to the terrible events in Japan were expected as there's always a negative market reaction to natural disasters. That said the down draft is usually short lived and the typical recovery takes 30 days because there is an almost immediate recovery effort.

From a numbers standpoint Japan is the third largest economy relative to GDP making up about 9% of the world's economy. Additionally the area affected by the disaster accounts for only 4% of Japan's output so in terms of global impact it is less than .5%. It is my view that the global economy is on the road to recovery and will not be derailed by these recent events.

**Middle East** – This is always a difficult study because every upheaval in an oil producing nation causes higher prices. Even if we didn't purchase oil from the Middle East, unrest would affect prices. Here is a brief overview:

- Currently the disruption of the flow of oil has been relatively limited – the concern is whether it will get any worse. The world's demand has steadily increased and the addition of unrest has caused an already tight market to be excessively priced. That said there is no rationale for \$5 per gallon.
- Most of our oil imports come from Canada, Mexico, and Venezuela. We get very little from Libya and Saudi Arabia accounts for less than 10% of our imports. Even though that is the case - a disruption is a disruption and will continue to negatively affect prices.
- A full scale revolution in Saudi Arabia would most likely cause a short disruption – a new government would need to have money and they are also the only country that has any significant unused capacity.

**QE3** – I put the odds of QE 3 at 50/50 because it is a split between letting the well thought out plans of the past play out and providing one more shot in the arm to the economy. The economy has been steadily, albeit very slowly, improving and the reason for the QE's were to make sure there was enough liquidity to pull the economy out of the terrible hole it was in. It has done its job but at some point it has to be left alone.

QE2 ends in June and for now we will have to wait until Bernanke's scheduled 4/23 press conference. If there is a QE3 then the market will get a boost because there will again be a renewed sense of liquidity – if not then we may have a bit more muted returns for equities through the end of the year. This uncertainty in the direction of the Fed dramatically drives home the importance of diversification.

### **Investing Overview**

The inflation rate is currently just a touch over 2.1% and is not expected to do anything but creep up slowly. I believe inflation will stay at the low end (below 4%) for quite a while because of the following factors:

- The Global Economy is strengthening which allows for more competition and lower overall pricing
- Despite the recent rise in prices the US is largely a service economy and until there are substantive wage increases inflation will remain in check
- Corporations have improved productivity with less expenses (more efficient) and will not have major increases in spending

Equities are usually the investment of choice in low inflationary environments. Typically the S&P 500 growth rate averages 9% when the inflation rate is between 1% - 4%. I do not expect the 4% barrier to be breached for quite some time.

We have made adjustments to take advantage of the current economic situation by increasing our exposure to dividend paying stocks and reducing our positions in commodities and high yield securities. As I have stated in the past, the key to staying a bit ahead of the markets is to be prepared for both the areas that will outperform and staying away from those that will under perform. Have a great Spring!