Economic & Market

Commentary

The Millennium in Review

not such a Stellar year

2000 was one of the more difficult years investors have encountered in quite a while. It started with fears of runaway inflation and ended with fears of recession…and the markets reacted accordingly. While the equity market performance of the last six months is still fresh in the minds of many (as the markets concerns have shifted from inflation to recession), many have forgotten how poorly bonds performed throughout 1999 and in the early part of 2000 as the markets feared inflation. We saw through the illusion of inflation and, given the monetary and fiscal policy we expect, believe we will avoid a recession. Long-term views are sometimes tough to adhere to when markets focus on short-term issues. *We believe that proper action by the Federal Reserve should alleviate concerns regarding the economy, and that the financial markets should react accordingly.*

Should we fear inflation, recession… or both? We believe an economic slowdown produces far greater problems than modest inflation, and we believe Federal Reserve Chairman, Alan Greenspan shares this belief. Without economic growth, it is likely that our government would spend more money than it earns, and would not continue to produce a budget surplus. If that happened, the United States would have to borrow money to make up the difference. A slow, or no growth nation with growing deficits (budget and trade) would find it hard to attract investors willing to finance these deficits. This would likely result in a declining dollar which would increase the chance of importing inflation as the price of imported goods rises as our dollar falls. If these events were to transpire, the Pandora's box of the 70's (stagflation) could be reopened. *We do not believe that is on the horizon, and have maintained asset allocations in accordance with that belief.*

Just as the fears of inflation peaked in March of this year, we believe that fears of recession are currently peaking. The expectation of a slowing economy has caused many analysts to lower earnings expectations for a number of companies by a factor related to the expected slowdown in the economy. As expected, many of the high-flying technology stocks have come back to earth, but have dragged other good companies down with them. While we own technology stocks, we focused on larger companies, and used a broad asset allocation strategy to help reduce risk. With the major stock markets posting negative results (Dow Jones Industrial Average down close to 5%, S&P 500 down over 9%, NASDAQ down over 39%, Dow Jones World Stock Index down over 17%) and the Salomon Broad Investment-Grade Bond Index posting close to a 9% gain, client accounts have performed quite well comparatively.

With the expectation that the Federal Reserve's policies will work in concert with the incoming administration's policies, we plan to stay the course with client portfolios. We understand that times like these can be stressful, and believe that this is the correct long-term decision. As always, if you have any questions regarding our outlook on the markets, or portfolio strategies, just call.

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