

Global Market Swoon

August 5, 2011

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Global stock markets declined sharply this week as a confluence of fears battered investor confidence around the world. The sell-off puts U.S. markets into the red for 2011 and more than 10% below their April highs.

So what's changed in the past few weeks to unsettle investors? There are four major factors contributing to the worsening investor sentiment.

First, the ugly fight over raising the U.S. debt ceiling has damaged business confidence not only here, but also around the world. The fracas that left the U.S. government within hours of a potential default has demonstrated to both Americans and foreigners alike our government's state of near paralysis. It has undermined faith that the federal government will be able to reach future agreements about how it can best aid the economy and how it can best create an environment that encourages companies to hire more workers.

Second, there is a creeping realization that the federal government is simply out of ammunition to help the economy. Additional fiscal stimulus appears to be unlikely at least through the 2012 election and the Federal Reserve already has its gas pedal to the floor (in the form of 0% interest rates). Will the Fed take additional measures to try to stimulate growth? Perhaps, but another round of quantitative easing is unlikely to have a lasting salubrious effect on the economy.

Third, the continuing inability of the Europeans to find a durable and sustainable plan for addressing their debt crisis has caused many global investors to head for safer ground. On Friday, the European Central Bank announced that under certain conditions it was prepared to begin buying Italian and Spanish government bonds in the open market. While this tactic may placate markets in the very near term, Europe has a long way to go before it can be sure that it has fully contained its debt crisis.

Fourth, at the end of July the U.S. Bureau of Economic Analysis (BEA) revised downward its estimates of economic growth in the first half of the year, leading many investors to wonder if the economy is about to slow further. The revised numbers showed that the 2007-09 recession was deeper than initially reported and that the recovery, thus far, has been weaker than previously estimated. All in all, investors have garnered little comfort from recent economic data.

This abrupt turn in confidence has, unfortunately, overshadowed the second quarter U.S. corporate earnings season—which so far has been excellent. U.S. companies are making

strong profits, maintaining high profit margins and have strengthened their balance sheets significantly. They are lean, efficient and have the wherewithal to invest in their futures. But the shenanigans in Washington and the bad news out of Europe have frustrated Corporate America deeply, and this exasperation is readily evident in the voices of executives as they report their companies' financial results and make projections about the increasingly cloudy future.

What the markets need now is simply for policymakers in both Europe and the U.S. to convince investors that they are up to the task of decisively addressing our economic challenges.

As always, please do not hesitate to call if you would like to discuss the economy, the markets or your account.

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