

A THOUGHT FOR THIS YEAR

WEB BUZZ 2012.01.03

Will 2012 be, as the consensus of Wall Street economists predicts, a year of moderate growth (2-2.5%) or will it be the year of financial blowup? Of course no one knows for sure. Maybe it will just be another year of kicking the debt can down the road - the old extend and pretend game the political class plays so well.

As we look back on others' predictions for last year, we must say that most were wrong. For example, the consensus called for a 2011 year-end number of 1,373 for the S&P 500 (9% growth) and 4% year-end yield for the 10-year government. Both clearly missed by a large margin. The various stock indices are fighting to break even and the 10-year government is around 2%. The old bugaboo of inflation that worried most market participants seems no longer to be a major concern. The general belief was that inflation was going to skyrocket in 2011, but that never came to pass. Now most believe it will only come in around 2% for 2012. We think it will be closer to 0%.

As we view the new year we see nearly all economic groups in the world slowing. All seem destined to be at stall speed and some, if not all, will probably fall into recession. The tremendous overhang of debt is not going away and unfortunately is being added to in huge amounts by the various sovereign countries. Month by month the rating agencies keep downgrading the European banks and countries. We imagine the U.S. will also receive a downgrade in 2012 along with some of our too big to fail Wall Street banks.

As you know, it has been our opinion that our most likely economic and market outlook will be much of what we have seen in Japan. The major difference was in which sector was most overleveraged. In Japan it was the corporate sector and in our case the consumer. This being the case, our common stock market might have more investment opportunities than theirs. We would hate to think our stock market will perform as poorly as Japan's has. If you recall, it's been twenty plus years since the

high was made in their market. On the other hand, their long government is around 1% and we might just reach that before it's all over.

One of the quarterly economic numbers that is seldom reported in the business news is real gross domestic income. It is somewhat similar to real GDP and, as a matter of fact, they tend to converge over time. Please note the following four quarter trend - +3.5%, +2.6%, +1.7%, and the latest +1.1%. If this trend continues or even just flattens out, 2012 will most likely be a recession year. As you recall, the consumer is approximately 70% of GDP. One of these days we may be able to project good times ahead, but this isn't one of them.