THE DANA VIEWPOINT

DEBUNKING A FEW MYTHS

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Myth #1: Manufacturing in the US is declining at a rapid pace. Not so says none other than Fed Chairman Ben Bernanke. In recent remarks to Congress, Bernanke said that manufacturing in this country has not declined as severely as some would have us believe. Instead, productivity gains have resulted in net decreases in employment in the manufacturing sector. In addition, most of this loss has come in light manufacturing – toys, clothes and small electronic devices. Gains are being made in heavy manufacturing industries – those that produce machinery for others. China does not have the skilled labor force necessary to produce this type of equipment, and Japan keeps building factories here to take advantage of our skilled labor. Japan's population keeps aging and shrinking so look for them to continue to build plants here.

Myth #2: The sell off in the housing and automobile markets will lead us into a recession. Yes, we have seen excesses in both these markets and a cooling-off period is necessary to work off inventories that have built up over the past several years. Fortunately, jobs are being created in other industries to take up the slack. Ten million new jobs have been created in the last five years, and new industries are opening up, notably in the alternative energy sector. Some may want to compare the current economic environment to that of the early 1930s when housing and auto production went into a slump, dragging the overall economy into a depression. However, unlike the 1930s when the Fed wrongly put the brakes on the growth in money supply, "helicopter Bernanke" has stated he would fly over America dropping massive amounts of money at the slightest hint of a depression or even recession. Mr. Bernanke has a helicopter pilot's license hence the nickname.

Myth #3: China and the rest of the world are holding us hostage through the amount of Treasury bonds they hold. Again, Chairman Ben has told Congress that if foreigners dumped all their treasury bonds on the market, it could be absorbed by the Federal Reserve and institutions in a very short period of time. A side benefit would be an increase in the Yuan against the dollar which would cut into China's pricing advantage. Not to be arrogant, but the rest of the world depends heavily on the US consumer to keep their economies growing. So it is doubtful that we will see a dumping of US debt by any nation.

Myth #4: We do not save enough. Many in the media are only looking at M1 or even M2 which

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is money in checking accounts, savings accounts, money market accounts and CDs. Investors are much savvier than that and today invest in higher-yielding corporate bonds and treasury securities, not to mention common stocks. We won't even mention money invested in the housing market as that may not be as liquid as other assets. Older investors are very focused on saving for retirement, and the investment advisory business is booming as a result of all the liquidity in the markets.

Currently, sub-prime mortgage lending continues to dominate the economic news. Mortgage delinquencies and defaults are increasing, but are actually lower now than they were during the 2001-2002 recession. The common stocks of sub-prime lenders have dropped dramatically. New Century Financial has dropped 94%, Fremont General 65%, and NovaStar Financial 85% to name just a few. As is typical in any booming industry, the housing market allowed for excesses in lending practices that are leading to the current fall out. The markets have their own self-correcting mechanism, and the worst thing that could happen now would be for the federal government to step in with regulations. It's a little late to close the barn door as the horses have already left. The banking industry has established tighter credit standards to stop further issuance of these types of mortgages. Many investors past and present jump on these financial trends, hoping to make easy profits, and they along with many professional investors will be burned. Dana Investment Advisors has long been an investor in pools of Ginnie Mae, Fannie Mae and Freddie Mac mortgages, primarily adjustable rates. These government agencies have been forced in recent years to tighten their credit standards and increase their cash reserves. We see no problems for these agencies as they guarantee full payment of principal and interest. In fact, prices of these mortgage pools have firmed up in recent weeks as investors are now seeking higher yield coupled with safety of principal.

Random thought for March 2007: China will soon become the largest English speaking country in the world.

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