



October 1, 2009

Dow: 9,712

Sour Grapes

What if they held a bull market and no one came? Would it still be a bull market? The stock market is up about 50% from its March 9 low, but disbelievers abound. Some investors are even shouting, “The emperor has no clothes.” Many investors are just frustrated as they missed the move. It is not unusual to have a sharp rise after a dramatic fall. As we have stated before, there is a treasure chest of cash sitting on the sidelines waiting to be invested in something other than money market funds. We have seen estimates of as much as 3-4 trillion dollars in money market funds. Psychology plays a big role especially at extremes in the market. Last March we saw an extreme in bearish sentiment and the market was grossly oversold. That marked a turning point. Are we at the other extreme now? We would think not as the high cash level indicates that there is still skepticism if not outright bearishness out there. It is still easy to be bearish on the market with economic indicators recovering slowly and unevenly. The government has taken on massive amounts of debt in the form of stimulus programs, the unemployment picture is gloomy and the schism over health care is a drag on consumer sentiment. We have had, throughout history, periods of extremes in sentiment. At this juncture we believe that Hans Christian Anderson’s emperor has clothes.

Capitalism. More sour grapes. Webster says capitalism is “an economic system in which investment in and ownership of the means of production, distribution and exchange of wealth is made and maintained chiefly by private individuals or corporations.” Further, the distribution of goods and services and their prices are determined by competition in a free market. The government’s job in this system is to protect property and ensure the rule of law. So why do so many want to take down the system that has given us the highest standard of living in the world, a system that is the most innovative and productive in the world, and a system that improves the standard of living in other countries? Sure, high unemployment, foreclosed homes, corporate scandals and a negative press can lead to unrest and questions about the veracity of capitalism. However, we have been here before, most recently the early 1980s when Americans were not feeling too good about themselves. It just took strong leadership and a sound monetary policy to set the stage for a twenty-five year boom. If capitalism is allowed to work its magic it will happen again. In fact, it is already beginning.

(CONTINUED ON REVERSE SIDE)

Inflation. If the Fed creates tons of money, but no one spends it, is it inflationary? Well, the Fed has created tons of money and financial institutions have access to it. However, they have become very tight-fisted with that money. The Fed has cajoled these institutions to make loans to businesses both large and small and to lend to consumers for autos and homes. So far these loans have just trickled out, but we expect momentum will take hold and lending will escalate. The Fed can then worry about inflation.

Herding Cats. That is Paul Volcker's analogy to today's global financial situation. Volcker of course was the Federal Reserve Chairman in the Reagan administration that successfully led us out of the period of high interest rates, high inflation and high unemployment. We were surprised and pleased when the President appointed him to head the Economic Recovery Advisory Board. The global economy will be different as we emerge from this recession and America must adjust to these changes. Volcker has made some very astute comments (*Interview with Charlie Rose on PBS September 28, 2009*) regarding these changes and our role, most notable the following:

“The balance of power in global leadership is shifting, symbolic of the relative, less dominant position the United States has, not just in the economy but in leadership, intellectual and otherwise.”

“Credible American economic leadership requires competence, not politicization. I would like to think that given the history of the past, given the strength, actual and potential of the American economy; we can still provide a kind of indispensable element of leadership here. But it's not going to be dictatorial, I'll tell you that. It is very hard to herd these cats together.”

Random Thought for October 2009:

“If you can find a path with no obstacles, it probably doesn't lead anywhere.”

Frank A. Clark

Dana Investment Advisors welcomes any comments to their newsletter and is more than willing to discuss or explain any aspect of the letter. Feel free to call us at 262-782-3631.

If you would prefer to have our newsletter e-mailed, please send your e-mail address to newsletter@danainvestment.com. If you would like to be notified when our portfolio managers will be broadcasting in the media, please send your e-mail address to media@danainvestment.com.