THE DANA VIEWPOINT

ACHILLES II

April 12, 2011
Dow: 12,263

Last month we talked about the US Achilles heel being the energy crisis. That's a short-term problem with a pretty simple solution – drill. We have the resources that would alleviate this problem, create jobs and stimulate the economy. The other Achilles heel is what Representative Paul Ryan calls "the most predictable crisis in the history of the country." We are talking about debt and it has one cause – spending. There is a complacency in Congress that does not want to address this issue. They prefer to kick the can down the road and let the next generation deal with it. Now that Congress has passed a budget bill for the fiscal year ending this October, perhaps they will get serious about cutting spending – more than the recent 1% budget cuts. Representative Ryan has laid out his road map for American Solvency and the President plans to introduce his budget bill later this week. Hopefully, these two plans will offer a starting point for discussions to deal with this problem and get America on the road to a strategy for stronger economic growth, a lower unemployment rate and debt reduction. Reduced government spending results in increased private sector spending and that is when jobs are created and economic growth is enhanced.

A new report, "Spend Less, Owe Less, Grow the Economy," was recently unveiled by the Joint Economic Committee for Republicans. It examines countries with developed economies like ours that struggled with rising government debt. They found when government debt shrank through spending cuts, jobs grew. For example, Canada reduced total government spending by 12.8 percentage points of GDP between 1994 and 2006 and boosted economic growth from under 1% to a robust 3.4%. Sweden's economy was shrinking in the early 1990s. After reducing Swedish government spending by 11.4 percentage points of GDP from 1994 to 2000, Sweden's economy revived with growth averaging 3.4%. New Zealand experienced the same effect. (*Investor's Business Daily 3-21-11*) In order for this process to work, the spending cuts must be large and credible. A 1% cut just will not be near enough.

The economic problems we face have been identified. That's the first step. The next step is for Congress to show some courage and take the necessary steps to correct it. All problems have solutions. There will be some pain associated with the solution, but the pain will be much greater if we continue to ignore the problem. Some of the pain will come from changes in Medicare and Medicaid, but the real third rail, Social Security, may be too much to address until after the 2012 elections. The American people certainly sent a message to Congress in the last election and now the ball is in their court. If they fumble it

(CONTINUED ON REVERSE SIDE)

away another message will be sent in November 2012.

An interesting poll from *Investor's Business Daily* shows that there is widespread confusion about the Social Security Trust Fund. Among all ages, 57% said they were unsure how the trust fund was invested or that it was invested in a mix of Treasury bonds, stocks and corporate bonds, while 12% said Treasury bonds and 28% said Government IOUs. Officially, the trust fund holds $2.6 trillion in special-issue Treasury bonds. In reality, it has no assets of any value to help the government afford the cost of benefits that have already overtaken the program's payroll-tax reserves. The Trust Fund bonds are, in effect, IOUs from one branch of government – the Treasury – to another. In 2011 the Social Security Administration will cash in a projected $45 billion in trust fund bonds, and the Treasury will have to borrow an additional $45 billion to redeem the bonds. The poll also showed 6% of respondents saying Social Security has no financing issue, 47% saying the program has a financial "crisis" and 44% calling it a "problem". We would call it a "major problem" and if not addressed soon, could turn into a "crisis." However, you can see how politicians will avoid this issue until after the 2012 election.

The economy continues to forge ahead albeit at a slower growth rate than most would like to see. The private sector created 216,000 new jobs in March and that is a continuing improvement. We need to see over 300,000 monthly for a strong recovery. While we are at the printer, the US, EU and China will be announcing their consumer price indexes. China and the EU are experiencing inflation and have raised their interest rates to slow this rate. So far our Fed is staying on course, adamantly believing there is not an inflationary problem here. The Fed seems to be more concerned about the sluggish recovery in the housing market than they are about rising commodity prices – especially oil and grains. Investors are more concerned about future inflation caused by the rapidly increasing money supply. Rising inflation in China is also being exported to the US making it difficult for the American consumer. The problem has been identified and the solutions are available. We just need action.

Random Thought for April 2011: "It is incumbent on every generation to pay its own debts as it goes. A principle which if acted on would save one-half the wars of the world."

Thomas Jefferson

.

15800 W. BLUEMOUND RD • SUITE 250 • 53005-6026 • P.O. BOX 1067 • BROOKFIELD, WI • 53008-1067 • 262.782.3631 • FAX 262-782-0581
365 ERICKSEN AVENUE.N.E. • SUITE 312 • SEATTLE, WA • 98110-1888 • 206.855.8781 • FAX 800.560.6227

E-Mail: dia@danainvestment.com
Web Site: www.danainvestment.com