



July 9, 2012
Dow: 12,772

LET'S TWIST AGAIN

A popular song in 1961 sung by Chubby Checker has been adopted by the Federal Reserve. They initiated the idea of swapping short-term debt for long-term debt to keep long rates low to stimulate the economy, particularly the housing market. The strategy was dubbed the *Twist*. Like the song, it has plenty of motion but goes nowhere. It's sort of like taking money from your left pocket and putting it in your right pocket, but it will not stimulate the economy. The massive \$800 billion stimulus followed by QE1 and QE2 likewise has failed to stimulate our economy. What is it that the Fed and our boys and girls in Congress fail to understand about basic economics? Japan tried zero interest rates in the 90s to stimulate their economy, and all they ended up with was a decade long recession. The Treasury is also fearful of tilting issuance towards longer maturities because of their fear of pushing interest rates higher. Corporations are also borrowing at what will probably be historic low rates. However, they are not investing much of this money. They are holding it for a sunny day. Now why would they do this when the return on equity in their business is 7% - 8%? That is the average return on equity of all publically traded companies. Of course, many companies have return on equity in excess of 20%. In the late 1970s and early 1980s the prime rate reached 21%. Companies were still borrowing and investing, because inflation was rising and debt could be paid off with cheaper dollars. So what's the difference today? Uncertainty. There were fewer onerous regulations in the 1980s and taxes were starting a downward trend. The passage of Dodd-Frank put many costly regulatory hurdles in the path of start-up businesses and even businesses trying to expand. High tax rates and the threat of higher taxes pushed corporations to build plants in China or other low tax rate countries. In the fall of 2010, President Obama met with Steve Jobs to hear his views on job creation. Steve Jobs was noted for being blunt and outspoken. He told the President, "You're headed for a one-term presidency." To prevent that he said, "The administration needs to be a lot more business friendly." He described how easy it was to build a factory in China. He said, "It was almost impossible to do so these days in America largely because of regulations and unnecessary costs." ("*Steve Jobs*" by Walter Isaacson page 544.) We need tax reform measures to encourage new business start-ups and to make the tax code fairer for everyone. Let's hope Congress can get its act together next year (it won't happen this year) and work together to make this happen. Money would then be flying off corporate balance sheets to expand business. In addition, many outsourced jobs would return home. Bottom line – we don't need lower interest rates as there is already plenty of money available.

From the Department of You Can't Make This Stuff Up: the Agriculture Department has been running radio and TV ads prodding people to sign up for food stamps. They claim that the food stamp program stimulates

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the economy. Even more incredulous, they are claiming that food stamps will help you lose weight. A record 44.7 million people received food stamps in fiscal 2011 up from 28.2 million in 2008. One in seven Americans now qualifies for food stamps. This program is ripe for fraud. Someone is probably printing counterfeit stamps already as the black market for these stamps is expanding.

The jobs report was released Friday and no matter how you spin it, it's anemic at best. The Labor Department reported that 80,000 jobs were created in June up from 69,000 in May. The average for the last three months is 75,000. We need over 200,000 new jobs created each month just to keep pace with new entrants into the job market. The unemployment rate remained at 8.2%. However, if you add in those who have given up looking for work, the unemployment number is a more realistic 14.9% and the labor participation rate is at 63.8%, a forty year low.

Before someone writes *The Rise and Fall of the United States of America*, let's look at what is also happening across America. Many states and cities are recognizing the fiscal problems besetting America and are taking steps to get their financial houses in order. Texas, Indiana, Ohio, New Jersey, Wisconsin, Kansas and others are balancing their budgets and setting the stage for a strong economic growth. Even Chicago, led by Rahm Emanuel, is leading the charge to competitive bidding on many city government projects and has ideas to privatize some government services, most notably Midway Airport. This is opening up a new age of private enterprise that will create jobs and reduce taxpayer liabilities. This new age of responsibility will trickle down to the individual level and save us from the plight of the European entitlement state.

Random Thought for July 2012:

You cannot strengthen the weak by weakening the strong.

You cannot help small men by tearing down big men.

You cannot help the poor by destroying the rich.

You cannot lift the wage earner by pulling down the wage payer.

You cannot keep out of trouble by spending more than your income.

You cannot further the brotherhood of man by inciting class hatreds.

You cannot establish security on borrowed money.

You cannot build character and courage by taking away a man's initiative and independence.

You cannot help men permanently by doing for them what they could and should do for themselves.

William J. H. Boetcker, 1916

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