Market Commentary
First Quarter 2009

The long-awaited Public-Private Partnership Investment Program (PPIP) to attack toxic assets on banks' balanced sheets was announced and greeted positively by the Street, yet the credit markets continue to be fragile. Some incoming economic data has shown signs that activity is declining at a less rapid rate—the first step in a potential recovery. There are also some positives emerging on the global front, although it is too early to say whether we are through the worst of the downturn. China has shown signs of improvement, but Eastern European banks may be the next financial crisis that needs to be addressed.

A combination of government action and aggressive Federal Reserve policy was necessary to prevent a complete financial collapse. Also, as we are the midst of a deep recession, reflationary policies from both fronts seem to be appropriate. There was a positive response to the Obama administration's plan to deal with toxic assets on banks' balance sheets, but uncertainty returned on the news that the government had forced out Rick Wagoner, the former CEO of GM. And, given the latest news on unemployment and the large drop in Americans' net worth, there is little doubt that the pressure from the public on politicians to "do something more" will grow. There has been hope in some economic data—"green shoots" as Treasury Secretary Timothy Geithner said—and the stock market is a forward-looking indicator. We do feel that waiting to dip our toes back into stocks until the economy has completely made the turn could be detrimental to longer-term performance.

While Wall Street cheered the government's plan by rallying substantially on the day it was announced, the success of PPIP is uncertain. Whether banks will want to sell at the prices being offered, and whether private capital will want to partner with the government given its heavy-handed nature, is yet to be seen.

There is some positive economic data: The steep fall in spending and manufacturing following the Lehman Brothers bankruptcy in September 2008 was so dramatic that it simply could not be sustained. After recovering from a state of paralysis during which consumers locked down, some pent-up demand has been building. Although the economy is still in decline, that pace is slowing. Corporations, suffering from falling revenue and profits, must cut expenditures and jobs. Businesses tend to wait for confirmation of lower demand before furloughing workers, and the unemployment rate tends to lag economic activity by about seven months. The unemployment rate will continue to rise, likely culminating in a peak unemployment rate approaching 10%.

The U.S. dollar has risen in a flight to safety. A modest decline in the dollar would be positive, as it would enable the United States to stave off the negative impact deflation has on U.S. dollar-denominated debt, and stimulate exports.

Only time will tell if glimmers of hope will turn into sustainable trends. We continue to watch for moderate U.S. dollar weakness and strength in commodities as a sign that reflationary efforts are gaining traction and that some increase in risk tolerance is occurring. In conjunction, we'd expect to see resource-related currencies and markets - both developed and emerging - improve to confirm a revival in the global markets.