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It's a Jungle Out There

Maintaining distance and perspective is one of the more difficult parts of my job. It may be true for anyone. Consider the inflow of news and data, 24/7. It's so easy to get involved in some piece and lose sight of the larger picture. The goal for me is twofold: first challenge is trying to perceive and understand the interconnectedness of the many pieces; second is comprehending which parts of the whole I have absolutely no control over and which parts I can react to and thereby preserve or make money for you, my clients.

Two 800-pound gorillas dominate the scene just now. Impossible to ignore them, they go by the names Sovereign Debt and Financial Regulation. The debt crisis currently being played out in the European Union, especially with respect to Greece but with Spain revealing its own weakness, is clearly the Union's problem to solve. Failure to resolve it could eventuate in a rapid downturn in the markets because the worldwide economic recovery would be affected. Europe was slow to respond in the early stages of this crisis. As I write this letter, the Union seems to have realized what its role can and must be. At the same time, the entry of the International Monetary Fund is a compelling sign that Europe's problem is not Europe's alone, nor is the solution.

New and effective regulation of our financial system is surely our problem to solve. What seem to be emerging from the political tug o' war are perhaps the largest changes in our system since those enacted in the aftermath of the Great Depression. We take for granted now the presence of such 'revolutionary' institutions as Social Security and the Federal Deposit Insurance Corporation. Painful as it was, the Depression was a powerful learning experience. Our current crisis would have been unimaginably deeper without recourse to the hard-won wisdom of the 1930's and 40's. What's clear is that the profound complexity of the financial system as it has evolved in recent decades requires a similar wisdom. Deregulation in the 80's and 90's has brought us the anomaly of banks 'too big to fail', and a Wall Street casino mentality in which anything goes. The imperative to bring control back into the system is clear and immediate.

With that macro perspective, I must try to understand and interpret the micro data on my particular screen. My index again approaches the 80% mark. Only a few times—ever—has this indicator registered above 80%. The year following the 1932 market rally of 80% saw a decline of 50%. By some research methodologies, the markets are perceived as relatively cheap compared to the last 20 years, not necessarily the good thing it may sound like. On the other hand, here's an interesting reading in a survey of investment professionals: only 17% believe the market will turn down in the next six months. Unfortunately, the last time the survey recorded a reading this low was 1987, the year we watched in disbelief as the markets found a huge banana peel. Caution and attentiveness—how else should we respond to the big gorillas?

And if we should figure it out, all of it, all the pieces in place, here comes the catastrophe in the Gulf of Mexico. Who knows the long term impact? At the moment, the word is 'staggering'. A humbling word, to be sure.