

July 9, 2010

## Are We Headed for a Double Dip?

### Bad Quarter for the Stock Market!

The first quarter of the year started out well, with the stock market moving up nicely on positive earnings news. Unfortunately, in the latter part of April, the news that Greece was in dire trouble with their debt, followed by the acknowledgment that a number of other countries had major sovereign debt, brought about panic in the markets around the world. Because the countries with the problems were in Europe, the panic resulted in a reduction in the value of the Euro.

The concern about liquidity followed, with a shift to safety, and strong fund flows to U.S. Treasuries. While the rest of the world looked to the U.S. as being stable and in a growth mode exiting the recession, U.S. markets did not see it the same way. U.S. markets responded by going down substantially. The S&P 500 finished the second quarter of the year down 12½%.

The overall concern in the U.S. was that if the rest of the world's growth slowed, the impact on U.S. growth would be negative and could stall the recovery. To some extent, this fear was proven correct, as new job formation that was very strong in April petered out in May and June. In addition, layoffs that had been dropping week to week picked up again and only showed a marked drop in the last week of June.

### Where are we going from here?

As I write this newsletter, consumer confidence is down, job formation has slowed to a crawl and layoffs continue unabated. With all this being said, it is very likely that we will see earnings for the second quarter up substantially from a year ago and better than the first quarter. What will be most closely watched will be the revenues that produce the earnings. If profits are up, with flat to slightly elevated revenues, that will not be good because it will indicate that increased profits are likely due to a reduction in expenses and not growth. On the other hand, if revenues are up significantly with increased profits, then that would indicate that the economy is continuing to grow and that earnings growth could continue into the next quarter. Beginning with the week of July 12th, we will begin to see this information unfold. For now, the markets are waiting for more information.

### The IMF and the Obama Administration

The International Monetary Fund in their recent global assessment, released on July 8th, concluded that the world economy will continue to grow faster than expected this year, but the recovery is overshadowed by major risks and the pace of growth is likely to slow. The IMF specifically told the Obama administration that they anticipate growth of 3.3% in the U.S. for

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2010 and then not to top 3% annual growth over the following five years. This is a more pessimistic outlook than the administration's, and it means the IMF projects the deficit and debt at a far higher level than White House forecasts.

The advice from the IMF is that the U.S. needs to raise taxes and reduce Social Security benefits to contain the U.S. budget deficit and public debt. The ratio of public debt to GDP is also a concern that could lead the U.S. into sovereign debt not unlike some of the European countries currently making headlines. The U.S. position is that, unless they continue to spend, the recovery could stall.

#### **So...are we headed for a double dip?**

With all the information noted above, there does seem to be one clear message: the economy is growing and earnings are recovering. We will

probably not have a rapid rebound, but we are moving forward. The larger question is: will the growth be sufficient to spark job recovery and bring back consumer confidence? For this we will have to wait and see.

#### **Conference Call**

The quarterly conference call will be held on July 20th at 3PM EDST and 1PM MDST. I am hopeful that the question of revenues and earnings will be partially answered by the time of the call and I will give you an update of what is happening.

If you would like to participate in this call, please ask Caroline Rose, 603-433-5515, for the call-in number and access code.

#### **Have a wonderful summer!**

Ed Mallon

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