

Private Wealth MANAGEMENT



Bonds & Baklava

James Carville, known as the “Ragin’ Cajun”, gained national attention in 1992 while working on Bill Clinton’s presidential campaign. In a now famous quote, he once said:

“I used to think that if there was reincarnation, I wanted to come back as the President or the Pope, or a .400 baseball hitter. But now I want to come back as the bond market. You can intimidate everybody!”

The bond market’s power to intimidate stems from the fact that ultimately, it is the bond market that decides what long term interest rates will be. This in turn affects what governments, businesses, and ordinary citizens can expect to pay on their debt (your mortgage rate is an example). A sharp rise in interest rates can be crippling for any borrower, even governments.

The government of Greece has just experienced the powerful intimidation of the bond market as their fiscal problems came to the attention of investors around the world. The fact that Greece has debt problems certainly does not make it unique. In fact, much of the developed world has debt problems including Japan, the UK, and much of Europe. You may remember my highlighting our own debt problems here in the US in the December client letter. In that letter, I described what we normally do when we need more money—we just print more of it. Unfortunately for Greece, they do not have that option.

Greece is part of the Euro monetary system and does not have its own currency. When it faces a budget deficit as it does now, it faces some difficult choices. One option is to cut spending (which they have started doing), but this is politically very challenging, as evidenced by the current strikes throughout Greece and other parts of Europe. Another option would be

to default on the debt and leave the Euro monetary system all together. I seriously doubt this will happen as that would really hurt any chances of borrowing money in the future. More than likely, bigger and wealthier siblings like Germany and France will need to come to the rescue—but if that happens, you can bet that Portugal and Spain will be expecting the same courtesy. We will be watching the Greece-bailout situation very closely as the final result will have implications for other sovereign debt as well.

Back here at home, more and more economists, strategists, and politicians are seeing improvements in our economy. But don’t break out the baklava just yet—unfortunately, the improvements look more statistical than structural. What I mean by that is that while GDP is growing, (almost 6% in the fourth quarter of 2009) the feeling on Main Street is still that of a recession. The ongoing and painful process of deleveraging (paying off debt) will be here to stay for several years. And until we start to see some real improvements in the labor market, this recessionary feeling will not change. On the bright side the severity of layoffs has slowed and temporary workers are seeing job gains as of late. Let’s hope this trend continues...We still recommend investors maintain a cautious view going forward, especially after the monster rallies in many asset classes in 2009. The theme of investing for income is strong and we expect that to continue going forward. Within equities, dividend paying stocks like Utilities, Telecom, and Consumer-Staples (not to be confused with Consumer--Discretionary) should provide a good total return over the long run. Within Fixed Income, we like certain step-up coupon bonds and feel that coming increases in tax rates should spur more demand for municipal bonds. Some of the best risk/reward opportunities as of late have been in the non-traded REIT space, providing above average

yields and good potential for capital appreciation in the future.

Rest assured, we are constantly looking around the world and in all asset classes for the best opportunities to protect and grow your wealth. Feel free to send us your questions and comments and let us know if we can serve you better.

Respectfully,

Vijay J. Marolia, MBA
Chief Investment Officer

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Registered Principal

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High yield/junk bonds are not investment grade securities, involve substantial risks and generally should be part of the diversified portfolio of sophisticated investors.

Bonds are subject to market interest rate risk if sold prior to maturity. Bond values will decline as interest rate rise and are subject to availability and change in price. Stock investing involves risk including loss of principal.