



WEALTH DIMENSIONS

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Opportunity in a Perfect Storm of Confidence

The steady drumbeat of bad news continues to emanate from newspapers, magazines and commentators. The announcement of an official bear market as the S&P 500 fell more than 20%¹ from its October peak, relentless oil and food price increases, crashing real estate, runaway inflation, and even rice hoarding are among the highlights the media uses to attract our attention daily. A recent headline in the Wall Street Journal even called this “The Lost Decade”.

There is little doubt that these issues affect our daily lives and can dampen our outlook for the future, but for some reason current levels of pessimism are far worse than economic data would suggest. According to the University of Michigan, consumer confidence measured 56.7 in June, the lowest monthly measurement since May, 1980.

Why all the pessimism?

One might speculate that the current combination of declining home prices, high oil prices, and sluggish stock market has led to the current level of anxiety, but all these factors were prominent economic concerns in 1980. By comparison, in 1980 unemployment was 7.5% (5.5% current)², inflation exceeded 14% (4.2% current)² and the prime lending rate was 18.5% (5.0% current)³. Inflation-adjusted oil prices spiked to the equivalent of \$135/bbl today, real estate values were in steep decline, and the stock market was coming out of the last “Lost Decade” of the seventies. The S&P 500 provided a scant 3.17%¹ annual return from January 1, 1970 to December 31, 1979, a remarkable 4% per year less than inflation. Using conventional macroeconomic metrics, current economic data should translate into a consumer confidence level almost 30

points higher than the actual June reading when compared to the economic climate in 1980.

If conventional economic measures do not fully explain these low confidence figures, the current political environment may provide some insight. Leadership has always played an important role in the public's perception of the future and Gallup polls do not suggest tremendous optimism that our leaders in Washington are up to the task. The most recent ratings of the President continue to hover near all-time lows around 30%⁴. What is equally concerning is that Congress' approval rating is at an all-time low below 20%⁴. As we head into the fall elections, the combative nature of the election process creates further anxiety and uncertainty. Once the election takes place, much of the rhetoric and uncertainty will subside and the political climate will calm as the President and new Congress develop their plans for prosperity.

Given the current economic and political climate amid the backdrop of one of the worst decades for US Large Company stock returns since the Great Depression, it is understandably difficult not to let this Perfect Storm of Confidence trickle into decision-making. While the litany of troubling news can be frightening, the reality is that to make money over the long haul, a good long-term investor has to lay the groundwork during rough times.

Price cycles exist in almost all markets and oil is no different. On an inflation-adjusted basis, oil prices reached a 50-year low as recently as 1998. Oil dropped to a low of \$8.65/bbl in December 1998, and the cover of the March 4, 1999, edition of the renowned Economist magazine read "The World is Drowning in Oil," followed by an article stating that prices may well be on their way to \$5.00/bbl. Exploration and drilling stopped, refineries rusted, and consumption soared as we built bigger homes and giant SUVs became the norm. As consumption grew and supply growth could not keep pace, prices have risen. We find it interesting that oil prices, adjusted for inflation, are now at the same level as they were at their highs in 1981. As they say in the commodity pits, "the cure for high prices is high prices." We don't know where oil prices will ultimately settle, but as prices rise, the viable sources of energy increase and demand decreases. We have already seen a marked increase in drilling and exploration, increased development of alternative energy technologies, and according to the Transportation Department, Americans drove 11 billion fewer miles this March than the previous March.

So where is the opportunity?

We have frequently discussed the fact that investors price into the market all known information and when things are at their worst, the markets tend to mirror that pessimism. What is also true is that investors tend to become too optimistic in good times and too pessimistic in difficult times. Often, when things seemed the darkest and consumer sentiment and investor pessimism were at extremes, it actually marked the turning point. The opportunity lies in the fact that when declining markets reflect deep pessimism, the risk is generally *decreasing* and opportunity *increasing*. For instance, in the decade of the eighties, the S&P 500 returned a compounded rate of return of 16.32%¹ per year – despite the pessimism that characterized the decade's dawn.

There will continue to be ongoing opportunities in the global markets for long-term investors. Through proper diversification and appropriate risk exposure, we continue to look forward to helping you capture these returns.

Stay the course!

We appreciate your continued confidence in our services.

Wealth Dimensions Group, LTD

¹ www.standardandpoors.com

² www.bls.gov

³ www.federalreserve.gov

⁴ www.gallup.com

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