



BOYER & CORPORON
WEALTH MANAGEMENT, LLC

Investment Commentary June 1, 2009

There have been signs of good news in our economy and around the world ...signs that the credit crisis is over, that the recession has ended and that the bear stock market is history. The stock market is certainly factoring in a fair amount of optimism. Since March 9th, the Dow Jones Industrial Average has increased 30%, the S&P 500 36% and the EAFE Index 42%.

In addition, the credit markets are behaving as if things are almost back to normal. During the credit crisis last September, the cost of borrowing soared to "financial Armageddon" levels. Investors everywhere sold bonds with any risk at all and poured money into U.S. Treasury Bills. So much money went into T-Bills that, for several weeks, the effective interest rate for a T-Bill was 0%.

A common measure of risk is the difference in interest rates that are paid between "risk-free" bonds (U.S. T-Bills) and bonds with risk (all other bonds). In other words, if the U.S. Government is able to borrow money at an interest rate of 1% (e.g. a 3-month T-Bill), very safe bonds might have to pay 2% (a "spread of 1%"), slightly less safe bonds might have to pay 3-5% and high-risk bonds might have to pay 5-7%. When the credit crisis was running full force during the last quarter of 2008, the spread between U.S. Treasury Bonds and ALL other types of bonds

increased to almost unheard of levels. High risk bonds (a.k.a. Junk Bonds) had to pay over 20% more than the interest rate on U.S. Treasury Bonds. Recently the spread on all bonds has decreased significantly, an indication that investors are much less worried about credit risk.

Other items of "good news":

The contraction in GDP for the first quarter of 2009 was revised from -6.1% to -5.7%.

The jobless rate in April was only 540,000, much less than the 600,000+ jobless rate to which we were becoming accustomed.

Pending sales of previously owned homes rose for the second straight month in March, suggesting that the housing slump has bottomed.

The price of a barrel of oil increased 29% during May from \$51.12 to \$66.31. You may think that is actually bad news but higher oil prices infer that economic activity is picking up, thus increasing the global demand for energy. Or you could recall that oil was trading for \$145 per barrel last July and opt to move this paragraph to the "Back to Reality" section (below).

Unemployment is just over 9% nationally (could be worse).



Back to Reality.....

The recent stock market rally has just brought it back to even for 2009. Since December 31st, the Dow Jones Industrial Average is down 3.1% and the S&P 500 is up 1.75%.

Unemployment is high and is likely going much higher. There are eight states with unemployment rates in excess of 10%. Michigan leads the way with unemployment of 12.9%.

Mortgage foreclosures hit another record in April. There were 342,038 foreclosures in April after recording 341,180 in March. Prior to March, the largest number of foreclosures in one month was 303,879 last August. There are over \$2.5 trillion Alt A mortgages and Option ARM mortgages yet to re-set (and default). They just began re-setting this year and the default rates have already begun to increase dramatically. Monthly foreclosures of this magnitude are likely to continue. This means you are going to continue to see additional "for sale" signs in your neighborhood for the next couple of years.



If you consistently spend more money than you earn, you eventually run out of money. If you want to continue to spend at the same rate, you must borrow money, either from credit cards or a lending institution or both. In addition to your previous daily expenditures, you now have to pay the interest on your debt and hopefully make payments toward the principal. However, if you haven't curbed your spending, you are unable to pay principal OR interest. Eventually you reach the point where no one will lend you money anymore and you are mired in payments to your lenders. Finally your lifestyle is forced to change whether you want it to or not. Some

people may actually resort to financial crime at this point.

Countries don't have the luxury of resorting to financial crime. Our country has been spending more than it earns for many years and, in an effort to stimulate the economy, it is borrowing (and spending) more money. Those borrowed funds eventually have to be repaid and, since countries cannot resort to crime to produce new funds, they have to turn to the citizens of the country and take money from them legally...by raising taxes. There is no way you can run a large deficit and not raise taxes. Taxes WILL be increased next year. Income taxes. Capital gain taxes. Estate taxes. All sorts of taxes.

The Office of Management and Budget (OMB) projects the U.S. budget deficit to reach \$1.84 trillion this year and \$1.25 trillion next year. Put another way, the projected deficit this year will be almost 13% of Gross Domestic Product and 8.5% of GDP next year. That is the largest deficit since World War II....by far. Although we ran huge deficits to fund World War II, the largest deficit since World War II was 6% of GDP in 1983. This year the deficit will be more than double the largest deficit in over 60 years.

The OMB and the Obama administration project the deficit to decline by the fourth year of Obama's term to under \$600 billion. However, they are using what we think are some optimistic projections for future growth. If unemployment continues to increase, tax revenues will fall well short of expectations.

The Congressional Budget Office projects that the total budget deficit over the next ten years will top \$9 trillion!! Running large deficits never come at a good time but if the CBO is correct about the next ten years,

this deficit could not be coming at a worse time. This is the decade that Baby Boomers are beginning to retire and collect Social Security. It is currently estimated that Social Security will run out of money in 2037. This prediction assumes life expectancies will remain constant.

When I was born in 1954, the average male could expect to live to age 66 (I'm planning on beating that). The average male born today can expect to live until age 75. When Social Security was created, it realistically was only expected to pay a beneficiary a few years after retirement at age 65. Today, you can begin collecting full SS benefits at age 66....but you can expect to live to age 75. Obviously the original design of Social Security has not kept up with reality. And here's the quiet ticking time bomb no one is discussing....our generation may accidentally change the life expectancy tables more than any generation. No, I don't have delusions of immortality, but I KNOW we are more conscious of what we eat than previous generations. I KNOW we don't smoke as many cigarettes. I belong to one of those "mega-gyms" where I exercise regularly and it's packed with people riding bicycles and running on treadmills. My parents NEVER exercised. And when I ask anyone my age if their parents exercised, the answer is always "no, never". So what happens in the year 2027 (just 18 years from now) when SS is still trying to pay people who, according to the life expectancy tables, are supposed to be dead?



Our Investment Commentary for April included a graph of monthly new foreclosures for the past four years. There are several points in the four-year period where it might

appear that the housing/mortgage foreclosure peak has been reached....two to three month periods where the number of new foreclosures declined....only to be followed by a month with a higher number of foreclosures. I point this out to illustrate that the severe recession in which we find ourselves will occasionally, from time to time, appear to be behind us. We will have a couple of months where it appears to be getting better. This is particularly likely to happen after hundreds of billions of dollars are pumped into our economy by the administration. If you recall, we had better than expected economic growth in the second quarter of last year....right after President Bush sent checks to virtually everyone in America. The stimulus was short-lived and the recession re-asserted itself.

At Boyer & Corporon Wealth Management, we continue to have grave concerns about the economy, both here and abroad. A couple of months of news that is "not as bad" are not enough to get us excited. We are not increasing our equity exposure at this time and we continue to keep our fixed income durations as short as possible.

To the extent that we own equities (stocks), we are much more prone to liquidate positions which appreciate in value. The "buy and hold" strategy is more effective during long term secular bull markets. When interest rates are declining and earnings are expanding, it's a great time to hold stocks. When interest rates are rising and earnings are NOT expanding, "buy and hold" can be a very disappointing strategy.