



Weekly Market Update – Week Ending September 3, 2010

Surge at Summer's End

Hurricane Earl unleashed turbulent winds, rain and waves along the Atlantic Coast. Yet the hurricane's timely departure gave many families the chance to spend the Labor Day weekend amid calm and sunshine at the beach. Equities, real estate and commodities snapped out of their summer doldrums from August with brisk gains during the first three days of September. The three-day gain in the S&P 500 Index outpaced 99.5% of all other three-day gains since January 1950. These markets had declined during August when stories suggested heightened risks to the economic recovery. Even the relatively optimistic observers of the economy acknowledge that it faces stiff headwinds. The jobs market and manufacturing sectors are burdened with excess capacity. Consumers might reduce spending to increase savings. These conditions might constrain economic growth. Prospective capital market returns appear limited given the outlook for sluggish economic growth and moderate to high valuation measures.

Key takeaways for fiduciaries:

- During an era of low market returns, some organizations will find that spending plans might require cuts or additional cash infusions.
- Organizations should re-evaluate strategic and spending plans given potential investment returns.
- Yanni Partners, a Division of GBS Investment Consulting, LLC, helps clients to integrate portfolio management with their overall financial management. We evaluate the portfolio's capacity to support the organizations' spending.

As a prelude to Labor Day, the Labor Department released the August employment report on Friday.¹ On the surface, the numbers looked bad: The economy lost 54,000 jobs, and the unemployment rate inched up from 9.5% to 9.6%. Some analysts found some positive signs upon closer review, such as 67,000 new private sector jobs. Yet a broad assessment reveals a lot of slack in the labor market. The "underemployment" rate rose from 16.5% to 16.7%. The underemployment rate includes unemployed people who are currently looking for work, those who have stopped searching and people working fewer hours than they want. The August 2010 values for both the unemployment and underemployment rates are close to historical highs based on the Department of Labor's records (beginning in January 1948 for unemployment and January 1994 for underemployment).

The slack in the labor market re-enforces another recent statistic: excess capacity in manufacturing. On August 17, 2010, the Federal Reserve Board reported that July 2010 manufacturing capacity utilization was 72.2%, which lagged its average of 79.2% from 1972 to 2009.² The unused capacity in the economy suggests muted growth prospects over the near-term. A relatively slow economic growth rate also suggests limited potential for equities, all other factors being equal. As we have mentioned in recent Updates, the valuation levels of equities appear moderate to high, thereby restraining the expectation for returns.



The fixed-income market presents a compelling case for low returns. As of Friday, the 10-year U.S. Treasury note yielded 2.70%. A bond's current yield provides a very good estimate of its future return.

The prospect for modest returns means that some organizations will not be able to rely on investment performance alone to achieve key organizational goals. For example, many underfunded defined benefit pension plans might require future contributions because investment returns might not be sufficient to improve the funded status of the plans. In order to fund planned capital improvements, some hospitals might face the prospects of deterioration in key financial ratios, such as days cash on hand, or seek other sources of cash. Effective financial planning requires coordination of spending and investment practices. Our firm helps clients to review their spending plans given potential market risks and returns.

<i>Periods as of September 3, 2010</i>	Week	Month to Date	Quarter to Date	Year to Date
S&P 500 Index	3.80%	5.28%	7.57%	0.41%
Russell 2000 Index	4.34%	6.87%	5.76%	3.70%
MSCI EAFE Index	4.04%	4.17%	10.51%	-4.11%
Barclays Capital Aggregate	-0.07%	-0.64%	1.72%	7.14%
MSCI REIT Index	5.94%	6.08%	14.97%	21.53%
DJ-UBS Commodity Index	2.59%	3.19%	8.33%	-2.93%

Index Sources: Standard & Poor's, Russell, MSCI Barra, Barclays Capital, Dow Jones, UBS

¹ Bureau of Labor Statistics, Department of Labor

² Federal Reserve Board