

Economic & Financial Market Update

January 2010

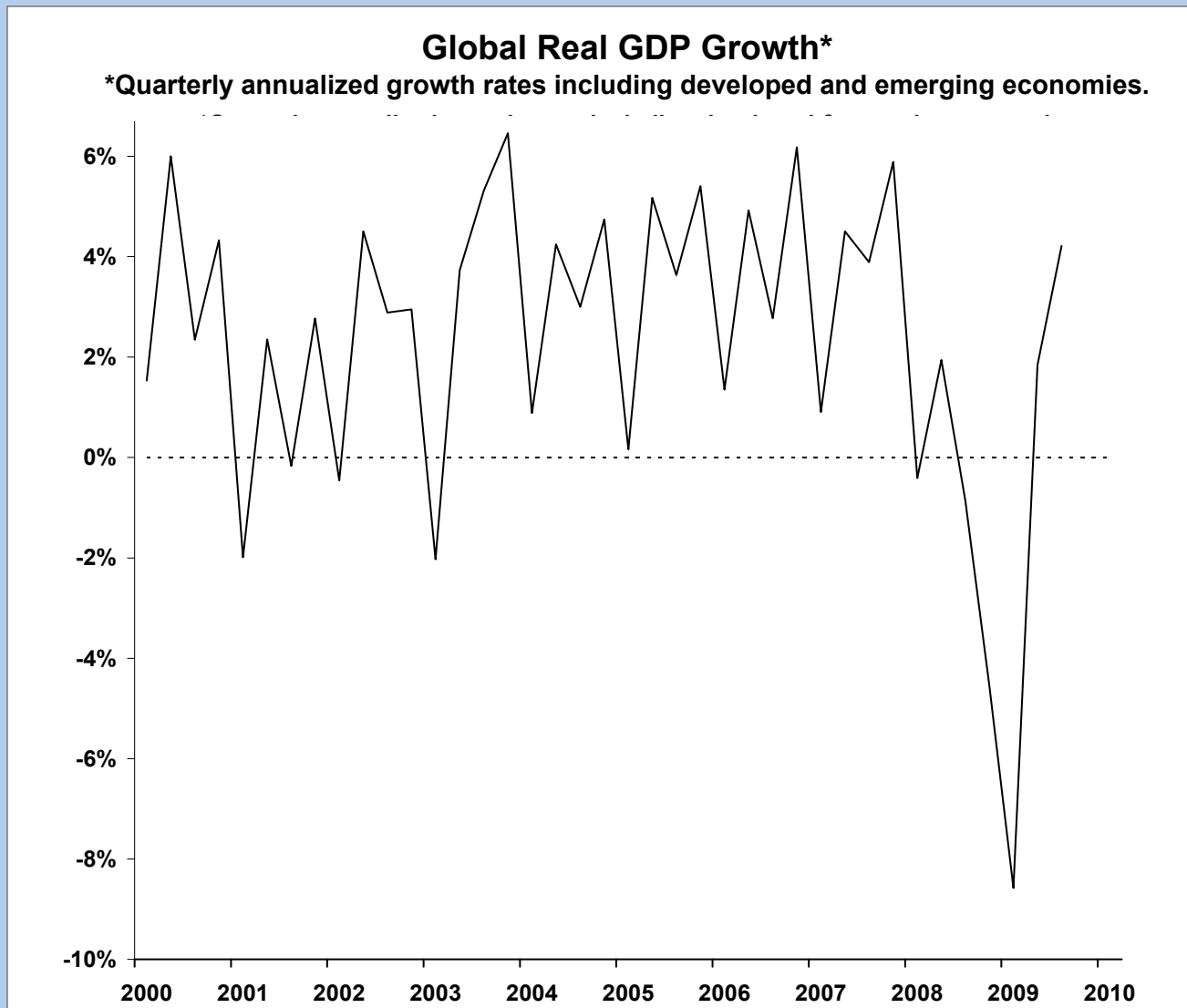
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WELLS CAPITAL MANAGEMENT

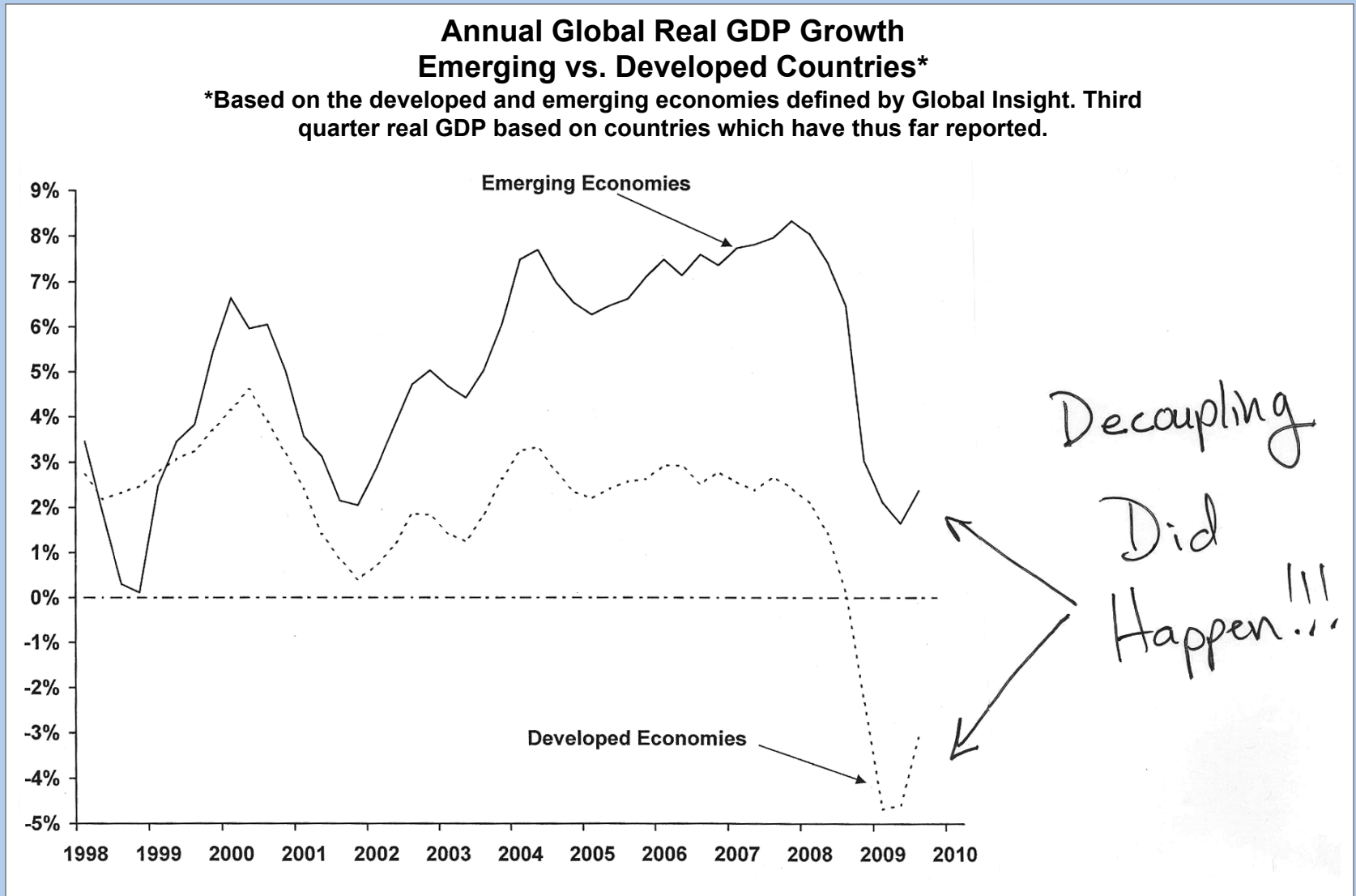


James W. Paulsen, Ph.D., Chief Investment Strategist

Back To Positive Growth!!!



The “EMERGING WORLD ASSET”!!!?



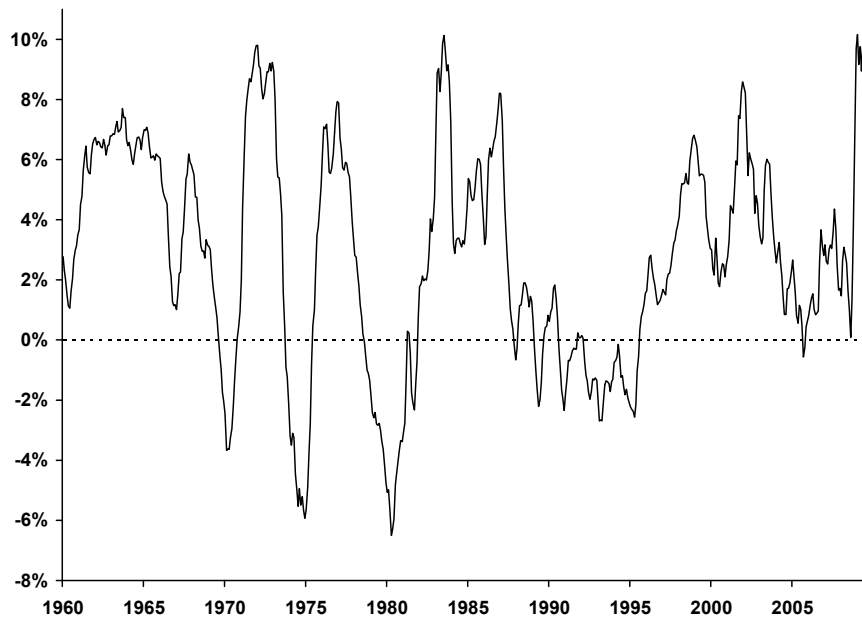
Economic Outlook? Six Major Forces for Growth!!!

- 1. Massive Policy Push!**
- 2. Reverse Corporate Purge!!**
- 3. A Returning Calm/Confidence!!!**
- 4. Addition by Less H&A Subtraction!!!!**
- 5. U.S. Trade Improvement!!!!!!**
- 6. Two Negatives Have Stalled!!!!!!**

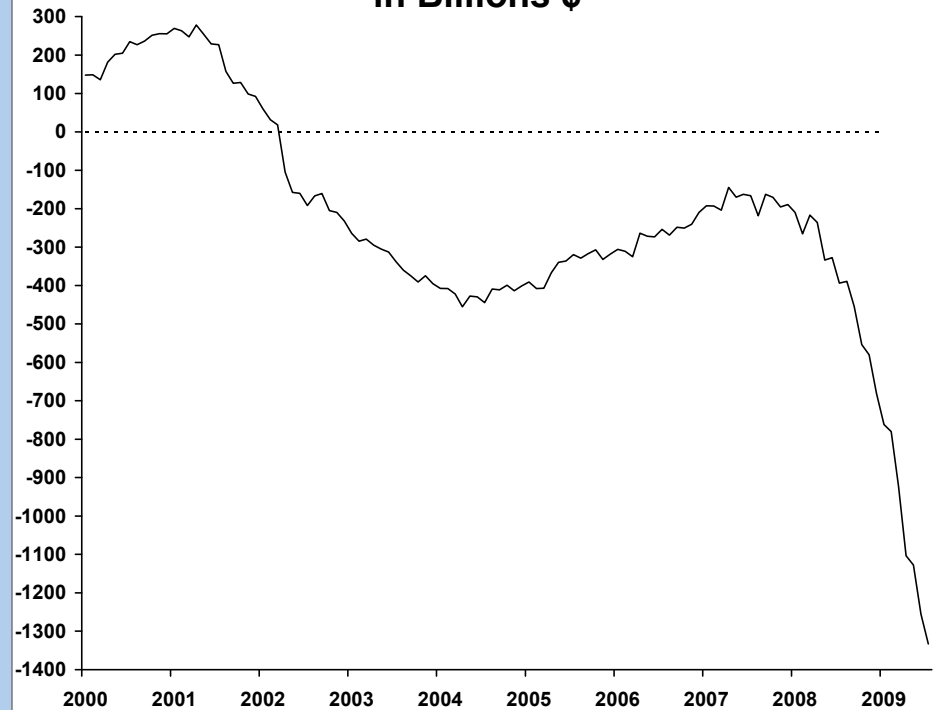


Stimulus Galore

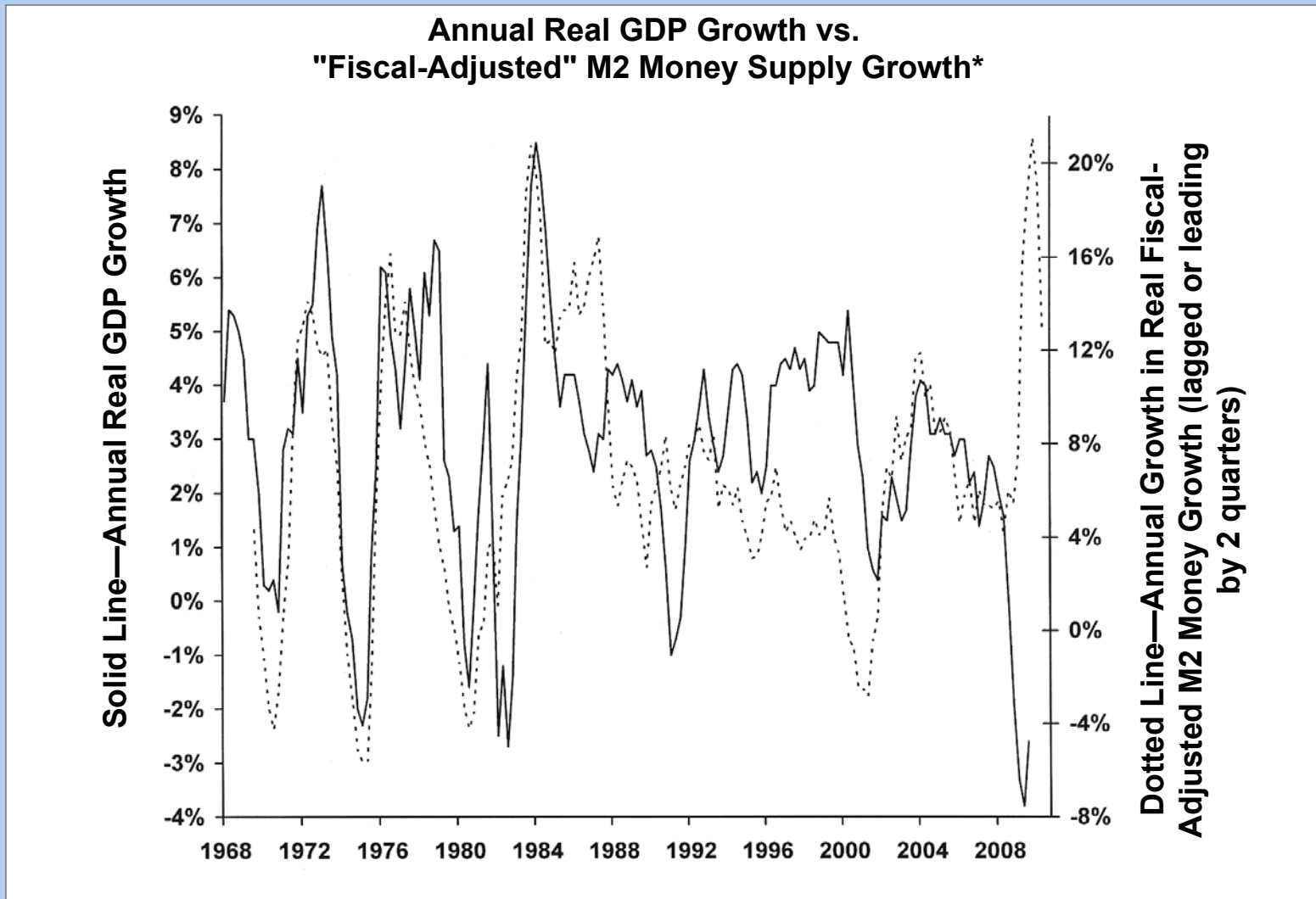
Inflation-Adjusted Annual M2 Money Supply Growth



Trailing 12-Month Federal Government Deficit/Surplus in Billions \$



Government Has Done Enough?

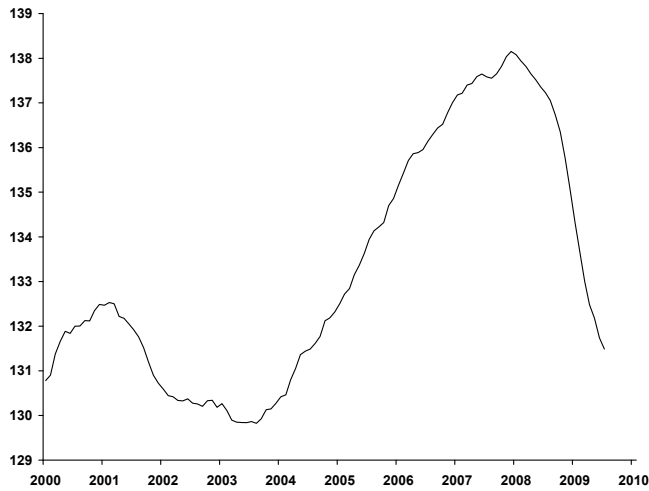


*Annual change in M2 money supply plus annual increase in federal net outlays or less the annual reduction in net federal government outlays (i.e., federal outlays less receipts) as a percent of initial base of M2 money supply one year earlier.

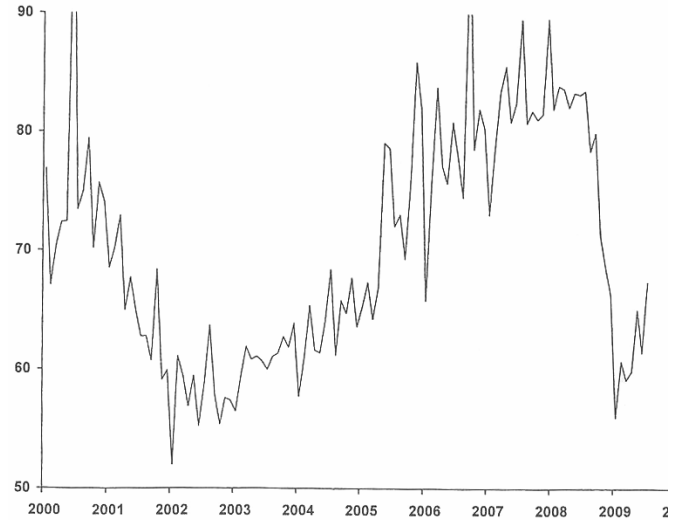


Reverse Corporate Purge!!?!

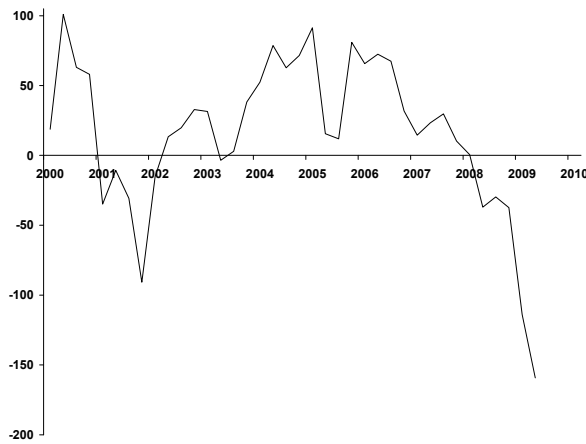
NonFarm Payroll Employment



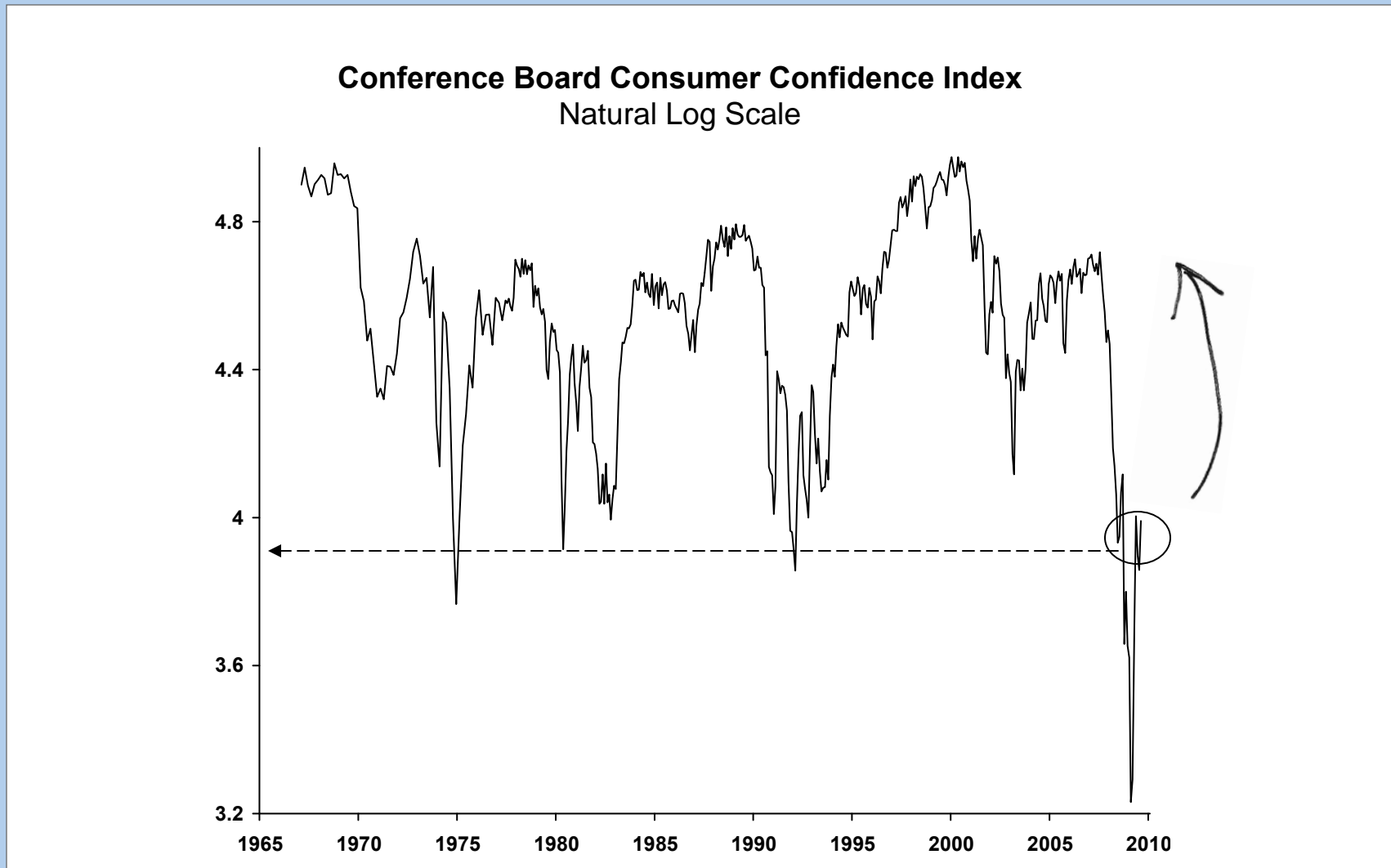
New Orders for Capital Goods



Change in Real Business Inventories



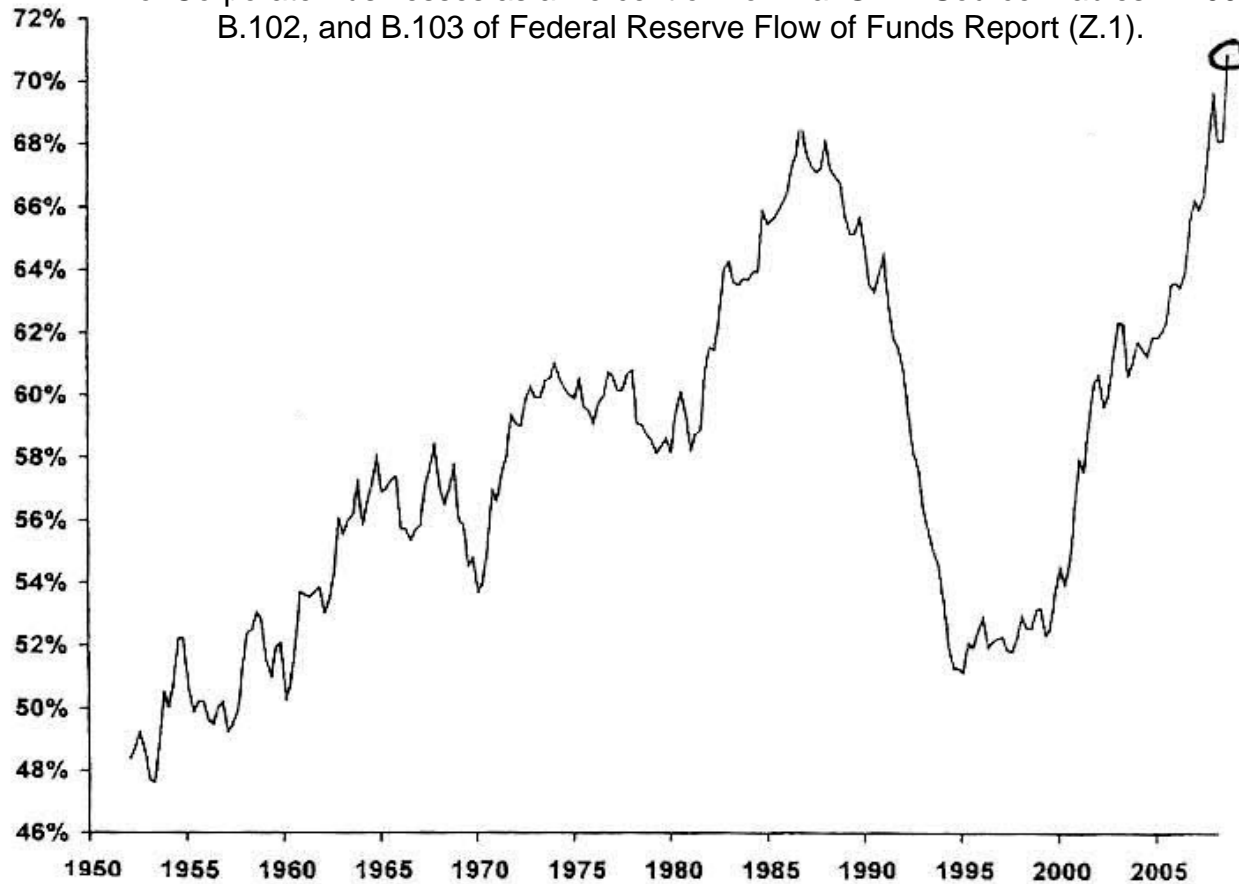
Improved Confidence!!!!



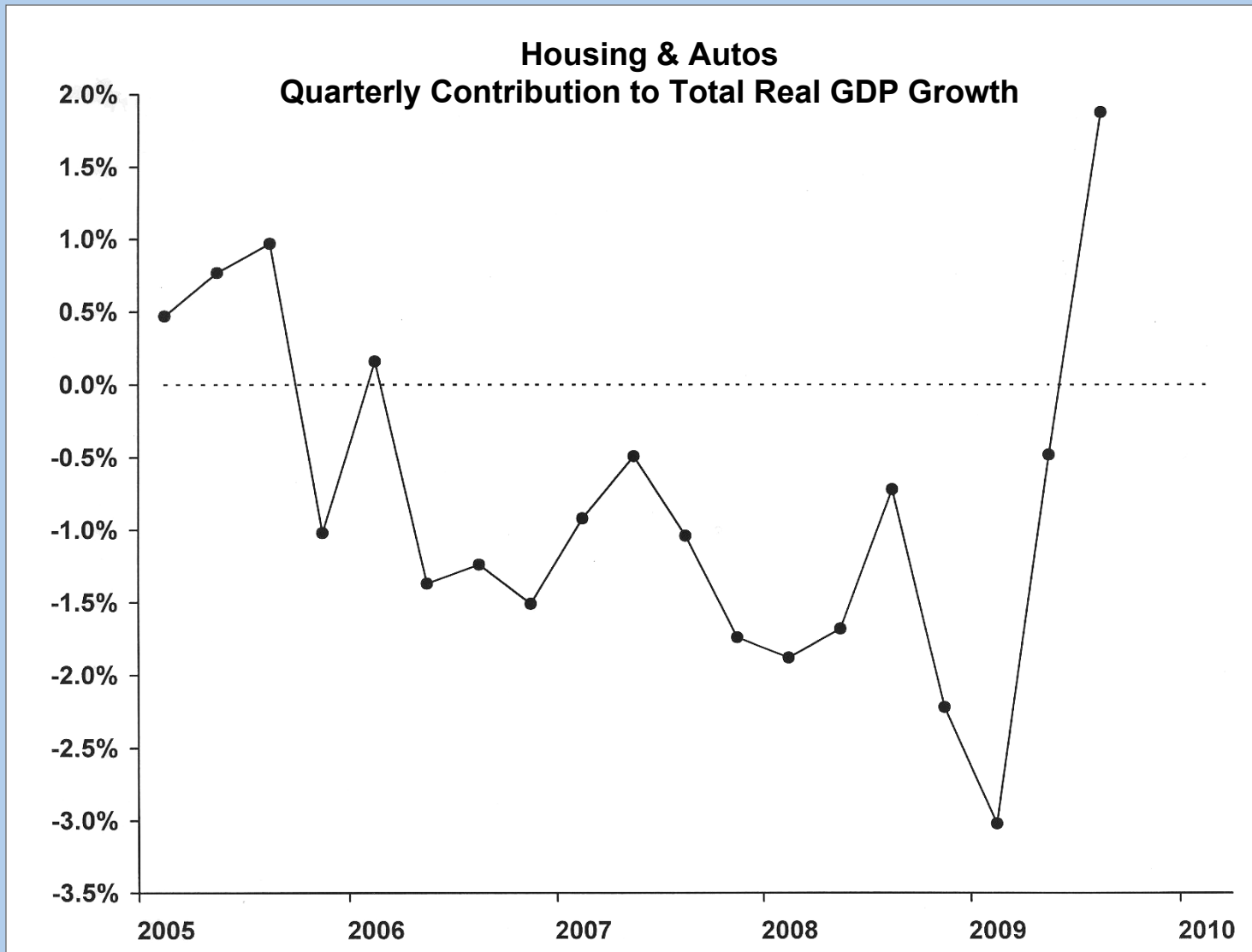
Sidelined Buying Power?

Private-Sector Cash Holdings to GDP Ratio*

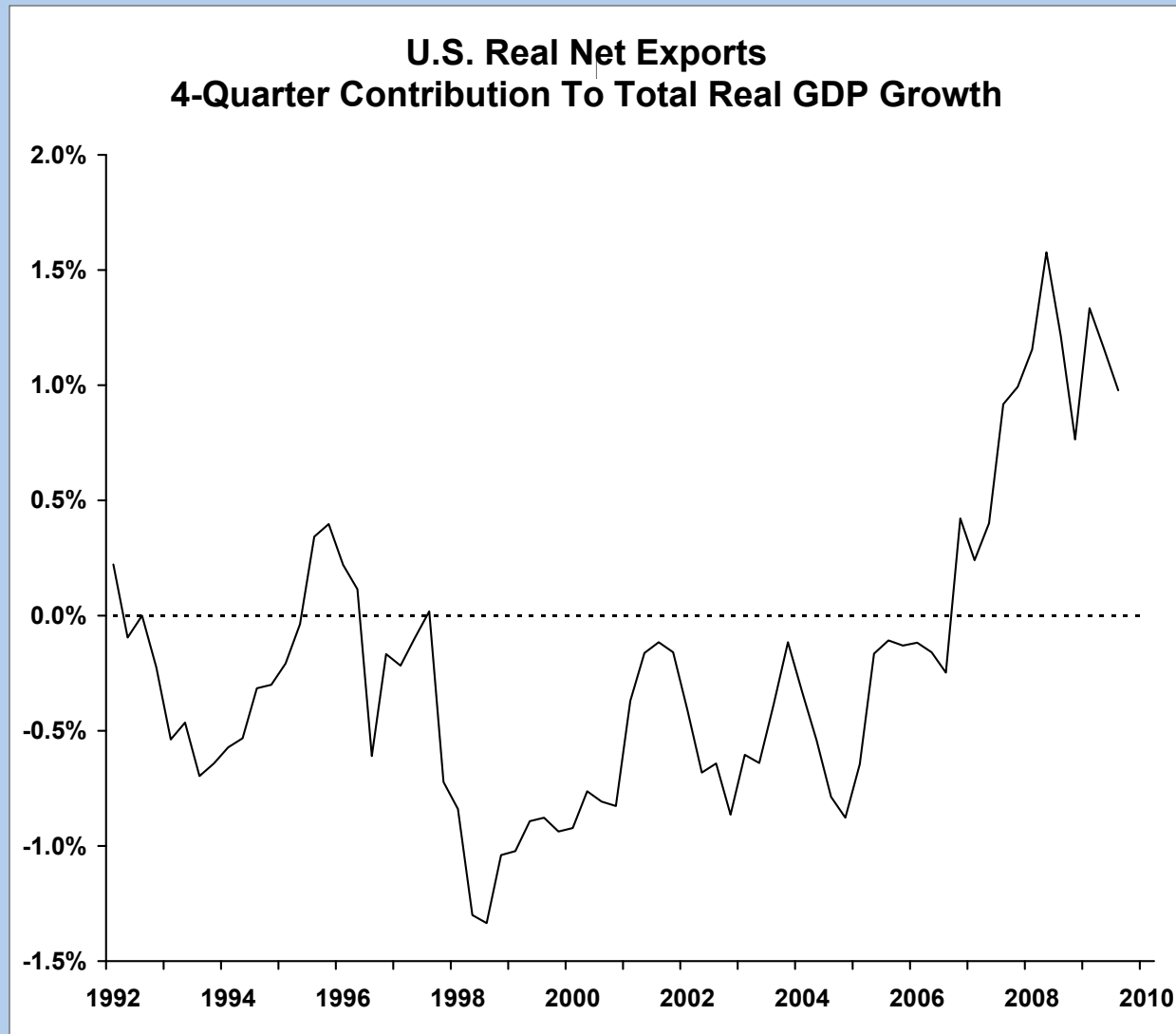
*Sum of cash holdings from Households, NonFinancial Corporations, and NonCorporate Businesses as a Percent of Nominal GDP. Source: Tables B.100, B.102, and B.103 of Federal Reserve Flow of Funds Report (Z.1).



Addition by Less H&A Subtraction!?!?

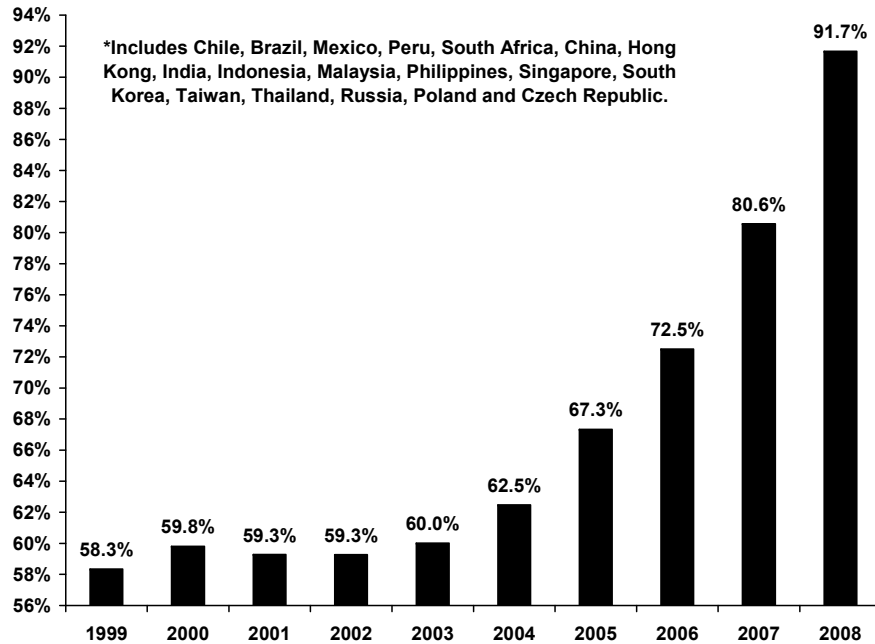


Positive U.S. Trade Improvement!!!

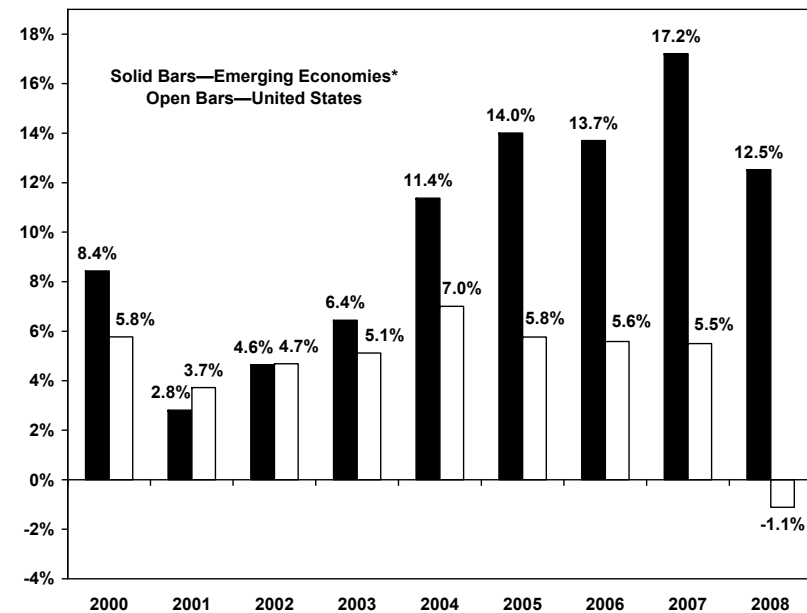


Cloning the U.S. Consumer!!??

**Total Private Consumption Expenditures in U.S. Dollars
Emerging Market Economies* as a Percent of U.S.**



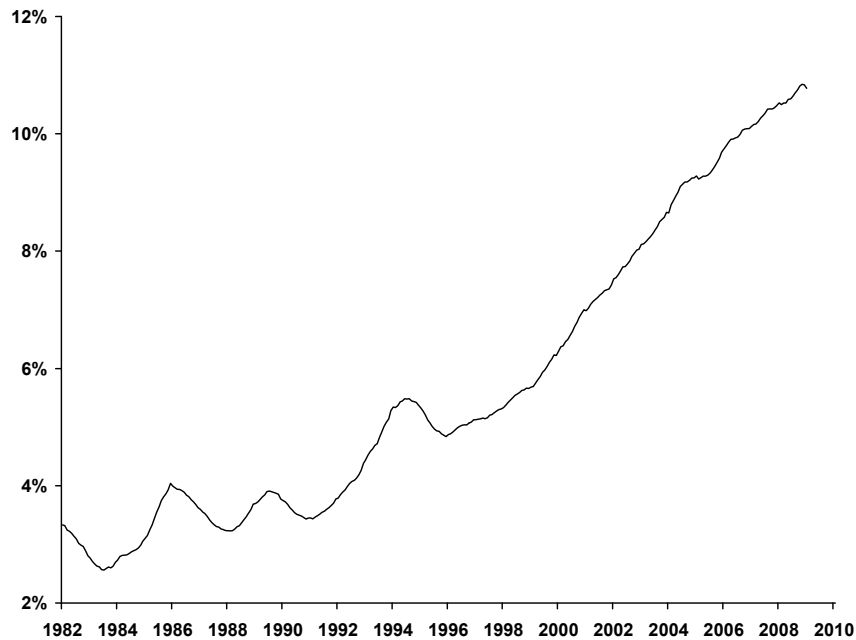
**Annual Growth in U.S. Dollar Total Private Consumption
Emerging Economies* vs. U.S.**



Emerging World Is New Force for Global Growth!!!

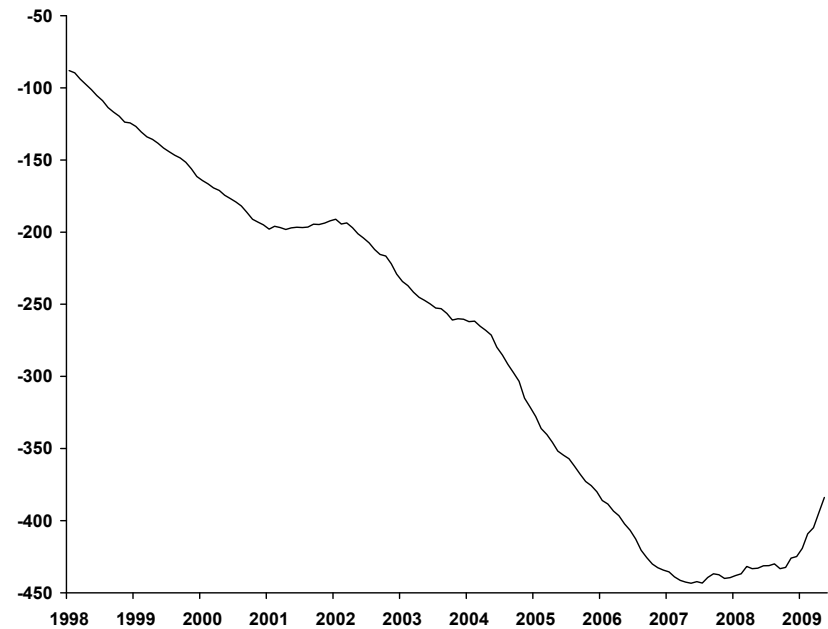
Emerging World "Headliner" Imports as a Percent of Total World Imports*

*Imports from China, India, and Mexico as a percent of total world imports.



U.S. Emerging Markets* Trade Balance

*Trailing 12-month sum of monthly net exports with the 22 countries comprising the Morgan Stanley Emerging Market Stock Price Index. Value is in Billions of U.S. Dollars.

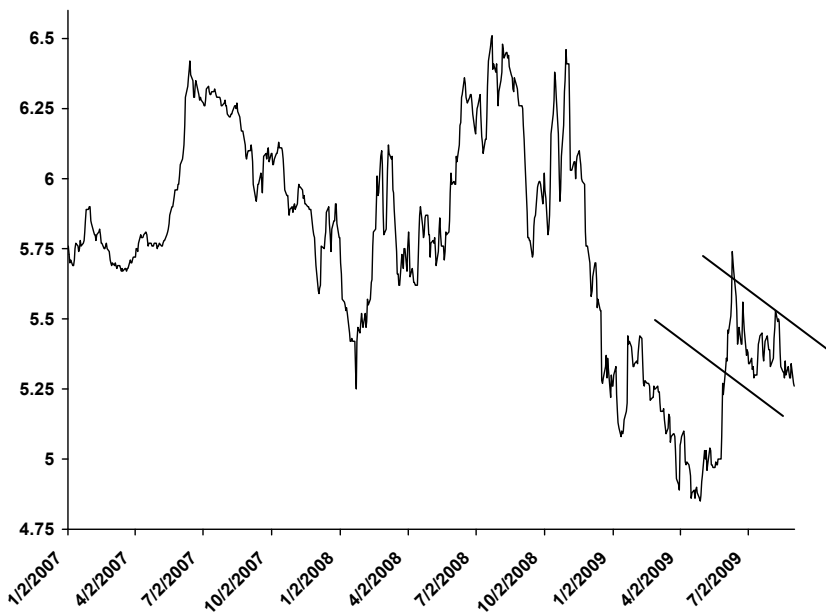


Savings & U.S. Net Exports?

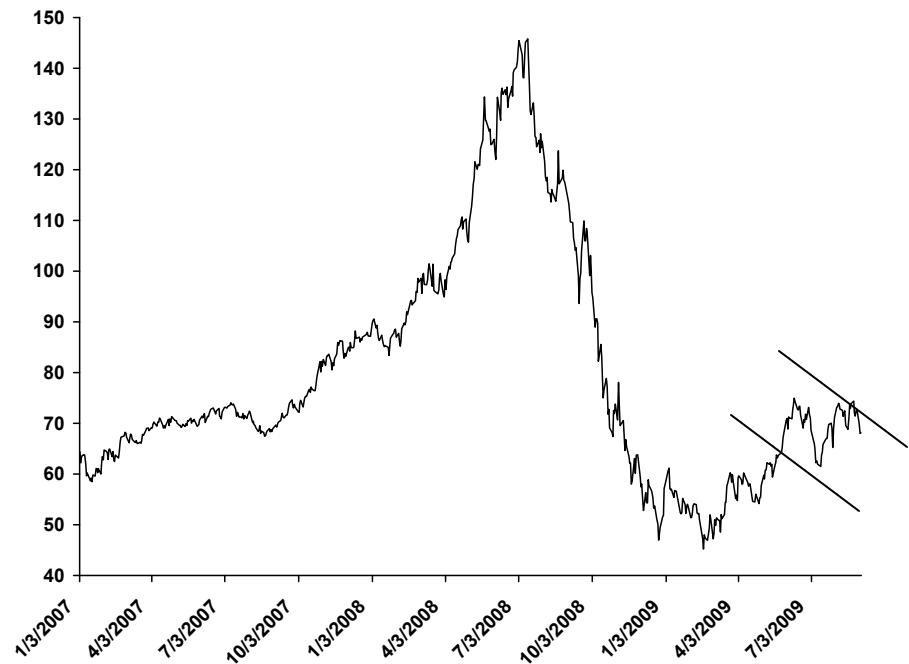


Two Negative Forces Stalled!!!!

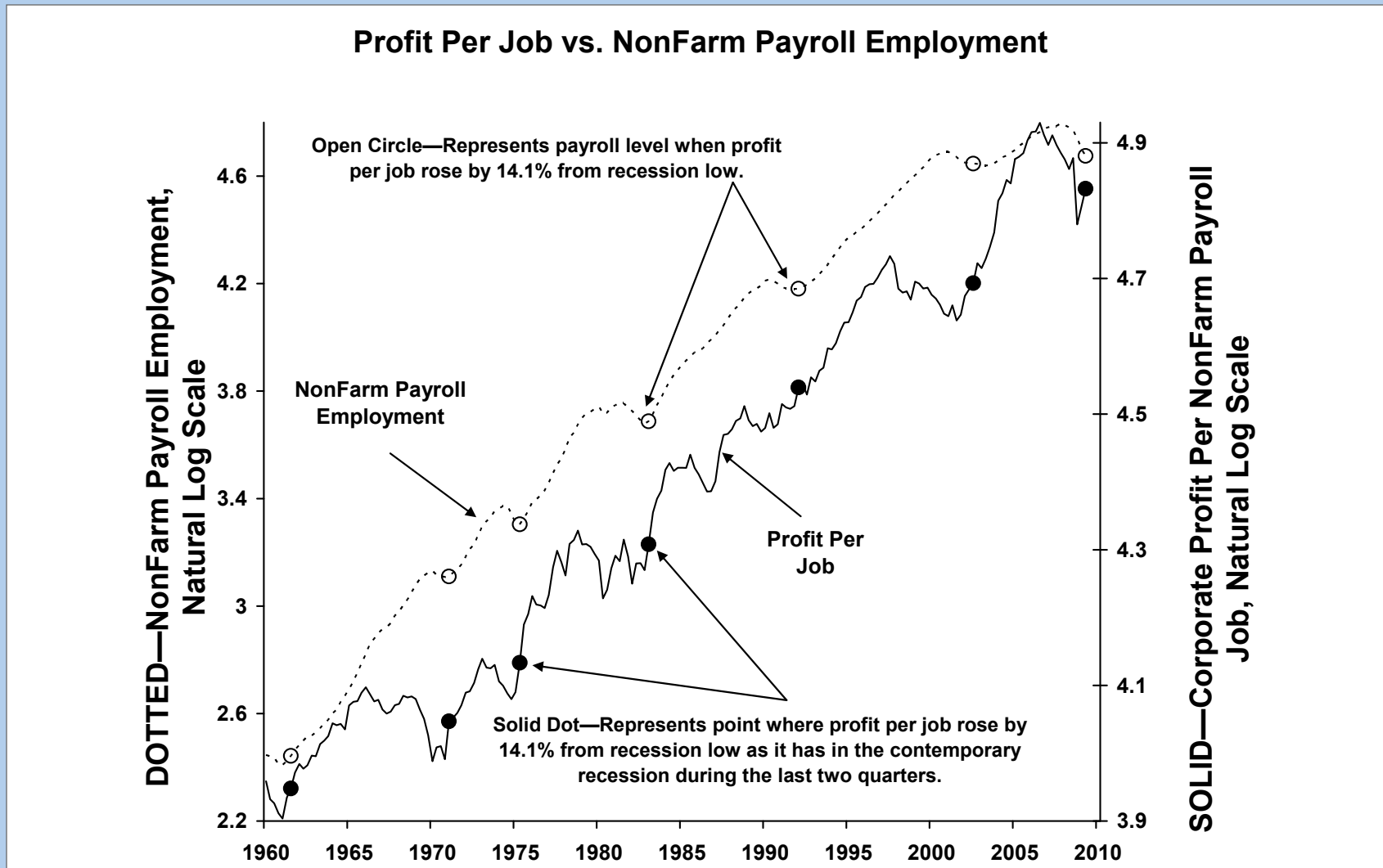
Bankrate's National Average 30-Year Mortgage Rate



Crude Oil Futures



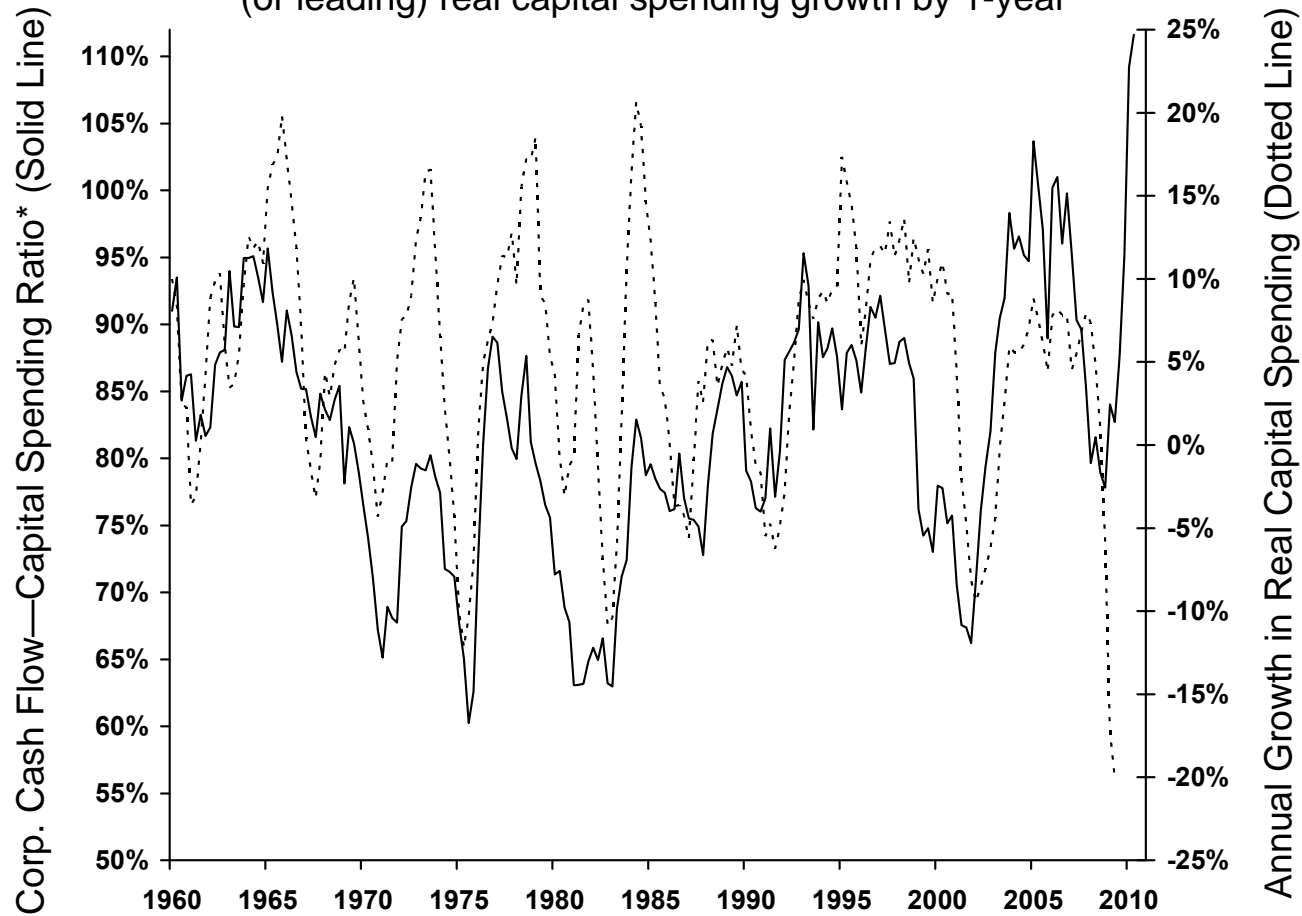
Profits to Rescue Jobs!!??



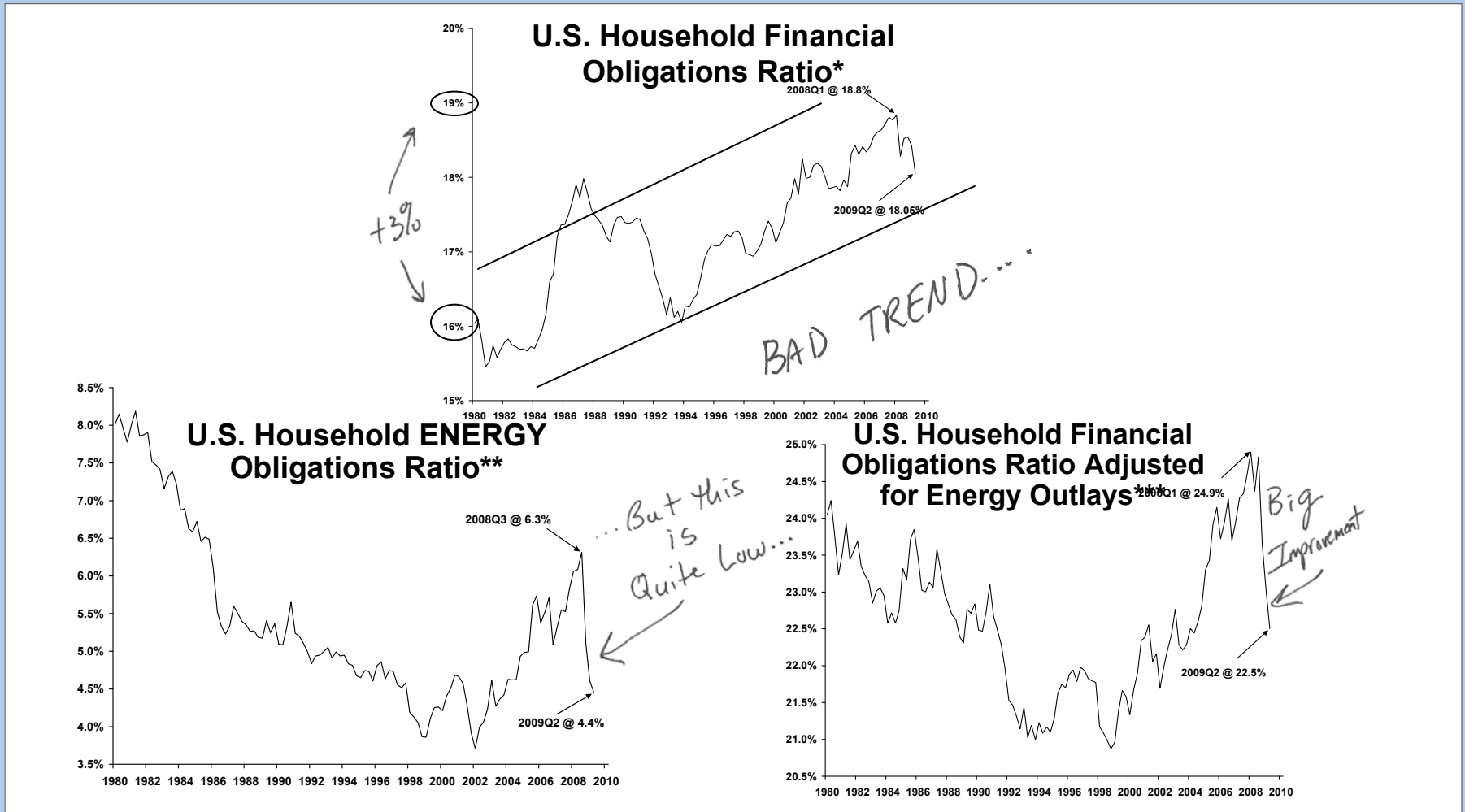
Business-Led Recovery!!!?

U.S. Corporate Cash Flow to Capital Spending Ratio vs. Real Capital Spending Growth*

*U.S. Corporate Cash Flow-Cap Spending Ratio is pushed forward (or leading) real capital spending growth by 1-year



How Bad Is the Household Burden?



*Includes all debt payments (principal and interest) on outstanding mortgage and consumer debt, auto lease payments, rental payments on tenant-occupied property, homeowners' insurance and property tax payments as a percent of Disposable Personal Income.

**Total Household Expenditures on Energy Goods and Services as a percent of Disposable Personal Income.

***Includes all debt payments (principal and interest) on outstanding mortgage and consumer debt, auto lease payments, rental payments on tenant-occupied property, homeowners' insurance and property tax payments AND Total Household Expenditures on Energy Goods and Services. All these outlays shown as a percent of Disposable Personal Income.

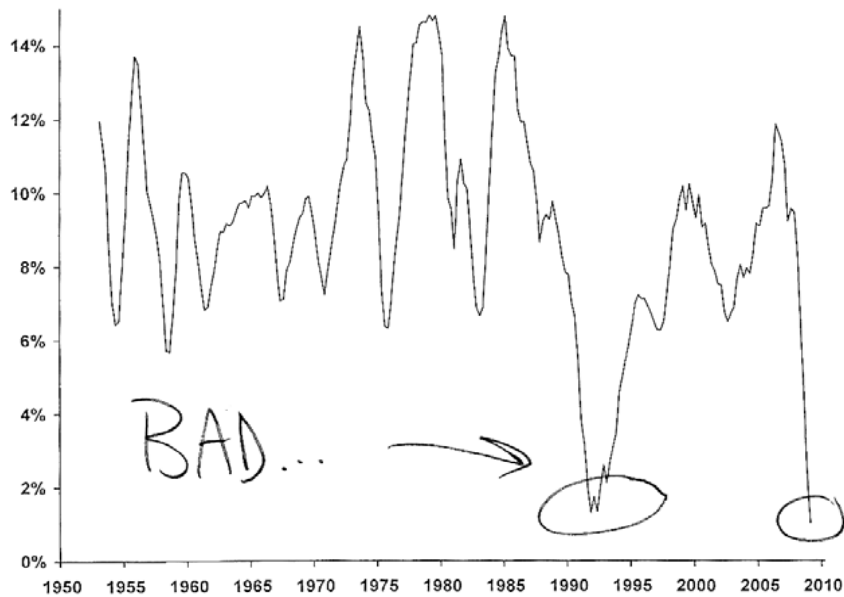
U.S. Household Environment By April 2010!!??

- **Debt/Energy Burden Significantly Improved!**
- **Job Gains For 2 to 3 months!!**
- **HH Net Worth “UP” Four Consecutive Quarters!!!**
- **Positive 401k Statements Four Consecutive Quarters!!!!**
- **Home Prices “UP” For 12 Months!!!!**
- **Consumer Bank Lending Restarts!!!!!!**
- **Record-Low Interest Rates ... AND ... 1% Core Inflation!!!!!!**

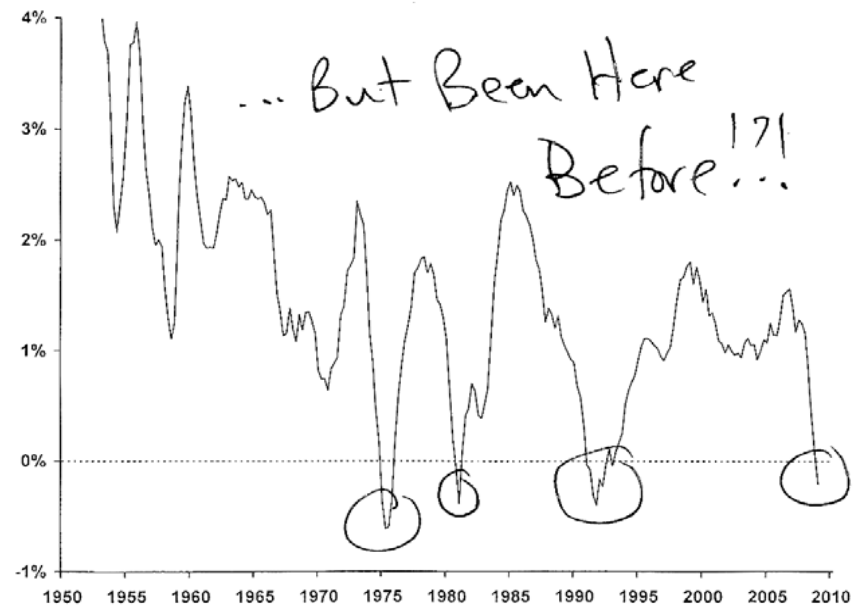


Worst-ever Lending Crisis?

Annual Growth in Total U.S. Private-Sector Debt



Annual Growth in Total U.S. Private-Sector Debt Inflation-Adjusted Growth



2008 CRISIS “The Depression that Wasn’t”!!!!

Legacy Question

**How should public officials manage
Fear/Confidence????**



Half Full ... Or ... Half Empty????

Most Seem Focused On:

- Overindebted/Undersaved U.S. Consumer?
- Aging Developed World Demographics?
- Leftward Shift in U.S.A. Politics/Economy?
- Only Average U.S.A. Equity Valuations?
- Fear/Lack of Animal Spirits?
- A Weak U.S.A. Dollar?

But Ignore:

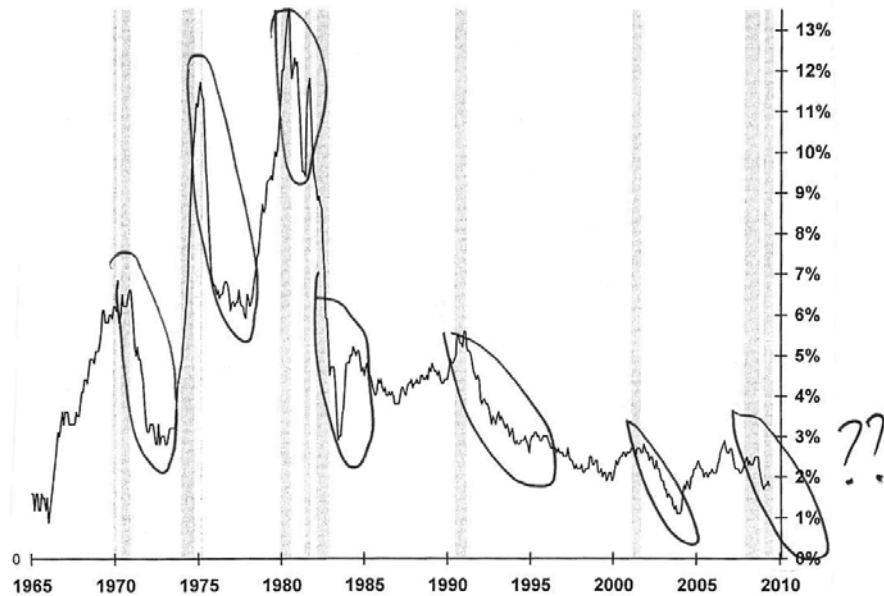
- Newfound Oversaved/Low Debt Emerging World Consumers!
- Young Emerging World Demographic with Ballooning Desires!
- Surge in Free-Market Capitalism about the Globe in Last 10–15 Years!
- U.S.A. Near-Price Stability (Core Inflation ~ 1%) with Record-Low Interest Rates!
- Massive “Dry Powder” on the Sidelines!
- An Improving U.S.A. Global Competitive Position!



Inflation Typically Falls “AFTER” Recessions!?!?

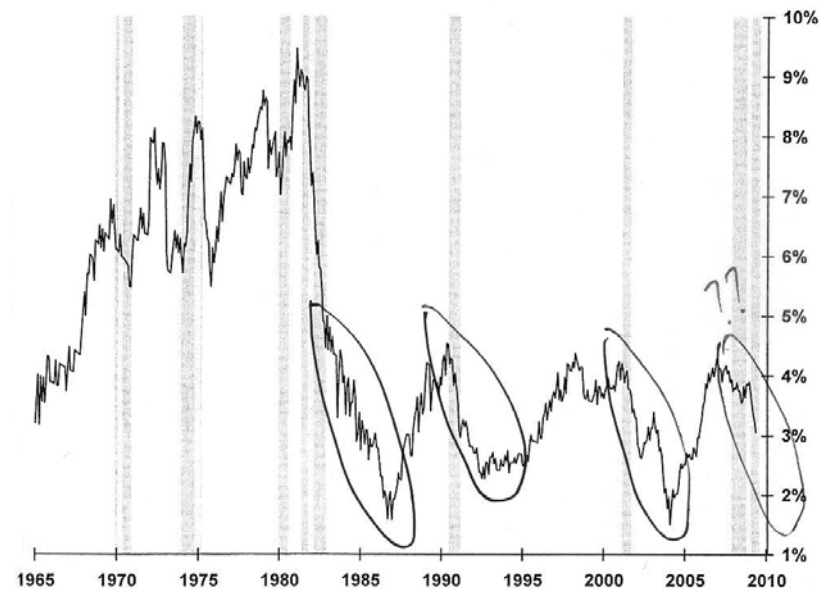
Annual Core Consumer Price Inflation Rate vs. Recessions*

*Shaded Areas Represent Recessions



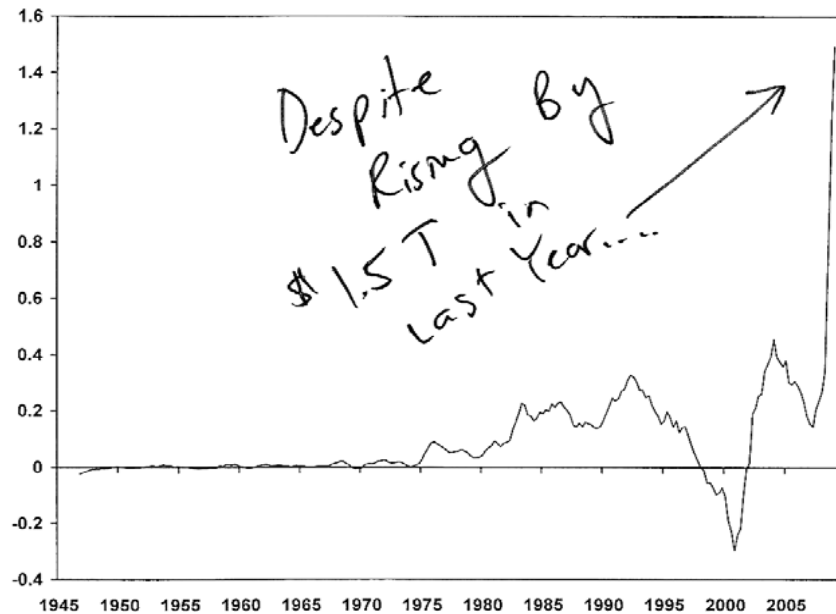
Annual Wage Inflation Rate vs. Recessions*

*Shaded Areas Represent Recessions

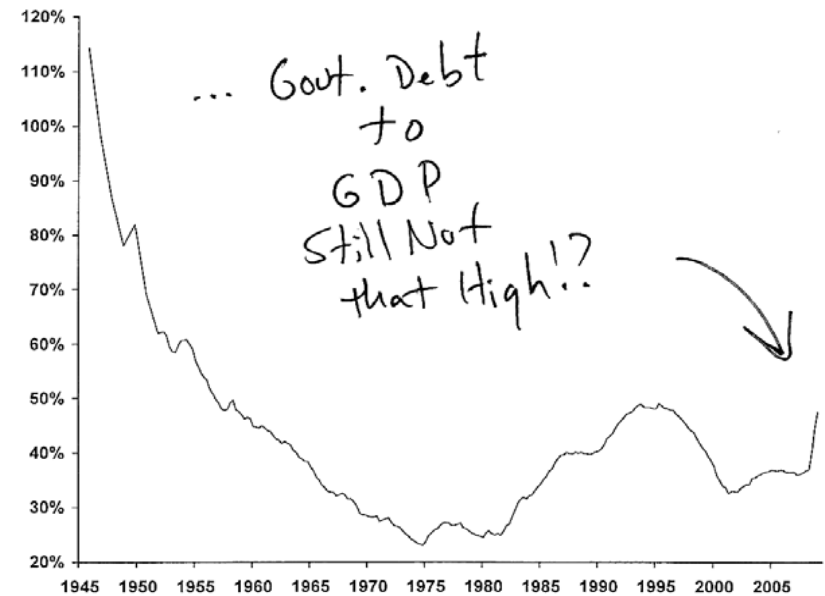


Government Debt Perspective?

Annual Change in Federal Government Debt
in Trillions U.S. \$

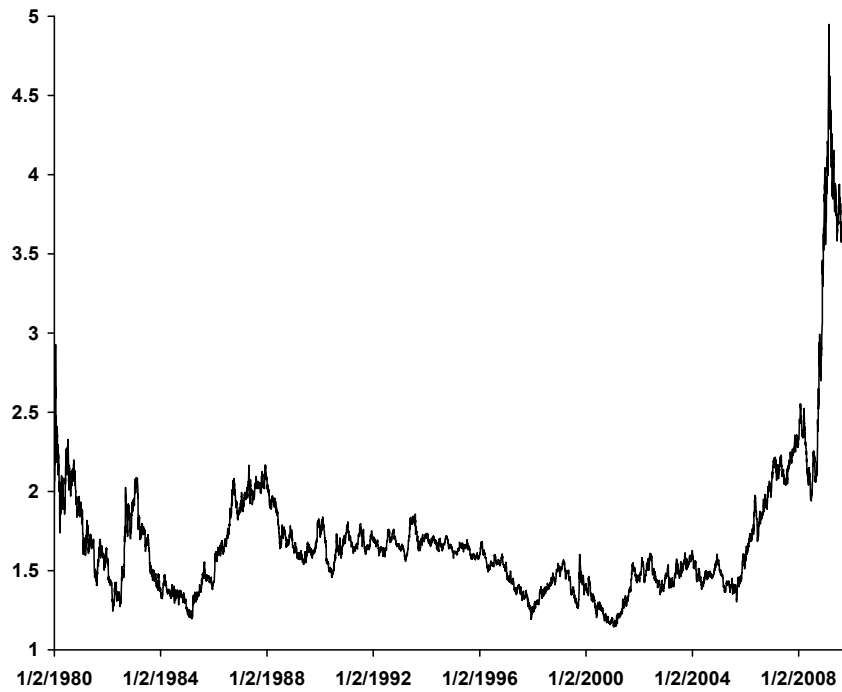


Total U.S. Federal Debt as a Percent of Nominal GDP

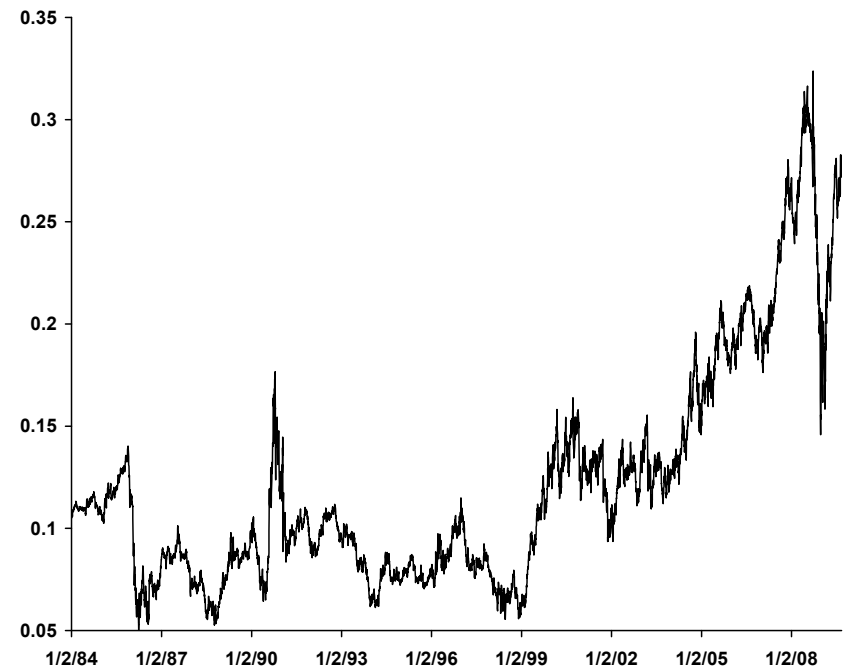


Gold & Oil Both Look Too High!??!

Relative Price of Gold
Price of Gold divided by CRB Commodity Price Index



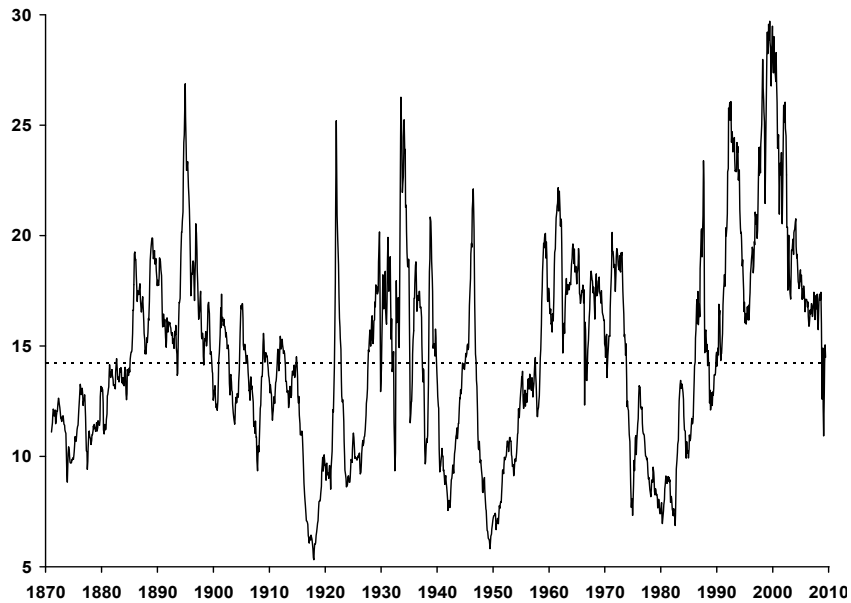
Relative Price of Crude Oil
Price of Oil divided by CRB Commodity Price Index



Valuation?

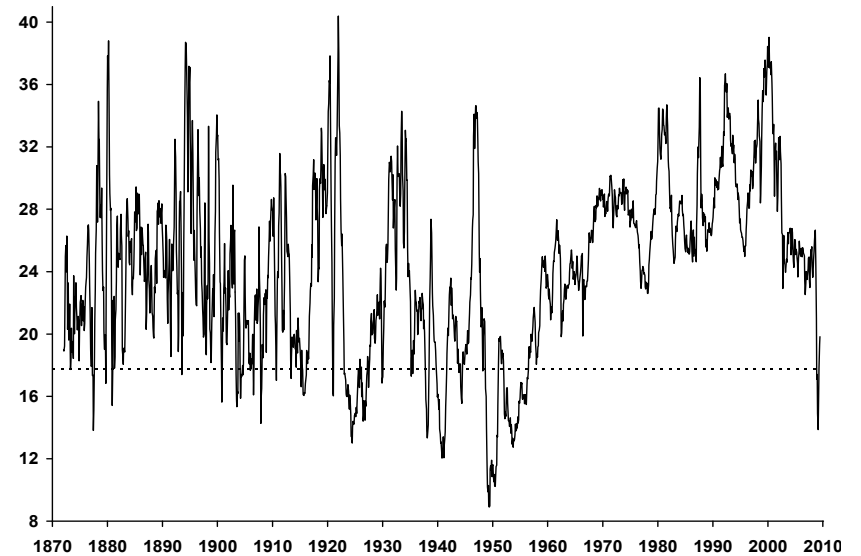
U.S. Stock Market Price-Earnings Multiple*

*Data Sources: Shiller, Bloomberg, and
Commerce Department Macroeconomy Database

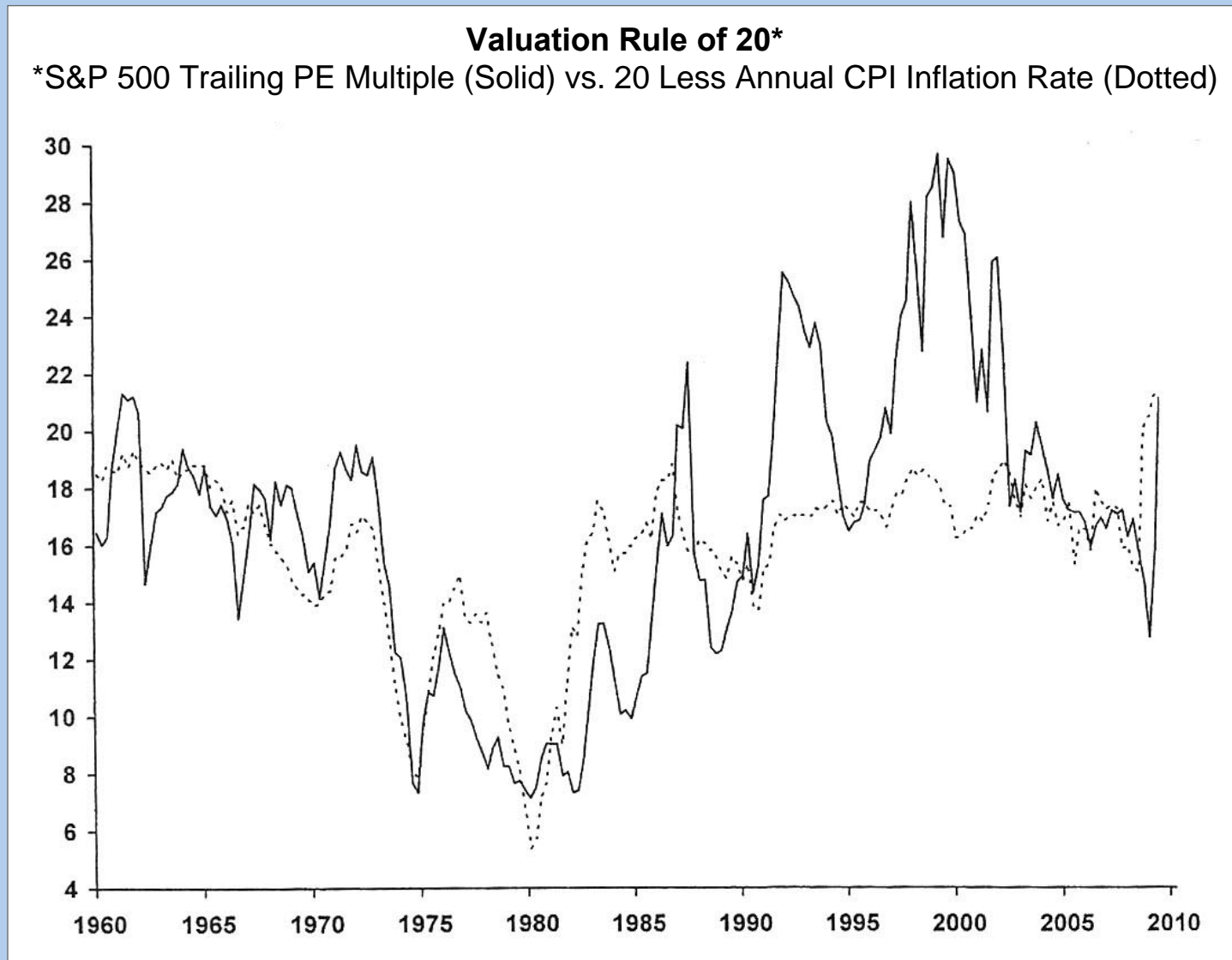


Stock Market Price-Earnings Multiple Adjusted for Inflation/Interest Rate Environment**

**Sum of PE Multiple, the absolute value of the inflation or deflation rate,
and the level of the long-term U.S. Bond Yield



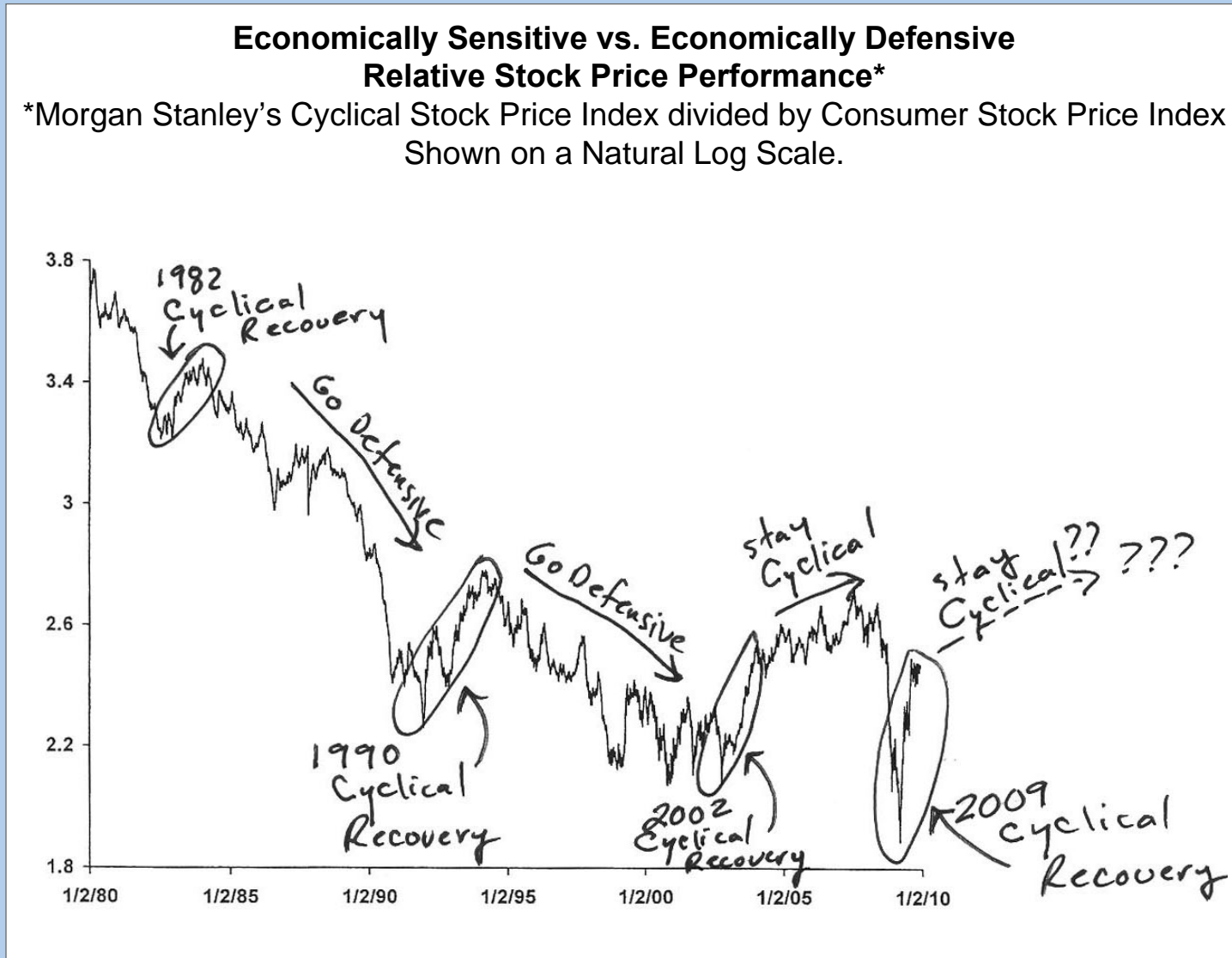
“Rule of 20” Has Worked Pretty Well!??!



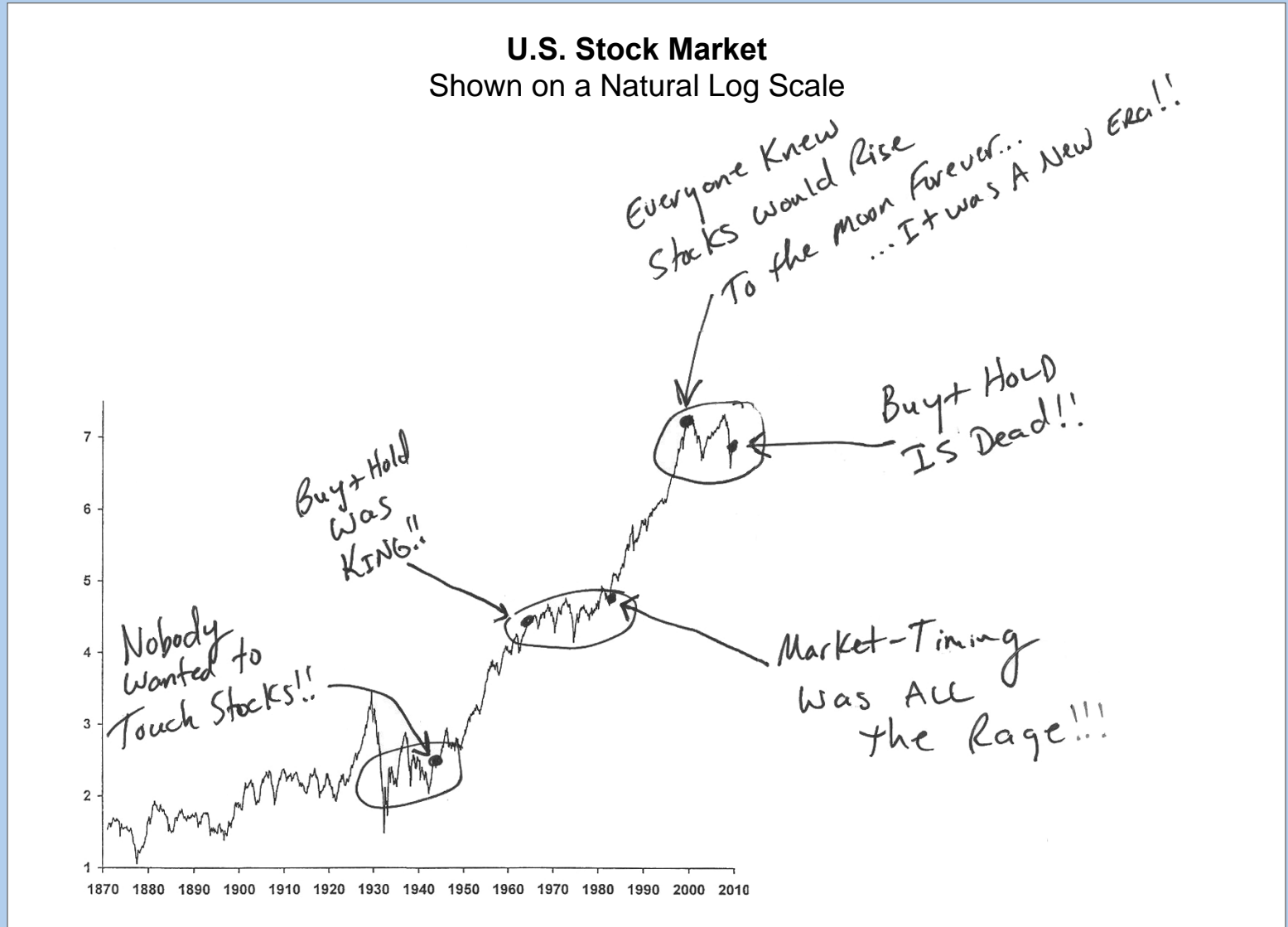
Cyclical Or Defensive????

Economically Sensitive vs. Economically Defensive Relative Stock Price Performance*

*Morgan Stanley's Cyclical Stock Price Index divided by Consumer Stock Price Index
Shown on a Natural Log Scale.



Is "Buy & Hold" Dead???

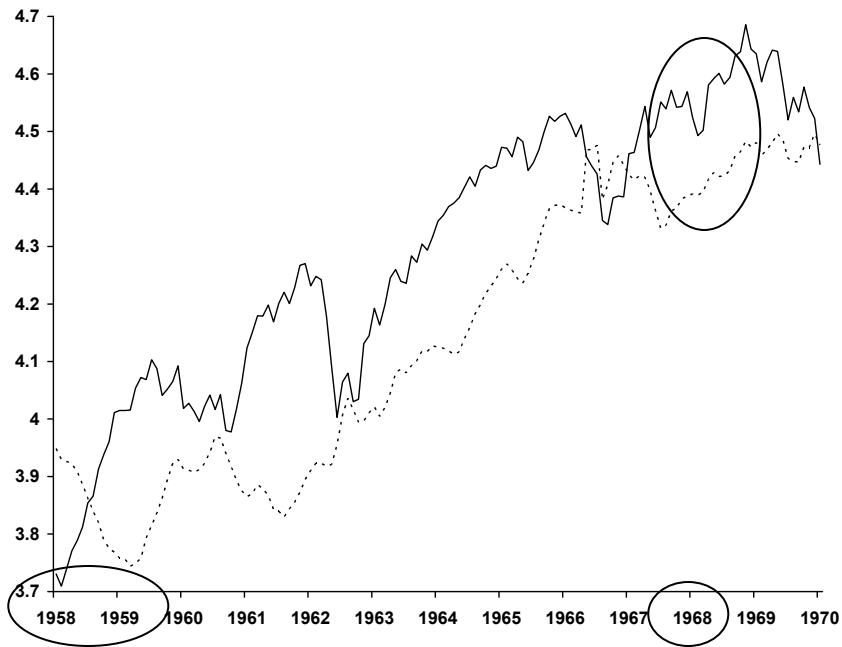


Back to the Future Stock Market???

S&P 500 Composite Stock Index Price vs. Earnings*—1958 to 1970

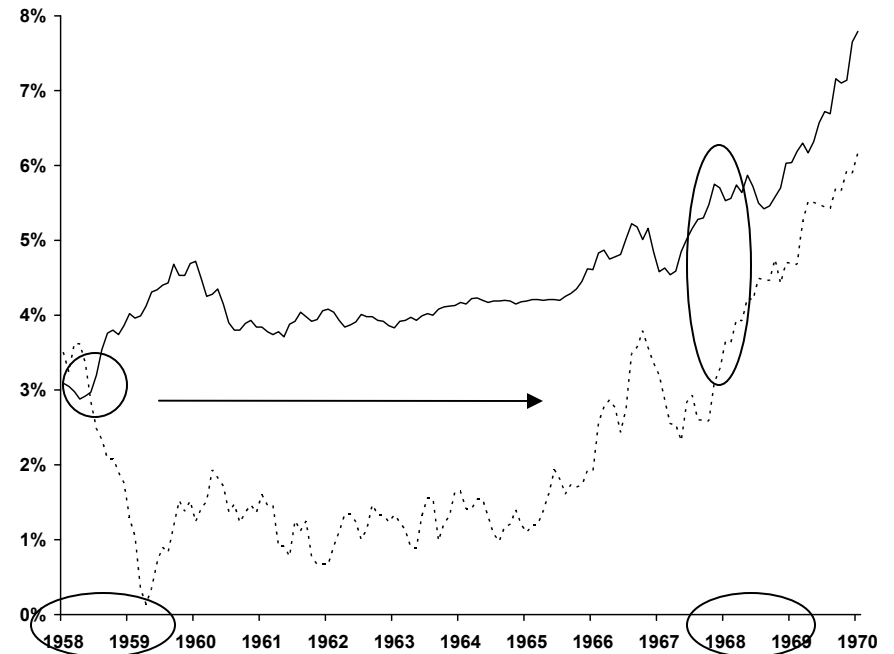
SOLID—S&P 500 Stock Price Index shown
on a natural log scale
DOTTED—Trailing 12-month earnings per share
(3-month moving average)

Dotted line is shown as 15 times trailing earnings per share so that when the stock market
(i.e., solid line) touches the dotted line it is at a 15 price-earnings multiple.

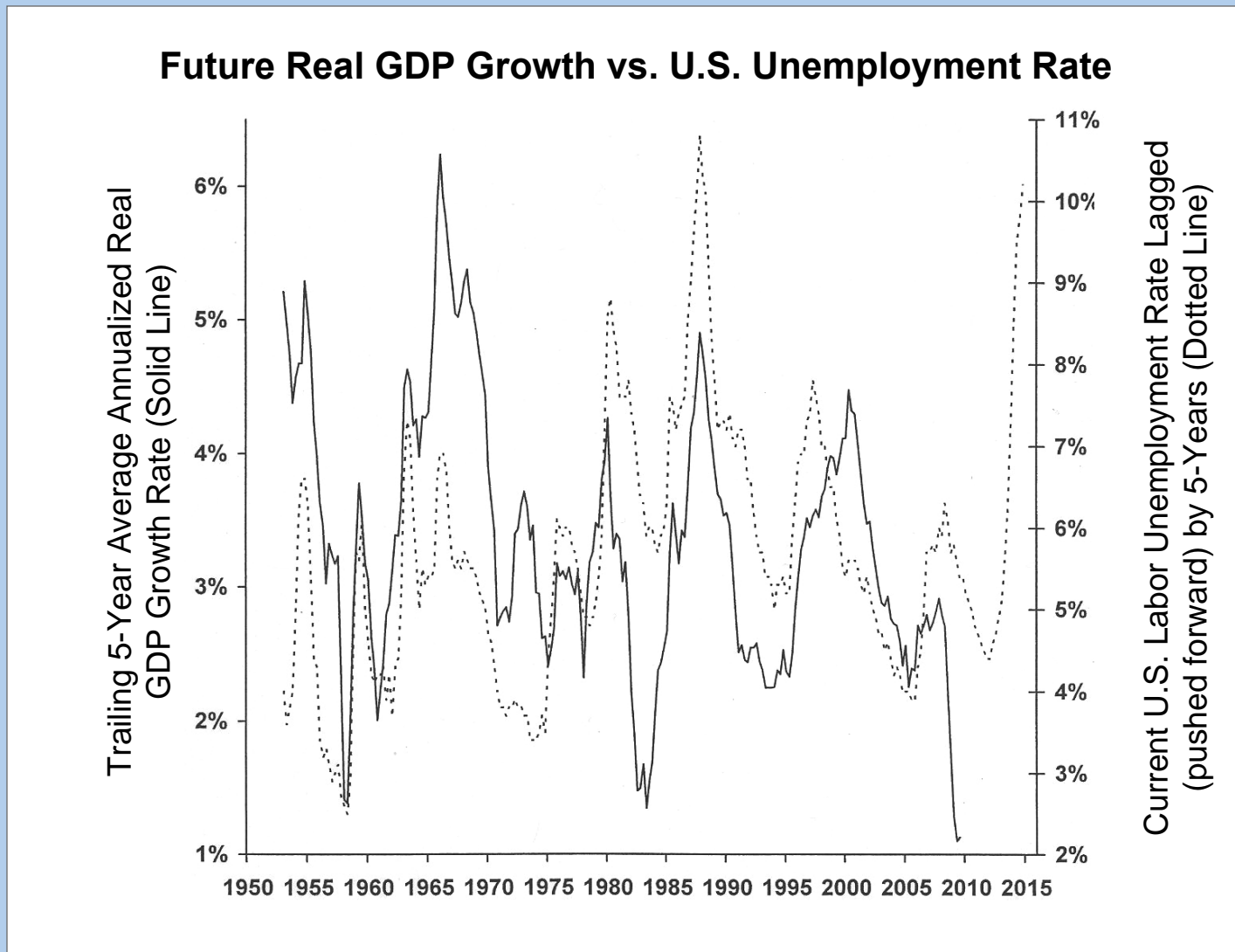


10-Year Treasury Yield vs. Consumer Price Inflation 1958 to 1970

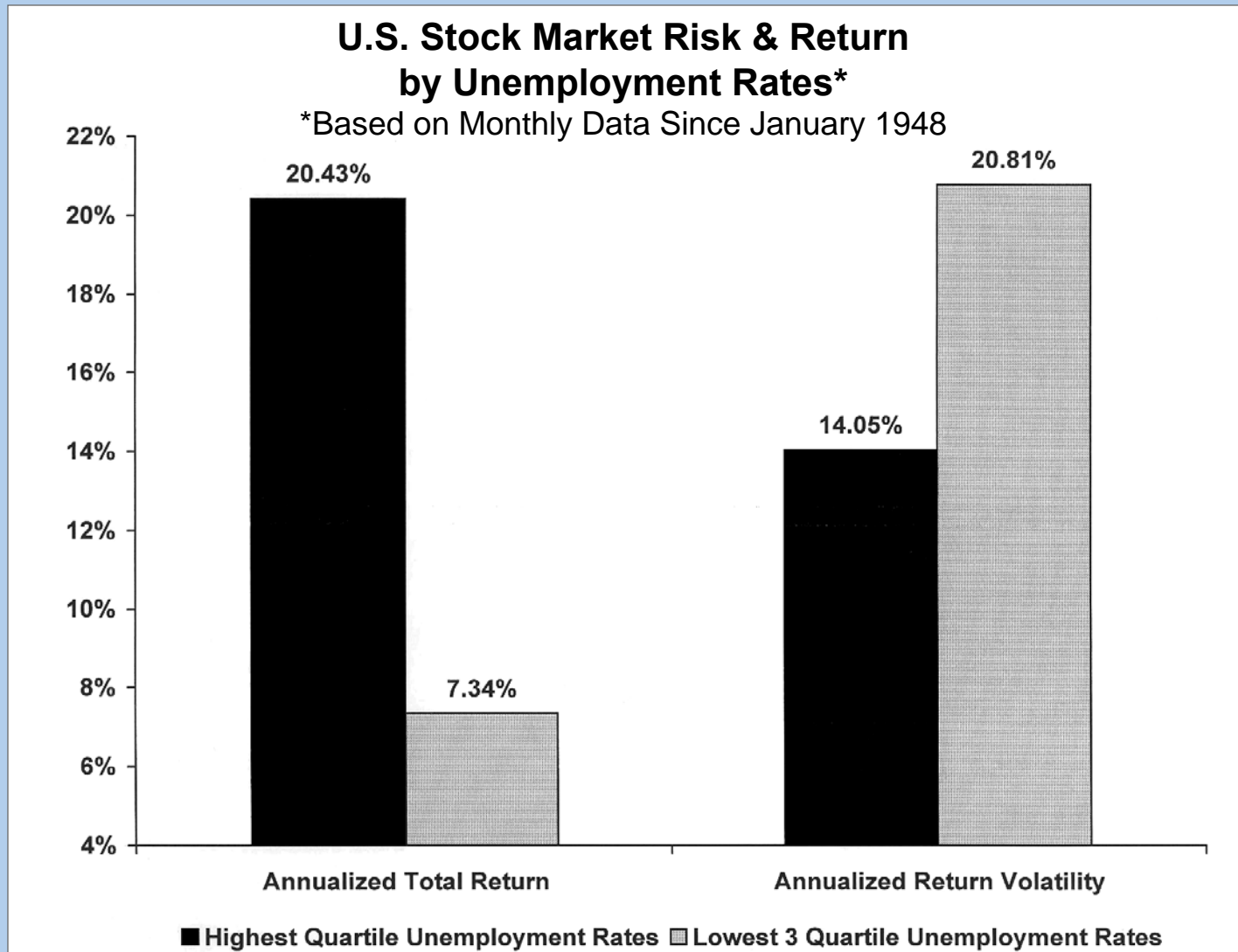
SOLID—U.S. 10-Year Treasury Yield
DOTTED—Annual U.S. Consumer Price Inflation Rate



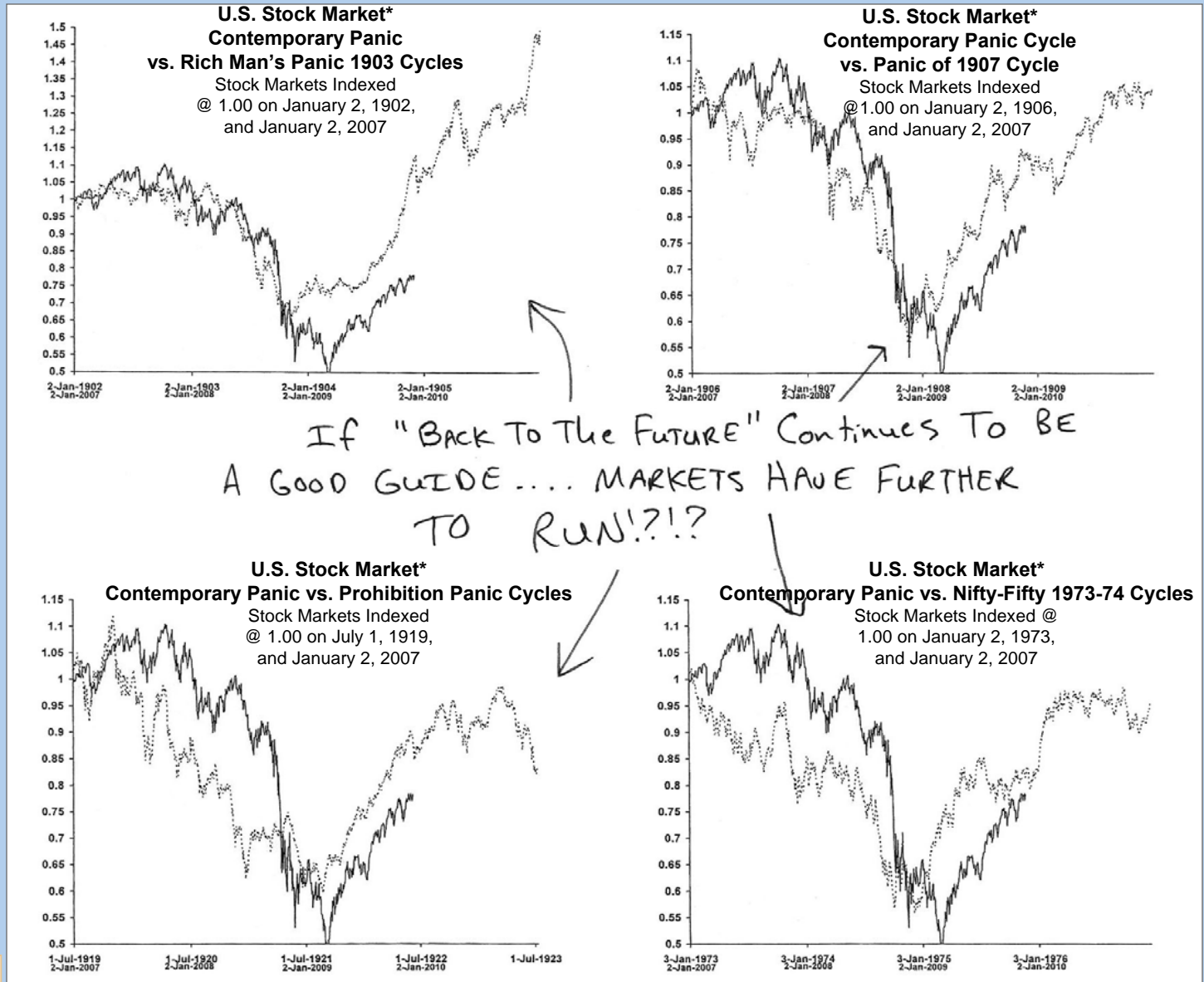
What Falls HARD ????



High Unemployment → Better Stock Market!?!??



The Ghost of Crises Past!?!?



Investors Take Note: “Fear Stronger Than Lust”!!!

“... the limbic system fires up far more intensely when it perceives a danger compared to when it senses a reward. The arousal from danger also comes on faster, lasts longer, and is harder to budge. Even the strongest *toward* emotion, lust, is unlikely to make you run, whereas fear can do so in an instant. The *toward* emotions are more subtle, more easily displaced, and harder to build on, than the *away* emotions. This explains why upward spirals, where positive emotions beget more positive emotions, are less common than downward spirals, where negative emotions beget more negative emotions. Human beings walk *toward*, but run *away*.”

An excerpt from “Your Brain at Work: Strategies for Overcoming Distraction, Regaining Focus, and Working Smarter All Day Long”



Thank You

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