



Personal Wealth Advisory, LLC

Wise strategies for your wealth and your life

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The News You Need to Know

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QUARTERLY ECONOMIC UPDATE

A review of 3Q 2011

THE QUARTER IN BRIEF

The Dow retreated 12.09% in the third quarter of 2011, its poorest quarterly showing since the first quarter of 2009. The debt troubles of a small European nation (and the fear of their contagion) kept U.S. markets down as much as a host of lackluster domestic economic indicators. Confidence waned on Wall Street and Main Street, and analysts began to second-guess the recovery. The real estate sector did show some year-over-year improvement, and consumer spending did not diminish. Investors hoped for better days while taking a pragmatic view of the near future.¹

DOMESTIC ECONOMIC HEALTH

The economy crawled forward, with occasional flashes of vigor. Consumer spending increases partly reflected notable jumps in food and energy costs. Personal spending jumped 0.7% in July and rose another 0.2% in August. Personal incomes actually slipped 0.1% in August, the first time that had happened in nearly two years.^{2,3}

As for consumer prices, they rose 0.5% in July and 0.4% in August after decreasing 0.2% in June. By August, annualized inflation was running at 3.8%; energy prices had risen 18.4% in 12 months. Retail sales rose 0.3% in July but were flat in August. Commerce Department data showed durable goods orders at an impressive +4.1% in July but just -0.1% for August.^{4,5,6}

The jobless rate remained stuck at 9.1% in July and August. By August, it had been 9% or higher in every month since May 2009. Consumer confidence plunged, with a mild rebound late in the quarter. The final September University of Michigan survey improved to 59.4, rebounding from the lowest level since November 2008 in August (55.7). The Conference Board's September number of 45.4 was little changed from the 45.2 of August (lowest since April 2009).^{3,7}

Upcoming Events

2011 Investment Summit

This event will cover the recent market volatility and current investment strategies for managing your portfolio in response to the ever-changing market conditions.

**Wednesday
November 2nd, 2011**

Session I
10:00 a.m. to 11:30 a.m.
or

Session II
7:00 p.m. to 8:30 p.m.

Location:

The Conference & Training
Center at IU 13
1020 New Holland Avenue
Lancaster, PA 17601

To register:

Please contact Pam Snow at
717-735-1170 or
psnow@pwallc.net
by October 26th

Seating is limited.

Mission:

*To help our clients make
wise financial decisions so
they can reach their personal
goals within the framework
of their values.*

Some of this was frustration over Washington. After the long debate in Congress regarding the nation's debt ceiling, Standard and Poor's downgraded America's credit rating a notch to AA+, which was detrimental to global stocks. President Obama called for bipartisan unity as he introduced the \$447 billion American Jobs Act late in the quarter, but some Republicans were loath to support a job creation measure that would be funded partly by income tax hikes. (In early October, Senate Democrats proposed including a 5% tax hike for millionaires in the bill.) The Federal Reserve did not haul out QE3, instead choosing to bring back its 1961 "Operation Twist" strategy of shifting \$400 billion into longer-term Treasuries to foster growth, a move that kicked off this month.^{8,9,10,32}

The Institute for Supply Management's manufacturing and non-manufacturing indices hinted at slower growth. ISM's manufacturing gauge read 55.3 in June, but just 51.6 by September; its service sector index was at 53.3 in June and managed a 53.0 reading for September.^{11,12}

GLOBAL ECONOMIC HEALTH

Hopes that Greece could avoid default seemed to fade as the quarter proceeded, with some economists contending it wasn't a matter of if but when. Wall Street hoped for decisive action from the European Union this summer, maybe even a revamp of its business model; that didn't happen. In August, German chancellor Angela Merkel and French president Nicolas Sarkozy proposed that all 17 EU nations write and pass constitutional balanced-budget amendments, and called for an EU-wide tax on financial transactions in 2012 and a joint-governance council that would meet twice yearly to try and fine-tune the Eurozone economy. Wall Street would have preferred that the EU create a Eurobond that could help cut borrowing costs for debt-plagued nations or bolster its bailout fund. At quarter's end, the EU was voting on whether to strengthen the bailout fund, but its leaders had thrown out a measure that would allow management of the euro via a council of heads of state instead of a central bureaucratic arm.^{13,14}

Asian economies contended with a clear drop in export demand. China's official PMI was at 50.9 by September, exactly where it was in June and well below the historical 55.7 average for the month. Japan's manufacturing sector contracted in September for the first time since April. Taiwan's manufacturing index contracted each month of the quarter, hitting a 32-month low of 44.5 in September; India's PMI dropped 2.2% to 50.4 in that month, its biggest monthly retrenchment since November 2008. One silver lining here: this slowdown could help to foster a soft landing for the Chinese and Indian economies, in which inflation exceeds central bank targets.¹⁵

WORLD MARKETS

The descents were severe. Data from Morningstar (in USD terms) tells the story: Sensex, -11.40%; CAC 40, -25.12%; FTSE 100, -13.74%; Hang Seng, -21.26%; Nikkei 225, -11.37%; All Ordinaries, -12.66%; TSX Composite, -11.39%; Shanghai Composite, -14.59%; DAX, -25.41%. The MSCI World and Emerging Markets indices respectively dropped 17.06% and 23.19% last quarter.^{16,17}

COMMODITIES MARKETS

At the end of the quarter, gold was the only precious metal posting a YTD gain (+14.1%) on the heels of its twelfth straight quarterly advance (+7.86%). Other marquee metals had it rough in the quarter: silver lost 13.6%, platinum fell 11.7%, palladium dived 19.2% and copper plunged 26.0%. Soybeans lost 9.7% in 3Q 2011, and the Dow Jones-UBS Commodity Index took an 11.3% quarterly hit. NYMEX crude lost exactly 17% on the quarter, with prices settling at \$79.20 a barrel on September 30. As for the U.S. Dollar Index ... it gained 5.7% for the quarter.^{18,19,20,21}

REAL ESTATE

The sector was far from healed, but there was some annualized improvement. While new and existing home sales wavered month-to-month, August data showed them respectively 18.6% and 18.8% above year-ago levels (existing home purchases unexpectedly were up 7.7% in August). By August, pending home sales also registered a 12-month gain (+7.7%). The latest available S&P/Case-Shiller Home Price Index (July edition) still showed prices down 4.1% year-over-year.^{22,23,24,25,26}

Mortgages grew even cheaper. Freddie Mac's Primary Mortgage Market Survey showed the following quarterly descents in average interest rates from June 30 to September 29: 30-year FRMs, 4.51% to 4.01%; 15-year FRMs, 3.69% to 3.28%; 5-year ARMs, 3.22% to 3.02%; 1-year ARMs, 2.97% to 2.83%.²⁷

LOOKING BACK...LOOKING FORWARD

Standing alone, the 3Q numbers might look like a bad Wall Street year. It was a quarter in which the Russell 2000 (-22.15%) tumbled into a bear market and the CBOE VIX (+159.32%) took off.¹

% CHANGE	Y-T-D	3Q CHG	1-YR CHG	10-YR AVG
DJIA	-5.74	-12.09	+1.16	+2.35
NASDAQ	-8.95	-12.91	+1.97	+6.32
S&P 500	-10.04	-14.33	-0.86	+0.89
REAL YIELD	9/30 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.17%	0.75%	2.27%	3.50%

Sources: cncb.com, bigcharts.com, treasury.gov, treasurydirect.gov - 9/30/11^{1,28,29,30}

Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly.

These returns do not include dividends.

On October 4, the S&P 500 was flirting with bear market territory (down 19.4% from its April 2011 high). So what will have to happen to help this market climate improve this fall? There are three potential catalysts that might emerge. One, a decisive and truly unified effort by the EU to address the debt crisis in Greece, Spain and Italy and arrange an orderly default for Greece. Two, a strong corporate earnings season featuring frequent, pleasant surprises. Three, a stream of data vouching that the economy is still growing – indicators that clearly do not hint at a recession. As you may know, the fourth quarter tends to be a very good one for Wall Street: across the last 50 years, stocks have gained an average of 3.6% in the last three months of a year. Investors are clearly hoping the historical pattern repeats in 2011.³¹

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