111309 Does This Make Sense?

By Gary Case

I find the recently reported quarterly profit by Ford Motor and this past Friday's headlines regarding the employment rate rising above 10% to be an interesting juxtaposition. It seems that Ford was able to produce a profit of around $1 billion while still losing somewhere around $800 million. How did they pull this off? Although I haven't read the financial reports in detail, it would appear that Ford accomplished this in part by taking advantage of the "Cash for Clunkers" program and by reducing costs associated with employees—translated "layoffs". Ford stockholders can indeed rejoice but former Ford employees may not be joining the party. Ford deserves kudos for refusing government aid through TARP, although Cash for Clunkers sort of feels like a government stimulus program. It seems as though Ford and many other companies are able to report positive earnings based on cost cutting measures and government intervention into the American business landscape.

Like Ford, many of us are delevering our balance sheets, trying to eliminate debt, perhaps saving more, and generally trying to spend less. Banks are trying to help us in this endeavor by limiting credit and generally discouraging the use of credit by raising interest rates on consumer (if not mortgage) loans. Small businesses and commercial real estate businesses generally seem to have limited access to capital. Indeed, it would appear that there are savvy investment and retail banking firms waiting for commercial real estate prices to erode to a level that allows profitable entry into that market. Never mind that those same institutions were formerly the main source of financing for the very ventures that will be purchased for pennies on the dollar. It must be tremendously difficult to accurately assess the risk of lending money to troubled ventures.

Sarcasm partially aside, I have rarely seen such diversity among credible observers while interpreting data from the economy and markets. Certainly things are different this time if only in the magnitude of change and the variety of opinions regarding our current state and projections regarding the future of economies and markets. The difference of opinion from supposedly informed market observers makes it difficult for savers and investors to position their portfolios. While the recent rally in risk assets is stunning in its magnitude and timeframe, the memory of the fourth quarter of 2008 is still painfully etched in our memory. However, that quarter will soon be a full year behind us which will allow one-year performance figures to look great! The tradeoff between long-term average returns and the impact of the sequence of returns has never been more stark, and controversial.

Good counsel for investors at this juncture would be to listen carefully to what is being said; but further, determine who is talking and what their agenda could be. Whose benefit are the comments serving, and what are the conflicts of interest inherent to the speaker and the message.