JUNE MARKET COMMENTARY

By Tom Crow

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		Gain (Loss) by Period			
Index	**Month End**	**Month**	**Most Recent Quarter**	**Year-to-Date**	**Trailing Twelve Months**
Dow Industrials	12,414	(1.2%)	0.8%	7.2%	27.0%
S&P 500	1,321	(1.8%)	(0.4%)	5.0%	28.1%
Nasdaq	2,774	(2.2%)	(0.3%)	4.6%	31.5%

The markets finished June with several strong days, but it wasn't enough to overcome the deep selloff from a couple of weeks earlier. The second down month in a row was enough to pull the most-recent quarter data for the S&P and the Nasdaq negative, with the Dow holding onto less than 1% gains for the quarter. The volatility index spiked from around 18 to almost 23, but has since pulled back to less than 17 and appears to be in a downward trend.

According to some analysts, the end of QE2 (Quantitative Easing 2) was also supposed to be the end of the US stock market. The same analysts said the strength of the last three days of June was nothing more than end-of-the-quarter window dressing by mutual fund managers. Just to prove the analysts wrong, July 1st was a stronger day than any of the four preceding; pushing the Dow back above 12,500 and even lifting the precious metals off their lows earlier in the day.

All the talk about volume drying up towards the end of the month was also not backed up by the numbers as June 29th and 30th were two of the month's highest-volume days. As impressive as the 5% recovery from the mid-June lows is, at 1,321 the S&P still has 3% to climb to get back to the late-April highs, and almost 15% to recover the October 2007 peak at over 1,550.

Gold and silver were in what most analysts were calling a long-overdue correction, but most are still bullish and predicting higher prices before the end of the year. Technicians say we haven't hit the target bottom yet while others say emerging-market demand for the metals will provide price support at or near the current level. The flood of investors back into metals following Moody's downgrade of Portugal seems to support that.

In last month's Commentary we said May's employment numbers were "awful." Q: What's worse than awful? A: This month's numbers.

The ADP private payrolls data on Thursday had analysts expecting 125,000 jobs created in June. They missed by just a little. The private sector added only 57,000 jobs and 39,000 government jobs were lost, resulting in 18,000 net jobs created. Further, May's "awful" number of 54,000 was revised lower to 25,000. And, don't forget, last month March and April's numbers were revised lower too.

The unemployment rate ticked higher to 9.2%, from 9.1% last month. In earlier Commentaries, we've said a rising unemployment rate was not necessarily a bad thing if it were occurring while jobs were being created in excess of 250,000/month because it would mean lots of folks were returning to the workforce. What we have here is the worst of all situations. The economy is not creating enough jobs to keep up with population growth and the unemployment rate is rising. It is now the highest it's been this year, so far.

Wholesale inventories also increased meaning even though we put some folks back to work making stuff, nobody's buying it. If July and August bring similarly dismal reports, a lot of analysts will be scrambling to revise their predictions and projections of a late 2011 recovery.

More mixed messages from the housing sector. The 12% drop in pending home sales in April followed through as sales dropped in May to the lowest level since November. The median price of a home sold was also down 4.6% from this time last year. Inventories dropped about 1%. I wish we could say that's because houses are being sold, but it's more likely some are being taken off the market, and fewer are being added. We are still feeling the effects of a backlog of short sales and foreclosures keeping a lid on price recovery.

The housing situation may be one of the biggest hurdles for the struggling economy to clear. For investors who gobbled up houses with easy money, the situation is unfortunate, but such is the risk of investment and speculation in any market. For individuals and families who only own one home and need to sell it, or need to be able to pull equity out to finance education or other major purchases, appraisal values that continue to decline can be devastating. Either years' worth of equity has been wiped out, or they recently bought near the peak and are now trapped, upside-down in their single-largest investment.

The Fed met week before last. Back in January, their estimate for US GDP growth in 2011 was between 3.4% and 3.9%. After April's meeting they cut that to 3.1% to 3.3%. Last week it was cut again to between 2.7% and 2.9%. The April estimate for 2012 GDP growth was 3.5% to 4.2%. It is now between 3.3% and 3.7%. Their estimates for inflation and unemployment were also increased.

The Fed also said they intended to keep rates very low, between 0.0% and 0.25% for "an extended time" if necessary. The sometimes-controversial QE2 program ended as scheduled on June 30th and there is no plan for QE3…yet. In retrospect, most non-government economists and analysts agree that QE may have warded off some deflation, but neither it nor the billions in stimulus spending did much of anything to create jobs or really turn the economy around.

The real math on cash-for-clunkers was abysmal. Apparently, the majority of the other programs were just as ineffective. Shovel-ready? We all know how well that worked out. Joking about it might be funny if there were some way to get the money back, but it's just gone. This was basically waste, fraud and abuse at its worst.

Just days after I typed the above paragraph, I ran across Alan Greenspan's testimony before congress in which he said, "There is no evidence that huge inflow of money into the system basically worked." He also said the only positive impact all the stimulus programs had was a weakening of the dollar which helped our exports, and that the Fed's quantitative easing programs have done little to loosen credit or boost the economy.

The president's own economic advisors released a report the Friday before the 4th of July weekend admitting the jobs created by stimulus funds were going away. They also admitted that the huge stimulus package was supposed to provide temporary help and was never intended to have a lasting impact on the economy. Whether or not each "stimulus" job cost $278,000, as one analyst contends, or less than that, the program was ill-conceived and very expensive…and it will have a lasting impact on our economy…it will just be a negative one.

The most level-headed criticism of the stimulus included an illustration of someone stealing a purse with $500 dollars in it and using the money to buy a flat-screen TV. Supporters of the stimulus point to the money spent, which can't be ignored, but opponents of the plan insist its supporters are ignoring the fact that it was taken from someone else who was probably also going to spend it on something.

This is a nice analogy, but I find in it one huge shortfall. The money in the example was stolen and spent. The stimulus money wasn't stolen; it was created out of thin air. If it was taken from anyone, it was taken from future taxpayers who will get to pay it back, plus interest, thereby reducing the amount of their own money they'll be able to spend on what they want.

This is the seldom-discussed lasting impact on the economy of the late, great stimulus program, and in my opinion, represents shameful economic irresponsibility of the highest order. It's about time our elected representatives understood there are consequences for their actions. Unfortunately, representatives before them knew this and exempted themselves and all future congresses from those consequences long ago. Do we really have to wonder why there seems to be no grasp of reality in Washington D.C.?

Republicans Eric Cantor and John Kyl walked out of the budget negotiations being led by Vice-president Joe Biden saying the democrats were refusing to yield on tax and spending increases. So…the republicans are saying no debt-ceiling increase without spending caps and cuts. The president has waded in, and he and the democrats are saying no budget cuts without higher taxes and spending increases, but are willing to accept a debt cap. (I thought we already had one…called the debt ceiling.)

I know this will shock you, but I'm siding with the elephants on this one. Why in the world would anyone in their right mind give congress, which has proven time and again to be completely irresponsible when it comes to controlling spending another dime of taxpayer money until they have some hard constraints in place?

In California, the legislature doesn't get paid until they submit a balanced budget for the governor's approval. Apparently they submitted one that wasn't balanced that the governor had no choice but to veto so they've been sent back to the drawing board with their paychecks on hold. Hmmm….Imagine that. You don't get paid if you don't do your job. What a concept!

Of course…just as I'm ready to pat Governor Brown and California on the back for doing a good job…we get news that he and the democrats in the majority forced a "balanced" budget through without involving the republicans at all. Unfortunately, it is balanced by relying on over $4 billion in increased revenues as the economy recovers. That's optimistic to say the least.

California's proposed budget is $82 billion, but they're already expected to exceed that by $22 billion, piling that debt on top of the $6 billion already accumulated…and $4 billion from an imaginary recovery is going to fix all this? I'm guess I'm just not comfortable with their math.

The president, in his June 25th radio address said, "We can't simply cut our way to prosperity. We need to do what's necessary to grow our economy; create good, middle-class jobs; and make it possible for all Americans to pursue their dreams." Apparently, we can't spend our way to prosperity either, so if I have to choose, I'm up for trying the spending cuts first. When the federal government learns to live within its means, then they can ask for a bigger allowance from taxpayers…not before. We've heard enough promises.

I've written it before and I'll repeat it. Government stimulus and government-created jobs are a net drain on the economy. They are economically less effective than charity or direct redistribution because they must include the government's administrative costs (overhead.) For the government to "invest" $1 into the economy, they have to take more than $1 away from a taxpayer. Booming US economic periods have followed tax cuts; not increases. The damage done by this type of economic policy is only compounded when the funds used for "investment" are borrowed.

Republicans are holding firm in their resolve that there be no tax increase while Democrats insist loopholes in the tax code need to be closed. Guess what? I agree with both, but I'll challenge both sides to go after more than just tax loopholes. Let's go after ALL tax AND legal loopholes, subsidies and exemptions for individuals, corporation and elected officials…especially the ones congress has generously afforded itself over the years.

Also from the halls of insanity, Mr. Geithner is telling congress and the American people that we simply have no choice but to increase taxes on small business and those making over $250,000/year. Didn't we pretty much prove that taxing the "rich" to fix this can't work in last month's Commentary? It's past time for a new Treasury Secretary.

While Greek citizens rioted in the streets over almost-certain cuts in benefits, the Greek parliament passed austerity measures that ensured they would continue to receive help from the European Central Bank and the International Monetary Fund. I will never understand the mentality that says, "Don't cut our pay or benefits", even when continuing them will almost certainly result in complete destruction of the system resulting in zero pay and benefits. Seriously…would you rather have a job that pays a little less than it did last year or no job at all?

In the grand scheme of things, just where is Greece? Why all the fuss? When ranked by GDP, it was number 31 out of about 190 with an annual GDP of about $305 billion (US dollars.) By comparison, the US is #1 at $14.7 trillion. Then, there's a big step down to #2 China at $5.9 trillion. The European Union, which is a collection 27 Member States including Greece has a combined GDP of $16.1 trillion. So…as a percentage of the European Union's GDP, Greece is less than 2%. As a percentage of the 10 largest countries' GDPs combined, Greece contributes a mere 0.74%.

Congress is supposed to work over the weekend to straighten out the debt ceiling and deficit mess. Whatever the outcome, you can be sure it will be accompanied by a lot of finger pointing, name calling and blame for all the enormous social and economic injustices which will probably never actually come to fruition being assigned to members of both parties. The fix to this problem is going to hurt. The longer we put it off, the worse it will be.

Hope you all had a safe and relaxing 4th of July Holiday! Stay cool this summer and we'll do this again in about a month.