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## OCTOBER MARKET COMMENTARY

By Tom Crow

November 7, 2011

Index	Month End	Gain (Loss) by Period			
		Month	Most Recent Quarter	Year-to-Date	Trailing Twelve Months
Dow Industrials	11,955	9.5%	(1.6%)	3.3%	7.5%
S&P 500	1,253	10.8%	(3.0%)	(0.4%)	5.9%
Nasdaq	2,684	11.1%	(2.6%)	1.2%	7.1%

October was everything September wasn't, but was it a Trick or a Treat? The Dow briefly recaptured the 12,000 level and even a 2.5% Halloween selloff couldn't crush one of the best months the markets have ever had. The one-month turnaround almost completely wiped out the damage done the month before.

The S&P 500's Volatility Index (VIX) had slipped below 25 and things were looking up. Then, as a near-perfect illustration of how over-reactive to any piece of news the markets have become, Greece's socialist prime minister made the monumentally stupid decision and announcement that the choice as to whether or not the country would accept austerity measures and financial bailouts would be put to a public vote. Hey...it's easier than governing, right?

Markets sold off and stayed off, even after the referendum was declared all but dead by several members of Greece's government. The VIX jumped 20%, which is an indication that a lot of the selling going on was short stock sales and bearish option plays. If there is a silver lining in this it's that this type of selling pressure doesn't usually last longer than a session or two...unless investors panic and start dumping stocks. The flipside is that when the shorts start to cover their positions on any sign of improvement, the ensuing rally is also short-lived, unless investors start buying in a big way.

The U.S. economy added 80,000 jobs in October and the unemployment rate edged down to 9.0% from 9.1%. Economists expected an increase of 90,000 jobs and no change in the jobless rate. September and August numbers were revised sharply higher. September's job estimates were up to 158,000 from 103,000 and job growth in August was revised up to 104,000 from 57,000. The broader measure of unemployment that includes underemployed workers fell to 16.2% from 16.5% in September.

I diagnose this set of numbers as fairly benign, but leaning a bit to the negative side. The jobs created are less than needed to keep up with up with baseline population growth, and the lower unemployment rate was due in part to a reduction in the workforce. Unfortunately, that means the number of folks who have exhausted their benefits and given up looking for work has grown. Maybe you can find some solace in that the number was positive, but it means we're still looking at little, if any improvement in the economy.

The Fed agrees with me. Last Wednesday, they slashed their growth outlook for this year and the next two, and also significantly increased its forecasted unemployment rate. They now see 2011 GDP between 1.6% and 1.7%, 2012 GDP between 2.5% and 2.9%, 2013 GDP between 3% and 3.5%. Earlier estimates called for 2011 GDP between 2.7% and 2.9%, 2012 GDP between 3.3% and 3.7%, and 2013 GDP between 3.5% and 4.2%.

The unemployment rate is now forecast between 9% and 9.1% this year, between 8.5% and 8.7% in 2012, between 7.8% and 8.2% in 2013 and between 6.8% and 7.7% in 2014. On personal consumption expenditure inflation, the Fed now sees 2.7% to 2.9% inflation this year, 1.4% to 2% inflation next year, 1.5% to 2% inflation in 2013 and 1.5% to 2% inflation in 2014.

I wrote in an earlier Commentary that Greece just doesn't matter much in the bigger picture of the European Union where it comprises less the 2% of the combined GDP. It matters even less, less than 0.5% to be more-specific in the world economy so what's the big deal? The big deal is uncertainty, and uncertainty is what investors fear the most.

Over the weekend, Greece's government survived a confidence vote and Prime Minister Papandreou said a national referendum on the issue was no longer on the table, and that he would step down as soon as a deal was reached. But, let's assume for a minute that Greece did vote. The media would have us believe the country would overwhelmingly

defeat the austerity measures. What then? Several things...first, they would almost certainly default on their debt obligations. That means the countries and banks that previously agreed to take 50 cents on the dollar would get nothing.

That might generate enough ill will towards Greece that they find themselves kicked out of the European Union. Then, at 180% debt/GDP, they go back to printing worthless drachma's like they did before the EU (primarily Germany) supported their currency and quickly find nobody wants drachmas at the current rate. Their only option is to print more to offset higher interest rates required to borrow, resulting in hyperinflation spiral a la Zimbabwe.

With China indicating no interest in throwing their money at this problem, the losses incurred by the EU thanks to Greece push rates for Italy above what Spain and Portugal could afford and the last of the PIIGS fails. But, this is what the Greeks want. No cuts in government spending. They refuse to acknowledge the crystal-clear handwriting on the wall. NOBODY has any real money to bail them out any more...not Germany, not France, not the US, and certainly not the EU.

I wrote most of the previous paragraph last week, having no idea how quickly Italy's situation would escalate.

This is where I might normally launch into an attack on out-of-control government spending, the occupy protesters, or anything else that might incense about half of my readers. Instead, I'm calling a time out. Most of you know my opinions on all this and complaining about it doesn't give you any clue as to what, if anything we can do about it.

As long as what's going on in Europe continues to overshadow the better-than-expected third-quarter earnings results here at home, I expect the markets will continue to be more volatile than usual and over-reactive to any and all headlines. It is going to be difficult to find, and harvest growth in stocks, and cash continues to pay next to nothing. Holding dollars in savings accounts or low-rate CDs just means you're losing purchasing power to even minimal inflation.

Gold is holding its own as bailout talks continue and most of our clients have some exposure to it through various exchange-traded funds. Beyond that, we will once again be forced to move to a more-conservative approach in our investment management. We will tighten up stop losses and use only our shortest hold-time expectations in an attempt to take some profits from stocks when we have them.

There are a few reasons to be optimistic. Historically, mid-October to mid-April is the best time to be in the markets. Some early indications that holiday spending might be strong could usher in a Santa Claus rally, which would be a great way to end the year. We can also hope that the increased visibility of the economic problems in Europe will lead to a quick resolution and a return to stability.

Enjoy your Thanksgiving. Do something to help those less-fortunate than you if you're able, and we'll be back with another update in about a month. In the meantime, please don't hesitate to call or e-mail us if you have questions.