



## Perspective on the Latest Market Events

### Commentary from Jim McDonald, Chief Investment Strategist

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Is the stock market sniffing out a nascent global economic recovery? On a year-to-date basis through April 2, the best performing region was emerging markets, up 8.2%. The BRICs were particular stars, with Russia up 35%, China up 33%, Brazil up 16% and India up 7%. Since the recent market lows set March 6, the best-performing stocks in the United States were those most leveraged to economic and financial market improvement. The financial sector climbed 50% (but was still down 25% year-to-date!), and the cyclical consumer discretionary, industrial and materials stocks all out-performed.

Global purchasing manager index (PMI) information appears to show some stabilization in global activity, although at very depressed levels. The JP Morgan Global All-Industry PMI has now risen in three of the last four months. The overall weakness in global economic activity over the last six months was started by the rapid fall in consumer demand, and was followed by severe production and inventory cuts by manufacturers. Regionally, the PMIs in the United States and emerging markets are improving first, while Europe and Japan are lagging. Recall that a key theme we have been highlighting is our expectation that the recovery in global economies and markets will be regionally differentiated – and that appears to be unfolding as emerging markets outperform the developed markets.

The most recent U.S. PMI data from the Institute for Supply Management, for the month of March, painted a somewhat mixed picture. The services PMI, representing the largest and less-volatile portion of the economy, saw a decline in its headline level to 40.8 from 41.6 in February. The more-volatile manufacturing PMI ticked up to 36.3 in March from the prior reading of 35.8. However, the components that our economics department has identified as having the best leading-indicator value were uneven. The supplier delivery level fell to 43.6 from 46.7 (meaning business is slower so items are shipping faster) but the new orders index jumped 8.1 points to 41.2. So while it does appear that business activity levels have stabilized at low levels, evidence of an improvement in conditions is still sparse.

Policy makers remain intensely engaged on multiple initiatives, including fighting the risk of deflation, working to restore the flow of credit, stimulating economic growth, and bolstering regulation. The Group of 20 meeting last week in London made modest progress in these areas – primarily furthering support for the International Monetary Fund (IMF) – but may have been most notable for the lack of fireworks. Sentiment surrounding the conclusion of the conference seemed to indicate that world leaders were somewhat successful in generating goodwill without committing



to significant policy changes. The low expectation for the announcement of additional stimulus plans was met, save for Japan's pledge of an additional \$51 billion in spending announced on the eve of the summit. The biggest accomplishment – the promise of an additional \$500 billion for the IMF – is more of a pledge than a commitment but is notable none-the-less.

The stock market has a long history of discounting changes in the economic outlook, both downturns and upturns. The severity of the collapse in global demand after the bankruptcy of Lehman Brothers in September 2008 has led to the most rapid decline in global production since the 1930s. The depth of this fall virtually ensures some improvement as credit begins to flow and long-deferred purchases are made. For these gains to be sustained there needs to be some stability in both the housing and labor markets – developments we are not yet confident of predicting. We are also heading into first-quarter earnings season, with the likelihood of weak earnings and poor guidance from many corporations. While we are encouraged by the early signs of stabilization in the global PMIs, we await further evidence of improvement before we will consider altering our defensive tactical asset allocation recommendations.

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