DELTA
FINANCIAL ADVISORS
Investment Counsel

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Economic Comments

Eighteen months into the current economic expansion, to many, it still feels like a recession. In fact, to provide continued support to the tepid economic recovery, the Federal Reserve Bank felt compelled to launch the QE2 - we only hope that it will be more successful than the launch of a similar behemoth, the Titanic. In this case however, the QE2 being referenced is the U.S. Federal Reserveôs second round of quantitative easing. What this means in practical terms is that the Fed has commenced another round of buying Treasury bonds, $600 billion worth, in an effort to drive up demand for the securities, raise their prices and drive down U.S. interest rates.

The central bankôs belief is that by flooding the economy with cash, banks will lend more money thereby boosting the still lackadaisical U.S. economy. Early results would suggest that the anticipation of the QE2 was far more effective in driving down interest rates than the actual reality of the Fed move as interest rates have moved up meaningfully since the QE2ôs early November launch.

Helping the Fedôs ability to take this action has been the continued lack of reported inflation in the primary U.S. inflation index, the Consumer Price Index (CPI). While having risen for 5 straight months, the indexôs last reading in November showed an increase of only 0.2% for a slight 1.1% increase in the prior 12 months.

One positive economic sign has been the continued recovery in factory output which has risen for five straight months. Although having rebounded by more than 10 percent since its most recent June 2009 lows, activity still remains more than 9% below its April 2007 peak. Looking ahead, the Institute for Supply Managementôs manufacturing index continues to project ongoing growth in this important economic cog.

On the political front, the resounding Republican/Tea Party victory in the mid-term elections caused the outgoing lame duck Congress to collaborate with the White House in producing a 2-year band-aid on the expiring estate tax regime and a 2-year extension on the current income tax rate structure. Although this $800 billion package will provide a stimulant to the U.S. economy this year, and as no reductions in current Federal spending was correspondingly approved, this myopic action causes one to question how long China and other international creditors will be willing to keep open the candy store for the deficit-addicted U.S. government.

Amidst these problems, the dollar has continued to see sharp

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declines against most major currencies in the face of the latest round of quantitative easing. Although this injection of billions of dollars of money into the economy has been aimed at spurring on U.S. growth, this effort has drawn criticism from major trade partners. They believe that this devaluation has come at their expense. Countries such as Brazil and South Korea have gone so far as to take action to mute new capital inflows, which have resulted from the dollarôs devaluation, by placing capital controls on incoming short-term investments.

In the most recent quarter, U.S. productivity continued to rise, but the growth rate has slowed markedly since late 2009. While not a long-term positive, the slowing productivity increases the likelihood that companies will hire more workers in the near term. With employment remaining poor, this can only be a positive as non-farm jobs for December were up much less than expected with only 103,000 new jobs created.

While the unemployment rate declined to 9.4% to end the year, the decreased rate was largely due to more than 250,000 adults discontinuing their job searches. With the overall participation rate for the work force falling to a recent low of 64.3%, the number of people looking for work or active in the work force has actually shrunk during this recession rather than growing by the 4+ million that natural population growth would have predicted. In general, the U.S. economy needs to grow by at least 300,000 jobs/month to impact the unemployment rate with at least 150,000 jobs/month needed just to keep up with population growth. With only 1 million jobs created in 2010 and with more than 3 million new labor participants, we remain far off of this mark.

The year ahead will remain full of challenges, not the least of which are the deficit/debt issues of many local and state governments. At this juncture, however, we remain optimistic that the current environment will continue to slowly improve. While we are traversing a near-term situation full of varied risks, we believe that the U.S. longer term economic potential remains strong.

Analyst Corner

The financial sector continues to struggle in the after-math of the mortgage holocaust of the last several years. While virtually no major player in the sector escaped this period unscathed, we believe that Wells Fargo (NYSE: WFC) is well positioned to flourish as the current troubles start being put in the rearview mirror. The bank has a simple, but well executed, strategy of creating strong customer relationships while maintaining good credit quality. The bankôs customer service driven model has given WFC a sharp advantage by providing very low cost deposits. These low cost deposits, in turn, have allowed WFC to have industry beating net interest margins - a critical long term advantage. We believe that the companyôs strong balance sheet and continued focus on quality lending should provide for attractive long term returns for the intrepid investor.

Market Comments

Wall Street broke out its noisemakers and party hats for the yearȇs final quarter. Celebrating the much anticipated mid-term elections, the U.S. stock market advanced almost 11% for the quarter and climbed 15% for the full year. Powering the market ahead was the consumer discretionary sector as Americans got in touch once again with their inner consumers. The continued hangover from the 2009ȇs ObamaCare celebration caused the medical sector to be the market laggard with less than a 1% rise for the year.

Looking ahead, we remain concerned about corporate sales. Revenue growth, which has been tepid since the start of the economic recovery, has recently started to slow. Sales grew by only 5.5% in the yearȇs third quarter and down from a 6.1% rate in the 2nd quarter and the almost 7 percent rate in the yearȇs first quarter. With corporate sales growth typically peaking at this stage of the economic recovery, the obvious concern is raised.

As is typically the case, analysts have started the year quite bullish with predictions for full year S&P 500 earnings of $96/share. If achieved, this level would surpass the prior peak achieved in 2006. To hit this mark, two key hurdles will have to be overcome - the ongoing weakness in the financial sector and the likely pressure on profit margins. While having somewhat stabilized, the financial sector will have to show some consistency, even growth, if the projected target is to be met. The other threat comes from commodity prices which are up sharply in the last 12 months; corporate revenue growth will have to be appreciable to overcome the recent commodity headwind on earnings.

A contrarian dark lining to the recent market silver clouds has been the recent reading of the so-called fear index, the CBOE Volatility Index (VIX). The index is commonly used as an inverse indicator of what may be coming down the road for the market. At year-end, the VIX was trading beneath a reading of 18 as compared to the historical average of around 20 and sharply beneath Mayȇs readings, following the Flash Crash, of 48. These readings suggest a marked degree of investor complacency in the face of continued high unemployment and mixed economic news.

This rosy view is consistent with the current Common Wisdom (CW) with most pundits predicting robust double digit gains for the stock market. We do not directionally disagree with the CW in that we believe that the market continues to have an upward bias. Our very large caveat, however, is that given the complacency that investors are currently feeling, we believe that the ride, as in 2010, could be quite rocky; investors should be prepared for meaningful retreats amidst the overall trend of market advances.

We continue to espouse our adamantly held belief that prudent investors should remain focused on appropriate asset allocation, risk management and expected asset returns in managing their investments.

Performance as of 12/31/10

	Close	Month	1 Year
DJIA	11,577.51	5.33%	14.06%
S & P 500	1,257.62	6.68%	15.07%
NASDAQ Comp.	2,652.87	6.19%	16.91%

	Quarter end yield	Prior Year end yield
10 yr. U.S. Treasury	3.31%	3.84%

Planning Thoughts

Few people, and none that we know, enjoy paying taxes. With Roth IRAs, the government offers a vehicle to save money on a permanently tax exempt basis (or at least under current tax law). For years, these accounts were only available to individuals and couples making beneath a certain amount of income. Starting in 2010, the government allowed higher earning tax payers to convert existing Traditional IRA accounts into Roth accounts in exchange for paying income taxes on the funds in question. However, higher earning individuals (currently $169,000 for couples and $107,000 for singles) were excluded from making regular annual contributions to these accounts.

Recently, we were made aware of a quirk where high earners who do not have existing IRA accounts, can go ahead and effectively make annual contributions to a Roth IRA. This trick can be accomplished by making a post tax contribution to a traditional IRA (for which high earners are qualified) and then converting this Traditional IRA account into a Roth IRA (for which high earners are also eligible).

If you would like to explore this strategy further, we would be happy to talk with you. Of course, before taking any such move, we would strongly urge you to talk with your tax professional to make sure that there arenǭt any unique issues in your circumstance that would prohibit you from pursuing this course of action.

Partners
Gerard A. Plauché, CFA
Clifford F. Favrot, CFA CFPÊ
Ainsley D. Bishop

Frank A. M. Williams,
Emeritus

Operations Manager
John T. Egnatchik

Office Manager
Angelle M. Verbois

Contact Us Toll Free:
1-888-522-9019

228 St. Charles Avenue, Suite 1100, New Orleans, LA 70130
504-522-9019 PHONE · 504-522-9676 FAX

www.deltafinad.com

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