Delta Financial Advisors

March 2008

Economic Comments

Although we were originally disdainful of the Federal Reserve's initial rate cuts last fall, the central bank appears to have been on the right path. The economic data has continued to turn less positive over the last several months. Since September, the Federal Reserve has cut overnight interest rates by 2¼ percentage points to 3.0%. Additionally, Wall Street anticipates further rate cuts totaling another percentage point over the next several months.

The Fed's recent actions have been focused on remedying the rapidly slowing economy but have ignored the substantial ramping up of inflation. The most current readings for both the core CPI and the CPI were higher than analyst expectations at 0.3% and 0.4%, respectively.

The likely rationale behind the Federal Reserve's action is its view that recent price increases are solely the result of the sharp run-up in commodity prices. Once commodity prices stop going up (they do not even have to go down but merely stop increasing), overall and core inflation should diminish. Critical to this theory is that the Fed will then have to be aggressive in raising rates once the current economic/credit crises pass.

The likelihood of recession has significantly increased as jobs creation has effectively ceased in 2008. 63,000 non-farm jobs disappeared in February following a loss of 22,000 positions in January. Employment declines were broad based with the manufacturing and construction industries seeing the sharpest declines in workers. In the face of this type of continued employment contraction, the economy's 7+ year economic expansion appears to be on thin ice.

Certainly, no economic relief is in sight from the housing market. The proportion of U.S. mortgages falling into foreclosure hit a record, 0.83%, in the last quarter of 2007 with adjustable rate mortgages leading the increase. For the first time since record keeping was started in 1945, Americans' home debt exceeded their home equity as homeowner's equity fell to 48% in the fourth quarter.

More critically, 8.8 million homeowners, or about 10.3% of all homes, are estimated to now have zero or negative home equity. Additionally, U.S. homeowners are demonstrating a surprising willingness to walk away from homes in which they have built up no equity. Rather than viewing their residences as their own personal shelters, many view these purchases as merely failed investments.

Despite the poor jobs data, the reported unemployment rate actually fell slightly to 4.8%. Unfortunately, the drop in the unemployment rate was not a sign of economic strength but rather an indication that almost 450,000 prospective employees ceased looking for work in the worsening labor market. Good news for the economy was absent from the energy front as oil prices topped their inflation-adjusted record set in 1980 as the commodity punched through the $104 per barrel level.

Fighting other grim indicators, the Federal government, to the eventual dismay of our children and grandchildren, continues its effort to stimulate the economy. The White House now anticipates the Federal deficit to exceed $400 billion for the current fiscal year, just short of the record set four years ago. The key drivers in this gaping budget deficit are the continued costs of military activities in Iraq and Afghanistan along with the recently approved $150 billion domestic stimulus package.

Looking at the economy as a whole, we have become increasingly pessimistic about its near-term prospects. If not already in recession, the economy appears to be teetering on the very precipice of one. The classic ingredients for a recession have been a tight money supply and strong wage inflation coupled with fear. While the first two ingredients are not in place, the fear component is certainly here in spades.

In hindsight, the scope and magnitude of the housing boom/bubble's impact were greatly underestimated. While a period of economic adjustment is required following the bursting of any asset bubble, we continue to believe that the business, legal and infrastructural framework found in the U.S. allows for elevated rates of growth over the long term. The next several quarters will likely remain rocky, but we remain confident in the longer term prognosis of continued and robust growth for the U.S. economy.

Market Comments

In the face of continued bad news from the housing and credit markets, the stock market remains unhappy. Continued credit market issues and rapidly accelerating mortgage losses continued to push the market's recent decline. Leading the

Delta Financial Advisors, L.L.C.

Performance as of 02/29/08				
	Close	***Month***	***YTD***	***1 Year***
DJIA	12266.39	-2.75%	-7.12%	+2.30%
S & P 500	*1330.63*	*-3.25%*	*-9.06%*	*-3.59%*
NASDAQ Comp.	*2271.48*	*-4.95%*	*-14.35%*	*-5.97%*
	Month end yld.	***Prior Yr. end yld.***	***12 mo. prior yld.***	
10 yr. U.S. Treasury	*3.53%*	*4.03%*	*4.55%*	

charge downward were the financial and telecom sectors while the commodity sensitive energy and material sectors were the only areas showing gains.

For all of the bad news in the stock market, it has meant good news for Treasury bond investors. Unfortunately, this happiness has not been widely spread amongst all fixed income investors as the recent flight to quality has almost exclusively been focused on U.S. government issued securities. The risk premium required by investors from all other bond issues has sharply widened thereby meaningfully reducing the gains realized by most fixed income investors.

With the broader stock market off over 15% from its October highs, we are close to bear market territory (meaning a decline of 20% or more from recent highs). While having only symbolic importance, entering into a bear market could have additional negative ramifications on investor sentiment.

Unlike the American consumer, corporate America is in relatively robust shape. The companies comprising the S&P 500 have seen an almost three-fold increase in their cash balances since 1998 while their debt levels have fallen. The driving force besides this change in strategy has been the shift to global operations which subject companies to increased currency, political and competitive risks. As a result, most companies are particularly well situated to face the current economic turmoil.

One question that we are often asked is “why we do not shift accounts to cash once the market signals a recession is coming?” The answer is two-fold although they both basically return to the same thing. First, we are not market timers. If an investor misses the few days where the market goes up sharply, they can lose more than half of their expected long-term returns.

Secondly, the market is not always correct. A popular Wall Street anecdote is that “the stock market has predicted nine of the last five recessions.” Not to suggest that the market is not a good economic indicator, it is, but rather that sometimes it is wrong.

The commonality of both answers is our belief that long term investment strategy should be identified and implemented without consideration of near-term market turbulence.

More so than other times, in volatile markets it is critical to be invested in a manner appropriate to your objectives and to your comfort level for risk. If you are questioning where you lie in regards to either of these issues, please call us so that we can discuss these matters further.

Planning Thoughts

With tax day coming way too soon for most of us, reducing the tax burden is on many people’s minds. One of the more beneficial methods is to maximize your contribution to tax-deferred or tax exempt accounts.

Tax payers have until April 15th to make contributions to IRA accounts while contribution rates to employee savings plans can typically be modified at will. While it is prudent not to have all of your savings in tax exempt plans, due to the unknowable vagaries of future tax laws, these plans do represent a means of compounding wealth (based on current tax law) on a tax deferred or even tax exempt basis.

If you are not familiar with these savings options, please let us know so that we can help familiarize you with the available options.

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