DELTA
FINANCIAL ADVISORS
Investment Counsel

October 2010

IN THIS ISSUE

Economic Comments

Following its August meeting, the Federal Reserve’s Open Market Committee (FOMC) announced that it would be buying Treasury securities with principal payments from its existing trillion dollar mortgage-backed securities portfolio. By taking its most aggressive move since the Fall of 2008, the FOMC was aiming to depress long term interest rates so as to provide additional stimulation to the economy. Driving the committee’s sharp action was the substantial deceleration in U.S. economic growth seen over the last two quarters since the winter of 2010.

Slowing global growth has led economists to reduce 2010 forecasts for U.S. GDP growth to 2.5%, down from initially robust estimates of 3.1% growth. Highlighting the slowed growth has been unemployment’s continued high levels, still hovering around 9.6% which has declined only slightly from 2009 highs. The recent September payroll report showed a decline for the fourth month in a row as 159,000 government positions were shed during the month, albeit primarily temporary census-related workers. Better news came from private employers who added 64,000 positions during the period.

The Federal Reserve has now kept overnight interest rates near zero percent for two years. Many corporations have taken this opportunity to issue new low cost debt. The challenge is that most of these enterprises are not investing these new funds but rather are stockpiling these cash reserves while waiting for economic activity to pick up. Since the impetus behind the Fed’s easy monetary policy is to encourage investment and job creation, an impasse similar to the chicken-and-egg scenario has come about where it is impossible to say which is supposed to come first. The economy is unlikely to show marked improvement until consumers and industry sharply increase their outlays, but consumers and industry are reluctant to sharply increase their outlays until the economy improves. The result: an economic stalemate exemplified by tepid economic growth.

Rather than using cash to hire new staff or invest in new capital, companies continue to focus on enhancing their immediate financial houses. With cash constituting more than 6% of assets, corporate America is sitting on its highest level of cash since the early 1960s. In a modest sign of action, corporate cash levels have fallen slightly since the year’s 1st quarter. Investments on new equipment and software grew meaningfully during the year’s first two quarters. All the

(Continued on page 2)

Economic Comments continued from cover

same, this type of investment remains significantly beneath pre-crisis levels. This uptick appears to be more the result of replacing old equipment rather than renewed enthusiasm for production expansion by Corporate America.

In assessing the near-term outlook, we take some comfort from the signaling of the commodities markets - in particular the recent performance of oil and gold prices; both supplies have had recent strong upswings. If traders were anticipating low growth or deflation, commodity prices would instead be suffering marked declines. With gold and oil prices rallying, this suggests market expectations of increasing demand or inflation - either of which would be a positive in the current low demand and near deflationary environment. Highlighting these marketsô volatility and sensitivity to global growth, or in this case decline, was the 25% fall in gold prices and 70% fall in oil prices amidst the economic free fall of the global financial crisis in 2008/2009.

On other fronts, labor productivity slowed sharply in the 1st quarter and actually turned negative for this yearô s 2nd quarter which, if this trend were to be sustained, it could be a meaningful problem. Yet, we view the recent report positively in that companies appear to be reaching the maximum possible output from their existing workers, as a result of the last two yearsô cost cutting, and they will soon be compelled to hire new workers to generate additional sales.

Taken all together, we anticipate the economy will continue to hobble along with modest growth for at least several more quarters. Although the risk of a second dip into recession remains elevated, we do not foresee this occurring. Unfortunately, with the historically high levels of unemployment and longer periods of unemployment between jobs, this period of tepid growth will be perceived by many in the labor force, or those desiring to re-enter the labor force, as being far more dire than actual economic data would suggest.

Analyst Corner

There can hardly be a person in the United States who has not heard of (or likely holds) a Visa® card. After having been owned by its affiliated bank for decades, and following its initial sale of stock in 2008, Visa *(NYSE-V)* became available to individual investors. In simplest terms, Visa is the world's largest electronic payment network. The company neither lends nor borrows money to /from its cardholders but rather collects fees by allowing cardholders and banks to access its network. Having recently resolved a major anti-trust lawsuit and with the implementation of new U.S. credit card rules, some of the more pressing uncertainties regarding Visaô s future have been resolved. Given the long-term secular trend of increasing global consumer credit, the companyô s unparalleled network, and attractive business model, we believe that Visa could be an attractive addition to a clientô s portfolio.

Market Comments

Recovering from Wall Streetôs recent swoon, the broader market gained more than 11% during the quarter, resulting in a year-to-date return of 3.9%. The yearôs market leaders have continued to be the consumer discretionary and the industrials sectors with 13+% gains while the healthcare sector has proven the marketôs laggard with modest losses from a post healthcare overhaul hangover.

Following a mid-summer market downdraft, the stock marketôs meteoric rise of 8.9% for September, was driven by two key factors: 1) expectations that corporate earnings for the 3rd quarter will not disappoint and 2) the belief that the upcoming Congressional elections will result in legislative gridlock. With the first issue being self explanatory, the second factor of Congressional gridlock is viewed as a positive for the markets in that Congress and the Administration will not be able to push through any new (read expensive) initiatives nor be able to institute any new anti-business policies. Historically, the best economic policies usually have resulted when both parties have been forced to work together rather than when one party dominates the White House and Congress and is thereby able to push through highly partisan legislation.

With money market rates having declined to effectively 0% (typically 0.05% or less), individual investors have poured $230 billion into bond mutual funds this year as they seek additional income. Fortunately, these smaller investors have been somewhat rational in their decisions as their new funds have almost exclusively gone into short maturity bonds. Nonetheless, these investors are now faced with the fairly unusual scenario where short maturity bonds are yielding less than the 1.9% average dividend of the stock market.

Looking forward to the 3rd quarter earnings season, analysts expect profits to rise 23% over the year ago level. While on a historic basis this expected increase is substantial, this profit growth still represents a sharp decline from the 49% and 52% earnings growth seen in the two prior quarters.

The roadblock that is being run in to, is that earnings have been growing robustly without appreciable revenue growth. The 2nd quarterôs profits were 10% higher than in 2008 although revenues were down by 6% during the same period. Although near-term corporate frugality has helped profit recovery, for the economy as a whole to grow, corporate revenues, too, must rise.

While the perception of stocks as a good long-term investment has been tarnished (and as evidenced by the stock mutual fund outflows of more than $70 billion in 2010), we continue to emphatically believe in the long-term value of holding a well designed and diversified portfolio of stocks, bonds and cash.

Performance as of 9/30/10

	Close	Month	YTD	1 Year
DJIA	10,788.05	7.85%	5.57%	14.12%
S & P 500	1,141.20	8.92%	3.89%	10.17%
NASDAQ Comp.	2,368.62	12.04%	4.38%	11.60%

	Quarter end yield	Prior Year end yield	Yield 1 year ago
10 yr. U.S. Treasury	2.52%	3.84%	3.31%

Planning Thoughts

There is a classic joke where you know that you are really in trouble when, during an emergency, an official shows up at your front door, explains that they are from the government and indicates that they are there to help. This joke bares a striking parallel to the current situation where Congress has promised to help tax payers by ñfixingò the Bush-era income tax, investment tax and estate tax cuts as they expire this year. The only problem is that the nationôs legislature has neither indicated when they will implement permanent ñfixesò nor what these permanent ñfixesò will be. Afraid to address this daunting task, and the resulting backlash that its actions will generate among voters, Congress has taken the far easier approach of doing nothing. Until, or if, Congress takes action, the default course of action will result in sharp increases in these three types of taxes.

The best near-term solution to this situation is to take only those actions that are compelling (such as selling fully priced and over concentrated assets at todayôs historically low capital gains rates) while maintaining flexibility regarding longer-term estate plans and income tax situations. Once Congress implements a new estate/income/investment tax regime, it will make sense to re-assess your circumstances in light of the changed environment. If there are any asset or estate dispositions that you are actively entertaining, we would be happy to visit with you on the positives and negatives of this proposed 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

DELTA FINANCIAL ADVISORS
Investment Counsel