Investment Insight

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2010 Mid-Year Market and Economic Outlook

A conversation with:
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Highlights:

- The "Four Ds"; debt, deficit, deleveraging, and disposable income, will be the framework that we view the U.S. economy and its growth, and the opportunity for stock market growth. All of these factors indicate that the expansion of this recovery will be moderate or modest.
- The risk of a double-dip recession happening in 2010 is 28%, while there is a 72% chance that we're going to have an ongoing recovery, which is in the modest 2% range.
- The consumer represents 70% of the economy, and since the consumption rate going forward is at a sub-historical trend, overall growth of the economy is at a sub-historical trend.
- We have passed the point at which global economic growth is going to be led by the U.S. or Europe. We think that Asia (excluding Japan) and Latin America are now the engines of global economic growth for many years to come.
- Heightened volatility requires investors to revisit portfolio allocations and rethink approach to equity investing. We do not believe that a buy-and-hold strategy can satisfy a risk budget that a client is comfortable with. Dynamic equity risk parameters can enable each individual client to have exposure to equities, but not expose them to the high volatility that is not desired.

The following discussion is moderated by Derek Roy, AIF®, Vice President - Investment Consultant. Additional comments have been contributed by Steven Denike, Portfolio Strategy Analyst – of Rochdale Investment Management. The below is a discussion from Rochdale's August 11, 2010 Advisor Forum Conference Call.

Q: Garrett, it's not official yet, but there seems to be a general consensus that the recession ended around the third quarter of 2009. However, if there is one thing I hear quite a bit of in my travels is that it certainly does not feel like a recovery. So, how would you describe things thus far, the so-called recovery that we have had?

A: Most polls that you and the listeners have most likely heard do reflect the sentiment across the country that we are not out of the recession yet. Let's first talk about why that is so. Most people relate the phase of the economy we are currently in to their job, wages, house values, and things of that nature. In that context, the housing market and housing prices are still well below the levels they were a couple years ago. Presently, the job market is still weak, unemployment is still high, and wage increases are not growing too much. We understand and accept that is the sentiment across the country, however, from a technical perspective or from an economist's perspective, we believe that the recession ended late in the third quarter of 2009 and we have been in an economic recovery phase for roughly 9 to 11 months.

Right from the start, it was our view that the context of the "Four Ds"; debt, deficit, deleveraging, and disposable income, will be the framework that we view the U.S. economy and its growth, and the opportunity for stock market growth. All of these factors indicate to us that the expansion of this recovery will be moderate or modest. In our opinion, those looking for a stronger recovery, a return to the historical growth rate of consumer spending, and those thinking that housing prices or housing construction is going to start ramping up again, truly misunderstand the impact of the "Four Ds."

In summary, we believe the first couple of quarters of the recovery were mainly stimulus-induced. We were getting 5% type GDP growth and that was a result of the government, rightfully so, putting a great deal of the stimulus into the economy. That is now slowly fading away. When that "stimulative" effect is taken away, you are going to end up at your base level or your base disposable income level, which we view in the 2% range. Thus, that is our macro outlook at this point.

Q: Garrett, speaking of "D" words, I think the most popular Google search term right now is "double-dip." Earlier in the year a lot of people were more optimistic, but it seems like there is some confusion right now between slow lethargic growth and negative growth. The data has recently shown things decelerating quite a bit. So, if you could kind of continue on this path about your outlook on the economy, what do you think the biggest risks are as we move through the fall into 2011?

A: We believe the possibility of a double-dip recession, based on our comprehensive multi-factor recession model, is now at a 28% probability, up from 22% a couple of months earlier. So, there is some increased risk that this economic recovery phase will not sustain itself and possibly relapse back into a recession. However, the risk of a double-dip recession happening in 2010 is 28%, while there is a 72% chance that we're going to have an ongoing recovery, which we have characterized as modest, in the 2% range. We see more evidence for that sustained moderate case, which is being very supportive to monetary policy. This translates to low inflation or low interest rates, which is ultimately saving people who are paying off mortgages, credit cards, and car loans, to the extent that they have variable rates. Those people are benefiting.

Although it is weak, we also see positive job creation. Whenever you have any type of job creation, it is very difficult to go back into a recession. Business spending, which is driven by corporate profits are very strong and steady. We also know the global economy in Latin America and in Asia (excluding Japan) is very strong. Therefore, when you put all of those factors together, you come up with a positive sign in front of GDP as compared to a negative sign, i.e., double-dip recession.

I would like to mention the government is well aware of all of these concerns and they are going to pull out almost every tool in the kit to preclude a double-dip. So, we do not see that risk as significant as the media at times would like us to believe, but we are carefully monitoring it and all of our advisors and clients will have access to the recession model. It is a very comprehensive, empirically driven multi-factor model, which we release every couple of weeks.

Let me use housing as an example of how this concept of double-dip is overly misunderstood. We all know that the housing industry is down substantially. The number of homes being produced, at one point, was approaching 2 million and now we are under 500,000. That is a substantial decline. Consequently, some people use that fact as evidence that we are going to have a double-dip recession. In fact, it is just the opposite, because every year this country forms about 750,000 to 1 million net new households, i.e., people that get married, who live with their parents, have to buy a home or rent a house, immigration into the country, divorces, and separations. All of these forms of demographic activity create an underlying demand, and as long as the sun comes up, this demand will continue.

Currently, people are staying in their homes and not purchasing new ones because of the uncertainty in the job market. So, since we are only producing about 400,000 to 500,000 new homes, we are eventually going to have to get back to building 750,000. That is a substantial positive aspect that is going to enter the economy over the next couple of years. That is a good example of why low levels of activity today are actually good to some extent because they

will have to get back to more normal levels in the next couple of years.

Q: One overriding theme throughout your response Garrett dealt with the consumer, so let me turn this next question over to you Steve. We know that 70% of the economy is the consumer, and it's no secret that the consumer is spending less and saving more, and dealing with employment issues. So, given the outlook for a very modest jobs recovery, how long do you expect this to play out? This process of the consumer really slowing down, pulling in their horns, and ultimately impacting the economy?

A: Well, this theme of post-consumerism is something that we at Rochdale have been talking about for some time. Personal consumption over the last 20 years has risen to a little over 70% of GDP. This is a huge increase. If you look back from the late '50s to the early '80s, that level was about 62% to 65%. Most of that increase was built on an unsustainable level of debt creation. We are currently in the process of deleveraging or reversing that buildup, but it is going to take some time. Deleveraging debt by itself does not preclude an economic expansion, but it is certainly going to limit its strength.

Spending so far in this recovery is roughly half of what has been typical of past recovery periods. We expect that to increase going forward, but at a level that's going to be far below the historical trend rate. That is not to say that progress has not been made recently, we have had debt payments as a hare of personal income decrease. After peaking at about 14% two years ago, they are down 2% from that peak. Unfortunately, a great deal of that has come from foreclosures and defaults, but nevertheless, levels are down which is a good sign.

However, if you look around at the overall consumer fundamentals, most of them are negative outside of maybe inflation and energy cost. Wealth is a big drag on spending, but the positive news is that throughout the nation we have increased net wealth across the board to about $6 trillion over the past 12 months. However, we're still down roughly 20% from the peaks we reached two years ago. The most important elements that we have confronting the consumer right now are jobs, income, and credit availability. These are the number one determinants impacting a consumer's decision to increase or decrease their rate of spending going forward. Credit availability still remains very weak, mortgage equity withdrawals have virtually disappeared from the stock market, and new home loans and credit cards are very hard to get at the moment. Additionally, even if a consumer has the willingness or the ability to add on debt at this point, the banks are still not lending.

The job market and income growth are on the other side of that equation. Real gains in wages have shown year-over-year growth at a negative rate for almost three years now, which has not happened since World War II. Job creation, while it has been positive, has not been great enough to offset all of the losses that we experienced over the recession. So, if the consumer represents 70% of the economy, and if you are going to have a consumption rate going forward at a sub-historical trend, you are going to have an overall growth in the economy at a sub-historical trend.

Q: Steve, kind of extrapolating from your answer, it strikes me that our economy is going through a painful transition from an asset-based economy to more of an income-based economy, at least this is the transition we are trying to make. Simply put, we cannot count on our houses any longer as ATM machines. So, this transition is going to come down to the labor market. We have had a few glimmers of hope in recent months, but the fact is that the unemployment rate remains stubbornly high particularly for this point of a recovery. Where do you see the unemployment rate going? Do you see companies hiring? That seems to be the million dollar question.

A: First, the good news. The jobs market has improved considerably over the past year. Roughly a million new jobs were created over the past six months. If you look back to the great recession at its peak, we were losing 700,000 jobs per month. So, this is a huge turnaround. Unfortunately though, many of these jobs have been temporary private sector hires, specifically census jobs. These temporary jobs will be fading over the next few months, causing concern that without this jobs growth, consumers may retrench further and slow their spending. This is definitely a risk and we are monitoring the data every month, and it is currently high on our recession monitor chart. Even though forward-looking indicators have decreased a bit recently, the hiring outlook looking forward is still positive.

A recent small business survey shows that the intention to hire has increased over the past month. It is positive for the first time and this is a huge source of job creation. However, the problem is the outlook for job demand is so weak, and with revenue growth expectations so slow, corporations are really hesitant to hire right now. Corporations are looking to maximize their shareholder value by increasing productivity and controlling cost, rather than hire new employees. Labor is the most expensive input, including benefits, so companies are turning to outsourcing in place of hiring. They are going overseas and finding cheaper labor there, or they are substituting technology for new hires. This is what we have confronting the job market right now. In the coming months, there is not going to be enough hiring to bring down the unemployment rate dramatically. We have lost roughly 7 or 8 million jobs over the great recession. Many of these jobs will not return to the market, specifically those in industries such as housing or financial services.

Therefore, we are looking at a multi-year period of an unstable job market. One factor that is going to keep the unemployment rate high is the number of workers that do not have any prospect in their current careers and have to be retrained, which takes some time. Another factor is that as we get some positive movement in the labor market, there is also a tremendous amount of unemployed people, currently on the sidelines. The unemployment rate is roughly around 10%, which is kind of misleading because so many people have left the job market and given up for the moment, frustrated with their search for employment. As we have positive hiring over the next few months, a good percentage of these people are going to come back into the labor force searching for jobs, which will make it hard to bring down the unemployment rate. Lastly, demand is just not going to be there for corporations and companies to hire at a strong rate. This is one of the themes or the fundamental issues surrounding the consumer that will prevent them going forward from spending what they have spent in the past.

Q: Garrett, if I could turn back to you. Building upon a couple of Steve's answers, consumer wealth has taken a huge hit and most of that has been in the form of declining real estate values. The question on everybody's mind is where do you see the real estate market going? Do you think the housing market might become any better as we move in to 2011?

A: So, let us write off the rest of 2010. We know that foreclosures are probably going to peak this year, adding supply that will put some pressure on pricing in the five sand states (the California's, the Florida's, the Nevada's, etc.). In our opinion, 2011 will be what we call, the basing year or the bottoming year. There is the potential in some of the states I just mentioned for slightly additional price weakness. We essentially are building in no negative contribution to GDP or to economic activity for 2011. The year might start off a little bit weak, but by the end of the year will be net, slightly positive. As I mentioned before, we need roughly 750,000 to 1 million new homes. We are building half of that right now. This pent-up household formation equation is going to come to bear beginning in 2011 and going into the following year. Therefore, our view is slightly positive on housing when we look forward to 2011.

Q: Another theme of yours has been about moving away from a consumption-based economy, and more towards a savings and investment based economy. As consumption has declined, it has been up to the manufacturing sector to contribute more towards economic growth. Exports have been up, but a lot of that activity is due to overseas in emerging market growth. So, if we broaden this topic to the entire global economy, what would be your thoughts on the global economic outlook moving forward?

A: At Rochdale, we believe that we have passed the point at which global economic growth is going to be led by the U.S. or Europe. We think that Asia (excluding Japan) and Latin America are now the engines of global economic growth for many years to come. There is no going back. That is the demographic fact of life. It is a debt and deleveraging fact of life.

The 2010 decade for the U.S. and Europe is one of debt, deficits, and deleveraging. There is no way around this and all of the factors that empirically get into that show that sustainable economic growth is below trend. As previously mentioned, global economic growth is being led by Asia (excluding Japan) and Latin America, and although they are moderating, they are still influencing growth with 8% in China and 4% to 5% in Latin America. These are great growth rates.

We agree that Southern Europe is either going to go into a recession or will come very close to one, but it is not that big of a contributor nor has it been in many years, so we are not too concerned. In my opinion, Northern Europe will be all right, as well as the U.S. When added all together, we see global economic activity remaining on track for this moderate level that we have been talking about.

Q: Garrett, in Europe specifically, the sovereign debt issue was not that long ago but all of a sudden seemed to fade from everybody's memory, do you think that will show its ugly head again? What do you specifically think about some of the sovereign debt issues they have had in the European countries?

A: It might be a great place to take a vacation, but we would advise investors to stay away from the Southern European countries, whether it is in stocks or bonds. Those problems have not gone away and they will absolutely not be able to grow their way out of that situation. They have done the smart thing and postponed it, but there is no doubt that those countries with debt and deficits are going to have to deleverage. As a result, severe sustained austerity will have to be implemented and that's not politically doable. So, they are basically going to do what the Greeks have always done which is restructure and default on their debt. For now, there is no chance that the situation has resolved itself and there is no chance that the situation in Europe is going to resolve itself in the next year or two. It is going to take the entire decade to get through the whole process.

Q: If we jump back across the pond but stay on this debt topic, never in my career has there been an agreement on a topic on Wall Street until now that here in the United States we are really on an unsustainable path as it relates to the budget deficit. When do you see our debt finally becoming an issue? What strategies out there do you think may be installed to deal with our deficit?

A: Let us first examine the history of our politicians. I can not ever recall the politicians of this country showing leadership on debt, deficits, social security, or entitlements. I can not recall an example of anything that was done proactively to address these accumulating and unsustainable trends. So, purely based upon the history of this country, no one should be optimistic that we are going to resolve the unsustainable level of deficit. We are going to address the debts in a chaotic way. Examples of chaotic activity include the government paying a little bit more interest on their bonds or we are not raising as much debt as we want to. There is a whole host of outcomes, but none of which anyone can predict due to the fickleness of the investor causing this kind of chaotic behavior. However, it is coming and I think that is the more likely path. There is not an American that would not love to see some leadership in our government take on the current levels of too much spending, too many entitlements, so on, and so forth.

So, let us review the four or five ways that historically every major economic power in world history has addressed this current situation that the U.S. is on track for. In order to reduce the debt and to solve the current deficit problem, there are four general strategies. One of them is to have the economic growth of the economy be so strong that rising tax revenues, without changing the tax rate, puts a great deal of profit back into the government's pocket, and instead of spending it they pay off debt. That is not an option for the U.S. economy for all of the reasons that we have just talked about.

The second, most often selected path is the confiscatory path. The invisible confiscation of saver's money given over to the debtors, also known as inflation. That is very likely to contribute to the reduction in the debt. If you allow inflation to be 3% for a decade, you have diminished the real value of that government debt by about 35% to 40%. That is a classic means to reducing the debt situation.

The third path is raising taxes. We do not see how taxes will not go up on some level, on several classes of people. We do not see default and restructuring happening in the U.S., but we absolutely expect that in several countries around the world over the next decade or two.

Currency debasement or printing money is the fourth path. The government has done a lot of that lately and we are not sure if the Fed, after 30 years of building up substantial credibility on monetary policy, is going to discard that good track record and start printing too much money. But, the bottom line is history shows that it is not predictable when the investors who have to buy government bonds are going to respond unfavorably or reject buying those bonds. What we do know is that every month $100 billion, this number is just hard to imagine, of borrowing has to occur for the next several years, at least the next two years, and at any time the investors can just simply say we do not want to take your bonds at 2% or 4%. We do not expect that to happen in the next year or two. In fact, if the politicians of this country showed any inkling of leadership, there is plenty of time to get the deterioration of the debt and deficits to stabilize, and then to gradually work their way back towards some level of economic sustainability. However, that is not our expectation.

So, the investment implication is that this uncertainty is not good for the economy and it is not good for the stock market. When people are less confident about the next couple of years, they consume less, invest less, make less long-term plans, and they are less willing to put money at risk in the stock market. So, the government really is in a self-defeating mode by not getting a handle on the deficit situation.

Q: Garrett, you mentioned the government growing revenue, which is usually called for raising taxes, and with the elections coming up this fall, what do you think the likelihood is of Congress letting the Bush tax cuts expire?

A: We at Rochdale have some substantial consulting relationships with political economists that are actively engaged on a daily basis in the Senate Finance Committee hearings, House Finance Committee hearings, and policy-setting meetings, and, every day we get quite detailed reports on conversations, discussions, and plans being floated. At the beginning of the year, there was virtually no case to be made for the extension of those Bush tax cuts. Now, based upon the inputs from our consultants and political economists, we are putting at least a 50% chance on the extension of some of those existing tax rates on the middle class. For the wealthy, which they are defining at $250,000, the odds are above 0%, but below 50%. So, we are putting it at approximately 20% to 30% that there may be some modification of the tax rate rather than go into the full tax rates that existed prior to the Bush tax cuts. Actually, part of the stock market rally that we were experiencing was the realization by investors of this trend change. It's not a secret on Wall Street that the politicians are being much more open-minded about not raising taxes in light of the weak, soft, modest economic growth.

Our position is the deficit is not going to be altered for the long-term by extending these tax rates on the middle class or everyone for a year or so. It is a drop in the bucket compared to the magnitude of misspending that's going on elsewhere. Now, we are absolutely against ongoing deficit spending, but for the next year, if it were up to us, we would cut a bunch of wasteful spending and extend the tax rates rather than do something else.

Q: One more policy question before we turn our attention to the markets, and that would be of interest rates. It seems like just a short time ago inflation was a really naughty word

and now everything is about deflation. So, what would you expect to see out of the Federal Reserve as we move forward?

A: Now keeping in context our "Four Ds," the research we have done, and research the firms we work with have done, it is conclusive that there is not an exception when you are going through a major secular deleveraging from an over indebted situation, all of those effects swamp the monetary policy effects. We have seen the Fed print a trillion or two dollars, and I would like to make an important point here about that. It is a technical point, but it's an absolutely critical point. When the Fed prints money, they issue the newly-printed dollars to the banking system. The banking system creates money, not the Fed. The Fed creates reserves, but the reserves are not actual money. Money is only defined when it is in the hands of the consumer or in the hands of business.

Think of it this way. If I printed a trillion dollars of newly printed dollar bills and put it in a hole that I dug in my backyard, I did not create money. Milton, Friedman, and Anna Schwartz have defined this very nicely. Money is something that is in the hands of those that can use it to transact and purchase goods and services. We know that the trillion or two dollars printed was delivered to the banks and put in their vault because the banks do not have any desire to give out loans to anybody. They are writing off their bad debts, which is completely necessary. The banks basically dug a hole underneath their basement and put that money there for future needs, for all of their losses, and so on, and so forth. Actually, what they did is just deposit it at the Fed.

There is not and has not been a lot of money creation causing concern about deflation. It is impossible to have two trillion dollars of money and talk about deflation. We are talking about deflation because there is no new money in the system. There is no turn over. There are no transactions going on. In summary, we are not a believer that deflation or inflation is going to be the case or the cause for concern over the next 6 to 12 months. We believe it will be something in between, which is low inflation or disinflation.

Q: Well, let us turn our attention towards the market and see if we can make sense of everything that you have talked about in terms of maybe trying to make and protect some money. 2009 was a good year, then 2010 hit and the volatility picked up. Obviously, the market hates uncertainty. So, what would be your outlook for the markets, for equities as we go through the latter half of 2010 and into 2011?

A: We have talked a lot about the economy and we are positive, but we are cautious where we have a tempered outlook. We are not in the double-dip camp as we think there is only a 28% chance, and we do not think there is going to be deflation and inflation.

When it comes to the equity market, it is a different picture. It is a brighter, more positive picture. The reason is businesses in this country (for the moment I am referring to the S&P 500 companies, specifically the executives of those businesses) over the last 10 years have undertaken a very extensive and intensive internal reorganization or revitalization to make sure they are low cost producers or highly efficient in their markets, as they wanted to survive the global competitive landscape. So, they have enacted labor saving technology, did a great deal of retraining, did some outsourcing, and a whole host of things over the last decade to make their business very efficient and effective. Lean and mean is a nice characterization. The business executives have looked forward and said the growth, they did not know the Great Recession would happen, is not in the U.S. or Europe, it is in Asia and Latin America. They have pursued those markets for many years. So, the businesses in the S&P 500 aggregate should not be viewed as U.S. businesses. That is not a surprise and 35% to 40% of the profits of all these S&P 500 companies are coming from outside the U.S., and those profits are growing in double-digits. When you have double-digit growth for roughly 40% of your pie and you have mid-single digits for the rest of your pie, you are having pretty good corporate profit growth. What we have seen is the stock market had a tug on the downside from the U.S. economic situation, the political uncertainty, the debt situation, the fiscal uncertainty, and it had a pull on the upside from the strong corporate profit growth of these companies.

First, we would like to reset the baseline. We hear a lot of people talk about the average P/E (Price to Earnings) ratio for the market is roughly 15 times. What we would like to do is have our advisors and clients reset that level. So, we are saying 13.5 is the new 15, and everybody should understand the thinking behind that. When you go back and do an analysis of major recessionary periods and you see what the valuation or the P/E valuation was, it historically, in the second and third year actually goes down and does not attain that average level. So, using 13.5 P/E rather than 15 is the first building block for our stock market outlook. The second building block is corporate profits, and that's at $88 to $92. So, if you use 13.5 times $90, you come up with 1215 for the S&P. The S&P is roughly at 1100, and that gets us to approximately a 9% expected return over the next year for stocks.

Q: Garrett, as we came out of the recovery, we had a substantial amount of client assets in cash. Then as we moved through the recovery, we allocated a lot of that money back towards the top end of each client's target equity ranges. Now, I understand from a strategic allocation point of view that we are still favorable in the equity markets, but we have relaxed that position on being fully invested and adopted a more flexible approach. Could you elaborate on

this flexible approach that you have adopted, this kind of dynamic process that we are using in client's accounts?

A: We have three main pillars: the macroeconomic outlook, the valuation of the market, and corporate profit growth. Those are three broad categories. We have gone through them and we know that the macroeconomic outlook has gotten a little less positive, 28% chance of a double-dip. Consequently, to reflect this economic valuation, depending upon each client's portfolio position and risk tolerance, we have moved from a fully invested and committed equity exposure to having 0% to 10% of cash in their portfolio. In our view, after a couple of months this soft patch will stabilize, and I think that's what the market's next expectation will be. We are either going to continue this weakening trend and validate the double-dip or we are going to stabilize at this 2% range, give or take, which will validate the ongoing recovery and give investors better reason to understand the "sugar high" we had from the stimulus. We were growing around 5% and we have slowed down to 2%, but we are not going to go down from 2%, to 1%, to 0%, and to -1%. We are going to stay in the 2% zone.

In essence, we have put a small amount into cash which has proved to be a good thing because the market has not gone anywhere over the last couple of months. As we get more evidence that the double-dip model that we use is slowly stabilizing, we will put that cash back to work. If the double-dip risks rise, then we will allow more than 10% cash to exist in the client's portfolio.

Q: Garrett, talking client's portfolios, and something that we are very proud of here at Rochdale, that of risk management or what we call "risk budgeting" for each client, it strikes me that recently there are so many things impacting the market that have nothing to do with fundamentals, from leveraged ETFs (Exchange-Traded Fund), to algorithmic trading, to high volatility hedge funds, etc. You kind of coined the term meta-risks for dealing with these sideline issues. So, could you explain a little bit on how we are dealing with this heightened volatility, this new non-normal equity environment, and what we are doing to manage some of these new risks?

A: As we mentioned earlier, we believe that using the 15 average P/E just does not support the empirical data, so 13.5 is our new 15. The same thing pertains to the risk in the stock market, the standard deviation, the draw-down, however you want to characterize it. For all of the reasons that our listeners are aware, we do not believe that the volatility of equities is going to remain in the normal ranges that it has historically. Now, we are not making this a lifetime forecast, but for this year and into next year, the volatility is going to be more than normal because of everything we have discussed.

Consequently, clients do not want full exposure to the stock market, which makes perfect sense. What we are trying to do is bridge those concerns by allowing people to have exposure to the stock market, but with circuit breakers. These circuit breakers are dynamic equity risk parameters that are established on a one-on-one basis with each client. The advisor, sales consultant, portfolio manager, and client work towards setting these parameters together so they can go through this process. Although it is a fairly complex process, it is a very understandable process. It enables each individual client who wants exposure to the U.S. stock market, but is concerned about heightened volatility levels to bring these meta-risks out of the portfolio with a pre-agreed convex approach.

I want to add the point here that the equity investor from 1982 to 2000 experienced an 18 year, golden two decades of buy-and-hold investing. In 1982, the P/E of the market was single digit and it expanded substantially over that 18 year period. Corporate profits rose substantially and all you had to really do was put your sail up, catch the wind, and experience a very nice long-term equity return. In 2000 through 2010, everyone knows that the equity investor has not made any progress, yet has experienced heightened levels of volatility. So, when you do the math, you are scratching your head saying, "Why am I exposing 50% or 60% of my money to this asset class that has not done anything for 10 years, and right now is experiencing more than normal volatility?"

For those reasons, we believe the firms and investment professionals who are articulating more of the same buy-and-hold, stay-the-course strategy, are truly out-of-step with their clients risk tolerance for their portfolios. We do not believe there is a way that you could use a buy-and-hold strategy and satisfy a risk budget that a high net worth client is comfortable with. Another approach is simply needed. You need to strategically rethink your strategy on how to keep the investor allocated to equities, but not expose them to the high volatility that they donot desire. Rochdale now has the tools, the knowledge, and the technology to do that on a personalized basis.

Q: Well Garrett, what strategically would be some of the other asset classes that you might favor at the current moment?

A: When we think about the outlook for economic growth, we are looking for 7%, 8%, 9%, and when you think like that rather than the historical 10% from stock, you think in terms of yield and dividend. We have some very strong offerings in high dividend income stocks, preferred stock strategies, high-yield bond strategies, and non-traditional assets that are providing very favorable, high quality, 7% or 8% type of yields. That's our favorite segment of the market. Next would be high-quality global businesses, U.S., and international. Lastly, we like the Latin American and Asian markets for medium type companies to provide some capital growth to the portfolio.

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