Monthly Chartbook

April 2008

Danger, *Danger*, Will Robinson

Really now, what good was Robot? He always said "danger, danger" right when it was upon them. How about some advance warning?

Big Picture

The next 18 months will determine if Ben Bernanke is viewed as a hero, or a goat. As we have said in the past it is clear now ***to us*** that the US Federal Reserve's job is to manage asset prices, not inflation or unemployment.

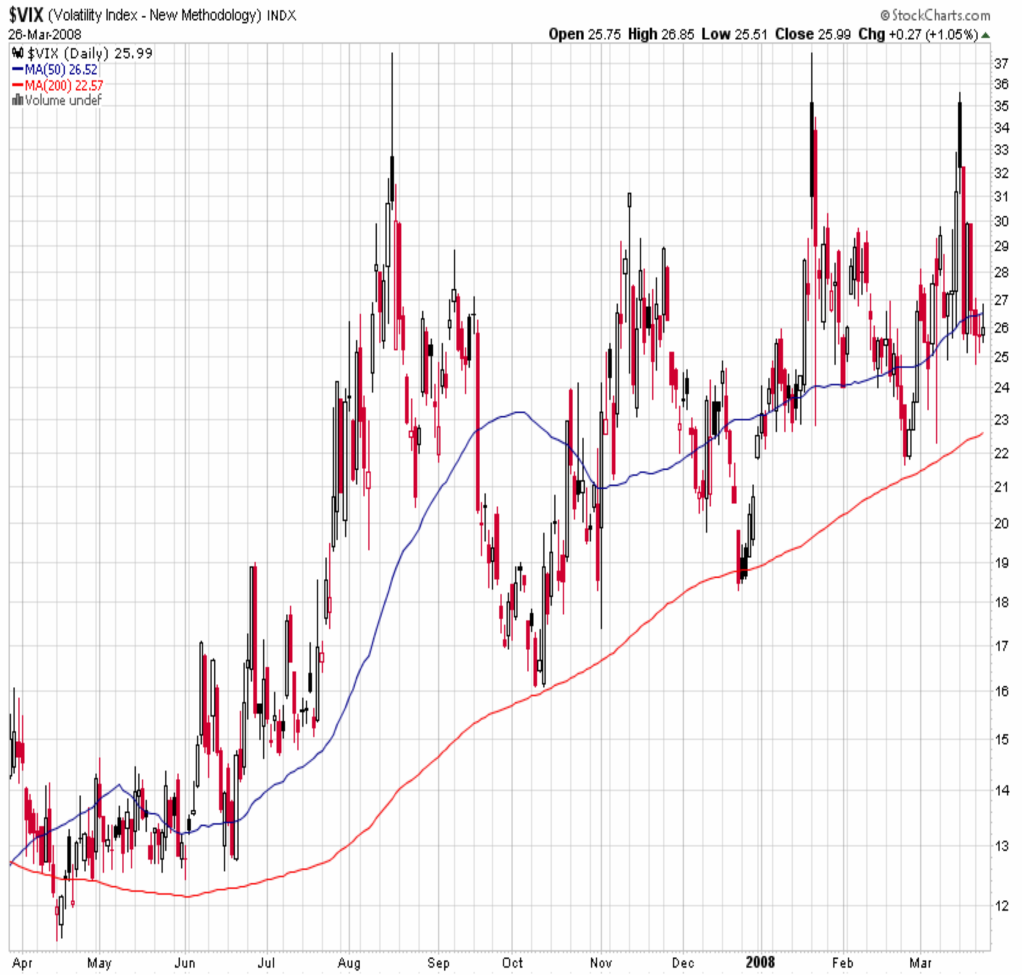
The real killer of market-traded asset values will be a contraction in the P/E ratio of common stocks if inflation expectations come "unmoored" to use Fed speak. *We are painfully close to that point*.

The Three Month Treasury Bills collapsing yield was the greatest sign of the fear and risk aversion that had swept the US Financial System. ***We went right to the brink…***

Macro-economic research

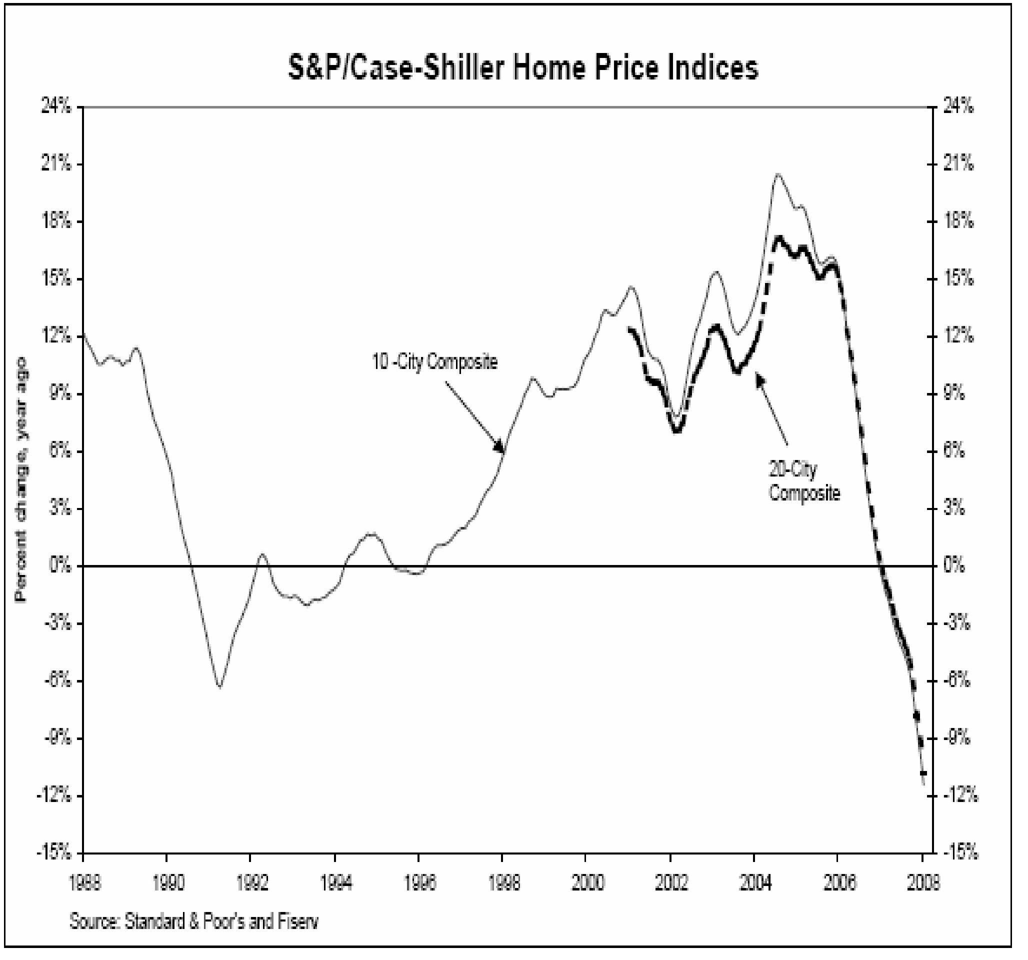
Yield spreads on the most risky class of investment are what is in the driver's seat. Until spreads settle down, stocks and esp. financials will be under pressure.

Macro-economic research



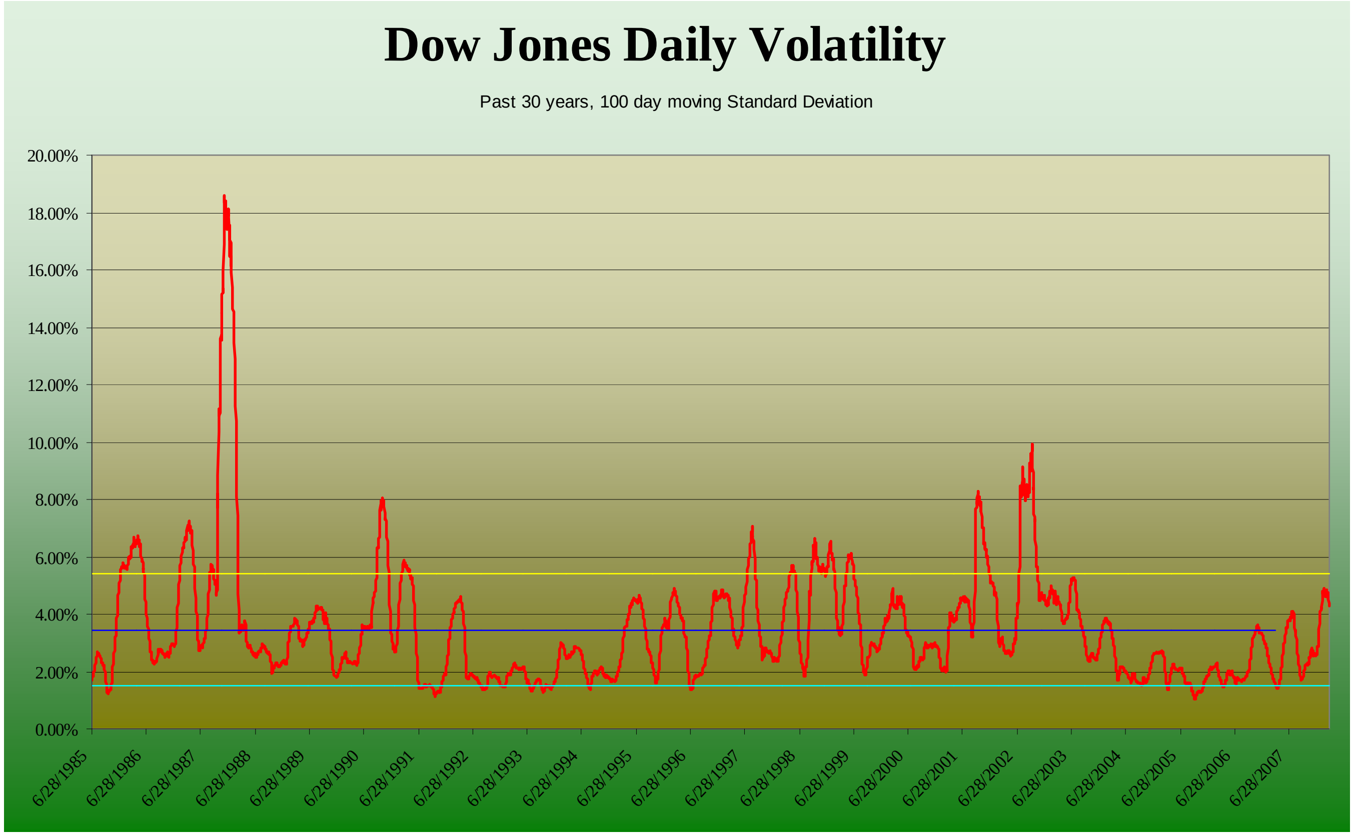
The VIX was low because of low risk spreads in the credit market, not vise versa. Volatility was nowhere to be found until yield spreads gapped out in July.

Macro-economic research



Home prices are front and center… the headlines read "**Home Prices Down 10% in January**". Ha, home prices were down 10% *year over year* in January. Further, without California, Florida and Arizona home prices are down just 5% year over year.

Macro-economic research



While market volatility (here measured by the Dow) has increased, it is well within the norms for the last 30 years.

The Macro View

•It's all about leverage, access to funds and de-leveraging.

•The Global economy is benefiting from commodity prices (emerging markets) and increased final demand from the so-called BRIC's (Brazil, Russia, India, China).

•It seems as though everyone is betting **against** the US dollar and **on** the ability for the World to de-couple from US growth.

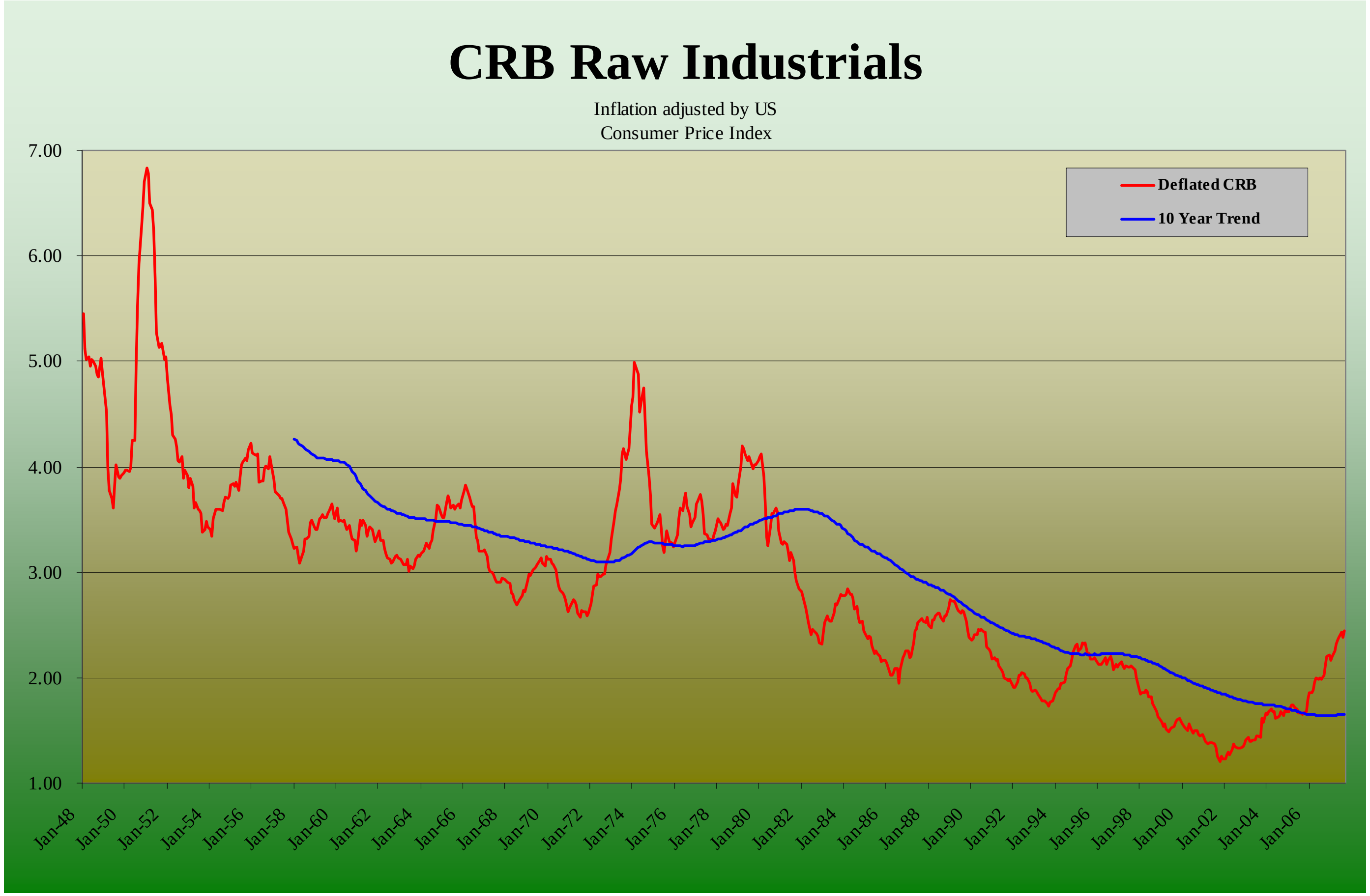
•A Consumer/Retail recession is upon us.

S&P 500 Financials Leverage

Ticker	Total Assets	Total Liabilities	Equity	Leverage	L Ratio	Beta
NYSE:BSC	$395,362	$383,569	$11,793	3.07%	32.53	1.71
NYSE:MS	$1,045,409	$1,014,140	$31,269	3.08%	32.43	1.80
NYSE:MER	$1,020,050	$988,118	$31,932	3.23%	30.94	1.56
NYSE:LEH	$691,063	$668,573	$22,490	3.36%	29.73	1.62
NYSE:SLM	$155,565	$150,341	$5,224	3.47%	28.78	1.20
NYSE:GS	$1,119,796	$1,076,996	$42,800	3.97%	25.16	1.71
NYSE:PFG	$154,520	$147,099	$7,422	5.05%	19.82	0.96
NYSE:PRU	$485,814	$462,357	$23,457	5.07%	19.71	1.26
NasdaqNM:ETFC	$56,846	$54,017	$2,829	5.24%	19.09	2.28
NYSE:FNM	$882,547	$838,536	$44,011	5.25%	19.05	1.68
NYSE:GGP	$28,814	$27,358	$1,457	5.32%	18.78	1.33
NYSE:C	$2,187,631	$2,074,033	$113,598	5.48%	18.26	1.35
NYSE:HIG	$360,361	$341,157	$19,204	5.63%	17.76	1.57
NYSE:CBH	$49,256	$46,472	$2,784	5.99%	16.69	0.70
NYSE:FHN	$37,015	$34,880	$2,136	6.12%	16.33	0.56
NYSE:LNC	$191,435	$179,717	$11,718	6.52%	15.34	1.36
NYSE:MET	$558,562	$523,383	$35,179	6.72%	14.88	1.04
NasdaqNM:NTRS	$67,611	$63,102	$4,509	7.15%	13.99	1.17

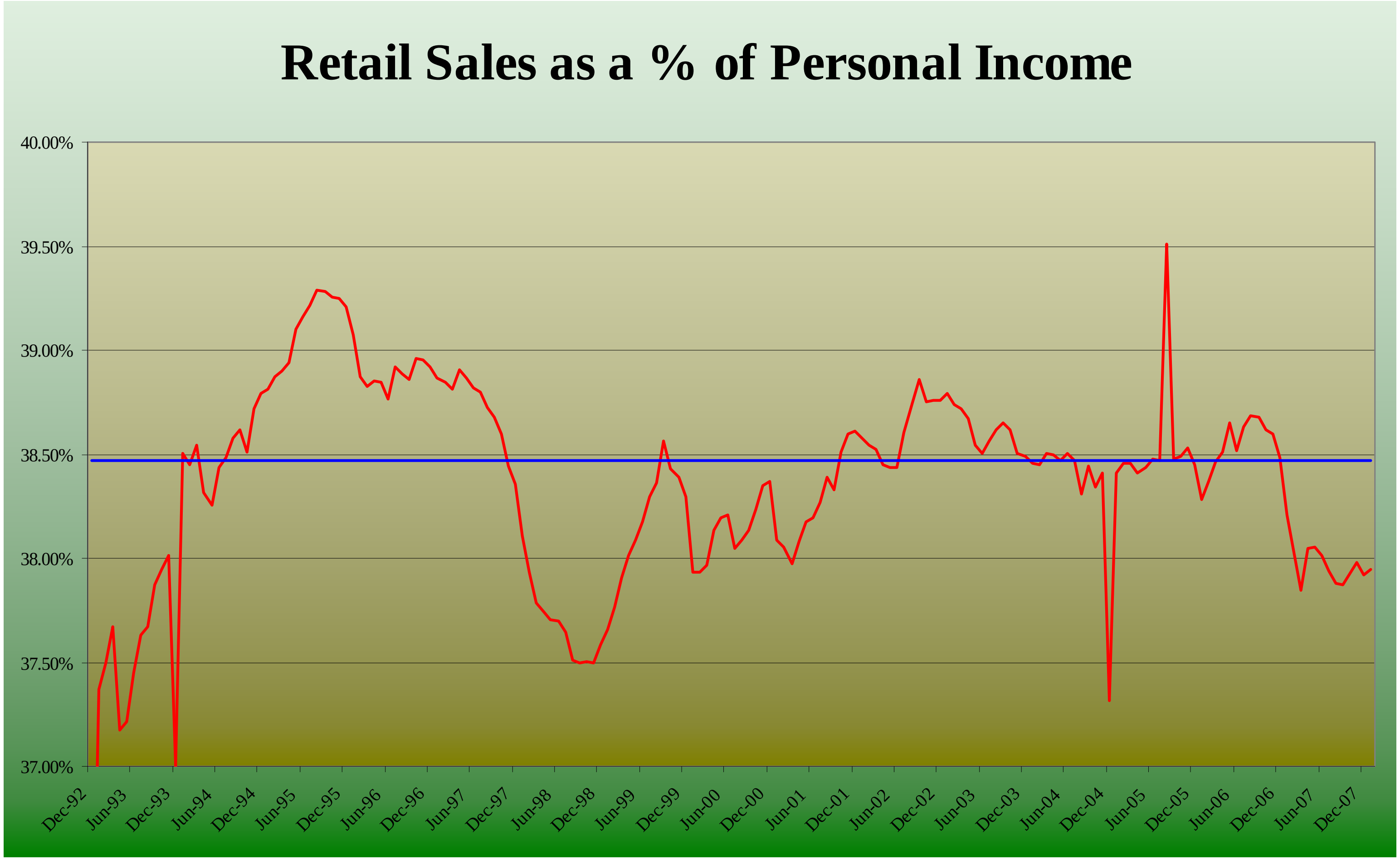
Bear was the first victim, with 30 to 1 leverage if your "assets" decline in value greater than 3% you are toast. ***BSC is toast.*** The red is the list of possible additional victims.

All Urban CPI deflated CRB Raw Industrials



If this is a 10-25 year Super Cycle, where are we on price??? Year 5, year 10? How about 5 years in, but priced like year 10. Not much room for error for the speculators who are long but don't own the raw commodity.

Retail Sales as a % of Personal Income



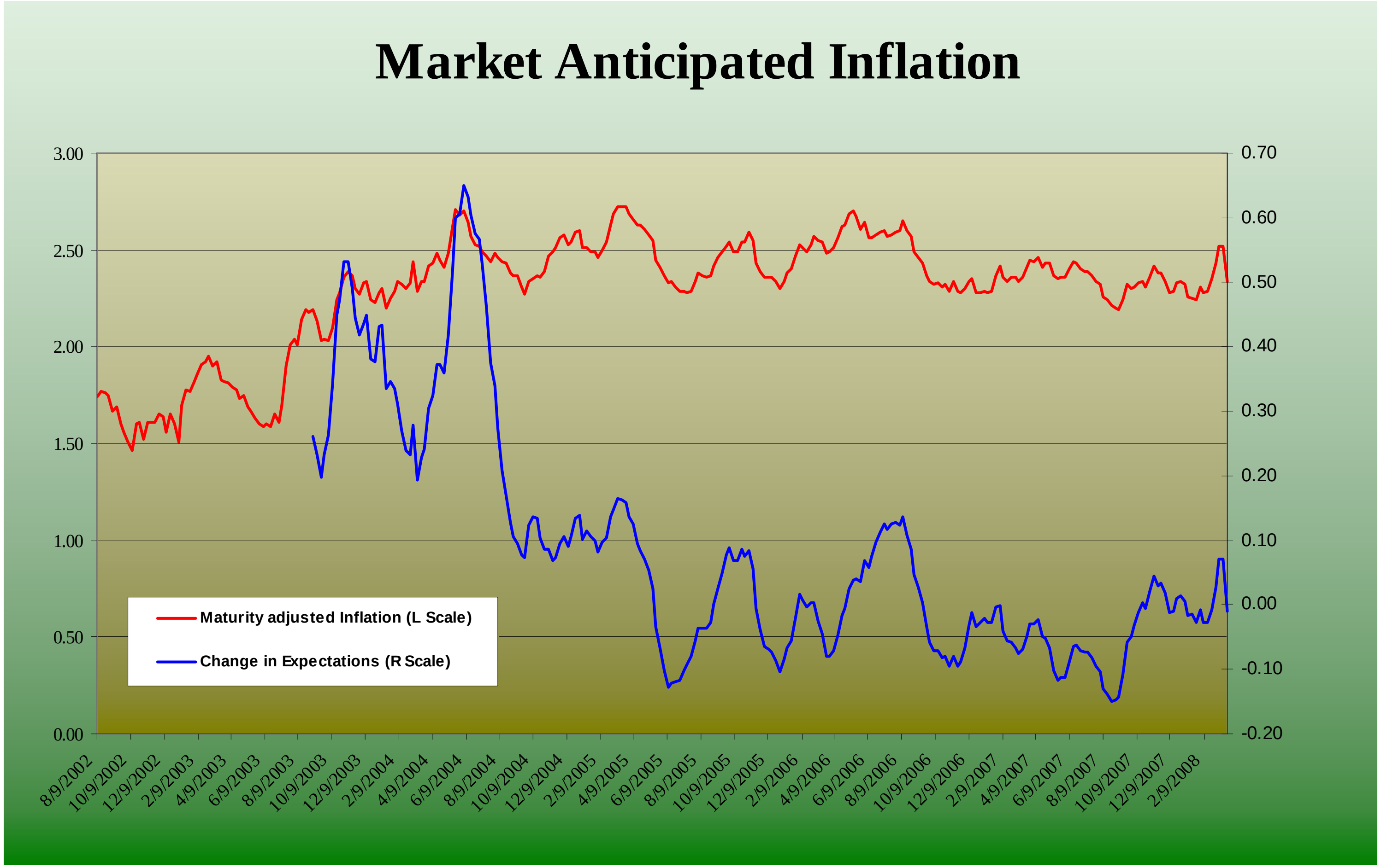
Retail looks to be in a rocky environment now that Mortgage Equity Withdrawal (MEW) is spent.

Inflation expectations

While inflation expectations in the USA have not come unmoored based on the 10 year TIPS and we don't believe that the Fed has printed any high power money, Gold has not been acting that way.

Getting the US$ to stabilize is critical to forward inflation scenarios. With a stable dollar would come stable oil prices and overall price pressures would moderate.

Inflation expectations



Long term inflation expectations have been steady so far…

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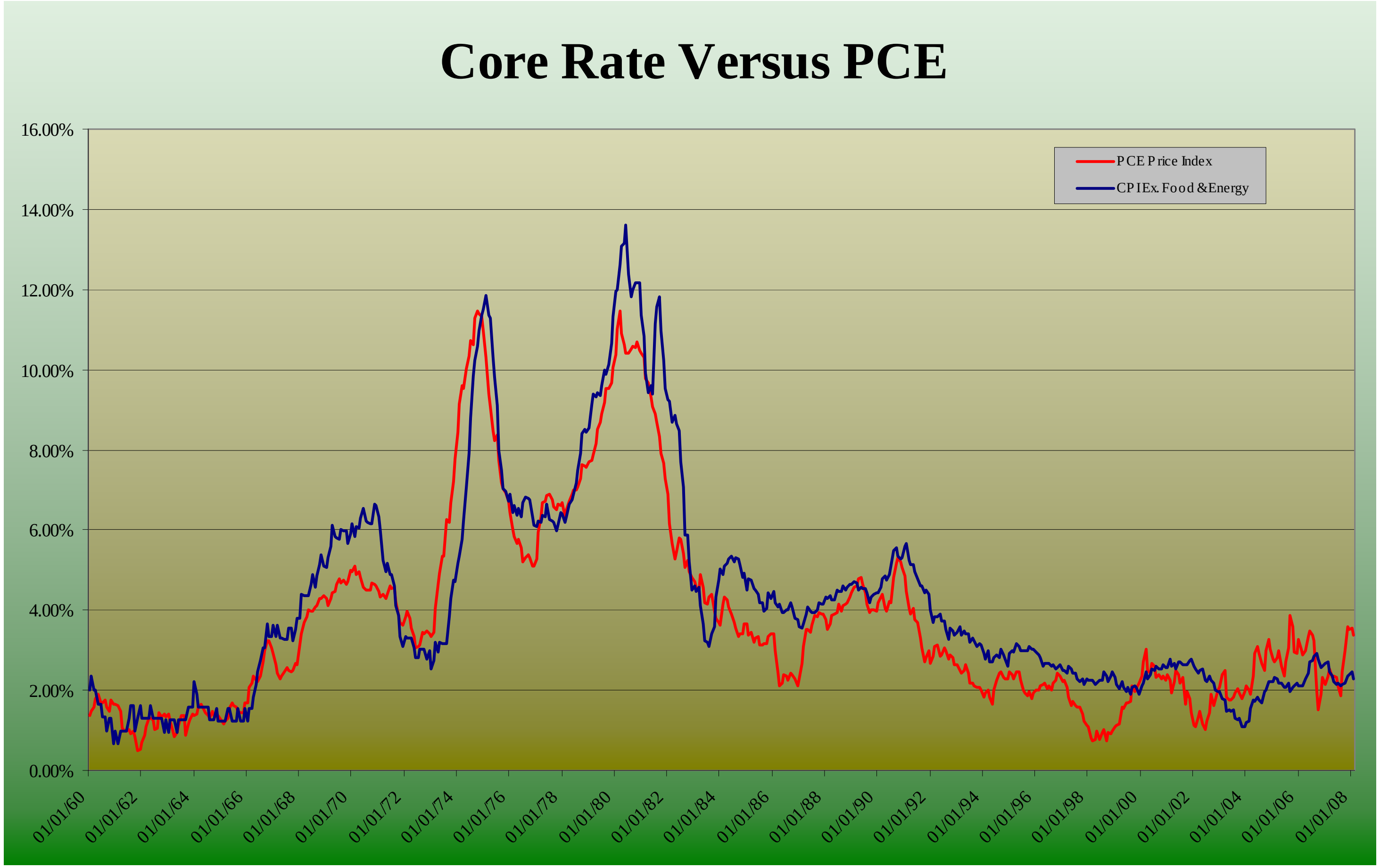
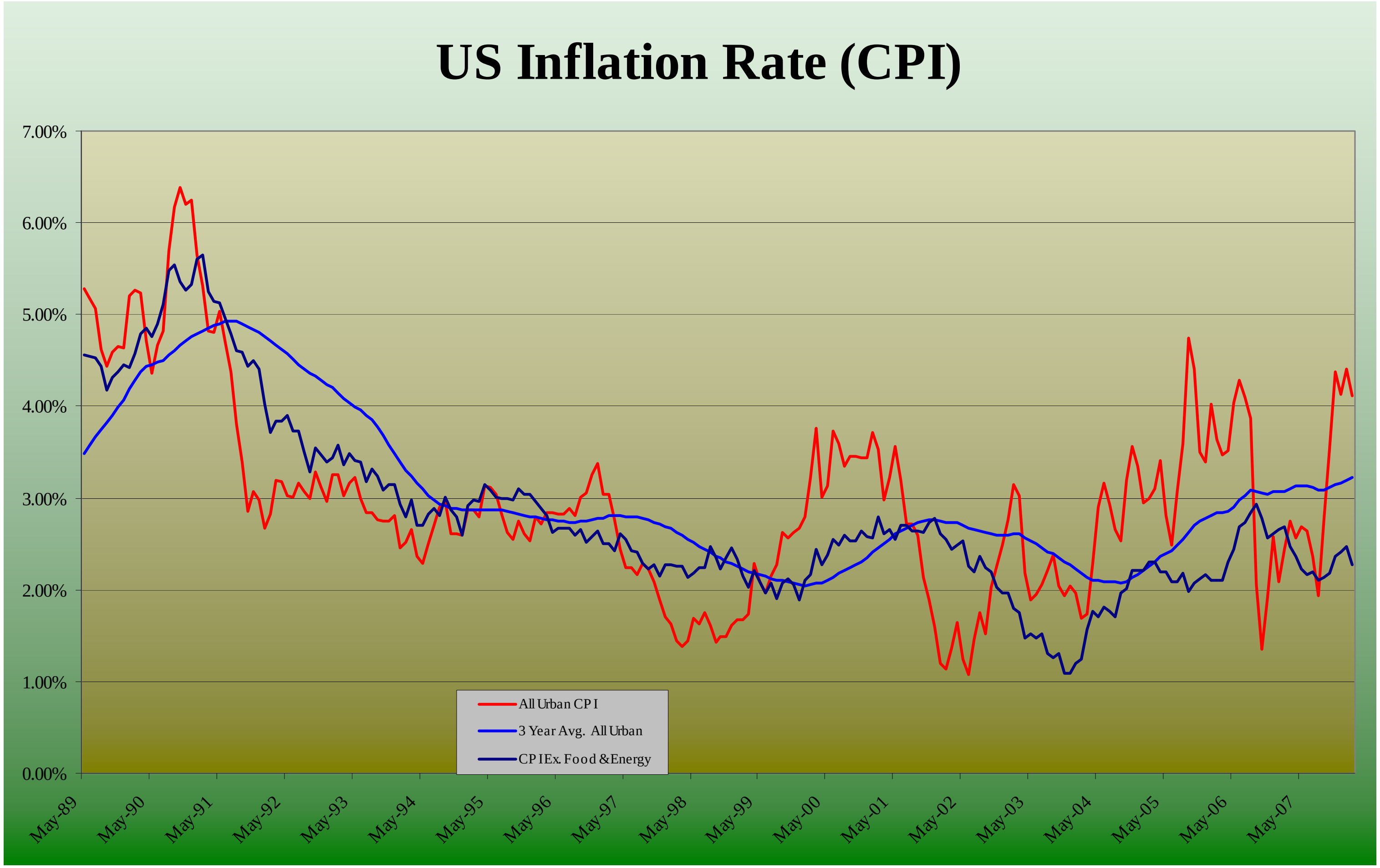
Inflation expectations



While it isn't the 70's, the numbers are elevated and the hawks on the Fed are squawking.

Inflation expectations



Look for the food and energy piece to come storming back… Packaged foods have not yet seen the raw price increases in the grains, they are coming.

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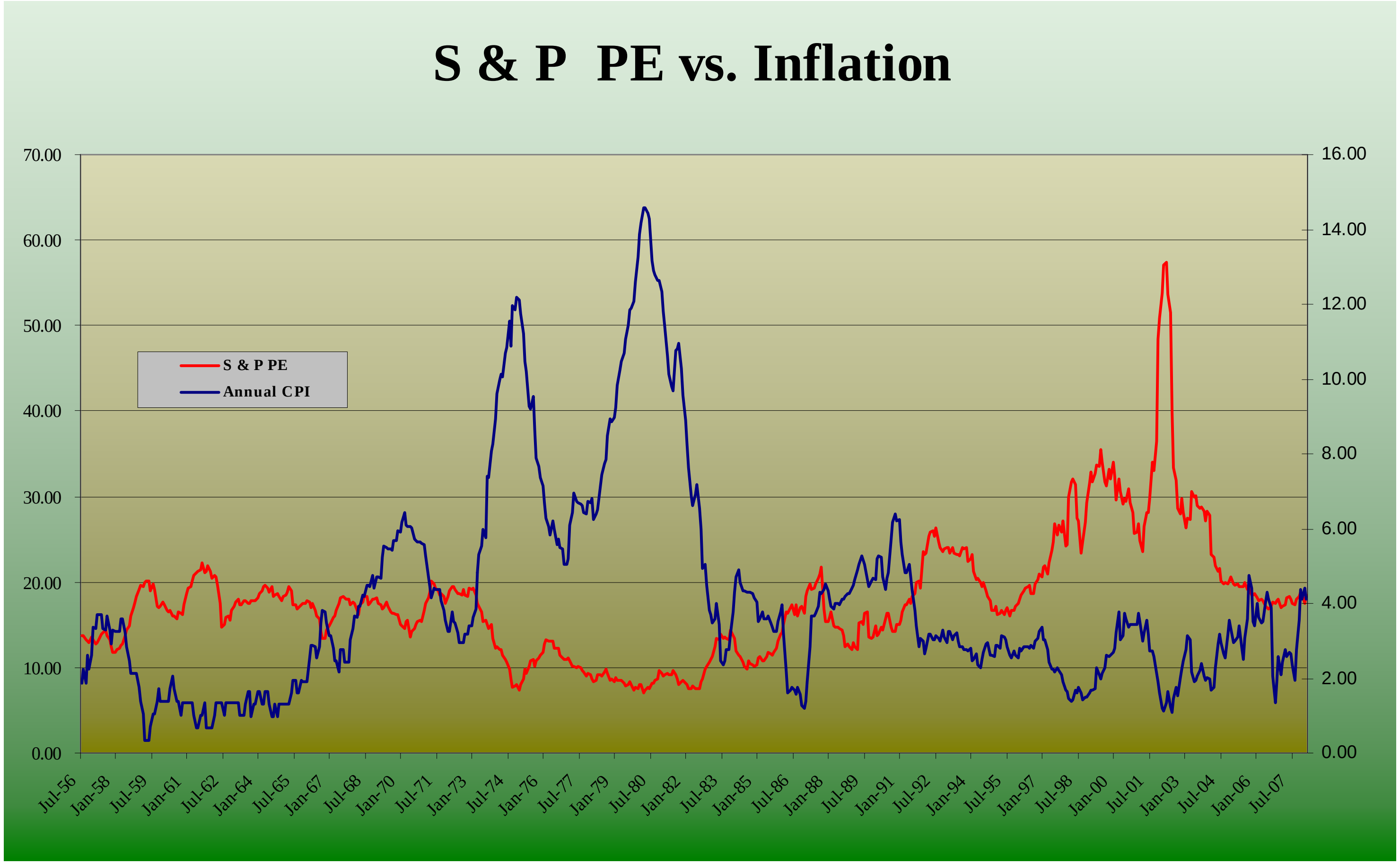
Inflation expectations



Inflation spiking higher could sink the P/E and really ruin the asset price control bubble. You think Banks are cheap today? Try them when the S&P 500 trades at 11x earnings. Ouch!

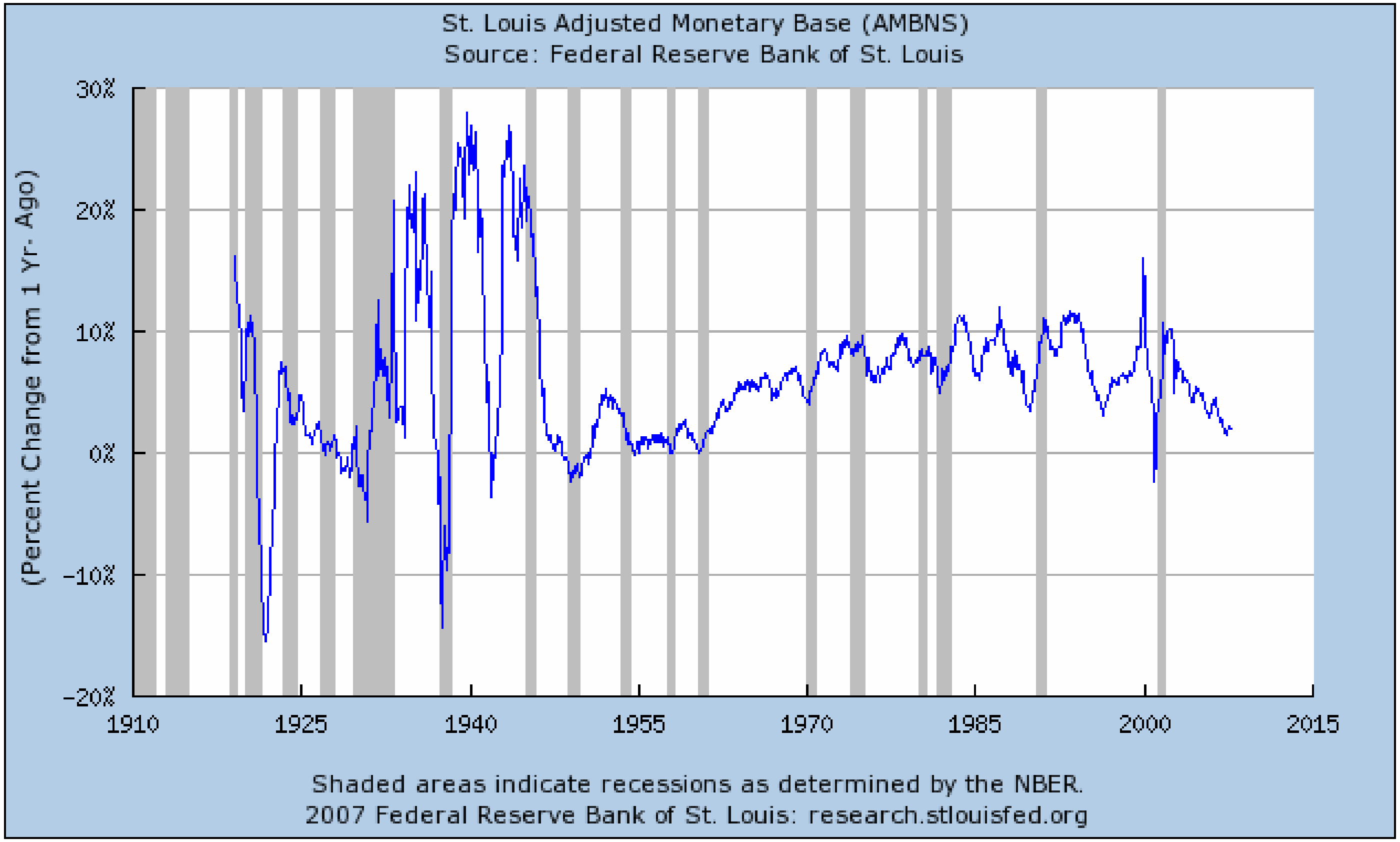
Federal Reserve Watch

50 bps there, 25 bps here…whatever it takes to keep charts pointed up. TLSF, ASAP, no recourse backstop. That's what they are gonna do…

Hopefully the Gulf Oil States won't abandon the dollar peg and spoil the party. We only get to print money to solve our problems because we are the world's reserve currency, our "exorbitant privilege.

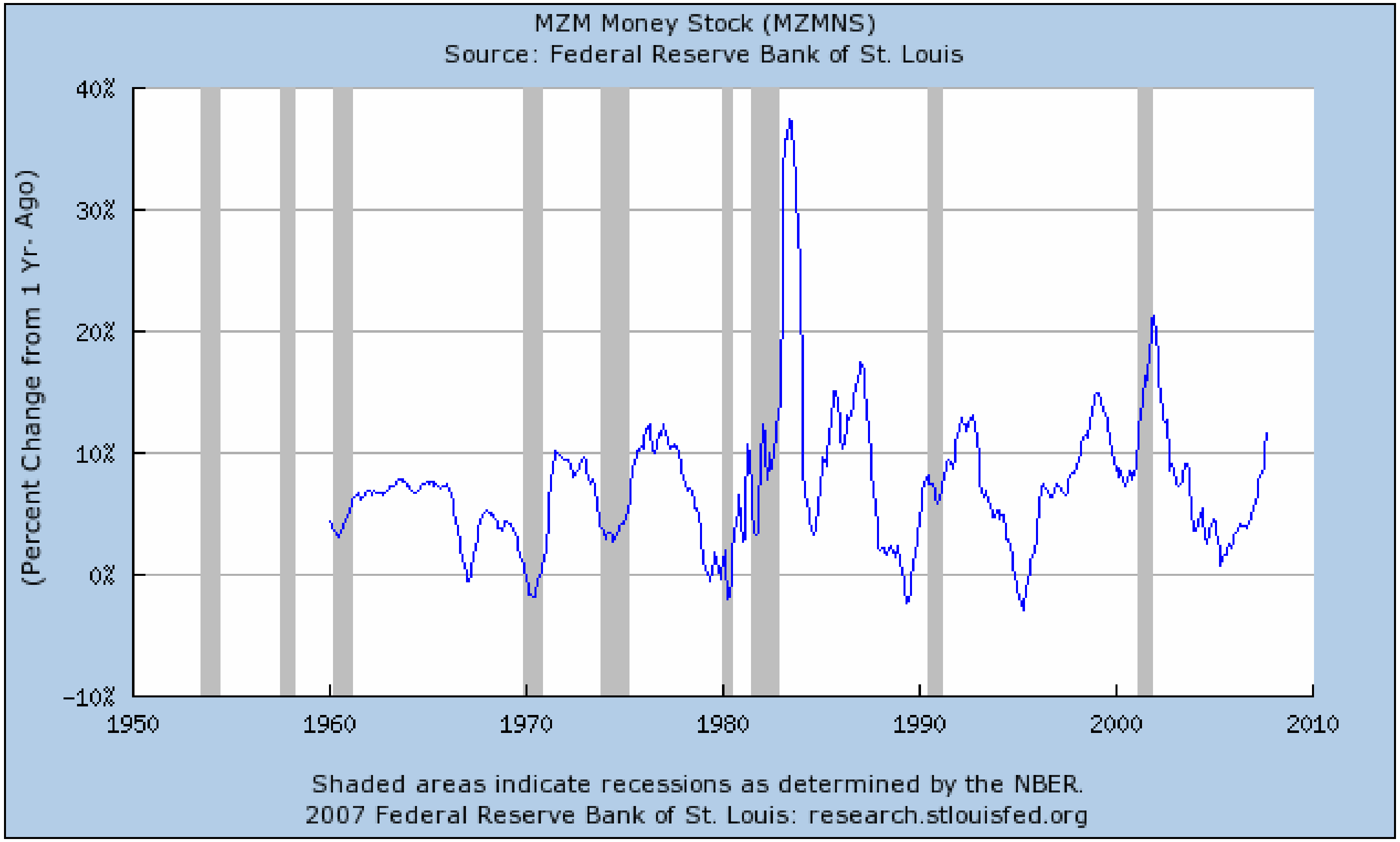
The Fed took the pressure off, but difficult decisions remain. *Let's take our medicine and get the bad assets off the books and move on.*

St. Louis Adjusted Monetary Base NSA Yr/Yr

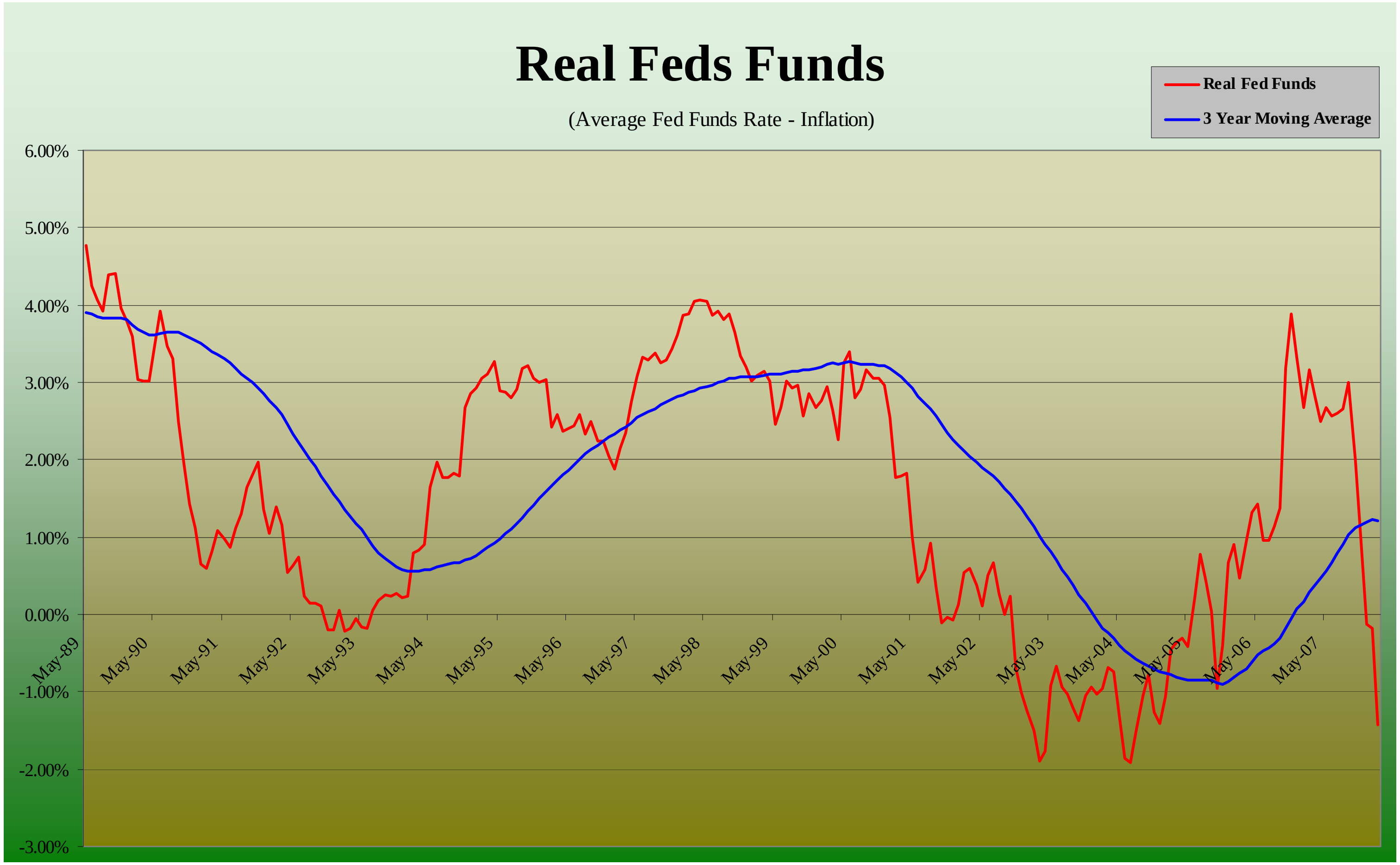


High powered money isn't even keeping up with all urban CPI? And we are blaming the Fed for money printing? How? They aren't using open market operations in the classic sense.

MZM NSA Yr/Yr

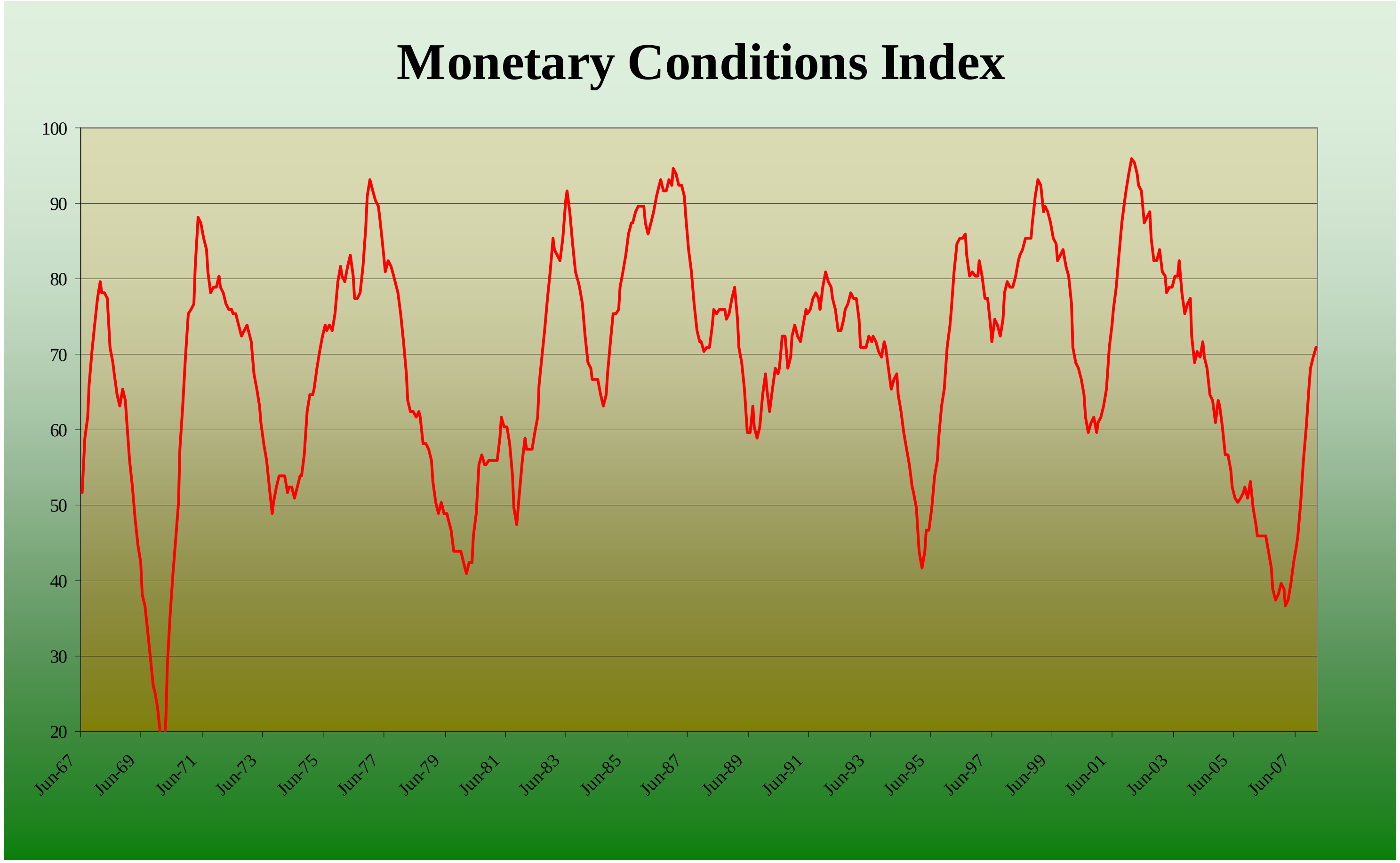


But MZM is really moving higher. Why the disconnect to the Monetary Base? Savings in the USA,….ha ha! No such luck. What the devil is it then?



Real Fed Funds was finally back to "normal" (not punishing savers), before the cutting began in earnest..

Federal Reserve Watch



Powerful Fed intervention. And, like many times in the past, this money finds its way into stocks and commodities quickly.

Federal Reserve Watch

The 3 month T-bill is going to need a real spread above whatever inflation really is to get the Gold/Oil/Dollar under control.

The Fed ***was trying*** to normalize things, and the wheels came off in the Subprime crisis.

Outlook

The Street seems to be settled on a melting up scenario with the US Economy just slowing, Global growth continuing and inflation moderating.

That sounds like a double barrel bet on the BRICs. Again, we say hope for the best, plan for the worst.