

July 15, 2008

Note

RE: Worst Enemy

A year ago, it was clear that a Real Estate bubble-burst was underway and that the Financial institutions who fed the speculative excesses of the period were going to pay dearly. Less evident was the ripple effect this problem would have on the rest of the economy. We can now look back and measure the damage done, or lack thereof, which the following table details.

Surprising no one is the big hit Financials have taken, driven by a 68% earnings decline. Compounded by the rise in energy costs over this period, Consumer Discretionary has been another hard hit Sector with a significant loss in corporate profitability. The big surprise of this table is the fundamental strength of the other eight Sectors.

EcnSec	July 3, 2007		July 9, 2008		Jul07 to Jul08 Change	
	Sum MktCap	Sum Earnings	Sum MktCap	Sum Earnings	MktCap	Earnings
Finan	3,662,336	265,370	2,140,371	85,369	-42%	-68%
ConDi	2,127,724	94,447	1,383,447	77,782	-35%	-18%
Utils	581,728	32,268	575,688	32,726	-1%	1%
ConSt	1,488,413	78,432	1,333,578	79,941	-10%	2%
HlthC	1,982,299	89,009	1,737,473	95,556	-12%	7%
Indus	2,016,177	105,558	1,648,861	115,069	-18%	9%
Mtrls	734,510	39,183	822,939	42,801	12%	9%
Enrgy	1,966,091	142,632	2,182,185	159,443	11%	12%
Telcm	669,102	25,226	474,114	28,780	-29%	14%
ITech	2,667,389	98,140	2,300,612	112,980	-14%	15%
Total	17,895,769	970,263	14,599,268	830,447	-18%	-14%
			Sans Finan		-12%	6%

Earnings are the ultimate measure of corporate health. With the exception of the two obvious problematic Sectors, corporate earnings have strengthened over the past year, yet the market has substantially sold-off in a largely indiscriminant manner. Strip out the emotions of the day and it's plain that paying less to get more is a pretty sound investment proposition, but not one an investor caught up in a panic will heed. This is a timeless issue, as Benjamin Graham observed decades ago, *"the investor's chief problem – and even his worst enemy – is likely to be himself."*

Helpful when the market gets hairy is an independent examination of the fundamentals that underlie it. When stock prices are falling at the same time most of corporate America is growing earnings, it's a buying, not a selling, opportunity. If one could invest in a vacuum, this would be an easy proposition, but our media-laden world makes investment life more challenging and consequently emotional control imperative.

In addition to the above, perhaps yesterday's enclosed Wall Street Journal article will prove insightful.

Keep the faith!

Lowell

http://biz.yahoo.com/wallstreet/080714/sb121582067258747665_id.html?v=1