
Critical Math Advisors

Quarterly Newsletter



October 2011

VOLATILE TIMES

The quarter ending September 30th was the worst quarter for U.S. equities since 2008. In Europe, it was the worst quarter in 9 years. Many financial stocks were down double digits for the period.

There may be a disconnect between the stock market's performance and economics. There have been reports from CEOs of American companies saying that their businesses are doing quite well. It has also been widely reported that companies are sitting on huge hordes of cash. However, reported data suggests that companies are not hiring, assumptively due to a lack of clarity regarding future employee related costs, particularly regarding healthcare and regulatory expenses. Economists have said that we need 300,000-400,000 new jobs per month to grow the economy. We have not seen that kind of growth in quite a long time.

Notwithstanding the seemingly favorable corporate observation, a widely respected publication, The Economic Cycle Research Institute (ECRI), said that there is a recession coming that can't be averted. ECRI has correctly called the last 3 recessions and recoveries without triggering any false alarms.

There seems to be a staggering amount of data affecting worldwide markets, including the possibility of a significant downturn in China. Should that occur while Europe and the United States are weakening, that could indeed enhance the likelihood of a further down leg in equities.

The Federal Reserve seems to have done whatever it can to use monetary policy to attempt to shore up markets. The problem seems to be that fiscal policy is what needs to be addressed, and that, of course, is the purview of the legislative and executive branches of government. It will be interesting to see if they can provide the necessary leadership.

Asset Management through Adaptive Allocation

A MULTI-STRATEGY and ACTIVELY-MANAGED APPROACH to INVESTING

which seeks to adapt to any given market environment, reducing market exposure when risk is deemed high and investing aggressively when risk is considered low.

GREECE IS THE WORD

Greece is broke by any definition. The powers that be in Europe seem to have a different plan every week for dealing with their debt crisis. It must be noted that the European Union is comprised of individual countries, with a currency that is relatively new, and to which not all European countries are members. Greece is not even the problem. It is such a small part of Europe economically that if it didn't exist, it would not significantly matter. If, however, other countries were to be tainted and adversely affected by this debt crisis, there could be serious repercussions. Currently, the primary concern is Spain or Italy, each of which has a different set of national difficulties and priorities. Spain has an exceptionally high unemployment rate and a very large problem of residential overbuilding. Italy has a huge tax evasion problem.

Many of the southern countries, including Italy, Spain, Portugal and Greece, have spent far too much and incurred too much debt relative to their national economies. The "frugal" northern European countries, such as Finland, Holland and especially Germany, are being asked to "bail out" their profligate southern neighbors. German Chancellor Angela Merkel has the unenviable task of trying to convince the German people that preserving the Euro and the Economic Union is less painful than not doing so. Unfortunately, in local elections during the past year, her party has been consistently defeated. Politically weakened, her task is that much more difficult. There are many moving parts in Europe, including national governments, the ECB, the IMF and others, which makes it very different than the United States. Here, for better or worse, we only have to deal with the Congress.

Up until now, all of the attempted solutions to the European crisis have been a day late and a dollar (or Euro) short. It is hard to imagine that when Greece defaults, or more politely is "restructured," that the stronger European countries and/or banks are not forced to shoulder a huge percentage of the losses. Only time will tell how long this cloud hangs over the global financial markets.

Critical Math Advisors has moved !!!

Our new location is:

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A POSSIBLE SOLUTION TO THE U.S. HOUSING CRISIS

Many millions of homes are already in foreclosure. Wouldn't it be nice if at least future potential foreclosures could be forestalled? How about this solution. Many homeowners are faced with the difficulty of their current home values being less than the amount of their mortgage, commonly known as being "underwater." Many of these mortgages are guaranteed by Fannie Mae and Freddie Mac, the two quasi-governmental agencies that have been so badly managed. A significant amount of these mortgages that are current and presently not behind in their payments cannot be refinanced because there is no equity in these properties. What if they were able to be refinanced so that homeowners who are current in their payments and have sufficient income to make those payments are allowed to refinance at rates around 4%, instead of the rate on their current mortgage of 6%, 7% or 8%. The key to this idea would be that their monthly mortgage payments would not be reduced. The money saved on reduced interest would instead go to reduce principal. In this way, banks would reduce their exposure and homeowners would be closer to building equity. The potential for future foreclosures might then be greatly reduced. Since Fannie and Freddie are already on the hook, they would benefit by a decreasing amount that would have to be guaranteed. The banks, of course, would have to have some incentive to do this or at least not be disincentived, as is the case currently. Is anyone in Congress listening?

Investment Strategy Positions as of September 30, 2011

(Subject to Change without Notice)

RUSSELL 2000 INDEX (IN, INVERSE OR CASH)	INVERSE	HIGH YIELD CORPORATE BONDS (IN OR CASH)	CASH	INFLATION PROTECTED BONDS (IN OR CASH)	IN
S&P 500 INDEX (IN OR CASH)	CASH	HIGH YIELD MUNICIPAL BONDS (IN OR CASH)	IN	FOREIGN BONDS (\$ US HEDGED) (IN OR CASH)	IN
EMERGING MARKET EQUITIES (IN OR CASH)	CASH	CONVERTIBLE BONDS (IN OR CASH)	CASH	REAL ESTATE INV. TRUSTS (IN OR CASH)	IN
STOCKS (NUMBER OF HOLDINGS)	0				

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How to Contact Critical Math Advisors

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