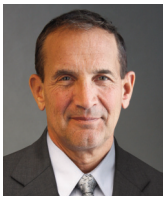

Strategist's Corner | November 1, 2011
by James Swanson, CFA
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The U.S. economy is ignoring the press, the polls, and even the market

Despite the critical press, negative sentiment surveys, generalized gloom, and even rioting, the U.S. economy and most economies of the emerging world continue to expand.

How is this possible?

- Business expansion in the United States is not faltering and in fact seems to be gathering momentum as we head toward 2012.
- European finance ministers have listened to the markets and have decided to act with conviction to prevent a domino-style collapse of the banking system. No solution, but better than expected.
- Equity and credit markets, shattered by volatility in the early summer and a sense of impending doom in August, have priced in some dire outcomes that do not now appear to be supported by the facts.

What are the facts?

- U.S. industrial production is rising; in the third quarter it was up 5.1%.
- Capacity utilization in the United States is edging higher. It was most recently at 77.4%.
- U.S. corporate profits, as measured by Standard & Poor's 500 Stock Index companies reporting, are stronger.
- Corporate revenues in the United States, all through the troubled third quarter of 2011, have gained at a pace that is three times the pace of nominal U.S. gross domestic product growth.
- U.S. consumers, written off for dead, seem to be alive. Retail sales are running 4% higher than at this time in 2010.
- Personal consumption, as measured by the U.S. government, has been rising at a real rate of 2.4%.
- U.S. car and new home sales have all been moving up from previous lows and very depressed levels.

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Conclusion

There has been an avalanche of negative surveys of U.S. corporate and consumer sentiment. However, people are behaving quite differently than these surveys would lead us to expect. Company captains are ordering more equipment and are expanding their businesses. And the average consumer is still finding his or her way to the store and buying online.

Markets, meanwhile, are priced for a more negative outcome than the facts would suggest. By historical standards, U.S. large-cap equities are trading at lower-than-normal P/E levels, and the U.S. credit markets have priced in dislocations that do not appear to be occurring.

The world's debt problems are still with us. But finally the leaders of the developed world seem to understand that there has to be a plan to reduce debt and encourage growth. The markets will next worry about the November 23 deadline in the United States for the report of the Deficit Super Committee. Meanwhile, a shortage of yield haunts the savers of the world, and companies continue to be more productive and make money in a slow and uncertain environment.

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