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Weekly Market Wrap

December 17, 2007

Review - Week Ending 12/14/2007

Stocks were down 2.0-2.5% across the broad market indexes last week as investors were disappointed by the Fed's 25 basis point rate cut. A few days later they found out why the fed is still worried about inflation, and stocks fell again. This week has a full calendar of economic data and should provide addition year-end trading fodder.

Commentary/Highlights

- **Following the Fed's rate cut, the Fed announced the next day a coordinated plan to auction short-term funds into the banking system through January. The ECB, Swiss Bank, Bank of Canada, and Bank of England will participate.**

- **Return of Stagflation?** On Thursday and Friday the market found out why the Fed has remained concerned about inflation. The PPI rose 3.2% in November, the 2nd highest monthly reading since 1947, and the next day the CPI showed an increase of 4.3%, 2.3% annually at the core level. Though most of the increase is from $100/bl oil and $10/bu wheat, the prospect of inflation tying the Fed's hands became real. Stagflation was much discussed over weekend, including comments from Greenspan. **European inflation rose to 3.1%, above 2.5% comfort zone. However, the ECB will likely refrain from increasing rates due to slowing global growth.**

- **Moody's Economy.com announced its Risk of Recession today at 52%, reflecting an economy that is "hanging by a thread".** It reflects consumer spending that has been dampened by the housing crisis, and business and consumer confidence levels that are both at multi-year lows.

- **Emerging market debt remains a favorite of institutional investment firms**. PIMCO has remain positive on the asset class due to more stable and growing economies, aided by strength in oil and commodities. 42% of emerging market debt is now investment grade. JP Morgan expects $40 billion in additional EM debt flows in 2008.

- **Good News? Take the Long View**: Long-term investors are reminded to keep their long-term horizons in focus. Recession talk is the headline, but <u>the economy and stock market do not always move together</u>. We have had 16 quarters of negative growth over the last 30 years and three recessions of two or more negative quarters. **The average one-year out market gain after negative GDP quarters: +5.07%, after recessions: +18.63**%. The AAII Sentiment Poll has had **11 weekly readings with bearish sentiment over 55% during the last 20 years, the market gained 21% one-year after the July 2006 reading and 33% one-year after the February 2003 reading.**

Index/Portfolio Returns	% Change Week	% Change QTD	% Change YTD
Lehman Aggregate Bond	-0.16%	+1.73%	+5.64%
Lehman High Yield	+0.12%	-1.24%	+1.93%
Dow Jones Industrial	-2.06%	-3.55%	+9.35%
S&P 500 Index	-2.40%	-3.48%	+5.35%
Russell 3000	-2.62%	-3.59%	+4.87%
MSCI EAFE Index	-3.47%	-2.49%	+8.13%
MSCI EAFE Small Cap	-3.29%	-4.73%	+1.87%
NASDAQ Composite	-2.60%	-2.43%	+9.13%
Russell 2000	-3.98%	-6.18%	-3.22%