

The Three Seasons

The snow is melting. The days are getting longer, the fields will soon be green again, and once more, migrating deer will be dodging highway traffic. Some things never change.

But over on Wall Street, the thought leaders think everything has changed. Over the past few months, we've read commentary from Wall Street analysts who speak of "the new normal." This theory argues -- dangerously, we think -- that "this time it's different." According to them, global aggregate demand has been permanently impacted by the events of the Great Recession. In other words, consumers won't repeat the spending binges of the past, since this new environment won't ever allow for easy credit again.

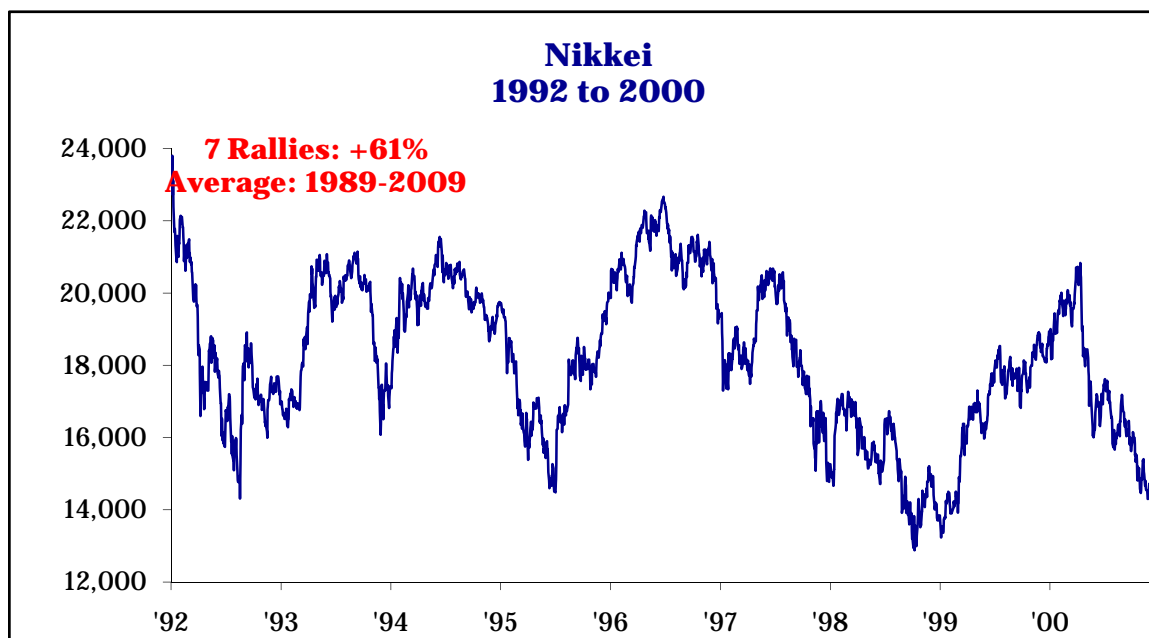
This troubles us for a number of reasons. First, we're loathe to believe any pundit who boldly claims "this time it's different." Investors who claimed that during the tech bubble in 1999 included those who loaded their portfolios with Enron and WorldCom. These were likely the same folks who thought housing prices would never decline, nor could they imagine a world without Bear Stearns and Lehman Brothers.

Secondly, it seems clear that we will be led out of the Great Recession by corporate spending, not consumer spending on housing and autos usually associated with a business cycle recovery. While the consumer is still nervous about the negative equity in his house and bleak employment opportunities, corporations have been reaping the benefits of lower expenses (due partly to last year's massive personnel cuts), lower input costs, reduced debt levels, and restrained capital spending. Consequently, corporate cash flows now significantly exceed capital spending, leaving the door open for a corporate-led capital expenditure binge that will also include new job creation.

The point is that there is rarely "a new normal." The economic and business cycles dance the same tango throughout the history of our capitalistic system, but sometimes the tempo changes. Put another way, as our friends at Strategas Research Partners suggest, we could be

entering a period of time in which the typical 5-7 year economic cycle is compressed into 3-5 years. The new regulatory environment will create circuit breakers intent on preventing another bubble. Most likely, the impact will be to nudge the economy back into a recession, albeit, a milder one, sooner.

What this all means for your portfolios is that, with shorter economic cycles, we will likely see more volatility. More importantly, the traditional “buy and hold” investment style will not work. It will become even more critical to invest more tactically. If you look at Strategas’ chart below, you’ll see the Japanese market from 1992-2000. While the overall return on the market was negative, the Japanese experienced *seven rallies averaging 61% each*. Had investors not been watching the cycles carefully, they would have lost money instead of having the opportunity to participate in significant rallies.



ClearRock’s investment model is based precisely upon these macro-economic cycle shifts. Our weekly proprietary economic “dashboard” informs our asset allocation decisions. We track the most significant data points as they are released, and interpret them in the

context of their impact on each of our investible asset classes. When the sum of these data implies a trend, we will tilt our model portfolios' allocation accordingly. Note that this tactical sector rotation is quite different from market timing. We are nearly always fully invested; we are simply shifting our allocations to those asset classes and sectors where we believe the best returns will be available. The key is that there are opportunities to enhance returns during periods of volatility by tactically managing portfolios.

The need to entrust a skilled and experienced investment manager has never been clearer. No matter what the season, we know that it doesn't pay to mess with Mother Nature.

The ClearRock Capital Team