

Monthly Chartbook

July 2007

Double, double toil & trouble

-Macbeth, W. Shakespeare

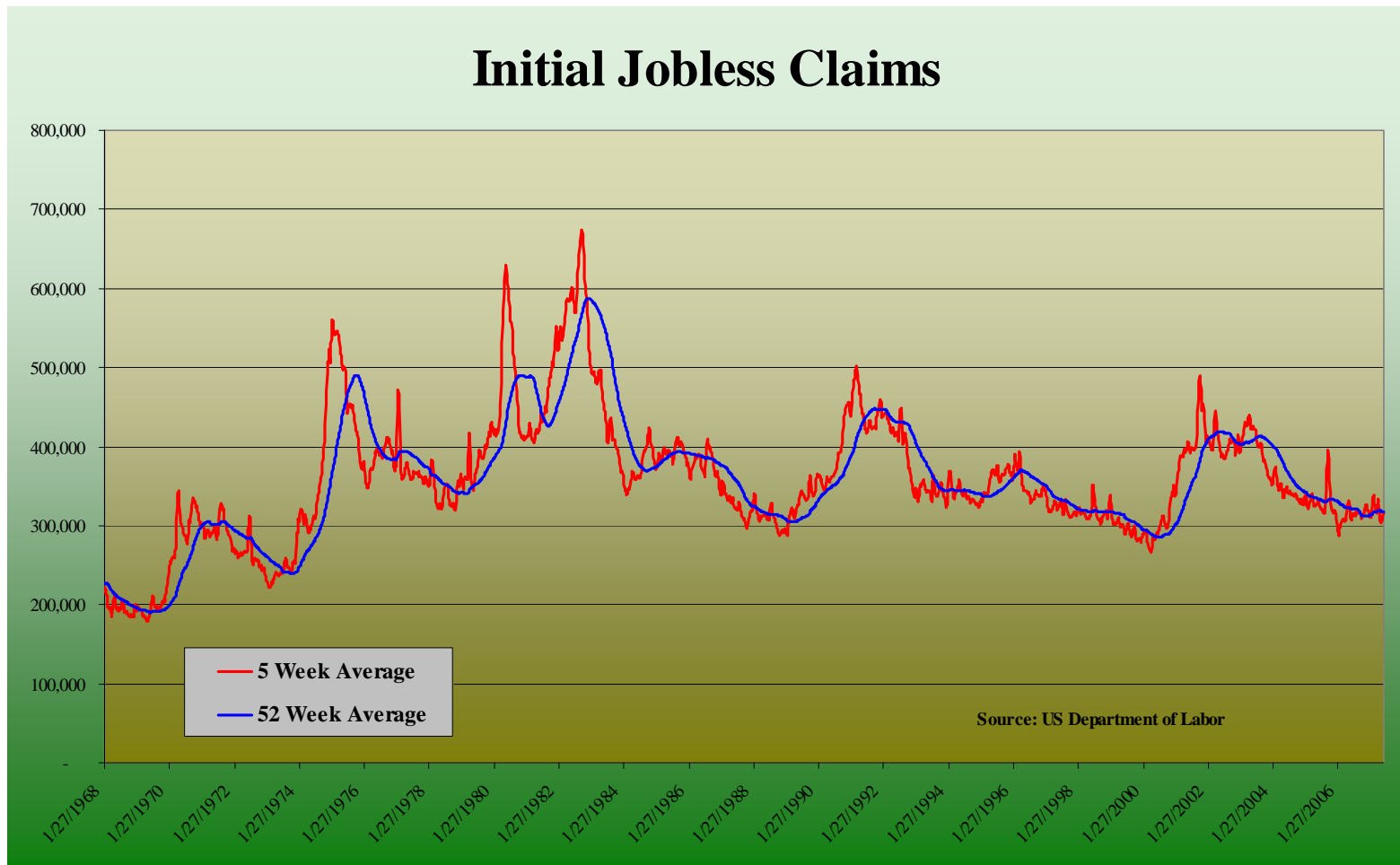
Betting on ever-high stock prices fed by a *witches brew* of “global liquidity”, private equity buyouts, and share buy backs?

Nothing about great fundamentals or valuations?

We scan the globe for low hanging fruit monthly, and currently find very little.

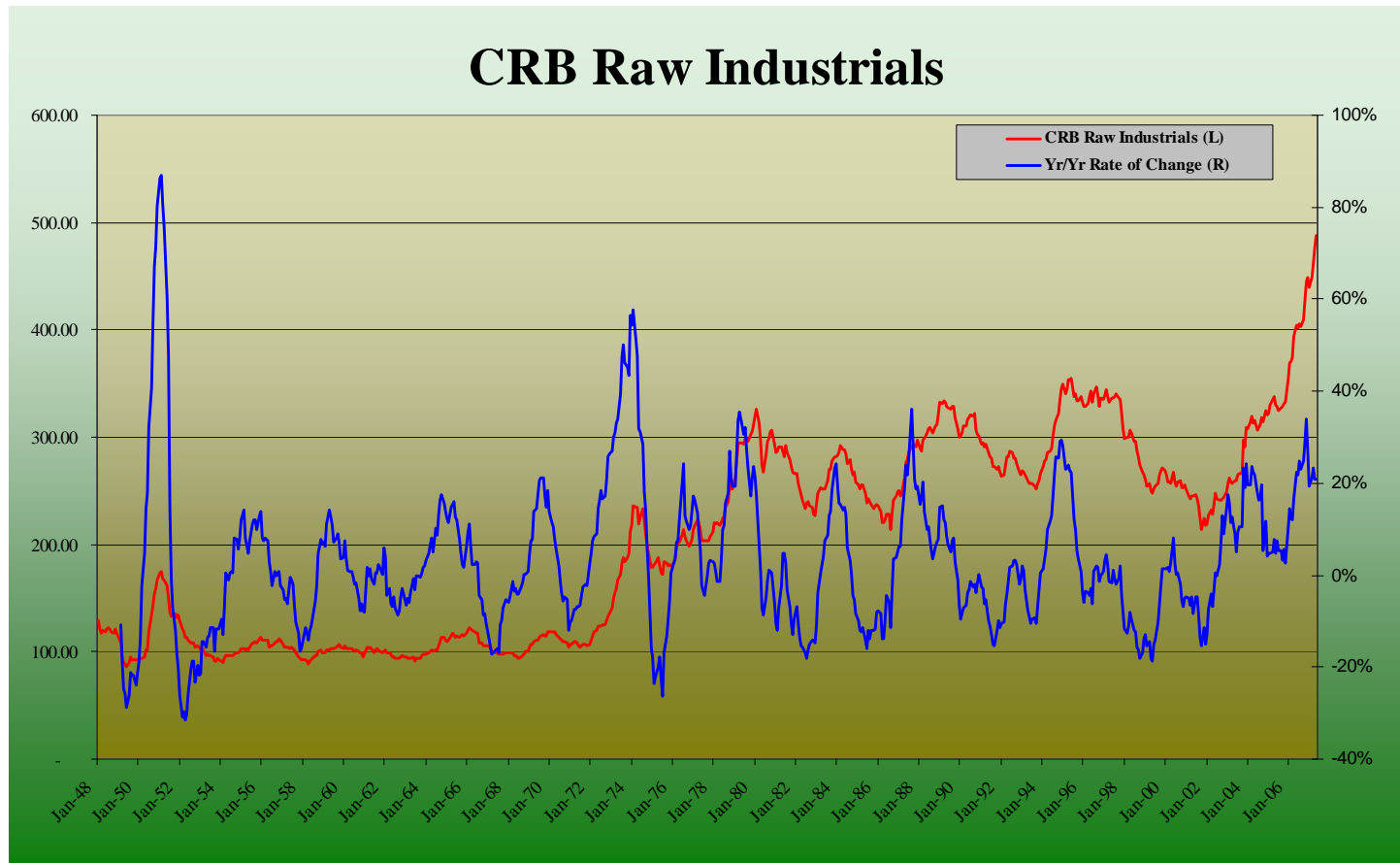
Where is the margin of safety?

Macro-economic research



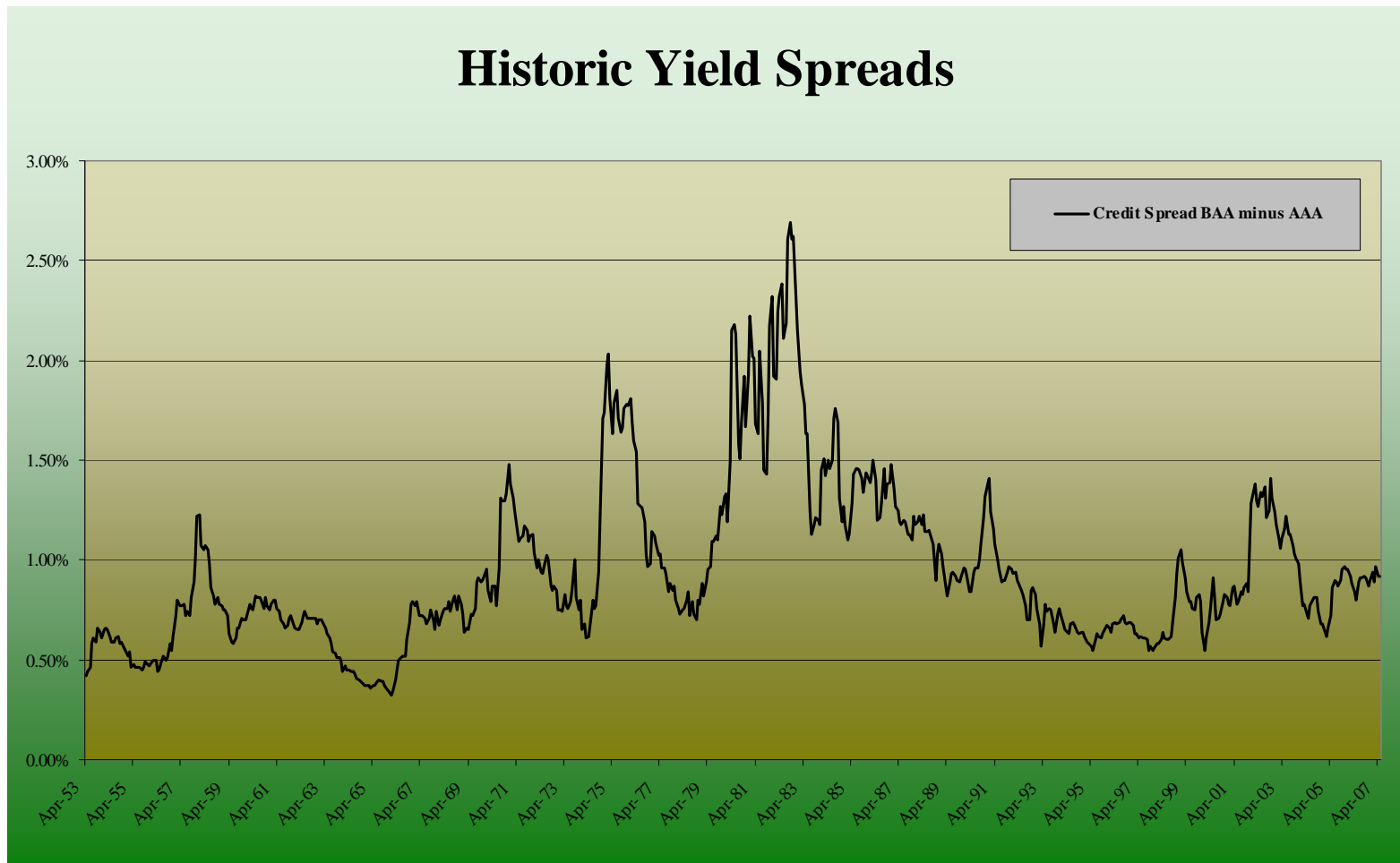
Jobless claims are at a level consistent with expansion.

Macro-economic research



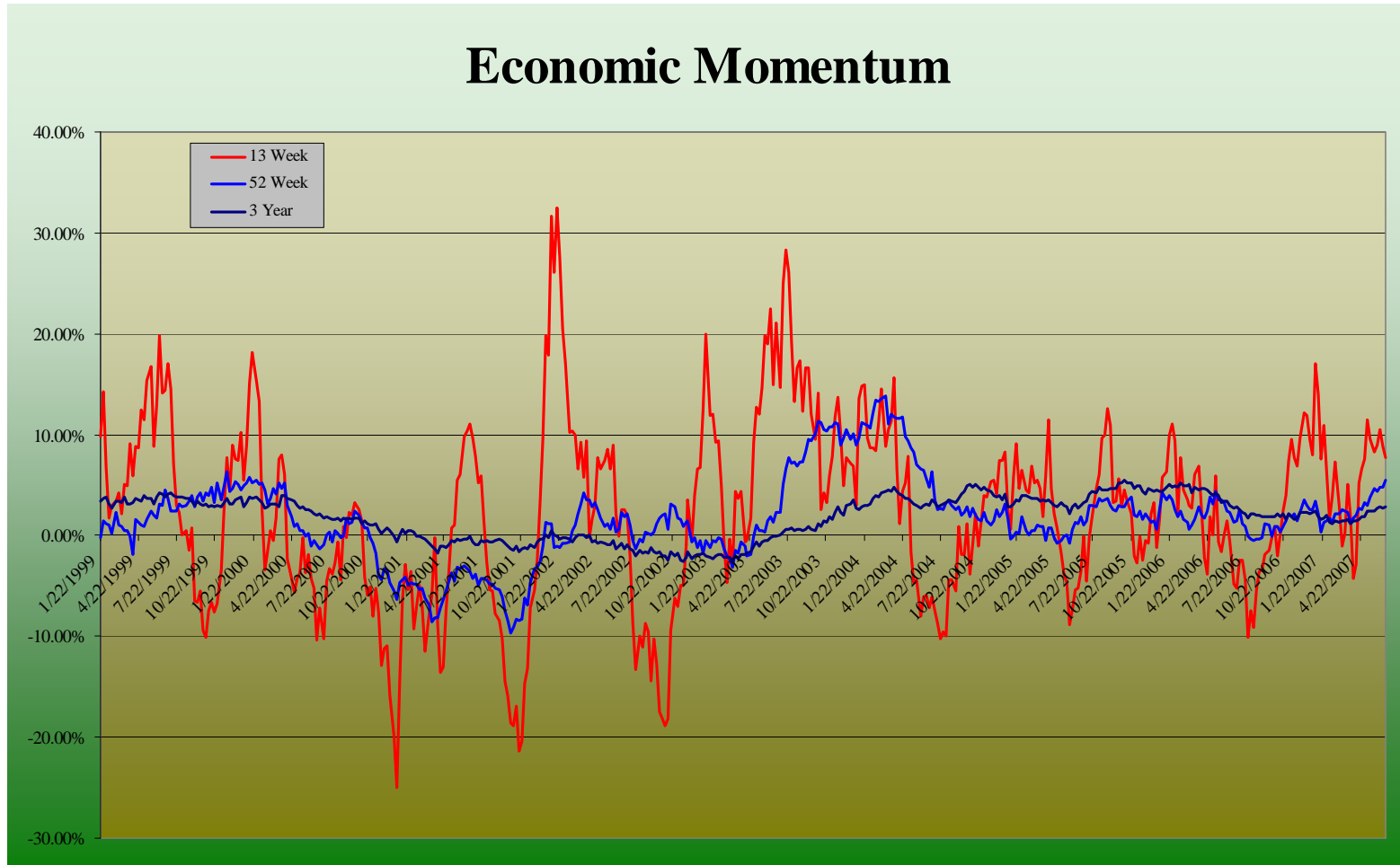
Sensitive industrial commodities are signaling continued expansion

Macro-economic research



Credit spreads have been well behaved.

Macro-economic research



The annual change of the ECRI weekly leading indicators are at a level consistent with growth.

So if the outlook is for continued growth, why the cautious outlook?

There is no margin of safety in valuations when (not if) something inevitably disappoints.

The markets haven't just wagered that rates will stay low and growth will continue, *markets have bet their life on them.*

Inflation expectations

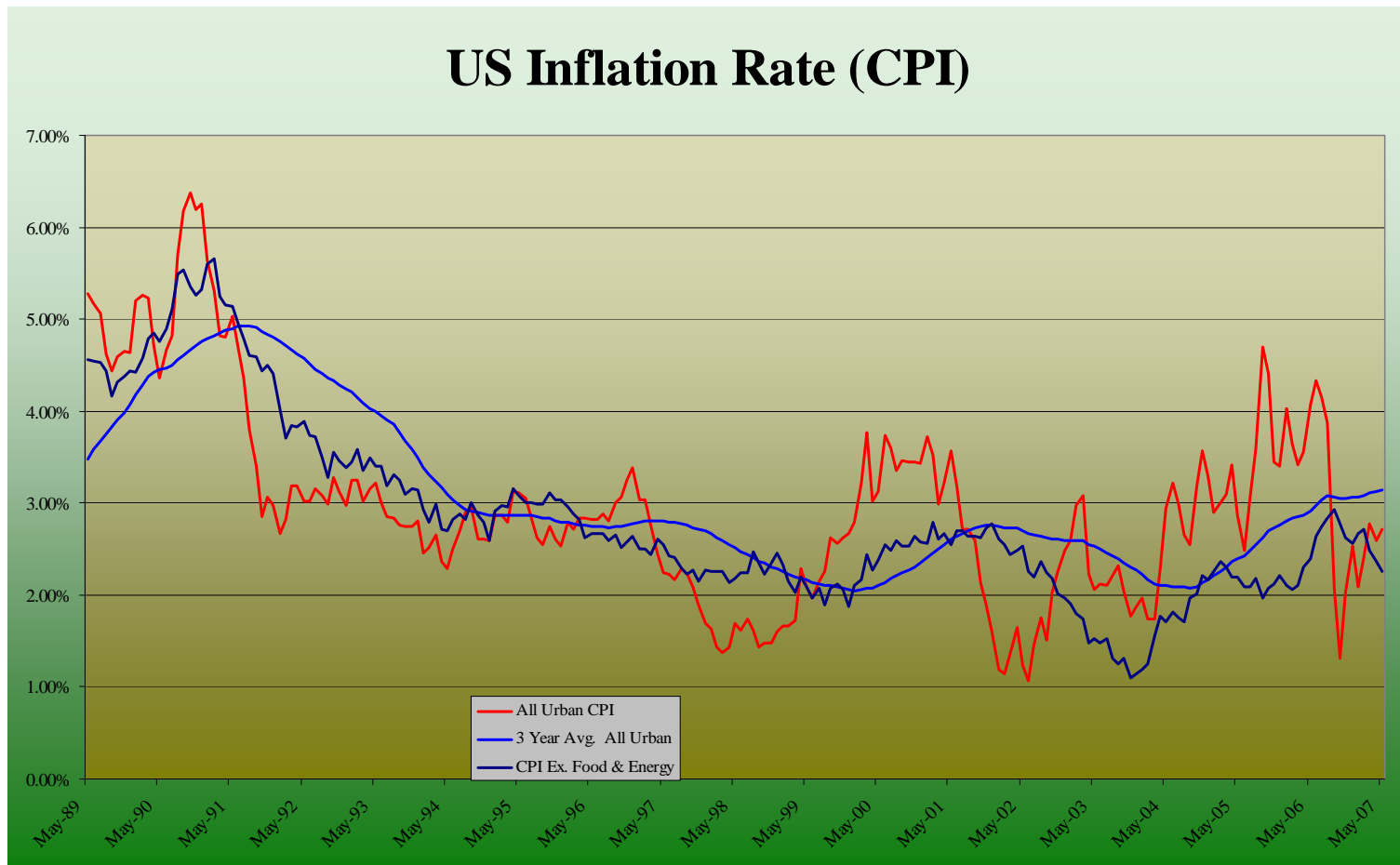
What the headline rate, the core rate, PCE, oil, and gold prices are all telling us is that prices are much higher than just a couple of years ago. Duh.

Great if you are a commodity producer, not so great for the average consumer.

Food and energy costs have bled into the so-called core rate of inflation, next stop...wages.

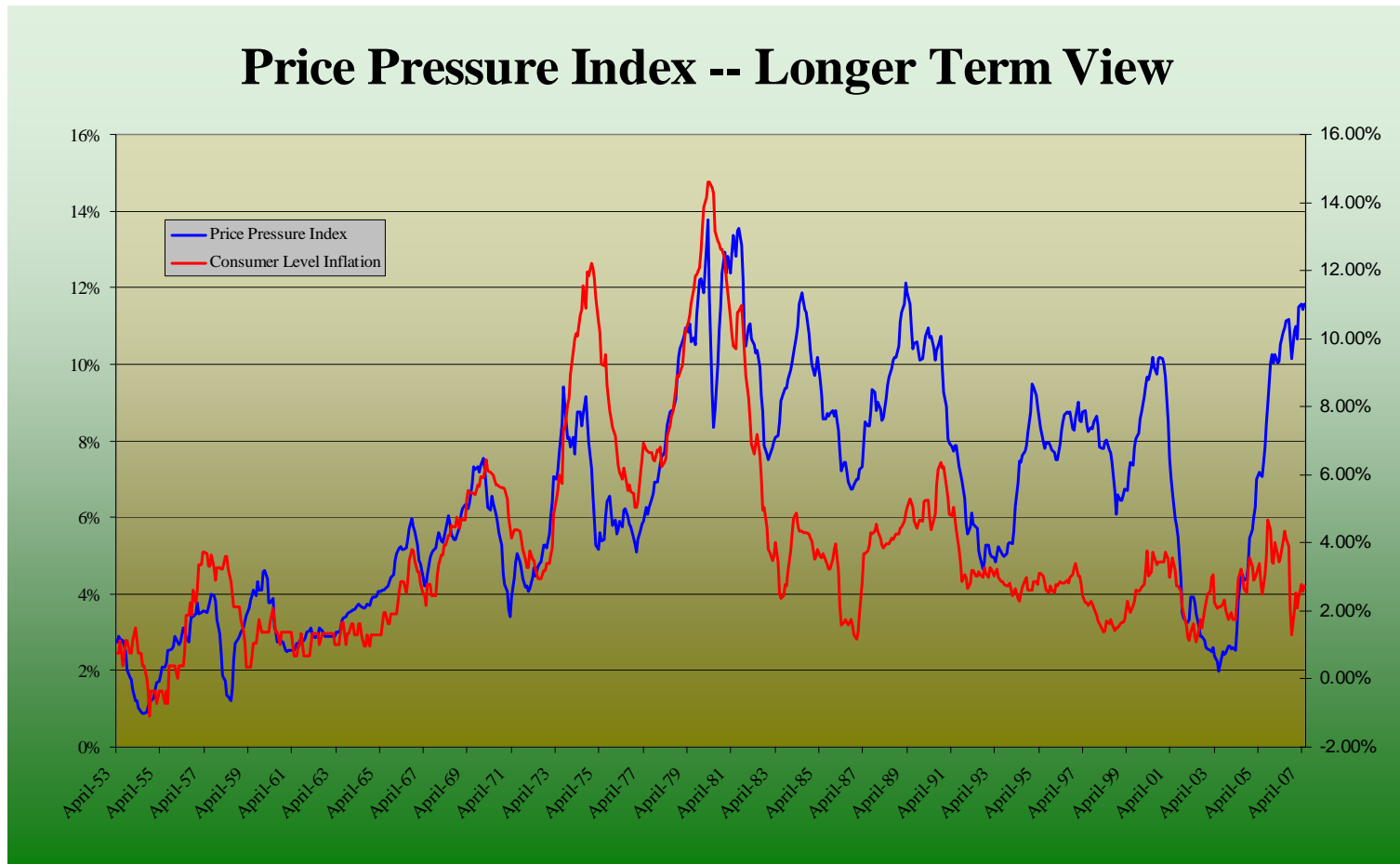
Let's see how much Dr. Ben likes it when wage increases stick, because if we don't go into a recession and we stay at or around trendline growth, it is hard to see prices climbing down dramatically.

Inflation expectations



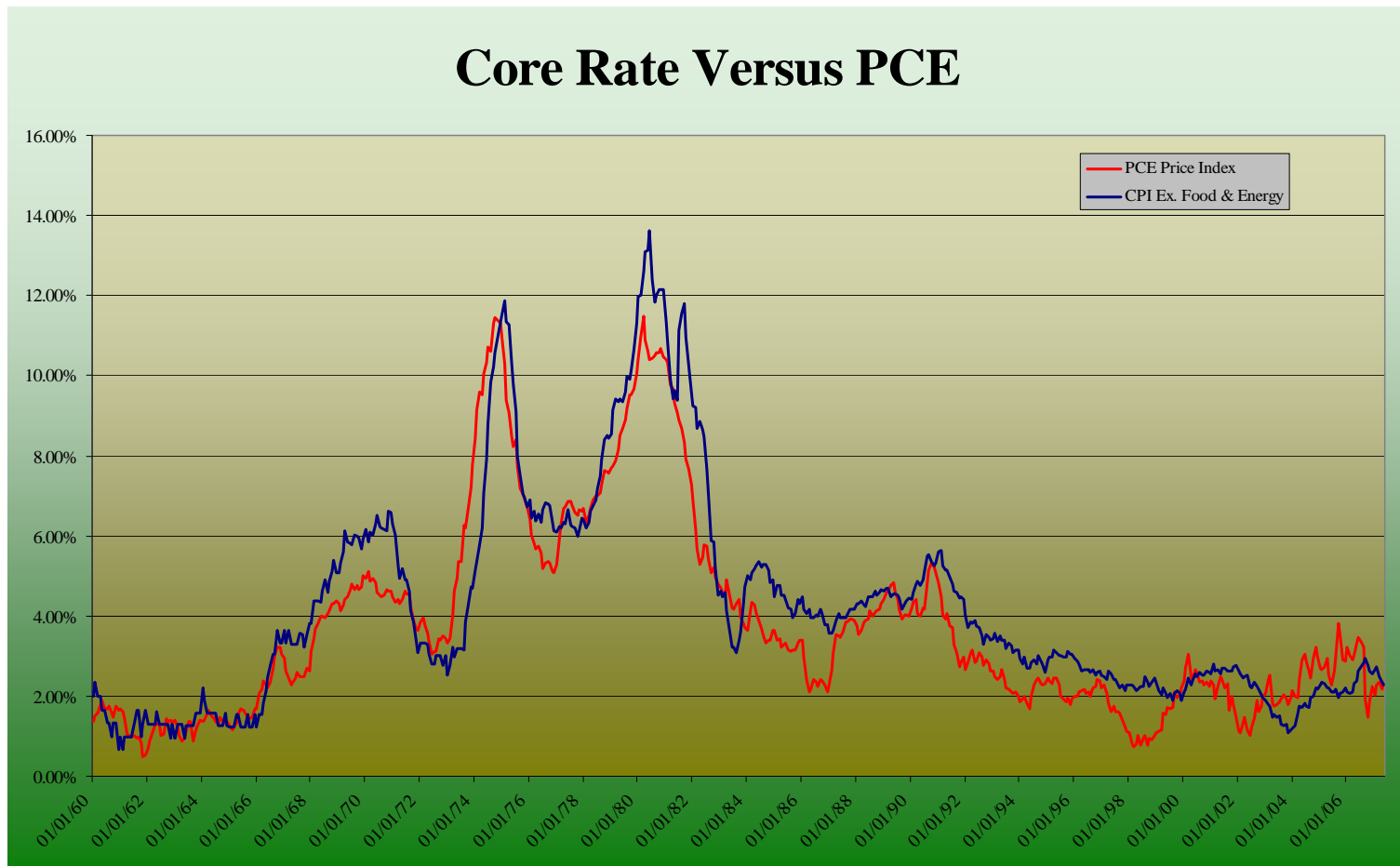
Based on as reported numbers, headline inflation numbers are cooking along at reasonable rates between 2-3%

Inflation expectations



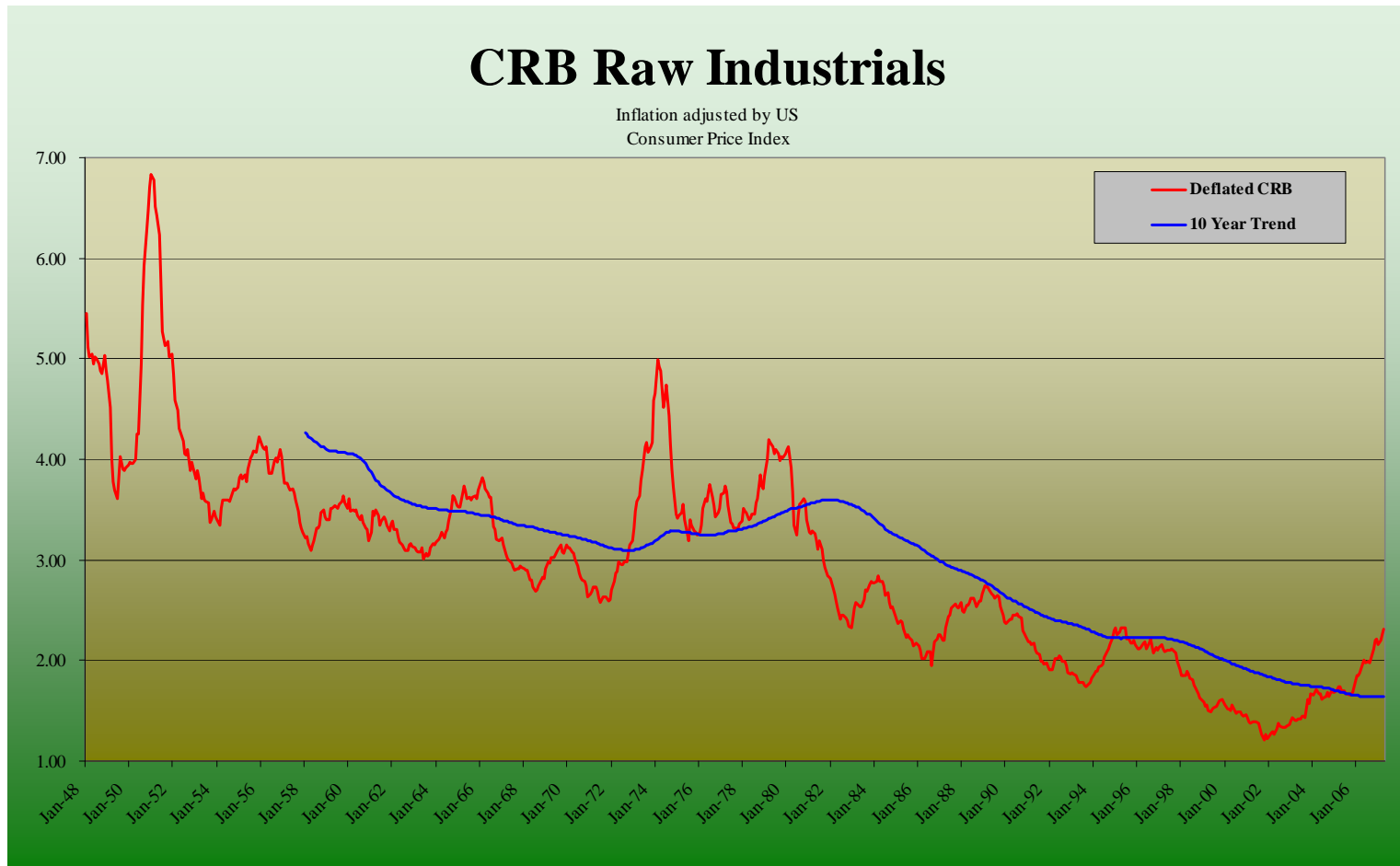
Our proprietary Price Pressure Index indicates that price pressures within the US economy remain at elevated levels.

Inflation expectations



Our TIPS spread model indicates inflation expectations of 2.43%

Inflation expectations



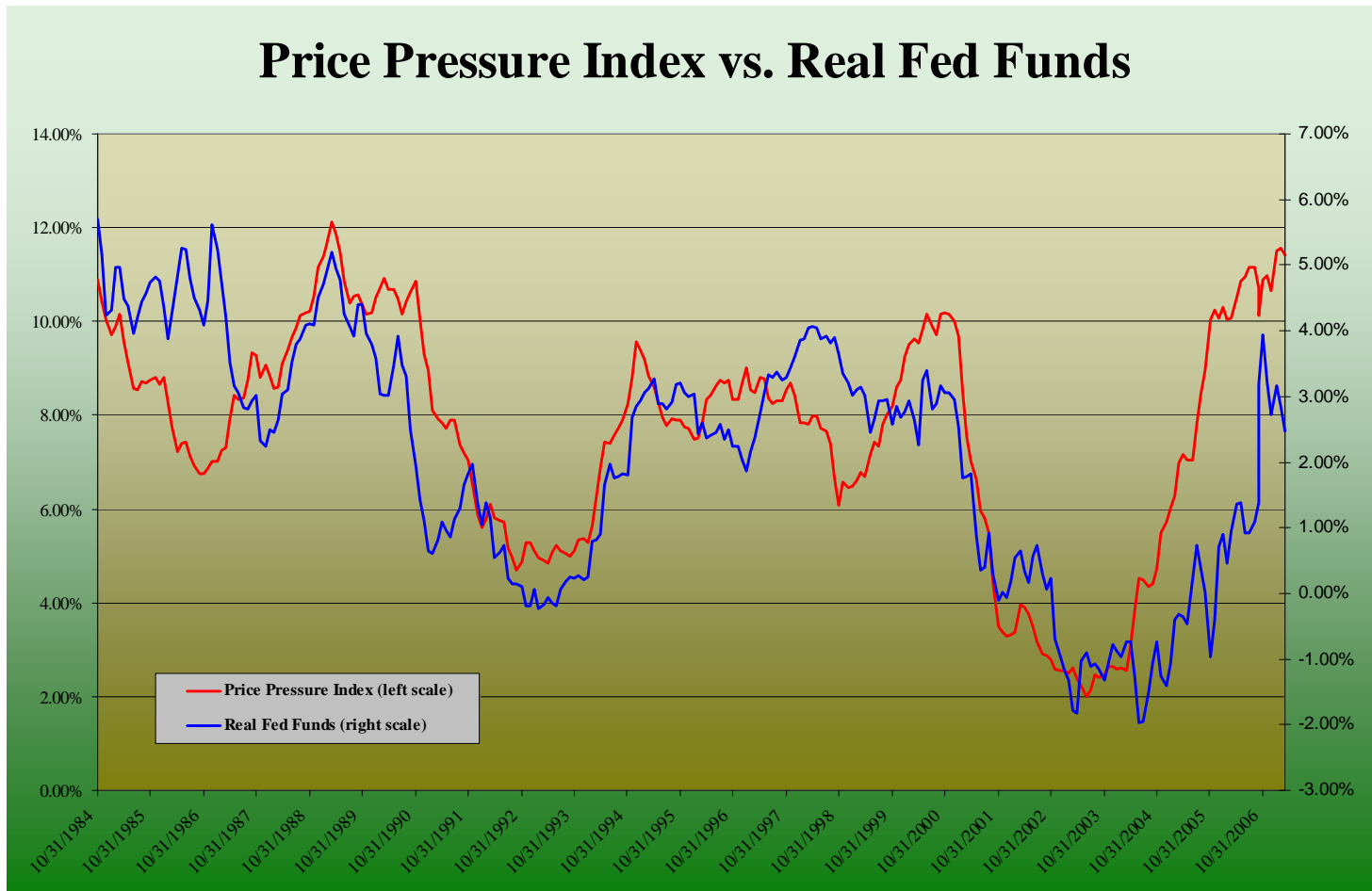
We continue to believe that we are in the early stages of a very long up cycle in commodity prices.

Federal Reserve Watch

Three kinds of people here. People who anticipate a cut in the Fed Funds rate, those who don't, and the small group of people at the Federal Reserve who actually will get to decide.

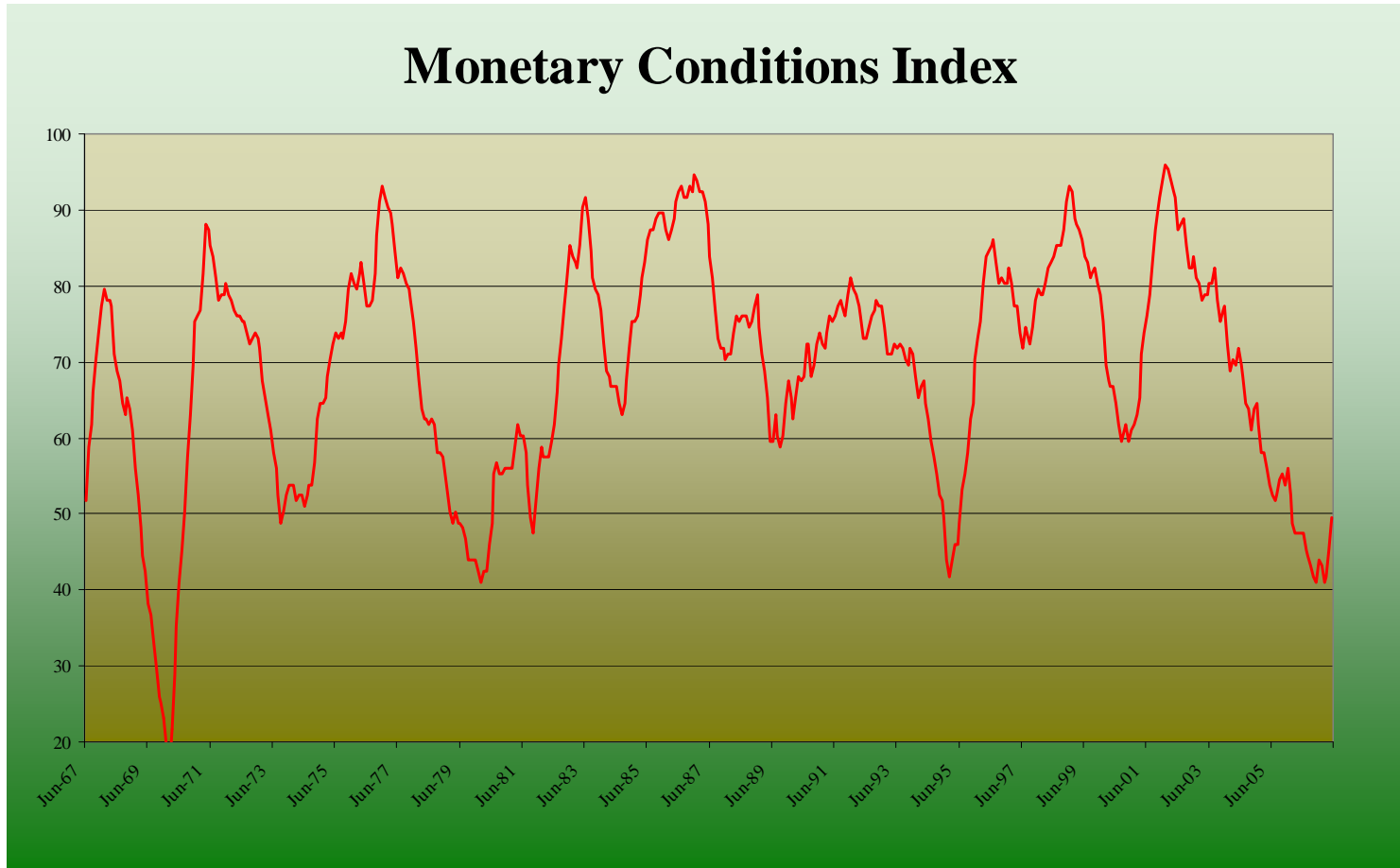
Without a dramatic slowing in the overall economy, not just housing and autos, it is hard to see justification for a rate cut on the horizon until prices slow.

Federal Reserve Watch



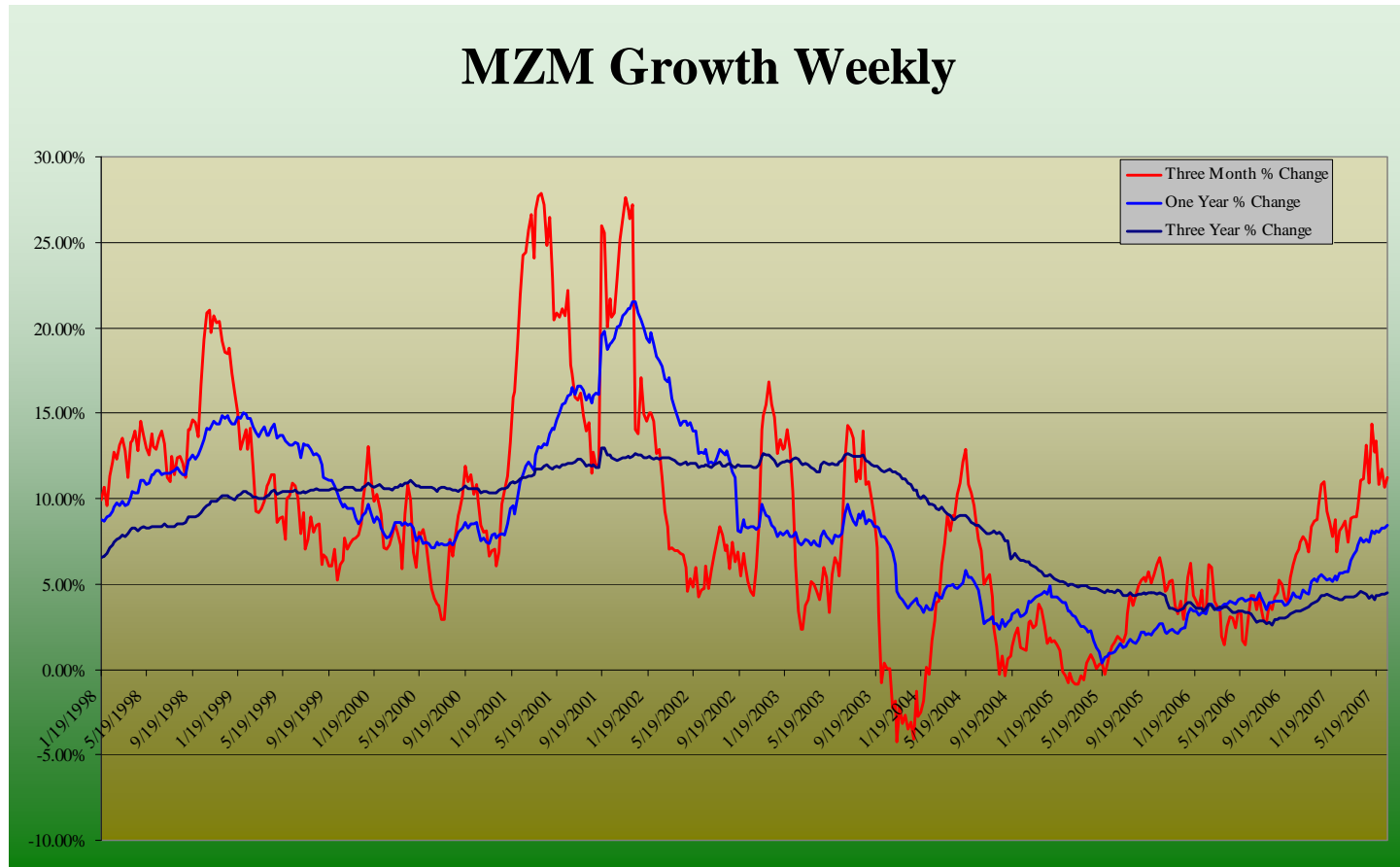
This remains the most interesting chart in the entire chartbook. It will take below trendline economic growth for prices to stabilize (read, a recession), before the Fed starts cutting interest rates again.

Federal Reserve Watch



Has this measure bottomed?

Federal Reserve Watch



Everyone is focused on the Fed Funds rate, but liquidity growth is running strong and is not tight.

Outlook & Forecast

(as of 6/30/07)

Index	Current	Forecast	Range	Time Frame	Comments
S&P 500	1502.97	Trading range	1400 -1500	9 Months	5-10% over-valued
Ten Year Treasury	5.03%	Trading range	4.75 – 5.10%	10-12 Months	An unanticipated shock here could be damaging, and is not outside possibility.
Inflation (all Urban)	2.72%	2.75%	2.35 – 2.95%	10-12 months	We don't think these accurately reflect costs.
Fed Funds	5.25%	No change	5.25%	12 months	Don't look for the Fed to cut rates anytime soon
S&P 500 Earnings	\$84	\$85.15	\$83. 50 - \$92.50	End of 2007	Not forecasting an earnings decline, but earnings growth will slow.

We are not anticipating a tremendous amount of upside in US markets in the coming three years. The trend for the past period has been gently positive with minimal downside risk. Given some of the economic clouds we see on the horizon, that isn't sustainable.

Our client portfolios are positioned accordingly with an emphasis on non-dollar assets and away from asset classes with out-sized three to five year returns.