



**GLASSMAN**  
WEALTH SERVICES, LLC  
FAMILY WEALTH MANAGEMENT

# January 2012 ECONOMIC REPORT

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## ECONOMY: Surprising Start to 2012

Economic data continued to show improvement in January, beginning the year where last year left off. The surprising, and most encouraging data, was released after the month ended, in the form of strong reports on the manufacturing and service sectors, as well as a larger than expected expansion in the labor markets.



### *Federal Reserve Will Hold Rates Near Zero until 2014*

The Fed unexpectedly announced its intentions to hold interest rates near zero until at least late 2014, which far exceeded previously stated expectations of a mid-2013 rate hike. In our report, *The Yield Drought - Retirees' Greatest Challenge*, we predicted that low yields would “exist for longer than most retirees believe, and perhaps longer than they can afford.”

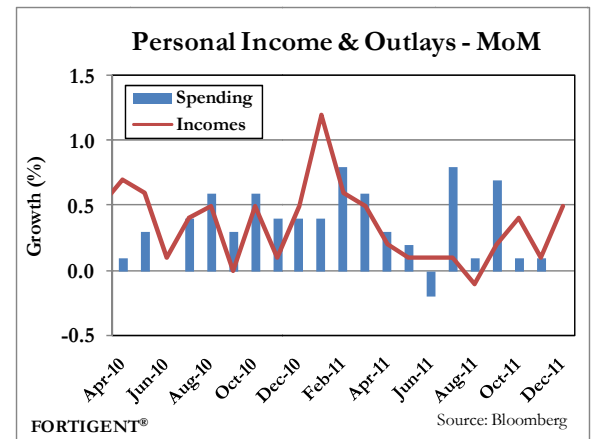
Click [HERE](#) for *4 Ways Retirees Can Beat The Yield Drought*, and to receive your copy of our report.

### *Incomes and Employment Up*

Incomes, which grew 0.5% in December, were above expectations and the biggest gain since March 2011. Spending to this point has largely been financed through savings, making December's income boost a much welcome improvement for consumers.

The outlook for jobs also continues to be positive. The Bureau of Labor Statistics reported nonfarm payrolls increased by 243,000 in January, more than 100,000 above consensus estimates. This, in turn helped the unemployment rate which declined unexpectedly to 8.3%.

While January's seasonal adjusted labor figures may have something to do with the strong employment numbers, it is difficult to deny the momentum occurring in the labor market. We still have work to do as the US job market remains 5.7 million jobs below its pre-recessionary level.



### *Manufacturing and Service Sectors - Positive News Continues*

The Institute for Supply Management (ISM) released two important reports on business conditions in January – its manufacturing and non-manufacturing indices.

While manufacturing continues to expand, new orders, which typically points to future growth, also had a solid gain. Given the larger size of the service sector, the non-manufacturing report is an important barometer for the US economy. It also experienced a gain, surprising economists who had anticipated only a minimal increase.



## Equities

### *US Equities*

Like its global counterpart, riskier segments of the US equities market, such as small and micro cap stocks, performed best. Growth stocks again outperformed value extending a trend that has persisted for most of the past five years.

**Corporate earnings reports - deceiving at first glance?** Two-thirds of the S&P 500 companies reportedly beat fourth quarter estimates; however, the 5.8% increase is much lower once the outsized results of Apple and AIG are stripped out. This brings the number closer to 1.0% growth, which is well below the mid-teens growth seen through the first three quarters of last year.

Many companies have attributed weaker results to a stronger dollar and a weakened Europe. Indeed, after reaching record levels in the fall, US exports have trended down because of Europe's troubled economic state.

**Irrational Exuberance Overtaking Fundamentals?** According to Bespoke Investment Group, 86% of the stocks in the S&P 500 are trading above their 50-day moving average price. Put another way, it is unlikely that 86% of S&P 500 companies have improved their fundamentals, (cash flow, balance sheet, income statements, etc.), to the extent that would justify the current price. It appears that investors are jumping back into stocks, buying the good with the bad.

### *Global Equities: ECB's 3-Year Unlimited Liquidity Sparks a Rally*

Global equity markets rallied to start 2012, with the broad all country world index rising 5.8% in January. It appears that investors' appetite for risk has also recovered with the strongest performance in the higher risk segments of the market.

The move by the European Central Bank to offer unlimited three year liquidity to European banks via the Long-Term Refinancing Operation (LTRO), appears to have provided the backstop for renewed risk taking. Since the ECB revealed that banks tapped its coffers for €189 billion in financing in late December, market reaction has been positive.

Even so, it is too soon to tell if a bull market is emerging. There are signs of life, though in the US economy, and the latest data from China seems to have softened fears of it experiencing a hard landing. However, Europe's problems have certainly not gone away. The prime example is the impending Greek default and its potential withdrawal from the Eurozone. Discussions between Greece and its creditors ahead of upcoming debt payments are reportedly quite contentious, and are already weighing on market sentiment in the early days of February.

### *International Equities*

The broad international index (ACWI ex-US) was led by more economically sensitive sectors in January, including materials, financials, and consumer discretionary. Materials and financials, both double digit performers, are recovering from 2011 in which each lost more than 20%.

**Germany Remains European Economic Engine** - Europe did not rally as sharply as other markets in January, despite being the epicenter of global risk. If not for larger index member Germany (approximately 13% of MSCI Europe), which posted double digit returns, performance would have been much worse. Eight of the ten poorest performing countries were European, including the only two negative returners – Ireland and Portugal.



In the face of bleak expectations for Europe’s economy, there were some encouraging data in January. Manufacturing, with Germany as the driver, returned to expansion territory. Stabilization in Germany’s economy is a welcome sign for Europe, as it is the engine of the region’s growth. Recent data suggests German GDP should rebound to positive territory after a temporary dip in Q4. A declining euro adds to this cause, as a weaker currency will benefit the country’s robust export economy.

**Japan muddled through in January**, and was one of the few market segments that failed to rebound from poor 2011 performance. This occurred despite generally positive economic data during the month. Household spending increased on a year-over-year basis for the first time in ten months, while industrial production advanced 4.0% on a month-over-month basis. Japan is showing signs of recovery from last year’s natural disasters, but in the face of an exceptionally high yen impacting exports and weak domestic demand, corporate Japan is having difficulty on several fronts.

**Fears of a Chinese economic slowdown eased in January** as a flurry of better-than-expected economic data hit the market. Growth outperformed expectations with a larger share of GDP derived through consumption rather than capital investment (an overt goal of Chinese authorities).

**Weakening dollar boosts emerging market returns** - Emerging markets were the biggest beneficiary of a weakening dollar in January, as currency gains added roughly 4% to performance. This was particularly evident in the EMEA and Latin American components of the index, as currency effects nearly doubled the local market returns for US investors. Emerging Asia, which outperformed the other components on a local currency basis, did not enjoy the same benefits and slightly trailed on a US dollar basis.

**Somewhat surprisingly, frontier markets failed to participate in January’s market rally.** After falling by nearly 20% in 2011, the index languished, rising just 0.6%. Renewed turmoil in Egypt and the Middle East may be dampening investor enthusiasm for frontier investments.

## Fixed Income: More Yield, Please!

While performance for core taxable bonds as measured by the BarCap Aggregate index was a healthy 0.9% in January, the big news was the Fed’s announcement that they plan to keep their funding rate near zero until 2014. This forced investors to reevaluate their expectation for future rate movements and add longer duration to their portfolios. A rally ensued, in particular for intermediate notes.

US Treasury Yields

Security	12/31/2011	1/31/2012	Change
90 Day	0.01	0.05	0.04
2 Year	0.24	0.21	-0.02
5 Year	0.83	0.70	-0.13
10 Year	1.88	1.80	-0.08
30 Year	2.89	2.94	0.04

SOURCE: BLOOMBERG

**Mortgage Backed Securities (MBS) performance was restrained** by uncertainty surrounding the Federal Government’s Home Affordable Refinance Program (HARP) forcing investors to reassess their expectations of future homeowner refinancing activity.

**The strongest sector was investment grade corporate debt with a 2.2% return in January.** Stronger economic data along with a sense of calm regarding Europe and investor need for yield likely drove demand.

**The high yield bond market realized \$7.2 billion of new investment in January** based on JPMorgan data. Since the start of Q411, this market has realized six of the eight largest weekly inflows on record, with ETFs gaining the bulk of this inflow. In January (and to some degree in Q4), this demand was not initially met with new supply, driving up valuations. Eventually underwriters and corporate managers took notice. New issuance in the final two weeks of the month was the strongest the market has seen since May 2011; a total of \$25.6 billion came into the market in January, based on Bloomberg data.



**Municipal Market:** Core, intermediate municipal bonds rallied in January due to the “January effect.” To explain: demand is usually hefty in January as investors look to rebalance and invest cash generated by coupon payments and late December/early January maturities. At the same time, there is a lack of new primary supply as Q4 is characteristically a stronger period for new issuance and there is little need for municipalities to tap the market for funding. This was indeed the case in January, as mutual funds experienced demand of \$6 billion. Banks also continued to allocate more resources to the muni market. At the same time, January’s primary municipal issuance was the second lowest of the last 10 Januaries, with just \$14.6 billion of bonds placed in the market. The net effect of this supply/demand dynamic was a strong rally.

AAA Municipal Yields

Security	12/31/2011	1/31/2012	Change
2 Year	0.47	0.44	-0.03
5 Year	1.10	0.98	-0.12
10 Year	2.28	2.15	-0.13
30 Year	4.22	4.02	-0.20

SOURCE: BLOOMBERG

**International Markets:** There was sense of calm in the international fixed income and currency markets as the European Central Bank’s financing efforts provided a burst of liquidity to both banks and sovereign debt markets. This calm and liquidity led to successful new bond offerings from Spain and Italy, as well as Hungary, which is seeking International Monetary Fund (IMF) aid.

## Liquid Real Assets

### REITs:

Mortgage REITs had a strong month after a weak 2011. However, President Obama’s announcement to extend refinancing flexibility to those with underwater mortgages may dampen returns.

To frame the discussion of possible impact, non-government lenders own about half the outstanding US mortgage loans (30 million), and a total of 11 million are underwater. The President expects that 3.5 million of those 11 million loans will refinance under the new plan with a total cost of \$5 to \$10 billion. Accounting for leverage, mortgage REIT exposure to Residential Mortgage Backed Securities is approximately \$300 billion. With this in mind, a \$5 billion to \$10 billion haircut will definitely impact mortgage REITs, but it should not cripple the industry. This could be one of the reasons why mortgage REITs (finished 2011 yielding ~15%) rebounded sharply in January.

### Commodities:

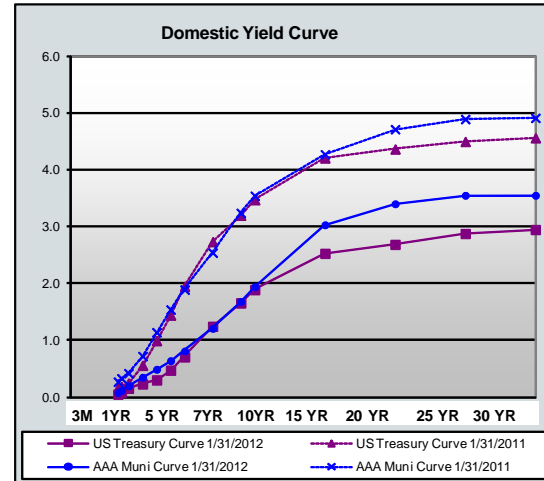
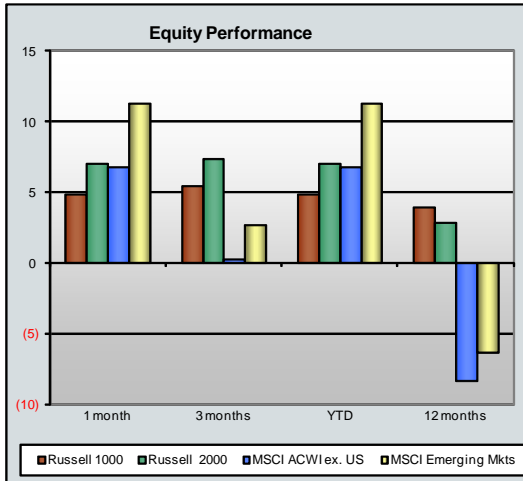
**Precious metals:** Gold rebounded after a tough Q4 due to the Fed hinting at a possible QE3 and a massive liquidity infusion in Europe. Chinese demand continued to rise but was partially offset by decreased demand from India, who recently raised import duties on gold to 2% from a flat rate of 300 rupees per 10 grams. Platinum and palladium shot up with rising auto sales (in the US, the number was the highest since cash-for-clunkers). Silver surged nearly 20% during the month with the help of a diminishing supply surplus.

**Industrial metals:** rallied after a tough 2011, due to renewed hopes of global economic growth. China reported record copper imports in December 2011, and looser monetary policy inside the Great Wall was also viewed as a positive. All of this was compounded by reported decreases in output from some of the world’s largest miners in 2011, despite record prices earlier in the year.

**Agriculture:** Improved rainfall in South America raised crop estimates for soy in Argentina. Wheat and corn were marginally lower, but rebounded in the first few days of February when news of less than stellar crop forecasts in Ukraine refocused attention on the Black Sea region. Coffee fell on expectations for record crops from Brazil (world’s largest coffee producer).



MONTHLY PERFORMANCE FLASH REPORT  
January 31, 2012



	1 month	3 months	YTD	12 months
<b>Large Cap</b>				
S&P 500	4.48	5.32	4.48	4.22
DJIA	3.55	6.43	3.55	9.12
Russell 1000	4.87	5.47	4.87	3.95
Russell 1000 Value	3.78	5.33	3.78	1.88
Russell 1000 Growth	5.97	5.62	5.97	6.07
<b>Small/Mid Cap</b>				
Russell 2000	7.07	7.38	7.07	2.86
Russell 2000 Value	6.65	8.10	6.65	0.73
Russell 2000 Growth	7.48	6.67	7.48	4.94
Russell Microcap	8.52	9.00	8.52	(0.50)
Russell Midcap	6.06	5.40	6.06	2.25
Russell Midcap Value	4.91	5.68	4.91	1.19
Russell Midcap Growth	7.25	5.14	7.25	3.42
<b>All Cap</b>				
Russell 3000	5.05	5.62	5.05	3.86
Russell 3000 Value	4.01	5.54	4.01	1.78
Russell 3000 Growth	6.09	5.70	6.09	5.98
<b>International Markets</b>				
MSCI EAFE	5.35	(0.67)	5.35	(9.16)
MSCI ACWI ex. US	6.81	0.26	6.81	(8.34)
MSCI Europe	4.71	(1.51)	4.71	(9.85)
MSCI Japan	4.52	0.75	4.52	(10.42)
MSCI AC Asia Pacific Ex - Japan	10.26	1.61	10.26	(5.47)
MSCI EAFE SMID	7.08	(0.07)	7.08	(9.79)
MSCI ACWI ex. US SMID	7.94	0.32	7.94	(10.12)
MSCI Emerging Mkts	11.36	2.70	11.36	(6.35)
MSCI EMEA	12.07	3.04	12.07	(6.30)
MSCI Latin America	12.63	4.29	12.63	(4.71)
MSCI Frontier Markets	0.56	(3.50)	0.56	(17.93)
<b>Sectors (S&amp;P 500 GICS)</b>				
Consumer Discretionary	5.91	6.57	5.91	13.15
Consumer Staples	(1.51)	3.91	(1.51)	14.05
Energy	1.50	2.49	1.50	(0.97)
Financials	8.13	4.81	8.13	(12.79)
Healthcare	3.10	7.21	3.10	15.65
Industrials	6.97	9.33	6.97	1.95
Information Technology	7.63	4.91	7.63	5.75
Materials	11.18	8.97	11.18	0.39
Telecom Services	(2.76)	1.90	(2.76)	6.29
Utilities	(3.63)	0.72	(3.63)	14.24

Source: Bloomberg, FactSet

	1 month	3 months	YTD	12 months
<b>Fixed Income</b>				
BarCap US Agg	0.88	1.90	0.88	8.66
BarCap 1-10 Muni	0.88	2.97	0.88	7.88
BarCap HY Muni	3.68	4.71	3.68	14.51
BarCap Inv. Grade Credit	2.21	2.35	2.21	10.32
BarCap Muni Long Bond (22+)	3.79	6.41	3.79	21.10
BarCap US Agg Securitized MBS	0.41	1.30	0.41	6.61
BarCap US TIPs	2.29	3.12	2.29	15.94
BarCap US Treasury Interm	0.51	1.46	0.51	6.80
BarCap US Treasury Long	(0.05)	5.86	(0.05)	32.74
BarCap US High Yield Loans	2.36	2.31	2.36	1.38
ML US High Yield BB/B Rated	2.55	3.10	2.55	6.06
ML US Convert ex-Manandatory	5.40	3.75	5.40	(0.38)
JPM GBI Global ex US Hedged	0.71	2.35	0.71	5.96
JPM GBI Global ex US Unhedged	1.70	0.65	1.70	7.85
JPM GBI-EM Global Div	7.42	2.22	7.42	7.19
JPM ELM+	4.29	(0.36)	4.29	(1.45)
JPM EMB+ Composite	1.47	2.28	1.47	11.47

	Latest Month end (1/31/2012)	3 Months ago (10/31/2011)	Latest Year end (12/31/2011)	12 Months ago (1/31/2011)
U.S. Dollar Index Value	79.29	76.17	80.18	77.74
USD vs. Yen	76.27	78.17	76.91	82.04
Euro vs. USD	1.31	1.39	1.30	1.37

	Latest Month end (1/31/2012)	3 Months ago (10/31/2011)	Latest Year end (12/31/2011)	12 Months ago (1/31/2011)
<b>Currency</b>				
U.S. Dollar Index Value	79.29	76.17	80.18	77.74
USD vs. Yen	76.27	78.17	76.91	82.04
Euro vs. USD	1.31	1.39	1.30	1.37
<b>Commodities</b>				
Gold (\$ per troy ounce)	1737.60	1714.85	1563.70	1332.80
Crude Oil (\$ per barrel)	98.48	93.19	98.83	92.19



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