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ALLIANCE INVESTMENT SOLUTIONS

HELPING YOU BECOME AN INFORMED INVESTOR

Economy Report

Reported by:

Mike Lathigee

CHAIRMAN & CEO
of Alliance Investment Solutions

Dear Member,

Economic indicators are giving off some positive signals for certain areas of the economy, but it is still too soon to claim the US economy is in a solid recovery. This month's newsletter focuses on some of the indicators I am watching and the story they are telling. It is important for you as an investor to understand the mixed signals some of these indicators are giving out, so you can avoid being in the wrong place at the wrong time. Here are some of the topics I cover in this month's newsletter.

How Greece reflects the larger global economy. Events in Greece are revealing just how deeply the economies around world are interconnected. Coordinated assistance from the international community may help Greece get through their crisis, but this situation is making the entire European banking system very nervous and very aware of the potential for disaster that exists should other countries find themselves in similar circumstances.

A strong US dollar causes problems for Canada. As the Canadian dollar strengthens against the US dollar manufacturers and retailers north of the border are finding their buyers heading south. At the same time American consumers have reduced their spending on all goods, including those made in Canada. Between the drop in Canadian exports and Canadians buying American, many Canadian companies are forced to make job cuts, close their doors or both.

US consumer confidence takes a dip and leaves everyone edgy. Few indicators have a stronger impact on the economy than the Consumer Price Index. For the past three months this index has gotten stronger, but February saw it dip. On one hand consumers are burdened with the job of holding the economy together by spending, while on the other hand they are focused on paying off debt rather than incurring more.

Real estate is still problematic. While declines in Commercial Real Estate values have been steep, the anticipated meltdown has not occurred yet. High unemployment numbers and low growth numbers warn that demand for commercial space is headed down. Meanwhile, many foreclosed residential properties are not making it to market and many foreclosures are being delayed. Is this a strategy by banks to keep their roles from swelling while manipulating the market until home values rise?

Where to look for investments in a sideways stock market. With the markets overbought short term, careful investors are looking for strong companies in strong sectors to buy on pull backs. In addition to warnings about bonds, retail stocks and the banking sector, I've included in this newsletter guidance on some energy and technology companies that show promise of stability long term.

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**Disclaimer: Contents of this report do not constitute investment advice.
You are to consult with your investment advisor before making any investment decisions.**

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March 2010 Economy Report

Monday, March 8th, 2010

We are entering the end of first quarter of 2010 and right now the markets are showing upward momentum. But we are not out of woods yet and it is important that as an investor, you understand some of the economic indicators and geopolitical situations that are driving the markets right now and how those factors may change in the near future. Here is a recap of some of the things I am watching carefully.

Recent US unemployment numbers are not predictive:

The unemployment rate is 9.7% in the United States, however, it appears that the markets perceived the latest job numbers as a positive since non-farm payrolls fell less than expected and the markets believe the numbers will be positive in March, too. The number for February showed 36,000 jobs lost while expectations were that 68,000 jobs would be lost. I guess the best way to view these current numbers is to think of this as "better than expected news, which is causing the traders to overreact to the upside.

While this news had a positive impact on the street, we need to remember that although the labor market appears to be improving 8.5 million jobs have been lost since the start of this recession. The official number of unemployed persons in the United States remains at 15 million, but this number does not include discouraged workers. The US Bureau of Labor Statistics defines "discouraged workers" as people who are not currently looking for work, because they believe no jobs are available for them. Also, when interpreting the true importance of these unemployment numbers we must consider their importance in the bigger picture.

In order for the current underemployment rate to simply stay where it is right now, GDP growth must be 3.3%. However, reports show that the International Monetary Fund is only predicting growth of 2.7% for the US economy. This is a significant underlying drag on this "better than expected" news. The most positive part of this month's job report numbers is that the manufacturing sector is showing positive numbers for the first time since the recession began. Manufacturing job creation is the strongest sign of unemployment recovery. Yet again, we need to consider how much of the stimulus spending is responsible for these positive numbers.

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"A great analogy I recently saw compared global economics to the earthquake in Chile causing a tsunami warning in Hawaii."

National economies are interconnected and what happens to one can happen to many:

Since the last economic report in February Greece has been the primary focus of the international financing community. Although a very small player on the international economic scene the Greek crisis can add to the next wave of turmoil for the global economy. Investors around the world are pouring money into government treasuries seeking a safe haven. However, if Greece were to default on its loans this would cause investors worldwide to question all investments in government treasuries. Other weak sisters to Greece are Portugal, Spain and Italy. A collapse in Greece could lead to instability and cause investors to pull money out of government treasuries for these three countries. In the extreme case of global collapse Britain is also in very poor shape with heavy debt. Europe is an area for investors to avoid as the cradle to grave socialism is destroying the economies.

Although the United States is healthier than Britain in relation of GDP to debt, a collapse in Greece could have a domino effect to include all markets. This would lead to higher interest rates around the world as investors demand higher interest rates to lure them to invest in treasury notes for these countries, and possibly for all nations including the USA. Higher rates would lead to higher interest rates on mortgages and make it more expensive for businesses to borrow money. At best, higher rates would stall a worldwide economic recovery and at worse they would promote another severe recession. The current situation in Greece shows clearly how interconnected the global economic community is, but most times people view Greece as a situation that has nothing to do with them. This is simply not true. The world is an irrevocably and deeply interconnected global village and what occurs in one corner of the world ripples out and touches every other country in some way.

A great analogy I recently saw compared global economics to the earthquake in Chile causing a tsunami warning in Hawaii. Following that analogy, it is easy to understand that an economic earthquake in even a small nation like Greece can cause large waves of consequences elsewhere. The subprime mortgage crisis in the US was just a small part of the global financial sector, but no one questions the impact it has had, nor the part it has played in the worldwide recession. The same fear exists with Greece. While small by world economic output standards, its

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"...the events in Greece as a small example of what will happen to the United States"

collapse could cause severe problems for larger more stable countries around the world.
I am a student of history and for those who don't buy my theory, take a look at the 1990s when investors had concerns about Thailand's foreign debt. This led investors to question the finances of several East Asian nations, resulting in the Asian financial crisis of 1997-98. We can expect a similar reaction for Europe if the situation in Greece is not handled properly. We can only hope that Greece's crisis remains contained to Greece, but that will require coordinated assistance from the international community. Already this situation has caused a sell off in the Euro, since Greece is a part of the Euro block. On a comparative basis the US dollar has soured against the Euro.

The most positive sign that Greece will get through this crisis and the world will not be dragged into it is the fact that Greece successfully sold $5 billion Euros of 10 year debt. This is about $6.8 billion US Dollars. This event has calmed worldwide investors somewhat.
Yet a huge concern remains. European nations are linked closely with one another through the banks and any crisis in one can spread quickly to others and the rest of the world. If a crisis spreads from one country to another many banks would be in trouble because many banks made loans to Greece and there would be a general pull back on bank loans in Europe. A pull back on loans in Europe would lead to a dampening of businesses and buying power in that block and less demand for American products as this cycle continues to turn.
Worse for the United States would be if investors seriously question US debt and perceive the events in Greece as a small example of what will happen to the United States. This perception is not unlikely, nor without basis.

The US is running large deficits partly due to the sharp decline in tax revenue because of the recession and partly due to increased spending in attempts to jump start the US economy.
As if this weren't enough to make the global financial community nervous, if bond investors lose faith in the US government's ability to bring its deficit down over time, then interest rates would rise to reflect this additional risk, which in turn would cause the recovery to grind slowly to a halt.
Let me give you a quick reminder about how interest rates work in the US.
The Federal Reserve controls short term interest rates, but longer term interest rates are controlled by market forces. These longer term rates control home mortgages and corporate loans.
If the US continues moving in its current direction then we will see higher Treasury bond rates. Higher Treasury bond rates would

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"A great example of this is the Russian Central Bank, which increased its position in Canadian dollars recently"

make the US deficit more expensive to finance. This would signal politicians that they need to trim the deficit more aggressively, which in turn means cuts to economic stimulus spending, which is the major reason the economy is moving out of recession.

Basically, the US is incurring more future debt by spending to stimulate the economy now, with the expectation that an improved economy will be able to pay down that debt in the future. Greece is unlikely to get assistance of direct financial aid from other European partners. However, it is asking for some form of support that would reduce its high borrowing costs on the international market. Yet speculators are driving up the price at which Greece can borrow money. As Greece attempts to curb their rising debt, Greek politicians announce cutbacks in all social spending and as a result we are seeing violent protests. The whole world is watching how the Greek government and the international financial community address this country's economic distress while keeping political unrest under control.
Another area I am watching has to do with fluctuations in currencies.

Currency Fluctuations Are Impacting Trade:

Earlier I stated that the US dollar is strong versus the Euro however, the US dollar has had a sell off against commodity currencies such as the Canadian dollar, which once again approaches par with the US dollar. The Canadian fiscal budget was well received by the international community and the Canadian parliament took huge strides to reduce the deficit from $56 billion to half that amount in the next few years. The international investment community applauded the fiscal responsibility of Canadian politicians and this led to the huge rally in the Canadian dollar.

This of course is great news for Canadian consumers who travel to the United States as their dollars have more buying power. It looks like Central Banks around the world are showing more interest in the Canadian dollar. A great example of this is the Russian Central Bank, which increased its position in Canadian dollars recently. I believe this trend for investors to move to countries with sound fiscal management will continue as the US dollar over time will loose its world's reserve currency status.
Still, not is all perfect with such a strong Canadian dollar rally. Retailers will be hurt as more Canadians travel across the border for better shopping deals and the manufacturing sector will also be hurt as the cost of exports become more expensive. Over 80% of Canada's exports go to the USA. So whenever the

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"The current environment of low interest rates also bodes well for gold as investors can borrow at low rates and speculate that gold will go higher"

Canadian dollar gets too strong weaknesses result in the Canadian economy as US importers order less from Canadian manufacturers.
The Canadian Manufacturers and Exporters Association estimates that for every one cent rise in value of the dollar, Canada's economy can lose up to $2 billion in exports and 25,000 jobs. These companies must cut the fat to ensure they can compete at par with the US dollar. As the Canadian dollar heads in the direction of becoming on par with the US dollar Canadian manufacturers must learn to compete.
Let's remember too, what happened last time the Canadian dollar soared above the US dollar.

Angry consumers demanded Canadian stores lower their prices to more closely match those in the US especially on books and magazines, which published both prices on the covers.
Also, many Canadian manufacturing firms went out of business as US orders dried up.
Other important investment classes that investors are following are gold, oil and natural gas. So let's take a look at what's going on in those areas.

Gold continues to hold its place as a hedge:

As Central Banks around the world struggle to control their debt and the fears of a possible double dip recession investors are once again poised to invest into gold. Gold hit a six-week high in terms of US dollars and has surged to all time record highs against both the plummeting Euro and Sterling.
Only commodity currencies like New Zealand, Canada, Australia and Brazil are holding pace with gold. The US dollar is moving up compared to the Euro and Sterling, however, gold is moving higher than the US dollar when compared to these currencies.
As governments continue to print money all investors must have a store house of some gold in their portfolio. Traditionalists have always stated an investors portfolio should hold a maximum of 2% to 3% in gold. But for years I have recommended holding as much as 20% in gold due to what looked like stronger worldwide economic fundamentals for that commodity. Over the past five years I have continued to lower that number and currently recommend investors keep about 5% of their portfolio in gold. This is definitely something you must discuss with your financial advisor.

The current environment of low interest rates also bodes well for gold as investors can borrow at low rates and speculate that gold will go higher. However, investors must be careful. When we see signs of extreme uncertainty investors continue to buy US dollars and seem to ignore fundamentals, which is bad for gold.

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"If you don't know how to do due diligence on specific companies consider holding an Exchange Traded Fund..."

Also, as the US dollar climbs those investors who short the US dollar are forced to cover their positions and this causes the US dollar to have short term spikes and generally gold will drop. The best strategy with gold is buy it and forget it and hope it never goes to $5,000 an ounce, because that means the international banking systems and several currencies including the US dollar will have collapsed.

Gold is and will always be a hedge against uncertainty in the markets and a protection against extreme situations that can occur. I will state for the record that I was laughed at when I urged people to hold 20% of their portfolio in gold. At the time gold was $300 an ounce. Still, I wrote extensively in several publications that I believed gold would rise in price. At that time investors thought the stock market's multi-year bull market would continue forever. Yet the Dow Jones has now returned to its level of a decade ago and since my earliest recommendations the price of gold has quadrupled.

Oil prices are fluctuating short term, but fundamentals tell a different story long term:

As a result of last week's February job report, which I talked about earlier, oil prices hit over $81 a barrel. It appears that the better than expected job report has led investors to expect that demand for oil will increase. This push to move oil prices up also coincided with the announcement by China's Premier that that country is on track for 8% growth this year. China is the second biggest consumer of oil after the United States, and such an announcement would imply that demand will rise. I don't agree with this over reaction by traders to drive oil prices up, because short term fundamentals indicate that worldwide oil supplies remain ample and demand for oil worldwide has continued to be weak. I suspect that short term crude oil prices will continue to bounce up and down on mixed signals of the recovery from the Great Recession.

However, longer term fundamentals that support holding oil in your portfolio are solid. This is due to the Peak Oil Theory and depleting oil supplies, subjects I have talked about at length for several years. If you don't know how to do due diligence on specific companies consider holding an Exchange Traded Fund focused on oil. As always, you need to

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"The overnight inter-bank rate will remain in a 0% to .25% range..."

discuss your own portfolio and investment strategies with your financial advisor.
Natural Gas has been a disappointment for investors. Despite severe weather in parts of the United States demand was not as heavy as expected and with warmer weather on its way we are not likely to see a strong natural gas rally until at least late Fall of 2010. Also worldwide gas supply is strong and inventory levels are high.

Obama and the healthcare issue will continue to be a factor in future US debt.

It is interesting that I am finding the investment community not paying as much attention to the Obama Healthcare overhaul as usual. This is for very good reasons. Frankly, investors don't ordinarily care about the deficit and health care chatter as long as stocks are going up. I find when stocks are moving down investors pay much more attention to things that cause them concern. The health bill, which the White House estimates would cost $950 billion over a decade, aims to fulfill President Obama's goals of expanding coverage to millions of people who are currently uninsured, while taking steps to control soaring health care costs. The White House projects that Obama's bill would extend coverage to 31 million people who are currently uninsured.

Obama's main focus is healthcare, but for most Americans the main concern remains the economy, their job situation and the elimination of debt. I will use Bernanke's most recent statements to update what is happening with regards to the interest rates that drive the lives of all Americans.

Bernanke continues to support the markets with low interest rates:

Bernanke told Congress that a weak job market and tame inflation will warrant low interest rates for an extended period. This is good news for all of us. Since this news the markets have continued their strong rally. The overnight inter-bank rate will remain in a 0% to .25% range and Bernanke maintains that this policy will be unlikely to change in the near term.

Distressed real estate continues to be problematic:

The major concern Bernanke expressed is in the Commercial Real Estate sector where defaults are supposed to spike this year. Budget deficits are also a major concern and although a US credit rating downgrade is not likely, he was concerned that unless Congress could provide a plan that shows how the deficit will fall, the bond market worries over

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"Las Vegas... there are thousands of empty homes, but that little inventory is being sent to auction."

a growing US debt could send long term interest rates higher. As I mentioned earlier, the market controls long term interest rates, not the Fed. The truth of the matter is that everyone expects a great collapse in Commercial Real Estate, which will set the market back again. The reasons for the expected collapse of commercial real estate lay in the unemployment numbers. Employment growth is necessary to drive demand for commercial space and with high unemployment, that demand is likely to remain weak for the foreseeable future. However, in a big surprise to many, Commercial Real Estate values have not yet seen the declines that were expected. Although the declines have been steep the predictions were much more dire.

Also, home defaults have not skyrocketed as expected and banks like Bank of America are changing policies to try to keep people in their homes.
Reports also show that a smaller percentage of mortgages were delinquent and the rate of those entering the foreclosure process slowed in the fourth quarter of 2009. These are possible signs that the foreclosure crisis has started to ease. However, I am not convinced as I see and talk to many people who have stopped paying their mortgages in the Las Vegas area and the banks are not foreclosing on them. I know one house where the owner has not made payments for nearly two years. That house has gone to auction six times and all six times the bank cancelled the listing. When I hear about these types of numbers I sometimes wonder if there is something else going on. Could it be that banks are delaying foreclosure in order to keep owners in the properties so the property is better maintained, and then when economic conditions are better they can foreclose and sell the maintained property at a higher price? It's a valid question. If you put yourself in the banker's shoes it does make some sense.

My friend and Realtor Jeff Bettger tells me in Chula Vista California the streets have several vacant homes on every block, but there are multiple bids on every property, which implies that the banks are in no hurry to sell them low. It sounds like the numbers being reported don't reflect what is really going on and investors need to realize that if they just read the numbers they might not make the best investment decision. The situation is very similar here in Vegas where my friend and real estate broker Kevin Kelly works. (www.landkings.com) Kevin's research shows that there are thousands of empty homes, but that little inventory is being sent to auction. I will inform you of the numbers each month, but keep in mind that there seems to be much more happening behind

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"This last consumer confidence number was very disappointing after three straight months of improvement."

the scenes than is being reported and that the official numbers may not be totally accurate. Gentlemen like Jay Brinkmann, chief economist of the Mortgage Bankers Association says, "We are likely seeing the beginning of the end of the unprecedented wave of mortgage delinquencies and foreclosures that started with the subprime defaults 2007."

Like most economists Brinkman is looking at the numbers, but the feeling I get on the street is much different with many foreclosures being deliberately kept off the market. Here are some of the numbers I'm looking at. The delinquency rate on one-to-four unit residential properties dropped from 9.64% to 9.47% quarter over quarter. Delinquencies include mortgages that are at least one payment or more past due, but not yet in foreclosure. Meanwhile 1.2% of outstanding mortgages entered the foreclosure process in the 4th quarter down from 1.42% in the third quarter. These numbers are from a study that covered 44 million loans on one-to-four unit residential properties, which is about 85% of all first lien residential mortgage loans that are outstanding in the country. There does seem to be factual support that fewer problem loans are actually entering delinquency, which I agree is a good sign. February has been a month with a mixed bag of good and bad economic indicators, but the indicator that drives all economies is the Consumer Confidence Index.

Consumer confidence takes a dip after recent gains:

Consumer spending is responsible for the majority of GDP activity for both Canada and the United States. Despite some positive signs this month, the worst sign is that consumer confidence once again has declined sharply in February and consumers are concerned about their debt, their job security and business conditions. The consumer confidence index is the result of a survey of 5,000 US households and measures how consumers feel about current economic conditions. The February report hit a 27 year low, the lowest since February of 1983. This means that consumers feel things are worse now than they were during the financial crisis at its height in 2008.

This last consumer confidence number was very disappointing after three straight months of improvement. Employment is the driving factor of consumer confidence, so if we see improved payroll numbers in March then consumer confidence should get stronger. Consumer confidence is definitely a number we have to closely monitor, because consumer

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" Only stocks that steal business from other retail companies will do well as consumer spending is expected remain stagnant."

spending drives two thirds of the United States economic activity and 50% in Canada. Once again, I will state that one report does not make a trend and I will be watching this indicator closely to see if it is a one month situation or a trend with another horrible month in March. I will keep you posted.

De-leveraging and eliminating debt is the overall theme everywhere:

Right now I am seeing a trend toward de-leveraging with countries, people and companies. It seems the universal consensus is elimination of debt. This will continue for the foreseeable future and the days of buying everything on credit are gone. Consumer spending will continue to be weak as consumers will be less likely to buy everything on credit. I spend much time in Nevada and this state has cut all programs and lay offs are everywhere. Although not popular there seems to be an understanding that it has to happen and this is happening with state after state. In Canada the Parliament cut many programs and consumers seems to be cutting back on all non-essential spending.

Recommendations for a Sideways Market:

Taken together, all these indicators and geopolitical factors combine to paint a picture of a slow, uncertain US recovery and an even more uncertain international financial picture. Yet, careful investors can still find opportunities based on solid fundamentals and growth trends. With this mix of indicators it is important to be careful in the markets. As I've said for several months, I believe we are going to see a traders market moving sideways for 2010. Unlike 2009 when we saw many bad stocks rise in the overall market euphoria, you will only make money in 2010 by selecting strong companies within strong sectors. That said, here are some cautions to help you narrow down your choices:
In the short term I believe the markets are overbought. However, at this moment the trend is up so it is time to start to take profits with stop losses in place to ensure you are forced out of stocks if a correction is sudden on bad news.

This is a time to avoid most consumer stocks in the market. Only stocks that steal business from other retail companies will do well as consumer spending is expected remain stagnant. Any choice in retail should be based on a company that has a huge competitive advantage as consumer spending trends are problematic.

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"The markets will not deliver easy profits as they have in the past and caution is recommended..."

I am still uneasy about bank balance sheets and will continue to avoid the banking sector until I believe banks are writing down their loans to market value instead of the value of the mortgage.
The story is different with Canadian banks that had great earnings reports.Keep in mind Canadian banks were much more conservative than US banks and never had stated income, stated documents and liar loans. Nor did they have adjustable rate mortgage loans or negative amortization and interest only loans. AIG Insurance, which took so many tax payer dollars, was back announcing it needed more money to the disgust of taxpayers. However, tax payers are now relieved that this disastrous company, which has been such a drain on the economy, sold its Asia division for more than expected. In addition, the stock soared as short sellers of the stock were forced to cover.

Some companies to discuss with your financial advisor in the energy sector are Suncor, which is oversold on its buyout of PetroCanada. Others that deserve consideration on pullbacks include Devon Energy and Encana.
Bonds are a good investment class, because interest rates are not running up. High yielding corporate bonds have done better than the overall market and might be a place to hold some funds. However, due to massive debt and low rates, it is wise to avoid government bonds, especially US treasuries. The technology sector seems poised to do well and the earnings in this sector outperformed expectations. Qualcomm, Dell and Microsoft led the way with better than expected earnings. As always, discuss these and any other investment ideas carefully with your financial advisor. The markets will not deliver easy profits as they have in the past and caution is recommended when selecting investments for both short and long term strategies. Looking forward to the Spring, we have some great opportunities coming up.

InvestFest 2010

I hope all of you will join me for Investfest 2010 in Las Vegas. Please go to www.investfest2010.com for the latest update. Every attendee is receiving hundreds of dollars in gifts including best-selling financial books, hugely successful DVD series on building your business, a low cost LLC for every attendee … and the list goes on.

Las Vegas Field Trip

Finally don't forget our next Las Vegas fieldtrip is June 7th starting the morning after InvestFest.

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"Our goal is to provide fantastic cash flow opportunites for our members and hope you will join us..."

At this time we have purchased 34 condos with several members. The one-bedroom units were purchased in the $35,000 range, the two-bedrooms in the $45,000 range and the three-bedrooms in the $55,000 range. The units all have very strong positive cash flow with monthly rents between $650 and $950. All these units previously sold above $150,000 just a few years ago.

All sales at this time are cash only, however once a pending litigation is settled with the condo conversion company then homeowners can get financing, which will create much more demand for this product. Our goal is to provide fantastic cash flow opportunites for our members and hope you will join us for the June 7th tour we've scheduled immediately aft the InvestFest is over. You can get your Field Trip ticket of only $197 by going to www.allianceinvestor.com/vegas.

That's all for this March Economic Outlook. As we watch the financial indicators and geopolitical events unfold it becomes more and more clear how connected we all are in this shrinking global community and how even small events in one country can impact every nation. We are living in very interesting times. Never before has it been more critical to have accurate and current information to base your financial decisions on.

As always, discuss your investment plans with your financial advisor and I look forward to seeing you at InvesFest 2010 and our Las Vegas field trip.

Michael Lathigee
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