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Market Outlook:

Excess

As energy prices continue to fall, many analysts are predicting dire straits for the entire energy complex going forward, particularly the fossil fuels and other ground-based sources. However, there is another school of thought that thinks the impact of falling energy prices might just be the panacea for cash-strapped consumers that years of stimulus have failed to provide. While I see no windfall effect from an annual $310 per family "tax break" that falling gasoline prices might provide, the net savings in the short-run seems to be creating a temporary boon to their pocketbooks. Economists are anxiously waiting to see if/how that money gets put to use. Bear in mind, though, that the savings "at the pump" are being offset by severe portfolio declines for those who own an evenly diversified portfolio that includes energy equities.

Despite a steady drumbeat of new highs in the market averages, it doesn't seem to be enough to quell investor apprehension about the overall strength and sustainability of the current recovery.

Witness the lackluster start to the holiday buying season. The numbers are incomplete, obviously at this juncture, but point to a lack of enthusiasm in traditional brick and mortar store sales as well as in internet purchasing. If you're looking for portfolio conclusions to draw from these data, and you are the kind of investor who dreads news-driven intraday volatility, avoid the retailers, cyclicals, and energy stocks. I would favor biotech and healthcare, traditional non-cyclicals, and global industrials at this point in the sales cycle.

More significant than foot traffic at the mall and energy stock price declines, however, is the potential for a global slowdown in industrial production and capital spending. European Central Banks are giving conflicting guidance about sustaining, or cutting, their monetary policies relating to interest rate accommodation and financial consolidation. We know that interest rates are low because of years of austerity packages, but within those same governments, politicians seem more intent on spending and investment *cuts* than on stimulus. The recent US mid-term elections were a mirror of governmental inefficiencies worldwide which confirm a political landscape of antagonism and gridlock rather than cooperation and problem-solving about infrastructure, business spending, full employment, and citizen participation. Right now, no politician wants to be perceived as a big spender. Thus, the global economic recovery has to carry on "on the cheap". Clearly, without consumer buy-in and corporate spending the recovery is stuck in neutral. Nevertheless, "safe money" is betting on a haven in the US.

This new era trend towards a more "efficient" business model foretells a social paradigm in which there will probably be a permanent underclass of non-participants. Even though smaller, more nimble business yields greater profitability, that same model prohibits an equivalent engine of consumer demand. It might indeed be easier today for corporations to meet profit projections of Wall Street analysts, but we are also witnessing an inadvertent side effect: public inertia and mistrust. This will perpetuate a *decline* in prices, not an increase, and further exacerbate the disinflationary effect that lower oil prices are having on the economy.

While it might make sense based upon the data that energy prices should decline, a paradigm in which consumers sit out or are excluded from the recovery is likely to do more harm than good in the long run.

Problem?

With one sector (energy) under such particularly stifling pressure, the broader market performance is left to struggle for gains minus a significant component. A capitulation in the energy sector does not specifically represent a death knell for all stocks, but its significance cannot be discounted. As stated above, broad repercussions about consumer confidence, discretionary spending, corporate profitability, and federal capital expenditures are all tied to the production, distribution, and consumption of energy products.

We shouldn't become accustomed to the temporary efficiencies of lower energy prices. It is a bait and switch game we ultimately cannot afford. We have seen how business is reinventing itself by doing more with less, spending less in the process. Weakness in the energy sector, and pressure on prices to stay low, might help in the current recovery cycle, but it places the bar too low for sustainability down the line. I perceive a potential vulnerability in the financial markets as a result of becoming "hooked on" cheap goods and services. There is nothing inherently wrong with an "affordable" economy, but I would prefer a scenario in which the glut in oil is eradicated, and higher prices ensue. Hard to do, since oil reserves are hitting 30 year highs. But the laws of supply and demand have not been rewritten, simply modified to fit our economic condition. Oil is cheap, that's a fact. But depleting resources hardly ever stay inexpensive unless manipulated to do so. This is not a negative sentiment about stocks and bonds, but a baseline assessment about the sustainability of artificially created gluts or shortages.

We should look at this price displacement as a transient condition, and an opportunity for cogent discussion about alternative energy, and other product sources, for future consumers.