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**Market Outlook:**

**Casino Royale**

There's that climactic moment in every card game when you have to turn over the last card, resulting either in a win or a loss. Last week, that momentous card was played by China, and it definitely was not a win for the global financial markets.

In a surprise move, the People's Bank of China (their equivalent to the Federal Reserve) depreciated their currency, the Renminbi, twice, by nearly 4 percent total. The reasons given were self-serving: the world's second largest economy took measures to devalue (decrease) the cost of their goods and services so that their exports might be more affordable for the rest of the globe, thereby assuring , at least by their thinking, a revitalization for their stagnating economy.

As a result, however, the world financial markets dropped precipitously, concerned that these monetary measures might create headwinds to the global recovery.

Whereas China implies that this move might be simply a *one-off occasion*, the market's interpretation of their intent only added to nervousness about the strength of future earnings and stock valuations across a spectrum of sectors.

Indeed, if the US dollar strengthens as a result of China's currency devaluation, America's own exports become higher-priced and less competitive. It is my belief that once we get past the initial knee-jerk reactions and finger-pointing jingoism, fundamentals which underpin our markets will become clearer and stronger.

China made this move now because of their desire to be a consistent "player" in the global arena. Usually, currency exchange rates happen in fractions, not full percentage points. The very magnitude and timing of this transaction shows how much the Chinese want to be taken seriously as a preeminent member of financial intercourse. Because they perceive a downshifting in organic economic momentum, their bold move was meant not only as a monetary statement but a geopolitical one, as well. And yet, the dollar/yuan equivalency rate now approximates the same value as last year. Clearly, this decision was made to make a declaration, and based upon the negative reaction of the markets, it was unwelcome and perhaps burdensome. Nevertheless, the card has been played and the winners and losers are being sorted out.

**Did it work?**

An unintended consequence of the Chinese decision, however, might be to hyper stimulate their economy at a time when a necessary pause might have been more in order. The last thing they want to do is to reignite a round of inflation, or worse, business failures, when they least can afford to have them. By ceding power to the "demand economies" of other nations, they also cede authority over their ability to maintain order and control over their financial destiny.

Meanwhile, here at home, it is possible that the markets might have overreacted to the news. For quite some time I have been writing about the anxiety investors have been feeling even as portfolio valuations continue to expand. Trading around "resistance levels" has made the market susceptible to exogenous noise, and selling sprees which remind everyone of an *"I told you so"* mentality. I contend that once the dust settles from the Chinese devaluation and the market's response, investors will get back to the business of fundamental evaluation of the sustainability of our recovery.

That task implies a serious assessment of sector strength and balance in the wake of a seismic bull run which began in the wake of yet another consumer calamity, namely the debt market crisis. Things are very different at the end of a bull phase than they are at the beginning, and our portfolio weightings need to reflect those differences.

Perhaps the "exogenous noise" to which we alluded did us a favor? It simply is not possible for markets to go up perpetually...and linearly...without pause or consolidation.