January 2007

FORECAST

Are We On the Edge?

Comments from the Certified Financial Analyst Society 2007 forecast dinner Jan. 19, 2007.

COMMENTS FROM THE EXPERTS

Russell Read, Chief Investment Officer, CALPERS

Henry "Chip" Dickson, Former Chief US Investment Strategist, Lehman Brothers

Jason DeSena Trennert, Managing Partner & Chief Investment Strategist, Strategas Research Partners

Russell Read, CALPERS:

CALPERS is the nation's largest institutional investor. Russell Read is responsible for the strategic plan for CALPERS' Investment Office including tactical asset allocation, risk management, business development, budget authority, new investment programs, trading technology, staffing and back office operations. Mr. Russell holds a Doctorate in Political Economy from Stanford University. He has previously worked for Deutsche Bank where he was responsible for $250B investment portfolio.

Comments from Mr. Read:

- US domestic stock markets will have a troubled year.
- Value stocks will do better than Growth stocks.
- CALPERS is focusing on investments in areas which require large amounts of capital: Natural Resources. Latin America shows continued signs of political risk. Asia needs huge investments in infrastructure in electrical generating and distribution facilities. Pollution abatement in China and India seen as lucrative.

Chip Dickson, ex: Lehman Bros.:

Chip was ranked in the top 10 of institutional investors in 2004 & 2005 in All-American polls. Prior to Lehman Bros. Chip was Sr. Bank Analyst with Saloman Smith Barney.

Comments from Chip:

- 15% growth in broad market
- large cap investors are cautious
- S&P 500 dominated with Financial stocks (>25) which should continue to do extremely well in 2007.
- Bonds will have a bear market
- S&P P/E are below historic mean giving room for continued appreciation in the market.
- Global GDP to grow from $45 Trillion in 2005 to $65 Trillion by 2010.
- Inflation dropping from 3.5% in 2005 to 2.5% 2006 and not a factor in stock prices.

Jason Trennert, Strategas Research Partners:

Jason is the Chief Investment Strategist at S.R.P.. The firm provides timely and insightful investment strategy and macro-economic research to the institutional investment community. Jason has spent many years doing economic forecasting for several firms and has a global reputation. He is a regular on Wall Street Week with Louis Rukeyser and the author of the book New Markets, New Strategies, 2005 McGraw Hill.

Of the speakers Jason was the most analytical in his presentation. He was clearly bullish on the market. Opening with the comment that "massive amounts of money in available for investment." Jason was clearly a contrarian. He pointed out trends in the market that he felt were not supported by the data, see below. He expects monetary policy to aide the market since inflation is under control and "Bernardi's FED will focus on quantitative methods" as opposed to Greenspan's FED which he likened to a "cult".

Comments from Jason Trennert:

- The forward P/E ratio on the S&P 500 has contracted by more than 46% over the past five years. This "takes the train wreck scenario out of the market for 2007.
- Retail investors are going into foreign equity funds.
- Consensus is that US Equities will be dogs.
- S&P undervalued, there is a good chance margins will continue on the upside. Financial stocks and stocks for the "Intellectual Property" economy will do well in the broad market. 40% of S&P profits now come from overseas business.
- Mergers and Acquisitions will continue to put positive pressure on the markets.
- Energy stocks should do well.

Summary

It is always frustrating sorting through conflicting investment advice. Two of the experts maintained that corporate returns would continue to be excellent and the current valuations of the S&P were modest leaving room for further appreciation. Energy stocks which are trading at Value stock P/E ratios are expected to show good upsides in 2007. Financial stocks, over 25% of the S&P will continue to drive the sector. Technology was only mentioned by not being mentioned. Mr. Read spent 5 minutes describing how yesterday's growth stocks became value stocks. Reading between the lines led me to believe that he was putting technology stocks into this broad basket.

REITs were not specifically addressed but the slowdown in the housing sector and subsequent reduction in prices has hurt some REITs. Commercial real estate stayed strong until 4Q2006 with a slight downturn.

Balopole Investment Management Corporation (BIMC) actions in 2006 paralleled the recommendations of Randy Russell of CALPERS for positioning in 2007. At BIMC we carefully follow economic developments. However, the disagreement among experts highlights the fact that the future remains unknowable. For this reason, BIMC continues to focus on individual company factors and fundamentals MORE THAN macro-economic forecasts and individual company projections. Quality investments are an investor's best defense against uncertainty.