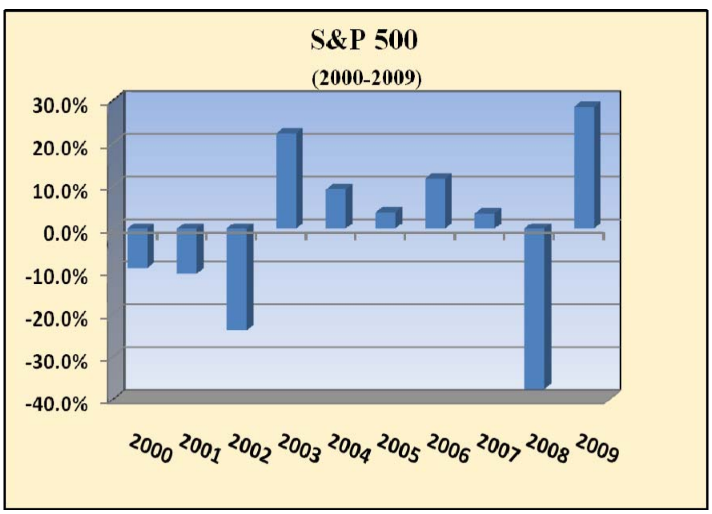
December: A Period Nicely Put

Market Summary December 2009

December put a period to the best year for stocks in the past ten. The final close of 1115.1 in the S&P 500 Index represented a very robust gain of 26.5%, surpassing even the 22.3% logged in 2003, which also was a year in which stocks surged back from a severe beating (see chart).

Taking another perspective, however, it can be said that the 2009 market did not surpass, but merely restored the rally of 2003. The S&P 500 stood only 3.18 points higher at the end of 2009 than it had on December 31, 2003 – a net advance just short of 0.3%. Over the entire ten years since the end of 1999, the index has lost just over 340 points, or 23.4%.

If encouragement is to be found in these numbers, it might be that the market, having twice ended a year in the vicinity of 1115, could be serious about holding it. By that interpretation, a base could be in place for at least a modest advance in 2010. In any case, the market seems not to be nearly so exposed as in October 2007, when it dangled perilously from its all-time peak of 1565.16.



Economy Growing

Economists polled by the Wall Street Journal are predicting robust profits for the fourth quarter of 2009, with productivity gains continuing in the 7-8% level (annualized). These numbers have inspired some prognosticators to call for growth of 5.4% in 4th quarter GDP, despite the recent downward revision of 3rd quarter growth to 2.2%.

The Institute for Supply Management (ISM), in its December survey of manufacturing activity, reported a fifth straight month of growth. The ISM's overall index stood at 55.9%, its highest level of the year (> 50% represents expansion). The ISM claims that this level of activity portends GDP growth of 4.6%.

Still more vigorous is the growth the ISM survey reported in new orders (65.6%), which was an increase of 5.2 percentage points over November, and easily the strongest growth reported for any month in 2009. Meanwhile, customers' inventories continue to fall, and at a faster pace, suggesting new orders should continue to grow. Only 7% of manufacturers' customers had excess inventories, whereas 37% had inventories considered insufficient, the ISM said.

Growth in manufacturing employment continued in December, and at a slightly faster pace than in November, 52.0% vs. 50.8%, the ISM reported.

Activity in the nonmanufacturing sector eked ahead in December, registering 50.1% in the ISM survey. It was the third expansion reported in the last four months, November having registered a contractionary 48.7%. Non-manufacturing production rose 4.4 percentage points in December, to 53.7%, the Institute said. Employment rose remained contractionary, 44.0%. but rose 2.4 points.

Jobs Losses Continue

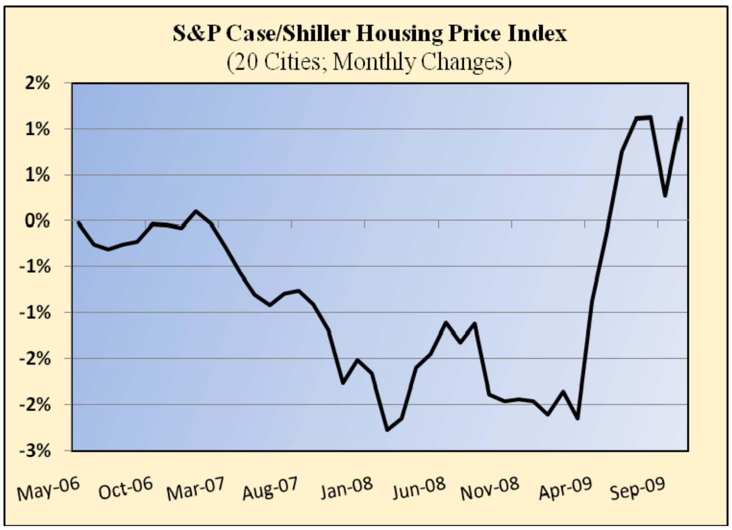
The Department of Labor's December employment report was a disappointment, showing a loss of 85,000 jobs during the month. The unemployment rate remained at 10.0%. Economists found solace in a 2.5% gain in temporary workers, considered an advance indicator of an increase in permanent hiring. Agencies are reporting that more and more temps are being hired with a view toward permanent employment, according to the Wall Street Journal. Surging productivity measures, noted above, when reduced to simple terms, mean employers have been finding ways to increase production without commensurate increases in payroll. This tactic has diminishing returns, however, and some observers say the breaking point is near.

Housing Prices Still Improving

The S&P Case/Shiller Housing Price Index reported in December that October data showed a fifth consecutive uptick (the data lag three months; see chart). Housing prices, like stock prices, now have regained the level they held in the fall of 2003. Year-over-year comparisons are still down (-7% for the 20-city index), but clearly improving.

Consumer Confidence

Consumers are a bit more optimistic about the future, but somewhat more glum about current conditions, according to the Conference Board. The Confidence Index rose nicely in December, to 52.9 from 50.6 in November (1985=100), and the measure for long-term attitudes rose 5.3 points, to 75.6. However, assessments of the present situation, already low, declined another 2.4 points to 18.8.



Equities Strong

Equity indices across the globe were positive for the month, the quarter and the year. The S&P 500 returned a very handsome 26.5% for the year, and 1.9% for December. The Dow Jones Industrial Average moved up 22.7% for the year and 1.0% in December. The Russell 1000 gained 28.4% for the year, and 2.43% for the month. The Russell 1000 Growth Index far out-performed Value for the year, (37.2% to 19.7%) and for the month (3.1% to 1.8%).

The S&P MidCap 400 Index gained a blazing 37.4% for the year – first among domestic equity benchmarks – and 6.3% in December. In smallcap stocks, the Russell 2000 Index gained 27.2% for the year and 8.0% for the month. Its Growth component rolled up gains of 34.5% for the year and 8.6% for the month. The Russell 2000 Value benchmark rose 20.6% for the year and 7.6% for December.

The highest gain for all indices last year was posted by the MSCI Emerging Markets, which gained 78.5% for the year; 4.0% for December. The larger-cap MSCI EAFE Index gained 31.8% for the year; 1.4% in December.

Publicly traded real estate came back strongly in 2009, as the Dow-Jones Wilshire REIT index gained 28.5% for the year, and 7.0% in December.

The Dow-Jones UBS Commodity Index gained 18.9% for the year and 2.0% for December. The Alerian MLP Index gained a whopping 76.4% for the year and 6.6% for December. S&P Natural Resources rose 37.5% for the year and 1.6% for December.

Bonds Mixed

The long Treasury bond took a pounding in 2009, dropping 12.9% for the year and 5.1% in December on the Barclays Capital Index. Shorter-term Treasuries suffered far less, the Barclays 1-3 Year Index finishing the year with a gain of 1.4% after dropping 0.7% in December.

In stark contrast, some higher-risk categories rolled up downright gaudy returns. The BofA Merrill Lynch US High Yield Index, for example, gained 57.5% for the year (3.1% for December). The JPM Emerging Markets Bond Index gained 26.0% for the year (0.3% in December).

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