

Market News

April 2009

Some the best-known economic and financial-market experts gathered at the University of Dayton in Dayton, Ohio, for the RISE (Redefining Investment Strategy Education) Forum in late March. They told graduate and undergraduate students from more than 200 colleges and universities worldwide that the financial crisis is far from resolved, but that the money-management profession will endure and become stronger. Panelists also responded to questions on many current topics.

Excerpts follow:

RISE Forum Highlights

Economic Outlook: Panelists debated the timing of the recovery and the likelihood of hyperinflation post-recovery, more than the cause of the decline. UBS global economist Andres Höfert looks for a slow recovery beginning in early 2010, with inflation rising to the 5-10% range afterward. Wachovia Securities economist Gary Thayer said that while high inflation and strong economic growth are typical following severe recessions, they're less likely this time than a slow recovery, with moderate inflation. Lawrence Yun, economist with the National Association of Realtors, agreed that "for the economy to recover, housing prices first need to stabilize." He said there's some evidence of stability, but home buying is unlikely to resume soon because so many other components of personal wealth have been affected.

Markets Outlook: Citigroup strategist Ed Kerschner said banks are also a harbinger of economic recovery, noting that "until the banking system is healthy, I don't see major gains in the market." Strategists Patrick Dorsey of Morningstar and Steven DeSanctis of Merrill Lynch, however, described the current market environment as a gold mine for traders. "I have no idea where the bottom is," Dorsey said, "But I see a lot of wonderful businesses trading at great prices." None of the panelists offered much support for further curbs on short-sellers, or for lifting mark-to-market valuation rules. Jeff Kleintop of LPL Financial Services said that neither mark-to-market nor the short-selling curbs last fall ultimately had much effect on market prices, although it may have extended the markets' slide. "Mark-to-market hit the banks at the wrong time, and changes are needed in how we apply it to regulatory capital." But he agreed with Dorsey, who said that "I don't see how making banks more opaque solves problems."

Governance Outlook: Panelists expect executive pay to become even more shareholder-aligned than ever, with less cash and more deferred equity. Roger Ferguson, president & CEO of TIAA-CREF, said he expects vesting periods to more closely mirror business cycles, so that the full effect of executive decisions are realized before rewards are available. John Surma, CEO of U.S. Steel Corp., said that compensation decisions are among the hardest he has to make, and will likely only get harder under new federal rules he expects soon. Ferguson said that the greatest risk to good governance in the future may be the increasing difficulty of attracting younger investors into equity markets. "It's going to be harder to get them into savings platforms with equity components," he said. "They will think that there's no way to win after this."

Stock buybacks take deep dive

As companies are forced to conserve cash, Standard and Poor's reports companies covered by its S&P 500 index reduced their stock buybacks sharply in 2008, down 42.4 percent, to \$339.6 billion, compared with \$589.1 billion in 2007. In the fourth quarter, stock buybacks were off 66 percent, slipping to \$48.1 billion in 2008 from \$141.7 billion in the fourth quarter of 2007.

Uptick rule is on the SEC docket

SEC chair Mary Schapiro announced in wide-ranging testimony before the Senate Banking Committee that she plans to discuss the reinstatement of the uptick rule at an April 8 SEC meeting. The rule was meant to prevent short sellers from adding to the downward momentum when the price of a stock is already experiencing sharp declines. It was removed in July 2007, and critics claimed it contributed to the jump in market volatility and short selling that summer. The SEC will face a problem if it does decide to reinstate the rule: each exchange has its own version. They are proposing to go further by making short sellers sell above the highest available bid, preventing them from starting downward price pressure by hitting the bid.

Converting from GAAP to IFRS will be costly

Accenture consultants surveyed 208 U.S. CFOs at companies with revenues of \$1 billion and up on what they thought would be the cost and time needed to convert to International Financial Reporting Standard (IFRS) from GAAP as the SEC has proposed. In the survey CFOs estimate they will spend between 0.1 to 0.7 percent of revenues to convert, with smaller companies spending disproportionately more. The CFOs predict it will take two to three years to make the conversion, with half of the work requiring external assistance. Fortunately, SEC chair Mary Schapiro said she wants to slow down the conversion timeline.

IRS reverses position regarding certain intangible assets

The Internal Revenue Service reversed a long-held position on the tax-free exchange of some intangible assets. In a letter issued by the agency's chief counsel in mid-March, the IRS stated that intangible assets such as trademarks, trade names, publication mastheads and customer lists can be separated from a company's goodwill assets, and be listed at their own value. Those assets then may qualify as "like-kind" property under the tax code, and swapped tax-free if certain criteria are met.

FASB proposes new guidance on market-to-market accounting

Following up on last month's article, "*FASB promises fair value guidance in 2009*," on March 17, the FASB issued two proposed guidelines for fair-market valuation on hard-to-value assets. The first guideline provides asset holders a method to determine whether a historically active financial asset has become an inactive or distressed asset. The second proposal provides guidance on how to account for securities losses on other-than-temporary impairments. Issuers must record losses on such assets, which holders either can't or won't hold to maturity, based on fair value. The FASB has been pressured for new regulations by Congress and banks, which have claimed that current rules have helped spawn the current meltdown, pushing the FASB to act with unprecedented speed to pass the two proposals within a target date of April 2. If both proposals are approved, they would be effective for interim and annual periods ending after March 15, 2009.



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