March 2012

IdahoTrust

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Market Insights

A periodic newsletter from Idaho Trust

2012 started off on the right foot, but has the economy truly turned the corner? Incoming economic data continues to be good, not spectacular, but good. Stock investors have been rewarded with a market rally since the fourth quarter of last year. Later this year the Presidential election will occur and the economy is expected to be a key component of discussions, as usual.

The New Year

Since the fourth quarter (Q4) of 2011 the economy has continued to churn out positive economic indicators and market volatility is markedly down from its 2011 highs. The S&P 500 is up 21.86% since 9/30/2011 with international stock markets gaining as well. The Dow Jones Industrial Average recently touched the 13,000 mark which it has not reached since 2008.

When investors are risk adverse typically they turn to bonds and treasuries as safe investments. Treasury prices, which experienced a significant rally in 2011 driven by risk adverse investors, have not changed materially since 9/30/2011. It appears that investors are becoming more confident and no longer pouring into treasury securities simply to find safety. This was not the case in 2011 when treasury yields were driven down significantly by investors simply looking for a safe place to put their money. Even infallible gold prices have tapered off slightly from their transcending highs reached last year. The Chicago Board of Exchange's S&P 500 Volatility Index (VIX), commonly regarded as a measure of investor's fear, has been steadily declining from its August peak after the downgrade of the United

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States' credit rating. It has reached levels that we have not seen since July of last year declining nearly 60% since last August. It appears that the series of positive economic indicators that have been coming in since the last quarter of 2011 have given investors more confidence in the economy and rallied stock markets.

Although concerns remain. The European debt crisis is not resolved. Greece appears to be teetering on the brink of default and membership within the European Union. Economic conditions in Europe continue to be difficult and many European countries have recently had their credit ratings downgraded. France, Italy, Spain, Cyprus, Portugal, Austria, Slovakia, Slovenia, Malta and the European Financial Stability Facility (EFSF) were all recently downgraded by the credit rating agency Standard & Poor's.

GDP Readings

In 2011, the media repeatedly discussed the possibility that the U.S. economy could slip back into another recession—a recession being defined as two consecutive quarters of negative growth. These worries were founded on the reported quarterly gross domestic product (GDP) levels in 2011. In fact, three of the four quarterly GDP readings came in at or below 2% in 2011. The good news is that the Q4 2011 GDP reading at 3.0% shows progress and Q1 of 2012's GDP reading is being predicted to come in at 2.10%. These GDP figures may not be enough to celebrate, but they appear to be enough to halt the discussions of a possible double-dip recession. In fact, Q4 2011 GDP figures initially came in at 2.8% but after positive wholesale inventories, freight volume, consumer credit and spending indicators were reported the final revised Q4 2011 GDP reading came in at 3.0%. Overall, the economy continues to be trending along at a gradual pace in what has been widely described as a square-root shaped recovery. GDP forecasts going forward call for cautious optimism in 2012, with quarterly growth stabilizing in the mid 2% range.

The Domestic Economy

Corporate earnings, which have been a bright spot for the economy, have been, as predicted, declining. Companies are still growing their earnings, just not at the same rate that they have been. Of the 500 member companies of the S&P 500, 467 have reported earnings this quarter-to-date and on average reported earning's growth of 5.11% over last quarter. To put this into perspective, last quarter the average earning's growth was 14.38%. Growth is projected to stay below the prior quarter's growth for the next few quarters. Some of this is due to sluggish demand from China and Europe. Although, earnings are forecast to pick back up in the second half of this year.

The labor market has shown signs of improvement. The weekly jobless claims numbers continue to come in below the 400,000 mark which is the point at which the labor market will start to improve. This has dropped the four-week moving average jobless claims, a less volatile indicator of the labor market, to a low that has not been seen since 2008. The unemployment rate has fallen to 8.3% from its 9.1% high in 2011. Non-farm payrolls, which measures employment gains in the private sector, has shown modest growth since October of 2011. All of these signals point to an improving labor market where improvement is needed.

Performers and Laggards

Large-cap stocks fared the best throughout what was a volatile 2011 outperforming mid- and small-cap stocks. However, mid- and small-cap stocks have started 2012 on a better note than large-cap stocks. Investments in companies with growing earnings, termed growth investing, did much better than investments in companies that appear undervalued, termed value investing, in 2011. This trend has not continued in 2012. The stock market's rally has been led by value companies slightly out performing growth companies.

Currently stocks still appear to be priced attractively. The S&P 500's Price-to-Earnings (P/E) ratio, a broad measure of a stock's current value as priced, is not as attractively priced as it was in the Fall of last year, but it is still trading below its 20- and 50-year averages. This indicates a historically affordable time to invest in equity markets. Currently the S&P 500 is trading at a P/E ratio of 14.07, its 20-year average P/E is 20.21 and the 50-year average is 16.52.

S&P 500 Sector Returns Since 9.30.2011

Information Technology Sector	25.69%
Financials Sector	25.80%
Energy Sector	27.02%
Industrials Sector	28.10%
Consumer Discretionary Sector	24.82%
Health Care Sector	14.84%
Consumer Staples Sector	12.50%
Materials Sector	27.82%
Utilities Sector	5.10%
Telecommunication Services Sector	8.83%

Sectors that typically have more exposure to the broad economy have performed very well since Q4 2011; for example, material and industrial companies. While non-cyclical companies that are more insulated from the economy have underperformed during this period, such as health care and utility companies. Overall, with the back drop of an improving economy and valuations below historical averages, the stock market currently looks attractive for long-term investors.

S&P 500 Index

3 Month	10.11%
Year-to-Date	8.99%
1 Year	5.10%
3 Year	25.48%
5 Year	1.58%

S&P 400 Index

3 Month	10.98%
Year-to-Date	11.40%
1 Year	2.54%
3 Year	31.41%
5 Year	4.65%

S&P 600 Index

3 Month	10.20%
Year-to-Date	8.83%
1 Year	5.12%
3 Year	31.32%
5 Year	3.37%

As of 2.29.12

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