



# Dunn Warren Investment Advisors, LLC

## *The Portfolio Reporter*

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*February 2012*

## **Balancing on a High Wire**

The title of *The Portfolio Reporter* this month could not be more apt: balancing between a U.S. economy that is fragile but improving and European countries in a decline. Second, the economic contraction in Europe creates risk of deflation, while central banks printing money around the world, risks inflation.

The economy has shown some improvement in the United States. The Institute of Supply Management announced on Wednesday, February 1 that their manufacturing index, which is a survey of purchasing managers about the state of their companies manufacturing growth, increased to 57.6 from 54.8. Additionally, this is an improvement from 50.6 set in August. Second, Durable goods orders, orders for manufactured items that are expected to last three years or more, increased in December to \$214 billion from the low set in September of \$199 billion

On the other side of the equation, Germany's Gross Domestic Product (a measure of domestic growth) declined 0.25% in the fourth quarter of 2011. The United Kingdom's Economy declined 0.2% in Q4 2011. So while the United States is seeing growth, the economy is balancing that growth against a decline in Europe.

There is a delicate balancing act required when investing in the market against the juxtaposition of a fragile economic state. Countries from the United States to China and Brazil have eased monetary policy. This means that these countries are providing easy loans to banks to loan more money to individuals and companies to generate growth for the economy.

In the last 10 weeks we have seen the following actions: The United States extended loans to European banks in U.S. dollars; the European Central Bank extended \$446 billion dollars of loans to over 500 banks in the European Union; Ben Bernanke, the Chairman of the U.S. Federal Reserve, suggested on Wednesday, January 25<sup>th</sup> after the conclusion of the Federal Reserve Open Market committee, that the U.S. will purchase more bonds, printing more money.

Europe and the US are not the only countries creating more money to goose the economy. Goosing the economy would prod, or give a spurt to the economy by fueling the economy with more money. Goosing the economy means printing more money and lending banks this money to lend to individuals and corporations. In turn, this enables individuals to go out and make more investments and purchase more items. China's central bank facilitated this on December 5<sup>th</sup> when it said it would reduce the ratio of money that banks have to set aside on deposit by 50 basis points among commercial lenders. Analysts are expecting further cuts by the Chinese Central bank to inject 350 to 400 billion Yuan RMB (55 to 63 billion U.S. dollars) into the market, as reported by the Associated Press on January 17<sup>th</sup>. Not to be left out, when India's policy committee met on Tuesday, January 24<sup>th</sup>, India's central bank slashed the minimum cash reserve requirement (CRR) by 0.50 percentage point to relieve tight liquidity, freeing up banks to lend more to individuals and companies.

The U.S. is on course to print money to stave off declining home prices in the U.S. and economic decline in Europe. This push by the U.S. Federal Reserve to increase money into the economy runs the risk of driving commodity prices higher, as international economies are trying to prevent their own slowdown. Previous monetary easing on the part of the United States drove the price of commodities higher, driving up inflation. Consequently, our investments need to benefit from the deflation potential on one hand, as well as the

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inflationary environment from printing money on the other hand.

In Variable Annuities, we have a mix of investments in utilities, consumer staples and healthcare, which are more resilient to an economic downturn. For the improved economic environment, we have added investments in small and mid-cap value. Last, we have a position in bonds. With the U.S. government indicating a willingness to purchase bonds and print money, this will keep interest rates low and the value of bonds stable.

In Exchange Traded Funds and Variable Annuities we continue to hold inverse funds which increase (decrease) in value if the market declines (increases). We also have added high yield corporate bonds to the government bonds. Last, our mix of utilities, consumer staples and healthcare continues, but we have added a position in biotechnology, regional banks and the Philippines.

In walking the high wire of the economy and the stock market, we are taking a balanced approach between the market risk of high valuations and a fragile economy. Hopefully a safety net is not required, but if it is, we have invested in some funds that will suffice.

*Please feel free to pass "The Portfolio Reporter" to interested friends and family members. For more information about your investments, please contact your financial professional.*

*The opinions expressed here are based on the author's views and should not be construed as financial advice. Model results do not represent actual trading and may not reflect the impact that material economic and market factors might have on the advisor's decision-making if the advisor were actually managing a client's money. Past performance is no guarantee of future performance. There can be no assurance that a client's investment objective will be achieved or that a client will not lose a portion or all of his or her investment. Please contact Dunn Warren directly for a list of the recommendations provided over the last year. Investing outside the United States involves additional risks, such as currency fluctuations, periods of illiquidity and price volatility. These risks may be heightened in connection with investments in developing countries.*

### **MONTHLY CONFERENCE CALL**

**Our next monthly conference call will occur Thursday, February 16th at 11 a.m. Mountain Time (1 p.m. EST).**

***Phone Number: 866-740-1260***

***Access Code: 4682824***

**To view slides on the internet during the call, go to [www.readytalk.com](http://www.readytalk.com) and enter 4682824 under "PARTICIPANT, Join a Conference".**