REVIEW & COMMENTARY
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Job (B)less America

The jobless recovery; that is what many have named our current economic condition. The threat that a jobless recovery provides is that the recovery won't be sustainable. The recovery to date has been the responsibility of the consumer who, through tax breaks, mortgage refinancing and low interest rates has continued to spend. The legitimate concern is that without new jobs being created, those responsible over the past few years will simply exhaust themselves and their resources, allowing the economy to fall back into recession.

Why no jobs? Many look to China whose manipulated currency remains artificially low thus placing U.S. manufacturing at uncompetitive levels. Though we will admit that many manufacturing jobs have been lost to China, we believe that there are many reasons why this trend, while not reversing, will not totally displace the U.S. manufacturer. One is that inventory control is one of the most vital issues to face American business. While labour rates are advantaged in China, inventory delivery can not be guaranteed. That is why large manufacturers such as Dell and many other technology companies continue to maintain facilities close to their customers. They won't take the risk of late deliveries.

Further, over the past 18 months it has become quite evident that the U.S. policy toward its currency has changed. In fact, it has changed dramatically. Despite Treasury Secretary Snow stating that the government supports a strong dollar, a reversal from earlier comments, a weaker dollar is one of the few ways to combat some of the U.S.'s financial shortcomings, namely a trade deficit that has grown exponentially over the past decade. In addition, a weaker dollar will advantage exports, a component of the economy that has suffered considerably over the same time period. But the weaker dollar has already shown evidence of this trend reversing. This past July, U.S. exports rose to levels not seen for over two years.

It is well known that both Japan and China have thwarted any appreciative pressures on their currencies but the U.S. has been quite direct in their admonishment of the practice. Admittedly, the thought that both these Asian powerhouses will allow their currencies to float may be fanciful, we would bet that the currency disadvantage will lessen over the next few years. Japan, after all, has been suffering for over a decade from deflation and is starting to show signs of an economic turnaround. China, eclipsing any nation in economic productivity, is in desperate need of raw materials and may have to provide some concessions to satisfy this demand. Even the relatively modest currency gains will translate into increased competitiveness for U.S. goods abroad which should not only strengthen GDP but also improve corporate earnings and, ultimately, employment opportunities.

Everyone loves numbers. The unemployment number tends to be the focal point these days. But even the drop in U.S. unemployment numbers from 6.2% to 6.1% in July is misleading. While it looks as if things are improving, the improved numbers merely reflect the fact that more people gave up looking for work. But if you look past the U.S. Labour Department's Unemployment number, there are a number of positive signs emerging. One is that temporary help positions continue to increase. This is usually the first step businesses take when demands turn. Another statistic that has been rarely referred to is the rise of self employment. With the exception of Dick Grasso and most of the other denizens of Wall Street, many unemployed start their own businesses. Small and medium sized businesses have created more jobs than any other sector over the past 10 years. A measure of the self-employed is Non-farm proprietors' income which showed annual growth of over 9% for the year ending July 31, 2003. To give you an idea of how influential this number is, according to Business Week, it represents 10% of all personal income and accounts for nearly a quarter of the increase in overall income in the past year. It is now at a level equal to boom years of the 1990's.

The most recent poor returns of the stock market mirror those of the 1930's; four straight years of down markets. Similarly, many people are drawing the same comparison with unemployment. Robert Barro, an economics professor at Harvard University recently detailed a comparison of the unemployment picture. While the good news is that present levels are no where close to those of 70 years ago, recessions in 1948-9, 1957-8 1974-5 and 1981-2 were also much worse. The most recent of these downturns 1981-2, one which most of us will remember, saw unemployment levels reach almost 11%.

Jobs may be slow to come back but they will. Interestingly, it took several years into the computer age before productivity started to show signs of marginal improvement. The recent rebound in the economy without a lot of new jobs is merely a reflection that this trend will continue.

While present employment numbers may not tell the whole story, we think the stock market is right; better times are ahead.

And given everyone's preoccupation with numbers, we have a few we would like to bring to your attention. We are celebrating our 10th anniversary as a money manager and our 5th year of independence under the Stodgell Investment Management banner. Thank you to all our loyal clients, friends and family for supporting our growth.

Stodgell Investment Management Ltd.