

### Battle of the Bulls and Bears

The two interpretations couldn't be much further apart – one holds that the stock market has managed to get past all the bubble nonsense and is prepared to settle into a longer term pattern of growth. This is the theory that holds that the bull market is real and here to stay for an extended period of time. The bear market assessment holds that the same conditions that triggered the bubbles in the early part of the last decade and again in the collapse that led to the last recession are setting up and threatening the market with another major crash. The two prime opponents in this debate have been disagreeing with one another for years and represent polar opposite positions despite being very good friends and colleagues.

Robert Shiller has been one of the leading doom merchants in the economic community for some time and he contrasts sharply with Joel Siegel who has been more consistently aggressive than many as far as asserting the strength of the markets and the economy itself. The two economists look at entirely different systems and indicators to assess what the market is likely to do and both have reams of historical data to support their position. This is part of what delights and informs economic debates but it drives the average investor crazy as there is no way to really debunk or support either theory completely. Shiller looks at the ten year average and the price-to-earnings ratio. He notes that under normal conditions stocks trade under 16 and that they are now trading at 20 and above. That suggests to him that a run of subpar performance is imminent. But Siegel scoffs at this dependence on the ten year average as too much has changed in the economy to allow the past to serve as that kind of guide. He holds that a better guide is analyst's long term projections as he thinks it is vital to eliminate all the special write offs that companies engaged in as they distort the averages that Shiller works with. He also points out that over an even longer term horizon; the performance of the market has averaged about 7% growth a year.

**Analysis:** What is perhaps the most interesting aspect of their debate is where they agree. Both hold that the government driven interventions have distorted the market and not always in a good way. They agree that some of the extraordinary measures that flooded the system with liquidity were good ideas but neither has been a big fan of the bank bail outs. They opposed the plans on principle as the both hold that moral hazard is a key concept but they also question the strategic execution that rescued Bear Stearns but left Lehman Brothers to founder. They also worry that all the government help has made the economy far too dependent on this largesse and that there will be a reaction when the process is reversed. Siegel is more confident in the ability of the Fed to pull this off than Shiller is.

This debate between two imminent economists who study the market closely illustrates how hard it is to get an accurate read on the subject. They can't both be correct and both have a track record of being accurate more often than not. The fact is that the economy is in a state of extreme flux and probably will be for some time to come. This is making predictions that much harder and leaves the investor with that much less to base their decisions on.

### States and Municipalities Worry About Losing Business Momentum

The competition for business development that exists between states and cities is always intense but lately the seriousness of the situation has become more and more obvious. The prime concern of most political leaders is whatever the constituents are most concerned about. In good times the issues are often ones of convenience and expansion. People want more amenities and more city services. They want new shopping centers, better schools, more convenient roads and better trash pick-up. The list of things that concern people gets very long and complex. When times are bad, the focus is often on jobs and the protection of their core assets. People become more focused on issues like the value of their homes and crime. Either way the political leaders at the state, county and municipal level are faced with demands that they can't meet without solid economic development. This is the prime reason that almost every community of any size has someone whose job is developing business opportunities for that community. This is the basis of the tax base and it is the crux of what keeps people in the areas as these are the companies that provide the jobs and the amenities that people want. In times of stress the ability of these communities to keep pace is threatened and over the next year or so the stress is likely to be as serious as it has been in some time.

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**Analysis:** The fact that local and state governments are going to be in trouble this year is no secret. As bad as last year's budget woes were, they are expected to be far worse this year. The tax revenue that supported last year's budget came from 2008 receipts. These were anemic as compared to the revenues generated in the past but they were downright generous as compared to the tax receipts that appeared in 2009. The majority of the states are looking at budget cuts that average around 20% and for some states the cuts will be twice that. The crisis extends to cities and countries as well. The ability of the various jurisdictions to carry out their normal levels of activity is in serious question and this has created some very hard decision making. The threat from a long term perspective is that cuts made this year and next could well compromise these communities for years to come. The challenge is to maintain the basic services that the constituents demand without losing all connection to the kinds of investment that business requires to stay engaged in a community. It is a real dilemma for those cities that face the most serious budget issues.

There is tremendous variety in terms of how different states and communities have reacted to the crisis but there appear to be three dominant strategies as far as the budget is concerned. One approach holds that the highest priority is to protect the weakest members of the community. This translates into protection for those programs that support the poor and the elderly. The social budget is left alone as much as possible and the cuts then come from programs that are generally focused on the business development efforts. These are the budgets that pay less attention to infrastructure development and less to efforts to promote the city. Marketing efforts end and so do outreach programs to draw in business. There is also a reduction in focus on the issue that most concern business. The lack of attention to infrastructure can compromise development plans if there are significant issues with roads, airports, seaports, rail lines and other transportation centers. These cities are often not in a position to offer much in the way of incentives either. The decision to protect the most vulnerable is hard to question but it leaves the entire city vulnerable in the longer term.

The second strategy is to focus on what would create the most work for the community as a whole. These are the communities that try to focus more energy on the infrastructure needs. The intent is to prepare the ground for more business expansion but at the same time encourage job growth by developing labor intensive projects. This is much harder than it seems as many of the projects are not executed by local labor and in many cases the development is far more technological and machine oriented than would be ideal for a job boosting program. The field of construction is highly specialized and it is not guaranteed that a major project will employ many of the locals – if any at all. The development of the needed infrastructure is certainly a development boon in the longer term as the investment will allow for expansion when the economy starts to recover but little of this effort provides immediate relief.

The third strategy is one that attempts to focus on the issues of business development even as other programs might suffer. This is exceedingly hard to pull off as the natural constituents of this approach are often not in the community as yet and it is very hard to prove that money spent on these efforts will have an immediate impact. The approach tries to look at what the business community requires to enter a given city or community. This is always a tricky assessment as the needs vary and it is often difficult for a given community to address them all. Over time, the highest priority issues have include the quality of the school system, the quality of the transportation infrastructure, the tax burden, quality of the workforce the housing stock and its average price, the existence of entertainment and cultural venues, the weather and the extent of city services. In many cases there will be communities that compete with one another in a single geographical region and this generally creates extreme pressure to offer more and to require less from the incoming business. Right now the City of Los Angeles is in a battle for its very existence as it loses more and more development to the surrounding communities and this is not a unique challenge for LA. Almost every major city in the US has faced the challenge of watching too much business drain to the surrounding communities.

The long term solution for a city or state is grounded in making the business community work for it. This is what creates the tax base and platform for future growth. This requires making the community appealing and reacting to the needs these businesses have but the process of accommodating these requirements in the middle of a fiscal crisis is daunting. The constituents that are losing services and watching their lifestyles erode are not supportive of the budget plans – even though they may well benefit in the longer run. This is a tricky process to sell in the best of economic times – and nearly impossible during times of stress.

### **Employment Not Expected to respond to Economic Growth Soon**

The latest manpower survey of employers reveals what many have been asserting for weeks. The majority of employers are not planning to add significantly to their work force in the near future. The survey revealed that about 73% of the employers expect their hiring to be flat this year but the good news is that very few are anticipating further big layoffs. There is both good and bad news in this survey. The fact is that employers rarely act proactively when it comes to job gains. When there is new demand and a need to add workers they will do so but very few hire in anticipation. That is the prime reason that employment remains a lagging indicator of the economy. The good news is that these surveys shift direction very quickly when economic conditions turn positive.

**Analysis:** One of the issues that has been brought up by the employers is the vast improvements in productivity that have taken place during the recession. This alters plans for hiring at least for a while. The gains have stemmed from both the use of technology and the fact that current workers are doing more than in the past. This latter factor is temporary however. There is only a limited period of time during which the workforce can and will perform at this level. Burn out and break down will occur at some point and productivity lags.



### **European Climate Change Directors Very Pessimistic About Progress This Year**

In the aftermath of the Copenhagen climate meeting the sense was that most of the momentum for a climate change agreement had evaporated but there had been those who still insisted that something tangible would be developed before the year was out. The first blow to this group of optimists was when the UN climate change director resigned his position in frustration over the pace of the talks. Now there comes a statement from Connie Hedegaard, the Danish Minister who put together the summit and serves as the European Union's Commissioner on climate change. She was trying to assert that there were some possibility for a comprehensive treaty this year but has now reversed her position and is convinced that nothing will develop this year and possibly not in the next two or three. She is now convinced that something catastrophic will have to occur before the issue is taken seriously and she is resigned to the fact that political agreement is going to be nearly impossible to achieve.

The critics of the climate change strategy that have been on display in the last couple of years are as divided as those who are supporting some kind of response. The extreme position as regards climate change skepticism comes from those who do not agree that the data supports any change at all. They have reacted very strongly to the shoddy science that has come from the UN panel on climate change and have asserted that too many of those engaged in the issue are biased. The other opponents of the climate change effort accept that there has been change and that the world's climate has been altered but they are not sure what to attribute the changes to. They generally accept that man made contributions are a factor but differ as far as the relative importance of greenhouse gas. They assert that draconian efforts to reduce it will cost hundreds of billions of dollars and may not make a measurable difference after all. Then there are the pragmatists who may accept the evidence of climate change and the role that man made pollution causes but are insistent that any plan that doesn't engage China, India, Russia and the other developing nations is less than useless as it will require industrialized nations to cripple themselves economically while some of the world's largest contributors are required to do nothing at all.

There are serious divisions within the community that wants action on climate change as well. There is general agreement on the problem and man's contribution but that is where the cooperation ends. Some are taking the purist stance and demand that the world's population cut their energy use seriously enough to reduce greenhouse gas emissions to near zero. That would mean a wholesale abandonment of the current lifestyle in the US, Europe and other developing states. Then there are the pragmatists who want to promote alternatives as fast as possible – more nuclear power, more electric cars, and more technological solutions in every sector. The gradations between the two positions are extensive.

**Analysis:** This is the crux of the problem for climate change negotiation. There is far too little consensus on the core issues and what is to be done about them. The current suggestions have been attacked as far too expensive and far too ineffective. Even the most ardent advocates for a policy recognize that anything that fails to include China in a meaningful way is doomed to be both a failure as far as emissions are concerned and a crisis as far as the economic growth of the developed nations are concerned. The fact that too many of those on both sides of the issue have engaged in overt manipulation of inadequate data only makes the situation more untenable. The time for an objective assessment is long past due but in the current environment, it would be almost impossible to create a panel that would have universal respect. The debate has become ideological and has been taken out of the realm of science and fact altogether.

### **European Monetary Fund is Given Slim Chance at Best**

The proposals to create a European version of the International Monetary Fund sounds like a solution to the current PIIGs problem as it would ostensibly establish a fund that could be used to bail out nations that are facing a financial crisis but the plan is certainly not as easy as all that. The IMF has been a controversial creation since its inception at the end of World War II and the EMF would be no less controversial given the fact that it would need to combine carrot with stick – just as the IMF does. The crux of the issue is whether an institution like this would have the power to impose the kind of budget restrictions and modifications the IMF is empowered to do. The IMF stick is that failure to accede to their demands means that the nation in question forfeits its access to the funds it needs. Countries turn to the IMF when there are no more options. The EMF would be inexorably linked to other pan-European issues and the threat the IMF has would not exist with the EMF. The IMF can just walk away and let the chips fall but an EMF would need to consider what that move would mean to other European issues.

**Analysis:** The most optimistic of analysts hold that the EMF is not likely to happen without a major treaty that would need to be ratified by the entire EU. That is simply not going to happen in the current environment and there is no major power that is willing to stake their reputation on this issue.

### **African Economy Set to Expand faster than Most in 2010**

The good news in Africa is that the growth rates that are anticipated this year are better than they have been in some time. Obviously some states will do better than others but the majority of the sub-Saharan states will grow at or around 5% for the year. That is still far too slow to drag this area out of development limbo but it is a vast improvement over what was chalked up in 2009.



### **Will They Never Learn?**

The Canadian government decided that the country's anthem was "inappropriate" and suggested that it be made gender neutral so that it would not offend. There is that line in there about the "True patriot love in all thy son's demand". It must be altered in some way – perhaps to "Tru-ish mildly supportive of government policy affection in most but not all thy progeny's request". The reaction from the population was swift and extreme and the government backed down in a hurry. It appeared that voters were ready to fire every last one of them over this. One can only marvel at what goes on in the minds of these people when their nation is just clawing its way from recession. But there are those who have attacked the Star Spangled banner as jingoistic, nationalist, militaristic and hard to sing on key. One can just imagine what could be done to that anthem.

**Analysis:** One could start with the first line as it discriminates against those who are visually impaired. "Oh say can you see?" That would need to be altered to "Oh say can you sense in some way?" You get the idea. In fact the version that is actually used leaves out some pretty interesting original verses from the original – such as this one: "Oh! thus be it ever, when freemen shall stand - Between their loved homes and the war's desolation! - Blest with victory and peace, may the heaven-rescued land- Praise the Power that hath made and preserved us a nation. - Then conquer we must, when our cause it is just, - And this be our motto: "In God is our trust." - And the star-spangled banner in triumph shall wave - O'er the land of the free and the home of the brave!"

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