



THE CATALYST FOR THE NEXT STOCK MOVE

With all the news focused on high gas prices, rising interest rates and a possible housing bubble, the fundamentals of the U.S. equities market continues to show strength. Not many would have expected the stock market to hold up in the face of these typically negative impacting factors. One main catalyst for the market has been the success in the corporate sector. The second quarter corporate profits grew by double digits, surprising most economists. Solid job growth with a steady 5% unemployment rate has also kept the U.S. economy on track this year.

There is little debate that corporate profits will have an increasingly difficult time continuing at their current double digit growth rate into 2006. With that established, should we continue to be bullish on the U.S stock market? If the savings rate in the U.S. is near zero, wage growth flat, and gasoline prices inflating, where will the stock market growth come from? One look outside the U.S. and we see an extremely positive trend. Cash savings world wide is estimated at \$11 trillion (the size of the U.S. annual GDP!) and growing fast. This cash glut has been fueling the housing boom and the global bond market boom. Both the housing market and the bond market respond to supply and demand. Most home owners have benefited from the enormous demand for homes due mainly to historically low interest rates. With bond yields down and bond prices high, it is obvious that the demand for bonds, especially U.S. bonds, is huge. Clearly, a large part of the global cash savings is in the housing and bond markets.

As portfolio managers, the real question we ask is, "What is next?" With the housing prices headed for an inevitable slowdown and bond yields continuing to be low, where does the cash go next? The logical answer is the U.S. stock market. While our market has performed well over the past several years, it is obvious that a large amount of investing dollars have stayed away. We contend that as real estate and bonds become fully valued and less of a growth opportunity, the U.S. stocks will come into favor. Specifically, we contend the additional capital from global savings will come into the market in a wide-spread fashion. We continue to like the large growth companies. Imagine the impact that just a portion of the \$11 trillion of world wide cash would have on U.S. stock prices.