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## Portfolio Commentary

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After a shaky ending to August, hopes for a new beginning in September were quick to be dismissed. Rising concerns over the troubled Eurozone made its mark this month, when worries over the global economic landscape morphed into a full throttle market panic. Compounding sovereign debt issues, the conflicting political and economic interests of countries in the EU delayed action by European policymakers. The delay seems all too familiar in U.S., fresh off the heels of similar political conflicts in Washington over the debt ceiling, the event which triggered Moody's downgrade of U.S. Debt. The weakening global economy, exasperated by growing concerns that European officials will not be able to contain the crisis, drove yields to their lows for the year. The 2-Yr reached a record low for 2011 on September 19th, at .16%, down from a high reached on February 8th of .85%. It comes as no surprise that the culmination of events contributed to a global equity sell off that just never seemed to end.

Stagnant economic growth in the US, reinforced by the bevy of weak economic indicators added further disappointment to the market. Topping the economic news, the release of the August labor report offered a flat reading in non-farm payrolls. Private payrolls rose just 17K in the same period and the unemployment rate remained unchanged at a staggering 9.1%. Economists polled by the Wall Street Journal believe the chance the U.S. will slip into a recession again over the next year are now one in three, the highest odds since recovery began in mid 2009.

In its continued efforts to energize a recovery, the FOMC reaffirmed its pledge to keep its benchmark interest rates at a record low at least through mid 2013 to and also that it was prepared to employ additional tools as appropriate to aid the economy. Secretary Geithner made an unexpected trip to Europe to implore his European counterparts to act quickly and decisively, suggesting a move similar to the US form of TARP made available to US Banks during the 2008 Crisis. During his visit, he said "It is completely within the capacity of the stronger members of the Euro area to absorb these costs. Costs would be much, much greater if they were to sit and do nothing."

Meanwhile, living up to elevated speculations surrounding the FOMC's two day meeting in September, the Fed announced Operation Twist as a means of providing market stimulus to the weakening economy. Relative to prior forms of intervention by the Fed, the plan does not include the injection of more capital into market. Instead, "Twist" includes an aggressive plan to buy longer term Treasury debt in an effort to bring down longer term rates and flatten the slope the yield curve. Although many economists and analysts believed the operation would carry little if any effect on long term rates, the strategy, has been somewhat of a success. Since the Fed's action was no more than a tacit acknowledgement that there will be no more meaningful stimulus, the early success of "Twist" offers a small glimmer of hope to an otherwise bleak market.

Rating agencies slashed the ratings of sovereign debt and banks, adding more fuel to the Eurozone fire. In Mid-September, Moody's downgraded the ratings of Societe Generale and Credit Agricole on concerns over their ability to manage exposures to Greek debt. Domestic banks, meanwhile, did not escape the whirlwinds of September unscathed. Bank of America, Wells Fargo, and Citigroup took a hit to ratings based upon Moody's belief of a decreased probability that the US Government would support the banks as it did in 2008. While Moody's did recognize improvements in the banks' overall credit profiles since the crisis, the primary decision for the downgrade was based on the diminished baseline assumption of systematic support. Moody acknowledged "there is an increased possibility that the government might allow a large financial institution to fail," taking the view that contagion would be limited and the government would not intervene as it once did in 2008.

The saga in the Eurozone will continue to distract US equity and bond markets while dictating the direction and associated volatility of both. This certainly keeps the market "interesting" and also creates opportunity to trade "the range". Europe opens strongly, US Treasuries trade off, creating opportunity to buy short dated Fixed Income securities at attractive levels. Negative news on one sector translates into contagion trading and again creates opportunity to find value. We have used the volatility to find attractive corporate notes and agencies for our clients' portfolios.

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