July 7, 2012

Dear Clients and Friends,

***"Living at risk is jumping off the cliff and building your wings on the way down."***
- Ray Bradbury (paraphrased)

Ray Bradbury, the *Fahrenheit 451* author who passed away last month, once said his seminal novel was not an attempt at predicting the future, but rather preventing it. Indeed, his many technological divinations –ATMs, earbud radios, oversized flat-screen TVs, and digital "walls" remarkably akin to today's social media websites – were paralleled by his dark vision of a dystopian world that was nevertheless rooted in the trending realities of his time.

Recent economic events highlight the monetary dystopia that is Europe, and the ultimate outcome is difficult if not impossible to predict. The Euro currency itself was established to mitigate trade volatility, but disjointed fiscal policies have thrown the viability of the Euro into question. Can a breakup of the Euro be prevented? Possibly – if the involved countries can better align their fiscal and monetary goals. Much easier said than done! To wit, a mere two weeks ago the Europeans announced a mechanism for aiding the struggling European banks; today they said that Spanish banks – among those most in need of capital – may not be eligible for the program. The Euro hit a two-year low against the US Dollar in response to the update.

Meantime the US heads toward the so-called year-end "**fiscal cliff**," when tax breaks expire and federal spending cuts kick in. The dire outcome, a marked slowdown in domestic economic activity, can be prevented if policy makers take appropriate action. The Federal Reserve has already announced that monetary policy alone may be insufficient to sustain economic growth, and that fiscal policy must follow suit. Unfortunately, politics plays a huge role in fiscal policy, and with the November elections approaching and rhetoric heating up, the odds of Republicans and Democrats forging a "grand bargain" are diminished. Let's hope they figure out how to build their fiscal wings before hitting bottom!

Uncertainty here and abroad has led to a slowdown in corporate earnings growth, with the next round of profit reports expected to show a decline for the first time in the past eleven quarters. Retail sales have also slowed, leading to concerns about the coming back-to-school shopping season. Unemployment has not improved in the past three months, but thankfully planned layoffs are trending lower.

Despite the earnings slowdown, **equity valuations remain very reasonable by almost all historic measures**, and though the projected annual earnings growth rate has slowed to around 5-6%, the absolute level of earnings remains near all-time highs. Similarly, **interest rates will likely remain low for the foreseeable future**, further supporting equity valuations. And the recent decline in commodities prices, especially gasoline, gives a tailwind to the consumer; every 10 cent decline in gasoline adds $11 billion to consumers' wallets over the course of the year, according to Moody's.

We continue to believe the most likely global scenario is one of "muddling through," with an extended period of slow growth marked by periodic spikes in volatility. In that environment, markets will react to news about the Euro and the US economy, but may drift sideways in the near term. That's not to say there won't be pockets of higher potential growth, but our primary focus remains on improving cash flows – dividends and interest – for your investment portfolios.

Sincerely yours,

Mitch Schlesinger
FBB Capital Partners

T | 301.657.8870 F | 301.657.0566 | www.FBBcapitalpartners.com | 4520 East-West Highway | Suite 450 | Bethesda, MD 20814