

# Perspectives

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## STOCK MARKET: WORST SELL-OFFS WERE OFTEN FOLLOWED BY RALLIES

The Dow Jones Industrial Average has fallen 15% year to date and a total of 20% since its high of 14,279.96 set in October of 2007. The U.S. dollar has lost 60% of its value versus the European currency since 2001. The price of gasoline has more than doubled in the past year and a gallon of diesel is over \$5. And housing prices continue to decline in most parts of the country. Why should you stay invested? The United States economy is positioned for explosive growth, but first let's look at what history tells us about similar rough patches for our stock market.

Since 1950, the U.S. stock market has encountered similar declines 10 different times. The worst three-month declines in the S&P 500 Index are listed below. In the subsequent 12-months following the worst declines, the stock market recovered all of its losses and has gone on to significant double-digit returns 8 out of 10 times.

3-Month Period Ending	3-Month Decline	Subsequent 12-Month Return
Nov-1987	-30%	23%
Sep-1974	-25%	38%
Jun-1962	-21%	31%
Jun-1970	-18%	42%
Sep-2002	-17%	24%
Sep-2001	-15%	-20%
May-1962	-14%	23%
Oct-1990	-14%	34%
Oct-1957	-13%	30%
Nov-2000	-13%	-12%

As history demonstrates, some of the worst short-term losses were followed by substantial rebounds. The snap-back rallies were often as abrupt and difficult to time as the original sell-off. In many cases, investors would have been better served by remaining fully invested during the entire period--enduring near-term pain but not missing out on the subsequent rebound.

### Is it different this time?

Yes, this time it is different--it's better. The high price of oil and the devaluation of the US Dollar have certainly taken a toll on the stock market but that is not the full story. There are structural changes afoot in the US economy. There is a shift in awareness of most Americans. They are becoming more conscious of the amount of energy they consume, not for ecological reasons necessarily but for practical ones. Today's mantra is spend less, consume less and become more efficient.

Americans are changing their behavior fundamentally in response to high energy costs. For example, we drove 50 billion fewer miles in our cars this year. General Motors has idled truck and SUV plants and their once popular Hummer division is for sale. Why has the price of oil and its distillates gasoline and diesel become so very expensive? The reason is not due to lack of supply and recent data tells us it is not caused by increased demand; the reason for oil prices rising began with our own legislators.

The US government has been spending money in an unsustainable way for the better part of 10 years. And the country has continued to print more currency to pay for the un-

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precedented spending. Just like a company that issues more shares, the original shares become diluted and worth less and less. This has resulted in a devaluation of the US Dollar over the past 7 years.

Oil is traded globally and denominated or priced in US Dollars. As the US Dollar has decreased in value, the price of oil has increased in order to maintain its comparative value. The lower the dollar goes, the higher the price of oil. So, if the dollar goes up, then oil should go down. But waiting for Congress to balance a budget or limit spending may never happen, so will any other factor help bolster the value of the US Dollar?

Yes. Prices of US denominated assets like real estate and stocks are cheap relatively speaking and now on sale in the global market place. As global investors, sovereign wealth funds and banks seek value to reallocate their investments, the US market is the most attractive option. More buyers of US currency and dollar denominated assets will at first stabilize the prices and later reverse the decline we have experienced over the past year.

The future for the United States is brighter for another reason. The high price of energy has made foreign manufactured goods more expensive to transport. And, the higher costs of food and other agricultural products have led to global wage inflation. As goods

once made inexpensively in China cost more to produce and ship, their comparative advantage versus domestic manufacturers has declined considerably. The functions once outsourced to emerging market economies to save money will likely return to US soil in the next 5 years. A migration of small and mid-sized manufacturers back to the US will likely find their homes in the once idled plants and factories of our South and Midwest, spurring more investment in our economy and a rebirth of our middle-class. It is always darkest before the dawn and the best days for the US and its stock market are ahead of us. Stay invested for the long-term.

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