

# 8 REASONS WHY (WE BELIEVE) THE RECESSION IS OVER

We believe the worst recession since the 1930s is over. Signs of recovery are everywhere. It's time for investors to look forward and to stop looking back. In this report, we discuss eight reasons why we believe this recession may be over.

## 1 Leading economic indicators are positive.

The Conference Board's Index of Leading Economic Indicators, which is designed to anticipate changes in the economy by three to six months, rose 0.6% in August for its fifth consecutive gain. This gauge has an impressive track record of calling turns in the economy. The stock market, another leading economic indicator, has already rebounded more than 50% from its March lows.

## 2 Global economies are recovering.

The Organisation for Economic Co-operation and Development's (OECD)\* composite leading indicators for its member countries recorded their largest increase in July since records began in 1962. For the first time ever, all 33 countries recorded an increase in June, and all but one rose in July. Japan's economy grew this past quarter for the first time since early last year. Europe also appears to be pulling out of recession, with positive growth reported in the most recent quarters in Germany and France.

## 3 The job market is improving.

Non-farm payrolls declined 263,000 in September, worse than expectations for a fall of 175,000 and compared with a decline of 201,000 in August. However, the decline in non-farm payrolls has slowed in six of the past seven months after reaching a peak decline of 741,000 in January. The decline in employment caused the unemployment rate to rise to 9.8% from 9.7% in August, as expected. Employment has been a lagging indicator of the economy, improving at the end of or well after every recession in the postwar period.

## 4 The Federal Reserve's efforts to stabilize the financial system worked.

The massive efforts to slash interest rates and provide trillions in funds to the financial system have succeeded in restoring conditions in the money and corporate credit markets. Corporate America has taken advantage of attractive rates to refinance old debt and fund new acquisitions. Companies issued more than \$800 billion in new bonds during the first seven months of 2009 – nearly a third more than a year earlier. In the money markets, the three-month London interbank offered rate is down to 0.28%, less than one-tenth of where this short-term benchmark stood at the worst of the credit crisis last October.

## 5 Bank lending is increasing.

Banks' profitability and capitalization have improved, and banks have started lending again. According to the Fed's recent periodic survey of banks, about 30% said, on net, they tightened lending to businesses in May, June and July, but that's down from roughly 40% in April's survey. The percentage of banks that tightened standards on commercial real estate loans dropped 20 percentage points to 45%. For residential real estate, the percentage fell to 20% from a peak of about 75% a year ago. Most banks expected lending standards across all loans would remain tighter than their average levels over the past decade until at least the second half of 2010. However, the improvement in bank lending should be enough to support economic recovery.

## 6 Expectations for 2010 economic growth continue to improve.

- In a recent *Wall Street Journal* survey, 80% of economists said they believe the recession either has ended or will end by September. In addition, economists continue to upgrade expectations for growth in the rest of 2009 and beyond.
- The International Monetary Fund said in a recently revised forecast that the world economy will expand 2.5% in 2010, compared with its April projection of 1.9%.

## 7 Housing has bottomed.

The S&P/Case-Shiller home price index advanced 2.9% in the second quarter from the previous three months, the first increase since 2006 and the biggest in almost four years. The index extended gains when it rose 1.2% in July from June, the biggest monthly jump since 2005. Foreclosure-driven declines in prices, government credits for first-time buyers and near-record low borrowing costs are expected to continue stoking demand.

## 8 Manufacturing is on the rebound.

The Fed said industrial production rose 0.8% in August compared to the month prior and followed a 1.0% increase in July. This was the largest back-to-back gain since 2005 and followed nine consecutive monthly declines. European industrial orders increased 2.6% in July compared to June, the second consecutive increase, according to the European Union's statistics office.

### Why Does It Take So Long to Call Recessions “Officially Over”?

The official “scorekeeper” of recessions is the National Bureau of Economic Research (NBER), a private organization in Cambridge, Mass. These folks aren't terribly interested in forecasting turns in the economy. Instead, they focus on making sure their recession start and end dates are absolutely accurate and not subject to future revisions. Robert Hall, who heads the NBER's Business Cycle Dating Committee, recently said it is “more important” this time around for the group to adhere to the principle of not calling an end to the recession until after economic growth has surpassed its previous peak, “which could take 18 months or more to determine.” The group took until July 2003, 20 months after the fact and well after stock prices had begun to recover, to declare the last recession had ended.

### Don't Bet Against History

Historically, the stock market has performed well once recessions end. The chart below shows the performance of the S&P 500 six and 12 months after postwar recessions ended. While history is not always an accurate guide to the future, it does suggest that investors who are out of the market are betting against a lot of history.

#### S&P 500 Performance after Postwar Recessions

Recession End Dates	% Change 6 Months Later	% Change 12 Months Later
10/31/1949	10.97%	19.57%
5/25/1954	18.63	29.98
4/30/1958	17.77	37.12
2/28/1961	7.86	7.51
11/30/1970	15.06	4.49
3/31/1975	6.57	30.63
7/31/1980	1.28	1.82
11/30/1982	15.46	22.18
3/28/1991	3.55	12.14
11/30/2001	-1.66	-10.04
7/31/2009 (est.)	TBD	TBD
<b>Average</b>	<b>9.55%</b>	<b>15.54%</b>

Source: Ned Davis Research. Daily data starting in 1947. Six months measured by 126 market days; 12 months measured by 252 market days. The S&P 500 index in not managed and is not available for direct investment.

### You Can't Recover If You're Not Invested

There are always risks to the outlook. The recovery could be uneven, or something unforeseen might derail the progress we've made. The stock market could correct at any time for any reason. But these things are unpredictable. Our advice remains the same: Don't base your investment decisions on predictions; base them on investment principles. Focus on the things you can control: the quality of the investments you own and the diversification of your portfolio. Maintain a long-term perspective.

It looks as though the economy is improving, but that doesn't mean you should throw caution to the wind. Instead, sit down with your Edward Jones financial advisor and talk about ways you can take advantage of the improving climate while still managing risk.

And remember, you can't recover if you're not invested.

\*The OECD, located in Paris, spells “organisation” as it's listed.