

January, 2005

Dear Clients and Friends,

The US economy will see modest but healthy growth, subdued inflation and only slight rises in interest rates this year, according to a survey of economists.

– Front-page headline from The Wall Street Journal, January 3rd, 2005

It's fun looking at the fashions back in those days, you know, all of the frills and bell-bottoms.

– Tiger Woods

One of the preceding quotes is about the future. As the former is almost precisely what we said was going to happen *last* year, the latter must then give us pause for concern about the coming trends in the garment industry and perhaps the economy as a whole. For indeed, the emerging economic climate looks startlingly like that of the early 1970s: Remember skyrocketing energy prices following the 1973 Yom Kippur war? The seemingly nonstop rise in food prices? Nixon's inheritance of LBJ's **guns-and-butter** spending policies, in which outlays for both domestic and military programs increased without a concurrent tax hike to pay for them?

All three characteristics of yesteryear have strong parallels today, but there are important differences, too. While prices at the gas pump seem high, the current price of crude oil is nearly 50% lower than the inflation-adjusted \$80 per barrel peak seen in the early 1970s. Similarly, though some food costs are rising rapidly – witness the recent 14% hike for your morning cup of Folgers – overall commodity food prices have moderated from the highs set last Spring. And the defense budget, which approached 10% of GDP during the Vietnam era, is less than 5% of total GDP today, according to the Federal Reserve. What's more, we've got a president who is staunchly opposed to price controls of any sort, in sharp contrast to the Carter administration and its mistaken economic policies that led to rampant **stagflation**.

So while we're not overly concerned about an economically induced flashback to the 1970s, we recognize that the stock market, like fashion, is fickle. If short-term speculators believe we are due for a period of stagflation, they will don their bell-bottoms and adjust their portfolios accordingly, creating opportunities for those with a somewhat longer point of view. And though we expect the markets to become increasingly volatile, the realities we discussed in our last letter – healthier corporate balance sheets, rising earnings, and **merger-related activity** – have not been diminished, and bode well for the future.

As you probably know, most of our growth as a firm has come through referrals. If you have an associate, relative or friend who might benefit from our services, we'd love to chat with them. We appreciate the confidence expressed by your relationship with WealthTrust•FBB and look forward to serving all of your investment needs.

Wishing you wealth and prosperity in the New Year,

Mitch Schlesinger
Managing Director

P.S. Just a reminder that our Bethesda office has moved. If you will be visiting the office and need directions, please don't hesitate to call.