



Thought for the Week: Monday, September 5th, 2011

Labor to have its Day?

Corporations have been reporting record profit margins, a fact due, in part, to the single minded manner in which salary costs have been cut.

For much of the last thirty or so years, enhanced productivity helped make companies more competitive, thereby increasing both revenues and employment. Now, companies are using productivity to either increase production without increasing labor, or maintain production levels but reduce staff numbers. Either way, profits rise. But clearly, productivity is a double edged sword as far as job creation is concerned.

Therefore, the expression "Jobless Recovery" has become popular as the stock market has risen in line with company profits. In recognition of Labor Day, let's look closer at the employment situation.

Is "Jobless Recovery" an Oxymoron?

Companies are doing most of what they can to maintain the economic recovery by improving their financial performance. The Federal Reserve has reduced short-term interest rates to near-zero levels (long-term rates next???) and the Government tells us it's doing all it can, pending the Presidential speech later this week.

Problem is - unemployment stays stubbornly high.

The issue is therefore simple: Unless employment improves there can be little confidence that an economic recovery will be sustained. Sure, selected monthly or quarterly figures, such as consumer sentiment, can periodically impress markets, but the current "Jekyll & Hyde" volatility will probably continue until the regular jobs numbers show signs of improvement.

The phrase "Sustained Recovery" therefore appears to be mutually exclusive with the word "Jobless."

Why is Employment Important to the Economy?

Employment is seen as a leading indicator for the economy and many markets as increasing employment generally leads to economic expansion. In most industries, you need more people to produce more, ignoring the effects of productivity.

Sure company profits can increase but for how long if people are not working? Consumer spending may have a few healthy periods, but forward looking markets will not be optimistic for long because low employment means low consumer spending. The bulk of consumer spending comes from employed consumers.

Consumer Spending is a substantial component of the U.S. economy; possibly the largest component. The more consumers in gainful employment, the higher consumer spending should be.

Once employment picks up, economists will feel more confident that better economic and consumer times consistently lay ahead.

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COMPREHENSIVE WEALTH MANAGEMENT

Jobs & Manufacturing – Not what you would Expect

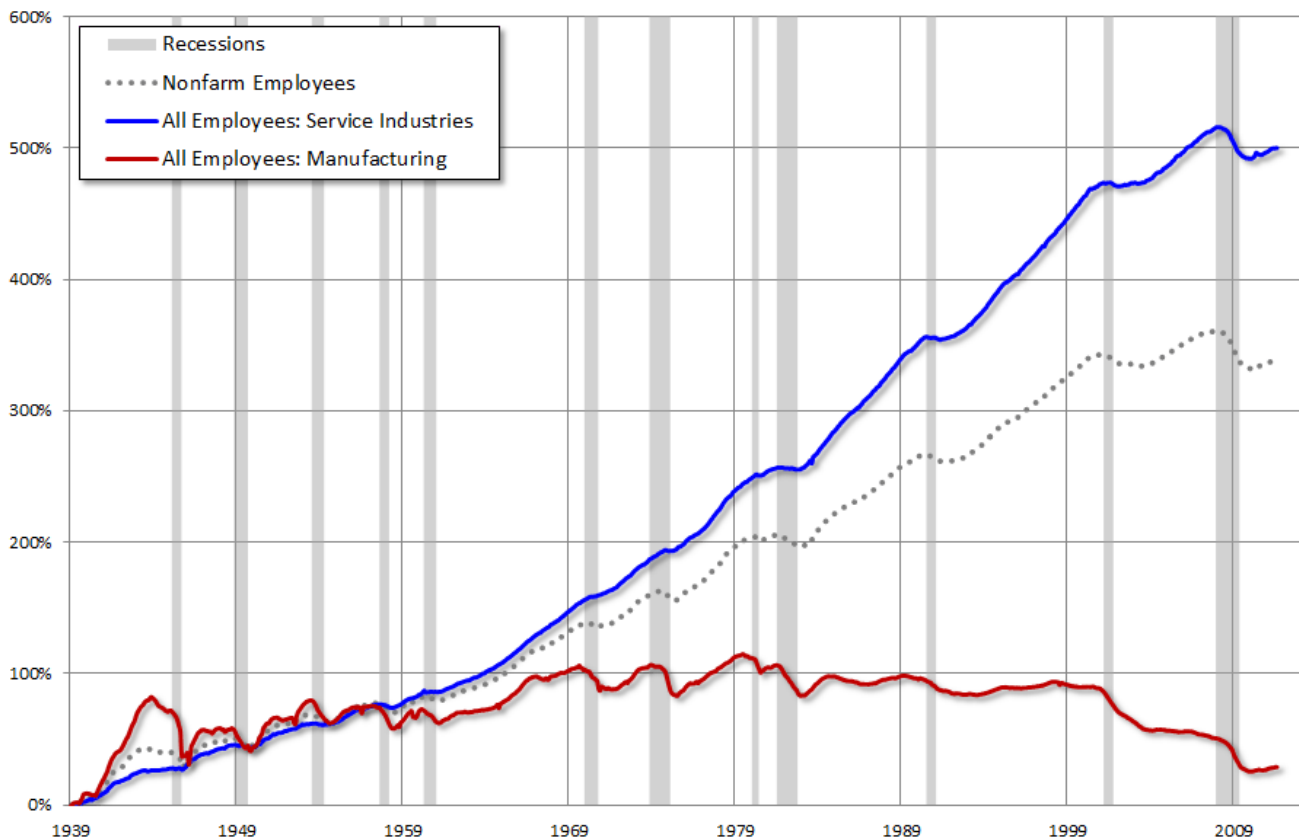
Raise your hand if you are expecting the renaissance in U.S. manufacturing companies to lead the wholesale reduction in unemployment, especially those companies that export to Emerging markets. It could happen but we also know that for every domestic job they create, more may be created overseas.

Maybe you are looking to the Government's infrastructure spending to dig us out of the jobs hole?

Companies and the Government definitely have a role to play in increasing employment, but look at the chart below showing the cumulative employment growth since 1939.

Employment Growth Since 1939 Service Industries versus Manufacturing

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Look at what happens after each recession – do you see manufacturing employment picking up? Not really. What we see with manufacturing employment is recessions being used as a reason to shed labor but rarely since 1980 does the level of employment rebound after the recession.

The same is not true for Service Industries. This is where post-recession employment is created. As productivity increases, jobs get relocated from Manufacturing Industries to Service Industries.

The recent recession was the first time Service employment fell markedly.

Although Manufacturing employment peaked in 1979, the decline has accelerated since 2001.

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Some Final Thoughts...

The U.S. is the most competitive country in the world; its companies dominate world trade, no matter what you think of the dollar.

We produce highly educated workers who work in highly profitable companies.

Its future depends on service employment not manufacturing where overseas competition and productivity probably means we will be uncompetitive for the foreseeable future.

The obvious area to apply job creating stimulus is the service industries, if the jobs are to have a good chance of becoming sustainable. This generally means smaller businesses and those who find it easier to transport their products and services overseas.

Service Industry:

An industry made up of companies that primarily earn revenue through providing intangible products and services. Examples include: finance, retail, transport, distribution and food services.

Manufacturing Industry:

Manufacturing industry refers to any business that transforms raw materials into finished or semi-finished goods using machines, tools and labor. Manufacturers include food production, chemicals, textiles, machines and equipment.

We believe strongly in the U.S. Manufacturing Renaissance as a place to invest, especially for those companies who export 40% or more of their products to emerging markets. However, the hard and soft data suggests a continued recovery in this sector will not generate a recovery in U.S. domestic employment rates. Profit growth and the benefits of earning revenues in appreciating non-dollar currencies gets funneled back to the U.S. in most cases; unfortunately, jobs are often created in the regions where the products end up, or where cost benefits exist.

Finally, the Financial sector of the Services industry is very important for job creation. A strong economy and a strong job market historically require a strong financial sector.

These are some of the macro economic issues we look at with regard to the prospects for employment, and therefore sustained economic growth.