



DOUCET ASSET MANAGEMENT, LLC

**Quarterly Newsletter**  
**Q1 2010**

DOUCET VALUE MOMENTUM PORTFOLIO  
DOUCET VALUE INCOME PORTFOLIO  
DOUCET MANAGED PORTFOLIO  
BIENVILLE MODEL

**January 2010**

***“Doubt is not a pleasant condition...but certainty is an absurd one.”***

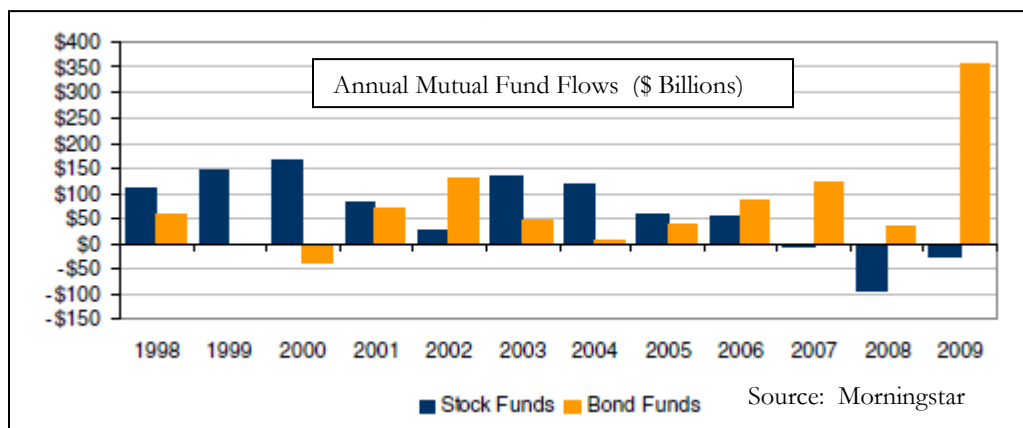
Voltaire, in a letter to Fredrick the Great in 1767

The “Great Recession” of the past two and a half years dealt a devastating blow to the healthy glow of American optimism and blinded it with visions of “financial Armageddon.” More airtime is dedicated to the conspiracy theories surrounding the S&P’s 70% rise over the past 10 months than the indexes negative 24% return (ex-dividends) over the past 10 years! Lost in the shuffle – improving corporate balance sheets, stabilizing unemployment rates, earnings exceeding expectations and improving confidence...in case you were wondering, this is what a recovery looks like. Hushed inflection points like these are easily missed given the cacophonous roars devoted to topics such as the surge of U.S. government debt levels and out-of-control spending, the potential impact of the recently wounded healthcare bill, the implications of the Massachusetts Senatorial race and the girlfriends of Tiger Woods. What is not missing from the investor’s mindset is a healthy dose of doubt and a plethora of questions created by the “new normal.” Thus, our focus this quarter is answering questions we have heard from many of you, and hopefully, to separate the numbers from the noise and fact from fiction.

**Are the Equity Markets Overvalued and Poised for Another Major Correction?**

While it is absurd to believe the markets efficiently price all current economic data immediately, it is equally incongruous to assume the market is never right. In the last century, a recovery in stock prices has preceded a resurgence in the overall economy in all previous recessions. An overlooked fact is despite its meteoric rise, the S&P 500 just recorded its worst performance for a decade since the 1930s. In contrast, bonds delivered above-average performance during the same period, recording a 7.1% compounded annualized return *relative* to stocks, the largest outperformance on record. There have only been two previous decades in which bonds have outperformed stocks: the 1930s and the 1970s. In both instances, stocks outpaced bonds in the following two decades by an average of 10%.

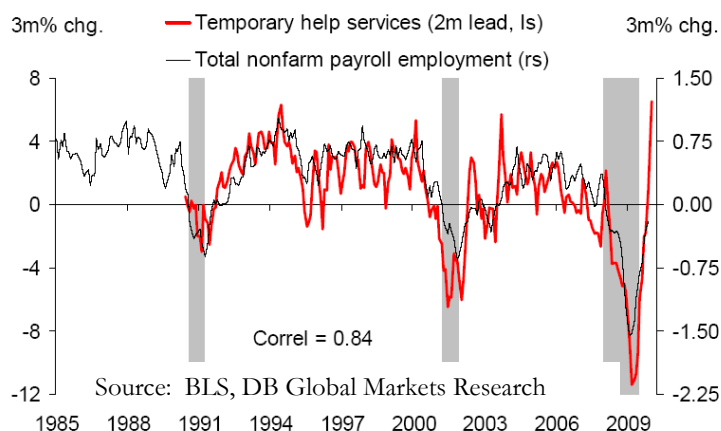
This decade long debacle for equities helped feed a high level of market skepticism and hastened the exodus from domestic equity mutual funds in 2009. While cash levels remain elevated (\$3.3 trillion) versus historical levels, the Investment Company Institute reports U.S. equity mutual funds saw outflows of \$40.3 billion in 2009 while investors plowed \$357 billion into fixed-income funds. Based on these numbers, it certainly does not appear investors are aggressively buying equities.



“Talking heads” and market pundits alike claim how expensive the market is based on historically high price-to-earnings (P/E) ratios. The problem with this logic is the “E” in the “P/E” has been muted much of the past eighteen months; it even went negative in Q4 2008. Bloomberg data show earnings for companies in the S&P 500 declined a whopping 40% in 2008 alone from 2007. Despite this fact, stocks are currently trading at about 18.5 times trailing 12-months earnings (TTM) – based on Q409 analyst estimates – and about 14 times 2010’s *cautious* analyst estimates. As a comparison, since 1926, the long term average P/E for the S&P 500 is 16.3 times. Additionally, the S&P is currently trading at about a 2.18 times Price-to-Book ratio versus its 31-year average of 2.41 times (Ned Davis Research). So while not “cheap” like levels were 10 months ago, stocks are certainly not expensive based on historical averages for common measures.

### Are Unemployment Numbers Going to Improve in 2010?

According to the Bureau of Labor Statistics December employment report, true unemployment in the United States is approximately 17% of the labor force, which equates to 25 million people who are without jobs or who are significantly *underemployed*. While official government statistics show unemployment leveling off at around 10% over the past three months, there is at least one sign that the employment ranks may be in the incipient stages of a recovery. Temporary workers have seen employment gains three months in a row with a gain of 47,000 jobs in the most recent month. The hiring and firing of temporary workers is typically seen as a leading indicator in employments trends since temps are typically the first to be downsized in a weak economy, and the first to be hired in a recovery.



Another hopeful sign for the unemployed can be seen in an analysis of the last 7 recessions. History shows that unemployment usually peaks 4 to 7 months after the stock market bottoms. Using the 6 previous recessions over the past 40 years as a guide, unemployment may have peaked in October. However, one major exception existed in the early 1990s when unemployment did not peak until 20 months after the October 1990 stock market bottom. The obvious fact that stands out about this period is it corresponds with a real estate crash and the Savings & Loan crisis.

Number of Months between a Low in the S&P 500 Index and a Peak in the Unemployment Rate			
Date of Recession	Date of Market Low	Unemployment Peaked	Total Months
Dec 2007 - ?	Mar 2009		?
Mar 2001 - Nov 2001	Oct 2001	Apr 2002	6
Jul 1990 - Mar 1991	Oct 1990	Jun 1992	20
Jul 1981 - Nov 1982	Jul 1982	Nov 1982	4
Jan 1980 - Jul 1980	Mar 1980	Jul 1980	4
Nov 1973 - Mar 1975	Oct 1974	May 1975	5
Dec 1969 - Nov 1970	May 1970	Dec 1970	7

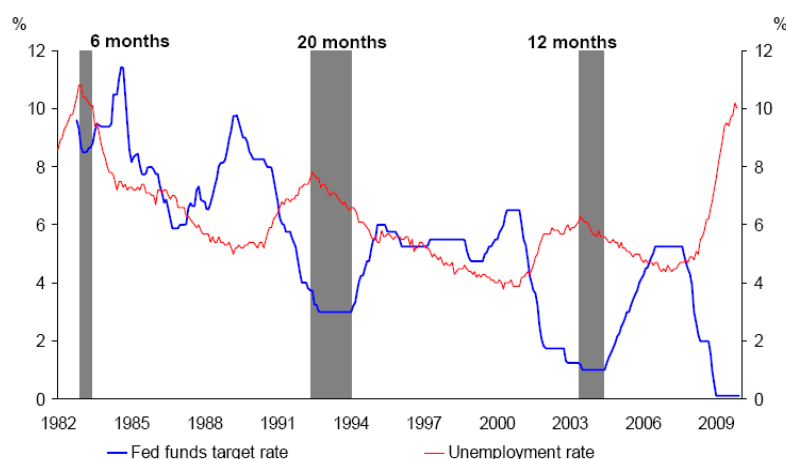
Sources: Bloomberg, Wallstreet Journal, Yahoo Finance

According to the National Association of Housing Builders (NAHB), the housing industry directly contributes 18% to the nation's GDP and indirectly, may contribute as much as one-third of the nation's GDP. Much like the early 90s, unemployment will likely remain stubbornly high until both real and "shadow" inventory of single family homes is absorbed by the market, allowing housing-related jobs to return.

### When Will Interest Rates Start to Rise?

While economic data no longer supports the emergency level of zero percent interest rates, there are several obvious reasons the Fed will "hold" down short-term rates as long as possible. Chief among reasons is the government itself is benefiting from low interest costs despite surging debt levels. Net interest costs paid on the public debt declined from \$260 billion in 2008 to \$199 billion in 2009, or \$61 billion, due to lower interest rates (Congressional Budget Office Monthly Budget Review, September 2009) despite issuing \$2.1 trillion worth of bonds last year. According to Deutsche Bank, 2009's total was 3.5 times the amount typically issued in a year. The Treasury is projected to issue \$2.6 trillion in 2010. At some point, the bond market demands higher yields for any further purchases. Yet, as evidenced by recent auctions, Treasuries are still being absorbed.

Historically, the Federal Reserve waited until well after unemployment rates started to fall before beginning to tighten credit. So if one assumes October was the unemployment peak, the earliest one would logically expect the Fed to begin raising rates would be in April. It is unlikely, however, that the Fed raises rates substantially without evidence that unemployment is trending downward.



Source: BLS, DB Global Markets Research

### Is There Any Good News in the Economy?

We monitor 58 economic indicators and of these indicator, 51 have shown year-over-year improvement and, for the most part, the others have at least stopped getting worse. Consider the following:

- Q309 GDP expanded by 2.2%, an improvement of 8.6% in just two quarters. (U.S. Dept of Commerce)
- According to the Chicago Purchasing Managers, the best gains in nearly four years were registered for business activity, production, new orders, and even employment.
- The ISM Manufacturing Index recorded its fifth straight month of expansion in U.S. manufacturing, and the fastest pace of expansion in more than three years.
- Business inventories increased in October by 0.4%, first time since 2008. (U.S. Dept of Commerce) Once the inventory liquidation comes to an end, inventory rebuilding will contribute further to GDP growth.
- In Q309, non-farm productivity increased by 8.1% from Q2, after already increasing 6.9% in Q2 (over Q1). Productivity is now at the highest level since 2003. (U.S. Dept of Labor)
- Corporate cash also could provide ballast for the stock market. American corporations slashed capital spending by 16% in 2008 and another 32% in 2009. As a result, cash now makes up 9.7% of their assets, well above the historical norm near 6.2%. (Barron's, Dec. 21, 2009)
- According to credit-insurance firm Euler Hermes ACI (an Allianz unit), business bankruptcy filings actually fell in Q309 from the previous quarter, marking the first quarterly decline since 2006.

### 2010 Census

As mandated by the Constitution, a census has been taken by the government every 10 years since 1970 in an effort to count every living person in the United States, both citizens and non citizens. According to USA Today, 3.8 million Census workers will be hired this year. The hiring binge will add jobs lasting a week to two years in length. At the height of this temporary hiring, the unemployment rate could decline up to 2.4% (based on a total of 157.5 million total U.S. labor force (Bureau of Labor Statistics)).

## What Is the Most Daunting Problem the Market Is Currently Facing?

The rapidly expanding level of U.S. government spending and debt is destroying the US Dollar and could be a hindrance to future economic growth. Based on the government's own first fiscal quarter budget review, the U.S. is on pace to spend \$3.5 trillion in 2010 and collect only \$1.96 trillion in taxes. That's not just overspending, that is spending 179% of total income! America is becoming so debt-laden I have been referring to it as "Argentina Light." Congressional leaders desperately need to read a book on economic history, as no great society has survived this pattern of behavior. At some point, our country pays "credit card-like" interest on their "credit card-like" borrowing unless real change actually occurs.

<b>BUDGET TOTALS THROUGH DECEMBER</b>			
<b>(Billions of dollars)</b>			
	<b>Actual FY 2009</b>	<b>Preliminary FY 2010</b>	<b>Estimated Change</b>
Receipts	547	489	-59
Outlays	880	877	-3
Deficit (-)	-332	-389	-56

Sources: Department of the Treasury; CBO.

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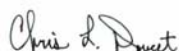
## Conclusion

Today's investment landscape reminds me of a story about the deadliest month in American history. Contrary to most guesses, this ominous of all months did not occur during the Civil War or World War II, but was in October of 1918. In that month alone, 195,000 U.S. citizens died of influenza. The then U.S. Surgeon General Vaughan stated: "If the epidemic continues its mathematical rate of acceleration, civilization could easily disappear in a matter of weeks." But almost as mysteriously as the plague appeared, the epidemic vanished. Within a few weeks, Americans were back in the streets celebrating victory in Europe and end of WWI. Interestingly, a vaccine was never developed and questions about the basis of its pathogenicity are still largely unanswered. The disease simply ran its course. Likewise, this crisis too will give way and business will quietly begin again.

## Firm News

Happy Wedding Anniversary to Roland and Esther Doucet. Congratulations on celebrating 49 years of marriage.

Sincerely,



Chris L. Doucet  
Chief Executive Officer

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- Form ADV: Please contact us at (205) 414-9788 to receive a current copy of our Form ADV II or the Schedule H Brochure.
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