THE TYCOON REPORT

# >: Wall Street's Contempt for the Individual Investor

*Monday, December 17, 2007 | Ben Schott*

Before I get into my rant for today, allow me to make a preemptive digression:

***What makes an investing newsletter valuable to its readers?***

In my opinion, it?s the ability to translate investing expertise into actionable advice in the context of current events.

That?s a fancy way of saying ?Take what?s hot in the world of investing news and help people make money from it.?

Like Chris Rowe?s article from last week
, in which he broke down all the buzz about CitiGroup and showed you how to make a decision about investing in the stock (or not) right now, today.

Or Teeka Tiwari?s article
, in which he put all the talk about a potential U.S. recession into perspective, and told you how he would play it within his investing framework.

Or Dylan's article , the latest in a "mini-series" on the mortgage meltdown that breaks down implications for the average homeowner and investor.

And there was Jason Jovine?s article
, in which he took some of the biggest news of the week ? the Fed cutting interest rates ? and explained how a professional investor figures interest rates into his or her investing model.

This isn?t to say that we?ve got it clocked, but I am proud of the fact that, if I put myself in the shoes of a typical investor, I would say that *The Tycoon Report* is delivering some extremely valuable content and putting some of the biggest news of the day into a context that can help me make better investing decisions.

**Now, On To The Point ...**

Normally, our approach has more to do with the ?how? of investing than it does with the ?why.? Also, we typically see our role as that of ?teacher? to ?student.?

That being said, I?m going to flip the script today talk a bit about why we invest, and I?m also going to ask YOU to educate ME.

It all starts with my building level of frustration with the process of starting a college savings plan for my 2-year-old daughter.

My dream, you see, is that Hannah will turn out to be a lot smarter than I was in high school, and that she?ll win a full academic scholarship to Harvard or Yale. But on the off chance that she doesn?t pull that off, I?m truly petrified by how much a quality college education is going to cost by the time she comes of age.

So there I found myself, with a little bit of money earmarked to start her college fund, and I started researching my choices.

Very quickly, I determined that a 529 plan was the way to go. The tax advantages, combined with the somewhat relaxed rules about how the money can be spent down the road, make it an obvious choice for me.

That being said, there is one thing that?s stopped me ? so far ? from actually opening an account:

Unless I?m mistaken, there?s no such thing as a self-directed 529 plan!

I?ve looked at more than 20 different plans offered by the major brokerages and financial planning providers, and everywhere I look it?s the same thing ...

These plans that I?ve seen only allow you to choose from a very small selection of mutual funds, just like the ancient 401(k) plans of old.

Some consider themselves cutting edge, offering ?age based? portfolio options that allow you to invest in more ?risky? funds when your child is younger, and move on to more ?stable? funds as he or she gets closer to college age. Wow, that?s deep.

Nowhere have I seen a plan that would allow me to invest my daughter?s college funds as I see fit as an investor and a parent. I can?t invest in

individual stocks.  I can?t put money into my favorite ETFs.  Forget trading options with this money.

I don?t know about you, but I find this supremely insulting.

My take on it is that the financial establishment, along with the state bureaucracies that run these 529 plans, essentially have the attitude that the next generation?s college money is far too important to be entrusted to their parents.

To me, that reeks of Wall Street?s contempt for the ?Regular Joe or Jane? investor out there.

So I have a few questions for you today about this ...

1. Has my research been incomplete?  Have you run up against the same problem and found a plan that is not so restrictive?

2. Do you think the plan sponsors are correct in limiting the investment choices in 529 plans to a few options selected and run by professionals?

3. Would you trust yourself to make specific investment decisions with your child?s college money?  (A related question: do you trust a complete stranger more?)

OK.  Rant over.  But it really gets me going every time I feel like individual investors are being insulted, patronized, or condescended to.

I very much look forward to hearing your thoughtson the topic.

Ben Schott
Chief Investment Officer
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**Tuesday, December 18**

*8:30 - Housing Starts (for November): Consensus 1190K, Building Permits (for November): Consensus 1150K*

Big Picture: Housing starts reached a 15-year low in September with no sign of the fundamentals (housing demand) needed to turn the direction over the intermediate term.  The plunge has been a large drag on economic growth, as further risk surrounds the defaults coming from sub-prime and other mortgage borrowers.  The upturn could be a long way off -- mid/late 2008 may be optimistic.  The correction for the inflated housing market was expected (and needed), but with a more moderate decline.  Stability will have to wait for new home sales to begin to tick higher and a smaller supply of unsold inventory.  Continued lending to low-risk mortgage borrowers is needed just to get the declines to decelerate.

Implications: Housing Starts are a measure of the number of residential units on which construction is begun each month.  A start in construction is defined as the beginning of excavation of the foundation for the building and is comprised primarily of residential housing.  Building permits are permits taken out in order to allow excavation.  An increase in building permits and starts usually occurs a few months after a reduction in

mortgage rates.  Permits lead starts, but permits are not required in all regions of the country, and the level of permits therefore tends to be less than the level of starts over time.

**Thursday, December 20**

*8:30 - GDP-Final (for Q3): Consensus 4.9%, Chain Deflator-Final (for Q3): Consensus 0.9%*

Big Picture: Q3 leaves the last four quarters with average growth of 2.8% as the Fed targets sub 'potential' growth (3%) to cool inflation pressures.  The risks for slower growth have been offset by the resilient economy to date.  The forward risks have increased dramatically with the mortgage credit crisis and the housing sector slipping into deeper recession.  Oil prices are weighing on consumers, as the labor market is showing some cracks.  Consumer spending will provide support given full employment and strong income growth, but will show weaker growth in the coming quarters.  Inventories will pull back in Q4 as global growth remains a positive given the weak dollar and the pace of exports.  Q4 will test just how resilient the economy is given all the headwinds.

Implications: Gross Domestic Product (GDP) is the the broadest measure of economic activity.  Annualized quarterly percent changes in GDP reflect the growth rate of total economic output.  The figures can be quite volatile from quarter to quarter.  Inventory and net export swings in particular can produce significant volatility in GDP.  The final sales figure, which excludes inventories, can sometimes be helpful in identifying underlying growth trends as inventories represent unsold goods, and a large inventory increase will boost GDP but might be indicative of weakness rather than strength.  The broad components of GDP are: consumption, investment, net exports, government purchases, and inventories.  Consumption is by far the largest component, totaling roughly 2/3rds of GDP.  In addition to the GDP figures, there are GDP deflators, which measure the change in prices in total GDP and for each component.  Though the consumer price index is a more closely watched inflation indicator, the GDP deflator is another key inflation measure.  Unlike CPI, it has the advantage of not being a fixed basket of goods and services, so that changes in consumption patterns or the introduction of new goods and services will be reflected in the deflator.

*8:30 - Initial Claims (for 12/15): Consensus NA*

Big Picture: Weekly initial claims can be volatile, as recent movement reflects increased loosening in the labor market.  Layoffs (seen in initial claims) have been rising and reached above 350K in late November while hiring (seen in continued claims) showed a sharp rise to leave the largest levels in two years.  Claims provide a nearly real time read on layoffs and the labor market as the unemployment rate reflects the broader combined read of layoffs and hiring.  The 350K for claims is worrisome as a 360 K level for the four-week average has been consistent with recession.

Implications: Initial jobless claims measure the number of filings for state jobless benefits.  This report provides a timely, but often misleading, indicator of the direction of the economy, with increases (decreases) in claims potential signaling slowing (accelerating) job growth.  On a week-to-week basis, claims are quite volatile, and many analysts therefore track a four-week moving average to get a better sense of the underlying trend.  It typically takes a sustained move of at least 30K in claims to signal a meaningful change in job growth.

*10:00 - Leading Indicators (for November): Consensus 0.1%*

Big Picture: Six monthly declines in 2006 reflect the weaker economy last year, as do the six declines over the first 10 months of 2007. The six-month growth is -0.5% as the last three-month string of declines was back in 2001. Over the last 17 years, the index correctly signaled the 1990 and 2001 recessions while providing a false signal during the 1995 soft-landing. The recession alarms go off when the cumulative six-month decline exceeds -1% or a string of three or more consecutive monthly declines. No recession warning bells yet.

Implications: The Leading Indicators report is, for the most part, a compendium of previously announced economic indicators: new orders, jobless claims, money supply, average workweek, building permits, and stock prices. Therefore, the report is extremely predictable and of very little interest to the market. Though this series does have some predictive qualities, it is a common criticism that it has predicted "nine of the last six" recessions.

*12:00 - Philadelphia Fed (for December): Consensus 8.0*

Big Picture: The regional manufacturing index is volatile but tracks the direction of national orders and production. The gains in orders and shipments follow the late 2006 stall tied to autos, housing and business investment. Late 2007 risk is tied to another potential stall in business investment given economic growth concerns and financing rates. The Philly index is independent of its components so can provide a misleading read and is especially volatile given the small region covered (mid and eastern PA, southern NJ and Delaware). The manufacturing sector moves in mini-cycles compared to the overall economy, and the regional measures move in even shorter cycles with far more month-to-month volatility.

Implications: There are many regional manufacturing surveys, and they tend to be ranked in order of timeliness and the importance of the region. The Philadelphia Fed's survey is first each month, actually coming out during the third week of the month for which it is reporting. Several smaller surveys are then released before the Chicago purchasing managers' report on the last day of each month. A few, such as the Atlanta and Richmond Fed surveys, are released after the NAPM and are of little value. The purchasing managers' reports are measured like the national NAPM -- 50% marks the breakeven line between an expanding and contracting manufacturing sector. For the Philadelphia and Atlanta Fed indexes, 0 is the breakeven mark.

**Friday, December 21**

*8:30 - Personal Income (for November): Consensus 0.5%, Personal Spending (for November): Consensus 0.5%, Core PCE Inflation (for November): Consensus 0.2%*

Big Picture: Consumer spending is slowing gradually given the drags from energy prices and home prices. However, the relatively strong 5.4% yoy pace is owed to the 6% annual pace of income growth supported by strong employment and wages gains. The Fed's favored core PCE price index stands at 1.9% yoy -- within the Fed's central expectation range through 2010. The fundamentals of consumer spending still remain strong but rising layoffs (initial claims) provides a risk to income and spending and the economy.

Implications: Personal income measures income from all sources. The largest component of total income is wages and salaries, a figure which can be estimated using payrolls and earnings data from the employment report. Beyond that, there are many other categories of income, including rental income, government subsidy payments, interest income, and dividend income. Personal income is a decent indicator of future consumer demand, but it is not perfect. Recessions usually occur when consumers stop spending, which then drives down income growth. Looking solely at income growth, one may therefore miss the turning point when consumers stop spending. The income report also includes a section covering personal consumption expenditures, also known as PCE. PCE is comprised of three categories: durables, nondurables, and services. The retail sales report will provide a good read on durable and nondurable consumption, while service purchases tend to grow at a fairly steady pace, making this a relatively predictable report, and ranking it well below retail sales in terms of market importance.

*10:00 - Mich. Sentiment-Rev. (for December): Consensus 74.3*

Big Picture: The push to a two-year high in January was largely tied to the drop in gasoline prices. The housing recession, troubled financial markets and rising energy prices since January has pushed the index down 23% to the lowest level since the 13-year low during the October 2005 Gulf Coast hurricane. The index is below the low point during the 2001 recession. The University of Michigan survey is significantly smaller (500 phone calls, just 250 in preliminary) than the Conference Board's, includes a longer outlook (for expectations) as questions are focused on the household compared to the business heavy CB survey. The index far better tracks the consumers' mood than spending habits better indicated through interest rates and income growth.

Implications: The Michigan index is almost identical to the Conference Board Consumer Confidence index, though there are two monthly releases, a preliminary and final reading. Like the Conference Board index, it has two subindexes -- expectations and current conditions. The expectations index is a component of the Conference Board's Leading Indicators index.

Source: www.Briefing.com