JPS Global Investments—The Quarter in Review

Volume 1, Issue 4. January 2008

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## Market Summary

The markets in the fourth quarter reinforced the theme of 2007: volatility and uncertainty. The trouble that began in the housing market with subprime mortgage-backed securities, has affected all credit markets and the economy in general. Credit is the fuel of the economy and banks are currently unwilling or unable to extend sufficient credit. The Dow Jones Industrial Average (DJIA) and The S&P 500 Index suffered their first fourth-quarter decline in 10 years and seven years respectively. Despite all that, The DJIA was up 6.4% for the year and the S&P was higher by 3.5%.

**Oil and Inflation.** Oil is close to $100 a barrel and was only $10 a barrel about a decade ago. That is not a good thing. Along with oil, many other commodities such as gold and corn are setting record prices. Ultimately, these price increases and a weakening dollar could lead to inflation. If this materializes, the Federal Reserve will become less willing to help the economy by cutting interest rates, as that can fuel inflation.

**The American Consumer** is a three-legged creature that has been able to stay in the race, but is at risk of finally losing its balance. There are three sources from which the consumer can derive money to keep spending: net worth (think "home"), credit cards, and paychecks. The first two sources are being constrained presently.

According to a December 7th Wall Street Journal article (Phillips, Ng, McKinnon), home prices nationwide are still at about 4.5 times household income. The long term average price of homes, from 1976 – 2006 has been approximately 3.5 times household income. This means, that if the home prices were to revert back to their long-term average, home prices will need to come down an additional 20%. That number would be higher in states like California and Florida. It is therefore not likely that the consumer is going to be able to use his or her house as an ATM machine in the foreseeable future.

With regards to credit cards, things are not looking too good either. Credit card default rates have been rising and banks are becoming less eager to lend in general, as a result of the continuing credit crunch. So the only leg that the consumer has left to stand on is the job market. Many economists and Wall Street folk will be paying close attention to the upcoming job market reports. Any signs of weakness have the potential to spook the markets, especially since the consumer represents 70% of our Gross Domestic Product.

**To the Rescue: The World Economy**. What has helped the U.S. Economy stay afloat are the strong economies else where, including Asia, parts of Europe, the Middle East, and Brazil. The dollar is down 9.6% on the euro for the year and this has been a boon to export oriented U.S companies, as well as large U.S. multinationals that are earning more valuable currencies in their overseas markets.

If the global economy remains robust in 2008, we may yet avoid a recession. Now that the "R" word is out of the bag, I should clarify where I stand on that issue. Economist on average are placing the likelihood of a recession at about 50/50. This is similar to the weather forecast: it either rains or it doesn't; there is no 50/50. I am holding on to my umbrella, just in case.

**Sustainable Investing Update**

**A Changing Climate for Shipping.** Cars take the spotlight in the discussion of green house gas emissions in transportation. This is not so surprising, considering their visibility and the prominent role they play in our daily lives. A type of transportation that has received little attention in the climate change debate, however, is the global shipping industry. This industry is a very significant source of greenhouse gasses. Ships carry over 90% of global goods by volume. Moreover, this volume has tripled since 1970.

A study conducted by the International Council on Clean Transportation concluded that ships release more sulfur dioxide than the entire global fleet of cars, trucks, and buses combined and an estimated 27% of global nitrogen oxide emissions. If the shipping industry were a country, it would rank number seven, in terms of total greenhouse gas emissions. The problem is bunker fuel, a tar like sludge by-product of the petroleum refining process. This is the main fuel used in shipping.

The market place is screaming for a solution and the companies that will provide it, will stand to prosperous handsomely. Here are some early possible solutions: Wallenius Wilhelmsen Logistics wants to use solar, wave, and wind energy to power ships on their voyage. Another company, SkySails, is developing large para-sails that can reduce a ship's fuel cost by 35%, with the first application to launch in December. The sky is clearly the limit here.

**Energy Legislation.** If it weren't for the well-publicized writers' strike in Los Angeles, one may have suspected that the talks in Bali were scripted by Hollywood. Chief U.N. negotiator Yvo de Boer broke down in tears and had to be led off the stage by his colleagues. The U.N. ambassador of Papua New Guinea received a thundering applause when he told the U.S. delegation "If you're not going to lead...please get out the way."

Then, in a classic EU vs. US battle, Paula Dobriansky, the chief U.S. negotiator, was booed for raising concerns on the issue of more funding and assistance for developing countries to acquire clean technology. As icing on the cake, Al Gore took the stage decrying his own country's lack of leadership on the issue of climate change. In the end, though short of agreeing to mandatory pollution limits, the U.S. decided to participate and sign the accord, which is to work out a post-Kyoto deal.

Back in Washington, the Energy Bill was signed into law. On the positive side, the bill will increase fuel economy standards to an average of 35 miles per gallon and the incandescent light bulb will be phased out. Now, 35 miles per gallon does not equate to setting the bar very high.

Currently, Europe and Japan are over 40 mpg already and are requiring efficiency levels in the high 40s by 2012 and 2015 respectively. China is looking for 35 mpg in 2009. Our promise of 35 mpg by 2020 is akin to a kindergartener promising to learn his ABCs by the time he enters 6th grade. It's a start, but we need to be more ambitious.

Unfortunately, major oil companies were also big winners and managed to hold on to their $9.4 billion worth of tax incentives over the next 10 years. Renewable energy suppliers were supposed to have been the beneficiaries of the oil tax incentives. Furthermore, they lost the provision in the Energy Bill that would have required utilities to purchase up to 15% of their electricity from renewable energy. On balance, the law does not come close to addressing the energy challenges we face, but it's a start and probably as much as can be expected under the current administration.

**Wall Street's Green Street.** Green has become Wall Street's darling. Going green is increasingly being viewed by the world's financial thinkers as a tremendous opportunity to earn some of the old-fashioned "green." According to data from the National Venture Capital Association and Thomson Financial, U.S. venture investments in green companies in the first 9 months of 2007 totaled $2.6 billion, compared to $1.8 billion for all of 2006.

On the carbon trading side, Nymex and a group of Wall Street trading firms are planning an exchange to trade carbon credits. This new platform will compete with the Chicago Climate Exchange, which is trading approximately 600 million tons of annual emissions at present. Some banks are also seeing the green in green by getting directly involved in carbon credit projects, rather than just being the middlemen in trading the credits. Barclays, Dresdner Kleinwort, and Morgan Stanley are all traveling the planet, financing hydro dams and wind farms.

Traditional power companies are also in on the action. Recently, Iberdrola, SA, a Spanish power company, spun off its renewable energy assets in an IPO as Iberdrola Renovables. The IPO raised $6 billion and gave the company a market value of over €22 billion. Clearly, Iberdrola believed its green assets had a premium value that was not being recognized as long as the assets resided on the balance sheet of a traditional power company.

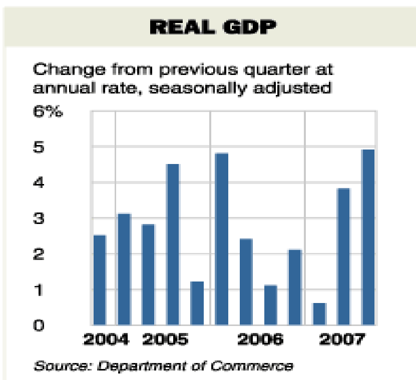
**Ethanol Craze(y)**. When it comes to alternative fuels and other clean tech solutions, it is important to keep in mind that not all ideas are good ideas, particularly if the federal government is behind them. A year ago, the Bush administration, Main Street, and Wall Street were all in love with corn ethanol on the grounds of energy independence and the environment. Now, it is thought by many, including the Organization for Economic Development and Cooperation, that the cure is worse than the disease.

The price of corn is up; the price of ethanol is not. Ethanol producers are getting squeezed, higher corn prices are a risk to food security in countries that import corn, and the environmental benefits may be a wash at best. Recently, two of the biggest ethanol producers, VeraSun Energy and US BioEnergy, announced their intent to merge. Further consolidation is likely as the industry struggles to return to profitability. Cellulosic ethanol, in my view, holds a bigger promise as it does not compete with the food stock. The advice to investors is to be patient and keep a cool head when pursuing clean tech investments. Not every bandwagon is worth jumping on; especially if it is loaded with corn.

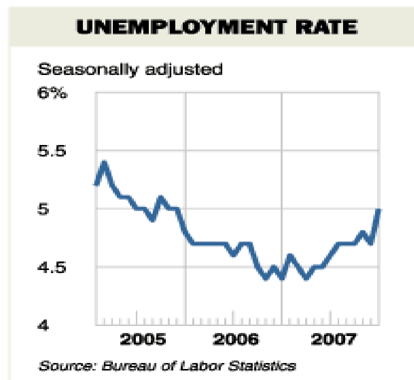
### Financial Markets Data

| Performance as of 9/28/07 | | | | |
|---|---|---|---|---|
| | Qtr | Yr-to-date | 1-yr | 3-yr avg. |
| S&P 500 Index | -3.3% | 5.5% | 5.5% | 8.6% |
| Dow Jones Ind. Avg. | -3.9% | 8.9% | 8.9% | 9.7% |
| NASDAQ | -1.8% | 9.8% | 9.8% | 6.8% |
| Russell 2000 Index | -4.6% | -1.6% | -1.6% | 6.8% |
| Domini 400 Social Index | -3.2% | 3.7% | 3.7% | 6.6% |
| *All returns are Total Return, with the exception of NASDAQ returns, which are Price Return.* | | | | |

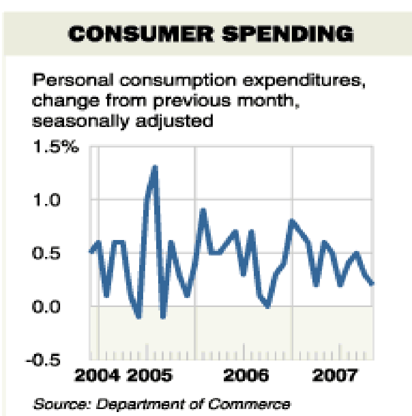
### Economic Indicators



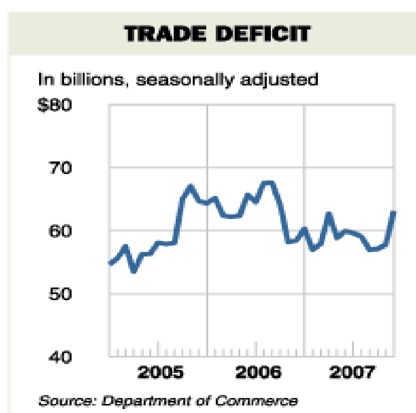

Q3: +4.9%




December: 5.0%




October: +0.2%




November: $63.1 billion

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