Marathon Strategic News

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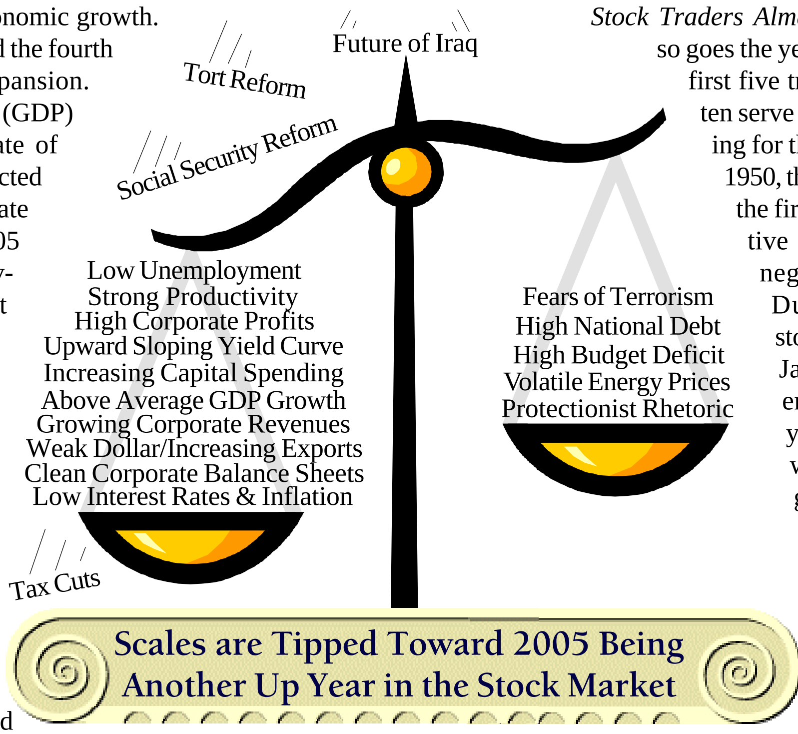
Economic Outlook

The New Year is underway and a strong case can be built for investor optimism. Barring any unforeseen exogenous events such as domestic terrorism, I believe that the uncertainties of 2005 will be small in comparison to those of 2003 or 2004. Last year investors were worried about the uncertainties of the US presidential election, increasing instability in Iraq, increasing price of oil, and domestic terrorism (including heightened fears around the elections). This year, in contrast, the list of investor fears has dwindled to domestic terrorism.

As 2004 came to a close, many economic signs pointed to continued economic growth. The economy has entered the fourth consecutive year of expansion. Gross domestic product (GDP) grew at an estimated rate of 4.5% in 2004 and is expected to continue to grow at a rate of 3.5% to 4.5% in 2005 (GDP has grown by an average 3.3% over the past 50 years).



As we take inventory of the positive and negative factors that may influence our economy over the next few years, I believe that the scales are tilted toward continued strength in the economy and stock market. I believe the main areas of concern are limited to a high but improving budget deficit, volatile energy prices, high national debt, protectionist rhetoric, and fears of terrorism. In contrast, the lengthy list of positive factors that will likely continue to support our economy include: low unemployment (with 2 million jobs created in 2004); very high productivity; record high corporate revenues, profits, and capital spending; an upward sloping yield curve; above average GDP growth; low interest rates; benign inflation; squeaky clean corporate balance sheets; and the possibility of Social Security and tort reform.

It Looks Like Goldie Locks Might Be Back

Our economy appears to be reaching a balanced "sweet spot" where growth and other factors are not too hot, not to cool, but are just right – sustainable for an extended period of time. Last year, the Federal Reserve's confidence in the economy prompted it to begin increasing interest rates toward more normal levels. The Fed increased lending rates five straight times last year from 1.0% to 2.25%. Further, it is widely expected that it will continue to increase rates in 2005 until they neutrally rest around 3.5% - 4.0%. All of these factors bode well for long-term investors in the stock market.

Watch out for Fortune Tellers

Every year investors are subjected to investment prophecies that are based on pure nonsense. During the month of January we chronically hear a claim popularized by the *Stock Traders Almanac* "How goes January, so goes the year." It further claims "The first five trading days of January often serve as an excellent early warning for the year as a whole." Since 1950, the stock market has finished the first week of January in positive territory 34 times and in negative territory 20 times. During the 20 years that stocks fell in the first week of January, the market experienced a loss for the entire year 45% of the time. In other words, if the stock market goes down in the first week of January, then flip a coin and that is what it will do for the rest of the year! Investment advice and insight like this is purely noise and should be uniformly ignored.

Stay Diversified - Do Not Try to Time the Market

Do not be tempted by greed or induced by fear into trying to "time the market" – it is a losing proposition! It is the economic fundamentals that determine the performance of investments over long investment horizons. As I have stated many times before, no one can successfully "time the market." This past year illustrated an important market timing lesson. The stock market slept for the first ten months of the year, and then suddenly shot up by 8% in November and December. Market timers usually miss part or all of these short upward bursts.

The best course of action in both bull and bear markets is to maintain a diversified, long-term, buy-and-hold investment strategy. Overall, I believe that the big picture, long-term outlook for the US economy and stock market is very strong.