

110 Fort Couch Road, Suite 108
Pittsburgh, PA 15241-1030
Phone: 412.851.1400 Fax: 412.851.1403
E-Mail: kfg@kapustafinancial.com
www.kapustafinancial.com



July 20, 2009

The Economy: Where are we headed?

The economy and the banking system are at a real crossroads. Most economic data is still negative although it does appear that certain sectors are beginning to flatten out.

An “official” end to this very severe recession may be in the early stages of occurring. That’s the good news. However, much of the economic news is still troubling. Among the many issues:

- Consumers are still not spending
- Unemployment is at a 26 year high with job losses projected to continue to increase into early 2011
- Foreclosures on homes have risen to historic levels – nearly 2 million in the first six months of this year alone
- Home values have declined substantially – 41% of people who purchased property in the last five years owe more on their mortgages than their homes are currently worth
- State governments are struggling – California and Michigan are broke, and more local governments are facing insolvency every day
- The federal deficit is growing at an alarming rate – more that \$1 trillion in 2009 alone – putting the dollar at risk as the world’s reserve currency

Yes, there will be a recovery in this economy, but almost certainly in a “step-by-step” fashion – not a classic “V” shape – signifying a more rapid recovery. Most of the experts – including the Federal Reserve – are signaling a jobless “slow growth” recovery.

We still don’t have the full picture regarding the government’s master game plan for recovery. Sure, there’s been a brief rally in the stock market, but the truth is the complexities and magnitude of the problem – coupled with the massive amount of government intervention – are still producing great uncertainty.

What about the banking system? The government has been telling us for months that the banking system is “better” and “functioning.” That’s certainly a key ingredient for a recovery, but the challenges for banks continue. The stabilization of the real estate market is tied so closely to an improvement in the banking system. The fact is that few new commercial loans are being made, residential foreclosures continue to climb, and banks still have staggering amounts of bad loans on their books - \$500 billion currently on their balance sheets. And what’s more perplexing is the governments recently announced plan that **does**

not remove the bad loans from their books – making it even more difficult for banks to bounce back.

What's our investment strategy going forward? Patience and discipline. As you know, we don't believe in trying to "time" the markets. We are examining investment opportunities for you – and will be working to increase investments in the equity and bond markets during the remainder of 2009. At the same time, however, our recommendations will be based on what we perceive to be current and ongoing risks.

This is still a very unpredictable economy and we believe we will have a clearer picture of what's ahead for the economy and the markets in the next 30 to 45 days as we receive more financial data and key economic indicators.

It's a privilege to work with you and, as always, if you have any questions, please don't hesitate to give us a call.

Sincerely,

George M. Kapusta, CFP
President, Kapusta Financial Group