The Sage Capital

Newsletter

June-July 2010

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A lot has happened since the last newsletter. We had the "flash crash", the BP oil well trouble, and to top it all off, the Greece / Euro credit issues. I, for one, am surprised at the resilience of the markets. There has been no question that the flight to safety has continued as precious metals, and treasuries have been strong. However, the market is still holding on as earnings have provided stability to the companies who have proactively navigated the ever-changing business landscape.

2nd quarter earnings are coming in and we are pleased at most of the results thus far. The industrial, material, and discretionary sectors have shown surprising strength. The global economy is continuing to provide growth opportunities for the large cyclical companies. The technology and financial sectors look to have been over-valued as recent earnings releases thus far have been broadly disappointing.

In this newsletter we will further examine the economic landscape, giving special attention to the inflation picture, housing, and employment

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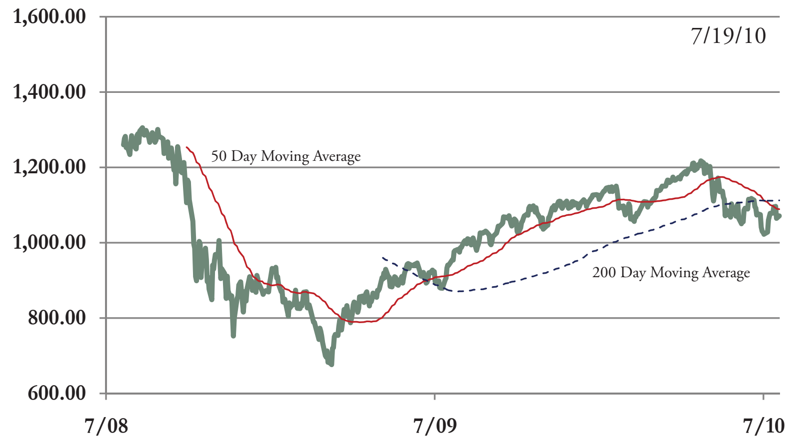
Market Overview

Figure 1: **S&P 500**

Data: Thomson Baseline
(S&P 500, Daily Closing Value,
50 and 200 day
moving averages)

The current broad market appears to be trading at a discount to historic valuations. While it may be too early to declare a healthy economy, we have seen signs of hope as many companies have displayed growth and financial strength in recent earnings releases.

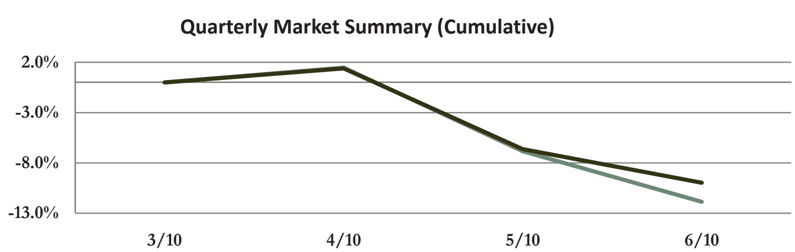


Price % Change:	
1 Month Ago	-5.4%
3 Months Ago	-11.9%
12 Months Ago	12.1%

Table 1: **S&P Performance**
Data: Thomson Baseline
(June 30, 2010 Data)

	Current	5 Yr Avg.
Forward P/E:	13.5	15.8
Dividend Yield:	2.1%	2.1%
Price to CF:	8.9	10.0
Price to Book:	2.0	2.4

Table 2: **S&P 500 Key Stats**
Data: Thomson Baseline
(July 19, 2010 Data)



	3/31/10	4/30/10	5/31/10	6/30/10
S&P 500	0	1.48%	-6.84%	-11.86%
Dow Jones	0	1.40%	-6.63%	-9.97%

Figure 2: **QUARTERLY MARKET SUMMARY**
Data: Thomson Baseline
(S&P 500 and Dow Jones
Monthly Closing Values)

Bond Analysis:

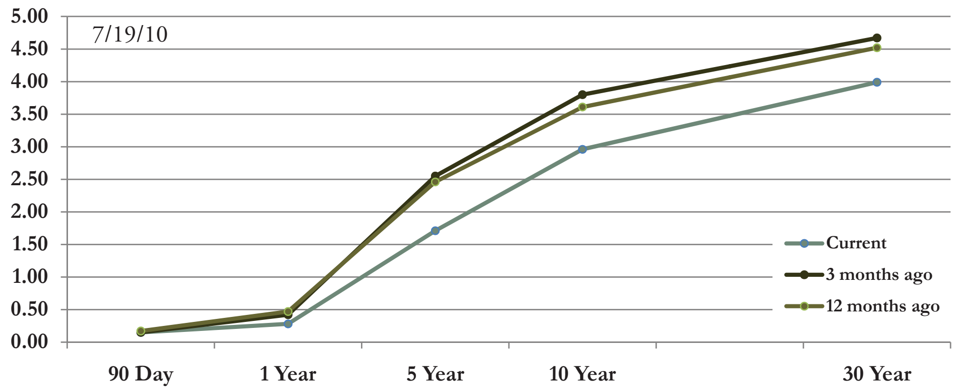


Figure 3: **BOND YIELDS**
Data: Thomson Baseline
(90 Day, 1 Year, 5 Year, 10 Year and 30 Year, Daily Values as of 7/19/10)

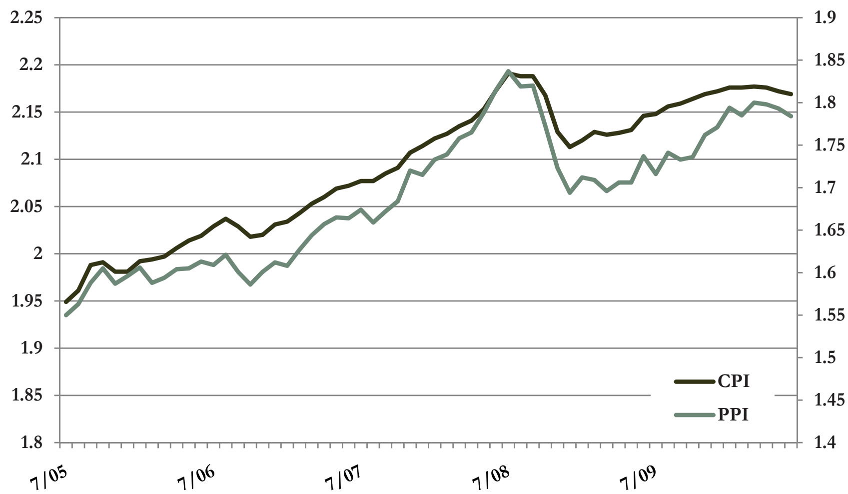
The Federal Reserve Board has continued to forecast a lack of relevant inflation and with production numbers failing to keep pace with prior months, there is little to suggest that inflation will pick up anytime in the near future.

The Producer Price Index declined 0.5% while core PPI increased 0.1%. The Producer Price Index declined for the third straight month led by another sizable decline in energy prices. Core PPI continued a slow but steady trend upwards. Most components remained relatively stable though fresh foods made a sizable decline for the third straight month.

The Consumer Price Index dropped 0.1% while core CPI increased 0.2%. This marks the third consecutive decline in the overall index led by sizable declines in energy prices. Most components remained relatively stable though apparel prices advanced 0.8% while transportation prices declined 1.0%.

Figure 4: **CPI AND PPI (INDEXED, 1982 = 100)**
Data: Thomson Baseline
(Producer Price Index and Consumer Price Index Monthly Closing Values)

Inflation has remained largely subdued with both the consumer price index and the producer price index falling for the third month in a row in June. The pullback in both indices has been led by declining energy prices.



The Economy

Unemployment:

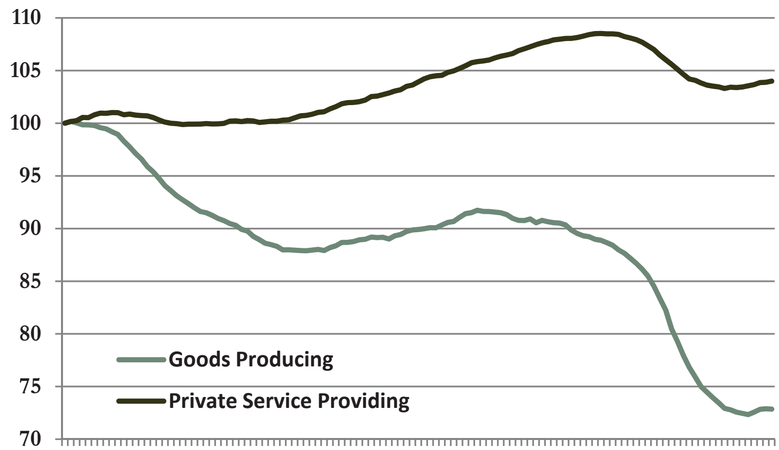
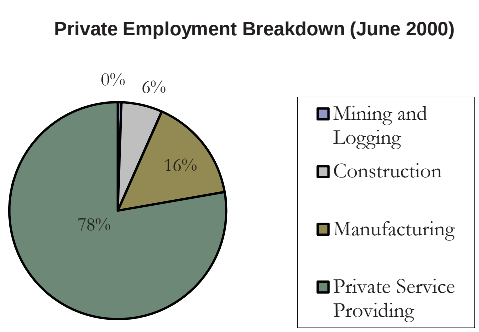


Figure 5: **TOTAL PRIVATE EMPLOYMENT (INDEXED, 2000 = 100)**

Data: Thomson Baseline (Total Private Employment; Monthly Values)

The unemployment rate fell to 9.5% in June and has declined to near annual lows. This suggests that the proportion of people who are looking for a job has peaked and is on a downward trend. However, the unemployment rate is still at an abnormally high rate and the decline has been extremely slow. Furthermore, the number of people looking for work (the labor force participation rate) has tumbled in recent months.

The current decline in jobs is largely due to a drop in goods producing jobs (Fig. 5). These jobs have been largely replaced by machines that can more cost effectively replace human labor and outsourcing. However, even goods producing jobs are bound to recover from current levels, and when combined with growing job sectors such as education and health services along with leisure and hospitality, the job market will recover. The only question is, how fast and to what extent will it happen?



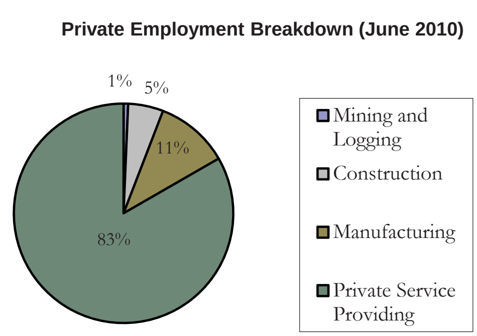


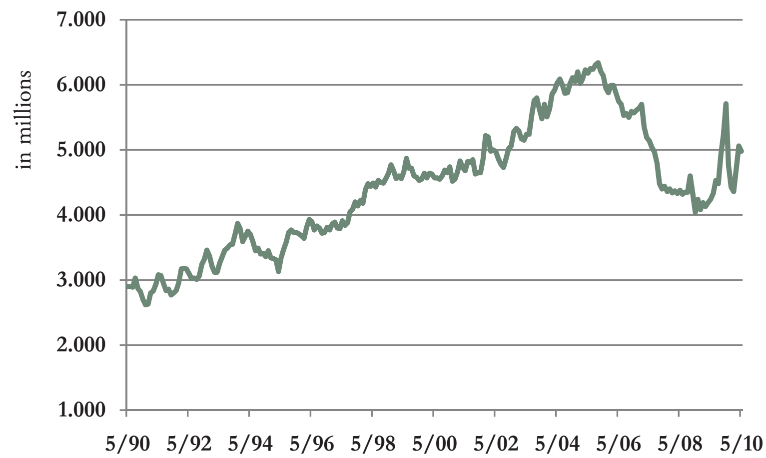
Figure 6: **PRIVATE EMPLOYMENT BREAKDOWN**

Data: Department of Labor Statistics

Note: Goods producing consists of mining and logging, construction and manufacturing

Housing:

Figure 7:
EXISTING HOME SALES
Data: Thomson Baseline (Existing Home Sales; Monthly Values)



New housing sales fell to 300,000 in May which was a 32.7% decline month over month and an 18.3% decline year over year. Existing home sales has been moderately stable but that does not wash away the hugely disappointing new home sales figure. After May's new housing permits disappointed, the June figure has rebounded suggesting that new housing permits and new housing starts may be turning the corner.

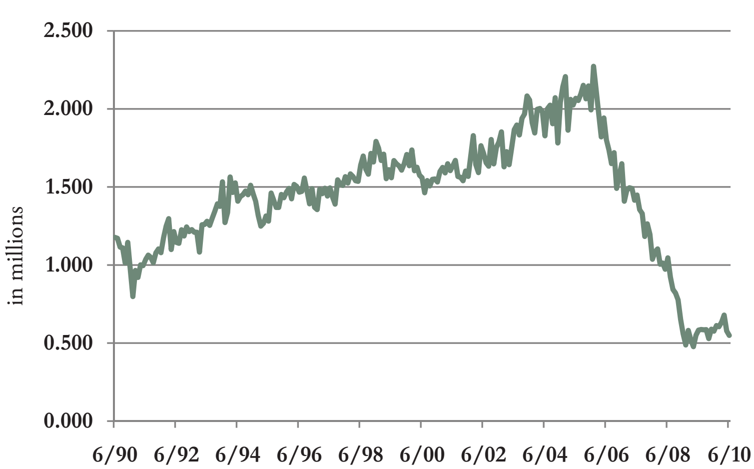


Figure 8:
HOUSING STARTS
Data: Thomson Baseline (Housing Starts; Monthly Values)

In the News:

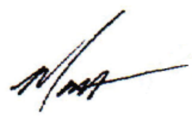
While the oil spill in the Gulf of Mexico has occupied the front page of most news headlines during the last couple months, we have also witnessed some major news events that will be long remembered. The financial problems in Greece have many wondering about the health of the Euro, and is likely one of the catalysts for the recent price increase in gold.

The price of progress has caught up with us in what Wall Street has coined the "flash crash". While technology has enabled us to improve the ease and efficiency in many aspects of our lives, including trading, we witnessed the downside of technological advancements and high speed trading combined with a global market. The market "flash crash" in early May saw the DOW plunge nearly 1,000 points in less than 10 minutes, and may have created an overhang, which has investors concerned over trading systems and the integrity of trading mechanisms in a high frequency trading market.

Thoughts

We will continue to review the earnings releases. While we continue to maintain a cautious stance on the economy, we are reminded of the "Rolling Stones" time is on our side. Every quarter brings new hope that things will slowly get better. We have been through a great deal of turmoil over the last couple of years and yet everyday brings new headlines, but the worst appears to be behind us.

Until next time,



Matt

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