

Progress

April 2, 2010—During a severe economic downturn, one expects companies to cut their dividends to preserve cash. That flexibility is an essential element of corporate fiscal management. Sure enough, during 2009 the companies in the S&P 500 index cut their dividends by an aggregate \$52 billion, including a record-breaking \$38.7 billion drop in 2009's first quarter.

The tide is beginning to turn. Corporate profits have recovered, with some companies holding substantial cash on the balance sheet. Dividend increases have returned. Through mid-March, dividend increases were announced by 77 of the S&P 500 companies, with a net value of \$4.4 billion. (Two companies cut their dividends.) To be sure, the cuts haven't been fully recovered, total payouts are projected to be 16% below the year-ago quarter. Still, analysts are predicting that dividends will grow 5.6% this year for the S&P 500.

In another hopeful sign, the S&P 500 reduced their borrowings in 2009's fourth quarter by \$282 billion. That brought their aggregate debt down to 28% of assets, the lowest in a decade.

Government debt

On the other hand, government debt is growing explosively. The U.S. government is expected to sell a record \$2.43 trillion of debt in 2010. The avalanche of supply so outstripped demand that, for a time in March, the yields on Treasury notes were very slightly higher than the yields on blue-chip corporate bonds, such as those of Berkshire Hathaway, P&G and Johnson & Johnson. The bond market appeared to be saying that investments in these companies were less risky than in the U.S. government.

In 2010 the federal government is expected to consume about 7% of total tax collections for debt service, a figure projected to rise to 11% by 2013. At that level the government could lose its AAA bond rating, warned Moody's Investors Service.

With unrestrained government spending, investors have to begin worrying about inflation. At the moment there seems little to fear. Core inflation was 0.1% in February, up just 1.3% from a year earlier. The yield gap on 10-year Treasury Inflation-Protected Securities (TIPS) fell to 2.20 points in March, from 2.45 points in January. So investors aren't seeing the risk on the horizon yet.

Housing

The Park Avenue maisonette of the late William F. Buckley, Jr., was placed on the market in May 2008 for \$24.5 million. As there were no takers, the "For Sale" sign was removed, to wait out the residential real estate storm. Reportedly, the property is now being offered at \$12 million.

That 50% price decline may not be representative of the value change for homes of ordinary mortals, but around the country residential real estate prices are far off their highs. The temporary extension of the federal income tax credit for home buyers will expire in the second quarter, with unknown consequences. However, a report from Fannie Mae stated that the extension of the tax credit was less effective than hoped, with home sales unexpectedly weak in

the first quarter. Apparently, most of those who were eligible for the tax credit were lured off the fence during its first round.

Until the housing market stabilizes, we are not out of the economic woods.

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