

# Charles Payne's Common Sense Newsletter

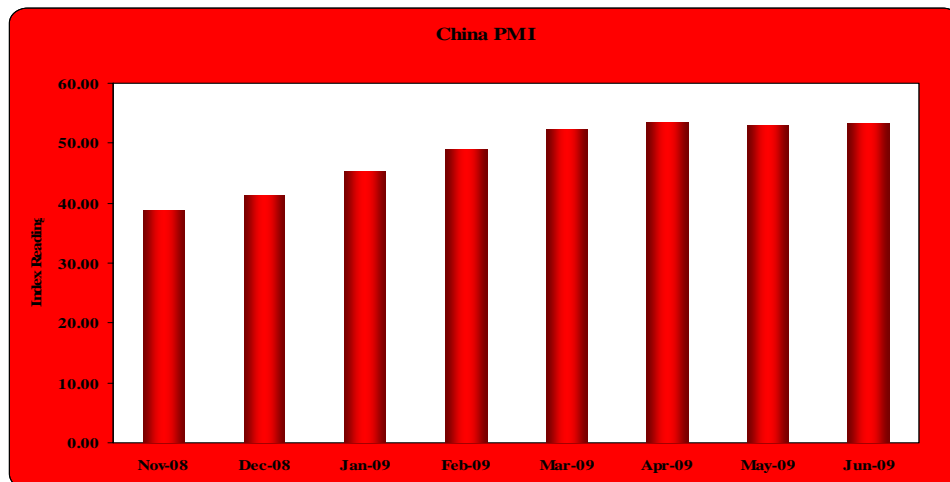
## July 2009



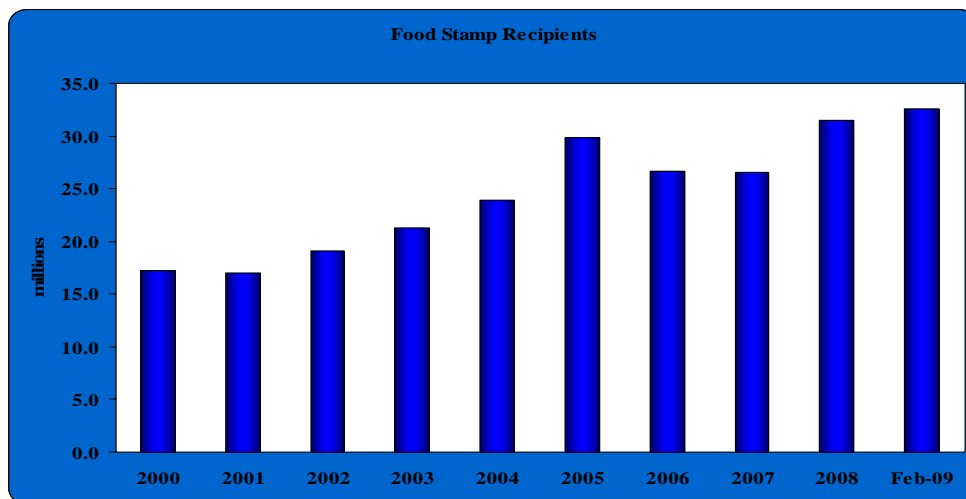
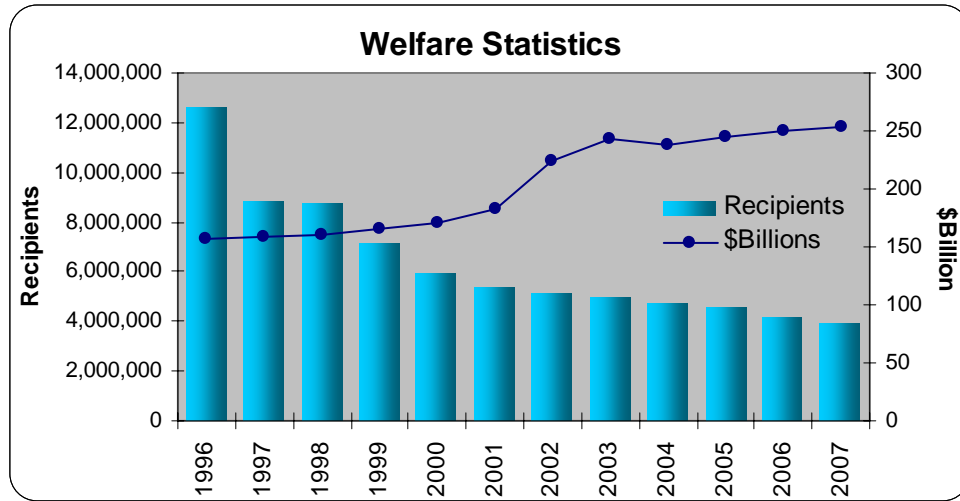
*Wall Street Strategies- Providing independent stock market research since 1991 through a balanced approach to investing and trading*

In like a lion out like a lamb, June was a month that saw the stock market rally grind to a halt as the onus on proof the economy is turning became more rigid throughout the month. Couple this with the fact that the June jobs number came in worse than expected and it has many wondering what will happen in the second half of the year. Last month, Vice President Joe Biden talked about the fact that most of the stimulus money hasn't even gone out yet and suggested there will be a tidal wave of growth in the economy once it starts to flow. I hope that the same tide lifts all ships, but the problem is the plan isn't truly designed to stimulate. One of the big problems with the current stimulus plan is that 1/3 of the money is going to things like food stamps and similar programs and 1/3 is going to government programs and bureaucracy. This only leaves a fraction of the funds for shovel-ready projects, and those have been very slow to get off the drawing board.

While the U.S. economy flounders, it is amazing to see China post its fifth straight month of economic expansion. In November of last year, China's Purchasing Managers Index slumped to a multiyear low reading of 38.8, and then their stimulus plan kicked in. Although fewer total dollars than the U.S. stimulus plan, the Chinese package tallied \$586.0 billion or 78.0% of the 2008 national fiscal revenue. The plan obviously faces no bureaucracy or hidden agendas, and coupled with record bank lending, has corrected the Chinese economy almost instantly. In the meantime, not only has our stimulus plan only trickled out but also the banks, recipients of \$600.0 billion or so taxpayer dollars, are sitting on 100.0% more money now than when the TARP program began. It's a serious problem. It's also a wonder how a communist country could be doing everything right while our government fiddles.



Where is our money going? Well, there are a record amount of people on the food stamp program and the welfare rolls are reversing a long-term trend. It is interesting that proponents of massive social spending point out how that money goes right back into the system and actually creates economic expansion. I've seen the work of famous and smart economists (not always the same) who have said for every \$1.00 distributed in food stamps it creates \$1.73 to \$1.84 in economic activity. But, food stamps don't create jobs. On the contrary, in some ways higher welfare and food stamp payouts could lure minimum wage earners off the job rolls. Of course, in June, there were 9.0 million people working part time that wanted to work full-time so there are plenty of people looking for opportunities.



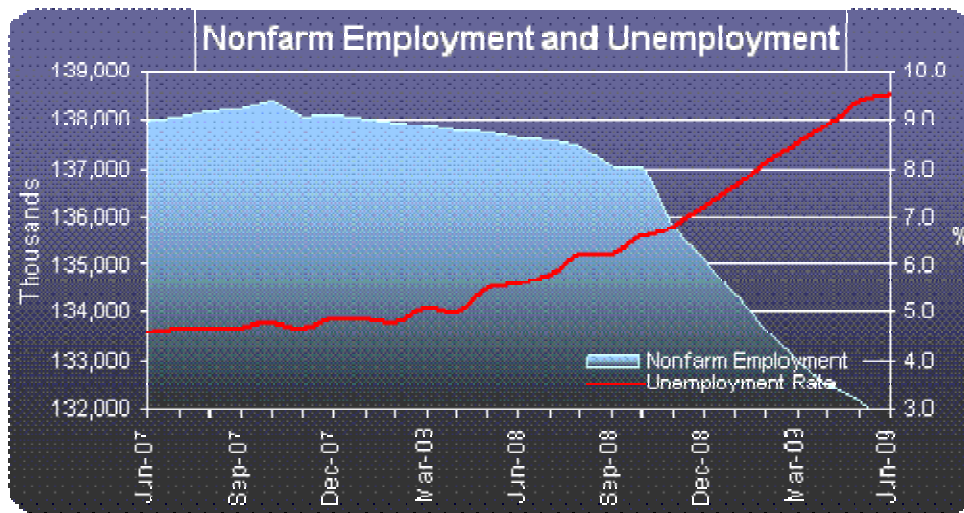
## Stimulus Distribution

Underscoring the problem with all the focus being on social welfare programs is that all the other government agencies waiting for their cut of stimulus have gone begging. In the meantime, Agriculture (food stamps) has received \$2.2 billion of an allotted \$3.2 billion and Health and Human Services (welfare) \$21.5 billion of the \$29.8 billion allotted.

Agency	Available	Paid Out
	(Thousands)	
Department of Education (ED)	\$44,772,426	\$7,585,126
Department of Health and Human Services (HHS)	\$29,814,171	\$21,518,730
Department of Labor (DOL)	\$20,516,829	\$6,570,771
Department of Transportation (DOT)	\$19,005,173	\$369,552
Social Security Administration (SSA)	\$13,031,986	\$13,015,975
Department of Energy (DOE)	\$5,809,167	\$140,911
Department of Housing and Urban Development (HUD)	\$5,186,408	\$708,799
Environmental Protection Agency (EPA)	\$4,407,747	\$12,760
Department of Agriculture (USDA)	\$3,233,803	\$2,153,378
Department of Justice (DOJ)	\$1,726,744	\$364,936
Department of Defense (DOD)	\$965,770	\$8,098
Department of Treasury (TREAS)	\$777,898	\$10,563
General Services Administration (GSA)	\$546,688	\$2,801
Department of Commerce (DOC)	\$542,228	\$241,077
Department of Homeland Security (DHS)	\$526,278	\$19,120
National Science Foundation (NSF)	\$517,339	\$0
US Army Corps of Engineers (USACE)	\$378,457	\$42,876
Railroad Retirement Board (RRB)	\$129,075	\$129,017
Corporation for National and Community Service (CNCS)	\$118,067	\$1,384
Small Business Administration (SBA)	\$109,733	\$23,170
Department of the Interior (DOI)	\$93,292	\$3,011
Federal Communications Commission (FCC)	\$63,225	\$1,773
Department of Veterans Affairs (VA)	\$35,144	\$1,721
Department of State (DOS)	\$28,511	\$6,290
National Endowment for the Arts (NEA)	\$19,842	\$69
Smithsonian Institution (SI)	\$17,505	\$488
National Aeronautics and Space Administration (NASA)	\$5,716	\$0
Agency for International Development (USAID)	\$5,312	\$109
<b>Total</b>	<b>\$152,384,534</b>	<b>\$52,932,508</b>

## Jobs Jobs Jobs

I'm not sure why the mavens of Wall Street thought that there would only be 350,000 jobs lost in June. Were they drinking Kool-Aid served by the administration or were they buying into their own hype? I speak to economists daily and it's amazing how many have bought into the notion of a major second half recovery. It could still happen, although I'm not sure if it's going to be sustainable.



## Notes from the WSS Research Desk

### A Double-Dip Recession is on the Horizon

*Carlos Guillen, Research Analyst*

While we still believe that the economy is worsening at a decreasing rate and that it should reach a trough toward the beginning of next year, mainly as major economic data continue to show signs that second derivatives are indeed turning positive, we fear that the possibility of a double-dip recession is increasing.

Part of the reason for our less optimistic view of a consistent recovery is that we believe energy prices are rising at an extremely quick rate, particularly crude oil prices, putting pressure on overall corporate earnings and on consumption. After bottoming at approximately \$42.00 per barrel in mid-February, crude oil has increased over 50.0% in just six-months. At this rate, crude oil could be close to \$100.00 per barrel by early next year. One of the reasons crude oil has been climbing at this rate, despite that the U.S. has cut back on crude consumption, is that other emerging economies, particularly China, have been ramping up consumption. Another reason is that the risk of devaluing the dollar has been increasing as the U.S. government has taken action to significantly increase liquidity in an effort to unfreeze the credit markets after the worldwide financial crisis.

### Crude Oil Price (Six-Months)



Another possible cause of a double-dip recession that we see comes from the massive amount of government debt. In June, the Congressional Budget Office (CBO) said that this year's U.S. budget deficit is now projected to be approximately \$1.8 trillion (\$100 billion more than estimated in March), representing 13.0% of gross domestic product (GDP), the highest level since World War II (this estimate was 11.9% in March). Next year's deficit is forecasted to be nearly \$1.4 trillion (\$300 billion more than previously expected), representing 9.9% of GDP (March estimate was 7.9%). The CBO now estimates a 10-year deficit of \$9.1 trillion under the president's policies. This is huge, and would add to the already existing debt of approximately \$11.5 trillion. In order to get a better sense of how large \$11.5 trillion is, we divided this figure by the U.S. population (about 300 million); this equates to just over \$38,000 in debt for every man, woman, and child among us.

The expected debt level for 2010 and beyond will likely cause long-term interest rates to increase in the not so distant future, stifling economic growth even before it is able to reach normal growth rates of 3.0% or more. Furthermore, there is also the risk that the Fed will monetize some of the current government debt. While it can be argued that this should help offset increasing interest rates, given the huge levels of expected borrowing, we do not believe the offset will be significant. What will certainly attenuate economic growth is the increase in liquidity resulting from the monetization of debt, which will continue to create inflation. At the moment, inflation is not a main concern since the liquidity that has been pumped into the financial system has been totally absorbed, but extended periods of low Fed funds rates combined with the monetizing of debt will surely create an inflationary environment, which may very well transform a lethargic economic recovery into another recession.

In sum, we believe that GDP will continue to decline in the June quarter by approximately 3.0% and then by roughly 1.0% to 2.0% for the rest of 2009. We do not see a GDP trough happening this year, but we do believe that GDP growth in 2010 will finally turn positive, although at a very lethargic rate of less than 1.5%. However, we believe the probability of a double-dip recession in the horizon of 2011 is increasing as the price of crude oil continues to ramp up, government debt continues to mount, and inflationary forces continue to strengthen.

## June Auto Sales: Looks Like Perfect Example of Green Shoots

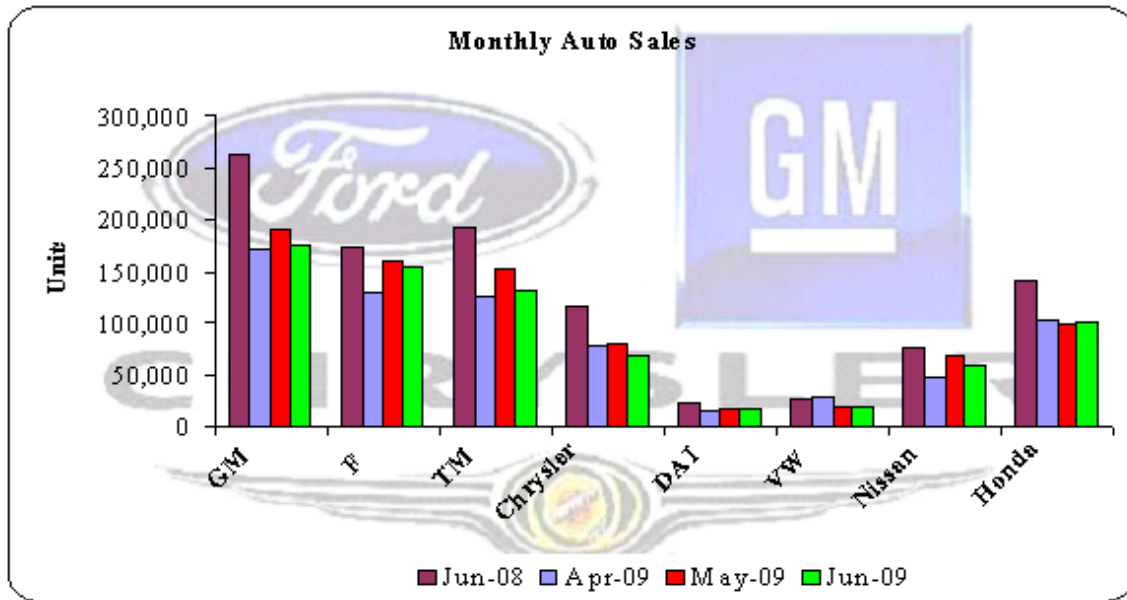
*David Silver, Research Analyst*

In our last sales update, we commented that the “green shoots” we saw during May looked more like weeds than anything else. The latest results are a new breed of grass; a hybrid of the stringy green plant and weed that require the perfect balance to turn into grass, otherwise, we are destined for more weeds. Ford (F) was the clear winner of the month, reporting only a 10.9% sales decline compared to June of 2008. However, the biggest negatives that we saw were again from General Motors and Toyota (TM), which saw declines of 33.0% and 32.0%, respectively. Much of the talk from the Street before the results were released was that industry seasonally adjusted annual rate of sales (SAAR) would increase to above 10.0 million units for the first time since December 2008. That, however, did not come to fruition as SAAR was 9.69 million vehicles down from 9.91 million in May, but still up from earlier in the year. January marked the first time in 26-years that SAAR slipped below the 10.0 million mark, between the years 2000 and 2007, auto sales averaged 16.8 million units. Every automaker (not just Chrysler and General Motors) has been cutting production to try to become profitable with a 10.0 million unit market in the United States, and while many of the companies are much closer, the entire industry would still lose money with that size of a market.

Chrysler went into bankruptcy and re-emerged a “New Chrysler” and is again producing cars. The silver lining is that many dealerships (of the 789 that were not closed) were running on only a few days of inventory left and many of the hotter selling vehicles were sold out. The first seven plants reopened June 28 (six in the United States), while General Motors is trying to follow a similar path and has idled many of its plants during its bankruptcy proceedings. Speaking of which, does anyone else realize that Fritz Henderson, CEO of General Motors has issued more ultimatums and threats than months he has been at the head job? While the situation may be dire, the boy keeps crying wolf that liquidation is the only way. Another interesting little tidbit about the General Motors saga is that both the Administration and management are trying to push around the courts. Don’t you just love checks and balances, I know I do.

Company	Vehicles	Change Y/Y	Change Year To Date
General Motors	174,785	-33.4%	-38.6%
Ford Motor Company	154,873	-10.7%	-33.6%
Toyota Motor Company	131,654	-31.9%	-37.3%
Chrysler	68,297	-41.9%	-45.4%
Daimler	16,271	-26.4%	-26.3%
Volkswagen	19,027	-26.0%	-19.9%
Nissan Motor Company	58,298	-23.1%	-33.0%
Honda Motor Company	100,420	-29.5%	-33.7%

With all the current incentives, I hope that the industry does much better over the next few months. However, with the employment situation the way it is, it is hard to foresee a massive rebound in auto sales. Cash for clunkers and other tax incentives, along with some pent up demand, should give a boost to auto sales in the second half of the year. However, we expect to continue to see “less bad” results through the end of the year. Our hope is that by October, we begin to see year over year sales increases, partially as a result of easy comparisons, added incentives, and an improving economy.



June was another busy month for the auto industry, as Chrysler re-emerged from bankruptcy as a new company run by Italian automaker Fiat, the UAW, and the U.S., and Canadian governments. General Motors entered into bankruptcy with a goal of emerging in 60 to 90 days and to re-IPO during 2010. Toyota announced it expects another annual loss and that it is completely redoing its business plan. Through all this, Ford continues to chug along. Remember back in 2007 when the government passed the energy bill that would give up to \$25.0 billion to the automakers to help the industry refit its facilities? Well, the government finally released the first bit of that money, with \$5.9 billion going to Ford, \$1.6 billion going to Nissan, and \$465.0 million going to Tesla Motors. Tesla is currently the only automaker in the United States that produces a fully electric highway ready vehicle. Additionally, Daimler took an equity stake of nearly 10.0% of the electric carmaker.

Ford continues to impress me with how well it is doing, and its new additions to its fleet including the new Taurus and the Fusion Hybrid have catapulted it with respect to higher fuel efficiency vehicles. However, we maintain that the industry is not out of the woods yet. Auto sales continue to be dismal, and the economy still has many job losses it needs to swallow. In previous commentaries, we said that we believed that more production still has to go offline to meet the current demand levels. The industry SAAR is improving, but not at a fast enough pace to save Ford, Toyota, Honda, Nissan, or Daimler even more pain. The mantra “less bad” continues to live in the auto industry.

Through the remainder of the year, we expect to see continued sequential improvements with the strongest months coming in October and November as the economy begins to show its first signs of growth (and not just the “green shoots”). That being said, we still like the foreign automakers, Toyota and Daimler being our favorites. However, we believe the most upside right now is in Ford. The company has an ambitious vehicle lineup, and while the new Taurus has some big shoes to fill, it will be a great improvement for the iconic Dearborn, Michigan company.

### **From Retail to S&P500, it’s Time to Touch it All**

*Brian Sozzi, Research Analyst*

One tidbit many are not talking about in their coverage of the retail sector is *co-tenancy clauses*. In short, a co-tenancy clause is one contained within a lease agreement that allows a retailer to exit the contract should an anchor store (think Sears) close up shop or occupancy rates in the mall fall below a certain level. Unfortunately, retailers on a broad scale do not breakdown for investors the precise amount of rent by quarter or year (it’s lumped either in COGS or operating expenses depending on the company). The topic of rent has always seemed to me rather secretive; retailers won’t go into great detail so analysts/investors just attempt to gauge directionally where rent outlays are headed.

That said, we track the amount of lease obligations retailers have in the current year and in ensuing years and benchmark it to cash flow trends. The lease obligation information is buried in the SEC filings of the companies. As a point of reference, I have included some of my notes regarding the future lease outlays from a few of the specialty apparel companies I cover. The talk with contacts remain on opportunities to lower rent expense or exit the lease altogether. Thus far, we have seen only modest cooperation by mall developers with retailers on rent, but I expect that dynamic to shift increasingly in the favor of the retailer going into 2010 (especially if the holiday season is a bust, which is possible).

Some further food for thought on co-tenancy kick out clauses:

- Should negatively impact those mall developers operating C-rated mall properties. If they lose a Sears (SHLD) or JC Penney (JCP) as an anchor tenant, specialty retailers could go into high gear trying to get out of the leases.
- Those specialty retailers that should theoretically benefit would be those with stores concentrated in C-rated or B-rated malls; of my coverage universe I would say a company such as Pacific Sunwear (PSUN) has the most opportunity should it have co-tenancy clauses
- Bigger picture: your traditional mall is a dying breed. It’s unfortunate to say, but it just fits with where I see the market right now and where it’s likely heading.

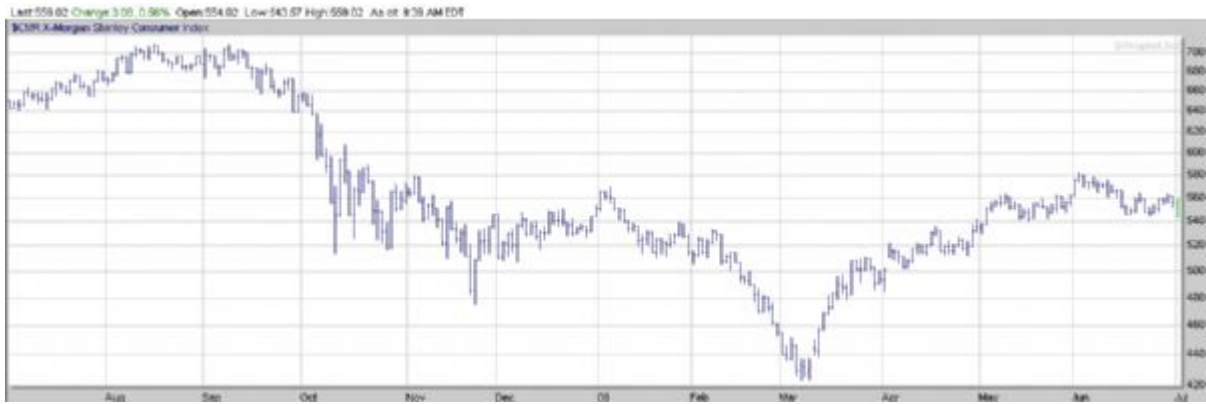
These numbers (in millions of U.S. dollars) speak volumes to retailers chasing an overheated market, which was evidenced from 2006-2008. Now, many of these companies have fallen on hard times, but the cash outflow associated with the lease is still real and of course painful.

Company	Less than One Year	One to Three Years	Three to Five Years	More than Five Years	Total
<i>Abercrombie &amp; Fitch</i>	314.6	624.7	555.7	1,302.1	2,797.1
<i>American Eagle Outfitters</i>	234.1	442.6	373.4	720.3	1,770.4
<i>Pacific Sunwear</i>	96.0	169.0	122.0	138.0	525.0
<i>Guess</i>	160.0	215.7	186.5	300.1	828.3
<i>Aeropostale</i>	98.8	186.2	162.6	198.5	646.2
<i>Hot Topic</i>	55.6	102.1	81.4	78.3	317.4
<i>Urban Outfitters</i>	132.5	392.5	232.1	328.9	1,086.2

*One Must Look Beyond the Headline Noise*

Second quarter earnings season is approaching at warp speed, and in many cases it's put up or shut up time for corporate America. It's widely held as gospel that the banking sector (minus regional players) enjoyed one heck of a party in the second quarter, benefiting from the perfect storm of cheap government money that was loaned out at high rates, fat fixed income spreads, and strong underwriting fees as companies took advantage of the improved economic climate to issue debt and equity. Considering that banks hold significant representation in the S&P 500, it's not entirely far-fetched to imagine the index shifts out of its recent consolidation gear and puts *rubber to the road*. By *putting rubber to the road*, however, I do not mean a material move higher as the S&P 500's advance from the March nadir (+36.0%) suggests the pricing into equities of a robust second half recovery in economic conditions. Nonetheless, upside earnings reports from banks as a result of the aforementioned factors, and likely bottom line beats by others that comprise the S&P 500 due to cost cutting measures and scant inventory on the books could be enough to get sideline money into the fray. Beyond second quarter earnings season, my sense is that we will require more than *stabilization* in economic data sets to justify further gains in equities; on the contrary we will need definitive signs of *improvement*.

Against this backdrop, I believe it's a dangerous proposition to allocate capital to consumer discretionary equities. Whether it's a retailer of pricey apparel or a sit down dining eatery, chances are if the stock is publicly traded it has surged from the depths of hell seen in March. As a visual example, check out the direction of the Morgan Stanley Cyclical Index (+100.0% from March) and the Morgan Stanley Consumer Index (+33.0% from March), both up handsomely during the last three-months. The buying activity into the underlying index stocks has been primarily on hope for a rosier second half economy rather than indications of a fundamental turn for the better in sales and operating margins (ex. items of course). An inability for these indices to breakout in June is telling, and should not be overlooked. In my view, the rebuilding of savings and balance sheet de-leveraging on the consumer side of the GDP equation are powerful forces that will play out well into 2010, which equates to fewer dollars in the hands of merchants selling discretionary goods or services. Despite efforts to cut operating expenses and squeeze the supply chain, the lack of demand will cause a recalibration in valuation of consumer discretionary equities as investors realize there is more to growing profits than simply jettisoning unproductive employees and loss leading store sites.



## **Crude Oil Outlook**

*Conley Turner, Research Analyst*

The price of crude oil continues to be impacted by an array of factors that range from geopolitical issues to the fluctuating value of the dollar versus other currencies. In recent weeks, the commodity's price has been influenced by activities of Nigerian militants against that country's oil installations. The fact that Nigeria is the largest producer in Africa and the fifth biggest exporter in the world makes what happens there of great importance to the price of the commodity. As a result of that ongoing situation there, the country's capacity has been cut by almost half to approximately 1.6 million barrels a day versus a known capacity of 3.2 million barrels.

The fact that the value of the U.S. dollar has been declining in comparison to other international currencies is a key supporter to the price of the commodity. Crude oil has an inverse relationship the value of the dollar. What can exacerbate this situation is all the government spending that is currently occurring. This is at the end of the day inflationary, and could result in the greenback weakening even further.

Another reason for the volatility in the price is the fact that the outlook for the U.S. economy continues to be a moving target. As a result, every bit of economic data released by the government is analyzed by the market in order to forecast the direction of the economy over the next few months. At this juncture, the prevailing consensus among market participants is for the commencement of an economic recovery towards the end of the current year. Should this actually materialize, demand could ramp meaningfully due to an expected increase in economic activity. This in turn is likely to lead to an eventual rise in the demand for crude oil and as a result, the price. Crude oil inventories continue to be at record high levels and this will have to be worked through if any sustained rally is realized. The obvious caveat is that as the price rises, it can realistically derail any economic recovery at least in the short-term.

The fact of the matter is that the economy is at a crucial juncture where those green shoots grow deeper roots and establish firmer footing or a double-dip recession can ensue. It stands to reason then that as market participants look for direction on a daily basis, the price of the commodity is likely to exhibit a significant amount of volatility.

The argument can be made that the rise in the price of crude oil in the past several weeks has been too aggressive and some degree of retracement is necessary. There is no guarantee that that this will occur and crude oil can conceivably be range-bound around the \$70.00 per barrel area.

In the long-run, however, there is considerable underinvestment in crude oil exploration and production. This will likely be a catalyst for a spike in the price of the commodity once an economic recovery is a certainty.

## The Housing Market

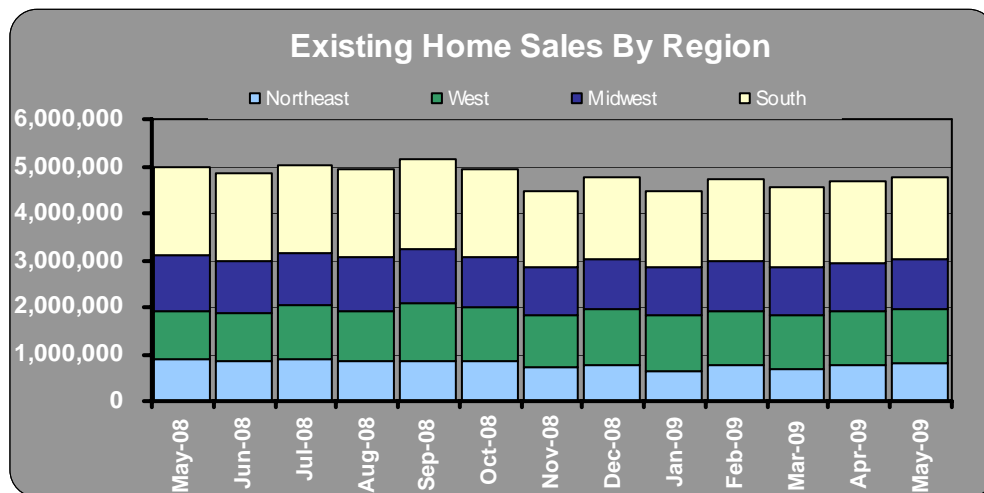
David Urani, Research Analyst

The latest round of home sales data is in, and mixed signals were the name of the game for May. Whereas previous months looked decent on the surface but then soured the longer we looked at them, the latest data appeared disappointing at first but perked up upon further inspection. Both new and existing home sales came in below consensus expectations, which was the first thing everybody noticed. In a sense, previous market sentiment that home sales were bottoming has been tempered a bit. On the other hand, grave worries about the impact of foreclosures and ongoing price pressure have eased; albeit, very modestly.

Existing home sales increased for the second month in a row during May, at a rate of 2.4% annualized to 4.77 million; the consensus was looking for 4.82 million. Sales were characterized by month to month boosts of 3.9% and 9.0% in the Northeast and the Midwest, respectively, while remaining flat in the South and decreasing by 0.9% in the West; sales of single family units increased by 1.9%. It was somewhat strange to see annual sales decrease in the West, although we should note that the numbers are annualized to take seasonal effects into account; with the extraordinary conditions in the housing market today including tax credits, low prices, other incentives etc., seasonal effects are being mitigated to a certain extent.

On a non-adjusted basis, sales increased by 7.8% month to month, with increases in all regions (including the West). We are somewhat worried about the West in the months ahead though, given that California was seeing a boost from a \$10,000 state-enacted tax credit for home purchases; as of June 10, \$88.3 million of the \$100.0 million program was used up and when it ends, demand may falter. Given the state of California government's fiscal problems these days, the possible extension of the tax credit is questionable.

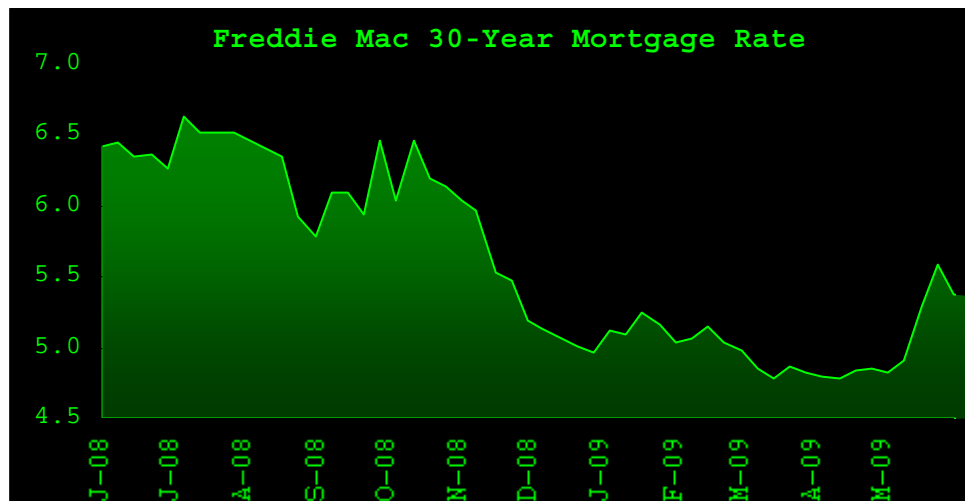
We were glad to see inventory come down by 3.5% for the month, especially after increasing by 7.9% in April; there is currently a 9.6 month supply on the market. Prices showed some signs of firming up, with the average increasing by 3.3% to \$215,600, although the number is volatile because of mix changes month to month, and furthermore the nationwide \$8,000 tax credit may be bumping up base prices.



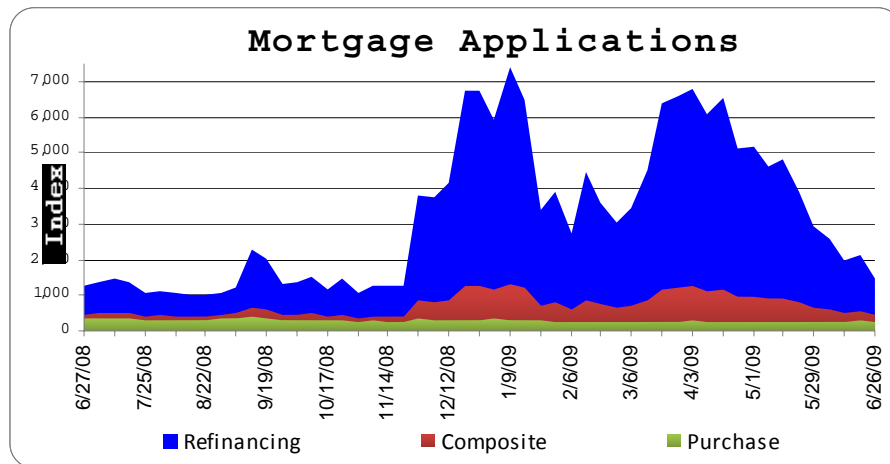
New home sales decreased by 0.6% month to month to an annualized rate of 342,000, falling well short of the consensus estimate of 360,000. It should be noted that the April numbers were revised down to 344,000 from 352,000, so the drop down to 342,000 wasn't as bad as it first looked. But, still, the Street was looking for an increase, and it simply didn't pan out. That being said, there were some silver linings in the new home sales report. A primary point of interest is that the only region to have lower sales compared to the previous month was the South (declined by 8.5%). Otherwise, the Northeast, Midwest, and West increased by 28.6%, 18.6% and 1.3%, respectively. Also, similar to the existing home sales report, supply came down and prices seemed to firm. However, shifts in geography and other factors can add volatility to the new and existing home price numbers, so we are not quick to rely on those numbers.

When tracking prices, indexes like the Case-Shiller and the FHFA index are generally more reliable, as they are more methodical and adjust for certain variances, although they are a month behind the other data. The FHFA index for April showed prices came down from March by 0.05%, indicating a slowing rate of decline than in previous months. But still, we are not ready to put our faith behind the report given that it only tracks homes with mortgages backed by Fannie Mae and Freddie Mac, plus as we stated earlier, tax credits are largely being applied to such homes which could be inflating the base price.

Combining the drop in new home sales with the smaller than expected gain in existing home sales, and there is a somewhat worrying indication that the demand surge we were seeing in the works is ebbing. A major factor in our opinion is the fact that mortgage rates are on the rise. After sinking below 5.0% for almost three months between March and May, rates are now hovering around 5.5% again. Essentially, when mortgage rates rise, the price of the home goes up, as monthly payments become larger. And, unfortunately, this could put the pressure back on prices heading into this month and beyond.



We can see the effects of higher rates directly affecting the volume of mortgage applications in the past couple of months. In March and April as mortgage rates hit record lows, there was an evident refinancing frenzy, spurred on by the government's plan to get underwater borrowers into more manageable loans. However, that demand has fallen off a cliff recently, and it seems clear that the urge to refinance has washed away almost entirely. With Bernanke & Company struggling to find a balance between the money printing press and inflation, we have to wonder how much more money the Fed can throw at the system without disrupting the economy. Furthermore, it is quite possible that the frenzy of refinancing flooded the securities market with supply, thus lowering prices and raising rates. We are afraid that any additional actions to spur mortgage lending will repeat this event, and essentially mortgage rates cannot be sustained at lows such as those hit in April.



The main question in our minds heading into the June number releases (at the end of July) will be how much price discounting was needed to maintain the upward momentum in sales? My inclination is to expect more price pressure ahead, especially since mortgage rates are trending higher. Not to mention foreclosure filings in May were still at the third highest rate on record (behind March and April), and this continues to affect supply and consumer confidence.

## Long Ideas

### Mosaic Company (MOS)

*12-Month Price target: \$90.00*

There have been some inconsistencies with the company and industry but the basic investment thesis is in place.

- The world is growing (by 75.0 million people a year)
- The world is getting wealthier and demanding better diets
- There is seasonality that works in the industry's favor as farmers can't resist price changes forever

### One-Year Performance



### La-Z-Boy Inc. (LZB)

*12-Month Price Target: \$7.00*

Let's be perfectly blunt, no one is buying furniture. Better still, demand for furniture was suspect when the housing market was running on the rocket fuel that was sub-prime mortgage originations. La-Z-Boy has been hit over the head from a fundamental perspective for as long as we have covered the company for institutions. That said, the latest quarterly report suggests a reversal of fortunes, finally. A few items stood out to us rather prominently, such as the reduction in net debt, free cash flow generation for the full fiscal year, and gross margin expansion at the core (excluding restructuring costs). In our view, these elements to the story speak volumes to the streamlining initiatives that La-Z-Boy has undertaken over the past two years. To experience an almost 25.0% decline in net sales year over year and leverage cost of goods sold, not to mention drive core operating profits, was impressive. Moreover, we would add that the Retail segment, under the direction of a new division leader, appears to have made progress on the product and expense sides.

We believe that what was seen from La-Z-Boy in the quarter is in fact sustainable. The company has removed considerable fixed costs from its operating platform, meaning the upside reported in the quarter was not just fueled by tightening of variable outlays and waning commodity input prices.

In conducting a deep dive of the quarter, cash and equivalents and restricted cash numbered \$36.1 million, providing La-Z-Boy sufficient liquidity going forward. Elsewhere, inventory was reduced 21.41% year over year, and long-term debt brought down to a manageable \$52.1 million (-47.63% year over year). The company's receivables turns were steady year over year, though the troubles in the dealer network drove the allowance for doubtful accounts to 19.2% of receivables from 8.9% a year ago. Mostly through adjustments to operating cash flow and much lower cap ex., La-Z-Boy yielded \$36.0 million in free cash flow in FY09 compared to \$21.8 million last year.

### One-Year Performance



### BJ's Wholesale (BJ)

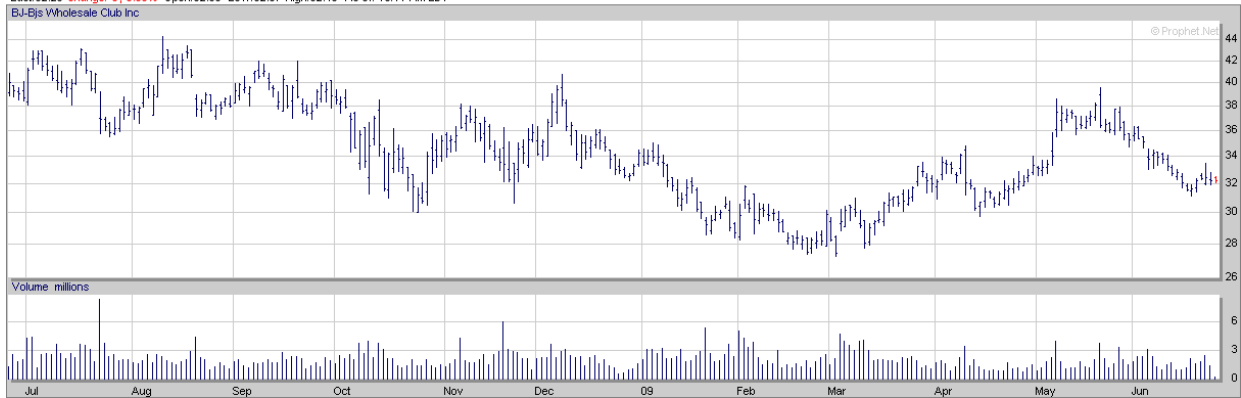
*12-Month Price Target: \$45.00*

We have closely followed the company for some time, and with the stock pulling back recently we believe an attractive point has been created. When all is said and done, the company will have had the strongest 2009 from the discount retail sector (despite some of the toughest year over year comparisons), delivering robust EBITDA growth on solid sales mix, among other factors. We continue to believe that BJ's Wholesale is gaining share from the likes of Costco Wholesale Club (COST) and Sam's Club by offering stronger presentations and value in fresh food. In fact, BJ's Wholesale notched double-digit percentage comparable store sales (comp) growth in each quarter of 2008 in fresh food; in 1Q09 it comped +12.0% on top of +10.0% a year ago. The company's efforts in fresh food presentation, store associates, and refrigerated food case build outs are facilitating the intended results.

The balance sheet remains in fine standing. All key indicators we track on the company suggest continued peer group outperformance (sales/earnings) going forward. BJ's Wholesale is driving traffic to its stores (+7.0% in 1Q09, highest in five years) and is retaining customers at a slightly better pace than internal projections.

### One-Year Performance

Last: 32.20 Change: -0.03% Open: 32.39 Low: 32.07 High: 32.49 As of: 10:11 AM EDT



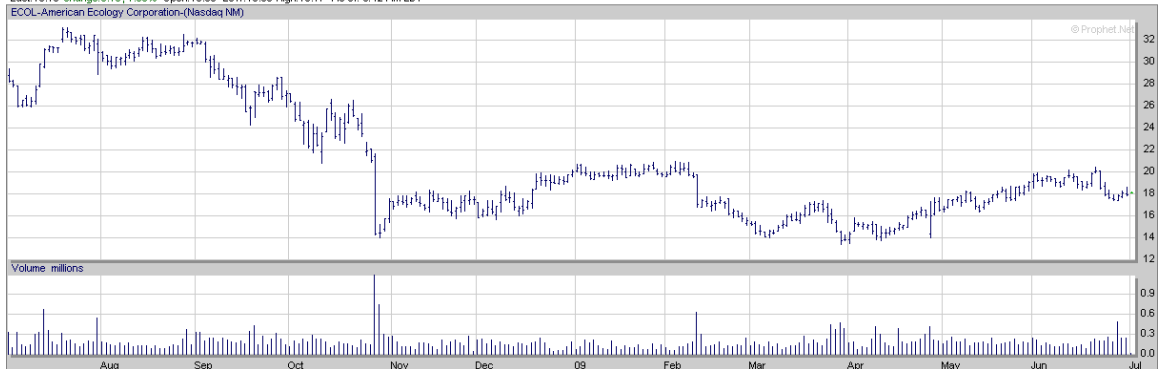
### American Ecology Corporation (ECOL)

12-Month Price Target: \$25.00

One of the many places that President Obama has his sights set on is improving the economy through a cap and trade system. American Ecology Corporation does radioactive, hazardous, polychlorinated biphenyls (PCB) and non-hazardous industrial waste management and recycling services to commercial and government entities, such as refineries and chemical production facilities, manufacturers, electric utilities, steel mills, medical and academic institutions, and waste broker/aggregators. There is no hiding it that the first quarter of 2009 was a an ugly quarter for the company, as only 213,000 tons of waste were disposed, compared to 343,000 tons in last year's first quarter. The drop came as a result of lower transportation-related service on bundled transportation and disposal contracts. CEO, Steve Romano, said "While our recurring Base business held up reasonably well, reduced waste shipments from both government and private industry clean-up sites drove lower than expected results." The stock hasn't lived up to its hype, but management has taken a worst case scenario approach to its fiscal year 2009 earnings per share estimates, therefore, if these green shoots really are sprouting up around the country, this could be one of the first companies to feel it. We would like to see a little more insider buying though.

### One-Year Performance

Last: 18.10 Change: 0.18, 1.06% Open: 18.05 Low: 18.05 High: 18.17 As of: 9:42 AM EDT

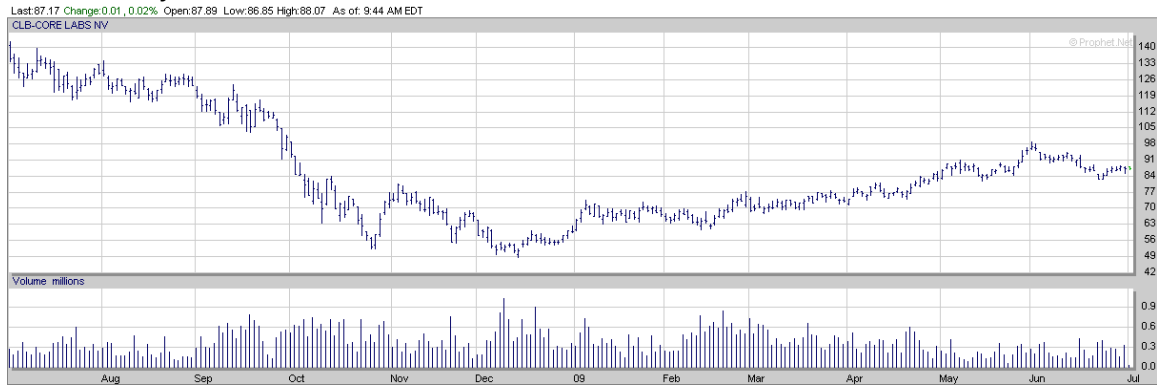


## Core Labs (CLB)

*12-Month Price target: \$98.00*

The fact that the company's services business is internationally focused and concentrated in oil exploration and production as opposed to natural gas is likely to be a positive catalyst once an economic recovery occurs in earnest. There is a better than even chance that the economy rebounds by 2011, which is likely to result in stronger earnings potential for the company. Shares of Core Labs are currently trading at a multiple that is somewhat discounted to its industry peer group but once improvements occur, the stock is likely to regain its historic premium.

### One-Year Performance



We are including a copy of our May 401K/IRA Monitor with this month's Newsletter.