DECEMBER 12, 2011 • VOLUME 116

Dr. BOB FROEHLICH

Executive Vice President & Chief Investment Strategist
Wealth Management, The Hartford

Dr. Bob is an executive vice president and chief investment strategist for Wealth Management at The Hartford. He is a member of The Hartford's Investment Oversight and Strategy Committee and an officer of The Hartford Mutual Funds.

MAY YOU INVEST IN INTERESTING TIMES

Something very interesting and unexpected happened to me last week as I traveled from Chicago to Birmingham to Atlanta to Greenville, and then back over to Atlanta, followed by New York and Chicago. While I was meeting with a small group of financial advisors in Birmingham, Alabama, one of the advisors summed up what's going on in our markets by citing what some believe to be based on an ancient Chinese proverb: "May you live in interesting times." While it didn't really hit me at the time, the more I thought about it, the more insightful it seemed. Talk about an integrated global economy—I never thought I'd be in this business long enough to find an advisor from Alabama using a phrase with possible Chinese origins to help explain investments to his clients.

I'm taking some liberty with "May you live in interesting times." I've changed the phrase slightly to "May you invest in interesting times." In my 35-year career in and around Wall Street, I don't think I've ever experienced a more interesting time in which to invest than today. How much more interesting can it get than now with record retail holiday sales, lower gasoline prices, record-low mortgage rates, India working to open up its retail industry, funds continuing to flow out of stocks and into bonds, the global interest-rate-easing cycle, and China's energy demand? I thought it might be good to touch on all of these interesting investment developments, beginning with record retail holiday sales.

RECORD RETAIL HOLIDAY SALES

The holiday shopping season certainly got off to a record start. It began on Black Friday, carried on through the first weekend of the holiday shopping season, continued over to Cyber Monday and into the week that followed. Before I show you the record sales numbers, I'd like to talk about why Wall Street calls the shopping day after Thanksgiving "Black Friday." While there are numerous theories, here's the one that's most widely accepted. Traditionally, many retailers operated at a financial loss for most of the year (January through November) and made their profit during the holiday season, beginning with the day after Thanksgiving. When accountants recorded this in their financial records, they used red ink to show negative amounts and black ink to show positive amounts. Black Friday was the beginning of the period when retailers no longer had losses (the red) and they started to show profits (the black).

Now that you know "why" we call it "Black Friday," let me show you "how" it worked this year. Total retail sales for Black Friday grew 6.6%, according to ShopperTrak. This represents the largest gain since 2007. The combination of bigger and earlier promotions, along with retailers opening their doors earlier than ever before, probably led to this increase. For the entire Black Friday weekend, retail sales were up 16.4% on a year-over-year basis—the highest year-over-year increase ever recorded.

> Over Black Friday weekend, retail sales were up a record 16.4% on a year-over-year basis.

Coremetrics, which analyzed Black Friday sales, found an even more interesting trend. While Cyber Monday (the Monday following Thanksgiving) is historically viewed as the big online shopping day, this year's online Black Friday sales were up 24% on a

NOT INSURED BY FDIC OR ANY FEDERAL GOVERNMENT AGENCY	MAY LOSE VALUE	NOT A DEPOSIT OF OR GUARANTEED BY ANY BANK OR ANY BANK AFFILIATE

FDIC BANK

year-over-year basis. I guess a lot of shoppers decided that they didn't want to set the alarm clock for 2:00 a.m. and fight the frenzied crowds at the mall. Instead, these people stayed home and shopped online. Some of them even shopped online while they weren't at home. This past Black Friday, online retail sales made on mobile devices jumped to 10% of all online purchases. Last year, mobile devices only accounted for 3% of all online purchases. Talk about investing in interesting times.

LOWER GASOLINE PRICES

Let me move on to my next interesting investment development: lower gasoline prices. According to the American Automobile Association, as we headed into this past summer's driving season, the average U.S. retail gasoline price was above $4.00 per gallon. The most recent reading as of November 27, 2011 shows that the average U.S. retail gasoline price dropped to $3.30 a gallon. That's a big drop in the price of gasoline in less than one year's time. There may not be a more important number for consumer confidence than the price of gasoline. Consumers face gas prices every single time they have to fill up their tanks. Also, no one has to explain this number to consumers—they know exactly what it means. Come to think of it—maybe this interesting investment development of lower gasoline prices helps explain my first interesting investment development of record retail-holiday sales.

Gasoline prices dropped substantially in less than a year's time. The price of gas may be the most important number for consumer confidence.

RECORD-LOW MORTGAGE RATES

Let me move on to my third interesting investment development: record-low mortgage rates. We currently have the lowest mortgage rates in my 35-year career. The best measure of mortgage rates is the U.S. 30-Year Fixed Mortgage Rate 13-Week Average. As of November 25, 2011 that rate stood at 4.12%, which, once again, is the lowest I've seen in my career. It's hard to believe that in the early 1980s this number approached 19%! It's almost mind boggling for investors to think about mortgage rates being that high. How in the world did anyone afford a new home with interest rates at those levels? At some point in time, these record-low mortgage rates may help fuel a turnaround in our housing and real estate market.

INDIA IS WORKING TO OPEN UP ITS RETAIL INDUSTRY

Let's look outside the United States for my fourth interesting investment development: India is working to open up its retail industry. Why is this important? The country has 1.2 billion potential shoppers—the second largest population in the world after China. In addition, Indian consumers now have more money to spend. The economy of India currently stands at $1.43 trillion. Of the 181 countries economies in the world that are tracked by The International Monetary Fund (IMF), India just barely missed cracking into the top 10—they're ranked number 11 in the world.

Recently, new retail industry regulations were seriously considered in India, but in the end, before the ink could dry on the new rules, the Indian government dramatically reversed its decisions. While the new regulations didn't actually pass, I'll describe them for you because it's important to point out the extent to which the country is seriously considering change.

Under the regulations that nearly passed, foreign corporations would have been able to fully own mono-brand retail operations. In a mono-brand retail operation, only one brand of product is in the store—think Apple computer store, for example. In addition, foreign corporations would have been able to take up to a 51% ownership in multi-brand joint venture retail operations. In a multi-brand retail operation, you can find multiple brands in the same store—think Best Buy stores, for example, where you can find Apple, Dell, and Toshiba branded products. This softening of restrictions would have been a tremendous shift from previous regulations which 1) only allowed up to a 51% stake in a mono-brand retail operation, and 2) completely banned investment in multi-brand retail operations.

If the softening of regulations had occurred, retail corporations with strong global brands could have benefited. This is a big blow to Indian Prime Minister Singh's effort to boost foreign investment into India. Stay tuned; this is a work in progress and things could change once again. Talk about investing in interesting times.

FLOW OF FUNDS

My fifth, and maybe most confusing, interesting investment development concerns the flow of funds. Specifically, I'm referring to the continued flow of funds out of stocks and into bonds. This might be the most confusing investment development I've ever seen in my career. The Investment Company Institute (ICI) tracks net fund flows for the mutual

fund industry. According to the ICI, individual investors poured $375.9 billion of net fund flows into bonds, while stocks had a negative fund flow amounting to -$8.9 billion in 2009. In 2010, the exact same trend continued as individual investors poured another $241.2 billion of net fund flows into bonds, while stocks had another negative year with fund flows amounting to -$37.8 billion.

Year-to-date numbers through October reveal the exact same trend. Individual investors put $90.5 billion of net fund flows into bonds, while net fund flows for stocks is once again negative at -$80.7 billion so far this year. So, for the last two years and 10 months, retail investors have poured $707.6 billion of net fund flows into bonds, while net fund flows for stocks during that same period were -$127.4 billion. These numbers are very confusing to me. Here's why. The biggest enemy of the bond market is rising interest rates. Well guess what? Interest rates, as measured by the Fed Funds Rate, are currently at zero. Rates can't go below zero, and they can only go one direction, and that direction is up. It isn't a question of if—it's a matter of when. With interest rates at zero, I don't understand why so much money is going into bonds. I wonder if all of these individual investors who are going into bonds understand what they're doing. I don't think they all have financial advisors. Talk about interesting times.

During the last two years and 10 months, bonds' net fund flows were $707.6 billion, while stocks' net fund flows were -$127.4 billion.

GLOBAL INTEREST-RATE-EASING CYCLE

My sixth interesting investment development is the global interest-rate-easing cycle. Brazil, Thailand, and Israel all cut rates recently, putting the interest-rate-cut count at 36 over the past three months. But the big ease was China's unexpected interest rate cut. China's central bank cut the Reserve Requirement Ratio (RRR) for banks by 50 basis points (0.50%) for the first time in nearly three years to ease credit strains and shore up the economy as inflation is contained. This will get even more interesting because I believe that even more interest-rate cuts will come from China. The global easing cycle is clearly underway. Talk about investing in interesting times.

Brazil, Thailand, and Israel all cut rates recently, bringing the number of interest rate-cuts to 36 over the past three months.

CHINA'S ENERGY DEMAND

Let's stick with China for my seventh and final interesting investment development. According to the BP World Energy Report, China accounted for 76% of the increase in world demand for energy from 2008 through 2010. Maybe even more interesting was the fact that from 2000 through 2002, China accounted for 38% of the increase in world energy demand. The increase from 38% to 76% is what those of us on Wall Street call a "double." China may be the single most important factor regarding energy that Wall Street has ever seen. From an investment perspective, nothing is more interesting to me than China.

Let me bring this commentary to a close with my customary pearls-of-wisdom quote. With the last two interesting investment developments focusing on China and the title of this commentary coming from an ancient Chinese proverb, I decided to tie my quote into China. It comes from Confucius, China's most famous teacher, philosopher, and political theorist. This is one of my favorite quotes from Confucius: "I hear and I forget. I see and I remember. I do and I understand."

Here's what I want all of you to do: "Have a great day, keep a positive attitude, and please join me in resolving to remain a long-term investor in a short-term world."

To sign up to receive Dr. Bob's weekly commentaries via email and to read past commentaries, visit HartfordInvestor.com.

The views expressed here are those of Dr. Bob Froehlich. Dr. Bob Froehlich's views are not necessarily those of The Hartford and should not be construed as investment advice. They are subject to change. All economic and performance information is historical and does not indicate future results.

Dr. Bob Froehlich's sources of information include Bank of Canada, The Bank of England, Bank of Japan, Bloomberg News, Business Roundtable, China Investment Corporation, CIA. World Fact Book, CNBC, Congressional Budget Office, Deutsche Bank, The European Monetary Union, Federal Reserve Board, The Financial Times, Freddie Mac, FOX Business, Goldman Sachs, International Monetary Fund, International Strategy & Investment, Journal of Commerce, Merrill Lynch, PIERS Global Intelligence Solutions, Strategas Research, Thomson Reuters, Union Bank of Switzerland, U.S. Census Bureau, U.S. Department of Commerce, U.S. Department of Labor, U.S. State Department, U.S. Treasury Department, The Wall Street Journal, and The World Bank.

PAST ECONOMIC PERFORMANCE DOES NOT ENSURE FUTURE RESULTS.

Distributed by Hartford Securities Distribution Company, Inc.

All information and representations herein are as of 12/11, unless otherwise noted. P6170_121211 108690 12/11