



Fulcrums and Flashpoints

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To a great extent, the market's balance in the shorter term rests on a fulcrum represented by the price of a barrel of oil. If oil prices break out yet again to the upside, it becomes very difficult to envision any area of the stock market doing well, even energy itself. Readers may recall that when the price of oil spiked to all time highs a week or two ago, even energy stocks declined.

If, on the other hand, oil prices retrace their recent parabolic moves and fall back to longer term and more sustainable trends, it would usher in a period of multiple expansion for the U.S. stock market and provide a breath of fresh air to the beleaguered consumer discretionary sector.

Why might oil prices decline? In a word, slowing overseas economies, particularly China. High rates of inflation, tight monetary policy, a decline in leading indicators and a stock market more than 50% off its highs all suggest that an overseas slowdown is much more plausible than many may recognize.

In general, we have been reducing our exposure to energy and the industrial complex, while taking a more positive posture on the consumer discretionary sector. While that may be a bit too contrarian for most investors to stomach, there is another angle worth exploring as well.

Necessity, someone once said, is the mother of invention. According to Google, Plato coined that phrase at some point in the 4th century B.C. The point, of course, is that we should never underestimate the power of creative minds when faced with real and pressing needs. New inventions may be conceived by gee whiz moments, but they are often only fully adopted when paired with painful problems.

While I don't yet know if we've hit a flashpoint in oil prices, it is very likely that we have. In an intensely competitive global economy, it is difficult for companies to raise their end prices to consumers. Eventually, they will walk out on you. (Incidentally, as the most open economy in the world, this may be one major reason why we haven't seen the big increase in our consumer price index the way other countries have. We have more choices.)

So, what's a company to do? Get more productive. Historically, energy and technology stocks have moved in opposite directions and perhaps that isn't a coincidence. Innovation may be on the upswing and investors should take note.

Kindest Regards,

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