

June 29, 2010

## What's a "Policy Error"?

*The market continues to agonize over potential mistakes from the authorities*

The indexes are trading at the May lows as this is written and fears of a double-dip recession (or worse) dominate the headlines. The economic numbers have softened lately so the pessimists have more ammunition than they had a couple of months ago, but the primary worry in the market involves potential "policy errors." That's the trigger for this note.

Policy is made by governmental authorities, whether local, national or at the central bank level. These outfits are populated by "policy makers", who have the power to create regulations, change tax rates, decide how much will be borrowed by government, and determine how much cash will be created. The last is the central bank function.

Not since the 1930's have the markets been so concerned about the performance of these non-market decision makers. Here's a short list of policy errors that keep investors on edge:

- The European Central Bank (ECB) fails to follow through on its plan to buy Eurobonds, which will support the European banking system.
- The Chinese authorities will go too far in their attempt to cool off their real estate market.
- The Federal Reserve tightens monetary policy too early.
- Regulatory reform of the financial sector fails to address the real problems exposed in 2008.

All these actions have one thing in common---they may trigger another recession---or a continuation of this one, depending on your view of the economy.

Investors are most comfortable when they know what the regulatory/tax/monetary environment will be. While there is always a certain degree of uncertainty about "policy", there's a lot more now than is normal.

Investors know how to analyze companies, but most of us know very little about the policy making world of the "authorities". And coming out of the crisis of 2008 there's very little agreement between governments about what to do to prevent a repeat performance.

At this point investors have little confidence that policy makers will get it right---they're human, so they never get it all right. But they hardly ever get it all wrong either.

As I indicated from London a couple of weeks ago, it is very difficult to be optimistic about the new world that needs to be built on the ashes of 2008. The markets and most of the economies of the world have recovered more strongly than most expected a year ago, but now what?

DOCK STREET ASSET MANAGEMENT

No one really knows, but we are not assuming that these problems take care of themselves. We are paying very close attention to our research sources in Montreal and Hong Kong for guidance in this area and we are ready to act quickly if a policy error develops.

What's happened in the market so far is the *fear* of a policy error, rather than a reaction to an actual event. We think, on balance, the authorities in various regions will get these decisions right enough for the world economy to pull through.

But we aren't complacent and we have plans in place in case things go wrong...again.

Best regards,



Daniel A. Ogden

[dogden@dockstreet.net](mailto:dogden@dockstreet.net)

DOCK STREET ASSET MANAGEMENT

263 Glenville Road • Greenwich, CT 06831

Main: 203.532.9470 - Fax: 203.531.0666

*Dock Street Asset Management, Inc. is an investment adviser registered with the U.S. Securities and Exchange Commission. You should not assume that any discussion or information contained in this letter serves as the receipt of, or as a substitute for, personalized investment advice from Dock Street Asset Management, Inc.*

*It is published solely for informational purposes and is not to be construed as a solicitation nor does it constitute advice, investment or otherwise.*

*To the extent that a reader has questions regarding the applicability of any specific issue discussed above to their individual situation, they are encouraged to consult with the professional advisor of their choosing.*

*A copy of our Form ADV Part II regarding our advisory services and fees is available upon request.*

*Our comments are an expression of opinion. While we believe our statements to be true, they always depend on the reliability of our own credible sources. Past performance is no guarantee of future returns.*