

Our regular readers know that we penned a piece in May 2000^{December 2004} titled “Deflationary Boom: Now or After Recession?” — in which we outlined the economic climate for the next decade, saying it would be characterized by high real GDP growth and productivity and low inflation and interest rates and that the Internet would set off a virtuous cycle of rising domestic demand, incomes, and wealth. This week we predict where the new job growth will come from.

Ten Sources of New Job Growth for the Decade

In this week’s commentary, we continue in the vein of our remarks last week on the positive outlook for growth in 2005. It seems that everywhere we’ve gone recently the talk has been about the loss of jobs and speculation on where new jobs will come from during the rest of the decade. So it seems apropos to discuss this topic as we peer into the future.

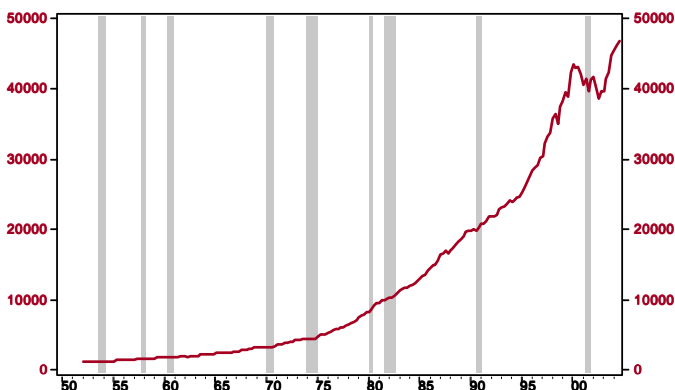
Capitalism, when underpinned with liberal democracy, is unique in its ability to allow individuals the freedom to create and innovate. Innovation tends to run in 50-year cycles. When it is implemented, the Schumpeterian phenomenon of job destruction and job creation proceeds at a rapid pace. In our commentary from May 2000, we discussed a virtuous cycle of demand that would ensue throughout the decade as the Internet strengthened its foothold in both business and consumer life. We hear frequently about one side of the phenomenon described by 19th century economist Joseph Schumpeter: job destruction. We have lost 2.8 million manufacturing jobs in the last four years. Most of these jobs have been lost to the combination of outsourcing and offshoring and the fact that the United States can no longer compete on price with low-cost Chinese manufacturing. No one expects us to; this is what is supposed to happen in a dynamic capitalist process. Jobs and skill sets obsolesce, and rote production gravitates to low-cost providers. But we hear less about the positive side: new jobs created. Except for an occasional news article or the monthly release of data from Manpower and the annual Bureau

of Labor Statistics *Occupational Outlook*, there are few daily articles in the financial press about job creation. This is the subject of this week’s commentary precisely because economists, strategists, analysts, portfolio managers, and chief investment officers alike cannot see where job growth will come from.

Wealth Creation

A few weeks ago, the Federal Reserve reported in its monthly flow of funds data that the United States had created 2 million more millionaires between 2002

Households, Nonprofit Organizations: Net Worth
Bil. \$



Source: Federal Reserve Board /Haver Analytics

and 2004. As the chart at left shows, total US household and not-for-profit net worth rose by \$5 trillion during the same period. Why did this happen? How did it happen, especially during a period of low M&A activity on Wall Street? Did the rich invest well and get richer? Did the average owner of real estate benefit from a sharp rise in prices and ultimately become a millionaire? Did portfolios invested in mutual funds and alternative investments perform positively? Since this particular measure includes both financial assets (stocks and bonds) and real assets (real estate, commodities, artwork, etc.), it is a bit of all of the above. The more interesting note is that this happened during a period when job growth was supposedly slim and economic growth was haltingly positive. So what do we conclude? *Wealth levels are rising because of the virtuous cycle of demand.* As wealth levels rise, the standard of living rises too, because those who have wealth create demand for new products and services that must be satisfied by the marketplace. You do not need to be among the ultra-rich to benefit from this phenomenon; you may gain merely by being a good saver or investing in real estate in the right area. As those with wealth can attest, the demand for services changes as one's wealth level rises. How does this work? Let's take the simple example of real estate

holdings: By investing in a primary residence, the price of that real estate has risen; financial innovation in products such as adjustable rate mortgages has allowed people to take "wealth" out of their homes and/or borrow against its value. When economists explain this phenomenon, they usually only talk about people consuming the equity in their homes, but many times the equity is invested in a second property or the asset is liquidated entirely and a new home in another less costly area of the country is bought, thereby freeing up capital to be spent or invested.

Construction

A total of 2.1 million new jobs were created in construction during the '90s. After a period of sub-par job growth, roughly 300,000 new jobs were created

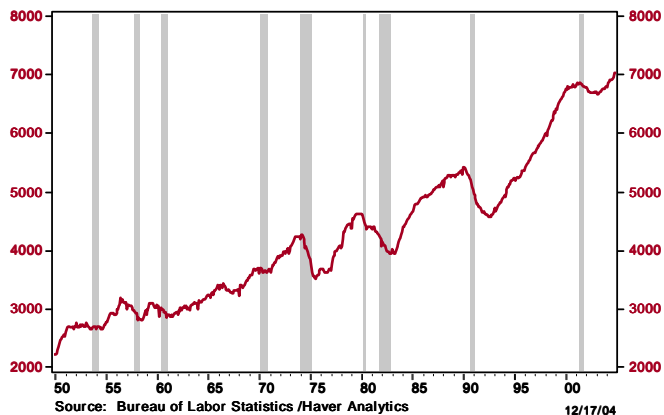
in construction in 2004. With demographics and wealth levels arguing for second homes, there are likely to be at least 2 million new jobs created in construction in this decade.

Trade, Transportation, and Utilities

What else to do with wealth but shop? Analysts during the Internet boom incorrectly predicted the dissolution of many brick-and-mortar retail outlets because they forgot that shopping is not just a necessary activity in the United States, it is also a leisure activity. Americans shop as a pastime. As wealth levels rise, they shop at specialty stores, boutiques, Internet outlets, and more. There is an endless supply of items that can be created to satisfy the desires of American consumers, who are the envy of the world. During the 1990s, 4 million jobs were created in the category the Labor Department calls trade, transportation, & utilities. This category

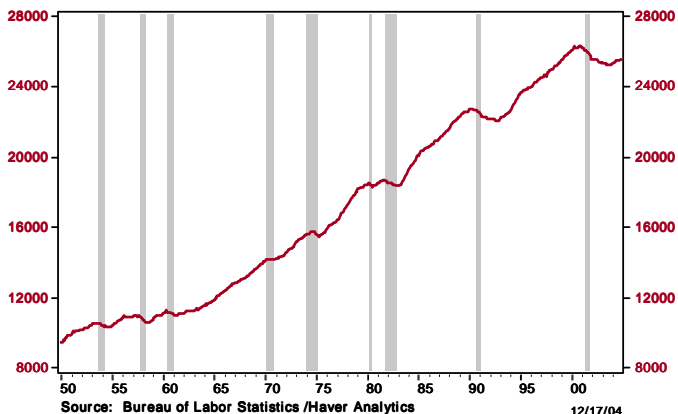
All Employees: Construction

SA, Thous

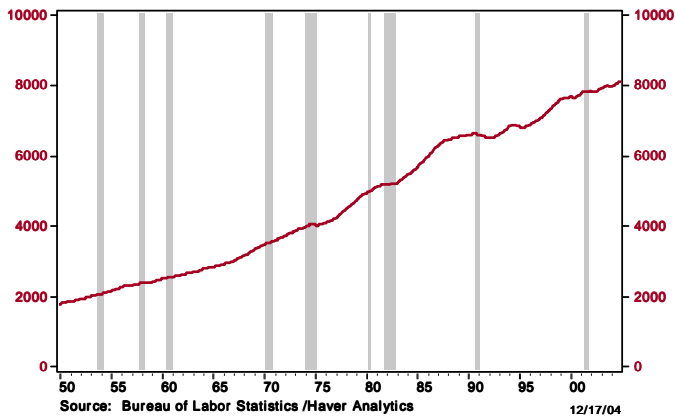


All Employees: Trade, Transportation & Utilities

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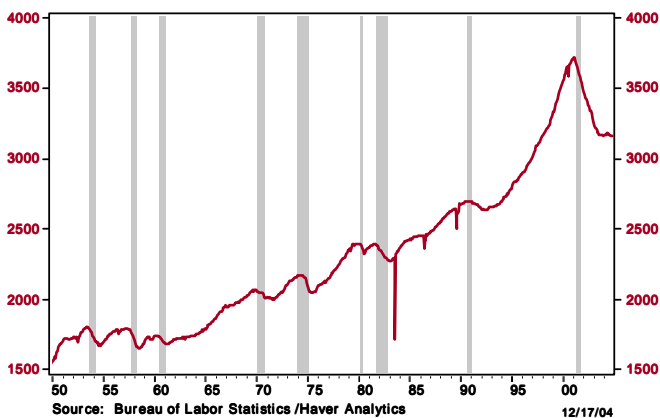
All Employees: Financial Activities
SA, Thous



financial advisers, tax experts, etc. Financial companies that serve these consumers will benefit. A total of 1.5 million new jobs were created in this category in the '90s and 300,000 were created in the last three years (note the job growth during a bear market). Expect at least another 2 million new jobs between 2005 and 2010.

Information Services

All Employees: Information Services
SA, Thous

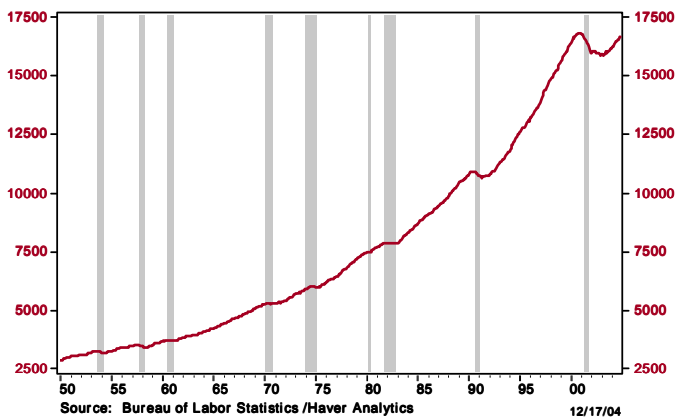


Jobs in information services also stand to rise smartly in this decade, as the greatest implementation of technology has yet to take place in small and medium localized service businesses and in the healthcare and construction industries. New medical technologies including interactive patient record systems are just starting to be implemented in major metropolitan areas.

Professional and Business Services

This brings us to one of our favorite topics: What do advanced societies do as their wealth rises? They demand more and more services. Why? Because daily tasks that they used to do themselves can be outsourced to other people. New jobs are created — from personal chefs and trainers to housekeepers and landscape architects. This requires the services of highly trained professionals of all kinds — life scientists, management consultants, lawyers, and accountants. Venture capital and private equity move to start-ups and new businesses, so those businesses grow and require new recruits. During the 1990s, 6 million jobs were created in professional and business services. Despite the hand-wringing over outsourced computer technicians and engineers, this category is set to show strong job growth for the rest of the decade as more and more people seek higher levels of education — lawyers and accountants as well as

All Employees: Professional & Business Services
SA, Thous



temporary workers. We expect 2 million new jobs to be created in this category.

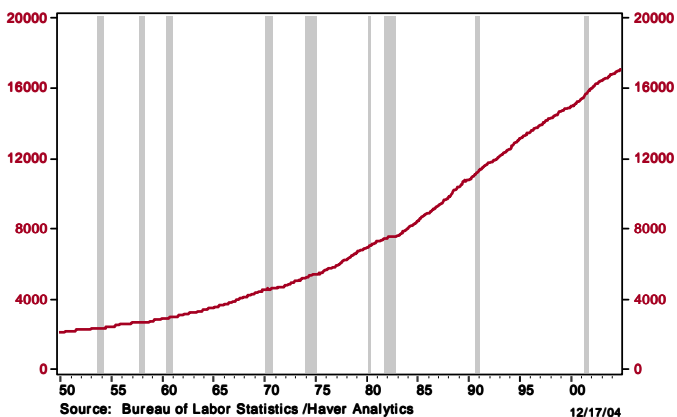
Education and Health Services

Of course, all of this job transition couldn't occur without the help of community colleges, higher education, outplacement consultants, psychologists, and coaches. Colleges and universities have been beneficiaries in many cases of large endowments and donations from successful graduates. These gifts are put to work in building construction and the establishment of new programs. As wealth levels rise in a society, so does the average level of education. This includes not only recent high school graduates, but also middle-aged baby boomers who decide to switch careers or get a degree they didn't previously have a chance to pursue.

This category also includes healthcare services, which as we all know will be in greater demand with an aging population. Higher levels of care and customized care will also be in demand. Five million new jobs were created in education and health services since 1991. In the last three years, 1.7 million new jobs were created. This category stands to grow by at least another 2 million in this decade.

All Employees: Education & Health Services

SA, Thous

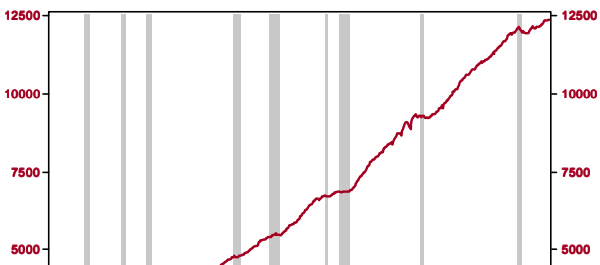


Leisure and Hospitality

This category includes performing arts, spectator sports, museums, amusements, and restaurants. Rising wealth levels increase the demand for recreation and entertainment. Jobs in this category grew by 2.7 million in the '90s and have already grown by 500,000 in the last three years.

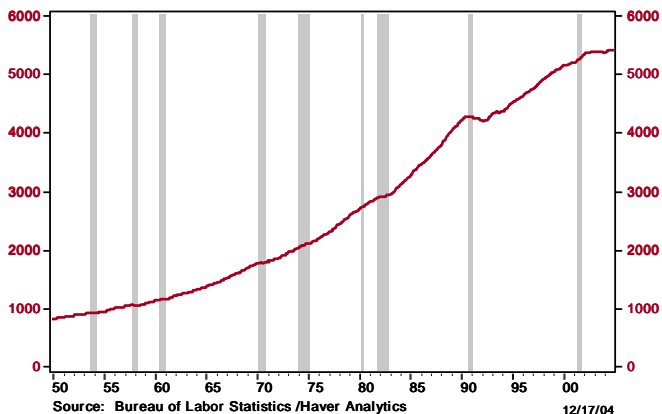
All Employees: Leisure & Hospitality

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All Employees: Other Services

SA, Thous



"Other Services"

The Bureau of Labor Statistics categorizes "other services" as a group that includes repairs and maintenance, personal and laundry services, and memberships and associations. Investment clubs offer information on managing wealth. Second homes need to be repaired and tended to. Growth in areas of the country where second homes are being built requires the requisite services to go along with them. One million jobs were created in this category alone in the last decade.

Hopefully, this commentary has given you a sense of what is currently going on in the country and what is possible in the next five years. We have not discussed government incentives to support this job growth, but they will surely come as a result of the upheaval that accompanies the Bush administration's "New Deal" and movement toward an ownership society for everyone.

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