

Weekly Commentary

May 18, 2009

The Markets

Human nature is just so – well, human. Yes, a sense of humor is required to survive as a stock market strategist, because the market is controlled by human emotions and we are all a bit off-center. Last week the S&P 500 had its worst loss since March. So what are folks doing now after the sell-off? Most are now questioning the nine-week rally and wondering if stocks got ahead of the outlook for the economy and the financial system. The answer is simple – of course they did, and that's what always happens because the stock market is looking ahead and attempting to discount the always-uncertain future. We stated last week in our Market Commentary that "the fact is that stocks have come a long way in a short period of time. Thus some additional caution and holding some buying power makes sense." We also stated that "the stock market is quite stretched-out for the short term."

Pullbacks are all part of normal market action, and we believe this one is creating buying opportunities. What we don't know at this time, is whether or not the market is correctly assuming that the economy will bottom in the next several months and will be doing moderately better by year-end. We believe that assumption is correct, but if not, the wait will be longer before the market will be able to sustain further solid upside. Investors are starting to look for positives and to ignore negatives. The current mood reminds us of the optimistic 10-year-old who, to test his optimism, was given a bag of horse manure for Christmas. Last seen, he had a big smile on his face as he ran around looking for his pony. We believe there is more good news (ponies) to come.

Over the weekend, Lawrence Summers, Director of the National Economic Council, said the economy is no longer in free fall. The facts back him up. The New York Federal Reserve Bank's May Empire State Manufacturing Index increased to -4.55 from -14.15 in April. While this number is still negative, indicating contraction, it was the best reading on this measure in nine months. Also, the April Industrial Production Index declined 0.5% after dropping 1.7% in March. And there was further good news as the May Michigan Consumer Sentiment Index increased to 67.9 from 65.1 in April. Pullbacks are a challenge for all investors due to human nature. Folks are happy and optimistic when the stock market is going up but unhappy and pessimistic when it's going down. Because we believe the economic outlook is improving and the supply/demand ratio for stocks is bullish, we advise using this pullback as a buying opportunity. Like the optimistic 10-year-old, we advise believing that a pony is out there - but be careful where you step.

Index Performance Statistics – May 15

Index	Close	Change	% Change	% YTD Change	52 Wk % Change
DJIA	8268.64	-62.68	-0.75	-5.79	-36.33
NASDAQ	1680.14	-9.07	-0.54	6.54	-33.56
S&P 500	882.88	-10.19	-1.14	-2.26	-38.06

Source: Bloomberg

*Price return — does not include dividends

US Housing Starts, Permits Hit Record Lows in April

New U.S. housing starts and permits unexpectedly fell to record lows in April, a government report showed on Tuesday, denting hopes that stability in the housing market was imminent.

The Commerce Department said housing starts fell 12.8 percent to a seasonally adjusted annual rate of 458,000 units, the lowest on records dating back to January 1959, from March's upwardly revised 525,000 units. Compared to the same period last year, housing starts tumbled 54.2 percent.

Analysts polled by Reuters had expected an annual rate of 520,000 units for April.

New building permits, which give a sense of future home construction, dropped 3.3 percent to 494,000 units, the lowest since records started in January 1960, from 511,000 units in March. That was well below analysts' estimates of 530,000 units. Compared to the same period a year-ago, building permits plunged 50.2 percent.

Building completions rose 4.9 percent to 874,000 units.

Last Week

After nine weeks of smooth highway driving, the rally hit a pothole. The retreat of the market began as investors responded to the lower than expected April advanced retail sales figures with broad-based selling. Commentary regarding a slower economic recovery from the Bank of England and Nobel Prize winning economist Paul Krugman saying the world economy could face a protracted slowdown gave reasons to take profits. The market did see some improvement later in the week on better than expected earnings reports and improvements in measures of liquidity, decreasing to levels not seen since the credit crisis began.

Beyond the news reports, technical signals had been flashing that the market is overbought. At this juncture, many Wall Street "gurus" believe we are due for a pullback of some kind after the sharp advance from the March low. The degree of the pullback among them varies, depending on their view of the type of rally we've experienced. However, most agree that confirmation of the rally being something more would be a move by the S&P 500 above its 200-day moving average, currently around the 945 level.

Weekly Focus – Think about it

"Sometimes your best investments are the ones you don't make."
-Donald Trump

Best Regards,

Jim, Aaron & Angela
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- * The Dow Jones Industrial Average is a price-weighted index of 30 actively traded blue-chip stocks.
- * The NASDAQ Composite Index is an unmanaged, market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System.
- * Bloomberg is the source for any reference to the performance of an index between two specific periods.
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- * Past performance does not guarantee future results.
- * The Markets prepared by Al Goldman, Chief Market Strategist, Wachovia Securities 5/19/09.
- * Last Week cited from Dean Meehan, Market Analyst, Wachovia Securities 5/15/09.
- * US Housing Starts cited from Lucia Mutikani, Reuters 5/19/09
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