



## Weekly Commentary June 1, 2009

### The Markets

Our Market Commentary last week was titled “A Show-Me Market” because we believed the market would need better economic news rather than “less bad” to rally. The market had been churning/consolidating for two weeks correcting the prior nine-week, 39% rally by the S&P 500, and probably waiting for some positive economic data. Well, the market got what it wanted, and it did rally. April existing-home sales increased 2.9% following a 3.4% decline in March, and new-home sales increased 0.3% after a decrease of 3.0% in March. Probably the best news was that the May consumer confidence index jumped to 54.9 from 40.8 in April. This strongly supports our opinion that the recession will hit its trough by late summer and will be growing modestly by year-end. Also, the first-quarter real GDP decreased at a 5.7% annualized rate, not the 6.1% annual rate estimated a month ago. All in all, economic reports this past week were fairly good, not just “less bad,” and the stock market responded as it should.

This week the stock market will have to deal with some additional mixed news. It was reported Monday, June 1, that April personal income rose 0.5% following a 0.3% decline in March, and April personal spending decreased 0.1%. On Friday, we get the May nonfarm payrolls report that is expected to show 520,000 jobs lost versus 539,000 in April, and the unemployment rate is expected to rise to 9.2% from 8.9% in April. Unemployment is a lagging economic indicator and will likely stay negative for a year or longer after the end of this recession. So, once again, the mettle of the market will be tested as the economic news shifts back to “less bad.” Investors increasingly have their eyes on the stars and not on the numerous potholes at their feet.

Last winter we stated that it was time to buy “straw hats” – stocks – when few wanted them, and thus prices were very attractive. Well, summer is officially only three weeks away, and the price of straw hats and stocks are up sharply. Despite our bullish stance on the stock market and optimism about the economy, we advise investors to be a bit cautious. Both the DJIA and the S&P 500 are back up, close to recent highs and extended. This does not mean that the stock market cannot go higher from here. We believe it does mean that the risk/reward ratio for new purchases has become dicey. We continue to favor quality growth companies in the technology, oil-service, health care, biotech and discount-store sectors. However, we would not chase stocks up here and would hold back some buying power, in the 20% range. If the market defies gravity, our readers will participate. Having some cash available to buy straw hats – stocks – on sale makes investment sense at this time.

## Index Performance Statistics – June 1

Index	Close	Change	% Change	% YTD Change	52 Wk % Change
DJIA	8721.44	+444.12	2.60	-0.006	-30.99
NASDAQ	1828.68	+136.67	8.07	15.950	-27.50
S&P 500	942.87	+55.87	6.29	4.390	-32.67

Source: Bloomberg

\*Price return — does not include dividends

## Changes to the Dow Jones Industrial Average

The Dow Jones Industrials will sport a new look beginning Monday June 8th, With General Motors officially declaring bankruptcy on June 1<sup>st</sup>, the longtime component of the Dow (originally added in 1925) had to be replaced. The newest member replacing GM is the insurance company Travelers, ticker symbol TRV.

In addition to the GM deletion, Citigroup is also being replaced by Cisco Systems, symbol CSCO. Cisco Systems becomes just the second stock from the NASDAQ to break into the Dow Jones Industrials. Microsoft, the first stock was added on November 1, 1999.

## Last Week

Better economic data drove the train this week as the market ended in positive territory. This helped the S&P 500 extend its monthly winning streak to three, the longest since 2007. Kicking off the bullish action was the May Consumer Confidence number, which jumped to 54.9, up from the previous month's reading of 40.8 and the consensus expectations of 42.6. The revised first quarter GDP report was also better than expected. This positive news gave investors optimism the worst of the recession may be behind us.

However, amongst the positive reports, there were reminders the economy is still in recession. On Wednesday, the FDIC reported there were 305 "problem" banks with an aggregate \$220 billion in assets as of the end of the first quarter. Also looming is that General Motors is expected to enter Chapter 11 on Monday. The market will likely weigh on the speed at which the government can turn the troubled automaker's current predicament.

Furthermore, as we resolve our current issues, new ones have begun to creep into the market. The first is the rise of the yield on the benchmark 10-year Treasury note, which touched 3.73% mid-week. The fear is that as the Fed sells more Treasuries the yields will have to move higher. If yields move higher, it could impact mortgage rates, thereby impeding the government's attempt to shore up the housing market. Another worry is that an increase in the money supply could cause inflation. However, Gary Thayer of the Wachovia Capital Markets Economics Group notes that it's not just an increase in the money supply that spurs inflation; it is also spending it. Given the slow growth of credit available, individuals and corporations have less to spend. Therefore, he believes inflation is likely to remain low during the next year.

Next week there is a full calendar of data releases scheduled that could determine if the rally gains steam or runs off the track. These include the Personal Spending and Income reports, the

May ISM Manufacturing, Vehicle Sales and the always widely anticipated employment report. On the job front, current expectations are for non-farm payrolls to show another 550,000 jobs were lost in May and the unemployment rate to rise to 9.2% from 8.9% in the prior month.

At this time, it appears investors are split fairly evenly between the bullish and bearish camps. The recent investor sentiment reading showed around 40% of investors are bullish compared to 48% bearish, according to the American Association of Individual Investors. This appears consistent with the action over the last three weeks as the upside to S&P 500 index was constrained by its May 8 high and the 200-day moving average, while the downside has found support around the 880 level.

## **Weekly Focus – Think about it**

“Timidity prompted by past failures causes investors to miss the most important bull markets.”  
~ Walter Schloss

Best Regards,

Jim, Aaron & Angela  
Kennedy Financial Services

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\* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

\* 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.

\* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

\* This commentary should not be considered individual investment advice and you should consult your financial professional before making any investment decision.

- \* You cannot invest directly in an index.
- \* Past performance does not guarantee future results.
- \* The Markets prepared by Al Goldman, Chief Market Strategist, Wachovia Securities 5/26/09.
- \* Last Week cited from Dean Meehan, Market Analyst, Wachovia Securities 5/22/09.
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