Weekly Commentary
August 10, 2009

The Markets

The most dangerous stage of any bull market is when the general mood is one of euphoria and money is almost thrown at stocks. We are not at that stage, not even close. What we do have is a market up 50% from the S&P 500 lows made March 9, a big increase in the bullish camp and a big drop in the bearish camp. Stock market action had started to look tired for several sessions until the very pleasant surprise provided Friday by the employment data. July non-farm payrolls decreased 247,000, less than expected, and the unemployment rate dropped to 9.4% from 9.5% in June and below the widely expected 9.6%. This is further evidence that the recession is probably “going, going, gone,” as we titled our Market Commentary last week. We also stated that the “easy” part of the rally was over. After the good employment news and the market’s solid advance Friday, should we become even more bullish and not at all short-term cautious?

As a market strategist, we must be flexible and respond to changes in market behavior. But, if we are too flexible, we run the risk of being whipsawed. So let’s sit back and think about why the market has been so strong since March 9. We believe the strength came from anticipation of improved economic news, the probable end of the recession and a very bullish supply/demand ratio for stocks. Well, the good economic news is now on the table, and a growing number of economists agree with us that the recession is over. The next major uncertainty facing investors is how strong the economy will be in 2010. We believe the economy will experience a moderate recovery next year, with modest inflation. Some believe that after a recovery we will have another recession - which is defined as a “W” type recovery - but this fear is not unusual as a recession ends.

There are a number of other uncertainties facing investors as well. The health-care bill will continue to receive a great deal of attention and concern. We believe a bill will be passed this year, but a much more moderate version than the initial plan. Also, we expect some political drama over how to regulate the financial system and what to do about too-big-to-fail financial institutions. However, there are always lots of things to worry about, and bull markets do climb a “wall of worry.” Although the good economic news is now old news, we still have the very bullish supply/demand ratio for stocks to support a higher market. Labor markets should continue to improve, but in a stair-step fashion. Improved employment will create additional buying power and make consumers feel more confident, and thus more willing, to spend money. We believe Iran will probably continue to grow as a threat to the world, but this fear is widely shared; a military solution, if it comes to that, should only be a short-term problem for the market. With the improving economy, cyclical stocks should do well. Meanwhile, there is some optimism in the stock market, but not euphoria. So enjoy, but don’t mortgage the farm!

Index Performance Statistics – August 10

Index	Close	Day Change	Day % Change	% YTD Change	52 Wk % Change
DJIA	9337.95	-32.12	-0.34	6.40	-20.75
NASDAQ	1992.24	-8.01	-0.40	26.33	-18.35
S&P 500	1007.10	-3.38	-0.33	11.50	-22.85

Source: Bloomberg
**Price return — does not include dividends*

U.S. Productivity Surges, Inventories are Lean

U.S. output per worker rose at its fastest pace in six years during the second quarter as businesses wrung more from shrinking staff in a sign that recovery from recession will be slow and unlikely to create a surge in hiring.

A Labor Department report on Tuesday showed nonfarm productivity, a gauge of hourly output per worker, jumped at a 6.4 percent annual rate, the sharpest since the third quarter of 2003 after a 0.3 percent gain in the January-March quarter.

"The bounce in productivity is another indication that the nasty U.S. recession is drawing to a close. The bad news is, however, that firms are still reluctant to hire," said Harm Bandholz, an economist at UniCredit Markets and Investment Banking in New York.

Last Week

The market continued to act well this week as the economic data showed further signs that the door on the recession may be closing. In addition to positive reads in manufacturing and housing, the unemployment rate for July unexpectedly fell to 9.4% from 9.5% in the prior month. Furthermore, the non-farm payrolls showed 247,000 jobs were lost last month, less than the consensus call for 325,000, and the prior reading was revised lower to 443,000 from 467,000. As a result, the S&P 500 index extended its current winning streak to four weeks.

In the coming week, investors will look for more reasons for the market to rally further off the March lows. From a technical perspective, this would be a “break on through” and hold above resistance, currently at 1000 on the S&P 500 index. However, with technical indicators such as the Relative Strength Index suggesting an overbought market, we could see some form of consolidation or correction. The Market Analysis team at Wells Fargo Advisors also thinks the market has gotten extended. In their opinion, the market taking a breather in the near-term would be a good thing as it would work off some of the recent excess, improve the health of the market and produce more attractive stock prices.

Next week there will be several data points that could make the bulls try to run or try to hide. These include updates on productivity, labor costs, retail sales, inflation and consumer confidence. Although it is not expected that the Fed will change interest rates on Wednesday following its FOMC rate decision meeting, investors will look for comments to compliment the recent positive data. On the earnings front, it will be back to school with scheduled reports from retailers Kohl’s, Nordstrom, Abercrombie, J.C. Penney, Macy’s and Wal-Mart. Other companies of note with quarterly profit updates include Applied Materials, Dr. Pepper Snapple, Pan American Silver and TheStreet.com.

Yes, Virginia, it looks like we're "breaking on through to the other side" of the recession. The positive second-quarter earnings tallies and economic data have helped the market lift about 50% from the March lows. However, with a market that appears extended in the near-term and the dog days of summer here, we could see some profit taking as Wall Street heads to the Hamptons for vacation. Therefore, we continue to recommend that investors review their portfolios to make sure current investments align with their investment objectives and risk tolerance.

Weekly Focus – Think about it

"Look at market fluctuations as your friend rather than your enemy; profit from folly rather than participate in it."
~ Warren Buffett

Best Regards,

Jim, Aaron & Angela
Kennedy Financial Services

* 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 e consider 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, Wells Fargo Advisors 8/11/09.

*U.S. Productivity Surges: cited from Reuters by Lucia Mutikani 8/11/09

* Last Week cited from Dean Meehan, Market Analyst, Wells Fargo Advisors 8/7/09.

* The opinions expressed here reflect the judgment of the authors as of the date the report and are subject to change without notice.

* This report was prepared by VSR Financial Services, Inc. Wealth Management Department.