



Weekly Commentary January 19, 2010

The Markets

The stock market was closed Monday in honor of Dr. Martin Luther King, Jr., but there will be lots of big “doings” in only four market sessions. Our nation will be focused on the Senate race in Massachusetts Tuesday as it holds major implications for the political environment. How much of a stock market factor it will be, no matter who wins, is unknowable. With the President’s State of the Union Message due Wednesday, January 27, the widely debated health care bill will receive maximum attention. Both of these are big-time stuff for the stock market to deal with. So what is a mere mortal, market strategist to do? One aspect of our job is clear at the moment and that is what we believe to be the long-term outlook for stocks. The economy is recovering slowly, and stocks appear reasonably priced, overall. Thus, we remain long-term bullish on the outlook for the stock market the rest of 2010.

The difficult problem relates to the short term. Most investors should not even worry about short periods like several weeks, but most do. We Americans are very impatient, and seeking almost instant gratification is a too common personality trait for most of us. The long-term outlook is based on fundamentals, the mood of investors and the amount of money available to buy stocks. All of these factors appear positive at this time. An opinion of the very short-term market outlook is, at best an educated gut feeling and we hope that the feeling is educated. Our gut feeling is a bit nervous. The main reason is that the stock market last week had to struggle to rise modestly and then was hit hard last Friday, January 15. This was a personality change in market action since the steady rise from mid-December, and personality changes must be respected.

Also, optimism in the stock market has risen sharply with the bullish camp way up and bears way down. We would not sell good stocks and we would remain bullish. The economic news last week continues to confirm that the economy in 2010 will be up moderately, and inflation should not be a problem. It was reported that industrial production increased modestly in December and consumer sentiment improved slightly. However, retail sales in December declined 0.2% after rising 1.8% in November. The December leading economic indicator index due Thursday is expected to rise 0.7%. This would be the ninth consecutive monthly increase. The economic data, plus a very good stock market since March 9, keep us bullish long term. The reason for stating our “gut” short-term cautious opinion is to provide some direction for very aggressive traders and to keep long-term investors from getting too concerned about a possible normal correction. It is important to remember that the stock market has experienced a very big party since March 9, 2009.

Index Performance Statistics – January 15

Index	Close	Day Change	Day % Change	% YTD Change	52 Wk % Change
DJIA	10609.65	-100.90	-0.94	1.74	28.12
NASDAQ	2287.99	-28.75	-1.24	0.83	49.61
S&P 500	1136.03	-12.43	-1.08	1.88	33.63

Source: Bloomberg

*Price return — does not include dividends

Record Cash Means S&P 500 at Half its 2007 Valuation

U.S. companies are producing more cash than ever, making the Standard & Poor's 500 Index cheaper than any time since credit markets froze just as investors say profits don't justify higher prices. While the 68 percent rally since March drove price-earnings ratios to the highest level since 2002, when measured by cash flow the index is 37 percent below the 12-year average and half its valuation of 2007, data compiled by Bloomberg show.

More investors are focusing on cash at a time when earnings are being skewed by \$1.7 trillion in global bank losses and writedowns and nine straight quarters of declining profits. Net income for the S&P 500 tumbled 67 percent for the year ended in September from the same period in 2007, while cash flow climbed 29 percent, according to data compiled by Bloomberg. "The market is still fairly to cheaply valued and represents the opportunity for gains," said Burt White, chief investment officer at Boston-based LPL Financial Corp., which manages \$269 billion. "Valuations on a cash flow basis indicate a market that is poised for continuations on recent gains."

Last Week

After a good start to 2010, the bull's patience was tested this week. Initially, equities extended recent gains on positive economic data and an anticipated positive start to earnings season. However, China's decision to raise its banks' reserve requirements to slow down its economy weighed on commodity-related stocks on concerns it would dampen demand. More importantly, earnings season had an inauspicious start as reports from Alcoa and JPMorgan were disappointing relative to expectations. As a result, the S&P 500 index moved into negative territory for the week during Friday's session.

Markets were closed on Monday in observance of the Martin Luther King holiday. However, it will still be a busy week on Wall Street. Specifically, earnings season gets into full swing with 66 companies in the S&P 500 index scheduled to report. Following the grilling on Capitol Hill and JPMorgan's disappointing earnings, particular attention will be paid to the financials with Citigroup, Bank of America, Morgan Stanley, and Goldman Sachs all scheduled to report next week. Outside of the financials, the notable companies on the calendar include IBM, Google, General Electric, eBay and Schlumberger. On the economic front, there will be updates on housing, inflation and manufacturing.

The recent sentiment readings would suggest the market may be vulnerable to a pullback. According to the weekly Investor's Intelligence poll, a contrarian indicator, the percentage of bulls increased to 53.4%, the highest level since December 2007. This compares to the 15.9% of newsletter writers who are bearish. From a technical perspective, the Wells Fargo Market Analysis group sees near-term support for the S&P 500 index at the 1120 level.

Weekly Focus – Think about it

“Those who cannot remember the past are condemned to repeat it.”
~ George Santayana

Best Regards,

Jim, Aaron & Angela
Kennedy Financial Services

Securities & Advisory Services offered through VSR Financial Services, Inc.
A Registered Investment Adviser and Member FINRA/SIPC
Kennedy Financial Services is Independent of VSR.

- * 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, Wells Fargo Advisors 1/19/10.
- * Record Cash Means: cited from Bloomberg by Alexis Xydias & Rita Nazareth 1/19/10
- * Last Week cited from Dean Meehan, Market Analyst, Wells Fargo Advisors 1/15/10.

* 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.