

# Weekly Commentary

## June 21, 2010



### The Markets

Last week's economic news was as mixed. The good news is industrial production and capacity utilization continue to move ahead while inflation is nowhere on the intermediate time horizon. The bad news is housing will continue to be a drag as the economy grows at a slower pace in the second half of the year. Industrial production in May rose 1.2%, well above the consensus estimate. Capacity utilization continued its climb toward 75% with the manufacturing segment remaining in the low 70s area. There is still plenty of excess capacity in the U.S. and global economy. That tends to keep a lid on inflation and will only change with a significant increase in demand from current levels, which we do not see in the next few quarters. Both CPI (Consumer Price Index) and PPI (Producer Price Index) were reported last week. The headline reading for CPI fell 0.2% while headline PPI dropped 0.3% in May. Energy prices were the main reason behind the drop. Core inflation (which excludes the food and energy components) at the consumer level rose 0.1% and rose 0.2% at the wholesale level. As we have said in the past, it is likely a number of FOMC members are worried more about deflation than inflation at this point. This week's two-day FOMC meeting (Tuesday and Wednesday) is highly unlikely to produce any change in interest rate targets or post-meeting press release language.

A number of housing indicators are deteriorating synchronized with the expiration of government tax credits. Market participants had hoped the housing recovery would continue after government supports were removed. Interest rates on 15- and 30-year fixed mortgages are at or near all-time lows. Last week's NAHB (National Association of Home Builders) sentiment survey dropped to 17 in May from the prior month's reading of 22. That probably explains why housing starts plunged more than 10% on an annual basis in May, well below market expectations. Builders are hesitant to start the construction of new homes in the face of less government subsidies. We look for stabilization in the volume and pricing of homes but at low levels in coming months. With high unemployment and stagnant wage growth, it is unlikely housing will be a primary economic driver any time soon.

### Index Performance Statistics – June 21

Index	Close	Day Change	Day % Change	% YTD Change	52 Wk % Change
DJIA	10442.41	-8.23	-0.08	0.14	25.22
NASDAQ	2289.09	-20.71	-0.90	0.88	29.61
S&P 500	1113.20	-4.31	-0.39	-0.17	24.65

Source: Bloomberg

\*Price return — does not include dividends

## **GM said to Prepare IPO Plan with Treasury Selling 20%**

General Motors Co. is preparing for an initial public offering that would sell 20 percent of the Treasury's stake in the automaker and reduce the U.S. to a minority owner, said two people familiar with the plan. The aim is to sell a fifth of the government's 304 million shares, said the people, who asked not to be identified revealing private discussions. That would reduce the Treasury Department's stake to less than 50 percent from 61 percent now. Final decisions on which owners will sell how many shares haven't been made and may change, the people said.

A registration statement may be filed in August, aiming for a November stock sale, said four people familiar with the plan. The sale will probably raise \$10 billion to \$15 billion, depending on the company's performance, the strength of the economy and the health of the IPO market, the people said. An August filing means Detroit-based GM could have the IPO ready around the time of the Nov. 2 congressional elections, said the people. If Treasury can sell enough shares, President Barack Obama could help other Democrats running for office by arguing that his administration's restructuring of GM is paying off, said Joe Phillippi, president of AutoTrends Consulting. "The government wants a successful offering soon so they can say that they took the company through bankruptcy, turned it over to independent management and are taking it public," said Phillippi, who is based in Short Hills, New Jersey. "This would be part of the campaign spin."

## **Last Week**

This week, investors tried to read the signs to determine the market's direction. Initially, the bears appeared to be in the driver's seat as stocks fell after a Moody's downgrade of Greece's credit rating to junk status, complemented by disappointing housing data and earnings from FedEx and Best Buy. However, the bulls got a chance to get behind the wheel as the manufacturing reports here and abroad came in ahead of expectations and Spain's debt offering was well received by investors. As of Friday morning, the S&P 500 index moved back into positive territory for the year on the heels of gains for a second consecutive week.

In fixed income markets, Treasuries traded in a narrow range but managed to post gains on the week. Mixed economic data brought bids to government bonds following Thursday's lower-than-expected Philadelphia Fed manufacturing number. In the corporate sector, British Petroleum saw heavy volume. The company's bonds traded off their recent low following the announced \$20 billion contribution to an oil spill fund and suspension of its dividend. For next week, keep an eye on the appetite for the auctions of two-, five- and seven-year Treasury notes totaling \$162 billion.

After two weeks of gains, investors will look to next week's economic data for more bullish signs for stocks. Given consensus expectations for no change in rates, pay attention to directions given by the Fed following Wednesday's conclusion of the Federal Open Market Committee Meeting. On the housing front, the May new home sales are projected to fall 18.7% month over month. The decline is likely a result of the expiration of the home buyer credit at the end of April. Other data points of interest include updates on durable goods and consumer sentiment.

With the end of second quarter quickly approaching, near-term market action could start to be influenced by earnings expectations. Currently, Wall Street projections see earnings for the S&P 500 index to rise 27% versus a year ago, according to Thomson Reuters. Next week, several companies are scheduled to report which may provide indications of whether the bar has been set too high. Of particular interest will be earnings tallies from Walgreens, Nike, Research in Motion, Accenture, Oracle and Adobe.

## Weekly Focus – Think about it

“A business like an automobile, has to be driven, in order to get results.”  
~ B.C. Forbes

Best Regards,

Jim, Aaron & Angela  
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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 Scott Freeman, Chief Equity Strategist, Wells Fargo Advisors  
6/22/10.

\*GM said to Prepare IPO: cited by David Welch & Jeff Green - Bloomberg 6/23/10

\* Last Week cited from Dean Meehan, Market Analyst, Wells Fargo Advisors 6/18/10.

\* 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.