



## Weekly Commentary February 22, 2011

### The Markets

Although last week's commentary focused on our belief that a couple of bricks had been removed from investors' wall of worry, we also pointed out that it would be naïve to dismiss the Middle East as a bygone risk after Egyptian President Mubarak's resignation. We said that things were far from settled in that country and high-profile copycat protests were taking place in other North African and Middle East countries. It turns out we were right: During the past seven days, we've seen the region's level of violence increase to another level. On Monday, February 21, CNBC even carried special coverage of the weekend's violence – especially in Libya, where an estimated 200 lives were lost. The implications for financial markets are obvious: With the violence spreading to countries where oil supplies are in harm's way, oil has spiked back above \$90 per barrel and gold has accelerated its rise as it serves as a safe haven. However, the stock market has continued to climb the wall of worry even as more bricks are seemingly being added with each passing day.

Stocks shrugged off the negatives last week and rose to multiyear highs, extending their winning streak to a third consecutive week. This has been a good example of how strong momentum and ample liquidity can continue to power a market higher in spite of a worrisome environment. The Dow Jones Industrial Average (DJIA) reached its highest level since June 2008 and rose 1% for the week. *The Wall St. Journal* pointed out over the weekend that the DJIA has now gained 4.6% during the last three weeks – its best such performance since August 2010. The S&P 500 also rose 1.0% and doubled from its March 2009 intraday low. *Barrons'* noted in its February 21 edition that it was the quickest doubling of the index since 1936.

Fed Chairman Bernanke took square aim at his critics at the G-20 meeting last Friday by defending the U.S. quantitative easing policy and rejecting critics who say that it is the sole reason for rising global inflation and may create asset bubbles. Bernanke declared that "spillovers can go both ways," implying that resurgent emerging economies have contributed to global commodity price increases. He also pointed out that nothing is stopping authorities in these fast-growing countries' economies from making policy adjustments to slow their expansion.

China's battle with inflation was back on the front pages as its central bank raised the reserve requirements for banks for the second time this year. *Barron's* reported it was the eighth time since 2009 that the requirement has been raised; it now stands at 19.5% - among the world's highest. Because of fears that these increases may slow global growth, such announcements in the past have tripped up the stock market, but it was not much of a factor last Friday.

Not surprisingly, Washington's deficit reduction talks got off to a slow start, and bipartisan negotiations are already running into roadblocks. Budget-cutting flare-ups have also escalated on the state level as they battle their own budget crunches. Celebrations of the Green Bay Packers' Super Bowl victory may now seem like a distant memory in Wisconsin as mass protests by state workers are taking place in response to Republican lawmakers' efforts both to get them to ante up more toward their benefits costs to keep jobs from being cut and to put limits on workers' bargaining powers.

This week is light on important economic releases, so the market will be left to its own internal dynamics, and we will see if investors seek out more safe-haven assets given the spreading

protests and violence overseas. The aforementioned risks point out that the market is subject to little room for error. The monthly Bank of America Merrill Lynch Global Fund survey reported its highest bullishness level in its 10-year history, signaling that the big money is onboard. Individual investors continue to come slowly back into equities as the streak of consecutive weekly inflows has now reached six. The Chicago Board Options Exchange (CBOE) Volatility Index (VIX), a measure of investor fear, has hovered near multiyear lows for the past two months – a sign of investor complacency. Our opinion is that the upheaval and violence in foreign lands could be the linchpin for a meaningful move higher in volatility, as evidence by the DJIA's 178-point decline Tuesday, tied to the unrest in Libya. While markets do climb walls of worry, occasionally they stumble on some of the bricks. This is no time to panic.

## Index Performance Statistics – February 22

Index	Close	Day Change	Day % Change	% YTD Change	52 Wk % Change
DJIA	12219.79	-178.46	-1.44	5.49	18.77
NASDAQ	2756.42	-77.53	-2.74	3.90	24.53
S&P 500	1315.44	-27.57	-2.74	3.90	24.53

Source: Bloomberg

\*Price return — does not include dividends

## Libya Revolt Widens as Expatriates Flee, Qaddafi Vows to Fight

Governments rushed to evacuate thousands of expatriates from Libya as army units defected and a former aide to Muammar Qaddafi warned that the spreading revolt may topple the regime within days. The U.S. has chartered a ferry that will take American citizens from the Libyan capital, Tripoli, to Malta today and Turkey said it has mounted the biggest evacuation in its history to remove some 5,000 nationals by sea and air. U.K. Prime Minister David Cameron said getting British citizens out of the Libya is the top Foreign Office priority, as his government deployed a Royal Navy frigate near Libya to help.

The evacuations follow Qaddafi's warning in a televised speech late yesterday that he will fight the uprising until his "last drop of blood." Heavy gunfire broke out again in Tripoli today and the streets were empty, the Associated Press said. Army units in Benghazi and Tobruk have defected, leaving the eastern port cities under the control of Qaddafi's opponents, his former chief of protocol Nuri al-Mismari said.

While Middle East rulers have tried to put down uprisings that have overthrown leaders in Tunisia and Egypt and spread to Bahrain and Yemen, none used as much force as the Libyan ruler. Qaddafi's crackdown on the week-long demonstrations has already left almost 300 dead, according to Human Rights Watch, and driven oil prices to a 2 1/2-year high. Libya holds Africa's largest oil reserves.

## Last Week

What a difference 710 days makes for the markets. Stocks gained this week on better-than-expected earnings from the likes of Dell (DELL \$15.33) and Deere (DE \$95.26). Also encouraging was the continued investment banking activity with the announced \$7.7 billion buyout of Family Dollar (FDO \$52.67) by private equity firm Trian Group and spinoffs by Marriott (MAR \$40.96) and Williams Company (WMB \$30.08). In addition, positive economic news on housing and manufacturing as well as the Fed's increased 2011 growth projections bolstered the bulls to look past inflation fears and the unrest in the Middle East. As of Thursday's close, S&P 500 index was up 0.85% for the week and has advanced over 100% from the bearish extremes of the intra-day low of 666.79 set on March 6, 2009.

The question heading into Presidents Day weekend is whether the pendulum of investor sentiment has swung to a bullish extreme, potentially setting the market up for a pullback. Reaction to the scheduled economic data next week could provide the answer with several releases of interest including updates on housing, durable goods and consumer confidence. Projections for Friday's second look at fourth quarter GDP is for a modest uptick to 3.3% from the initial reading of 3.2%. Along with the data, speeches by Fed presidents Kocherlakota, Plosser, Hoenig and Bullard and Treasury auctions of 2-, 5- and 7-year notes totaling \$99 billion will garner attention.

Fourth-quarter earnings season comes to an "unofficial" end with Wal-Mart's (WMT \$54.75) report on Tuesday. To date, of the 387 companies in the S&P 500 index with results on the books, 72% reported earnings ahead of consensus estimates, according to Bloomberg. In addition, earnings are up 36% year-over-year, driven by the financials, materials and energy sectors. Along with Wal-Mart posting profits we will get releases from fellow retailers including Target (TGT \$53.15), TJX (TJX \$49.20), Sears (SHLD \$92.76), Home Depot (HD \$38.18), Lowe's (LOW \$26.14), Macy's (M \$24.06), JC Penny (JCP \$36.94) and Gap (GPS \$23.03). In the energy patch, Chesapeake Energy (CHK \$30.49), Forest Oil (FST \$39.65) and Transocean (RIG \$83.14) are scheduled to post results. From tech, we get releases from Hewlett-Packard (HPQ \$48.62), Applied Materials (AMAT \$16.42), and Salesforce.com (CRM \$140.94). Other expected earnings results next week to keep an eye on include Expeditors (EXPD \$54.45) Diana Shipping (DSX \$12.60), Hormel (HRL \$26.52), Medtronic (MDT \$40.27), VF Corp (VFC \$87.61), Flowserve (FLS \$130.74), Foster Wheeler (FWLT \$39.60), Fluor (FLR \$75.63), AIG (AIG \$42.06) and Newmont Mining (NEM \$58.96).

## Weekly Focus – Think about it

"The internet is clearly about more than sports scores and email now. It's a place where we can conduct democracy and get very large amounts of data to very large numbers of people."

~ Frank James

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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- \* You cannot invest directly in an index.
- \* Past performance does not guarantee future results.
- \* The Markets prepared by Scott Marcouiller, Chief Technical Market Strategist, Wells Fargo Advisors 2/22/11.
- \* Libya Revolt Widens: Alaa Shahine, Ola Galal, and Nayla Razzouk, Bloomberg 2/23/11
- \* Last Week cited from Dean Meehan, Market Analyst, Wells Fargo Advisors 2/18/11.
- \* The opinions expressed here reflect the judgment of the authors as of the date the report and are subject to change without notice.
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