



## Weekly Commentary July 19, 2011

### The Markets

U.S. politicians continued their posturing on the federal budget and deficit. As the debt ceiling negotiations reach the boiling point, it remains to be seen if U.S. leaders will “kick the can” down the road and opt for a short-term solutions or grow up and address the long-term structural issues facing the federal budget. In our view, playing games with the U.S. credit rating and kicking the can down the road may have more serious long-term consequences. In recent accounts, it appears that both sides are taking small steps toward reaching some kind of deal, and both have indicated that a default is off the table. We view any movement as positive, but considering the hard-nosed approach that both sides have taken, we expect negotiations to go down to the wire.

Similarly, European officials seem content to kick the Greece problem down the road in an attempt to give continental banks a little more time to insulate their balance sheets from an eventual default. The European bank stress-test results were viewed as a relief but with a high degree of skepticism. Analysts seemed most interested not in the results but in the volumes of data that the regulators released. The data will let analysts perform their own stress tests and may provide a level of comfort (or discomfort) with the banks’ exposure to risky sovereign debt.

The news flow this week will be hot with the market watching several big stories, including the U.S. debt ceiling negotiations, European bank stress test, the potential for a Greek debt default and earnings from almost a quarter of the S&P 500 companies. Last week’s market action was anything but hot with every sector except energy trading lower. Year-to-date, the best performing sectors have been health care and energy while the worst performing ones were financials and telecom. We expect the market to be volatile as it attempts to discount the U.S. debt talks, European default risk and quarterly earnings.

### Index Performance Statistics – July 19

Index	Close	Day Change	Day % Change	% YTD Change	52 Wk % Change
DJIA	12587.42	202.26	1.63	8.72	23.04
NASDAQ	2826.52	61.41	2.22	6.55	27.18
S&P 500	1326.73	21.29	1.63	5.49	22.45

Source: Bloomberg

\*Price return — does not include dividends

## Debt Compromise Pressure Intensifies in U.S.

A bipartisan Senate proposal for a \$3.7 trillion debt-cutting plan praised by President Barack Obama faces resistance from House Republicans, as lawmakers intensify efforts for a compromise on government spending less than two weeks before a threatened default. Obama said he will renew talks at the White House this week with congressional leaders as the Democratic-led Senate and Republican House pursue divergent paths toward ending the stalemate over lifting the nation's \$14.3 trillion debt limit.

"The problem we have now is we're in the 11th hour and we don't have a lot more time left," Obama said yesterday, referring to an Aug. 2 deadline officials have set for raising the debt cap. The president, in remarks at the White House, said he will urge congressional leaders "to start talking turkey" and get "down to the hard business of crafting a plan that can move this forward." House Republicans last night passed their debt-reduction plan 234-190 -- legislation that stands little chance of passing the Senate and that Obama has said he would veto if it did. The measure would cut and cap government spending and allow the debt ceiling to be raised by \$2.4 trillion only if Congress approves a balanced-budget amendment to the Constitution.

The Senate plan that emerged yesterday from the so-called Gang of Six combines spending cuts with a smaller amount of tax increases. While House Republican leaders indicated a willingness to consider the proposal, they and other members of their fiscally conservative caucus continue to stress opposition to a debt compromise that includes more taxes.

## Last Week

The refrain was the same this week, as Euro zone debt concerns and a stalemate in U.S. budget talks continued to hang on the bull's back. Worries that Italy will succumb to debt contagion and a pair of credit downgrades hurt equities. Specifically, Fitch downgraded Greece's credit rating and Moody's lowered Ireland's rating to junk status. In addition, Moody's and S&P moved closer to a downgrade of the U.S. government's debt amid deteriorating talks in Washington. These concerns made Fed Chairman Bernanke backpedal; initially he said the central bank is open to a third round of quantitative easing if the recovery moderates. However, he retracted his statement saying the Fed is not prepared to take further action amid ongoing concerns about the U.S. debt ceiling, which erased earlier gains. With the market rally into the close of the second quarter, earnings are now being held to a higher standard. Dow component Alcoa (AA \$15.46) kicked off the season but failed to beat lofty expectations. Meanwhile, economic data, which has been the bane of the bull's existence, actually helped this week. June PPI and CPI showed inflation may be moderating and import prices declined for the first month this year, aided by a drop in energy prices. In this week of mixed messages, the caution signs were still flashing; as a result the S&P 500 Index was down 2.3% going into Friday's session.

Looking ahead, we will have much data to digest. Housing data will garner attention with housing starts and existing home sales scheduled to hit the tape as well as a weekly update on mortgage applications. Also of interest will be the release of the leading indicators index with the consensus calling for a decrease to 0.2% in June after the 0.8% boost in May. Additionally, look out for industrial data by way of the Empire Manufacturing and Philadelphia Fed Indices. Lastly, after this week's release of the FOMC minutes revealed a more cautious Fed, investors will look for clarification from regional presidents Hoenig and Evans as they weigh in on recent action.

After a rocky start to second-quarter earnings season, next week's reports may help investors make up their minds. Following encouraging results from JPMorgan (JPM \$40.35) this week, investors will hope the bevy of banks scheduled to report follows suit. In particular, Goldman Sachs (GS \$129.89), Morgan Stanley (MS \$21.11), US Bancorp (USB \$24.69), Northern Trust (NTRS \$44.44), BB&T (BBT \$25.32), Bank of America (BAC \$10.07), SunTrust (STI \$24.64) and PNC Financial (PNC \$57.26) will release profit tallies. Along with the financials, investors will look to see whether Apple (AAPL \$357.90), Qualcomm (QCOM \$54.90), Microsoft (MSFT \$26.47), SanDisk (SNDK \$41.14), eBay (EBAY \$32.19), Seagate Tech (STX \$16.68), and Yahoo! (YHOO \$14.63) are headed down the right path. Other notable companies due to stop by the corner of Broad & Wall include Halliburton (HAL \$51.83), Johnson & Johnson (JNJ \$67.66), Coca-Cola (KO \$67.67), Freeport-McMoRan (FCX \$54.25), Mosaic (MOS \$66.08), Pepsi (PEP \$68.60), Harley-Davidson (HOG \$41.80), Abbott Labs (ABT \$53.16), AT&T (T \$30.58), and Caterpillar (CAT \$107.58).

## **Weekly Focus – Think about it**

“Until you play it, St. Andrews looks like sort of real estate you couldn't give away.”  
~ Sam Snead

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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- \* The Markets prepared by Scott Marcouiller, Chief Technical Market Strategist, Wells Fargo 7/19/11
- \* Debt Compromise Pressure: Catherine Dodge & Julie Hirshfeld Davis, Bloomberg 7/20/11
- \* Last Week cited from Dean Meehan, Market Analyst, Wells Fargo Advisors 7/15/11.
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