Weekly Commentary
August 9, 2011

The Markets

Thrill seekers need not head to a theme park this summer when they can simply turn to the stock market, which continues on a tremendous roller-coaster ride. Following the worst week in more than a year, the stock market trumped it with a free-fall last week and its worst performance since November 2008. The S&P 500 declined 7.2%, and the Dow Jones Industrial Average (DJIA) declined 5.8%. In simple terms, investors lost their confidence, and large- and small-market participants alike headed for the exits, not only in the United States but around the globe. *The Wall Street Journal* summed it up well this past weekend when it said the global sell off was fueled largely by the unfinished business left by the debt crisis, spiraling fears of contagion in Europe, disappointing U.S. economic news and renewed worries about overlooked questions like future growth in China.

We said last week in our discussion of the new debt-ceiling legislation that the devil is in the details. In this case, the detail that seems almost assured to bring more drama in Washington in the coming weeks is the stipulation that the next round of cost savings/revenue enhancements must be determined no later than November. The drama has already started and taken a new twist: congressional finger pointing resulting from Standard & Poor's (S&P) deeming the deficit reduction in the legislation too skimpy and dramatically, although not totally unexpectedly, downgrading the nation's debt rating from AAA to AA+ with a negative outlook.

There were high hopes for the Federal Reserve meeting this Tuesday, and equity investors greeted the outcome positively, triggering a 429-point rally by the end of the session. The Fed acknowledged that economic growth has been slower than the Open Market Committee had expected. Also, a somewhat slower pace of recovery is expected in the next few quarters, and downside risks have increased. This news initially spooked investors into thinking that the Fed might have a more dire outlook than it is letting on, and hence, the news could be a potential negative for stocks. The market did like the Fed's commitment to hold short-term rates at low levels through at least mid-2013. Policymakers also stated that they are prepared to employ additional tools as needed to promote stronger growth while keeping inflation in check.

The dramatic stock market decline on August 8 – the worst one-day loss for stocks since December 2008 – underlined the rapid drop in investor confidence. It extended the S&P 500's decline to 11 days and the pullback to approximately 17%. These are the types of environments where stock market bottoms have typically formed. The market is very oversold, and pessimism is extreme after the market's sharp drop in the past two weeks. Market volume has risen sharply over the past three sessions to levels now consistent with past significant market bottoms. The VIX index or "fear gauge" – the label given to the Chicago Board Option Exchange (CBOE) Volatility Index – measures how much investors are willing to pay for options to protect against stock market declines. This index spiked to 49 on Monday, which signals a very high degree of fear and a level consistent with past stock market bottoms. These are all characteristics that one looks for when the market is reaching climactic setting preceding an upturn. Unfortunately, we can never know the exact timing or level of the bottom. But there are indications that it's in the offing.

Market volatility like we have seen in the past two weeks is never easy for investors to experience. The market's action as of Tuesday's close says that investor sentiment has reached a point where it may fully reflect all the negative factors for the time being.

Index Performance Statistics – August 9

Index	Close	Day Change	Day % Change	% YTD Change	52 Wk % Change
DJIA	11239.77	429.92	3.98	-2.92	5.59
NASDAQ	2482.52	124.83	5.29	-6.42	9.02
S&P 500	1172.53	53.07	4.74	-6.77	4.59

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

Bernanke's Interest-Rate Timeframe Draws Most Negative Votes in 18 Years

Federal Reserve Chairman Ben S. Bernanke's plan to hold interest rates near zero through at least mid-2013 provoked the most opposition among voting policy makers in 18 years as central bank consensus frayed. The Fed chief achieved unanimous support on the Federal Open Market Committee in 2008 when he lowered interest rates to near zero, and in 2009 when he launched $1.73 trillion in bond purchases. Last year, his plan to buy another $600 billion in assets drew one dissent. Yesterday, three policy makers dissented from the decision to apply a specific date to the Fed's low rate pledge for the first time.

Bernanke's move shows that a Fed chairman can govern with more than two opposing votes, opening the door to bolder action if necessary, said Roberto Perli, a former economist in the Fed's Division of Monetary Affairs, which helps craft the language of the FOMC statements. "We have reached the point where Bernanke is taking control and saying we have to do the right thing no matter how many people dissent," said Perli, a managing director at International Strategy & Investment Group in Washington. "It shows the committee can move forward."

Seven members of the panel favored the action. Richard Fisher, president of the Federal Reserve Bank of Dallas, Charles Plosser of Philadelphia and Narayana Kocherlakota of Minneapolis voted no, preferring to maintain the existing "extended period" language. The last time three FOMC voters dissented was on Nov. 17, 1992, under Bernanke's predecessor, Alan Greenspan.

Last Week

This week was downright cruel to the bulls. Stocks melted under unbearable summer heat that the economy is faltering. Fears of recession bubbled to the surface as the July ISM manufacturing index expanded at the slowest rate in two years, and consumers culled their spending habits as their incomes rose by the smallest amount since September. Adding to investor anxiety were comments from ECB president Jean-Claude Trichet that inflation remains a risk and stands ready to provide additional funds to banks. Strengthening of the greenback prompted by Japan's intervention to weaken the yen sent commodities and basic material stocks sharply lower. With the employment report looming large over Friday's trade, the S&P 500 index lost 7.1% to put it down 4.5% for the year as of Thursday's close

As stocks wilted in the hot summer sun, investors sought shade over in bond land. Treasuries benefitted sending the yield on the 2-year note to an all-time low of 0.25% and yields on some short term Treasury bills into negative territory. The 10-year note advanced to push its yield down to 2.40%—a mere 1 basis point above last November's low of 2.39%. Even with the specter of a possible downgrade of the U.S. credit rating, investors continued to move out on the curve. In the past two weeks, the 30-year Treasury bond has rallied nearly 12 points since July 25 to send its yield tumbling down by 65 basis points from 4.32% to 3.67%. With the sharp rally over in bond land, it will be interesting to see what the appetite will be for next week's bond auctions of 3-, 10- and 30-year Treasuries totaling $72 billion.

Given the signs the economy is sputtering, Tuesday's FOMC Meeting will take center stage next week. The Fed keeping rates unchanged is a foregone conclusion. Therefore, investors will likely focus on the statement released at 2:15 pm ET as well as Fed Chairman Bernanke's press conference that follows for indications the central bank is considering another round of stimulus. With a spate of positive economic data recently, the hope is that the bar is set low enough for some upside surprises from next week's scheduled updates on productivity and labor costs, the trade balance, consumer confidence, retail sales, and business inventories.

Although the economy has shown signs of slowing, corporate earnings have remained strong. With 408 of companies in the S&P 500 index reporting second-quarter earnings, 75% have reported results ahead of Wall Street analyst estimates, according to Bloomberg. Unfortunately, earnings season winds down next week. Of the companies left to report, the department stores Macy's (M $26.13), Kohls (KSS $47.67), JC Penney (JCP $28.67) and Nordstrom (JWN $43.15) will be under the microscope after disappointing personal spending and same-store sales reports. Also of interest in the retail space will be earnings by Advanced Auto Parts (AAP $52.74) and Brinker (EAT $22.28). Despite losing some of its luster, Cisco's (CSCO $14.82) earnings release on Wednesday will garner attention. Other notable profit tallies scheduled to hit the tape next week include media moguls Walt Disney (DIS $35.35) and News Corp (NWS.A $14.56), food stuffs Tyson Foods (TSN $16.25) and Sara Lee (SLE $18.29), and utility Consolidated Edison (ED $51.74).

Weekly Focus – Think about it

"A nation that is afraid to let its people judge the truth and falsehood in an open market is a nation that is afraid of its people."
~ John F. Kennedy

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 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 Scott Marcouiller, Chief Technical Market Strategist, Wells Fargo 8/8/11

*Bernanke’s Interest-Rate: Craig Torres and Joshua Zumbrum, Bloomberg 8/9/11

* Last Week cited from Dean Meehan, Market Analyst, Wells Fargo Advisors 8/5/11.

* 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.