Financial Research Education & Data

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Trading Week Starting
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The FRED Report

Summary of Market View

INSIDE THIS ISSUE:

Special points of interest:

- A look at other key indexes shows that leadership remains in the small to midcap space, which is normal when emerging from a recession.
- Our longer term view remains that rates are going up, and that appropriate strategies will mitigate this risk.
- We believe that a summer rally in commodities will lift energy markets.

The stock market has failed to correct short term and while the chance of a pullback remains, it is less likely now that the IWM has closed above 70 twice last week. The summer rally could be starting earlier than expected, and so far the leadership still looks to be commodity related areas.

Bonds staged the sort of false breakdown we have been concerned with. Rates still look higher, but this remains choppy and difficult to trade.

Oil and gold may continue to advance here – we added oil stocks to our list last week, and look to add more, plus maybe more of the GLD.

We examine the BRIC countries, and remain optimistic on our non-US growth theme areas.

Stocks Review

The stock market continues to gain ground and about in the way that we have been expecting. The IWM has completed two closes above 70 and in addition has built a small technical flag formation suggesting further advance. The SPX still remains below 1200, which gives the bears some ammunition (for new subscribers – email or call me and I will point you to some reports which explains our thinking here). **A look at other key indexes shows that leadership remains in the small to midcap space, which is normal when emerging from a recession**. Also heartening is that the Dow Transports continue to lead the Industrials. **A little known feature of Dow Theory is that when the Transports lead the market is healthier**. A simple look at the Barron's Market Lab section shows that the leadership last week breaks down as follows: Dow Transports gain 2.62% vs. Industrials .64%. Russell 2000 gain is 2.77% vs. S&P 500 gain of 1.38%. **As long as the indexes perform in this way and breadth remains strong, we remain intermediate term bullish.**

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Advisors should continue to allocate client cash to mid and smaller cap managers, for their higher risk accounts for now, which begs the question – "For how much longer?" **Our research piece on smaller cap outperformance at the end of recessions, written back in January of 2010 (*see that Monthly Report on the site*), suggests that this can continue for two years**. Right now our best guess is that the recession will end officially at the end of this summer, in time for the mid term elections. At that time, watching the relative performance between the Russell 2000 and the S&P 500 will be important for a while, but may not end. For now these trends look to continue.

Fixed Income Review

As we expected – the TLT staged a false breakdown and then reacted strongly back into the trading range. You can see this also on the charts of the TYX (30-year yield), and TNX (10-year yield) below. We continue to feel that it is going to be difficult to hedge bond yields, with lots of choppy movement in these markets, until bonds hit some seasonal weakness which often occurs in the fall**. In the meantime, we continue to advocate shorter maturities, laddered maturities and a more cautious approach to the fixed income markets**.

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One other idea that may be helpful to those who do not buy individual bonds would be to look at some unit trusts rather than mutual funds.   These trusts do mature eventually which lessens principal risk in the event of a raise in rates. Some firms maintain a secondary market in these instruments as well. One could get a decent yield and maturity combination in this way.

Our longer term view remains that rates are going up, and that appropriate strategies will mitigate this risk.

Commodity Review

We added stocks to our *Idea Generation: Equity Trades* list in this area, principally in the petroleum complex. **We believe that a summer rally in commodities will lift these markets**. Indeed, this rally may have already started. This rally is seasonal in nature, but in this case may very well be helped by a strengthening economy. We are also looking at adding in the Metals, as gold is looking stronger. We have had a position in gold since last summer and are looking to add to it. We continue to have questions on silver, which also looks strong but has a tendency to underperform gold until the very end of a commodity bull.

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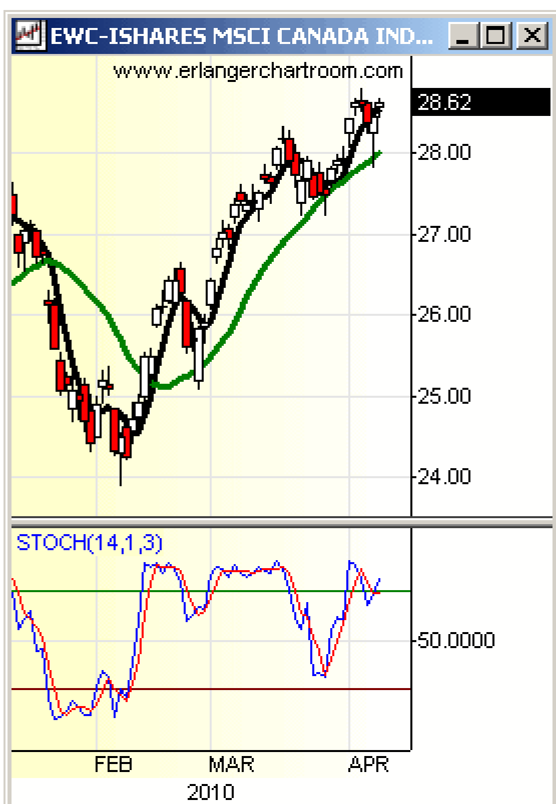
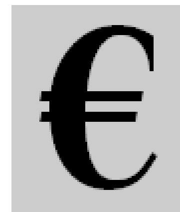
For asset allocators, ETF traders, and mutual fund buyers there are several ways to position for a summer rally in these areas. One way we like is to buy the Australian stock market ETF (EWA) as this market will benefit from a rise in gold and raw materials, and in addition has a decent yield. Canada also looks positioned to benefit (EWC). Advisors could also place some money in energy funds or ETF's. However we invest in this area, it looks promising for the rest of the year.

We caution advisors: There may be a surprise and we could see the dollar, as well as commodities rise. We have written of this before, and there is precedent for this. There are all sorts of supply/demand relationships that could come into play. Should clients want to hedge a falling dollar this can be done with currency ETF's. We believe this area of the market can rise regardless of dollar strength or weakness. We show charts of the Dollar and Canadian market below. While these would normally be in our "International" section we include them here because they are important to our commodity growth theme.



International Review

We continue to see strength in Asia. **The Chinese and Japanese indexes have continued to react well.** This remains an excellent harbinger of worldwide growth. As an adjunct to this idea we look for the commodity rally mentioned in the commodity section. **China has definitely firmed** and their market is also being led by small caps. This is a sign that domestic companies are starting to do better, which in turn means to us that the economic recession continues to abate. A move through 47 on the FXI implies higher highs, and we feel that is likely because the HAO has already moved through that ETF's respective high. Supplying countries, such as Japan continue to do well. The EWJ has closed through the 10.50 area and could now test the 11.50–11.70 area this summer. Recall we have been a proponent of the JOF Japanese small caps, and that index also looks strong with a test of 10.50 or so likely this summer.



"The Chinese and Japanese indexes have continued to react well."

In terms of raw material producers – the chart of the EWZ is germane. Brazil has recovered and the EWZ could test 80 to 84. The EWC is making new recovery highs and could test 32 – 34 in a summer rally.

The bottom line here is that both the consumer countries and producer countries are improving enough to suggest that the story this summer will be continued economic recovery with a return to inflationary pressures. Also, see the "Other Charts of Interest" section of this report for more on this.

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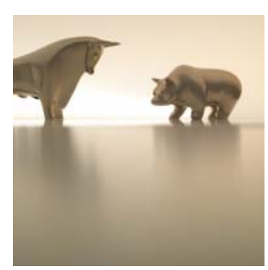
Weekly Chart of Interest

We continue to have questions on the BRIC countries so we will look at India and Russia here (we wrote about Brazil and China in the "International Section").

First India, which has improved and looks like an advance could be expected this summer: The PIN (PowerShares India) could test 26 or so. Frankly, Russia (the last of the BRIC's) looks a bit more interesting to us as it should do better if Oil improves, which we expect. Russia has lagged the others because oil has been a drag on this market for the last year. For the rest of the spring and summer here it could turn into a short term leader. For the more aggressive country allocator – a position in RSX (Market Vectors Russia ETF) seems warranted. It could test the 45 area from this area.

About Our Organization

The FRED Report was started to provide Financial Advisors across firms and platforms access to unbiased market research. The President of the Fred Report, Fred Meissner, CMT, has been practicing Technical Market Analysis since 1983 and has worked in the research departments of Merrill Lynch and Robinson – Humphrey /Smith Barney. In addition he has served the public as a portfolio manager and financial advisor. We know the problems advisors face and have devoted our career to helping advisors find the best possible investments in all environments. We want to help you help your clients and grow your business.



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