



IS THE BANDWAGON BECOMING CROWDED?

Last month the U.S. equity market was sending solid indications going into the second quarter earnings season that the results were going to be better than expected. The numbers did not disappoint, resulting in July being the best month for equities since 1992. The rally was anticipated by us with the large amounts of cash in idle on the sidelines and the “show me” investment environment. Companies that can prove to investors that business is going well are getting rewarded with a significant increase of investor demand for their stocks.

As the cash returns to the equity market, the concern we have is recovering too fast. In an orderly recovery, upward market moves are followed by a move sideways. If the market recovery gets ahead of itself, a pullback in stock prices can follow. However, whether we have a small pullback in stock prices or not, the overall longer term movement is heading in the right direction.

We still believe that the U.S. equity market recovery will be a two step process. The first step (already occurred) was a quick snapback that erased part of the drop caused by the panic riddled sell off. The second step (still to come) will be a steady recovery that will build slowly as the most skeptical cash trickles into the equity market. The current “snap back” rally has progressed higher than we anticipated. However, we are pleased that our current investment strategy has allowed our clients to outpace the recent rally. As always, we are focusing our equity holdings on companies that will not only recover quickly, but continue to grow after the economy begins to grow.

POSITIVE FACTORS FOR THE MARKET

One of the necessary factors of a sustainable rally is a skeptical investor. A popular term for this is when the equity market climbs the “Wall of Worry”. In other words, the market goes up despite the existence of negative indicators. If everyone believes the market is going up then we get an unsustainable rally that will not hold and a subsequent downfall. We continue to see a struggling job market and single family and commercial real estate lack footing. For some economist, this leaves the strength of the consumer in doubt and therefore plenty of bricks for the “wall of worry”.

The media continues to help build the wall of worry. To combat the consistent loss of viewers and readers to media outlets, they have resorted to scare tactics. This is a trick long been enjoyed by politicians in Washington. Sensationalist journalism seems to be at an all time high as evidenced by the over use of the word - Crisis. We went from the real estate crisis straight to the financial crisis and now we are neck deep in a health care crisis. If the media would just report what was going on as opposed to trying to arouse emotion in the viewer, maybe we wouldn't have 27 million Americans on antidepressant medication!

The one fundamental fact that is now seemingly forgotten by the media, inexperienced money managers, and brokers is that over time the companies that consistently make money will have their stock prices rise and reward investors. Just because the market has a positive run does not mean the market HAS to immediately pull back.

While we don't know the timing of the payoff, we do know that if a company is consistently growing its market share, the stock price will eventually reflect the growth. As investors, not traders, we look at putting our investments into companies that are making money and growing market share. By focusing on this and not on just the company's stock price, we know that our investment will grow. Outside influences may be causing the stock prices to swing back and forth but the payoff will still be there.



The demand potential for stock investment continues to grow and without supply growing substantially, prices must go up. There have only been few companies that became public over the last year and a small number looking to become public companies in the near future. Couple the lack of IPO's with the mergers and acquisitions of public companies and a positive trend for equity market prices is emerging.

As the second quarter earnings season comes to a close, we continue to assess our current stock holdings making sure each company is providing the appropriate reward for our investment. We also look for new companies that can further bolster our already market outperforming performance.

As always, thanks for your trust.

Dennis Deen