

Rochester Financial Services

Fee-Only® Financial Management Services

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Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Crude Oil	Gold
10,974	1,187	2,430	698	3.99%	6.40	\$1,132	\$78.70

Principal



Investment Strategy Report

With the Economy Beginning to Add Jobs, Can Anything Stop The Stock Market?

The story in my last month's letter was whether the weak jobs picture would derail this bull market. Unemployment claims seemed to be persistently high and the fear was that investors would begin to get impatient with the lack of job growth and start to dump stocks. Well here we are a month later and the stock market is doing just fine, hitting 18 month highs for most of the indexes. Stocks have climbed over 5% in the past month and that was *before* this past Friday's job report which showed that 160,000 new jobs were added in March, the highest amount in 3 years. The stock market continued higher today in its first opportunity to show its approval of the report. So if the stock market did fine when investors were uncertain about the job market, how will it do when the jobs picture is looking a lot brighter? Dow 11,000 here we come!

It does look like we should expect higher stock prices ahead. As I mentioned in last month's letter, "the stock market is focusing more on the economic recovery and not letting the negative headlines get in its way". For many analysts, this month's favorable jobs report was an inevitable result of an economy that is gaining momentum. Frank Curzio (StansberryResearch.com, 3/27) wrote that "American companies are enjoying some of the best conditions in decades". "The largest 500 American non-financial companies have 10% of their assets in cash, the largest amount since the 1960's". Government stimulus will continue to spur growth as will record low interest rates. Worker productivity is at record highs and "manufacturers like Boeing and Caterpillar are increasing production".

Jay Chitnis (Yieldquest.com) states (3/15) that "moderate gains in consumer spending ... suggest that we may be on the cusp of a self-reinforcing cycle of spending and job growth". Based on gains in manufacturing, industrial production, and business sales, he predicts that this recovery will not be sub par, as many are forecasting. Corporate capital spending is also set to increase since 1) companies are flush with cash and 2) they have been underinvesting for the last few years and have much catching up to do. Commenting on last week's job report, Chitnis (4/5) states that the report might be indicative of a more robust recovery of the economy in general and in jobs in particular. Looking back at the recoveries from the recessions of 1973-74 and 1980-82, during the first 9 months of recovery, total new jobs created were 2.5 million (from 7/75 to 3/76) and 3.3 million (from 3/83 to 12/83). He feels that similar job growth in 2010 is quite possible, which would push the unemployment rate back down to 8% by year end, much less than widely expected.

So with all this good news about an economy gaining momentum, it seems like nothing can stop this market - except for rising interest rates. Something had to be the party pooper here and many of you might have been hearing about interest rates starting to spike higher. In the past 5 weeks, the yield on the 10 year Treasury has risen from 3.61% to 3.99%. Most of that rise has occurred since March 24th. It seems to be due to the fact that the Federal Reserve has stopped purchasing mortgage backed securities, although this has been known for months now. From 1/109 to 3/31/10, the Fed purchased \$1.25 trillion worth of these securities. With the Fed now out of the picture, it is almost guaranteed that rates will have to move higher in order to find buyers to take the Fed's place.

When mired in a recession, rising interest rates are looked at as a good thing. It is signal that the economy is improving. In Japan, where their 10 year Treasury has been stuck below 2% for 20 years, they would love to see an improving economy cause their interest rates to rise. In the US, the 10 yr rate bottomed in January of 2009 at 2.1% and has risen to its current level amidst our recovery. However, as rates continue to rise, they have been known to choke off economic growth, as the cost of borrowing increases. And not only can that cause problems for the stock market, but rising interest rates are an anathema for bonds as well. During the next few weeks, I will be re-examining our bond fund holdings. I will most likely be adding to funds that can do well in a rising interest rate environment and sell the more traditional funds that can be expected to underperform.

IRA Contributions – You still have about a week left to make your IRA contributions for 2009 (provided you're not filing an extension). Please call me if you need help making the decision. *Jeff Feldman*

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