

# Rochester Financial Services

Fee-Only® Financial Management Services

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Principal

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Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Crude Oil	Gold
12,807	1,361	2,864	855	3.28%	6.87	\$1,541	\$112.96



## Investment Strategy Report

### Strong Earnings Propel Stocks Higher

The major stock market averages ended April on a high note, hitting highs not seen since the spring of 2008. But similar to 2008, oil prices are also climbing and fears are beginning to mount that \$4 gas prices might crimp our burgeoning recovery. Up until now, strong retail sales have been one of the factors contributing to the economic rebound. But can the consumer continue to shop in the face of rising transportation costs? It was exactly 12 months ago that our optimism was shattered with the flash crash and the subsequent 15% stock market correction. Economic growth slowed amidst fears of a double dip recession. Now, 12 months later, we see consumer confidence experiencing a drop last month, unemployment claims that had dropped to an average of 380,000, now backing up to 420,000 the last few weeks, and first quarter GDP falling to a lower than expected 1.8%. Has the stock market gone too far too fast?

The stock market has gone far very quickly, rising about 30% since September 1st. So propping up the defenses and taking some profits now would not be a bad idea. If nothing else, future gains will be harder to come by. However, the first quarter earnings reports have definitely been solid. Multinationals are benefiting both by the strong growth of the emerging market countries as well as the weak dollar, which makes US products more attractive to foreign buyers. As an example, Cummins, which makes diesel engines for heavy machinery, hit an all time high after reporting tremendous earnings driven by strong growth in China, India, and Brazil. If Cummins is doing well, things can't be too bad.

Wall Street is focusing on earnings, and it is projected that the earnings for the S&P 500 for 2011 will come in at a strong \$93 to \$95. Applying a modest 15 to 16 times earnings multiple would make a level of the mid 1400's for the S&P a very attainable target for 2011. That could be another 6-8% market increase, making this year another double digit gain. Continued weakness in the housing sector and slower than hoped for job growth will continue to be negatives. But most investors would agree that the recovery remains on track and corporations across the board are seeing improvements. The stock market has been very impressive during its march higher. It appears that it is doing so with good reason.

**Market Sectors - 1)** The emerging markets continued their winning ways in April. The fund representing my largest position in this sector was up 6.0% last month. I am continuing to add here as long as the recovery from the sell-off in January appears to be staying on track. **2)** Gold made new highs again last month, finishing April at a new all time high. Silver did even better, as its rise began to be described as parabolic. While it underwent a 10% correction today, silver still seems poised to go much higher. While our precious metals stock funds didn't do as well as the metals themselves last month, it does seem that both the metals and the miners will continue to move higher as global currency devaluations persist. **3)** For many of you, I began to add biotech funds to our portfolios. This sector can be described as one of the classic "boom/bust" sectors. These stocks can do nothing for years during the "bust" years. And then, when the boom takes over, they can rise hundreds of percent in short periods of time. We can very well be in the early stages of a boom period. The sector has done nothing since 1999 and has now begun to rise. In addition to their potential upside, there is also the added benefit of diversification, since the biotechs don't move in lock step with the rest of the market. It also seems that the healthcare sector in general might be beginning to outperform. I will continue to monitor both of these sectors of the market. **4)** I have saved the worst for last. In my strategy for fixed income investing in the face of rising interest rates, I have staked quite a bit on the Yieldquest bond fund which stands to benefit from rising interest rates. In the face of staggering Federal deficits, it's hard to imagine that interest rates can fall, but that is what has been happening recently. So this fund, instead of benefiting from rising rates, has been getting hit very hard by falling rates. April was a particularly bad month for the fund and as a result, I have begun selling it. I still feel that rates eventually have to rise, but know that "markets can stay irrational longer than I can stay solvent". I will continue selling the fund if its poor performance continues. As a partial consolation in this area, all of our other bond funds had very strong months. *Jeff Feldman*

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