

Summer 2011

Market Strategies



Switchback Routes

The second quarter roller coaster ride resulted in lots of volatility, but ended essentially flat for the three-month period. This might seem surprising, considering the market fell for six straight weeks from early May to late June attempting to duplicate last year's 10 percent slide. A strong rally in the last week recovered much of the paper losses; therefore, halfway through 2011 the stock market as measured by the S&P 500 index is slightly positive with a 6 percent gain. Over the long run, there are many similarities between a portfolio's performance and that of a long-distance road trip. Long-term success is dependent upon knowing the target destination, the best mode of transportation and having the right navigational tools. Quite often the road you're on might take a dip or bend to go around a lake or traverse a mountain; these switchbacks in the road are as natural as a six-week slide in the market.

In our advanced society, we have tremendous technological tools to assist us at every turn. A recent family vacation from here to Boston highlighted the innovations available over the last forty years. As a child sitting in the backseat of the family sedan with the windows open to stay cool, reading a map was the way to navigate the best available route to Boston. It was still necessary to stop two or three times to ask directions to the hotel reserved over the phone months earlier. Today, we can change reservations via the internet on our phone along the way, use MapQuest to produce a custom route, or follow the GPS in our minivan that can give us directions to our hotel in six different languages. Similarly, to follow the stock market in the '70's we had to pay close attention to the 6:00 p.m. news as the anchor provided a brief daily market update. If you wanted to check on a particular stock, the newspaper was the only real source of current data unless you had time to sit in the "bullpen" at a brokerage firm and read the electronic ticker. Today it is possible to see every trade of your favorite stock while walking through a park. Public access to every economic tidbit of news is easily available for free rendering newspapers dispensable.

The advent of the information age does not necessarily render better decisions. Much of the news promoted to fill the 24-hour news cycle is not productive for investment analysis. During a period when the market is sliding six weeks in a row, and this data is received six times daily, it can be discouraging to say the least. If we told you on January 1st the stock market would be up 6 percent by July 4th, it might have reduced some anxiety along the way. Knowing not to panic or take action on irrelevant data is the result of learned experience. While most of our clients remember the 1970's, most did not have the assets they have today. You were busy raising families, earning a living and saving a little along the way. We have managed assets through these periods and have records of what happens during budget battles and periods of rising interest rates. Our disciplines have taught us not to make rash decisions when the market has a retreat before the next ascent when quarterly earnings are being reported.

The quarterly corporate earnings numbers being reported continue to be a positive for the market. While certain sectors of the economy continue to disappoint, namely housing, banking, utilities and consumer spending, the economy is growing, but just at a snail's pace.

We also have great concern on the inability of our electorate to successfully manage our national budget responsibly. If they are mutually obstinate and don't make real changes to spending and revenues, it could force another government shutdown akin to 1995. Experience tells us the market will drop on the news and then recover when the solution is found. During the quarter it creates volatility, but will be a non-event over the course of a year. Few people even remember the cantankerous mood of Washington when Newt Gingrich forced the shutdown with President Clinton. This is a political event, not an economic event, and all are working primarily to get re-elected.

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Switchback Routes

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Worldwide interest rates are rising, but U.S. interest rates should remain low for the foreseeable future, so our bond management remains high in quality and short in duration.

In summary, a car ride from here to Boston is a northeast migration. Many times the digital compass in a car might read SW or S traveling through the Appalachian Mountains of Pennsylvania or the Hudson River Valley of New York; nevertheless, since we know our final destination is long-term, we are not changing course. Our earnings GPS on the publicly traded companies you own is for higher earnings ahead. Higher earnings produce higher share prices and the result is nicer accommodations at your trip destination. If a specific company disappoints, we'll make the requisite change; this is equivalent to a flat tire. It's an unfortunate surprise, but the problem is resolved and soon you're back on the road.

We appreciate you allowing us to be your portfolio navigator. The trip may not always be direct, but we'll get you there safely.

Enjoy the remainder of the summer; we'll worry about the news!



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