

# The Advantage Advisor

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## Market Commentary:

Lest you think your eyes are deceiving you, yes those are positive returns shown in the table to the right! The month of March provided almost a complete reversal of what occurred in February, and April's returns have thus far proven nearly as strong. While it may be early yet to call this a true reversal and a new bull market, we can certainly say that there has been a change in the posture of the marketplace.

The key to the recovery is a shift in investor sentiment. The VIX chart below shows real change in sentiment and expectations. The VIX index measures the premium investors are willing to pay in order to insure against downside risks for stocks. What we can gather from this chart is that the area above the 37.5 level represents an extreme, fear driven market, while the area below 37.5 represents more rational or normal market conditions.

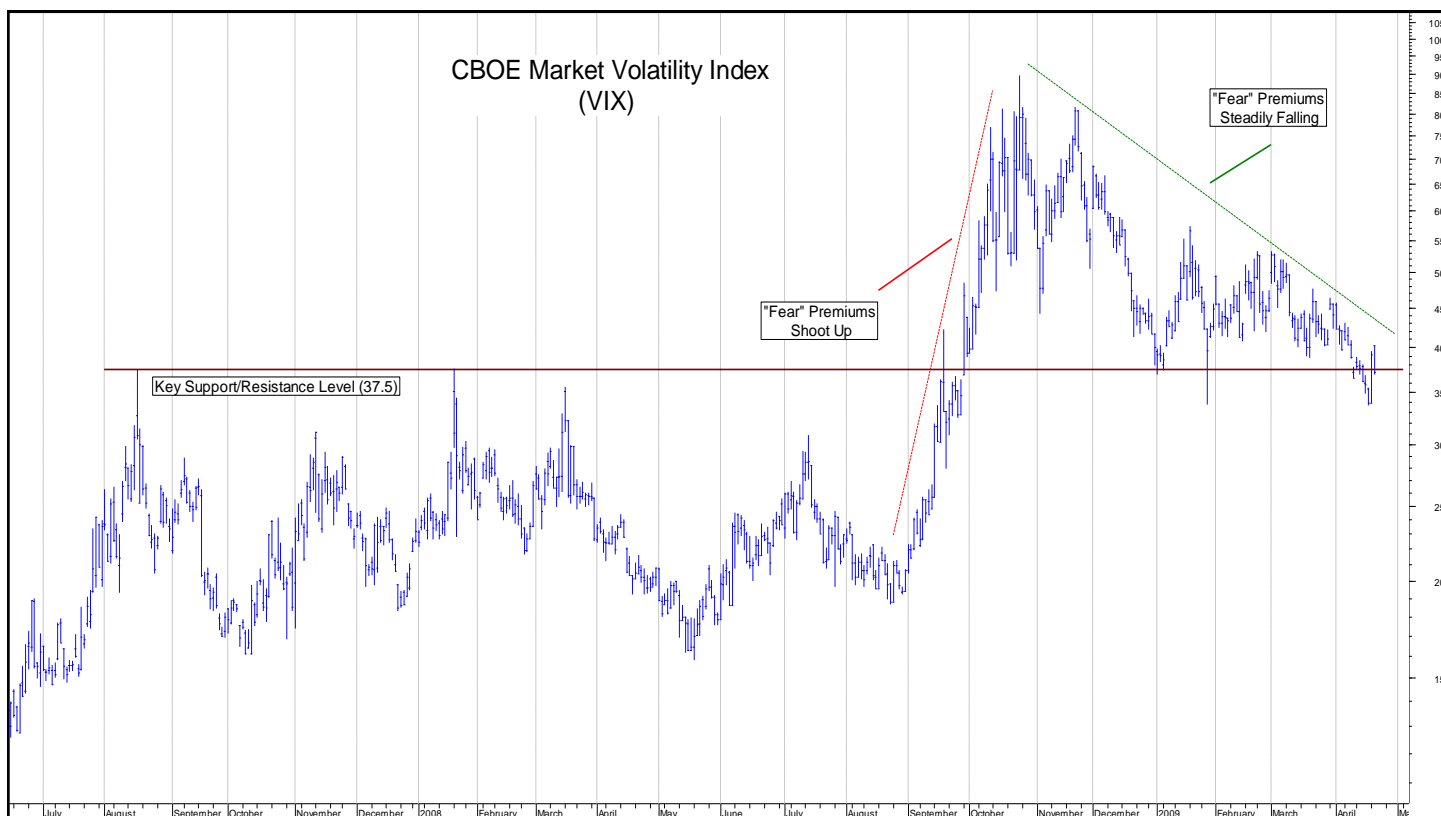
As you can clearly see, there was a huge run up in those premiums beginning last September, reflecting increasing fear and anxiety on the part of investors.

Market Statistics for March

| Market Index                 | Closing Price | % Change |
|------------------------------|---------------|----------|
| Dow Jones Industrial Average | 7,609         | +7.7%    |
| S&P-500 Stock Index          | 798           | +8.5%    |
| Russell 2000 Stock Index     | 423           | +8.7%    |
| Shearson Treasury Bond Index | 17,964        | +4.5%    |
| Dow Jones World Stock Index  | 152           | +7.8%    |
| Nasdaq Composite Index       | 1,529         | +10.9%   |

More recently, we have been making steady progress in moving back toward the more rational range. What that tells us is that investors are no longer willing to pay so high a price to insure against further losses, and that expectations for improving stock prices are on the rise.

We should expect some consolidation in prices before the next significant advance can take place. The six week run we have just experienced actually qualifies as a bull market unto itself. The timing and size of the next advance is dependant on increasing confidence on the part of investors, but there is an historically high level of cash waiting to be returned to the markets. As investor confidence grows that cash will make its way back in.



# The Economic Picture

The US economy is moving into late stage 6, so we need to begin preparations for changes as we see the rotation into stage 1, early growth. It is important, however, that we don't jump the gun on things and become too aggressive too early. For now, we can expect to see more consolidation in our economic indicators before any significant improvement and even growth. What I mean by that is we will see a slowing in the pace of the contraction before we see things turn to actual positive growth. We are beginning to see those effects now.

As an example, I have included a chart of the ECRI Weekly Leading Index (WLI), which is an early indicator of economic conditions. As you can see by the chart, this index has made a definite turn in the right direction. However, you should also note that the percentage annualized change is still negative. Once that rate moves from negative to positive, then we will have real reason to become more aggressive in our investing.

Just one other thing to keep in mind: Economic contractions have a beneficial effect as well. They cause businesses to "cut out the fat", to become leaner and more productive at a much lower cost point. This will eventually translate into much higher profits than were possible from the same businesses before the contraction began.

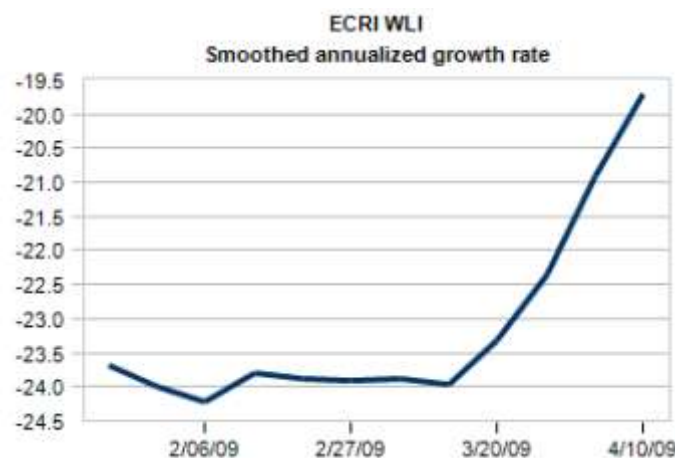
Current Economic Position:  
Stage 6 - Recession

## Economic Indicators

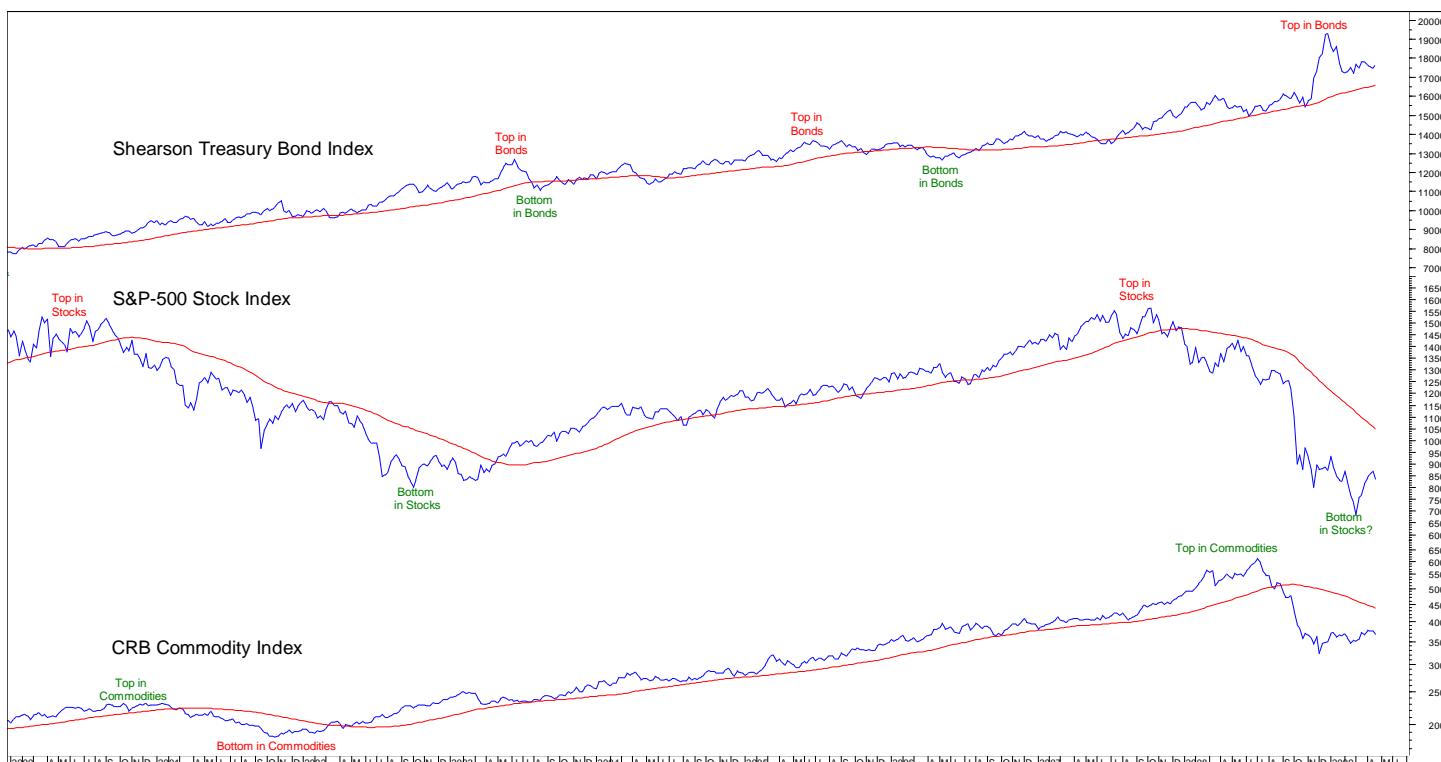
|                               | Latest | Prior  |
|-------------------------------|--------|--------|
| <b>Growth</b>                 |        |        |
| GDP                           | - 6.3% | - 0.5% |
| Productivity                  | - 0.4% | +2.2%  |
| Employment Cost Index         | +0.5%  | +0.7%  |
| Capacity Utilization          | 69.3%  | 70.3%↓ |
| <b>Inflation</b>              |        |        |
| Consumer Price Index          | - 0.1% | +0.4%↑ |
| PCE Deflator (Personal Inc)   | +0.3%  | +0.3%↑ |
| Implicit Price Deflator (GDP) | +0.6%↑ | +3.9%  |
| <b>Sentiment</b>              |        |        |
| Consumer Confidence Index     | 26.0   | 25.3↑  |
| Unemployment Rate             | +8.5%  | +8.1%  |
| Personal Income               | - 0.2% | +0.2%↓ |

↑=revised up, ↓=revised down

Source: Moody's Economy.com



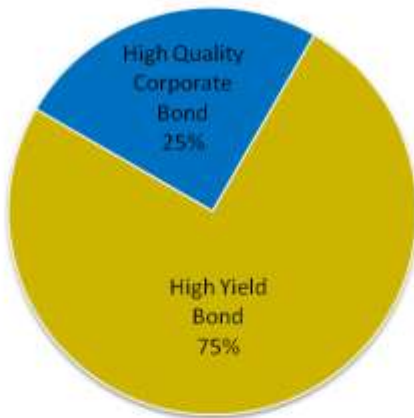
Source: Moody's Economy.com



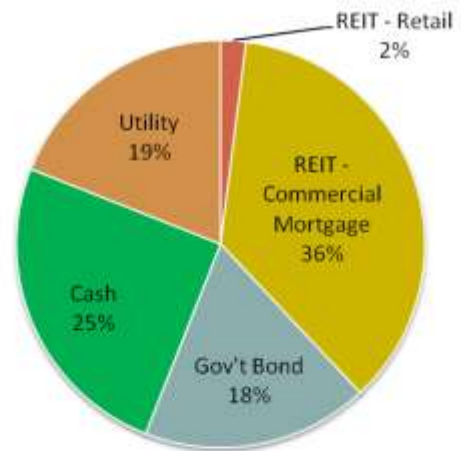
Source for data: Investor's FastTrack

# Current Investment Management Strategy Allocations

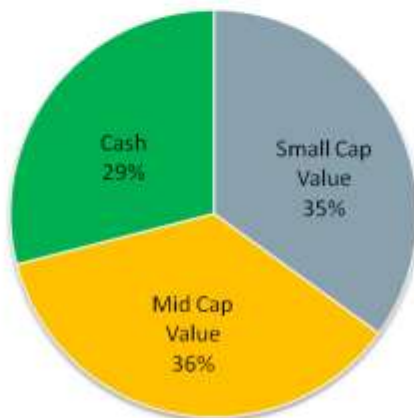
**Bond Strategy**



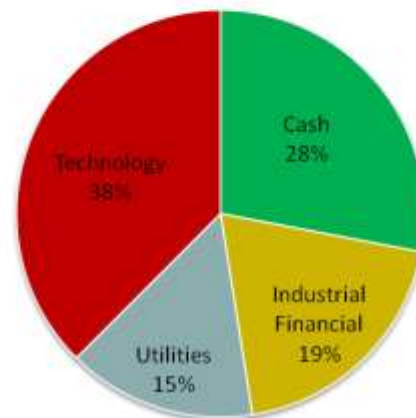
**Current Income Strategy**



**Stock Strategy**



**Strategic Allocation Strategy**



## Investment Strategy Update:

Our investment strategies have been very busy over the past month. The dramatic turn in the markets has led us to move back into more fully invested positions, though still somewhat on the defensive side. Where we move from here will depend entirely on the pace of improvement (or lack thereof) in the economy and investor sentiment. As sentiment improves, we will move from an emotion driven market to a fundamental driven market, and that will allow for much more stability as well as predictability.

Our bond strategy is now 100% invested, holding

75% high yield bonds and 25% high quality corporate and government bonds. The current income strategy continues to hold a higher than normal level of cash as a defensive posture. We will maintain that posture until there are visible signs of growth returning to the economy.

Our stock based strategies have both reversed the defensive hedges we had set in place, but still hold around 29% in overall cash. So long as we see continued improvement in sentiment we will look for market pull-backs as opportunities to become more fully invested.