Market Update – Second Quarter 2012

Rick Grimshaw, CPM® CIMA®  
Senior Vice President  
Portfolio Management Director  
Branch Manager  
May 29, 2012 Commentary  

503-221-7616 or 360-992-7990  
rick.grimshaw@mssb.com  
10-year US Treasury Yield: 1.74%  
DJIA: 12454  S&P 500: 1317  
[5/25/2012 source: Thomson/Reuters]

[See Important Disclaimers at the end of this Commentary]

CNBC Anchor, 7:00 a.m. PDT, Tuesday, May 29, 2012:

“Investors are risk-on this morning on the first trading day after the Memorial Day Holiday”.

Am I the only one that has a major problem with the current catch-phrase “Risk-On” or “Risk-Off” that has entered the Wall Street lexicon in the past couple of years?

Investing and Portfolio Management, to me, does not have an ON-OFF switch. Yet the popular financial media repeatedly keep this concept front-and-center. This is a marathon, not a 100-yard dash. Assumed in the “Risk-On” and “Risk-Off” expression is the ability to turn on and off your investment portfolio like a water hose. I don’t know anyone who can implement such a thing, except perhaps for the big hedge funds. Certainly you and I cannot, and, I believe, should not.

What does the expression say about our regular, systematic contributions to retirement plans like a 401(k) account? What does it say about finding value opportunities in prices of securities when there has been a recent correction, as it appears now?

Let’s look back at the past few months as an example. Here are some reference points, taken from closing prices of the Standard and Poors 500-stock index [source: Thomson/Reuters].
Michael Jones, Chairman and Chief Investment Officer, RiverFront Investment Group, on March 30th published his Strategic View, which commented “While we think markets appear due for a pullback or a consolidation, improving monetary policies and economic fundamentals should limit any decline to a normal 5% to 8% correction within an upward trending market, in our view.” [RiverFront Investment Group, “Expecting a Less Turbulent Summer™, 3/30/2012].

I had the pleasure of moderating a discussion featuring Michael at the 2012 Annual Forum of the Portfolio Management Institute in April, where he elaborated on the above, specifically mentioning the European Central Bank’s long-term refinancing program, implemented in October, 2011; a reduction of U.S. consumers’ debt payments as a percentage of income to levels not seen since 1982 and 1990, lessening recession risk; and policymakers in emerging markets dropping interest rates, which could spur growth.

A more rosy economic view was also shared at PMI Forum [4/18/2012] by Brian Wesbury, Chief Economist of First Trust Advisors, who cited a number of improving trends and statistics to the portfolio manager members in attendance. Included were a variety of factors like consumer spending and retail sales; business investment and commercial/industrial loans; housing starts; industrial capacity utilization, plus private payrolls. He paid particular attention to the impact of technology, sharing that it took 15 years to sell 15 million personal computers—seven years to sell 15 million Smartphones—and just two years to sell 15 million iPads. Brian puts faith in people, not faith in governments. He encouraged the audience to invest in people and ideas. He concluded: “What we have is a sustainable, self-reinforcing economic recovery”, a message he repeated in his commentary of May 21, 2012 [First Trust Advisors, L.P.; Monday Morning Outlook].
Finally, the major investment management firm, Franklin-Templeton Investments, recently released the results of an annual, worldwide investment survey, with this summary: “Many Americans Remain Reluctant to Invest in Equities, Largely Keeping Investments Close to Home in 2012…Despite strong U.S. equity market returns in early 2012 that sent the Dow Jones Industrial Average back above 13,000 by the end of February—a level not seen since May, 2008—indications are that many Americans remain investment spectators, reluctant to participate in the equity market rally” [News Release, Franklin Templeton Investments, “Global Investment Sentiment Survey”, May 14, 2012].

Certainly the media has lots to report on. A partial list includes fiscal problems in Europe, stubborn unemployment in the U.S., a weak recovery, China’s economy growing at a slower pace, the 2012 U.S. presidential election and more.

When I combine the improving economic environment, as reported by Jones and Wesbury, with the public pessimism seen in the Franklin-Templeton survey, my conclusion remains that patience and discipline should remain cornerstones for investment and portfolio management. I’ve mentioned several times over the years my favorite investment expression: “The markets will do whatever they can to frustrate the majority of people at the same time!” [Grimshaw, Portfolio Management Update, 11/2/2009]. Beneath the headlines, could there be a summer rally in our future? Markets can and will frustrate investors, in my opinion, and the consensus can be wrong. I find there are too many bears out just now and multiple bullish reasons to invest, in my opinion.

As always, we appreciate our loyal readers and clients, and hope you and yours get your share of the summer weather. Hit the “pause” button. But stay away from choosing “On” or “Off”. You’ll be better served by doing so.

With best wishes,

Rick Grimshaw, CPM® CIMA®
Senior Vice President, Branch Manager
Portfolio Management Director

Certified Portfolio Manager®
Certified Investment Management Consultant℠
Sources for all facts: Thomson/Reuters, Wikipedia. Research Sources: Morgan Stanley Smith Barney LLC, First Trust Advisors, Franklin-Templeton Investors, Riverfront Investment Group, Portfolio Management Institute

If there is a specific fact or reference you'd like a more detailed citation for, please contact us and we can provide the source.

1Michael Jones, Brian Wesbury, Robert Stein and Strider Elass are neither employees nor affiliated with Morgan Stanley Smith Barney LLC. Opinions expressed by them are solely their own and do not necessarily reflect those of Morgan Stanley Smith Barney.

2Portfolio Management Institute is an independent association of discretionary portfolio managers within Morgan Stanley Smith Barney LLC, dedicated to educating and improving the skills of its members.

The information set forth was obtained from sources we believe to be reliable, but we do not guarantee their accuracy or completeness.

The views expressed herein are those of the author and do not necessarily reflect the views of Morgan Stanley Smith Barney or its affiliates. All opinions are subject to change without notice. Neither the information provided nor any opinion expressed constitutes a solicitation for the purchase or sale of any security. Past performance is no guarantee of future results.

This material does not provide individually tailored investment advice. It has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The strategies and/or investments discussed in this material may not be suitable for all investors. Morgan Stanley Smith Barney LLC recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a Financial Advisor. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives.

S&P 500 Index is an unmanaged, market value-weighted index of 500 stocks generally representative of the broad stock market.

Dow Jones Industrial Average is a price-weighted index of the 30 "blue-chip" stocks and serves as a measure of the U.S. market, covering such diverse industries as financial services, technology, retail, entertainment and consumer goods.

Index information is provided for informational purposes only. An investment cannot be made directly in a market index.

Portfolio Management is an advisory program in which the client's Financial Advisor invests the client's assets on a discretionary basis in a wide range of securities.

Morgan Stanley Smith Barney LLC. Member SIPC. CRC Reference Code 509072.