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February Review of Global Financial Markets

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Commentary & Summary – The market's overall mood has brightened considerably from last fall as the winter rally roars on and the markets are off in 2012 to their best start in years. On a year-to-date basis through February 3, NASDAQ is the real star up 11.5%, with the S&P 500 Index up 6.9% and the Dow up 5.3%. Global markets are also participating with the Dow Jones Americas Index up 8.2%, Europe also up 8.2% (Stoxx Europe 600 Index), and the Dow Jones Asia-Pacific Index up 9.4%.

The global stock market rally has pushed many of the tough global issues off the front burner for now, but they have not gone away and will undoubtedly resurface sooner than we would wish. Think DEBT as far as the eye can see in the U.S. and Europe. Think Iran, Israel, Syria, the Strait of Hormuz, nuclear threats in the Middle East, and so on, the list is endless and politicians seem unwilling and unable to deal with them. But the markets are strong and investors are recovering some of their losses, and that is what counts, at least for now.

At its last meeting, the Federal Reserve pledged to keep interest rates low through 2014, for three years! While this appeals to those already indebted, it risks inflation and hurts savers, especially retirees. It also forces savers to take on more risk in order to generate the income they need to pay their bills. And this is just a pledge. Bernanke himself has said that if inflation rises above the Fed's magic 2%, it will have to raise rates anyway.

Another event that caught our attention was the Facebook IPO filing with the SEC. It's hard not to be impressed by its size and global reach. According to the filing Facebook has 845 million active users; 179 in the U.S. and Canada, 212 million in Asia, 229 million in Europe and 225 million elsewhere. The filing alone has renewed investors' interest in tech stocks. Some have estimated that 27-year old Mark Zuckerberg alone will be worth about \$30 billion after the IPO is completed in the spring, and there are many other insiders who will make millions when the stock starts trading. Zuckerberg attended Harvard, which just celebrated its 375th

anniversary, and during that time its endowment, the largest of any educational institution, has amassed a little over \$30 billion.

And as expected, Kodak, founded by George Eastman in 1880, filed for bankruptcy protection under Chapter 11.

It is likely that volatility will continue scaring investors, but we still consider any weakness as an opportunity to accumulate stocks gradually. As we noted last month, we want to take advantage of volatility not become a victim. To do so investors need to have a greater than normal reserve of cash, so that when opportunities arise they have some firepower. It is always difficult to sell winners to raise cash, so remember the old Wall Street adage; sell when you can, not when you have to. Also, be prepared for the inevitable corrections that enable you to add to core positions at lower prices.

In all of this we are mindful of two things. No one knows what the markets will do in the future, and rallies often start when things look the bleakest.

1. **S&P 500** – This index closed last week at 1344.90 within 2% of its 2011 peak. Year-to-date it is up 6.9% but still 14% below its all-time high of 1565.15.



2. **NASDAQ** – Closed the week at 2905.66, hovering near an 11-year high. Year-to-date it is up 11.5% but still 42% below its all-time high of 5048.62.



3. **Dow Jones Industrials** – And the Dow closed at 12,862.23 testing its 2011 high. Year-to-date it is up 5.3% but still 9% below its all-time high of 14,164.53.



4. Stocks above 200 DMA – In our opinion this is one of the most important charts to use when trying to determine whether stocks are oversold or overbought. In past issues we have noted that investors who ignore the data are generally sorry. You will find more detail in our December 2011 issue.



5. Election Cycle – The 3rd and 4th year are generally good for stocks, but since 2011 was 0% you could make the argument that 2012 may be good to make up for 2011. Or you could say that we have already enjoyed the gains from this presidential cycle in 2009 and '10 and we should not expect more.

Party	President	First Year	Second Year	Third Year	Fourth Year
R	Coolidge	1925 N/A	1926 11.1%	1927 37.1%	1928 43.3%
R	Hoover	1929 -8.9%	1930 -25.3%	1931 -43.9%	1932 -8.9%
D	FDR - 1st	1933 52.9%	1934 -2.3%	1935 47.2%	1936 32.8%
D	FDR - 2nd	1937 -35.3%	1938 33.2%	1939 -0.9%	1940 -10.1%
D	FDR - 3rd	1941 -11.8%	1942 21.1%	1943 25.8%	1944 19.7%
D	FDR / Truman	1945 36.5%	1946 -8.2%	1947 5.2%	1948 5.1%
D	Truman	1949 18.1%	1950 30.6%	1951 24.6%	1952 18.5%
R	Ike - 1st	1953 -1.1%	1954 52.4%	1955 31.4%	1956 6.6%
R	Ike - 2nd	1957 -10.9%	1958 43.3%	1959 11.9%	1960 0.5%
D	Kennedy / Johnson	1961 26.8%	1962 -8.8%	1963 22.7%	1964 16.4%
D	Johnson	1965 12.4%	1966 -10.1%	1967 23.9%	1968 11.0%
R	Nixon	1969 -8.5%	1970 3.9%	1971 14.3%	1972 19.0%
R	Nixon / Ford	1973 -14.8%	1974 -26.5%	1975 37.2%	1976 23.9%
D	Carter	1977 -7.4%	1978 6.4%	1979 18.6%	1980 32.5%
R	Reagan - 1st	1981 -4.9%	1982 21.5%	1983 22.6%	1984 6.2%
R	Reagan - 2nd	1985 31.7%	1986 18.7%	1987 5.3%	1988 16.6%
R	Bush	1989 31.7%	1990 -3.1%	1991 30.5%	1992 7.6%
D	Clinton - 1st	1993 10.1%	1994 1.3%	1995 37.6%	1996 23.0%
D	Clinton - 2nd	1997 33.4%	1998 28.6%	1999 21.0%	2000 -9.1%
R	Bush, GW - 1st	2001 -11.9%	2002 -22.1%	2003 28.7%	2004 10.9%
R	Bush, GW - 2nd	2005 4.9%	2006 15.8%	2007 5.5%	2008 -37.0%
D	Obama	2009 26.5%	2010 15.1%	2011 ---	2012 ---
Average		8.1%	9.0%	19.4%	10.9%

Source: Thomson Reuters.

6. Emerging Markets – This is a great table ranking 19 emerging market countries by how their stocks have performed in each of the last 10 years. Note this is only part of the chart. To access the complete chart click on the link below and be patient depending on how efficient your computer is, or go to www.usfunds.com and click on Periodic Table of Emerging Markets.

The Periodic Table of Emerging Markets							
2008		2009		2010		2011	
	Chile -22.13%		Russia 124.69%		Peru 64.99%		Philippines 7.65%
	Mexico -22.70%		Argentina 118.21%		Argentina 54.35%		Indonesia 5.40%
	South Africa -23.06%		Turkey 102.46%		Indonesia 49.52%		Malaysia 4.45%
	Colombia -26.88%		Peru 100.99%		Thailand 47.04%		Thailand 3.45%
	Malaysia -36.23%		Indonesia 92.10%		Philippines 43.26%		South Africa 2.76%
	Korea -39.66%		Taiwan 83.31%		Chile 37.59%		Mexico -2.39%
	Brazil -41.22%		India 83.25%		Colombia 36.04%		Korea -10.97%
	Taiwan		Brazil		Turkey		Chile

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Going forward, growth in the global economy will most likely be in emerging markets rather than the mature and heavily indebted developed countries. To participate using an ETF we use the Vanguard MSCI Emerging Markets ETF (VWO). Frankly we trust Vanguard more than other firms and like the fact the fund is a hybrid with 75% in emerging markets and 25% in developed markets thereby reducing volatility. We also like individual countries like Russia (RSX) and Singapore (EWS). And we are ready to move on China when we see a turn using FXI.

7. Bonds – Note the stampede from equity funds into bond funds starting in 2007. Our guess is that this will end badly when the Fed runs out of ammo.

Epic Exodus

Out of the stock frying pan, into the bond fire

Year	U.S. Equity Funds (mil)	Total Bond Funds (mil)
Annual Average 1990-1998	\$99,331	\$27,193
1999	\$176,341	-\$4,081
2000	261,381	-50,042
2001	54,509	87,878
2002	-26,228	141,525
2003	119,988	33,089
2004	100,984	-10,921
2005	18,018	31,166
2006	290	60,428
2007	-64,709	108,318
2008	-147,496	29,542
2009	-27,711	380,417
2010	-94,663	241,397
2011*	-131,652	128,482

*Includes December data, which is estimated.

Source: ICI, Barron's WWW.AGORAFINANCIAL.COM

8. Dividends – There are more than 40 dividend-focused ETFs available to U.S. investors featuring a wide variety of product types and investment objectives; there are dividend ETFs covering U.S. stocks, developed international economies, and emerging markets. There are ETFs that focus solely on high yielding financial stocks (KBWD) and others that avoid the financial sector entirely (DOO). Consistency of distributions should be a core component of dividend-focused strategies. SDY, PFM and VIG are some that focus on consistency.

If you are looking for individual stocks, you may find the list below published in the January 23, 2012 issue of Barron's, page 20, of interest. The accompanying article in Barron's also list 10 blue chip stocks with stingy dividends or no dividends that may be pressured into raising their dividends in the future. The list includes XOM, AMGN, DIS, CSCO, UNH, ORCL, AAPL, BRK.AQ, DTV, and GOOG.

Dividend Leaders

These stocks offer bond-like yields of 4% or more, and their dividends look sustainable. Such companies as AT&T, Pfizer and Merck have been lifting payouts.

Company/Ticker	Recent Price	Dividend Yield	Annual Dividend	Payout Ratio
Federated Investors / FII	\$18.27	5.3%	\$0.96	61.2%
AT&T / T	30.42	5.8	1.76	72.4
Leggett & Platt / LEG	23.60	4.8	1.12	76.5
Lockheed Martin / LMT	83.71	4.8	4.00	50.2
Amer Electric Power / AEP	41.10	4.6	1.88	59.5
NYSE Euronext / NYX	27.21	4.4	1.20	44.6
Merck / MRK	39.26	4.3	1.68	43.7
Cablevision Systems / CVC	14.24	4.2	0.60	46.6
Waste Management / WM	33.85	4.2	1.42	61.6
Pfizer / PFE	21.84	4.0	0.88	37.9

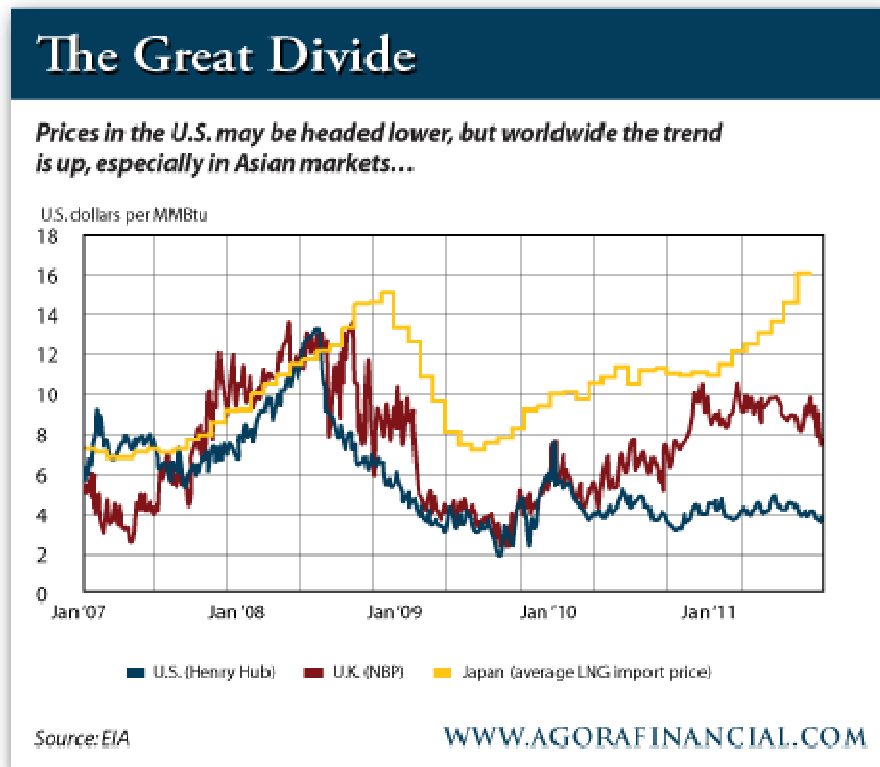
Sources: FactSet; Bloomberg

9. Natural Resources – Another great table from U.S. Global Research. In our opinion, every portfolio should have a significant allocation to natural resources.



Source: Bloomberg and U.S. Global Research

10. Natural Gas – We love out-of-favor sectors such as natural gas. When the recovery comes, and it will come, long-term and patient investors will make a lot of money. Note the prices in Japan are \$16 per MMBtu, in the U.K. \$8, and in the U.S. less than \$4. What do you think the large U.S. producers of natural gas are doing right now? Planning and building facilities to convert stranded natural gas in the U.S. to liquefied natural gas (LNG) so they can ship it to Asia, Europe and other locations.



11. Eastman Kodak – There is nothing we can add to the extensive coverage of Kodak’s bankruptcy and its affect on shareholders, employees, retirees and other stakeholders. There is much discussion of whether or not the common stock will have any value going forward. We don’t know and are hearing arguments on both sides. For those interested, the new trading symbol is EKDKQ.



12. New Arc Model - Bullish

Indicator	Current	Last Week	Last Month	Interpretation
Economy				
C-Score	901	901	910	9 Mo Recession Prob <5%
Super Index	14.1%	11.5%	17.1%	4 month Recess Probability
Risk				
SLFSI	0.575	0.64	0.765	Moderate Risk
Market				
% Positive sectors	100%	95%	81%	Strong
Median Strength	29	22	15	Neutral
% Penalty Box	29%	33%	33%	Moderate Uncertainty
30-Day Forecast	Bullish	Bullish	Bullish	

Sources: Stlouisfed.org, PowerStocks Research, and NewArc Investments, Inc. ©2012