

GUARDIAN

A PUBLICATION FOR THE CLIENTS OF PORTFOLIO STRATEGIES, INC.

Market Commentary

by Bill Whatmough, Senior Portfolio Manager



Sixth century B.C. philosopher Lao Tzu once observed, "Those who have knowledge, don't predict. Those who predict, don't have knowledge." Yet, there are financial pundits out there trying to do just that, many times, unsuccessfully.

Instead of guessing what the market might do in the future, we feel it is important that we monitor your account daily and make adjustments according to what the market is actually doing. This is just one of the many benefits of having Portfolio Strategies manage your account.

John Williamson
Managing Partner

U.S. STOCKS CLOSED SHARPLY HIGHER for the month of March, wiping out small losses in most of the major market averages that were incurred in the first two months of the year. Gains for the month were strongest among the smaller capitalization stocks as the Russell 2000 Index led the way gaining almost 8.1% in March to close the first quarter up 8.8% for the year. The Nasdaq Composite also rose smartly, up 7.1% for the month bringing their first quarter gains to 5.8%. Larger cap issues lagged a bit as the S&P 500 Index gained 6.0% while the Blue Chip dominated Dow 30 Industrials tacked on 5.3% in March, bringing their first quarter gains to 5.3% and 4.8% respectively.

Improvements in the rate of change for a number of key economic indicators gave investors hope that the economy is slowly building a sustainable base. These indicators included new consumer goods orders, capacity utilization, employment, and hours worked. It is good to see the numbers positive, but there is a long way to go to replace the eight million plus jobs that have disappeared over the last three years. The markets were able to fight off some disappointing news as well. Other key indicators such as building permits, housing starts, consumer spending, consumer

confidence, and durable goods orders slowed from previous quarters. Since real estate and housing has been the main motivator of the economy for the past several years, it will be important to see improvement in this area. Likewise, since consumers drive the economy, if consumers don't become more confident soon, further expansion of the economy is unlikely.

Meanwhile, the Fed is likely to continue to try to decrease the money supply and begin to lift interest rates. The Fed tried to decrease the money supply in January and both the stock and bond markets tumbled. In reaction

to that, the Fed once again increased the money supply and markets once again surged in the month of March. Despite all of the Fed's talk about an exit strategy, it does not look like the Fed is confident enough of the economic underpinnings to get out of the stimulus business quite yet. ❁

Source for indices returns is Zephyr StyleADVISOR.



The Guardian is published by:

Portfolio Strategies, Inc.

1724 West Union Avenue, Suite 200

Tacoma, WA 98405

(253) 383-1676 or (800) 959-2001

Website: www.portstrat.com

Financial News and a Grain of Salt

IN ONE OF OUR FAVORITE MONEY MANAGER INTERVIEWS, the manager is asked to account for his recent investment success. He replies that it was due to deciding to ban financial news broadcasts from the office. Turning off the television not only saved time spent watching market updates but also gave the manager an opportunity to form his own unbiased view of the market and individual investments.

While financial news can be great entertainment, it's easy to get a distorted view of the financial markets and individual investments if you rely on the news media. In fact, one contrarian indicator is to bet against any company or market prognosis featured on a major magazine cover. The theory is that by the time the trend reaches the cover of a major publication, the news is already fully reflected in stock prices. The only way for prices to go is in the opposite direction.

To test the contrarian indicator, three finance professors at the University of Richmond reviewed headlines from stories in *Business Week*, *Fortune*, and *Forbes* for a 20-year period. Their goal was to determine whether positive cover stories were followed by superior future performance and negative stories preceded inferior future performance in comparison with an index or another company in the same industry and of the same size.

Based on 549 cover stories, categorized positive and negative, the professors found that after the stories were published companies that received the most positive coverage underperformed while those who suffered negative coverage overall managed to beat the market.

What's happening?

By the time news makes the front cover of a major publication, all too often, it's not news. The market has typically already priced the information into share prices. The market decline in 1987 resulted in a rash of articles at the market's bottom that were the exact reverse of future reality. Among the 1987 cover stories were:

U.S. News - How to Ride Out the Bear Market

Newsweek - Heading Off Hard Times

Time - The CRASH

Business Week - How Bad?

As the researchers pointed out in their paper, "positive stories generally indicate the end of superior performance and negative news generally indicated the end of poor performance." The market has repeatedly turned around and performed exactly opposite of media expectations. Individuals who use the news coverage as the basis of their investment decisions are all too often destined for failure.

Our advice to individuals is to regard financial news as entertainment rather than a reliable view of the future. Take it with a grain of salt. Be aware that favorable news may already be reflected in the value of the investment. Investing based on news coverage has a very poor track record of success. 🍷

PRRST STD
U.S. POSTAGE
PAID
TACOMA WA
PERMIT 356

1724 West Union Avenue, Suite 200
Tacoma, WA 98405

PORTFOLIO STRATEGIES
INVESTMENT MANAGERS

