

Compass Points

Bringing you our latest tactical investing ideas



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Overview

This bi-weekly update provides an in-depth look at the latest tactical investment thoughts from LPL Financial Research as presented in the Portfolio Compass. This publication is designed to cover a broad investment landscape and present ideas to assist when considering portfolio strategy and to customize investment solutions.

Prudence on Precious Metals

	Fundamentals	Technicals	Valuation	View			Bias
				Negative	Neutral	Positive	
Commodities - Precious Metals	●	●		■	■	● ← ○	
Consumer Discretionary	●	●	●	■	■	●	→

● Negative ● Neutral ● Positive

As of 08/31/11

Please refer to the Portfolio Compass publication for complete details.

Compass Changes

- Downgrading Precious Metals to neutral/positive from positive
- Adding a positive bias to our neutral view of the Consumer Discretionary

Investment Takeaways

- Our investment view is little changed since our last publication. We believe financial markets have taken an overly pessimistic view of the global economy and are biased to increase exposure to stocks and economically cyclical investments. Until then we remain cautiously positioned as we await confirmation from economic reports and policy makers.
- We downgraded Precious Metals following recent price appreciation. Precious metals may continue to play a role in investment portfolios, but the recent surge in gold prices warrants a more cautious view.

Economy

- Economic data, on balance, reflected modest deterioration since our last publication. Weakness among regional manufacturing surveys garnered the most attention with the Philadelphia Fed Index exhibiting particular weakness. The survey period for the Philly Fed report took place between August 8–12, 2011, a period of extreme volatility in the stock market and likely adversely affected sentiment. We believe the poor results may have been exaggerated but, nonetheless, forecasts for the broader, national Institute of Supply Management (ISM) manufacturing survey are now lower. The upcoming ISM report may reflect economic contraction but not necessarily a recession. Weekly jobless claims have increased slightly but,



on a positive note, consumer spending has been resilient. Aside from the ISM report, monthly jobs data will provide the latest top-tier economic data on the economy. While the odds of recession have increased we believe the economy will avoid recession and resume growing from the current soft patch.

Equity and Commodities Asset Classes

- We downgraded Precious Metals to neutral/positive from positive following a surge in gold prices. While we believe precious metals can continue to play a role in portfolios, given policy makers attempt to reflate developed country economies and our view that the U.S. dollar may remain under downward pressure, the recent price increase warrants a more cautious. Since early July, the price of gold surged from just over \$1500 per ounce to \$1900 before finishing the month just above \$1800. Such acceleration may be unsustainable and subject to a short-term correction in our view. Furthermore, the near-term benefits of precious metals are reduced with stocks and bond markets mostly pricing in a recession. Additional near-term price appreciation may be limited.

Equity Sectors

- We added a positive bias on the Consumer Discretionary sector. Consumer spending has remained remarkably resilient through recent market turmoil and is also reflected in the resilience of Consumer Discretionary stocks as well. Going forward, the sector may be poised to benefit from good back-to-school shopping results and, being one of the more economically sensitive sectors, poised to benefit from further improvement in the broad stock market.

Fixed Income

- Corporate bond markets, high-yield bonds in particular, have diverged from the recent improvement in stock prices. We believe more economically sensitive segments of the bond market, such as corporate bonds, have shown greater sensitivity to European bank funding fears as a result of the European debt problem. While measures of banking stress are elevated (see this week's Bond Market Perspectives for more) they are generally below levels of spring 2010 and well below levels that prevailed during the financial crisis. We continue to find value in corporate bonds, particularly high-yield, and improvements in key measures of bank funding pressures, perhaps as a result of new policy initiatives from European leaders, would serve as a positive catalyst for corporate bonds.



IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide or be construed as providing specific investment advice or recommendations for any individual. To determine which investments may be appropriate for you, consult your financial advisor prior to investing. All performance referenced is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

Past performance is no guarantee of future results.

Stock investing may involve risk including loss of principal.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise, are subject to availability, and change in price.

Because of their narrow focus, sector investing will be subject to greater volatility than investing more broadly across many sectors and companies.

High Yield bond portfolios concentrate on lower-quality bonds, which are riskier than those of higher-quality companies. These portfolios generally offer higher yields than other types of portfolios, but they are also more vulnerable to economic and credit risk. These portfolios primarily invest in U.S. high-income debt securities where at least 65% or more of bond assets are not rated or are rated by a major agency such as Standard & Poor's or Moody's at the level of BB (considered speculative for taxable bonds) and below.

A commodity is a basic good used in commerce that is interchangeable with other commodities of the same type. Commodities are most often used as inputs in the production of other goods or services. The quality of a given commodity may differ slightly, but it is essentially uniform across producers.

Corporate bonds are considered higher risk than government bonds but normally offer a higher yield and are subject to market, interest rate and credit risk as well as additional risks based on the quality of issuer coupon rate, price, yield, maturity and redemption features.

The ISM index is based on surveys of more than 300 manufacturing firms by the Institute of Supply Management. The ISM Manufacturing Index monitors employment, production inventories, new orders, and supplier deliveries. A composite diffusion index is created that monitors conditions in national manufacturing based on the data from these surveys.

International and emerging markets investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors.

Consumer Discretionary Sector: Companies that tend to be the most sensitive to economic cycles. Its manufacturing segment includes automotive, household durable goods, textiles and apparel, and leisure equipment. The service segment includes hotels, restaurants and other leisure facilities, media production and services, consumer retailing and services and education services.

The Philadelphia Fed Survey is a business outlook survey used to construct an index that tracks manufacturing conditions in the Philadelphia Federal Reserve district. The Philadelphia Fed survey is an indicator of trends in the manufacturing sector, and is correlated with the Institute for Supply Management (ISM) manufacturing index, as well as the industrial production index.

Precious metal investing is subject to substantial fluctuation and potential for loss.

Precious metals portfolios focus on mining stocks, though some do own small amounts of gold bullion. Most portfolios concentrate on gold-mining stocks, but some have significant exposure to silver-, platinum-, and base-metal-mining stocks as well. Precious-metals companies are typically based in North America, Australia, or South Africa.

This research material has been prepared by LPL Financial.

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