

Compass Points

Bringing you our latest tactical investing ideas



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Overview

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

Economic data has been mixed to weak since our last publication but we still see the economy on track to surpass consensus estimates over the first half of 2010.

The Agriculture Angle

| | Fundamentals | Technicals | Valuation | View | | | Bias |
|----------------------------|--------------|------------|-----------|----------|---------|----------|------|
| | | | | Negative | Neutral | Positive | |
| Commodities - Agricultural | ● | ● | | ■ | ● | ■ | → |
| Energy | ● | ● | ● | ■ | ● | ■ | |

● Negative ● Neutral ● Positive

As of 01/20/2010

Please refer to the Portfolio Compass publication for complete details.

Compass Changes

- Adding positive bias on Agricultural Commodities Asset Class
- Removing positive bias from Energy Sector

Investment Takeaways

- **Positive bias on Agricultural Commodities** – A streak of cold weather coupled with strong Emerging Market (EM) demand support our positive bias on agricultural commodities asset class.
- **Removing positive bias on Energy Sector** – the sector has performed well but after the price of crude oil reached the low 80s, the high end of our expected range, we believe further upside is limited over the near-term.
- **Assessing Currency investments** – We continue to explore opportunities of US dollar strength versus the Yen or the Euro as we expect stronger domestic economic growth and the Federal Reserve (the Fed) to raise rates before the Bank of Japan (BoJ) or ECB. Additionally, both currencies remain elevated relative to the US dollar.
- **Assessing Retailers** – We assess our exposure to the Retail industry within our overweight to the Consumer Discretionary sector following a modestly better than expected holiday shopping season.

Economy

- Economic data has been mixed to weak since our last publication but we still see the economy on track to surpass consensus estimates over the first half of 2010. Most notably, the December jobs report was a clear disappointment with the economy losing 85,000 jobs and failing to extend



improvement seen the prior month. However, weekly jobless claims continue to improve and along with additional stimulus and businesses' need to restock inventories we believe job growth is coming.

- December retail sales were weaker than expected but we note some encouraging signs. Retail sales are up 8% on annualized basis since the end of the third quarter and holiday spending was 1.8% on annualized basis versus consensus expectations of a 1.0% increase. We believe consumer spending expectations remain too low and leave room for an upside surprise to fourth quarter Gross Domestic Product (GDP) and first quarter 2010 GDP estimates.
- We continue to explore select currency opportunities as we span the universe for 2010 but deferred for now due to potential uncertainty surrounding the upcoming Federal Open Market Committee (FOMC) meeting. While our recommended portfolios remain biased towards a weaker dollar, exposure is biased towards emerging market currencies. Over the course of 2010 we believe a de-coupling may occur where select developed nation currencies, such as the Yen and Euro, may depreciate versus the US dollar. U.S. economic growth has been stronger and on a faster track to recovery. Fed rate hikes are likely a ways off but would likely come before the ECB or BoJ produce their first rate hike. Credit issues in Greece also highlight the challenges facing the Eurozone. Of the two currencies, we are still biased towards US dollar strength relative to the Yen.

We place a positive bias on Agricultural Commodities as we believe poor weather and strong EM demand create a favorable supply-demand balance.

With oil reaching a near-term high we believe agriculture may provide a substitute as we look to maintain commodities exposure as part of our broader investment strategy.

Equity Asset Classes and Commodities

- We place a positive bias on Agricultural Commodities asset class as we believe poor weather and strong EM demand create a favorable supply-demand balance. The USDA crop report, which signaled higher inventories of select commodities, led to weakness which we found as an attractive entry point. We believe the next report may counter recent supply findings and the full impact of colder than expected weather over much the past several weeks has not fully been priced into markets. Furthermore, with oil reaching a near-term high we believe agriculture may provide a substitute as we look to maintain commodities exposure as part of our broader investment strategy.

Equity Sectors

- We removed our positive bias on the Energy sector following recent good performance and rise in oil prices. We believe that a price per barrel of oil in the low \$80s is a near-term high and additional gains from energy stocks might be limited. We believe the price of oil will be range-bound between \$70 and \$85 and may seek to add exposure should the price of oil fall to the low end of the range.
- We assessed our exposure to the Retail industry within our overweight to the Consumer Discretionary sector. While we believe that profits for retailers will be good, most earnings reports are several weeks away and may lead to a performance lull following a modestly better than expected

Stock investing involves risk including loss of principal.

The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.



We believe that China will move very gradually and not offset strong domestic demand and strong regional demand that underlies our favorable EM equity and EMD view.

holiday season. Exposure to Industrials, which is likely to continue to benefit from global economic growth, may provide a better immediate-term horizon. In the end, we preferred to maintain existing exposure as we believe there is too much pessimism in Consumer Discretionary stocks generally and margins are likely to be good.

Fixed Income

- Sovereign risks and concerns over China's gradual monetary tightening led to underperformance of Emerging Market Debt (EMD). We are watching China's actions closely but believe that China will move very gradually and not offset strong domestic demand and strong regional demand that underlies our favorable EM equity and EMD view. Although central bank hikes are a risk for EMD, we still believe the pace of increases will be gradual and not enough to offset neither the income advantage nor the upward credit quality trends of the sector.

IMPORTANT DISCLOSURES

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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.

High Yield/Junk Bonds are not investment grade securities, involve substantial risks and generally should be part of the diversified portfolio of sophisticated investors.

Mortgage-Backed Securities are subject to credit risk, default risk, prepayment risk that acts much like call risk when you get your principal back sooner than the stated maturity, extension risk, the opposite of prepayment risk, and interest rate risk.

Alternative investments may not be suitable for all investors and should be considered as an investment for the risk capital portion of the investor's portfolio. The strategies employed in the management of alternative investments may accelerate the velocity of potential losses.

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

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

The market value of Corporate Bonds will fluctuate, and if the bond is sold prior to maturity, the investor's yield may differ from the advertised yield.

Small Cap stocks may be subject to higher degree of risk than more established companies' securities. The illiquidity of the Small Cap market may adversely affect the value of these investments.

Mid capitalization companies are subject to higher volatility than those of larger capitalized companies.

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