



# Weekly Market Commentary



April 5, 2010

## When Leading Indicators Peak

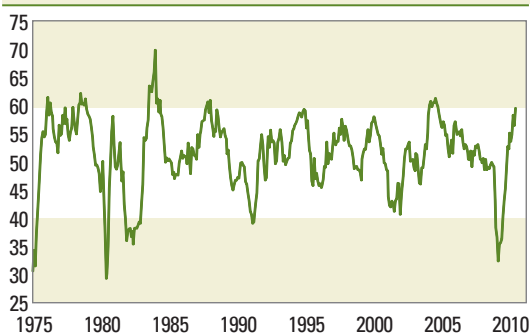
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#### Highlights

- The first quarter of 2010 was a good one for investors. However, leading economic and market indicators may be close to peaking which may result in weaker market returns going forward.
- While the Institute for Supply Management Purchasing Managers Index (ISM) has given a consistent signal when the recession is ending, it also signals when the recovery momentum peaks and the economy begins to transition to a new stage.
- Last Thursday's ISM reading for the month of March at 59.6 may be at or near a peak. Historically, over the six months following the peak in the ISM, stocks were up only 1%, on average, after posting strong gains leading up to the peak.
- With leading indicators, such as the ISM, at or near a peak, stock market price momentum may begin to fade and a focus on yield may be more appropriate. Both High-Yield Bonds and Real Estate Investment Trust (REIT) may offer attractive yields able to boost total return.

1 ISM Index



Source: LPL Financial, Bloomberg 4/2/10

The first quarter of 2010 was a good one for investors. The stock market, measured by the S&P 500, posted a total return of 5.4%. Small company stocks, measured by the Russell 2000 index, were up an even stronger 8.9%. Even bonds, as measured by the Barclays Aggregate Bond Index, were up a respectable 1.8%. However, we believe gains are likely to be more modest going forward. One of the factors supporting our belief is that leading economic indicators may be at or near a peak.

One of the best leading indicators for the economy and markets is the Institute for Supply Management Purchasing Managers Index (ISM). The Institute for Supply Management is a group that represents purchasing managers. They survey them each month and publish the results in the form of an index. Purchasing managers are at the front of the line when it comes to activity in manufacturing. Manufacturing companies need supplies to produce products and purchasing managers order these supplies. When demand starts to pick up for manufactured goods these managers need to order more supplies. When demand pulls back they respond by trimming their orders.

Although manufacturing makes up only about 40% of S&P 500 company earnings, demand for manufactured goods has proven to be a timely barometer of business activity of all types. This index is published at the beginning of each month offering one of the earliest signals as to how the economy and outlook for business is faring each month.

The long history of the ISM shows us how effective it has been in signaling each recession and recovery. While the ISM has given a consistent signal when the recession is ending, it has also signaled when the recovery momentum peaks and the economy begins to transition to a new stage. Looking back at the ISM over the past 35 years we can see that there have been a number of peaks and troughs that led the direction of economic and profit growth. The index has typically troughed around 30-40 and peaked around 60. [Chart 1]

Last Thursday, April 1, the ISM was reported for the month of March and the stock market welcomed the good news that the index rose to 59.6. However, now that it is at 60, there is a key question for investors: is it at a peak? If it is, returns are likely to be flat and volatile going forward.

The S&P 500 has tended to perform very well during the year leading up to the peak in the ISM. Over the past 35 years, the S&P 500 was up 18%, on average, in the 12 months prior to the peak in the ISM. However, once reaching the peak returns were flat and volatile. Over the six months following the peak, stocks were up only 1%, on average.

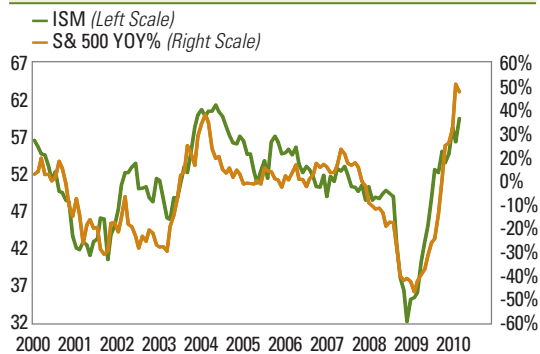


ISM Peak	S&P 500 Price Change	
	12 Months Before Peak in ISM	6 Months After Peak in ISM
Feb. 1976	22.2%	3.2%
Jul. 1978	1.85%	-0.7%
Nov. 1980	32.4%	-5.6%
Dec. 1983	17.3%	-7.1%
Oct. 1987	3.2%	3.8%
Oct. 1994	1.0%	9.0%
Jul. 1997	49.1%	2.7%
Nov. 1999	19.4%	2.3%
May 2004	16.3%	4.7%
<b>Average</b>	<b>18.1%</b>	<b>1.3%</b>

Source: LPL Financial, Bloomberg 4/2/10

The S&P 500 is an unmanaged index, which cannot be invested into directly. Past performance is no guarantee of future results.

## 2 ISM and S&P 500 Year-Over-Year Performance



How closely the performance of the stock market and the ISM track each other can best be seen in the nearby chart. [Chart 2] With momentum in the ISM at or near a peak, stock market performance is likely to stall and become more sideways and volatile.

We will watch the LPL Financial Current Conditions Index (CCI) closely for confirmation of a peak in economic momentum. The CCI has continued to push higher, but it is also likely near a peak. Other indicators like the slope of the yield curve and commodity prices may also be at or near a peak. With leading indicators, such as the ISM, at or near a peak stock market price momentum may begin to fade. As stock market price momentum fades, a focus on yield is appropriate. Both High-Yield Bonds and REITs may offer attractive yields able to boost total return.

### IMPORTANT DISCLOSURES

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

Stock investing involves 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 and are subject to availability and change in price.

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Barclays Aggregate Bond Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell Index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index.

High-yield/junk bonds are not investment grade securities, involve substantial risks and generally should be part of the diversified portfolio of sophisticated investors.

Investing in real estate/REITs involves special risks such as potential illiquidity and may not be suitable for all investors. There is no assurance that the investment objectives of this program will be attained.

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.

The fast swings of commodities will result in significant volatility in an investor's holdings.

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