

# Rochester Financial Services

Fee-Only® Financial Management Services

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October 5, 2011

Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Gold	Crude Oil
10,940	1,144	2,461	658	1.88%	8.30%	\$1,640	\$79.55

Principal



## Investment Strategy Report

### Stocks Suffer Another Month of Steep Losses As Europe and Now China Remain Concerns

When the market "crashed" in early August and then experienced a 10% rebound, the tendency was to believe that the worst was over. The S&P 500 had hit an intraday low of 1101 and a closing low of 1119 on August 8th and 9th. It ended the month significantly higher at 1219 amidst a feeling that Europe was getting its house in order and the threat of the European contagion had diminished. However, market historians will tell you that the stock market often likes to retest its lows, especially this time of year. Looking back, I now know that the end of August would have been a good time to raise cash. But we always want to believe that it's different this time, that lows don't have to be retested and September doesn't have to be a bad month for stocks (it happens to be the worst). For most of September, the stock market traded in a narrow range, a far cry from the extremely volatility of August. And then at the end of the month, the market fell apart, with most of the losses occurring this past Friday (Sept. 30th) and Monday (Oct. 3rd). Between those 2 days and the early part of yesterday (Oct. 4th), the market dropped 7.3%. It not only tested the Aug. 8th and 9th lows, but it plunged right through them and hit a new intraday low of 1075 yesterday. However, since 3 pm yesterday through the end of trading today, the market staged a dramatic rebound to recover most of those 3 days of losses, putting us back in that trading range.

Looking at the performance of our portfolios for last month was particularly frustrating because not only did our US stock funds get hit, but all the sectors that we have for diversification suffered badly. Especially hard hit were the gold stocks and emerging markets. And this brings up the concern about China that entered the picture a few weeks ago. China has been one of the true bright spots in the world economy the past few years, as it has sported an economic growth rate in the neighborhood of 10%. The problem with growth rates that high is that they are not sustainable. Periods of boom are invariably followed by periods of bust, unless the country can engineer a "soft landing", a moderation of growth to a more reasonable level. This past month, reports from China indicated that growth was slowing, but investors feared that instead of a moderate slowdown, it would be an extreme one which would lead to a substantial drop in China's demand for raw materials. This caused a drop in the price of all commodities and precious metals. Commodity and mining stocks got hit hard as did emerging market stocks. My feeling is that the selling was overdone. China is still projected to grow at a 6-7% rate which might qualify it for the sought after soft landing. As for the future of gold stocks and emerging market stocks, here is what Steve Sjuggerud of Stansberry Research has to say:

"Emerging markets are incredibly cheap right now. They're paying a 4% dividend yield. Dividends reached this high in 1985 and these stocks soared 4-fold in less than a year. Yields came close in 1993 and 2003. In both cases, these stocks soared 3-fold. It happened in the bust of 2008-09 and these stocks nearly doubled after that (10/3). He goes on to talk about gold. "Gold stocks are 19% undervalued. Over the last 8 years, whenever gold stocks have gotten this cheap, triple digit returns have followed soon after" (10/5). And about stocks in general, "Many major stocks around the world haven't been this cheap in a generation (except for the bottom in March 2009). Commodities are now cheap. Real estate is an extraordinary value. I wouldn't be surprised to see many different assets double within 2 years after the market bottoms" (10/5).

Bond funds also did not do well last month, as selling hit all investment sectors. I finally sold our positions in the Yieldquest fund. While I still feel that there is a strong possibility that interest rates will be going higher, there are other funds that I will be using to balance out our fixed income holdings.

In summary, while I share in your frustration at the losses we have sustained, I do feel optimistic that despite the economic problems that exist throughout the world, there will be opportunities that will present themselves in the coming months.

**Required IRA Distributions for 2011** - For those of you who are either over 70 or have inherited IRAs, I will be contacting you over the next several weeks to plan your required distributions for this year. *Jeff Feldman*

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