

**Market Outlook:**

**The well-informed investor**

We've been watching for several weeks as the stock averages have been registering a series of new highs, wondering how the effusiveness of owning stocks *really* corresponds to the underlying news and data. I'm still of the belief that you must play these rallies selectively and cautiously. This is truly where an investment discipline becomes more valuable than hyperbole or hunch.

I've tried also to point out in these missives that the divergences in the numbers are subtle, but significant enough that there is no such thing as a sure bet or an all encompassing A to Z rally. Even if your portfolio is currently "in the black" for the year, you can't afford simply to rest on your laurels at these lofty heights.

Having said that, we are far from morphing into a huge negative bear phase. To the contrary, the rally is justified and based upon years of rebuilding and economic reorganization. It's just that not every sector, nor every stock, is matching up against others with the same degree of precision.

We remain bullish on those sectors that demonstrate end-user demand (biotech, energy, utilities) at the same time favoring categories that hedge our portfolio's bullish posture (basic materials, foodstuffs, cyclicals). Somewhere in the middle lies the great unknown both in terms of equity price performance as well as earnings expansion potential (financials, industrials).

The coming months are going to be revealing as we digest all sorts of exogenous news events (terrorism, politics) and organic machinations (new highs, trend reconfigurations). It is important to be aware both of the positives *and* negatives that inject themselves into any comprehensive analysis. Without a doubt there are plenty of variables on both sides of the equation.

One must also factor that trends are transitory, constantly ebbing and flowing, and that nothing...in either direction ...is indelible or permanent.

That is why we continue to look for "one-off" transactions to fill in the gaps, and also to broaden our portfolio diversification. While there certainly might be some unavoidable valuation capitulation in the near future, we don't want to give it all back by inadvertently forgetting our fundamental tenet that *asset allocation plays a greater role in the probability of portfolio capital appreciation than does any single security within that portfolio.*

In conclusion, we view the current market trends as solid but pointing towards a possible exhaustion.

**Primer**

When evaluating a "trend" we look not only at where we are, but where we've come from. In that regard we are clearly topside of the current price trend in the global averages and relative strength integers. Think about it: we would not only have to confirm current underlying statistics to move higher from here, but also to place our faith in the fact that gains will extend several standard deviations well above their valuation levels begun nearly six months ago.

By definition, quantitative science tells us you can't fill a vessel "fuller than full" (100%) nor empty it more than "empty". One would conclude, then, that successful portfolio management at this juncture breaks down to a game of statistics in which you, the investor, must decide "*how much is enough?*" The worst thing any client can do is to become greedy.

What if you miss the next up-leg? How much is the gamble worth?

One can always find a reason to be bullish about the long term. It's the waves and troughs that I get paid to worry about....

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