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Quarterly Market Review: April-June 2010

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The Markets

Investors who had been waiting for a correction finally got it this quarter as equities took a pause after their year-long rally. Concerns about Europe's ability and willingness to stave off sovereign default, Goldman Sachs's troubles with the SEC, the Gulf oil spill, financial reform, the mysterious "flash crash", and worries about the possibility of a double-dip recession made for a jittery second quarter despite generally strong corporate profit reports.

After reaching the 11,000 mark--a level not seen since before the fall of Lehman Brothers--the Dow erased all its 2010 gains; it's now down almost 13% from its late April high. Volatility reigned, knocking the S&P 500 down just over 15% since late April, while the NASDAQ dropped close to 17% during the same time. Not even the small-cap Russell 2000's Q1 gains could keep it in positive territory for the year; it has fallen the furthest (almost 18%) since its year-to-date high on April 23. Despite the bad quarter, the Russell is still up almost 20% since this time last year, while the broader S&P is more than 12% higher year over year. Even the Global Dow is up 5% from last June.

The volatility sent investors seeking comfort in Treasury bonds. By quarter's end, yields on the 2-year Treasury had briefly hit historic lows as prices rose to reflect demand. Investors preferred shorter maturities, and spreads between 2-year and 10-year yields narrowed as the 10-year yield fell almost half a percent during the quarter. Gold also benefitted from global anxiety, hitting new highs above \$1,250 an ounce, while the dollar rose almost 10% against the euro. Oil prices drifted lower, dropping under \$80 a barrel.

Market/Index	End of Quarter	Quarterly Change	YTD Change
DJIA	9774.02	-9.97%	-6.27%
NASDAQ	2109.24	-12.04%	-7.05%
S&P 500	1030.71	-11.86%	-7.57%
Russell 2000	609.49	-10.19%	-2.54%
Global Dow	1710.71	-15.38%	-13.80%
Fed. Funds Target	.25%	0	0 bps
10-year Treasuries	2.97%	-87 bps	-88 bps

Quarterly Economic Perspective

- Newly hired census workers buoyed unemployment statistics, which remained just under 10%. Inflation stayed relatively benign at the consumer level, which allowed the Federal Reserve to keep its target rate just above zero. However, the Bureau of Labor Statistics said wholesale prices continued to be higher on a year-over-year basis. The Bureau of Economic Analysis said gross domestic product (GDP) for Q1 came in at 2.7%, substantially lower than the previous quarter's 5.6%.
- Eurozone countries agreed to protect the euro by setting up a massive bailout package of loans and loan guarantees designed to prevent restructuring of or default on the sovereign debt of weaker members, such as Greece, Spain, Portugal, and others.
- As the deadline for the first-time homebuyer tax credit drew near, home sales perked up and then fell off a cliff. Despite mortgage rates that Freddie Mac said were the lowest since its recordkeeping began in 1971, by the end of the quarter, new single-family home sales plummeted 32.7% in the space of a month, according to the Census Bureau.

- China announced it will allow its currency to fluctuate more rather than being so closely tied to the U.S. dollar. However, the World Bank foresees soaring housing costs, higher inflation, and a lower trade surplus hampering China's growth this year and next. In turn, the Fed sees current conditions overseas being "less supportive of economic growth" here.
- Regulators here and abroad adopted measures designed to avoid future "flash crashes," such as circuit breakers on individual stocks that move 10% or more in five minutes. Though an investigation into the May 6 drop of nearly 1,000 points in the Dow identified contributing factors, it did not pinpoint specific causes. Hearings into the causes of the 2008 financial crisis, coupled with the SEC's charging Goldman Sachs with fraud, helped speed efforts to put together a financial regulatory reform bill, which neared a vote by Congress as the quarter ended.

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DATA SOURCES--Economic: Based on data from U.S. Bureau of Labor Statistics (CPI/PPI inflation, unemployment); U.S. Dept. of Commerce (GDP, housing starts, retail sales). Performance: Calculated based on data as reported in WSJ Market Data Center (indexes); U.S. Treasury (Treasury yields); U.S. Energy Information Administration/Bloomberg.com Market Data (oil spot price, WTI Cushing, OK); www.kitco.com, www.goldprice.org (spot gold, NY close); Oanda (currency exchange rates). The Dow Jones Industrial Average (DJIA) is a price-weighted index composed of 30 widely-traded blue-chip U.S. common stocks. The S&P 500 is a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy. The NASDAQ Composite Index is a market-value weighted index of all common stocks listed on the NASDAQ stock exchange. The Russell 2000 is a market-cap weighted index composed of 2000 U.S. small-cap common stocks. The Global Dow is an equally weighted index of 150 widely traded blue-chip common stocks worldwide. Market indexes listed are unmanaged and are not available for direct investment.

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