



RESEARCH REPORT

June, 2010

Market Overview & Strategy Comments: *Economic Fundamentals Remain Positive Despite Some Recent External Shocks.*

After a fairly calm first four months of the year, the markets got choppy again last month. The VIX Volatility Index, often referred to as the “fear gauge” because it measures the implied volatility of the S&P 500 index options, tripled at one point in May and ended the month roughly double where it started. We discuss the international shocks that hit our markets.

<u>Key Statistics</u>	<u>Current</u>	<u>Change Since Previous Month</u>	<u>2010 Change</u>
Dow Jones Industrial Average *	10136.63	-7.9%	-2.8%
S&P 500 Index *	1089.41	-8.2%	-2.3%
S&P 500 Ave. P/E Ratio **	13.6x	-1.9x	-2.0x
NASDAQ *	2257.04	-8.3%	-0.5%
1 Year Treasury Bill Yield	0.34%	-7 bps	-13 bps
10 Year Treasury Bond Yield	3.31%	-38bps	-54 bps
30 Year Treasury Bond Yield	4.22%	-31 bps	-41 bps
Municipal Notes - 1 Year Yield	0.70%	+0 bps	+25 bps
Municipal Bonds - 10 Year Yield	3.50%	-10 bps	+0 bps
Reuters/Jefferies CRB Futures	\$254.80	-8.2%	-10.1%
Gasoline NY RBOB (\$ per gal.)	\$2.02	-15.7%	-1.6%
Natural Gas (\$ per MMBtu)	\$4.34	+10.7%	-22.1%
Gold (\$ per Troy oz.)	\$1212.20	+2.7%	+10.7%

* price only ** based on 2010 earnings estimates.

The Reuters/Jefferies CRB Futures Price Index is an arithmetic average of commodity futures prices with monthly rebalancing.

Gasoline NY RBOB price excludes local, state and federal taxes (the “wholesale price”).

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Market Overview & Strategy Comments: *Economic Fundamentals Remain Positive Despite Some Recent External Shocks.*

After a fairly calm first four months of the year, things got choppy again last month. The VIX Volatility Index, often referred to as the “fear gauge” because it measures the implied volatility of the S&P 500 index options, tripled at one point in May and ended the month roughly double where it started. This was its biggest jump since October 2008. Accompanying the jump in fear, last month produced the worst May for the stock market since Germany invaded France in 1940! And while what happened pales in comparison to what happened in May of 1940, one thing is similar – the shocks that hit our markets were for the most part external. While some concerns surfaced after domestic consumer spending slowed in April, the rest of the shocks all came from overseas:

- The trillion dollar rescue package in Europe sparked worries about currency and interest rate stability, as well as the entire structure of the Euro region. Citizens of the countries footing the bill for the bailout – such as Germany and France – and of the countries being bailed out, such as Greece – hit the streets to protest either the costs of the bailout or the austerity measures they included.
- Budget shortfalls cost Spain its AAA debt rating, sparking worries about its banks.
- The slumping euro, which fell over 5% last month and is now down roughly 20% over the past six months, raised fears in Europe about a currency collapse.
- China’s efforts to slow down their housing market sparked fears the global rebound in manufacturing could slow.
- The domestic BP oil spill, while not creating a direct economic impact, has only added to the general level of anxiety and uncertainty facing the global markets.

Contributing to the slide in May was the “Flash Crash” which sent the market down 10% intraday on May 6th. *While we shouldn’t underestimate the risks from these external shocks and the disheartening nature of the market volatility, we also shouldn’t let these worries distract us from the fundamental news that we see as actually fairly good.* It includes:

- Stronger business spending. The CEO of leading capital goods company Eaton noted that “we are really seeing strength in every quarter of the world.” Most companies’ earnings reports characterized the U.S. as recovering, Europe a bit slower, Latin America steady and Asia strong.
- A stable housing market. Despite the end of the first-time buyers’ tax credit, housing affordability is at a record high, prices are down, and inventories of new homes are at their lowest in decades. With mortgage rates back below 5%, we should see a jump in refinancing activity, putting money directly into consumers’ wallets.
- U.S. layoffs are down to pre-recession levels and job growth has resumed.



- Although Europe is facing an expensive bailout, it is likely to see a boost in economic growth due to the weaker euro. Profit estimates for key U.S. exporters are rising and should offset at least part of any slowdown related to government bailout spending cutbacks.
- Strong global growth outside of Europe should give the export sector a boost. India has returned to pre-recession growth rates of over 8% and China's growth is even faster.
- Global inflation is modest, giving policymakers needed flexibility to keep interest rates low. Inflation at the thirty country OECD (Organisation for Economic Co-operation and Development) is stable at around just 1.5%.
- Gasoline prices are down and they may fall further, giving consumer confidence a boost and keeping a lid on household expenses.
- Global leading economic indicators are their highest in over 30 years.

As touched on in the past, our economy's transition from consumption and debt towards exports and savings (savings rates are now up to 3.6%) will take time. Keep in mind that leading up to the recession, housing peaked at roughly half our GDP growth in 2005 and was behind a similar percentage of job growth from 2001 to 2006. Today, however, housing made no contribution to first quarter 2010 growth while exports contributed 20%. Therefore, we must get used to seeing volatility in growth and in the markets. In the short-term, this domestic shift and our dependence on growth outside our borders is making life difficult for investors trying to hold fast to their long-term strategies. However, while little consolation at the moment, not only are we seeing solid economic fundamentals, but positive core indicators for stocks as well:

- Based upon 2010 estimates, stocks are trading for less than 13x earnings. Historically, when inflation and interest rates have been this low, P/E ratios were closer to 17x, 30% higher than current prices.
- \$3 trillion in money funds is still sitting on the sidelines, fuel for future rallies and evidence of investor caution.
- Most widely watched sentiment measures are pointing to bearishness surging and bullishness waning, good news from a contrarian perspective.

While stocks are now in the red for the year, the fundamentals are coming in stronger than we and most others expected at the start of the year. Although the short-term direction of the markets is becoming increasingly unpredictable, the long-term fundamental outlook for stocks appears to still rest on solid ground. Therefore, we recommend that clients maintain the recommended allocation to stocks they selected with their portfolio manager and only change equity weightings due to shifts in their personal needs and objectives.

CORE HOLDINGS LIST FOR 2010

Source: FactSet, First Call, Value Line, Bloomberg & CAM Estimates.

			Recent	2010	2011	2010	2011	Est EPS	P/E to	Market		Div
June 1, 2010	<u>Company Name</u>	<u>Ticker</u>	<u>Close</u>	<u>EPS</u>	<u>EPS</u>	<u>P/E</u>	<u>P/E</u>	<u>Growth</u>	<u>Growth</u>	<u>Cap(\$mm)</u>	<u>ROE</u>	<u>Yield</u>
	Standard & Poors 500	SPX	1,089.41	\$79.91	\$91.81	13.6x	11.9x	8%	1.5x	9,849,403	13%	2.1%
Financials:	Bank Of America	BAC	15.74	\$1.04	\$1.92	15.1x	8.2x	8%	1.0x	157,919	3%	0.3%
	Berkshire Hathaway Cl "B"	BRK/B	70.55	\$3.86	\$4.01	18.3x	17.6x	5%	3.5x	68,345	7%	0.0%
	MasterCard	MA	201.77	\$13.66	\$16.37	14.8x	12.3x	18%	0.7x	22,362	54%	0.3%
Consumer Staples:	Avon Products	AVP	26.49	\$2.00	\$2.33	13.2x	11.4x	9%	1.3x	11,348	64%	3.3%
	Coca Cola	KO	51.40	\$3.43	\$3.74	15.0x	13.7x	8%	1.7x	118,582	30%	3.4%
	Colgate Palmolive	CL	78.09	\$4.84	\$5.34	16.1x	14.6x	10%	1.4x	38,299	91%	2.7%
	Diageo Plc ADR	DEO	61.28	\$4.44	\$4.87	13.8x	12.6x	8%	1.5x	38,381	48%	3.8%
	Fomento Economico Mexico	FMX	42.18	\$2.91	\$3.69	14.5x	11.4x	19%	0.6x	9,116	13%	1.5%
	H.J. Heinz	HNZ	44.18	\$3.00	\$3.24	14.7x	13.6x	10%	1.4x	13,971	59%	4.1%
Health Care:	Becton Dickinson	BDX	71.30	\$5.27	\$5.78	13.5x	12.3x	11%	1.1x	16,637	24%	2.1%
	Johnson & Johnson	JNJ	58.30	\$4.83	\$5.25	12.1x	11.1x	7%	1.5x	160,795	26%	3.7%
	Novartis AG	NVS	45.01	\$4.91	\$5.17	9.2x	8.7x	4%	2.0x	118,719	16%	3.7%
Consumer Discretionary:	Johnson Controls, Inc.	JCI	28.53	\$2.11	\$2.57	13.5x	11.1x	13%	0.8x	19,192	NMF	1.8%
	Target Corp.	TGT	54.53	\$3.83	\$4.37	14.3x	12.5x	13%	1.0x	40,292	17%	1.2%
	Toyota Motor Co. ADR	TM	72.34	\$2.85	\$4.87	25.4x	14.9x	5%	3.0x	124,714	2%	1.3%
Technology:	Cisco Systems	CSCO	23.16	\$1.68	\$1.91	13.8x	12.2x	12%	1.0x	132,270	17%	0.0%
	EMC Corp.	EMC	18.62	\$1.19	\$1.37	15.6x	13.6x	15%	0.9x	38,275	8%	0.0%
	Google	GOOG	485.18	\$27.97	\$32.22	17.3x	15.1x	19%	0.8x	119,271	20%	0.0%
	International Business Machines	IBM	125.26	\$11.26	\$12.40	11.1x	10.1x	10%	1.0x	160,627	74%	2.1%
	Qualcomm	QCOM	35.56	\$2.34	\$2.56	15.2x	13.9x	17%	0.8x	58,332	8%	2.1%
Industrials:	3M Co.	MMM	79.31	\$5.55	\$6.21	14.3x	12.8x	11%	1.1x	56,553	28%	2.6%
	ABB Ltd. ADR	ABB	17.01	\$1.06	\$1.31	16.1x	12.9x	4%	3.2x	39,622	23%	0.0%
	Danaher Corp.	DHR	79.38	\$4.37	\$5.04	18.2x	15.8x	14%	1.2x	25,770	11%	0.1%
	United Technologies	UTX	67.38	\$4.65	\$5.33	14.5x	12.6x	12%	1.1x	62,871	21%	2.5%
Energy:	Apache Corp.	APA	89.54	\$10.14	\$12.86	8.8x	7.0x	9%	0.8x	30,199	NMF	0.7%
	Petroleo Brasileiro S.A. ADR	PBRA	30.97	\$3.90	\$4.39	7.9x	7.0x	6%	1.2x	57,306	20%	0.5%
	Sasol LTD ADR	SSL	36.00	\$3.94	\$5.14	9.1x	7.0x	5%	1.4x	23,007	17%	3.3%
	Schlumberger, Ltd.	SLB	56.15	\$2.91	\$3.92	19.3x	14.3x	15%	0.9x	66,976	18%	1.5%
Telecom Services:	America Movil ADR	AMX	47.34	\$3.77	\$4.31	12.5x	11.0x	13%	0.9x	47,226	46%	1.0%
	China Mobile Hong Kong	CHL	46.57	\$4.27	\$4.40	10.9x	10.6x	4%	2.4x	186,859	24%	3.5%
Transportation:	CSX Corp.	CSX	52.25	\$3.51	\$4.15	14.9x	12.6x	11%	1.2x	20,337	13%	1.8%
Exchange Traded Funds:	iShares MSCI EAFE Index	EFA	48.32	-	-	-	-	-	-	31,572	-	3.0%
	iShares MSCI Emerging Mkts	EEM	38.10	-	-	-	-	-	-	32,284	-	1.5%

0% weighting in utilities and materials.

The above is a list of common stocks currently held in clients' portfolios. Not all stocks are held in all portfolios for various reasons. Upon request we will furnish a list of all equity recommendations made within the past twelve months. This list includes the name of the security, date and nature of the recommendation, price at which the recommendation was acted upon, and the current market price of the security.

It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list.

Please contact Mickey Herst for a copy of the list.

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