



RESEARCH REPORT

May, 2010

Market Overview & Strategy Comments: *The Manufacturing Wheel of Fortune!*

Economists are playing their own version of the game show “Wheel of Fortune” – only instead of trying to guess the letters on the giant game board, they are guessing the letter whose shape best represents the economy’s future performance. In order to provide an easy visual for investors, economists typically pick from three letters – V, W, and M – when trying to describe a recovery. We give our thoughts on the recovery.

<u>Key Statistics</u>	<u>Current</u>	<u>Change Since Previous Month</u>	<u>2010 Change</u>
Dow Jones Industrial Average *	11008.61	+1.4%	+5.6%
S&P 500 Index *	1186.69	+1.5%	+6.4%
S&P 500 Ave. P/E Ratio **	15.5x	+0.1x	-0.1x
NASDAQ *	2461.19	+2.6%	+8.5%
1 Year Treasury Bill Yield	0.41%	+0 bps	-6 bps
10 Year Treasury Bond Yield	3.69%	-15 bps	-16 bps
30 Year Treasury Bond Yield	4.53%	-19 bps	-10 bps
Municipal Notes - 1 Year Yield	0.70%	+10 bps	+25 bps
Municipal Bonds - 10 Year Yield	3.60%	+0 bps	+10 bps
Reuters/Jefferies CRB Futures	\$277.71	+1.6%	-2.0%
Gasoline NY RBOB (\$ per gal.)	\$2.39	+3.7%	+16.8%
Natural Gas (\$ per MMBtu)	\$3.92	+1.3%	-29.6%
Gold (\$ per troy oz.)	\$1180.10	+6.0%	+7.8%

* 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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Securities are identified for illustrative purposes only. This should not be construed as a recommendation to purchase or sell any securities.



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Economists are playing their own version of the game show “Wheel of Fortune” – only instead of trying to guess the letters on the giant game board, they are guessing the letter whose shape best represents the economy’s future performance. In order to provide an easy visual for investors, economists typically pick from three letters – V, W, and M – when trying to describe a recovery:

V – V shaped recoveries are the most straightforward. A steep drop is followed by a sharp turnaround and a rapid recovery. Most V shaped scenarios imply that the downward slope was in some way an overreaction to an external shock from which things quickly recovered.

W – The W shaped scenario implies a sharp drop, followed by a quick bounce back, but then another leg downward. Eventually the recovery resumes, creating the last leg of the W. The W description has been applied not only to the 2008 recession that was followed by today’s growth, but also to the current improvement in housing. A W implies a more bearish outlook, and anticipates the current expansion will run out of steam in the near future before staging a more lasting recovery down the road.

M – An M shaped timeline implies expansion – such as 2002-2007 – followed by a steep drop, but then followed by a sharp recovery, and then another cooling off period. M shapes are somewhere in between bullish and bearish and, at least for the moment, those in the M camp believe we are now in the second upward leg of the cycle – and that a cooling off is just around the corner.

While we believe it’s better to leave this wheel of fortune to others, there are ample signs we are in a sharp cyclical recovery and that it could be sustainable. For example:

- Good economic news is being led by exports and capital investments, both of which drove economic growth last year and in the first quarter of 2010. Strength in these sectors is offsetting drops in new construction.
- The ISM index, which points to the health of the manufacturing sector (above 50 indicates expansion), fell from 50 to 32 during the recession but has since soared to 60, its highest since 2004.
- 2010 profit growth may reach 40%, led by retail, financial and technology companies.
- Most companies are saying that demand growth is coming from Latin America and Asia, with Europe still muted and the U.S. a bit better.
- Domestically there is clearly pent up demand for non durables such as computers, autos and appliances. Both businesses and consumers have hunkered down for the past few years due to the credit crunch and are now replacing worn out items.
- Exports to emerging markets are now 55% of the total, up sharply this past decade, and now exceed those to developed markets. This transition and this new source of growth is a huge plus for the manufacturing sector in the U.S.
- Inflation is low, benefitting from excess capacity.
- Layoffs are receding and job growth is back with some notable technology companies stepping up hiring. Business investment appears to be focused on technology upgrades.
- Savings rates are remaining well above pre-recession levels.



Regardless of which letter economists pick to describe the recovery, it is clear that it is being driven by manufacturing. Exports and business investment are picking up the slack we see in other areas of the economy, such as the construction market and consumer spending. Construction could take years to recover, while consumer spending should remain subdued as consumers build savings and unemployment takes time to come down. Meanwhile, government stimulus may not be able to do much more than it already has done.

For the financial markets, there are several implications. If savings rates stay up and inflation down, bonds should continue to do well despite stronger growth. Moreover, the search for yield continues to support prices; bond fund inflows continue to sharply outpace equity funds, garnering over \$75 billion in the first quarter of the year.

For stocks, we may see the current cyclical led market continue as these companies benefit from massive 2009 cost cutting efforts and a sudden improvement in international demand, not to mention the moderate rebound in domestic demand. The result has been a market advance much more variable than seen in 2009. Several sectors in the S&P are down this year, as investors focus on volatile, highly cyclical, lower quality (rated C&D by S&P) stocks instead of solid citizen growth stocks in the consumer, health care and utility areas.

Still, even after the 2009 and early 2010 rally, U.S. stocks remain their least expensive in at least two decades as earnings reports and estimates soar. During 2008 analysts couldn't keep up with falling outlooks, and now they can't seem to keep up with rising ones; fully 80% of companies have beaten estimates! And if 2011 growth meets current targets, we could be back to all time highs in profits, yet prices are still 20% below their peaks. "The stock market is incredibly inexpensive," said one portfolio manager who works for an \$11 billion asset management firm. "I don't know how the bears can argue against how well corporations are doing. (source: Bloomberg)."

Not surprisingly, stocks such as *United Technologies, Danaher, Target* and *Schlumberger* have been some of our leading performers this year. To broaden our exposure to the recovery, we have also added *CSX* and *Johnson Controls*, and continue to look for opportunities. Many of the economically sensitive stocks we are buying and considering for purchase are beneficiaries of growing levels of investment and consumer demand in emerging economies, which is creating new growth markets for companies which sell auto technology, energy efficiency controls, heating/cooling equipment, networking equipment and a multitude of other products. Many of these are considered mature industries in the U.S. and/or developed Europe, but are emerging industries in places such as Brazil, Mexico, India and China; as incomes rise for emerging economy citizens, they are trading up and buying brand name household products and foods as well as spending money on the first family car, computers, air conditioners and international vacations. As investors, it makes sense to seek out companies who can meet these new and growing demands.

Securities identified are for illustrative purposes only. This should not be construed as a recommendation to purchase or sell any securities. The securities mentioned may or may not be held in all client portfolios. For a list of current recommendations, please see the back page of this report and/or contact your portfolio manager.

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
May 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	1,186.69	\$76.66	\$95.44	15.5x	12.4x	8%	1.6x	10,725,823	13%	1.9%
Financials:	Berkshire Hathaway Cl "B"	BRK/B	77.00	\$3.52	\$3.71	21.9x	20.7x	5%	4.1x	71,303	7%	0.0%
	MasterCard	MA	248.04	\$13.53	\$16.21	18.3x	15.3x	18%	0.8x	27,488	54%	0.2%
Consumer Staples:	Avon Products	AVP	32.33	\$2.04	\$2.38	15.9x	13.6x	9%	1.6x	14,045	64%	2.7%
	Coca Cola	KO	53.45	\$3.44	\$3.77	15.5x	14.2x	8%	1.8x	123,312	30%	3.3%
	Colgate Palmolive	CL	84.10	\$4.86	\$5.38	17.3x	15.6x	10%	1.5x	41,247	91%	2.5%
	Diageo Plc ADR	DEO	68.14	\$4.56	\$4.98	14.9x	13.7x	8%	1.7x	42,677	48%	3.4%
	Fomento Economico Mexico	FMX	47.33	\$2.92	\$3.76	16.2x	12.6x	19%	0.7x	10,229	13%	1.4%
	H.J. Heinz	HNZ	46.87	\$3.04	\$3.32	15.4x	14.1x	10%	1.5x	14,822	59%	3.6%
Health Care:	Becton Dickinson	BDX	76.37	\$5.27	\$5.78	14.5x	13.2x	11%	1.2x	18,000	24%	1.9%
	Johnson & Johnson	JNJ	64.30	\$4.84	\$5.25	13.3x	12.2x	7%	1.7x	177,228	26%	3.4%
	Novartis AG	NVS	50.85	\$4.75	\$5.06	10.7x	10.1x	4%	2.4x	134,123	16%	3.3%
Consumer Discretionary:	Johnson Controls, Inc.	JCI	33.59	\$2.08	\$2.56	16.1x	13.1x	14%	1.0x	22,606	NMF	1.5%
	Staples, Inc	SPLS	23.53	\$1.31	\$1.57	18.0x	15.0x	15%	1.0x	17,178	12%	1.5%
	Target Corp.	TGT	56.87	\$3.74	\$4.28	15.2x	13.3x	13%	1.0x	42,045	17%	1.2%
	Toyota Motor Co. ADR	TM	77.09	\$2.77	\$5.00	27.8x	15.4x	33%	0.5x	132,903	NMF	1.4%
Technology:	Cisco Systems	CSCO	26.92	\$1.63	\$1.85	16.5x	14.5x	12%	1.2x	154,191	17%	0.0%
	EMC Corp.	EMC	19.01	\$1.19	\$1.36	16.0x	13.9x	15%	1.0x	38,962	8%	0.0%
	Google	GOOG	525.44	\$27.99	\$32.19	18.8x	16.3x	19%	0.9x	128,786	20%	0.0%
	International Business Machines	IBM	129.00	\$11.27	\$12.34	11.5x	10.5x	10%	1.0x	165,423	74%	2.0%
	Qualcomm	QCOM	38.74	\$2.33	\$2.54	16.6x	15.2x	18%	0.9x	63,450	8%	2.0%
Industrials:	3M Co.	MMM	88.67	\$5.49	\$6.11	16.2x	14.5x	11%	1.3x	63,228	28%	2.4%
	ABB Ltd. ADR	ABB	19.16	\$1.07	\$1.32	17.9x	14.5x	4%	3.5x	44,630	23%	0.0%
	Danaher Corp.	DHR	84.28	\$4.33	\$4.97	19.5x	16.9x	13%	1.3x	27,361	11%	0.2%
	United Technologies	UTX	74.95	\$4.65	\$5.33	16.1x	14.1x	11%	1.3x	69,934	21%	2.3%
Energy:	Apache Corp.	APA	101.76	\$10.30	\$13.04	9.9x	7.8x	11%	0.7x	34,306	NMF	0.6%
	Petroleo Brasileiro S.A. ADR	PBRA	37.94	\$3.90	\$4.37	9.7x	8.7x	6%	1.5x	70,203	26%	0.4%
	Sasol LTD ADR	SSL	40.65	\$3.95	\$5.14	10.3x	7.9x	5%	1.6x	25,973	17%	2.9%
	Schlumberger, Ltd.	SLB	71.42	\$2.92	\$3.94	24.5x	18.1x	15%	1.2x	85,190	18%	1.2%
Telecom Services:	America Movil ADR	AMX	51.48	\$3.82	\$4.35	13.5x	11.8x	13%	0.9x	51,354	46%	0.9%
	China Mobile Hong Kong	CHL	48.90	\$4.23	\$4.34	11.6x	11.3x	4%	2.6x	196,207	24%	3.3%
Transportation:	CSX Corp.	CSX	56.05	\$3.46	\$4.13	16.2x	13.6x	10%	1.3x	21,816	13%	1.7%
Exchange Traded Funds:	iShares MSCI EAFE Index	EFA	54.41	-	-	-	-	-	-	35,519	-	2.6%
	iShares MSCI Emerging Mkts	EEM	42.05	-	-	-	-	-	-	35,480	-	1.4%

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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