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Weekly Market Wrap August 23, 2010

Review - Week Ending 08/20/2010

Markets were mixed last week with broad large cap indexes slightly declining while small cap and bond indexes eked out modest gains for the week. Earnings season has wound down and the economic calendar is summer light, but recently merger and acquisition activity has been heating up, providing at least some potential short-term catalysts for stocks going into fall.

Commentary/Highlights

- **It's a Global Economy:** S&P 500 companies reporting 47% of their sales came from outside the US during 2009.
- **It's a Government Economy:** According to the Department of Labor 1 in 6 Americans now work for the government either at the federal, state, or local level.
- **Mixed economic news:** Industrial production rose a modest 1% in July, and leading economic indicators remained positive-but just barely. But jobless claims rose again and single family housing starts fell to a 15-month low.
- **Bond Bullishness is Nearing Extremes:** Bond investors are betting interest rates will be lower longer, driving 10-year treasury yields down to 2.61% and 2-year treasury notes to 0.49%. Bond inflows have vastly outweighed equity inflows during the last two years and are leading to a great debate on Wall Street. Citigroup's Tobias Levkovich and Professor Jeremy Siegel are comparing the rush to the rush into technology stocks before that bubble burst. David Rosenberg and Robert Shiller argue that low rates make sense with low inflation and the Fed's promise to keep interest rates low. Don't fight the Fed goes the adage-but stay tuned this debate will rage for a while.
- **Merger and Acquisitions Are Heating Up:** Retail investors may still be on sidelines but corporations are starting to put their \$2 trillion in cash to work. Mining giant BHP Billiton recently bid \$39 billion in cash for fertilizer giant Potash. Meanwhile, Intel bid \$8 billion for security software maker McAfee, and Dell and Hewlett Packard are in a bidding war for cloud computing storage company 3Par.
- **Recession and Unemployment Taking Toll:** Fidelity Investments reports that hardship withdrawals from 401K accounts have risen to 11%, with loans on accounts rising to 22%, as investors seek to cushion foreclosure and unemployment events.
- **Hedge Fund Super Stars Throwing in Towel:** Stan Druckenmiller, former manager for George Soros suffered his worst year this year and is returning \$12 billion of client money. John Pellegrini is also returning billions in client dollars after scoring huge gains with Paulson and company during the housing crisis. Both cite difficult market conditions and inability to generate strong returns in the current environment.

| Index/Portfolio Returns | % Change Week | % Change QTD | % Change YTD |
|-------------------------|---------------|--------------|--------------|
| Barclays Aggregate Bond | +0.24% | +1.90% | +7.33% |
| Barclays High Yield | +0.29% | +3.63% | +8.31% |
| S&P 500 Index | -0.43% | +4.29% | -2.65% |
| Russell 3000 | -0.45% | +3.95% | -2.34% |
| MSCI EAFE Index | -1.24% | +6.40% | -7.67% |
| MSCI EAFE Small Cap | -0.59% | +5.45% | -2.04% |
| MSCI Emerging Markets | +0.81% | +8.16% | +1.49% |
| NASDAQ Composite | +0.29% | +3.34% | -3.94% |
| Russell 2000 | +0.23% | +0.36% | -1.60% |