

## Thank God It's Friday!

June 1, 2007

Two weeks ago we discussed market bubbles, and compared the current stock Market to that of 2000. By every definition, the US stock market is not in a bubble. Today's JOBS report showed an increase of 150,000 jobs, and the unemployment rate remains at a very low 4.5%. This is very positive for the economy, and stocks celebrate these kinds of numbers.

Some near-term concerns have us on guard primarily GDP and interest rates. This week's GDP report for Q1 showed the slowest economic growth since 2002. The Fed minutes indicate housing slowdown may be worse than the initially profiled. Despite these events, stocks rallied to new highs.

The hottest market event this week was another blow-up on the Shanghai market, which slid 6.5% when the Chinese government raised taxes to cool their market. It is important to recognize that the Shanghai market is only available to Chinese nationals living on the mainland. The rest of the world, us included, can only invest in China via the Hong Kong exchange, which is less over-heated. It is the Shanghai market that people are calling a bubble, and for all intents and purposes, it is. The index is up over 50% already this year, on top of 130% gain in 2006.

What made the Shanghai sell-off so interesting this time is that the US Markets didn't even blink. If you recall, in February, the same Shanghai stock market fell 9% in a day, which caused a ripple effect across the globe, and sent the DOW plummeting 500 points. That weakness spread for a week and a half. This time, the weakness lasted less than an hour and a half.

A bubble implies an environment that is excessive, and stretched beyond its means. Prices become over-valued by traditional measures, yet investors feel there is no end to the upside; the sky's the limit. Some will defend such activity, by saying that "it's different this time". That somewhat describes the housing market of the last few years. But not our stock market today.

We take investor sentiment very seriously in our approach with the Market. There is indeed a sense of euphoria in certain areas, and most of them are based on the growth in China. Emerging markets have soared to levels never seen before. Money has been thrown in that direction with reckless abandon. The Chinese economy is surging, no question about it, particularly ahead of the Olympics next summer. But their government has a major challenge on its hands, in managing the economy without letting it spin out of control. Commodity prices have skyrocketed, largely due to real demand, but also on speculation of future needs and questionable supplies. The conventional belief has China and the rest of the emerging markets continuing to soar without a slowdown in sight. That has us on guard.

Chinese stocks continue to rally along with the rest of global markets. To put it in perspective, 8 million brokerage accounts were opened in China last qtr, compared to 7 million all of last year! History has shown that investors are very successful at chasing performance; buying high and selling low. Isn't it supposed to be the opposite?

The stock market still looks very attractive long-term. Blue chips have finally caught wind. Companies continue to buy back stock at a rapid pace. Mergers and acquisitions are a constant theme and the market has been liquidity driven. However, the US economy has been slowing while stocks are growing. A significant sell off in Asia would certainly impact the US market. But a correction would shakeout these excesses, and would set the table for a continuation of the bull run. The market at large is not in a bubble.

By: Mike Frazier

INDEX	06.01.2007	12.31.2006	%Change
DOW JONES	13,668	12,463	+9.7%
S&P 500	1,536	1,418	+8.3%
NASDAQ	2,613	2,415	+8.2%
Bond YIELD	4.96%	4.71%	+5.3%*