

DSA Communiqué

June 2010

Communication is Key

Our goal is to effectively communicate to you what we're thinking about investments; financial planning issues, the economy, and maybe, even the political landscape. We intend to also use this communiqué to keep you posted on what's going on at Droms Strauss as we continue to grow and enhance the level of services we provide for you.

We welcome your questions, comments and feedback; please contact us at any time.

The Summer Solstice

Next week will mark the beginning of summer with the June Solstice – when the tilt of the Earth's axis is most inclined toward the sun, causing the sun's apparent position to reach its southernmost extreme. The name is derived from the Latin *sol* (sun) and *sistere* (to stand still), because at the solstices, the sun stands still in declination, the apparent movement of the sun's path north or south comes to a stop before reversing direction.

Recently, the question on many of our clients and friends minds has been about the market: has it too reversed direction or perhaps, just taking a breather from spring before it really heats up during the summer? This Communiqué attempts to address this very question.

SELL IN MAY AND GO AWAY? SAYS WHO?

After the stock market debacle that ruined what should have been the “very merry month of May,” some of us may be regretting now that we didn't “sell in May and go away” as the old Wall Street adage suggests. However, we may all feel better if we look at the actual results of the “sell in May” approach to market timing. To throw a little light on this issue, we went back twenty years and calculated the difference between holding the S&P 500 Index compared to selling either at the end of April or the end of May. To simplify calculations, we ignored interest that would have been earned on money out of the market and we also ignored dividends on the S&P 500, so the interest and dividends are approximately a wash. We calculated the return differences two ways: one if we sold the S&P at the end of April (anticipating a down May) and one if we sold at the end of May.

What we found was that over the past 20 years, selling in April or May and staying out of the market through the end of December provided a better return than hanging in all year only six times in the last 20 years. In all six of the outperformance years, selling at

the end of April or selling at the end of May both outperformed buying and holding. Conversely, in all 14 years when holding all year provided the higher return, holding for the year outperformed selling either at the end of April or the end of May. So, “sell in May and go away” worked well only 30 percent of the time over the last two decades. Not surprisingly, “sell in May” works best in down markets, and was the superior strategy in 2008, 2007, all three years of the 2000-01-02 market crash, and in 1990.

Last year’s amazing rally following the March 2009 market bottom would have earned returns of 1.8% for selling in May and a loss of 3.4% from selling in April compared to a full-year gain of 23.5% for the S&P. For the market debacle year of 2008, when the S&P lost 38.5%, selling in April would have lost 5.6% and selling in May would have lost 4.6%. Cumulatively over the past 20 years, the cumulative gain for holding the S&P 500 would have been 155.3% compared to 78.8% for selling at the end of May and 41.2% for selling at the end of April. So the efficient market crowd looks to be right on this one - - if all it took to beat the market was to sell in May and go away, everybody would do it, the markets would always go down during the second half of the year, and we wouldn’t have to worry about diversifying or rebalancing our portfolios.

SUMMER & FALL 2010

So, given that we did not sell in May, what is our forward expectation for market returns? The recent turmoil in Europe is having obvious negative effects here in the U.S., but the U.S. economic outlook is still encouraging. To add a little perspective on the problems that began in Greece, it is worth noting that the GDP of Greece as a percent of the GDP of the European Union is about the same as the GDP of Atlanta, Georgia as a percent of GDP of the United States. The GDP of Hungary is even smaller at less than 40 percent of the GDP of Greece and the Hungarian government is now backing away of its earlier statements that Hungary might have to default on some of its debt obligations. The combined GDP of all the member countries of the European Union is estimated to be only slightly larger than U.S. GDP (\$14.51 trillion vs. \$14.26 trillion), with U.S. GDP the highest in the world, followed in order by China (\$8.79 trillion), Japan (\$4.14 trillion), India (\$3.56 trillion) and Germany (\$2.81 trillion) rounding out the top five.

In testimony before the House Budget Committee last week, Federal Reserve Board Chairman Ben Bernanke expressed his opinion that as the economic stimulus from government spending begins to wind down toward the end of this year, gains in the private sector will sustain the recovery and that “the economy appears to be on a track to continue to expand through this year and next.” Chairman Bernanke also noted that he expects the sovereign debt crisis in Europe to have only a modest impact on the U.S. recovery if markets continue to stabilize and that he does not anticipate seeing a double dip recession. Furthermore, he noted that the Fed’s recent decision to renew dollar swap lines with the European Central Bank “sends an important signal to global financial markets that we will take the actions necessary to ensure stability and continued economic recovery.”

As we commented in a recent client note, the current consensus of leading business economists is that the bottom of the Great Recession was hit in June 2009 and that the current recovery is now one year old. The National Association of Business Economists consensus is that the US economy will grow “above trend” in 2010-2011 at an expected inflation-adjusted GDP growth rate of 3.2 percent. Most corporate earnings announcements continue to come in above expectations, unemployment is easing, inflation is nearly non-existent, interest rates are low, and the economy is growing. Also, at less than 14 times expected earnings, the S&P is reasonably priced. Envisioning the economy and the markets two to three years out, we expect that we will see positive returns over the next two to three years as the economy works its way free of the last vestiges of the Great Recession. Hence we believe it makes good sense to remain invested in a diversified portfolio consistent with your financial situation and risk tolerance.

What’s happening at DSA

We are very pleased to announce that during this quarter we’ve had several members of the DSA Team attain some very significant achievements. Mike Murphy recently passed the Series 65 Examination administered by the Securities and Exchange Commission and is now officially, “a registered investment adviser”. Bob Hines has just this past week completed his three year experience requirement and is now a Certified Financial Planner (CFP®) and last, but not least, Rachel Strauss has successfully completed the 5 modules of study for the CFP® certification and is now studying for the comprehensive examination.

Referrals

Please take a moment to recommend us or share contact information for an individual, family or a business colleague you think could benefit from working with us. With the addition of three professionals over the past three years we’ve increased the depth and breadth of our level of expertise and, just as importantly, our ability to provide you and each DSA client the highest level of service. Be assured that we will regard your friends, family and business colleagues with the highest level of consideration.

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