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Fears of an economic relapse were stoked by comments from the Federal Reserve last week. The statement that came at the conclusion of the regularly scheduled Federal Open Market Committee meeting said “the pace of economic recovery is likely to be more modest in the near term than had been anticipated.” That was enough to send the “risk off” trade into full bloom. The Dow Jones Industrial Average lost 350 points or 3.2% for the week, to close at 10,303. Smaller stocks, which are considered riskier than their larger brethren, fell a stiff 6.3%. Meanwhile, Treasury bonds rallied as investors sought the safety of government securities. Along with scant inflation readings and the Federal Reserve’s stated intention to purchase Treasury securities to maintain its \$2 trillion balance sheet, the 10-year Treasury bond yield fell to 2.67% from 2.82% the previous Friday.

INDEX	WTD	YTD	1-YR
DOW JONES	(3.2)	0.5	12.7
S&P 500	(3.7)	(2.0)	8.7
S&P 400	(4.8)	2.0	13.8
RUSSELL 2000	(6.3)	(1.8)	7.3
MSCI EAFE	(4.7)	(6.1)	2.2
MSCI EM	(2.9)	0.8	17.2
TYPE	CURRENT	12/09	12/08
3 – Mo TREASURY	0.15	0.07	0.08
2 – Yr TREASURY	0.53	0.81	0.76
10 – Yr TREASURY	2.67	3.58	2.21
30 – Yr TREASURY	3.85	4.49	2.68

SOURCE: BLOOMBERG AS OF 8/13/2010

Investors are also fretting about the threat of a hard landing for China’s economy. Chinese officials have been deliberately attempting to slow growth to combat speculation and concerns of inflating prices. However, recent data indicate a deceleration of activity that spooked investors worried about what this could mean for a global economy that is already sputtering. We think that China’s growth will stabilize and eventually reaccelerate, contributing to a rising world economy. In the U.S., slowing growth is troublesome at a time where the margin for a policy error is extremely thin. Yet, we are not convinced a double-dip recession will occur and, therefore, maintain a positive bias toward stocks. Not all stocks, however. We prefer high-quality, dividend-paying, large company stocks. Especially when compared to their U.S.-based small capitalization counterparts. Not only do large companies have more ballast in a potentially volatile environment, but their global presence enables them to benefit from revenue sources housed in faster-growing emerging economies. In addition, larger companies are enjoying an accommodating capital market for cheap funding, providing a buffer to margins should pricing power wane. Combined, large-cap dividend payers can reward patient investors even if the economic news only stops getting worse.

