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Calculated Investing

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Special Market Commentary ~ August 2011 Correction

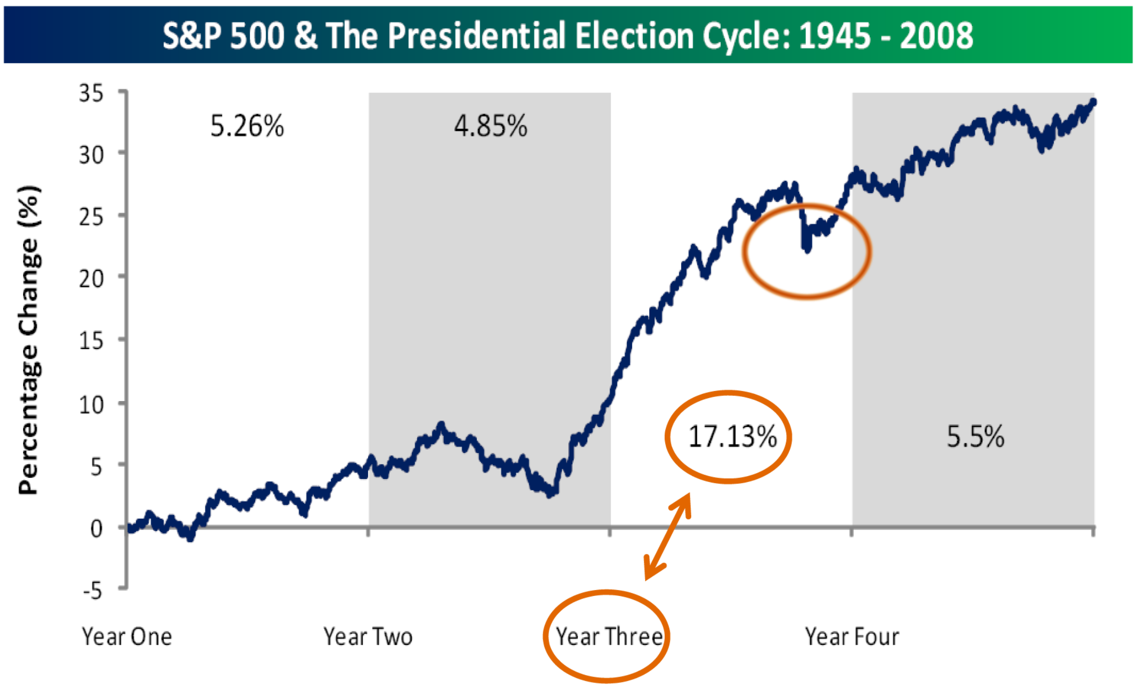
August 8, 2011

While the jury is still out about the effect the S&P downgrade of U.S. Debt will have on our markets, there is no denying that economic and political news have played a part in the current test of investor fortitude. Summer just isn't the time to be focused on only the negative news. Trading volume, per usual, is down. Wall Street traders are on vacation. Washington is dysfunctional as ever. The economy remains stale at best. All the while a highly publicized, debt battle royal transfixed the nation. In the meantime, the markets did what they always do: they added volatility in a thinly traded summer environment. Nothing new here. Is this the start of another waterfall event, or simply a normal pullback in a larger cyclical bull move, which began in 2009?

In our view, this correction has been anticipated, and is not a waterfall event

At Navellier, we frequently reference the four-year presidential cycle and the behavior of the markets during each of those four years. Of all the years, the third year of the cycle is most prone to a violent downside market move, one of fairly short duration and considerable volatility. This event tends to occur during the lighter trading months of late summer. This correction also sets up very strong market conditions which tend to last well into the summer of the 4th year of the election cycle. We see this correction as just that: an incredible buying opportunity and market entry point for what has historically been the next leg up.

Current Election Cycle - Positive History[1]



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There should be no considerable shift in market leadership going forward

Coming out of waterfall corrections we frequently see stocks with very poor fundamentals lead the way. Often, higher quality growth stocks take their time in gaining traction and it is during these periods where relative underperformance can occur. Short, sudden pullbacks tend to be different. Frequently, stocks that were leading the way going into a short-term pullback recover quickly and within a quarter or two are setting new market highs. We expect that will be the case coming out of the 2011 summer correction and that many of the growth stocks in our leading growth portfolios will rally sharply. This should be especially true in the higher quality stocks in our Large Cap Growth Portfolio as this asset class has a little more predictability. The Large Cap Growth Portfolio has had very low turnover in the past year, which means our system is indicating that the macro market environment is quite stable at this point. Our research process usually results in a lot of conflicting data when markets begin to fall apart, and that is not the case right now.

Recovery from short corrections makes or breaks long-term market returns

It is during violent downside moves, complete with news of impending doom, that investors tend to react emotionally, and understandably so. At the same time, these are the periods that require the most resolve to achieve long-term investment goals. The dynamic nature of the market post short-term correction makes it very difficult to re-enter the market should one decide to raise cash. Now is the time to be a well-informed investor and not to make emotional decisions. For those with longer time horizons and a clear understanding of the level of risk that they can tolerate, this is a time of tremendous opportunity.

The bad news is baked in the cake

Watching just about any financial news program on TV this past week makes you wonder if there is even going to be a tomorrow. Of course the fixation with negative stories is driven by the business of the news. Yet, in the face of all the negative economic and political news, the market has been quite resilient up to this point. Corporate America, which tightens its belt as always during economic slowdowns, has been extremely productive and profitable. While the outlook for a continued international business environment, which has been favorable for U.S. corporations, is cloudy at best, senior management at the well-run corporations have been diligent in lowering debt levels and building cash reserves. While the market is undoubtedly telling us that the 6-9 month outlook shows little promise for big GDP gains, the longer-term outlook remains very strong. Historically, there is little doubt of the ability of Washington to “engineer” a better macro economic climate going into an election year. With the S&P news now broken, our politicians have been slapped on the wrist hard and there is no doubt they will continue to shift towards larger spending cuts going into an election year. This news should be warmly received by our markets and should help drive 4th quarter market returns.

Zero to Hero

While we understand the challenge that faces investors emotionally during these times, we remain committed to trying to deliver excellent performance over a long-term market cycle. We acknowledge that in order to achieve great results you have to experience short periods where your strategy will be extremely out of favor. Our focus is on your clients’ long-term returns. Informing clients with a clear picture of long-term return behavior is paramount to our mutual success as managers, advisors, and trustworthy investment professionals. We maintain a large selection of products at Navellier, some of which are defensive in nature. Still, our opinion for the remainder of the election cycle remains strongly bullish for U.S. equities. We believe this recent pullback is a normal correction, which sets the stage for a very strong 12-month period of returns.

LOUIS G. NAVELLIER

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[1] **Source:** Bespoke Research, Navellier Applied Research. Graphs are for discussion purposes only. Taken from sources believed to be reliable. Information may be incomplete or condensed. The S&P 500 is an unmanaged index of 500 widely traded stocks. It is not possible to invest directly in an index. Investing in equities can result in the partial or complete loss of all monies invested.