

THE OMNIVEST MARKET VIEW



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Stocks to Outperform Bonds Again in 2011

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It may not feel like it, but the S&P 500 outperformed the fixed income market for a second year in a row. For 2010, the S&P had a total return of 15.06% versus a 6.43% total return gain for the broad bond market. We believe that stocks will outperform fixed income for a third consecutive year in 2011.

The conundrum for asset allocators is to understand that rising commodity prices and rising interest rates are compatible with rising equity prices and equity valuations. At first blush, rising interest rates are supposed to suppress economic activity and dampen equity market performance.

However, we believe that rising interest rates should give confidence to those investors who are willing to shed risk-free assets in favor of risk assets. First, interest rates remain at near historical lows and need to normalize in order to promote investor confidence. Second, rising commodity prices are the result of supply/demand imbalances where demand is out-stripping supply. Third, even with unemployment at stubbornly high levels, consumers are spending again. Perhaps the increased spending is the result of consumer stabilization following a two-year period of deleveraging.

Mixing all of the above ingredients together creates a fairly bright outlook for risk assets in the year ahead. Our expectations for the year ahead is that the S&P will have another year of double digit returns with the bond market settling for low single digit returns.

Thematically, we believe that emerging market equities will outpace developed market equities again. Rising commodity prices and rising commodity linked currencies will promote rising consumer income and therefore rising consumer spending. As such, we prefer emerging market consumer discretionary stocks over developed market discretionary stocks.

We also expect that bank stocks will continue to gain upward momentum this year and expect money center banks to be market leaders.

In the fixed income markets, we remain quite negative on municipal debt, long-term Treasury debt and other high quality debt instruments. Corporate credit debt continues to look attractive and we still believe that high-yield debt will outperform investment grade debt.

Finally, commodities should have another good year as the global economy expands and emerging economies grow at an even faster pace. Unfortunately, unemployment conditions are not expected to improve much this calendar year as companies focus on capital spending and productivity gains. The US dollar will likely suffer as interest rate differentials expand in favor of other currencies.

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