CLEARVIEW INVESTMENT PARTNERS

250 Newport Center Dr. Newport Beach, CA 92660 (877) 762-6208 www.cviewip.com December 30, 2010

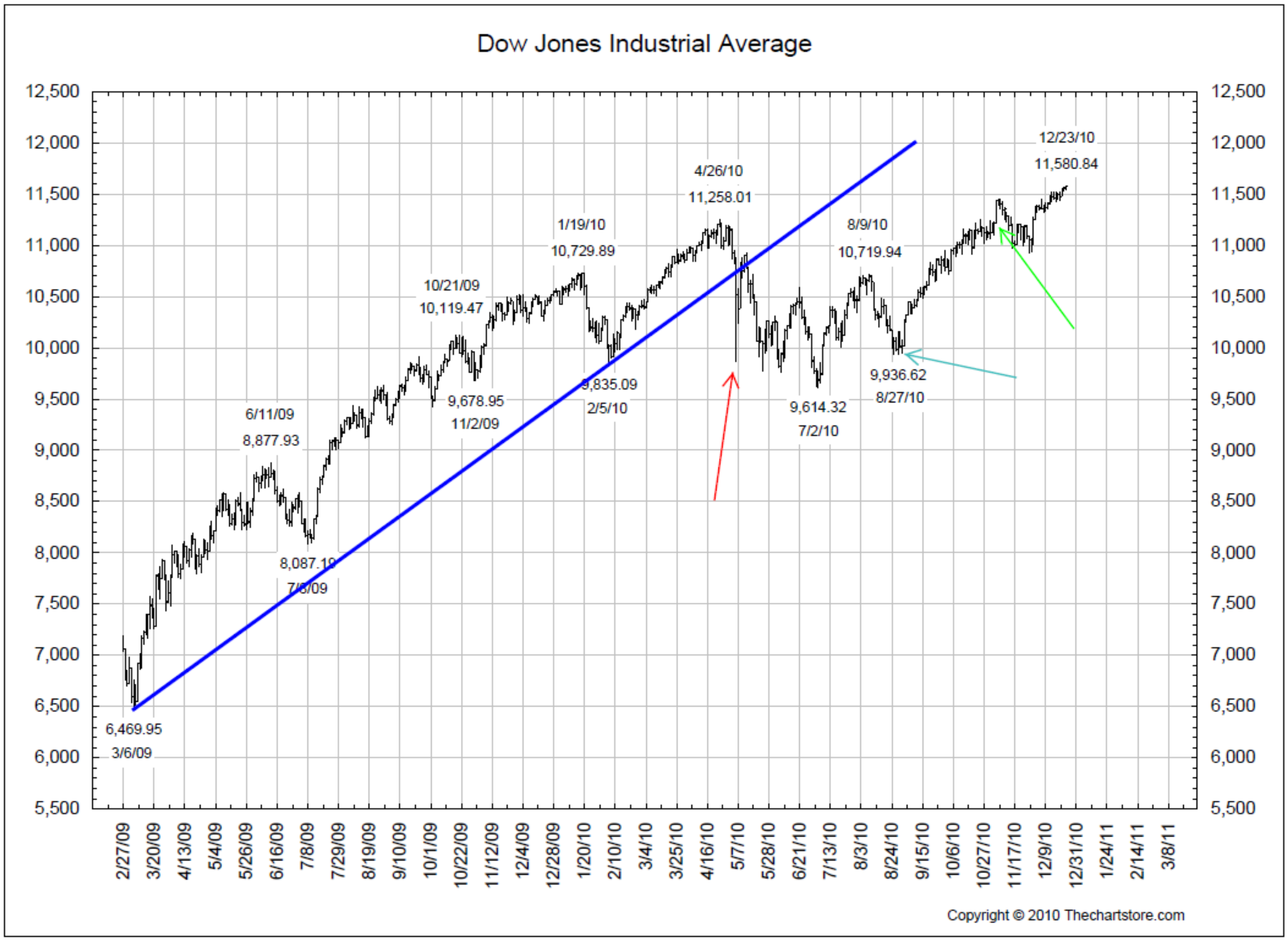
Tech Spotlight

We will start out this month as we did last time, talking about Quantitative Easing II. The purpose behind QE2 was to help the economy and the real estate and stock markets by keeping interest rates down (it is extremely unusual to hear the Fed talk specifically about wanting to directly affect the direction of the stock markets). Instead, we see that interest rates have risen somewhat dramatically since the official announcement of QE2 right after the election in November. Based on what we hear in the media, though, that even though interest rates are up rather than down, the economy seems to be on the mend and the stock market is up. Unfortunately, real estate does not look as healthy as the stock market currently does. Still, the media continues to present that we should avoid the threat of a second dip into a recessionary environment, and that we appear to be on, at worst, a muddle-through path to a recovering economy. Time will tell. We'll see if the economy is really ready to come off of the life-support provided by quantitative easing when QE2 runs out in June of 2011. Talk of a possible QE3 has begun, but, at this point it is just talk. We hope that it is not necessary for the Fed to implement another round of quantitative easing.

So, as we mentioned, the stock markets are up. Following are two charts of the Dow Jones Industrial Average of 30 Companies (DJIA), one near-term and the second intermediate- term.

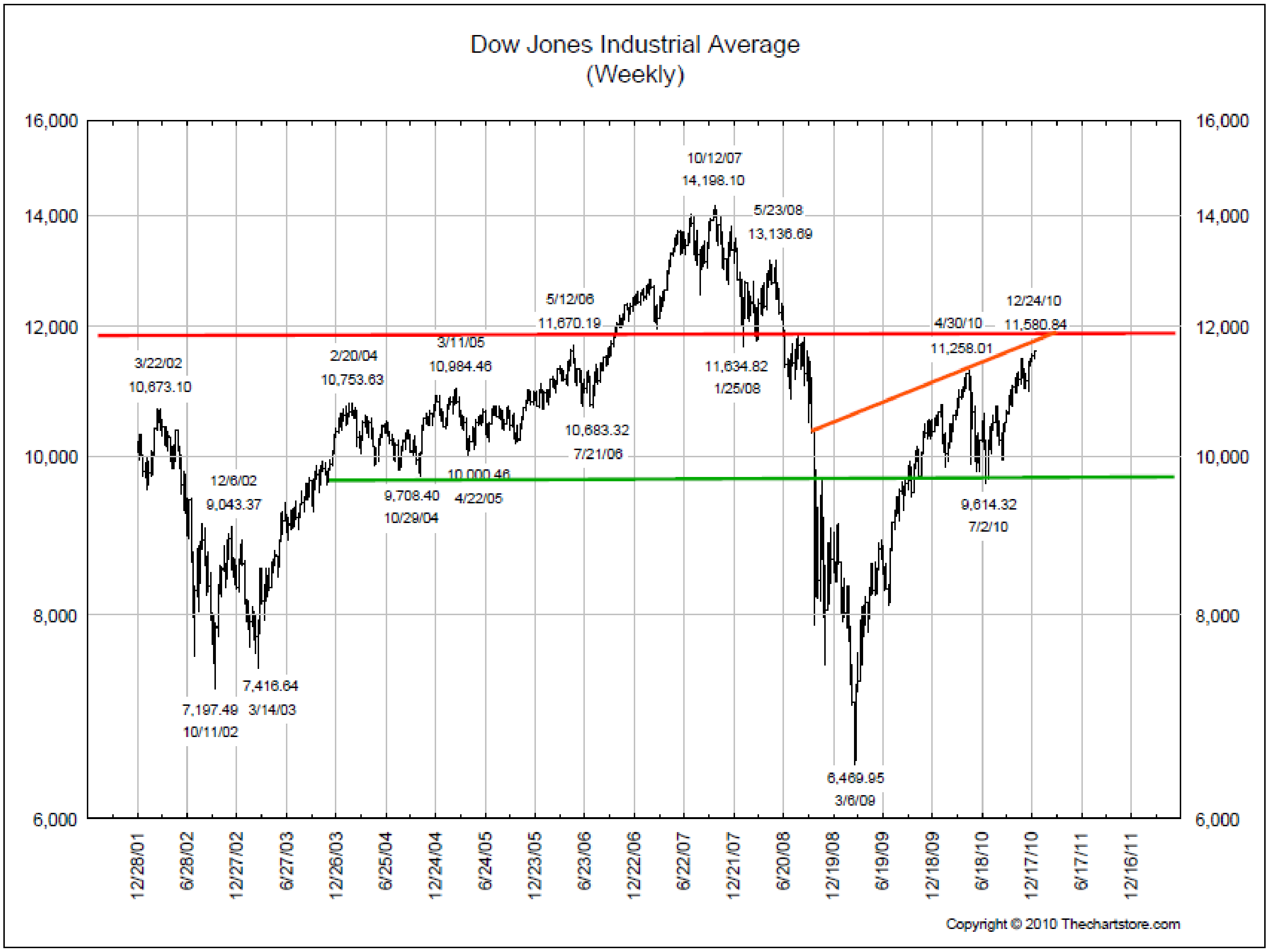
As you can see in the first chart below, the blue intermediate-term trendline going back to the March 2009 market lows was broken in May during the May 6th "Flash Crash" (red arrow). What gave the trendline break much validity was that the ensuing rally from the flash crash stopped in the area of the uptrend line and then proceeded to move lower than the May 6th Flash Crash low three separate times during May, June and July, respectively. After rallying off of the July lows, the markets again looked like they were going to move to new downtrend lows until the Fed came out in late August and early September (light blue arrow) and "unofficially announced" that the Fed was seriously considering a second round of quantitative easing coincident with their November meeting. The markets immediately began to react as if QE2 was going to happen and that it would be good for the economy. When the Fed officially announced a second round of quantitative easing at their November 3rd meeting (green arrow) the market rallied, corrected down 5% and then began to rally again.

Data as of December 23, 2010



Trading volume on the New York and OTC exchanges has fallen by a quarter (25%) over the past month from the already low trading levels that existed before the November elections. So, how much higher can the Dow 30, and the other stock markets by osmosis, continue to rally before experiencing some kind of normal pullback? The answer may lie in the second chart shown below. We are expecting the Dow 30 to possibly rally up to between 11,700 to 11, 870 (red resistance line) before experiencing a “normal” and perhaps “healthy” correction of 5-10% which would take the markets back down toward their November lows. Assuming that is the extent of any market correction, then we would expect the markets to, once again, move higher and begin an assault on the May 2008 rally high of 13, 136. Though you cannot see it on the chart below, 11,700 corresponds with the market top back in 2000. Consequently, we expect this area to provide at least some temporary strong resistance to the market’s low-volume advance in the near future.

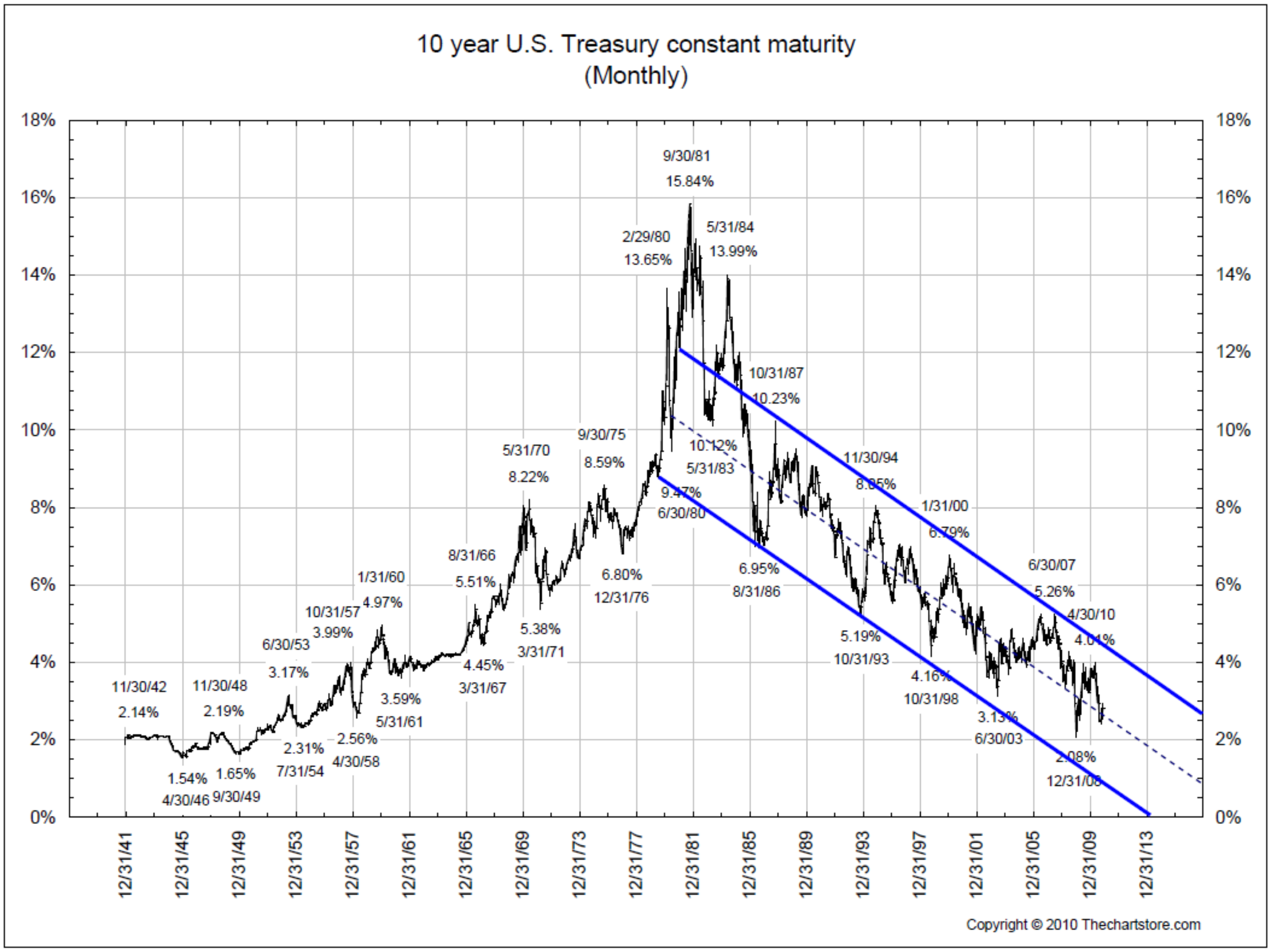
Data as of December 24, 2010



However, should a near-term market correction develop that would break below the November lows, we would then expect a further correction down to as low as the July lows around 9,600 (green support line). Many analysts are now beginning to talk about a market correction in January 2011. If there is one thing we have learned over the years, when too many people begin to expect a definitive course or trend for the markets, the markets will do their best to confound investors (see the John Maynard Keynes quote in the September issue).

Now, what about the effect of QE2 on interest rates, as we originally mentioned above? The following two charts will tell this story and from a longer-term view, and help to keep it all the consequential market action in perspective.

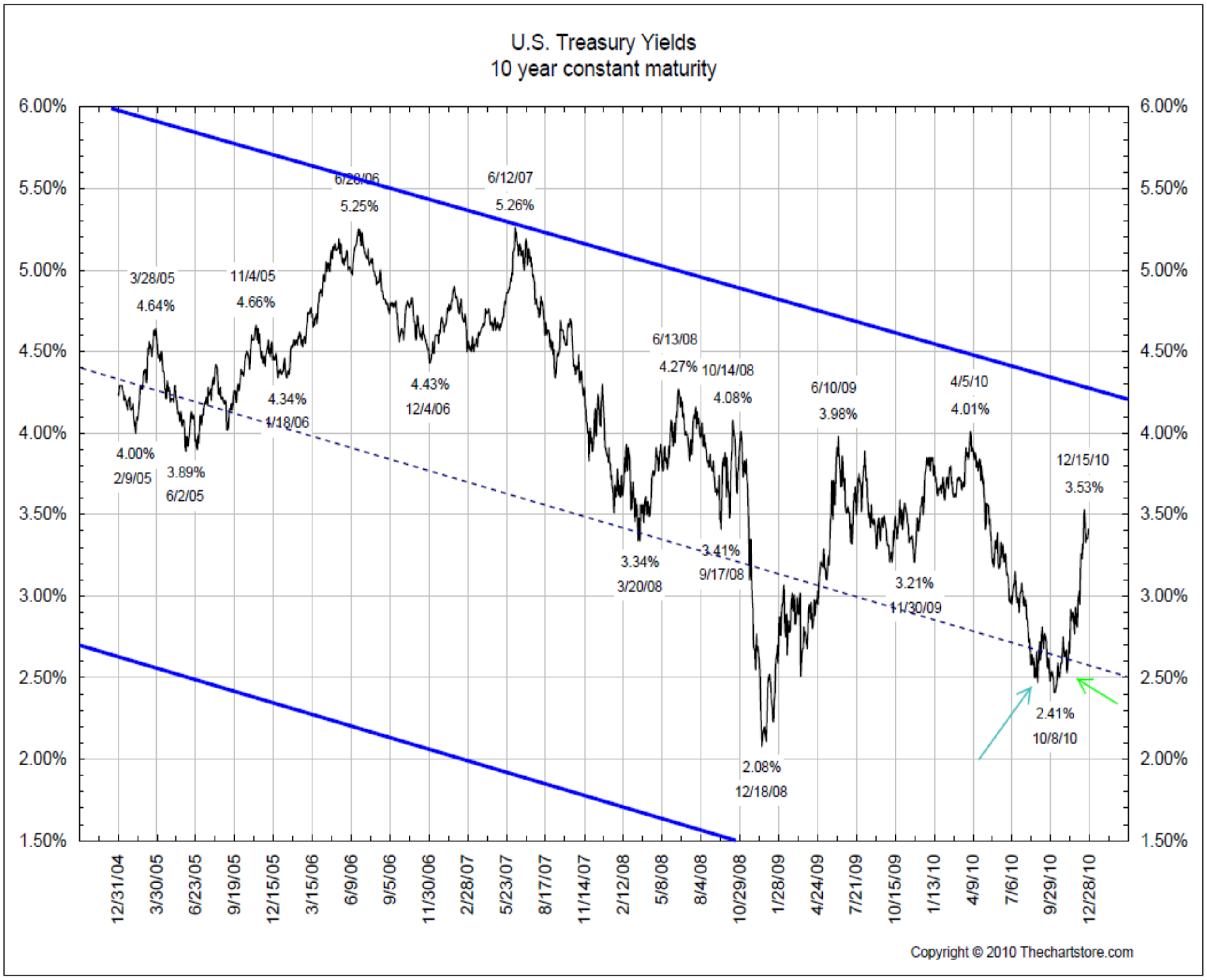
Data as of November 2010



We'll start with the longer-term view. While one of the Fed's goals in implementing QE2 was to keep long-term interest rates low, the immediate effect was to see a 40% rise in the yield of the 10-year Treasury Bond from 2.5% to 3.5% in just 6 weeks! However, when we look at this from a long-term time horizon, as in the chart above, we see that this is part of the normal "ebb and flow" of the interest rate yield for the 10-year Treasury over the past 25 years. As we have discussed in previous editions, until the interest rate yield breaks out above the upper blue downtrend line (currently around 4 to 4.25%), we expect to see rates continue to "ebb and flow" to the downside. We would not be surprised to see the yield on the 10-year Treasury eventually get down to 1% before this is all over.

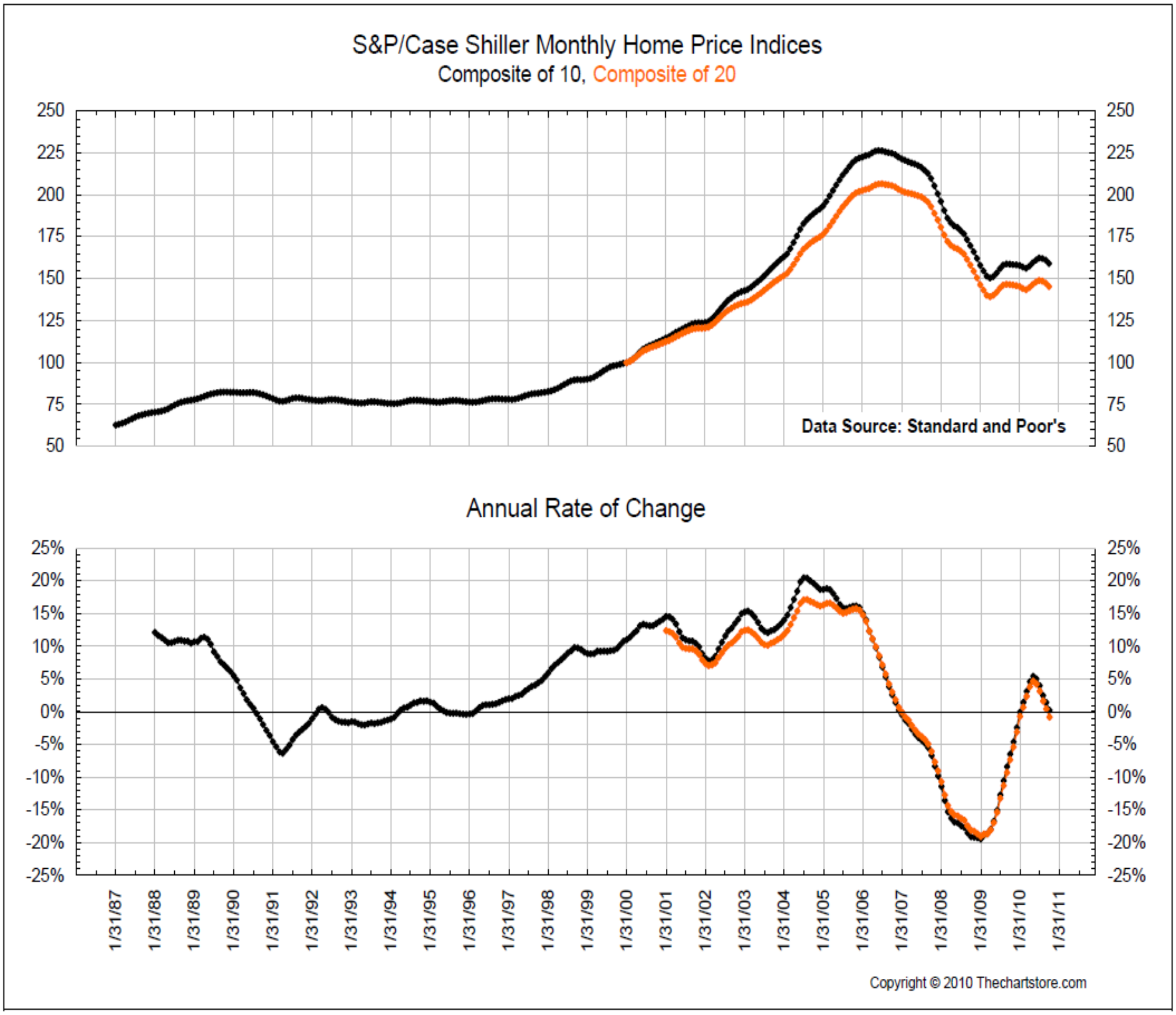
But what about the near-term? Let's look at the next shorter-term chart of the 10-year Treasury Yield:

Data as of December 24, 2010



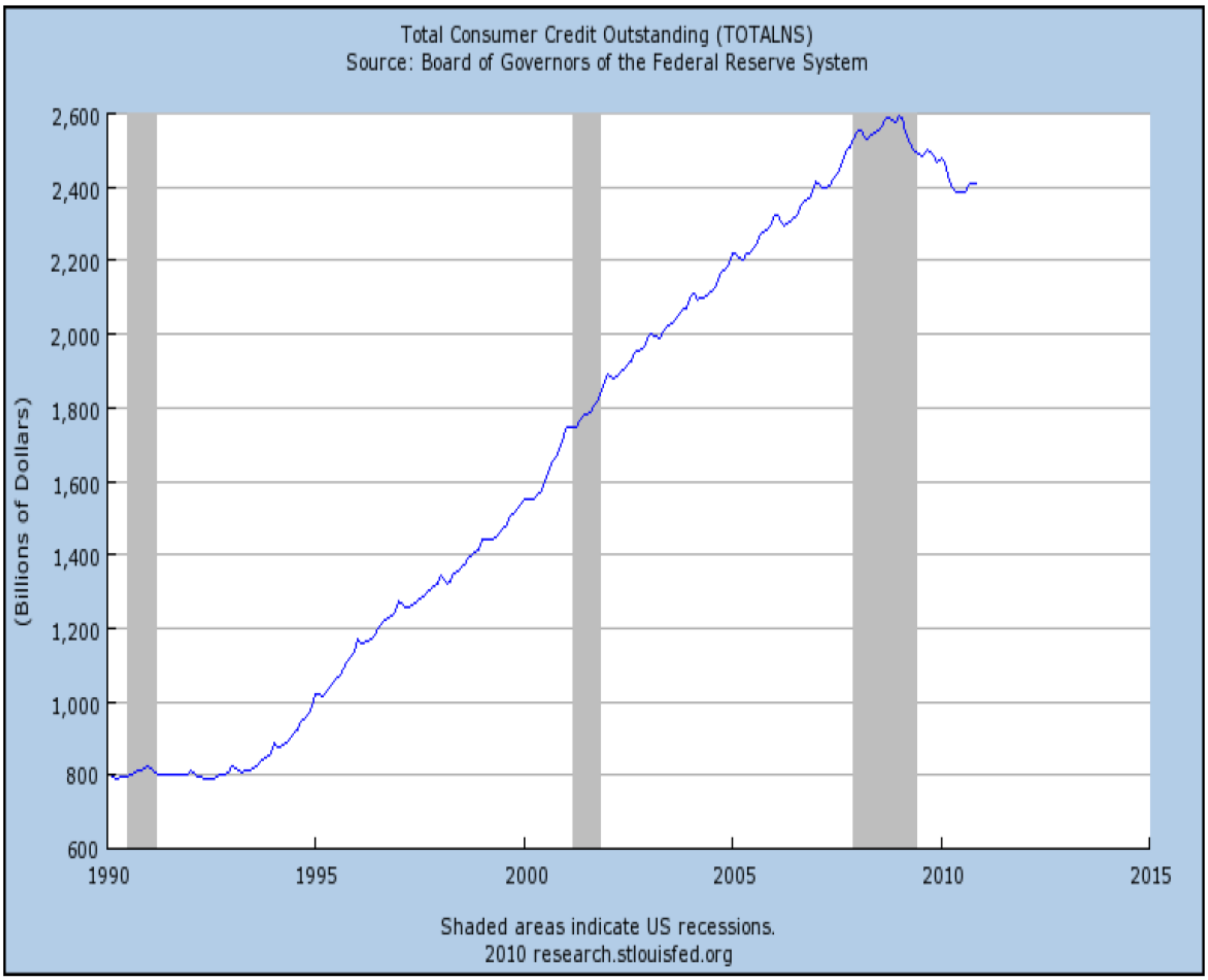
We have drawn in the trend lines from the longer-term chart above. The light blue arrow represents, as it did in the Dow 30 chart, when the Fed informally began to talk about QE2 and the green arrow when they began to formally implement QE2. You can see more clearly the dramatic move up in the yield for the 10-year Treasury. Again, all of this move is within the 25-year down trending channel for the 10-year treasury yield. The short-term effects of such a rise, though, are not necessarily comfortable to deal with. Interest rates on home mortgage loans have likewise jumped and have slowed the sales on homes – which is not what the Fed appeared to want. The data in the following chart from S&P and Case Shiller is only through October 2010 (there is an almost two-month lag between the end of a month and when the data is completely rounded up and then available for statistics and chart generating):

Data as of October 2010

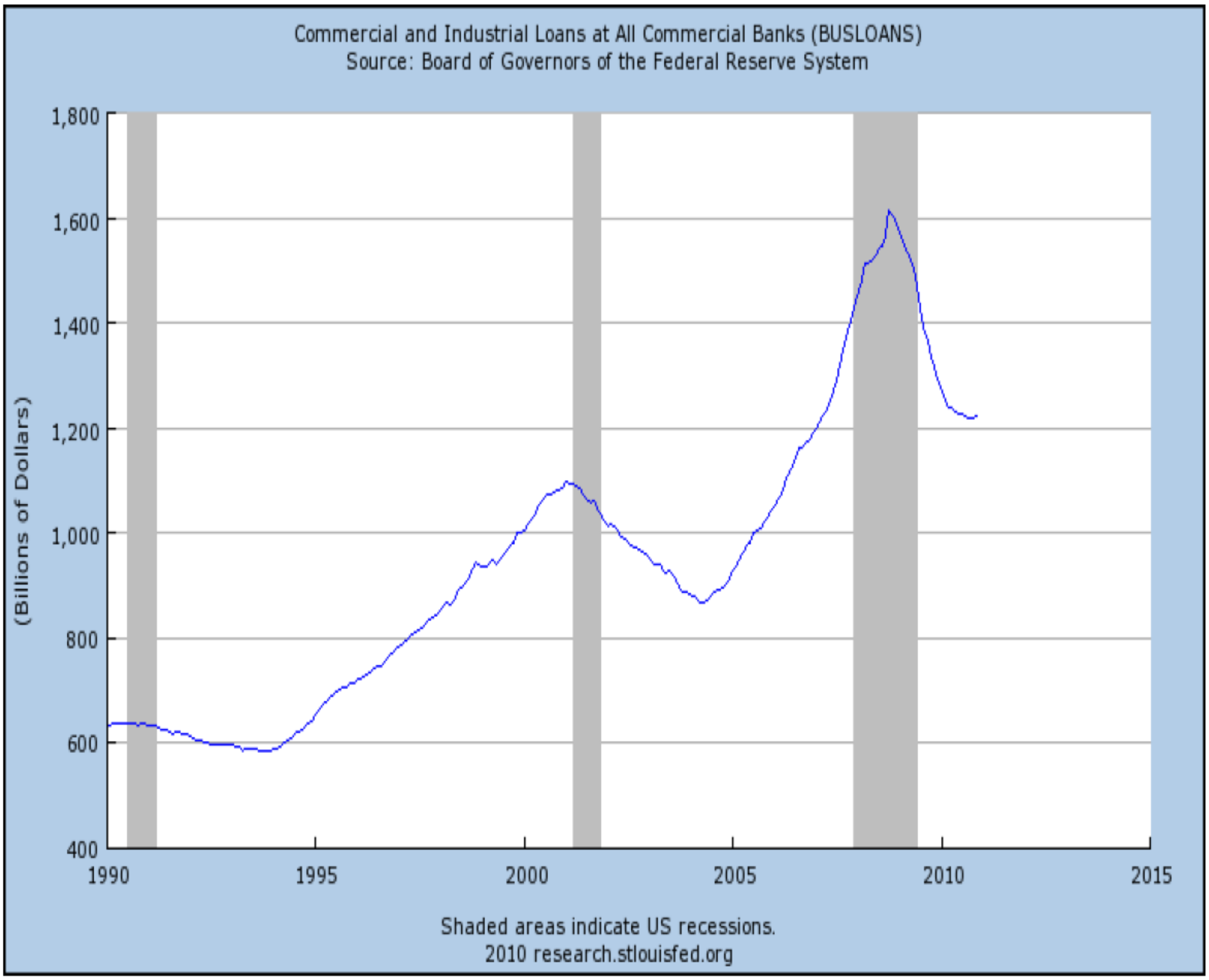


The average price level of homes in the largest 10 U.S. metropolitan cities and the largest 20 metropolitan cities/areas fell by roughly a 1/3 before hopefully bottoming in 2009. Price levels have since bumped up a little (making the Fed happy), but the recent change in direction (beginning in the summer) and now the rise in interest rates may lead to another drop in home prices. Moody Analytics recently came out and estimated that home foreclosures will finish around 1.8 million in 2010 and they estimate 2.0 million more in 2011. These are headwinds that the Fed is hoping to offset with QE2, but it does not initially appear to be working, at least as it regards to real estate.

Consumer spending, as we have discussed before, represents about 70% of the U.S. economy. We keep our eyes on consumer credit as an indication of consumer spending. When we last looked at this chart in September (with data through July), we only saw that consumer credit was still continuing to contract. However, there has been a bump up in credit during September and October. We are guessing that credit expanded a little more in November and December and hope to see that trend continue into 2011. It'll be springtime before we see the numbers through February 2011. In this regards, QE2 may be having a positive effect as the monies that banks are receiving from the Fed may be working their way, albeit slowly, back into consumers' hands and into the economy. The Fed will be watching this very closely and, I'm sure, will have a lot to do with whether they feel a need to implement a plan for a QE3 in the summer.

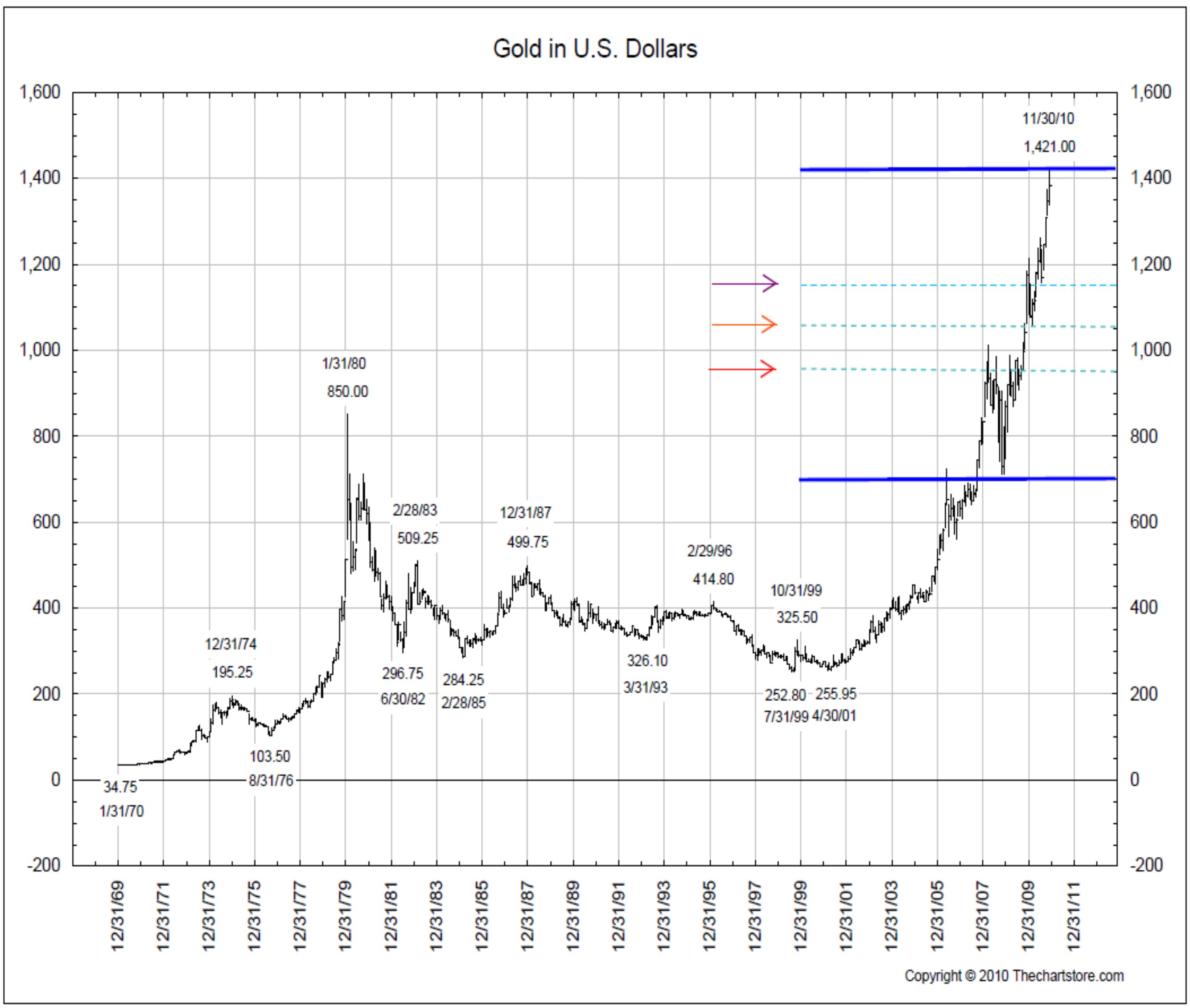


While consumer credit, and so consumer spending, has appeared to pick up, we are not quite seeing the same bump up in commercial and industrial credit and their consequential spending. Fortunately, as you can see in the chart below, the rate of contraction in commercial and industrial loans has slowed and is hopefully in the process of bottoming. We will revisit these numbers in the spring and look to see if commercial credit begins to expand rather than contract. Economies are really all about credit. More than most statistics, the chart above for consumer credit and the chart below for commercial and industrial loans will tell us about the U.S. economy and its direction.



Gold and silver have had almost parabolic runs in 2010, somewhat coincident with the fall in the U.S. Dollar and fears of inflation from possible long-term effects of QE's 1 & 2. Given the rise in gold and silver prices, it would be "normal" for their prices to consolidate their gains and rest a bit by retracing part of their runup before continuing on their longer-term bull market run (the green uptrend line is a good guide for maintenance of a bull market for gold and silver). A number of technical analysts use Fibonacci Retracement numbers as one method in trying to calculate where a specific asset market could correct to in both bull and bear markets. For purposes of the following two charts, we will use the two horizontal bolded blue lines to mark the retracement "boundaries" from which correction levels (the dotted light blue lines) are calculated.

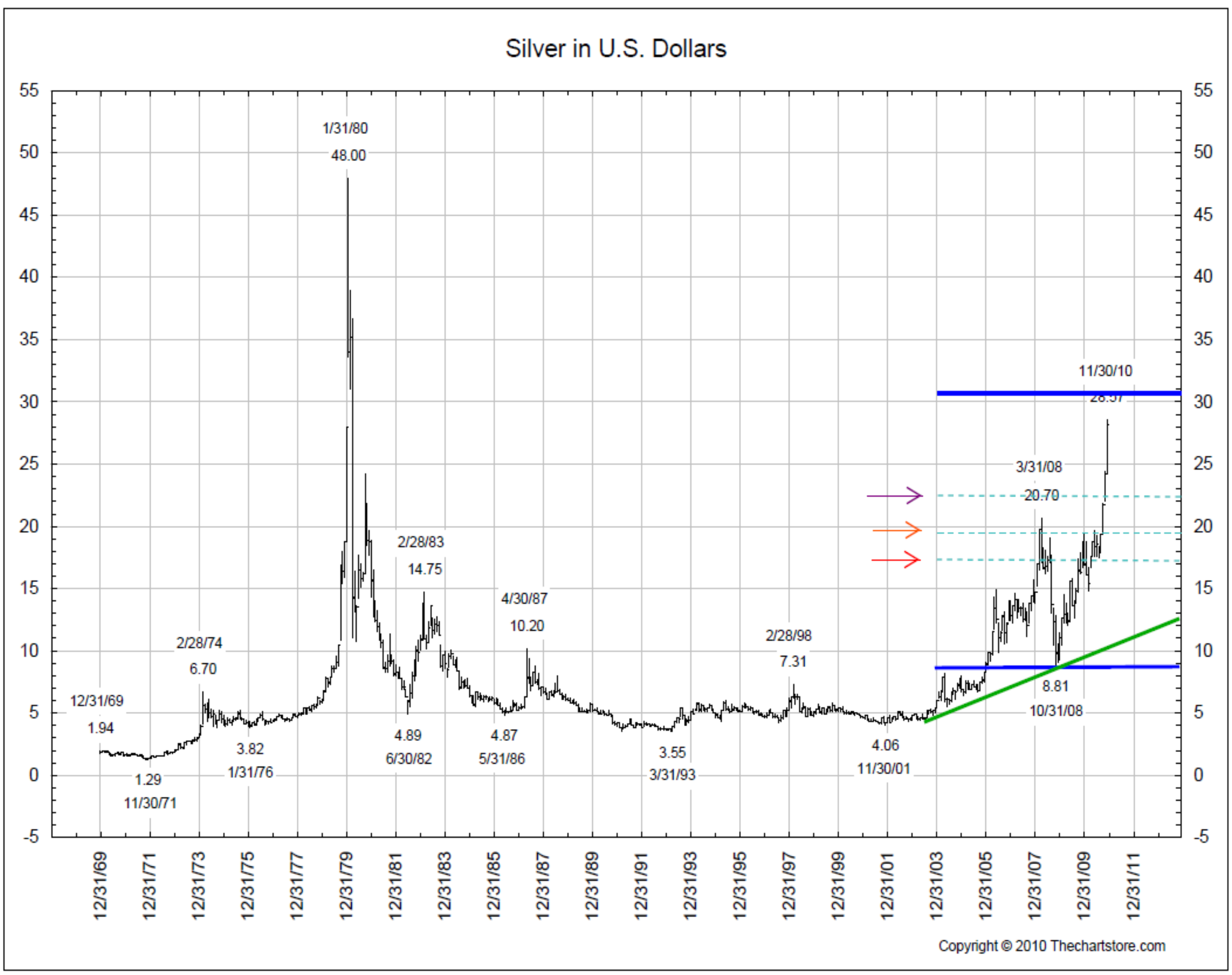
Data as of November 2010



For gold, the potential retracement/correction levels work out to be $1,145 (38.2% retrace – purple arrow), $1,060 (50% retrace – orange arrow) and $975 (61.8% retrace – red arrow). The most probable minimum correction would be down to $1,145. The largest orderly correction we would expect, without panic selling, would be down to $975.

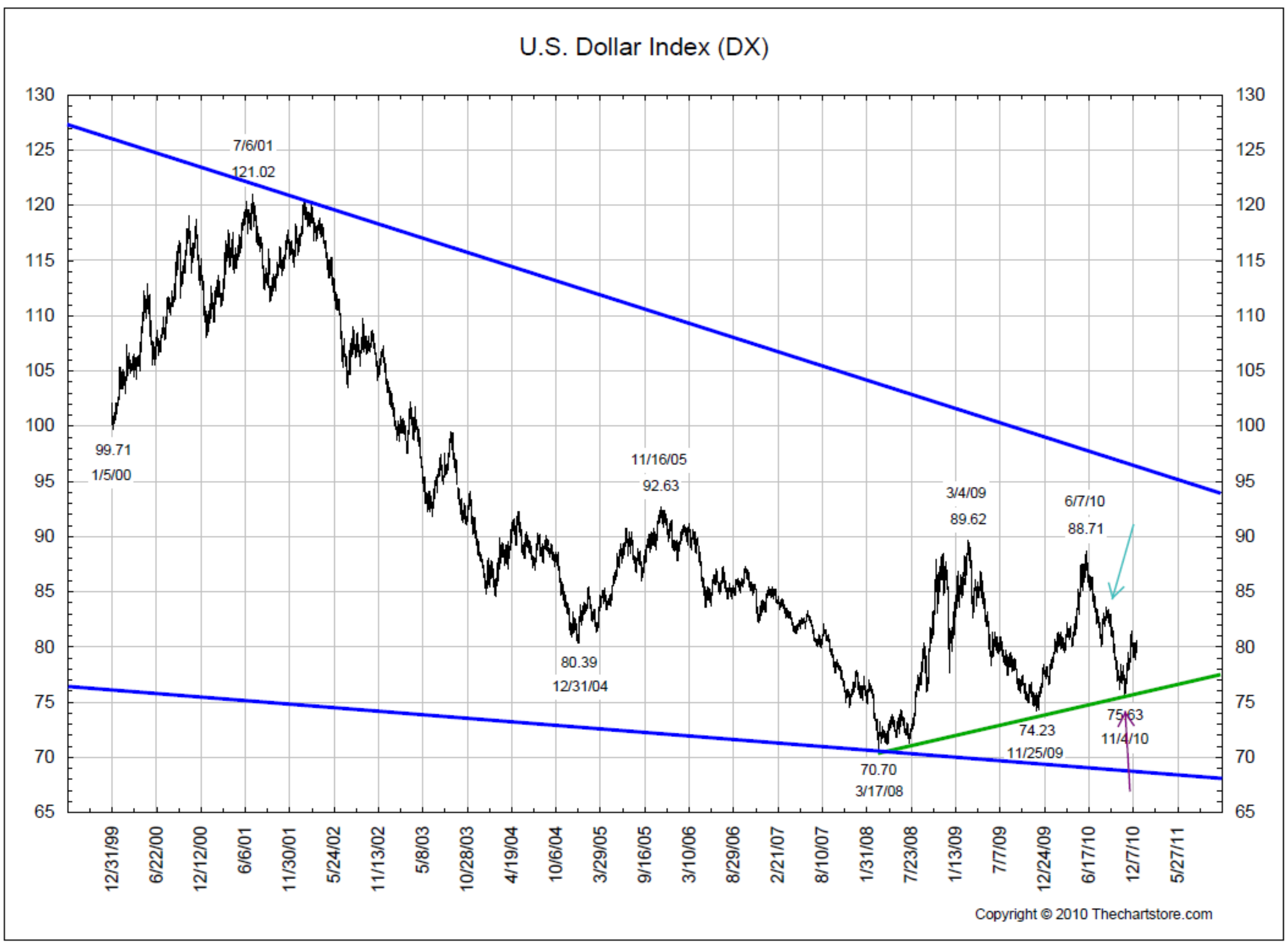
Similar levels for silver are as follows (I raised the upper "boundary level to $30.50 to take into account silver's new December high): $22.21 (purple arrow), $19.65 (orange arrow) and $17.09 (red arrow). So, like in gold, we would expect silver to correct down to $22.21 at a minimum and possibly down to as low as $17.09 without panic selling. This does not mean that the price of silver has to go down to $17 in order to have a meaningful consolidation/rest before resuming its bull market march higher.

Data as of November 2010



Lastly, we'll take a look at a shorter-term chart of the U.S. Dollar. One of the side effects of more quantitative easing would be to make the U.S. Dollar cheaper versus other foreign currencies. This would make U.S. companies that sell goods globally happy because their goods and services become less expensive in foreign countries and thus more competetive versus local goods and services. But the Fed is seeing that the effects of QE2 are not working out quite as they had intended, as we saw with interest rates, and now as we see with the U.S. Dollar. The light blue arrow represents when the Fed informally began talking about QE2 in late August/early September (note the effect they wanted they got with a slide in the value of the U.S. Dollar versus foreign currencies). But once they began implementation of QE2 in November (purple arrow) the dollar began to rise in value – not really what the Fed wanted to see happen. As you can also see, the shorter-term chart of the dollar is showing the establishment of a significant uptrend (notice the rising correction lows along the green uptrend line since 2008). This short-term uptrend in the dollar would be part of the reason for a correction/retracement in the price of gold and silver.

Data as of December 17, 2010



We will come back in February to review the 2010 year-end numbers to see how the holiday season “spirit” has either helped or possibly hinder the economy.

2011 should prove, as did 2010, to be a very interesting year for all of the various markets.

But, before then, we at Clearview Investment Partners wish you and your family a Happy New Year! And that 2011 (which, as my brother keeps reminding me, is suppose to be pronounced as “twenty eleven” and not as two thousand eleven) be a healthy and prosperous year for us all!

Kenneth G. Hobbs III
Managing Partner

TECHNICAL ANALYSIS

Seeks to define the trend of various markets, be it short-term, intermediate-term or long-term.

Remember, markets never move straight up or straight down, they move more like the ocean tides, surging (trending) up or surging (trending) down until the tide changes direction. We use various chart time horizons to give us an idea of how far a wave will move within a tide. Our intent is to keep clients apprised of changes in the various markets' movements in the months and years ahead.

Technical Analysis operates under three Basic Premises:

1. Market Action discounts everything. Or …

   Supply Versus Demand governs market action.

2. Prices move in trends. And …

   Trends stay intact until broken.

3. History often (but not always) repeats itself. Or …

   At the very least, it sure seems to rhyme.

The study of charts is based on the evaluation of past events to determine future probability. We seek a stock, or other asset or financial instrument, forming a particular pattern. We note that this pattern resembles that which typically precedes an asset's upward or downward move. In this way we are able to use our knowledge of the way a particular asset has acted in the past to estimate this particular asset's most probable future move. There will be a rational, logical and fundamental explanation for a particular chart formation usually following a given move in price.