Market Brief

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The views and opinions contained in this market brief are those of Capital Allocation & Management, Inc. and have been researched and analyzed by Robert Kennedy, CIO, Capital Allocation & Management

	2-Dec-05	25-Nov-05	Weekly % Change	YTD % Change	12 month % Change
Nasdaq Composite	2,273.37	2,263.01	0.46%	4.50%	5.84%
S&P 500 Index	1,265.08	1,268.25	-0.25%	4.39%	6.20%
Dow Jones Industrial Average	10,877.51	10,931.62	-0.49%	0.88%	2.69%
MSCI EAFE (Intl.)	1,632.90	1,610.48	1.39%	7.75%	11.20%
Wilshire 5000	12,692.76	12,702.41	-0.08%	6.03%	8.16%
10 Year U. S. Treasury Yield	4.51%	4.43%	1.81%	NA	NA
30 year U.S. Treasury Yield	4.72%	4.68%	0.85%	NA	NA

Not surprisingly, equities *seem* to have entered a consolidation mode last week, as most of the major indices experienced their first weekly decline in over a month. Equity traders apparently focused upon renewed gains in the energy sector, as well as the continuing signs of economic strength which, taken together, may belie the markets' faith that the Federal Reserve will soon pause in its efforts to curtail economic strength. The continued rise in gold prices also has created some nervousness among market watchers. Indeed, Jim Bianco (a widely followed bond market analyst) recently suggested that the rise in gold prices is an inflationary signal that will lead to substantially higher market interest rates in 2006. While it is relatively easy to agree with the idea that market interest rates will move higher in 2006, we do not necessary believe that the recent move in gold is necessarily indicative of higher inflation expectations. Just like with the energy markets earlier this year, we suspect that the recent strength in gold is more a result of momentum investors (primarily hedge funds) that are "piling on" as the year draws to a close. Be that as it may, the reality is that gold is moving up and, traditionally, that means that inflationary expectations are rising.

Another consideration of last week's declines revolves around the fact that the major indices all ran into technical resistance with their latest probes to new highs. Strictly from a technical point of view, consequently, it makes sense for the equity markets to test their recent breakout levels. These levels may be approximated as S&P 500 1246, DJIA 10,660 and NASDAQ 2200. If these levels are tested and the markets reverse (i.e., move higher), as expected, we should then see the markets rally to new highs. On the other hand, if these levels fail it may mean that the highs for the year are in. The best scenario is that we simply consolidate for a few days then ramp higher again. Overall, given the economy's continued strength, we remain bullish and expect higher price levels either later this year or early next year.

The Treasury markets also experienced declines, last week, with various economic reports highlighting strong economic growth. The Fed Funds Futures markets, after recently reducing the odds for continued rate hikes beyond the Fed's January 31st meeting (which will be Alan Greenspan's last), have turned course and now suggest a 60%+ probability that the Fed will push rates higher after their March meeting with a target of 4.75%. This places heightened importance on the Fed's comments after next week's meeting, where it is widely expected that the Fed will raise rates another 25 basis points to 4.25%. Two weeks ago, Fed analysts were convinced that the Fed would indicate that it was about to "pause." If the post meeting comments do not support this idea, we suspect the Treasury market will experience a bout of volatility.

Economic Reports: It is a pretty slow week for economic reports. On Tuesday, October Factory Orders should show a 2.2% rise, after September's decline of 1.7%. Also on Tuesday, the third quarter's productivity report should be revised upward to 4.5%, after an initial estimate of 4.1%. On Friday, the University of Michigan's estimate of consumer sentiment should post a reading of 85, after November's level of 81.6.