

# Meeder Financial

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Following new recovery highs for the major stock market indices during April, concerns regarding sovereign debt and the sustainability of the economic recovery weighed on the financial markets during May. Investors expressed their apprehension by driving the euro currency to multi-year lows as well as selling risky assets such as stocks and commodities around the world. Alternatively, U.S. Treasury securities were the beneficiary of emerging fears, and experienced price appreciation and declining yields. The price of gold, another safe-haven asset, increased to a new all-time high of approximately \$1,250 per ounce. Although financial markets are conveying uncertainty, recent data suggests that the economic recovery remains on track. For the month of May, the Dow Jones Industrial Average ended down 7.56%, the S&P 500 ended down 7.98%, and the Russell 2000 Index of small-cap stocks ended down 7.59%.

The sovereign debt crisis in Europe has served as a key catalyst for igniting investor concerns and spurring declines in financial markets around the world. Despite a massive bailout loan package totalling nearly \$1 trillion provided by eurozone members and the International Monetary Fund (IMF) for troubled countries, investors remain wary of the potential for default within the European community. Furthermore, many European countries struggling under heavy debt burdens have resorted to austerity measures intended to reduce deficits through public spending cuts and/or higher taxes. Economists are concerned that the reduction in public spending and jump in tax rates could push some countries back into recession, especially since the economic recovery appears fragile in many developed economies.

In fixed-income markets, the month of May was dominated by investors moving away from investment grade and high-yield corporate debt instruments in an effort to reduce risk exposure. This recent move began in April and has persisted since. The main reason for the short-term shift in sentiment was uncertainty. Investors grew more and more concerned over events unfolding in Europe, reregulation of the financial industry, the future landscape of taxes and questions surrounding the strength of the domestic and global economies. The month of May marks the first month in the past year to realize such a move away from riskier investments. While this sector has

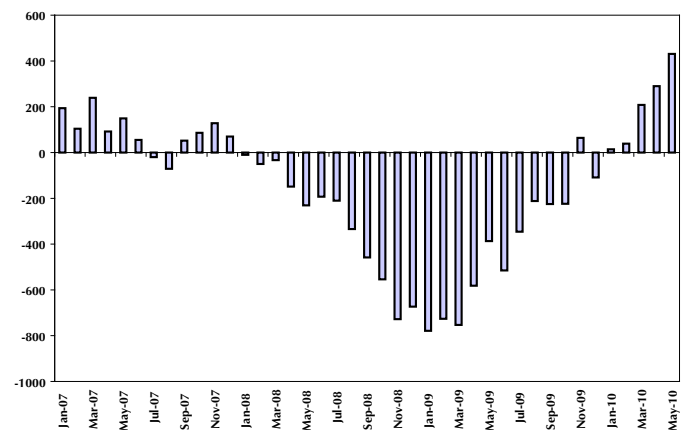
## OUR MISSION

*Every day, our mission is to exceed, with integrity, passion and discipline, the expectations of our clients' overall investment experience.*

realized more volatility of late, most investors still believe over the long-term it should outperform. This is consistent with the current backdrop of the economy which we believe is growing at a sustainable pace. Corporate earnings continue to improve while interest rates remain low suggesting the environment is supportive of further expansion.

Since risk aversion heightened in May, U.S. Treasury securities outperformed all other sectors in the fixed-income markets for the month on a total return basis. Longer dated maturity holdings also outperformed shorter dated maturity holdings. U.S. Treasury securities have continued to trade in a volatile range for the past year. If we use the 10-year U.S. Treasury note as a proxy, yields have been cycling between a high of 4.00% and low of 3.15%. U.S. government agency and mortgage-backed securities also performed relatively well for the month of May. The housing market fall may have abated for the near-term giving market participants the confidence to remain holders of these debt sectors.

**Chart 1: Non-Farm Payrolls (in Thousands)**



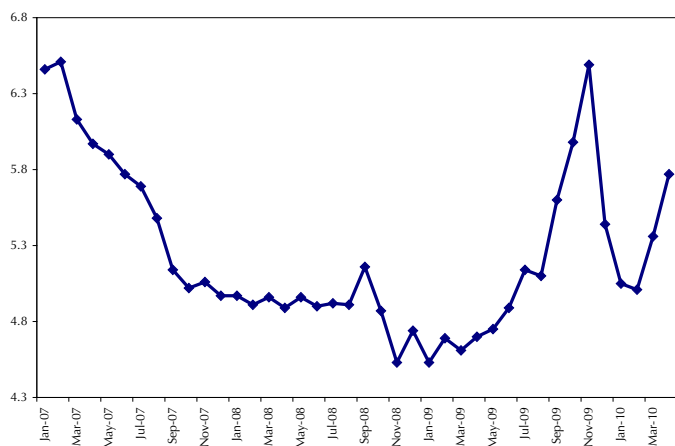
Source: Bloomberg

Job growth in the U.S. continued during May, but at a much slower pace than anticipated. Nonfarm payrolls increased by 431,000 (see Chart 1), although 411,000 were temporary workers hired to conduct the 2010 Census. When excluding the temporary Census workers, the net increase of 20,000 jobs failed to match the 218,000 private sector jobs added in April, signaling to investors that job growth momentum may have stalled. However, since the year began the U.S. economy has added a total of 928,000 jobs (including census workers),

illustrating that the job market is improving despite a reduction in the recent pace of private sector payroll additions. The unemployment rate fell from 9.9% in April to 9.7% in May, which is also where the rate held for the first 3 months of the year. However, many economists anticipate further increases in the unemployment rate as unemployed workers re-enter the labor force.

Many economic indicators continue to signal that the U.S. economy remains on the recovery path. The Institute for Supply Management Manufacturing Index (ISM) was reported at 59.7 in May, making it the tenth consecutive month above 50, which indicates economic expansion. Furthermore, the ISM Non-manufacturing Index remained steady at 55.4 in May, which is the fifth consecutive month above the expansion level of 50. Continued readings above 50 in both the Manufacturing and Non-manufacturing ISM indexes provide support that the economy is gaining momentum. Additionally, although not as strong as February and March, retail sales increased 0.4% in April, and are up 8.8% from last year.

**Chart 2: Existing Home Sales (units in millions)**



The housing market received its final boost from the homebuyer tax credit, which expired at the end of April. New home sales, existing home sales (see Chart 2), and housing starts all increased significantly in April, yet questions remain regarding the sustainability of recent growth without government stimulus efforts to spur such activity. Although the homebuyer tax credit has expired, a positive result of recent market turmoil is low U.S. Treasury security yields, which in turn influences mortgage rates. As of the time of this writing, the 30-year fixed mortgage rate was approximately 4.72% compared to 5.59% a year ago according to Freddie Mac. Housing activity through

the remainder of the year will prove vital to answering the question of whether or not government stimulus efforts have spawned actual demand.

**Maintaining Defensive Position**

While lingering uncertainties present challenges to the global economy, we believe opportunities in the equity markets will persist over the near-term future, but that volatility will continue as well. As a result, we stand ready to adjust our defensive position in order to manage risk for our clients. Due to readings from our investment models, we are maintaining a small defensive position in the applicable funds and portfolios.

Our investment models have also remained relatively consistent since we transitioned into 2010 across the dynamic of large-, mid-, and small-cap companies. We have maintained an overweight position in small-cap stocks, and we have also maintained an overweight in mid-cap stocks. Additionally, our models have continued to indicate a preference for value investments, and we have responded by maintaining an overweight allocation toward value investments across all capitalization ranges. In terms of sector exposure, we have maintained an overweight to the energy sector due to model indications. We are also overweight the consumer staples and healthcare sectors, while being underweight the technology sector. We will continue to closely monitor market conditions and our internal investment models, making select tactical shifts as necessary to take advantage of opportunities and protect against downside risk.

Our fixed-income portfolios are positioned to accommodate the potential for an economy with sustainable growth. The duration of our fixed-income portfolios remain slightly below that of our benchmarks, which should provide a benefit in a rising rate environment. In accordance with our models, we also continue to favor the investment grade corporate debt sector over government agency and U.S. Treasury securities.

*Thank you for your interest in our investment management services. For more information on our portfolios or investment strategies, including fact sheets and prospectus, please contact us at Toll Free 866-633-3371.*