



Markets This Week

May 13, 2006

In This Issue:

Investment Idea

Quiz

Our Results

Market Highlights

Behavioral Finance Indicators

Answer to the Quiz

Investment Idea

Question:

Should I buy stocks with a market order or a price-limit order?

Answer: Let us first define these two terms. If you place a market order you will be buying at a prevailing (and unknown) price. On the other hand, a price-limit order allows you to buy stocks at a specified or better price.

A price-limit order carries less risk than a market order. In fact, new investors should almost never use a market order. Let us look at the IPO (Initial Public Offering) of Tim Hortons (symbol THI) (Chart 1) as an example. The IPO was sold at \$27 to a small portion of the public before it started trading. If you had placed a market order on the first day of trading, you would have bought it at about \$36 as the market opened. With a price-limit order of \$32, you would have bought Tim Hortons at \$32.

Chart 1. Tim Hortons' Price Per Share



Chart courtesy of StockCharts.com

Please keep in mind that a price-limit order does not guarantee that stocks will decline to your pre-specified level for you to buy them.

Quiz

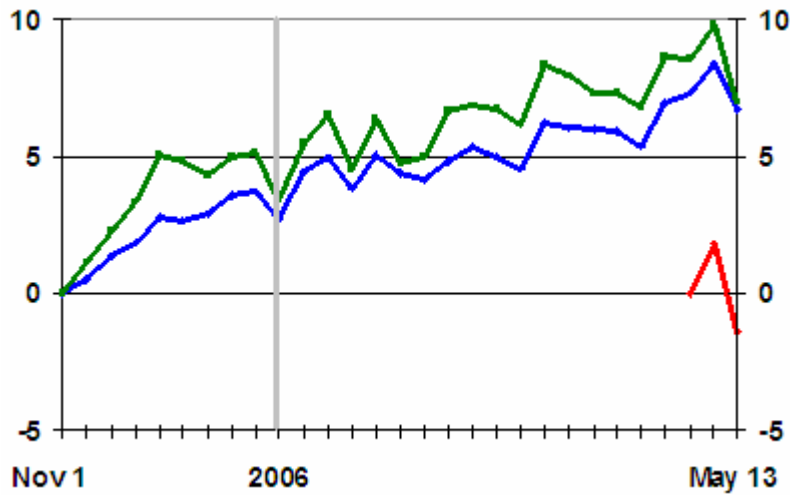
An ABC stock finished trading yesterday at \$10 per share. You have placed a price-limit order to buy 100 shares at \$9.80 per share. As the market opens, ABC starts to trade at \$9.70 per share. At what price did you buy the shares?

- A) \$10
- B) \$9.80
- C) \$9.70
- D) \$9.60

Answer at the bottom of the newsletter.

Our Results (Cumulative %)

Chart 2.



Symbol	One-week %	Since Inception %	We Bought On	We Sold On	Expected Return %	Risks	Reasons
Members Info	-3.99	-1.63	May 1, 06	-	Market + 4	Medium	Trend investing
Members Info	-2.36	-1.25	May 1, 06	-	Market + 2	Low	Investment style
InvestWELL Picks (Average)	-3.16	-1.44					
Passive 60/40	-1.56						
S&P 500	-2.60						

Last week, our **InvestWELL Picks** declined by 3.16%, which was more than the general market. Thus far, Our InvestWELL Picks holds only two positions, which has a potential to expose them to greater volatility.

It is interesting to note that the conservative 60/40 portfolio almost caught up with the S&P 500 index. Hence, the buyers of only US equities over the last 6 months were exposed to greater volatility, yet, as of now ended up with nearly the same return. This is an important lesson that diversification and risk reduction really work.

Market Highlights

May 7 – May 13, 2006

- In case you did not listen to the market news during the last two days, the equity market suffered very heavy losses (S&P 500 lost 2.4% in the last two days) (Charts 3 & 4). The media has attributed the losses to the fear of inflation and the rising interest rates announced on Wednesday. It is partially true but, overall, we beg to differ. The rise in the interest rates was widely expected even before Wednesday, however, the last time we checked markets were cyclical and the current market has been in an overextended mode for a few months.

Charts 3 & 4. S&P 500: 5 Years and Last 10 Days



Charts courtesy of StockCharts.com

- The Canadian markets declined in tandem with the US and International equities (Charts 5 & 6).

Charts 5 & 6. TSX Canada: 5 Years and Last 10 Days



Charts courtesy of StockCharts.com

- During the last week, gold and gasoline went up while US dollar and consumer confidence declined. It also appears market fear and general risk aversion are rising.
- The European economy expanded by 0.6% in the first quarter of 2006, the fastest pace since 2004. Evidence of strengthening economy has increased probability that the European Central Bank will raise interest rates next month.
- The Bolivian decision to nationalize its energy resources has been discussed by many international leaders. The nationalization may have severe consequences for long-term investment prospects of many emerging markets i.e. investors will shy away from them because of the uncertainty. On the other hand, it is important to acknowledge that the gains of free trade and economic growth should be shared by the majority of the population rather than a small elite.
- The Globe and Mail reported that Canada's top CEOs' salaries increased by 39% last year. Most of the gains are attributable to stock options.

Worth Watching

- Last week, Barclays Global (www.ishares.com) issued new ETFs (Exchange Traded Funds) that focus on a number of interesting industries. For instance, investors can buy US Health Care Providers (symbol IHF), US Medical Devices (symbol IHI) or US Home Construction (symbol ITB). The new instruments are very reasonably priced with an annual fee of 0.48%.
- The OECD (Organization for Economic Co-operation and Development) released its study that compared the total taxation level in various countries. The highest taxes are in Sweden (50%), Denmark and Belgium. The lowest in Mexico (19%), Japan, Korea and the US. The taxpayers in highly tax countries do benefit by having universal health care, generous pension plans and more affordable education. On the

other hand, taxpayers from countries with low taxes have greater choice over how to spend their money.

Behavioral Finance Indicators (see explanation)

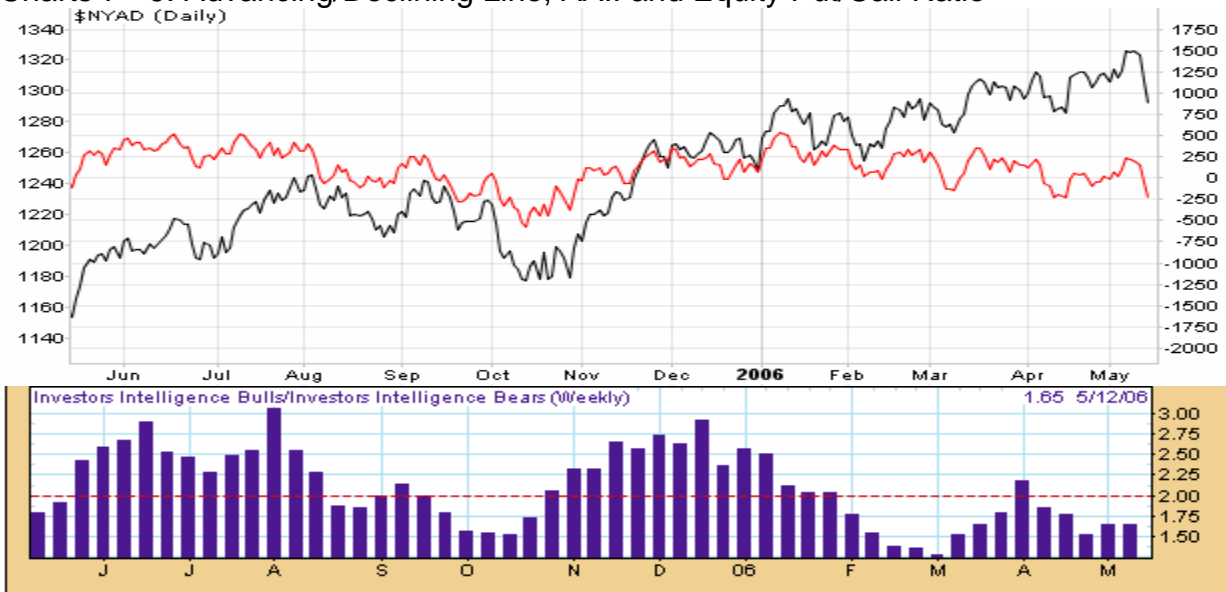
For the last few weeks, we pointed out that equities were having a difficult time penetrating the resistance level (1315 on the S&P 500). Usually, what cannot go up, will come down. This is exactly what happened last week as equities plunged. We have noted a strong divergence developing on the advancing/declining ratio since January 2006. This type of divergence can only last for so long before it gets corrected.

We are not sure if the recent downturn spells only a healthy correction or an outright long-lasting bear market. In any case, the upcoming weeks may not be pretty. In the long-run, however, the capital markets offer a great potential for capital appreciation.

For an historical comparison, please look at August 2005 on Charts 7, 8 and 9. Please consider the following factors:

- Chart 7 – the divergence between prices (black line) and the advancing/declining line (red line) since January 2006
- Chart 8 – the confidence of small investors (as represented by AAll, i.e., the ratio of bulls/bears). This indicator provides a signal which contradicts other indicators (i.e., low confidence of small investors)
- Chart 9 – the declining put/call ratio indicates that small investors have confidence that the market will advance (red line).

Charts 7 - 9: Advancing/Declining Line, AAll and Equity Put/Call Ratio





Charts courtesy of StockCharts.com and DecisionPoint.com

Answer to the Quiz:

C is correct.

A price-limit order will get you the shares at a pre-specified price level or better. The market has opened at \$9.70, which was below your price-limit order. Hence, you bought shares for less than you were planning. This is a good thing.

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