



Markets This Week

May 27, 2006

In This Issue:

Investment Idea

Quiz

Our Results

Market Highlights

Behavioral Finance Indicators

Answer to the Quiz

Investment Idea

Question:

How do mutual funds represent their investment styles?

Answer: Mutual funds use style boxes which show a fund's market capitalization (from small capitalization stocks to large ones) and investment objectives (from value stocks to growth stocks) (Chart 1).

Chart 1. Investment Style box

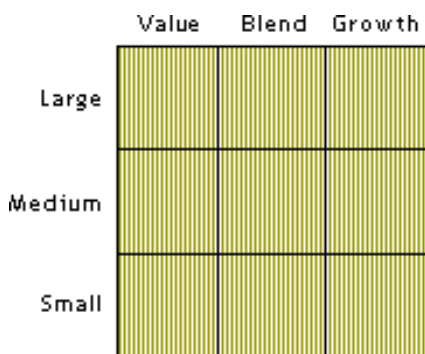


Chart courtesy of The Motley Fool

The style box helps investors determine how closely their investment strategy is aligned with a style followed by a particular mutual fund. Naturally, investors would gravitate towards funds whose investment style matches with their investment strategy.

Quiz

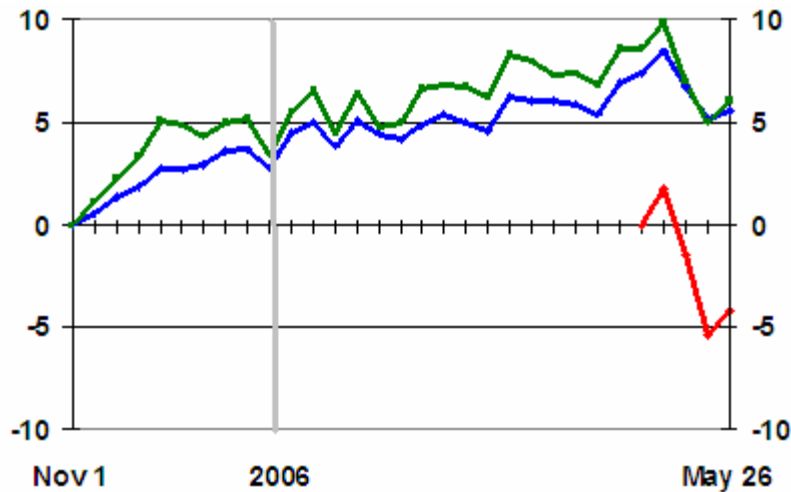
What is the investment style of the S&P 500 index?

- A) Large Cap and Value
- B) Large Cap and Blend
- C) Mid Cap and Growth
- D) Small Cap and Blend

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	0.93	-5.39	May 1, 06	-	Market + 4	Medium	Trend investing
Members Info	1.46	-3.07	May 1, 06	-	Market + 2	Low	Investment style
InvestWELL Picks (Average)	1.20	-4.23					
Passive 60/40	0.35						
S&P 500	1.04						

Last week, our **InvestWELL Picks** outperformed the general market by a small margin. The InvestWELL Picks holds only two positions, which exposes InvestWELL Picks to greater volatility.

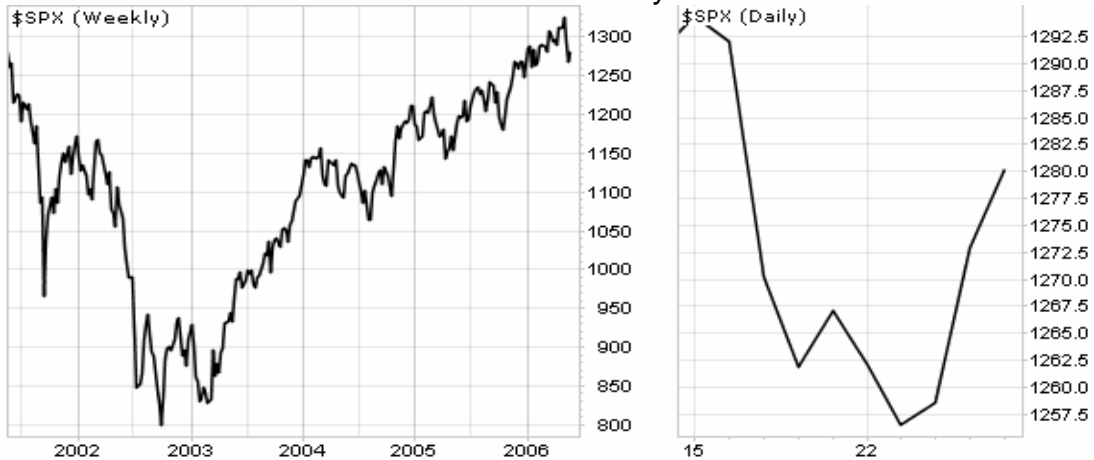
Since the inception on Nov. 1, 2006, the conservative 60/40 portfolio has achieved a solid return and a lower volatility than the S&P 500 (Chart 2). This proved the value of diversification and good risk management practice.

Market Highlights

May 21 – May 27, 2006

- In the last week, the US equities staged a welcome rebound which was initiated from a deeply oversold level and supported by a slew of positive economic news e.g. housing market, GDP and personal income

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



Charts courtesy of StockCharts.com

- The Canadian markets breathed a sigh of relief as the TSX climbed up in tandem with the US markets (Charts 5 & 6).

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



Charts courtesy of StockCharts.com

- The volatility index (symbol VIX) has recently moved to levels unseen in over 2 years (Chart 7). Usually, high readings of VIX indicate there is a lot of fear in the market and a potential for a turnaround. Similarly, we believe the markets will likely rebound, but are unlikely to return to their previous highs.

Chart 7. S&P 500 and VIX (1 Year)



Chart courtesy of StockCharts.com

- The Bank of Canada raised its key interest rates to 4.25%, its highest level in almost 5 years. At the same time, the Bank of Canada signalled that it will put interest rate increases on hold for some time given the moderation of economic growth. This is welcomed news for borrowers.
- The well-known OECD (Organization for Economic Co-operation and Development) has published its twice-yearly review, which warns the US Federal Reserve about high deficits, deep trade imbalances and low savings. The report predicts that the value of the US dollar will need to fall to the extent of one third to one half. Translation - the holders of US dollars need to fasten their seatbelts.

Worth Watching

- Domini Social Equity Fund (symbol DSEFX), one of the most known mutual funds that specializes in Socially Responsible Investing, wants to move away from indexing formula to active management. The founder, Ami Domini, believes that the social screening added value to the stock selection, but the fund was constrained by the way an index is weighted. We believe that DSEFX is an interesting case of self-imposed restrictions that may not be the most optimal. All investment strategies should allow for seizing opportunities when they arise.
 - The Chicago Mercantile Exchange has finally rolled out futures and options that allow investors to hedge against the fall of the real estate prices in 10 major US cities: Boston, Miami, New York, San Diego, San Francisco, Washington D.C., Chicago, Denver, Las Vegas and Los Angeles. For most home owners, real estate is the largest (and rather illiquid) asset.
-

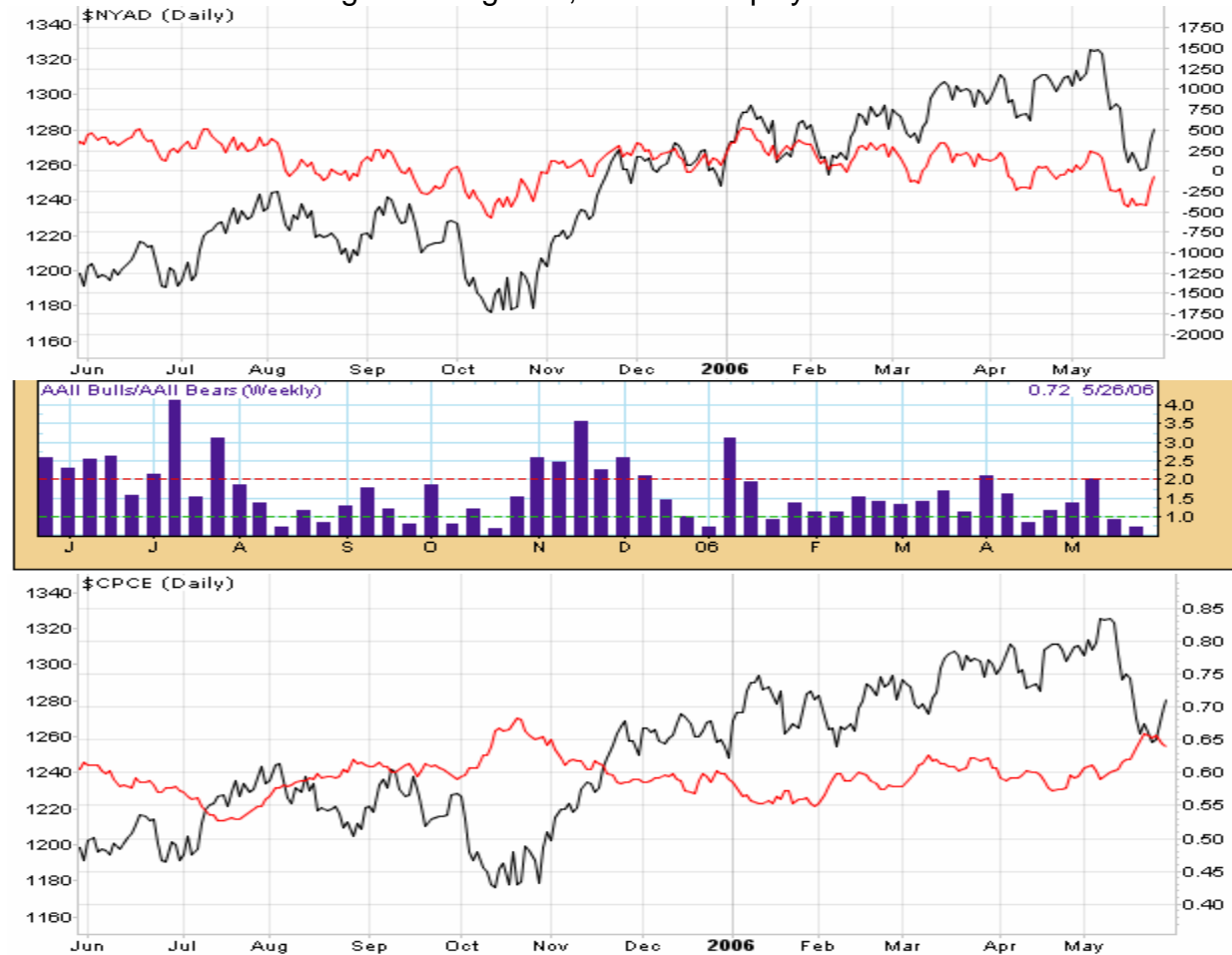
Behavioral Finance Indicators (see explanation)

Given the readings of most of the behavioral finance indicators, we believe the stock markets will likely rebound in the upcoming weeks. However, the market will likely not be able to reach the recent highs.

Please consider the following factors:

- Chart 8 – the divergence between prices (black line) and the advancing/declining line (red line) is narrowing but the two started to diverge in February this year.
- Chart 9 – a low confidence of small investors (as represented by AAll, i.e., the ratio of bulls/bears) points to a short-term rebound. Small investors are usually a contrary indicator.
- Chart 10 – the rising put/call equity ratio indicates that small investors are losing their confidence that the market will advance (red line). Again, an excellent contrary indicator pointing to a rebound in a short-term.

Charts 8 - 10: Advancing/Declining Line, AAll and Equity Put/Call Ratio



Charts courtesy of StockCharts.com and DecisionPoint.com

Answer to the Quiz:

B is correct. The S&P 500 index represents the largest 500 US companies. (i.e. large caps) Some of them are value stocks (i.e. low P/E ratio) while others are growth stocks (i.e. high P/E ratio). Hence, it is following an investment objective known as blend (Chart 11).

Chart 11. S&P 500 Investment Style Box.

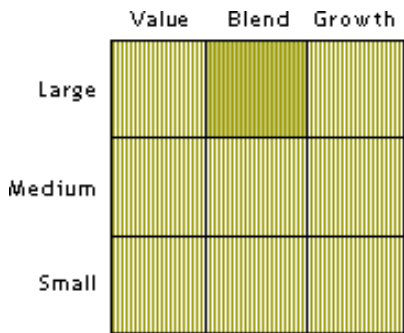


Chart courtesy of The Motley Fool

Copyright

The contents of this publication are the property of InvestWELL Financial and may not be summarized, reproduced, or rebroadcast in any fashion without our written permission.

Disclaimer

InvestWELL Financial's first priority, as a provider of independent and unbiased financial information, is to educate our clients. Not only do we provide practical information about securities, but we also coach our clients to become successful independent investors. As such, InvestWELL Financial does not assume any responsibility whatsoever for the use of any information from the website or related publications. Although all sources of information are vetted and the information is believed to be reliable, it is not provided as investment advice. Past performance is not an indicator of future performance in securities. Each portfolio must be balanced and based on personal circumstances. High-risk investment decisions should be made in consultation with a professional.

InvestWELL receives no commission or benefit of any kind from the companies whose securities InvestWELL Financial showcases. We do not necessarily own shares in the showcased securities, but if we do, these shares would only form a very small part of widely-held and publicly distributed companies. There is no intention whatsoever of profiting in a manner where the price-impact of trading or holding of a security might arise. The website and related publications of InvestWELL Financial are intended to only be used for educational purposes.

Thank you for reading Markets This Week.

Please feel free to share it with your friends.