

# The Week

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## Ready for spring and some good news again

*The first day of spring is finally here, and after the long cold winter, many people are ready for some relief. It won't be long before the weather is consistently warmer and people begin to feel better. This is often a good time for the stock market. We just need to get a little better news too.*

Winter is a difficult time for many people. We trudge through the ice and snow, waiting for some relief in the spring. Often, the final weeks of winter can be the most difficult because many people's spirits are worn down by the effort it takes to make it through the cold and dark days. This year, problems of the bad weather were compounded by bad geopolitical news. Consequently, the stock market turned from a steady advance earlier in the winter into another volatile correction toward the end of the season.

Obviously, the news has not been good recently. The disaster in Japan continues to unfold while the turmoil in the Middle East and North Africa has turned into a military conflict in Libya. These problems may continue to weigh on investor sentiment and the stock market over the near term. However, if events take a turn for the better, the stock market could also turn up because the long-term fundamentals remain favorable.

The first problem hitting the market this year was the turmoil in the Middle East with protests in Tunisia, Egypt, Libya and now Bahrain. Along the way, the Japanese earthquake and tsunami caused a nuclear reactor crisis. It seems the problems were piling up just like the snow. Of course, some days the news did not look as bad as others, and the stock market bounced up again. Unfortunately, it is probably too early to assume that these problems are behind us like the winter soon will be.

That's because the United States is now involved in another military conflict in the Middle East. At this point, our mission, along with other countries from the United Nations, appears to be limited to enforcing a no-fly zone over Libya. However, this is the third military conflict for the United States in the Muslim world, and many people are already

wondering if this limited action may turn into another long-term war that will be difficult to exit.

Looking back, investor sentiment turned from very positive early this year to very concerned in just a few weeks. This shift in sentiment is normal during a stock market correction. In fact, many investors have turned more cautious as the news deteriorated. So far, the current stock market correction is deeper than the short downturn last November but not as severe as the more extended market pull back last summer.

Experience shows that once prices begin to decline, sentiment tends to follow a pattern. At first, investors are concerned but not worried. After all, the markets do not go in only one direction, and a dip in prices is not unusual after an extended advance. However, if the news continues to deteriorate, then sentiment declines along with the market as uncertainty replaces confidence. In most corrections, sentiment usually becomes very negative at the lows when investors begin to fear that the market decline could persist for a long time and extend a lot further than originally expected. This is often how things appear at important market lows when investor confidence has been drained by persistent bad news.

As long as the economy remains healthy, the stock market is likely to recover from these periods of doubt. Unfortunately, it may take a little more time before the current string of bad news lessens, and the investors begin to see the light at the end of the tunnel again.

Fortunately, all the news is not bad. Last week, the Federal Reserve upgraded its assessment of current economic conditions, acknowledging that the economy is now on a firmer footing. In addition, the Philadelphia Federal Reserve's March business activity index jumped to its highest level

since January 1984. This is an encouraging sign that the breadth of the economic recovery is more widespread and sustainable.

The Federal Reserve has not yet said that the recovery is self-sustaining. But policymakers may be taking a step in that direction by saying that the recovery is on a firmer footing. This could also be an early sign that the Fed is getting ready to stop its current round of stimulus when the second round of quantitative easy or QEII is scheduled to end in June.

In summary, the calendar tells us that spring is here and the weather is going to improve. If the geopolitical news also takes a turn for the better, the current correction in the stock market could end and prices could advance again. At this point, the bottom of the correction may not yet be in place because investor sentiment does not appear as negative as it often gets at important market lows. Therefore, we remain cautious in the short run while continuing to be positive on the economy and the stock market over the long run.

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