





A Tale of Two Wallets, Revisited

Why we're betting on the enterprise, not the consumer

The disparity we recently observed between macroeconomic data such as housing prices (bad) and corporate lodging demand data (not so bad) reminded us of a thesis we first posited back in June 2008, when we wrote a piece entitled "A Tale of Two Wallets" (available upon request). In that piece, we indicated that we'd much rather bet on the "wallet" of the average US Fortune 500 company than that of the average US consumer.

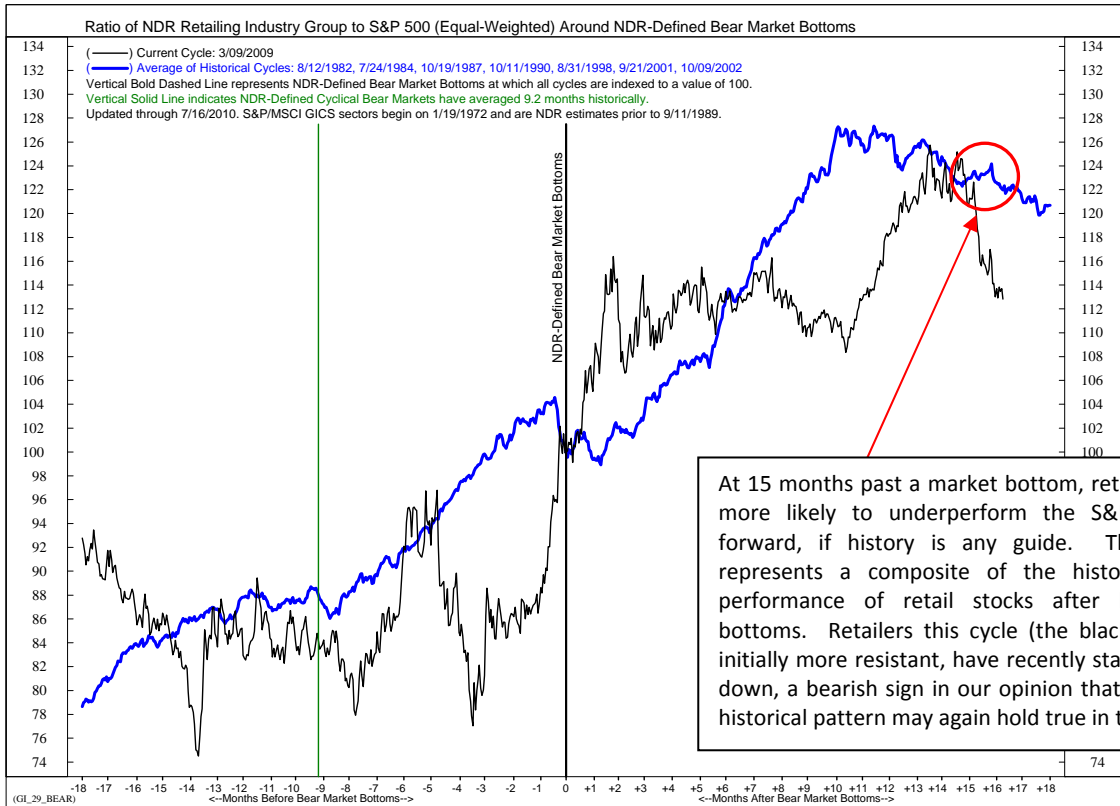
What's the investment implication? *We think that now is a good time for investors to look through their portfolios and consider raising risk management stops on certain consumer-cyclical stocks. As a potential use of the funds, we'd recommend looking to replace consumer exposure with reasonably valued stocks in sectors, such as software, whose customers are primarily other large corporations.*

 <p>US CONSUMER WALLET <i>After two years, still dire...</i></p> <ul style="list-style-type: none"> • Housing markets have not recovered despite massive Fed stimulus and low mortgage rates. • Consumer debt levels are still near historical peaks. • The unemployment rate is still hovering around 10%. • Consumer sentiment levels are still low, and nervousness concerning stock market volatility and low interest rates is affecting confidence. 	 <p>US CORPORATE WALLET <i>Stronger than ever...</i></p> <ul style="list-style-type: none"> • Many corporate balance sheets are currently high in cash, cash flow is currently exceeding capital expenditure, and cash flow as a percentage of GDP is at an all-time high (source: NDR research). • Credit conditions remain constructive, with the debt markets open for funding at attractive rates. • Global diversification means less reliance on domestic revenue and more exposure to emerging market economies
--	---

Is the rally for consumer cyclicals long in the tooth?

If historical bear market bottoms are any guide, traditional consumer cyclical stocks could be nearing the end of their run of outperformance. Research provider Ned Davis Research (NDR) performed an analysis of relative strength trends of various industry groups relative to the S&P 500 before, at, and after bear market bottoms (NDR uses a blend of relative price data from the last seven cyclical bear markets, starting in 1982, to arrive at a composite). As evidenced by the blue line on the chart below, relative strength for the retailing sector starts to peak around 11-12 months after an average bear market bottom. However, in this current cycle (the black line on the chart), it appears that relative strength may have actually peaked later, at around 14 months. If relative strength has truly peaked, the chart suggests to us that it could potentially have further to fall.

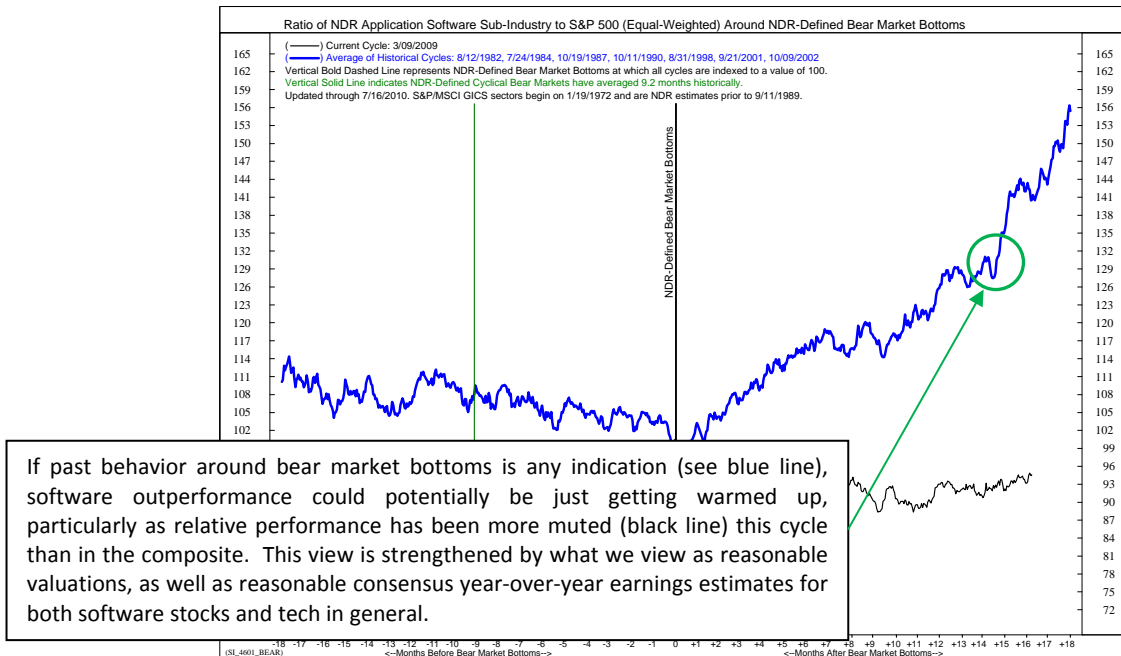
Retailing Industry Group Price Performance Relative To The S&P 500



© 2010 Ned Davis Research Inc. Further distribution prohibited without prior permission. All Rights Reserved. See NDR Disclaimer at www.ndr.com/copyright.html. For data disclaimers refer to www.ndr.com/vendorinfo/ Past performance is no guarantee of future results.

Now, compare retail’s performance 15 months past the bull market bottom with another supposedly “cyclical” industry -- software. Software has historically continued to work well after bear market bottoms are established, as suggested by the chart below.

Application Software Industry Group Relative Price Performance



© 2010 Ned Davis Research Inc. Further distribution prohibited without prior permission. All Rights Reserved. See NDR Disclaimer at www.ndr.com/copyright.html. For data disclaimers refer to www.ndr.com/vendorinfo/ Past performance is no guarantee of future results.

While we don't put a lot of faith in overlay charts in isolation, we do think that this historical pattern, in conjunction with attractive valuation for tech stocks both in absolute and relative terms may hold some predictive power. More specifically, we believe that the stocks in industries like software that sell into other enterprises companies are both reasonably priced and have reasonable embedded expectations for future growth.

Bottom Line: We believe that now is the time to raise risk management stop levels on stocks of companies that source their revenue primarily through serving the US consumer. *We would focus risk management attention most acutely on the following industries:*

Teen Apparel Retail	Internet Commerce
Transports	Casinos/Gaming
Specialty and Hardline Retail	Financials
Electronics Retailing	Autos

Tech Stocks That We Like

We still find many stocks in corporate-facing businesses, particularly in the tech arena, reasonably valued and technically attractive, particularly given the recent sell-off in tech stocks in the wake of disappointing earnings from IBM and Texas Instruments (TXN-N-\$25.55). Below are some of our preferred ways to play this theme:

- **IBM (IBM-N-\$129.79):** Despite a negative stock reaction to earnings, we still believe that IBM is an excellent value, and that its software business is still on track.
- **Cisco Systems (CSCO-NasdaqGS-\$22.73):** CSCO's networking equipment will help power the wired enterprise of tomorrow, with future growth in corporate areas such as telepresence.
- **Sigma-Aldridge (SIAL-NasdaqGS-\$53.45):** SIAL's biochemical testing kits are used in scientific research labs and healthcare facilities, an example of a non-consumer, non-cyclical customer end market.
- **Amdocs (DOX-N-\$28.59):** DOX sells mission-critical customer care and billing software into large telecommunications operators. With the growth and added complexity of smartphones for enterprise use, we expect business prospects for DOX to remain solid going forward.
- **PowerShares Dynamic Software Portfolio (PSJ-NYSEArca-\$21.01):** PSJ is a software ETF that contains the kinds of names we expect will benefit from continued strength in enterprise spending.
- **PowerShares Dynamic Media Portfolio (PBS-NYSEArca-\$11.62):** Large corporate ad spending continues to improve in areas such as Internet, cable and satellite TV, and even magazines, thus reinforcing the idea that media is typically a "late cycle" economic play.

Technology and Internet-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.

Exchange Traded Funds (ETFs) are sold by prospectus. Please consider the investment objectives, risk, charges and expenses carefully before investing. The prospectus, which contains this and other information, can be obtained by calling your financial advisor. Read it carefully before you invest.

Caution: Many of these companies are reporting earnings in the next 1-4 weeks. Risk-adverse investors who are uncomfortable with near-term volatility may want to wait until after earnings season to buy, as technology stocks often tend to be volatile during reporting season.

Doug Sandler, CFA, Chief Equity Officer • 804-549-4803 • dsandler@riverfrontig.com
Sam Turner, CMT, Portfolio Manager • 804-549-4808 • sturner@riverfrontig.com
Chris Konstantinos, Portfolio Risk Manager • 804-549-4810 • ckonstantinos@riverfrontig.com
Paul Louie, Portfolio Management • 804-549-4807 • plouie@riverfrontig.com
Riverfront Investment Group, 9011 Arboretum Parkway, Suite 110, Richmond, VA 23236
www.riverfrontig.com

RiverFront Investment Group, LLC, is a registered investment adviser. The company manages several fee-based portfolios comprised of various equity and fixed-income securities. Any discussion of specific securities is provided for informational purposes only and should not be deemed as a recommendation to buy or sell any individual security mentioned. We own shares of IBM, CSCO, IGV, SIAL, DOX, and PBS in our managed discretionary portfolios. Other securities mentioned may be considered by Riverfront Investment Group for purchase or sale in client portfolios in the future. Opinions expressed are current as of the date shown and are subject to change. They are not intended to be investment recommendations. Past performance is no guarantee of future results.