Continuum Global Asset Mgt., LLC

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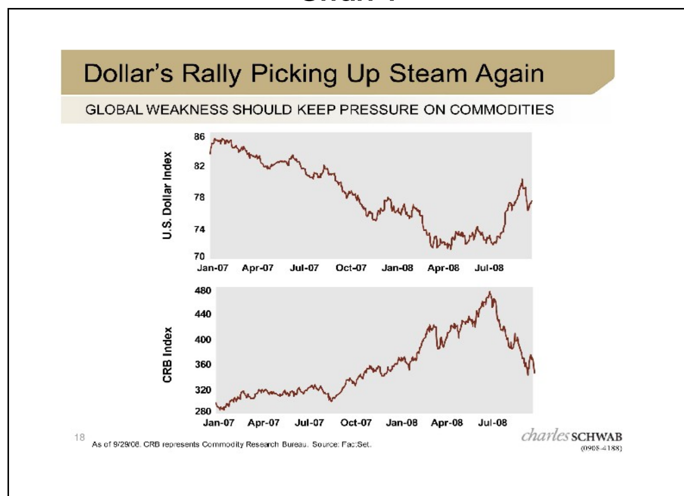
Sector Review

Capital markets are constantly in a state of flux ; an understantement. The truth is that we as investors are constantly trying to learn and refine our approaches. Unfortunately, the markets have an uncanny ability to throw curve balls that either compel us to swing when we shouldn't or force us to freeze when we should have swung: you get the picture.

Even though I believe that in the long term markets reward companies that continue to add value in their respective fields, markets have a ruhless way of punishing investors when they turn a blind eye to the laws of nature. Nature has a way to normalize things, whether they are bubbles or busts. In the short and intermediate term, most market participants are trying to outperform markets by crowding areas that seem attractive, undervalued or apparently seem the areas of growth.

In an endeavor to capitalize on this phenomenon, following is a brief analysis of major sectors which I believe addresses the short to medium term movement of assets based on fundamental and investor sentiment (superfluous) variables.

Chart 1[1]



Commodities

Up until mid 2008, commodities and energy were the darling sectors of Wall Street. The adjacent Chart 1 clearly illustrates the inverse correlation of commodities index with the dollar. I believe that there are two dimensions in the movement of commodities. The fundamental layer, which includes the increase in global demand for commodities as the emerged and emerging economies, continues to consume more and more of these basic goods and materials. In addition, the superfluous dimension in the rapid increase in commodity price inflation was the role of institutional and to a certain extent retail investors. This artificial increased buying pushed commodities and energy at unsustainable levels which actually resulted in reduction in consumption at various levels.

I still believe that fundamentally the acceleration in worldwide consumption of commodities is still intact. As mentioned, the strength in the dollar has an inverse relation to the price of commodities. I believe that the dollar could continue to strengthen under two main scenarios:

1. US rate of interest start to stabilize and the Federal government (FED) start to raise rates.
2. The US economy strengthens relatively.

The recent liquidity crunch within the financial sector has compelled the Bernanke and Paulsen team to pump enough money in the system that in my view may give rise to unexpected hyper-inflation. Remember, the FEDs major mandate is price stability; in other words to contain inflation. If the US economy stabilizes and starts to show some strength, the FEDs will be encouraged to consider raising rates. These variables lead me to think that the probability of the dollar strengthening is higher going forward.

If the dollar continues to gain strength the superfluous trades will put downward pressure on commodities. Even though the commodities index has lost approximately 40% of its value since 2nd quarter 2008, there may be another 10-15% decline due to market (systematic) risk. Eventually, fundamental worldwide demand should prevail and commodities should be a great asset to own. As food and energy remains the most basic and necessary consumable goods, the best of breed companies in this sector should outperform the market over the next 2-5 years. **Some examples of exchange traded funds in this area would be Ultra long Oil & Gas Proshares (DIG) and Ultra long Basic materials Proshares (UYM)[2].**

[1] *Source: Charles Schwab & Co.*

[2] ***NOTE: Ultra long / short funds trade with approx. twice the volatility of the underlying index. Not a solicitation.***

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Industrials

The natural progression to commodities would be the advent and use of industrial goods and machinery. If we rewind back to Y2K, we can remember the chaos and anticipation during that time. Most companies were spending significant amounts to ramp up their systems to confront the change from two digits to four. Spending on technology hardware, software and services fueled the market bubble which lasted till the end of first quarter 2000 and then spiraled downwards.

As mentioned above, agriculture products (food) are the basic consumables needed at an accelerating pace as more and more emerging countries increase the per capita income and disposable income. The increasing demand compels the need to augment agriculture productivity in these respective countries. The main ingredients needed to accomplish this would be agriculture related machinery, better seeds and fertilizers and maybe more efficient irrigation systems. Therefore, the long term benefactors of this phenomenon would be companies like Deere & Company (agriculture equipment & machinery), Monsanto (higher yielding seeds), and Potash Inc (fertilizer). **Another way to invest in industrial companies is to use an exchange traded fund in this area known as the Ultra long Industrial Proshares (UXI)[3].**

Fixed Income

We all know that the US Treasury bonds are the safest security in the world as they are backed by the full faith and the credit of the US government. At time of abnormal and heightened uncertainty and risk, investors start to divest risky assets and gravitate towards safer ones. Capital markets have experienced investors selling most asset classes, starting with stocks, preferred stocks, corporate bonds and even municipal bonds to hide under the security of US treasury bonds.

Historically market downturns have experienced the same phenomenon of investors moving out of risky asset classes and moving into treasury securities. During the October 1987 crash, investors moved into 1-3 month treasury notes, even at the expense of selling treasuries going beyond 6 months. In other words; total panic and chaos. In the aftermath of virtually all these instances, money left the short term treasuries in search for higher returns as markets stabilize and uncertainty diminished.

I believe that as the markets start to stabilize, and they will, most assets either parked in the money markets or invested in short term treasuries will start to gravitate into higher yielding securities. A safe way to benefit from this phenomenon repeating would be to consider buying funds that benefit from being long on municipal bonds. Some exchange traded funds which invest in municipal bonds have lost over 25% of their values since the beginning of September primarily due to selling pressures. In addition, these funds are currently paying dividend yields close to 6% (majority yield is both State and Federal tax free).

Some examples of exchange traded funds in the municipal bond area would be Eaton Vance Insured CA Muni BD Fund (EIA) with a current yield of over 6.5% or Nuveen CA Performance Plus Muni Fund (NCP) with a current yield of over 7%[3].

I would emphasize that these directional concepts are configured for growth and should compliment the total portfolio based uniquely on each individual's financial objectives and needs.

[3] *NOTE: Ultra long / short funds trade with approx. twice the volatility of the underlying index. Not a solicitation.*

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