



Market Commentary - January 2012



FTSE 100	5,782	S&P 500	1,316
Resistance	5,809	Gold	\$1,677
Support	5,600	GBP/EUR	1.1954
VIX	18.67%	GBP/USD	1.5559

Introduction:

The FTSE 100 finished 83 points (1.51%) higher during the month of December, with investors being rewarded with their traditional “Santa Claus Rally”. Since then the market has climbed a further 210 points, not totally unexpected given the well-known “January Effect”, which historically sees gains in the first month of the New Year.

Fundamentals:

Companies are in general performing well and the macro picture looks brighter too with US unemployment recovering to a five-year low. In the UK, stocks are cheap on a historical basis. That does not leave investors complacent over the threat of European contagion, however the stock market is a forward looking discounting mechanism and at these levels much is already priced in.

Technical:

Following recent advances, the FTSE 100 is now approaching overbought territory with the upper Bollinger band lying at 5809, the natural level of resistance. However, with the RSI having unwound an overbought position (above 70) and now lying at 58, there could be further to run in this upward leg. The downward sloping 200 day moving average is now starting to flatten and should this start to point upwards, investors will take this as confirmation that we are at the beginning of a new bull market. The 200 day moving average along with the psychological 5600 level should provide support in the near term. That is not to say that macroeconomic events could not bring this market down – with the 5480 level providing some support. However, we believe that any resultant pullbacks could offer good entry points.



Market Commentary (cont)

Seasonality:

Year 2012

2012 is the Year of the Dragon in the Chinese Zodiac. The year of prosperity.

First Quarter

The FTSE All-Share has risen no fewer than 19 of the 25 years between 1990 and 2005, posting an average gain of 4.28%

Market Scenarios:

Bull Case Scenario

Our view on the stock market is rather positive. Despite the macro-economic backdrop, companies are reporting strong earnings and it is acknowledged that stock markets tend to follow changes in EPS, rather than GDP. The seasonal factors are in the bull camp's favour and if a credible solution for the EU/Italian debt situation is found, a relief rally would surely follow. Though corrections are a risk, they can be treated as a buying opportunity.

Neutral Case Scenario

A more pessimistic scenario could see the market drop to the support level of 5,480 which is the lower bollinger band and thereafter trade sideways with the upper range being at 5,809.

Bear Case Scenario

In the bear case scenario in which sovereign debt issues come to the fore, the market could fall back to the 4,950 to 5,450 range and go sideways throughout 2012.





Preferred Investments:

RSA Insurance Group has been selected again as the "Penultimate Profits Prospect" (PPP) in the "Dogs of the Dow" theory. This theory selects the 10 highest yielding stocks in the FT30 and then invests equally in the 5 with the lowest absolute share prices, the PPP (the single stock selection) being the stock with the second lowest share price. RSA is a FTSE 100 company, with a very **attractive dividend yield of 8.58%** (covered 1.1x). The shares are cheap both on a fundamental (7.8x forward p/e multiple) and on a technical level, where the shares are trading at a multi-year low. Investment bank JP Morgan has a 148p 12 month price target, 37% above the 109p share price.



Market Commentary (cont)

Chart Legend:

	20 day moving average	(signifies the short-term direction of the security, prices tend to gyrate around their 20 day m/a)
	50 day moving average	(signifies the medium-term direction of the security)
	200 day moving average	(signifies the long-term direction of the security - whether it is in a bull or bear market)
	bollinger bands	(an indicator that measures 2 standard deviations away from the 20 day m/a)

Technical Analysis Guide:

RSI (relative strength index) - indicates whether a security is overbought (above 70) or oversold (below 30). Also when the RSI moves above 50 that is considered bullish (or vice versa).

ADX (average directional index) - indicates whether a security is in a trend (above 20) or not in a trend (below 20). For trending markets moving averages work best when considering lines of support/resistance. For non-trending markets Bollinger Bands work best (sell at upper band, buy at lower band).

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Index

