

Weekly Commentary

May 31, 2011

The Markets

Starting in July, it may cost you more to wake up in the morning.

Starbucks announced last week that it was raising the price of bagged coffee sold in its cafes by an average of 17%. Interestingly, the rising price of coffee represents the confluence of several macro factors affecting the world today, according to Bloomberg.

First, farm goods are becoming more expensive as the cost of fertilizer is rising and being passed onto consumers.

Second, the developing world from Brazil to Asia is becoming more affluent and one outcome of that is they are more willing to pay up for high-quality goods -- including coffee.

Third, adverse weather conditions are affecting various crops including coffee. In fact, poor weather has helped curtail coffee production and kept global coffee inventories held by exporting nations near a 40-year low.

Overall, as the rising price of coffee suggests, consumer prices are starting to creep up. The Labor Department reported that the Consumer Price Index rose 3.2% for the 12 months ending in April. Does this increase worry the government? Apparently, not yet.

The Federal Reserve, which is charged with keeping inflation under control, prefers to look at what they call the *Core Inflation Rate*. The core rate “strips out volatile food and energy prices,” and it rose only 1.3% for the 12 months ending in April, according to TheStreet.com.

So, if you don't buy food or consume energy, then inflation's not a problem. All who do buy food and consume energy -- please raise your hand!

Data as of 5/27/11	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	-0.2%	5.8%	22.2%	-1.3%	1.1%	0.5%
DJ Global ex US (Foreign Stocks)	0.5	2.0	26.7	-4.7	1.1	4.9
10-year Treasury Note (Yield Only)	3.1	N/A	3.3	3.9	5.1	5.5
Gold (per ounce)	2.8	8.7	26.6	19.1	18.3	18.7
DJ-UBS Commodity Index	1.8	1.8	30.5	-8.6	-1.5	4.5
DJ Equity All REIT TR Index	1.4	11.5	26.6	2.1	3.8	11.4

Notes: S&P 500, DJ Global ex US, Gold, DJ-UBS Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT TR Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.

Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association.

Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly.

N/A means not applicable or not available.

IS THERE A WAY TO PREDICT WHEN THE NEXT RECESSION WILL HIT?

According to economists at the Conference Board, as reported by Bloomberg, “Historically the yield curve has been the first of the leading indicators to signal a turn in the business cycle.” The yield curve is simply a graph showing the interest rate on various government securities from the shortest maturity date to the longest.

Today, we have a rising or “steep” yield curve, which means short-term interest rates are *lower* than longer-term rates. In other words, the graph of these rates slopes upward to the right.

At the short-end of the yield curve, the Federal Reserve is holding the benchmark fed funds interest rate near 0%, while the 10-year Treasury Note yielded 3.06% last week. The “spread” between these two rates, of about 3%, is among the highest in history, according to Bloomberg. When the spread is high, that typically means the economy is growing and there’s no recession in sight.

Conversely, when the yield curve “inverts,” meaning short-term interest rates are *higher* than longer-term interest rates, that’s when you have to watch out for a new recession. Bloomberg reports that an inverted yield curve preceded the past seven recessions by an average lead time of 15 to 16 months.

In the most recent recession, the yield curve inverted in June 2006 and the recession started 18 months later in December 2007.

Of course, no indicator is foolproof and past performance is no guarantee of future results. However, the yield curve is one simple indicator that bears watching and, right now, it suggests the economy should do fine for the foreseeable future.

Weekly Focus – Memorial Day Thought

“Let every nation know, whether it wishes us well or ill, that we shall pay any price, bear any burden, meet any hardship, support any friend, oppose any foe to assure the survival and the success of liberty.” -- *President John F. Kennedy*

Best regards,

* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

* The DJ Global ex US is an unmanaged group of non-U.S. securities designed to reflect the performance of the global equity securities that have readily available prices.

* Gold represents the London afternoon gold price fix as reported by the London Bullion Market Association.

* The DJ Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.

* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.

* The DJ Equity All REIT TR Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.

* The Dow Jones Industrial Average is a price-weighted index of 30 actively traded blue-chip stocks.

* The NASDAQ Composite Index is an unmanaged, market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System.

* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.

* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

* Consult your financial professional before making any investment decision.

* You cannot invest directly in an index.

* Past performance does not guarantee future results.

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