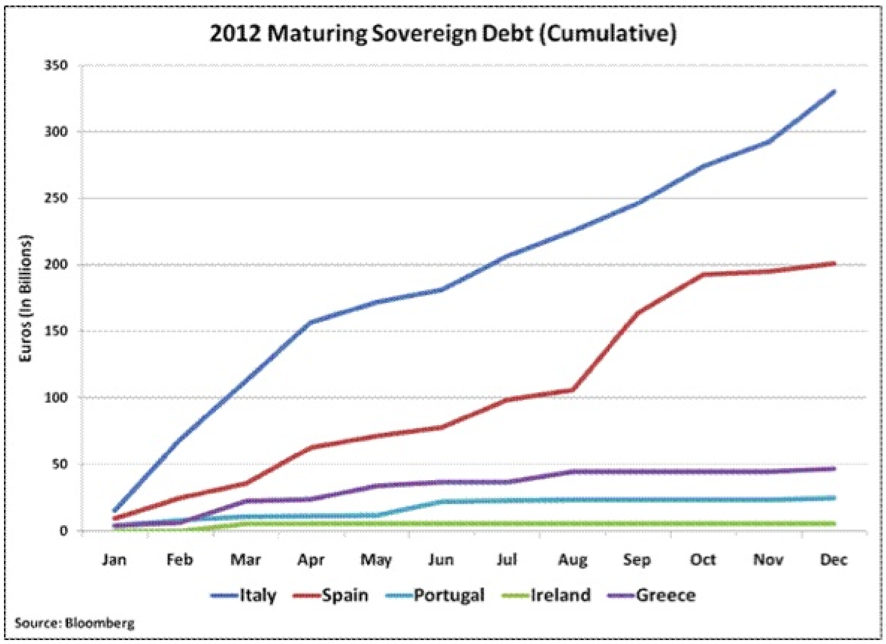
Fusion Flash – Short-Term Outlook

January 24, 2012

The U.S. economy has picked up momentum going into the New Year as indicated by recent job numbers and to date the market has continued its climb upward from the October lows. We continue to err on the side of caution and are confident this approach will be rewarded in time. It is likely the consensus which has driven the market higher is underestimating the magnitude of the shock from Europe which will likely rear its head again in February and March. The key item we will be watching closely is how successful countries in Europe are at rolling over maturing debt. The chart below shows the large amount of debt that must be refinanced.



Note that Italy has to rollover $150 billion euros by April, with a large portion of that coming due in February and March. It is important to recognize that Italy is the third largest bond market in the world compared to the relative small amount to be dealt with in Greece. Thus what happens in Italy in the coming months will be critical to what trajectory the stock market takes in our view.

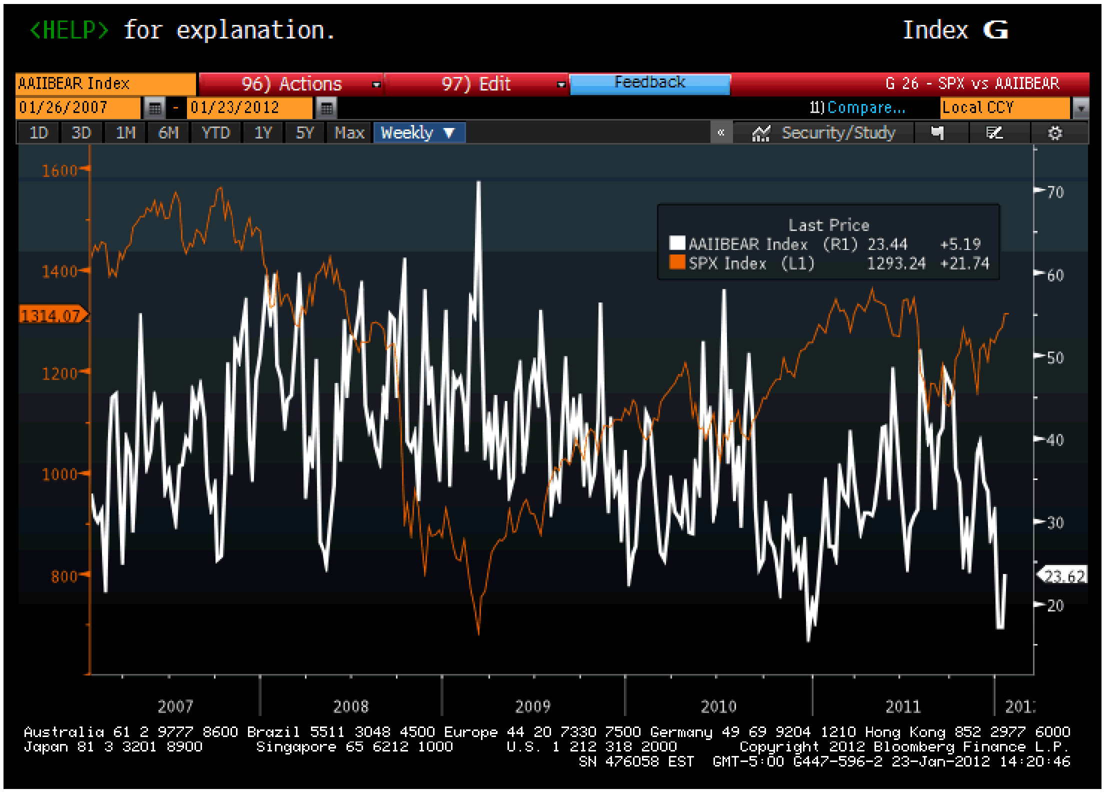
Our behavioral analysis which looks at both Market Sentiment and Technical Analysis has moved into negative territory showing a higher probability of a market selloff in the coming weeks. We continued to be positioned conservatively in our *Tactical Equity Strategy* with 36% in cash (an increase of 7% since the end of the year as we exited the U.S. Industrial Sector) and a very low exposure to Europe. While January is off to its best start since 1987 as measured by the S&P 500, the next likely move in global equity markets is down. In the event the market does move higher in the coming weeks we will look to further increase cash levels as our longer term outlook remains cautious.

The market appears to be reaching near-term resistance levels and a correction is likely in the coming weeks. In the intermediate-term we continue to have many concerns and will react to ongoing macro issues as events unfold.

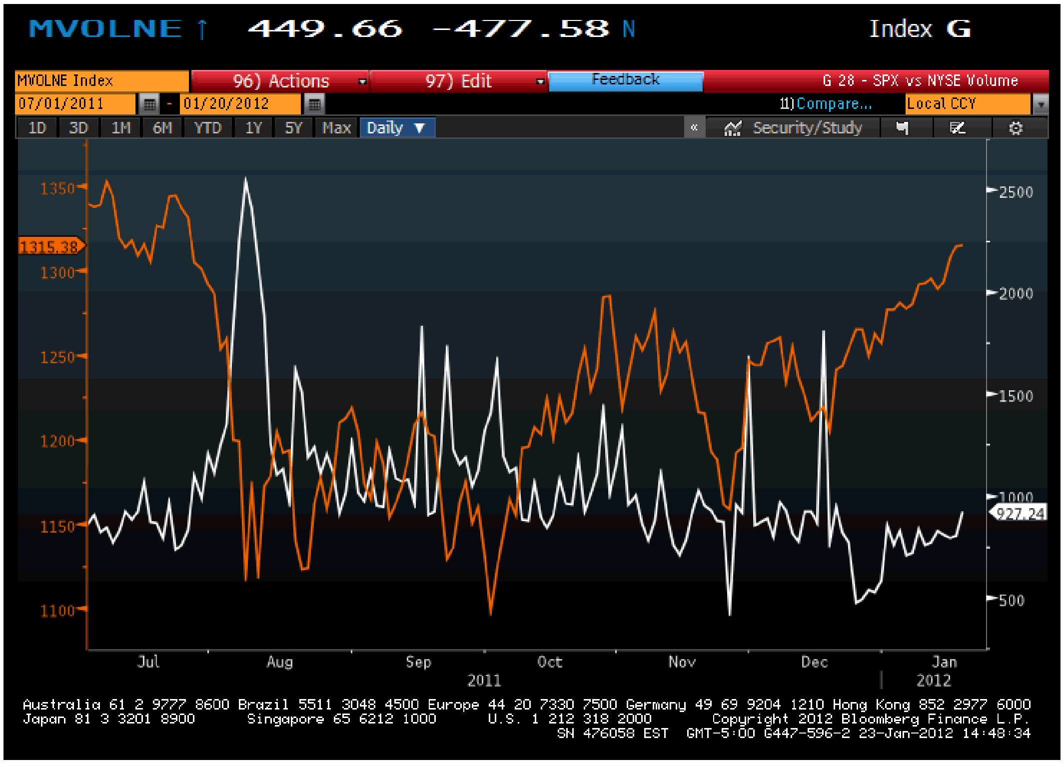
Market Sentiment Readings:

American Association of Individual Investors Bear Index - has decreased significantly since early December showing a lower level of bears among individual investors at 23. This shows that complacency is beginning to take a foothold as the market rally appears to be in its later stages.

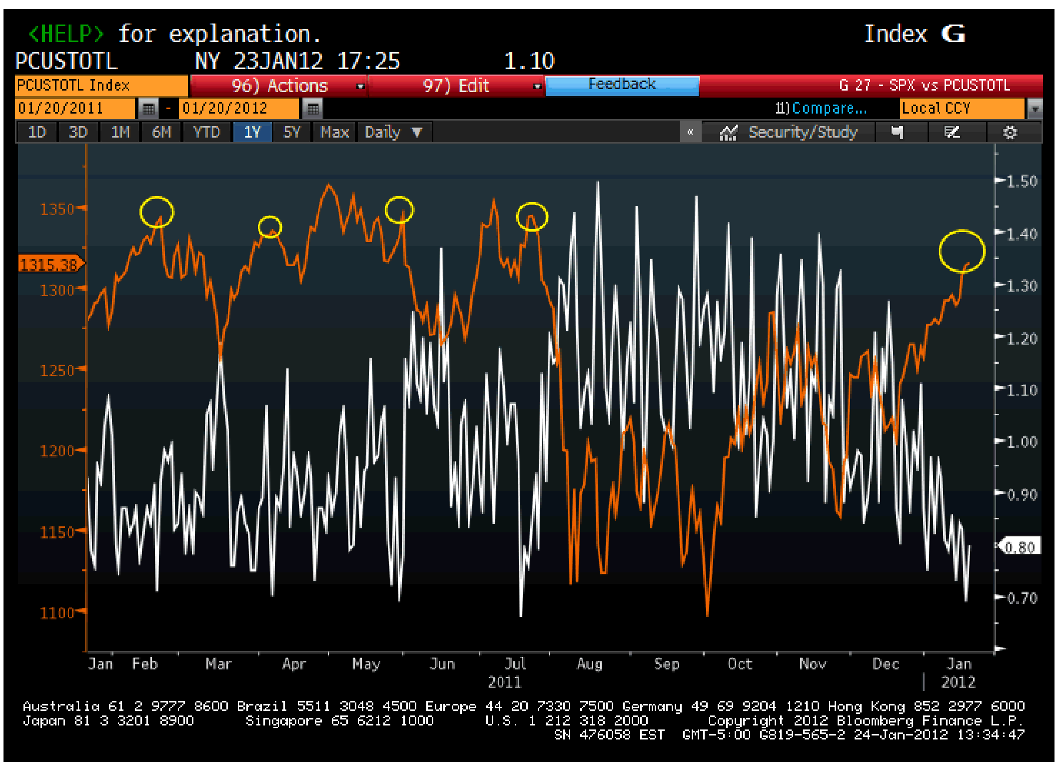
The chart below is updated through January 19th and compares the AAII Bear Index versus the S&P 500. Note the white line showing large drop from the Sept/Oct highs to last week's low reading. When this has occurred in the past it was generally indicative of a market in the topping process.



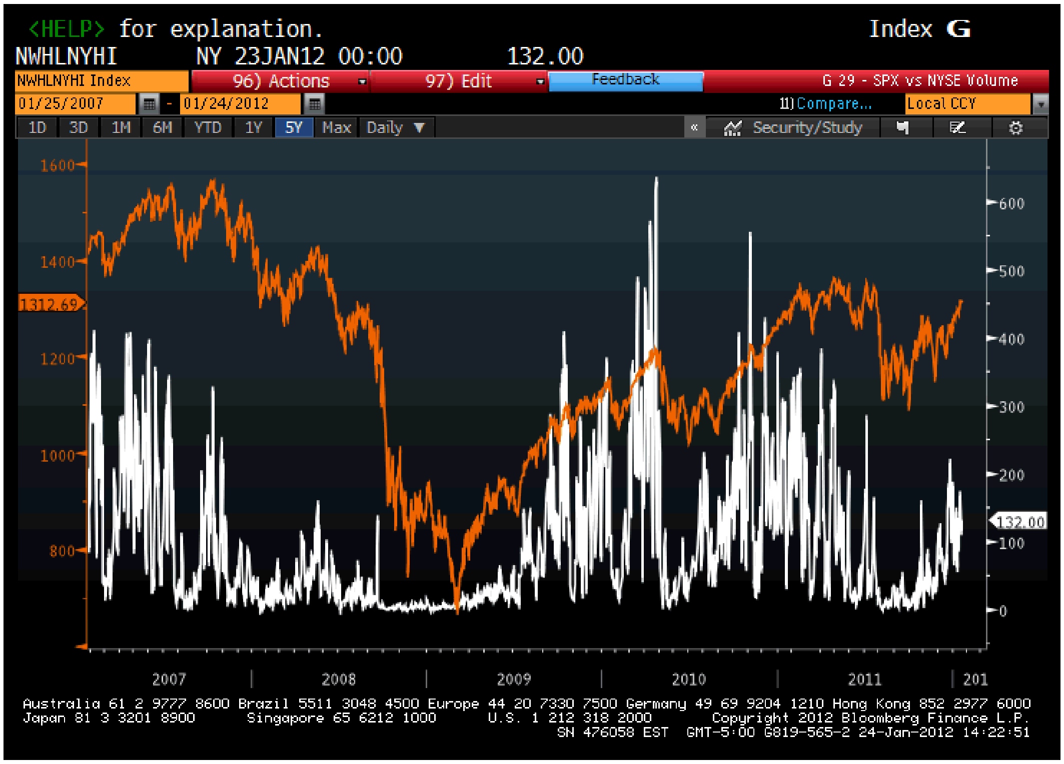
NYSE Volume - The chart below shows volume on the NYSE (white line) vs. S&P 500 price levels. Volume has been below average so far this month causing us to question the strength of the current rally. Generally a sustainable move to the upside takes place on higher volume. This should be watched closely for an indication of the strength or weakness of the market direction in the coming weeks.



Put/Call Total Equity Index - The chart below compares the Put/Call Total Equity Ratio versus the S&P 500. Note the white line representing the Put/Call Ratio has dropped to one of its lowest readings over the past year at .70 which has coincided with sharp pullbacks in 2011. Readings near this level are denoted by the yellow circles and show an increased likelihood of a market selloff in the coming weeks.



<u>Number of NYSE stocks reaching new 52-week highs</u> - increased into the end of the year and has pulled slightly back in January. Overall this reading has a positive bent showing that more stocks are above their recent highs, but when contrasted with below average volume we score this as a neutral indicator at this time.



Technical Analysis:

The S&P 500 has passed through heavy resistance levels at its 200 day moving average (the yellow line in the chart below). We were incorrect in our outlook that the market would pullback at this level. The next area of resistance in our view is the market highs from back in July 2011 around the 1340 level. This is likely the upper end of the trading range and the probability is high this will act as heavy resistance for the foreseeable future.

In summary, our analysis of sentiment indicators and technical analysis points to a market that will likely begin a downward move in the coming weeks.

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