First Trust

Quarterly Market Overview

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Mr. Carey has nearly a quarter century of experience as an Equity and Fixed-Income Analyst and is a recipient of the Chartered Financial Analyst (CFA) designation. He is a graduate of the University of Illinois at Champaign-Urbana with a B.S. in Physics. He is also a member of the CFA Society of Chicago and the CFA Institute. As CIO, Bob and his staff supervise over $48 billion in assets.

Mr. Carey has appeared throughout the United States and Canada as a guest on television and radio programs. These programs include: Bloomberg TV, CNBC and Canada's Business News Network and on Chicago's WBBM Newsradio 780's Noon Business Hour. He has been quoted by several publications, including *The Wall Street Journal, The Wall Street Reporter, Bloomberg News Service, and Registered Rep.*

Manufacturing still plays a critical role in the U.S. economy

On January 21, 2011, President Obama proclaimed the following: "We're going back to Thomas Edison's principles. We're going to build and invent stuff," according to IndustryWeek.com. He noted that for America to stay competitive globally, we need to export more goods. He vowed to double exports over the next five years; an interesting turnabout considering President Obama's perceived disdain for Corporate America. His differences with the Chamber of Commerce, for example, are well documented. Whether he is simply observant enough to want to leverage all of the momentum being built in the U.S. manufacturing sector (see charts below) or is playing politics in an effort to seem amiable in the face of persistent high unemployment – only time will tell. After all, the 2012 election is looming and the manufacturing sector is hiring.

But guess what? U.S. manufacturers cannot find enough skilled workers to meet demand, according to a recent article from Reuters. Some CEOs are having to recruit employees from abroad. Factory jobs account for about 9% of overall employment in the U.S. Due to the evolution of cutting-edge technologies, manufacturing has become a highly skilled and specialized industry. A high school diploma isn't enough to secure a job these days.

Despite the shallow talent pool, the manufacturing sector is leading the U.S. economy for the first time since the 1970s and companies in this space are "lean and mean," according to a *Kiplinger's* interview with James Paulsen, economist and chief investment strategist at Wells Capital Management. The U.S. is still the world's largest manufacturer, producing 21% of all goods – the same share it held 30 years ago, according to the National Association of Manufacturers. Industrials and materials are two sectors that Paulsen believes should be owned heading into the second half of 2011.

Three facts about U.S. manufacturing **(Source: NAM.org)...**

– U.S. produces 21% of global manufactured products, followed by China at 15% and Japan at 12%.

– Workers in U.S. plants and factories are twice as productive as those workers in the next 10 leading manufacturing economies.

– U.S. manufacturing produces $1.6 trillion of value on an annual basis. On its own, it would be the 9th largest economy in the world.

A look at how Industrials are performing **(Source: Bloomberg)...**

– S&P Industrials Index was the second best performing major sector in 2010, up 26.7%. The S&P 500 was up 15.1%.

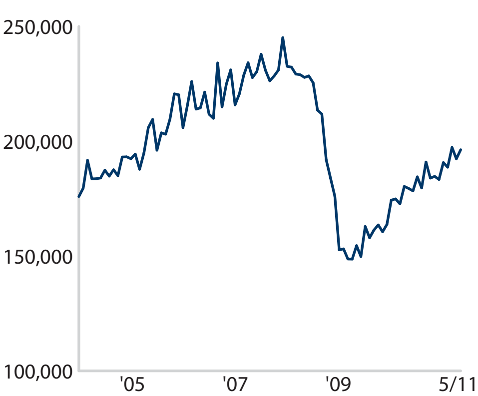
– S&P Industrials Index has been the sixth best performer so far in 2011 (thru 7/15), up 4.8%. The S&P 500 was up 4.7%.

– Industrials sold off on profit taking in Q2. The soft patch in some economic data spooked investors. The S&P Industrials Index was the second best performer in Q1, up 8.2%. The S&P 500 was up 5.4%.

– Dallas Federal Reserve President Richard Fisher stated on June 28 that he expects second-half U.S. economic growth to be "much stronger than the first half," according to Dow Jones Newswires.

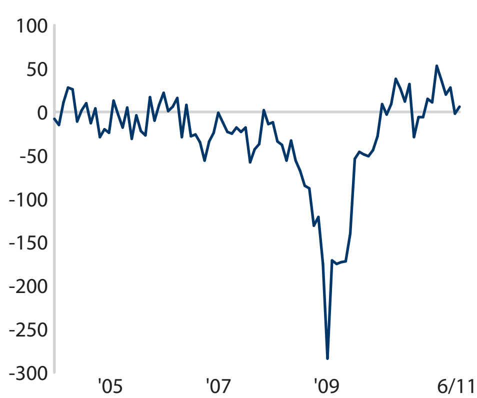
– The estimated 2011 earnings growth rate for the S&P Industrials Index is 14.7%, compared to 17.3% for the S&P 500 (which benefits from a 40.0% pop in Energy), according to Standard & Poor's. For 2012, the edge goes to Industrials with an expected growth rate of 18.4%, compared to 14.9% for the S&P 500. The P/E on the S&P Industrials Index is 12.62, based on the 2012 earnings estimate.

New Orders for Durable Goods ($ millions)



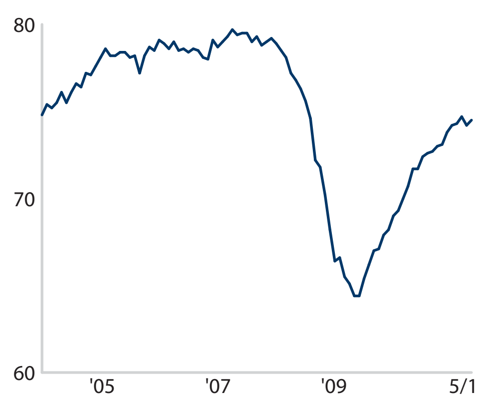
Source: Haver

Manufacturing Employment (thousands)



Source: Haver

Manufacturing Utilization (%)



Source: Haver

Cloudy with a chance for Gains

This ain't your father's Internet trade...

Think of the cloud as a natural extension of the Internet. While it has a certain buzz about it, we would not put the level of euphoria even close to what was experienced back in the late 1990s. And that is a good thing. It is still the case that cloud computing companies will carry higher betas than the broader market, but investors should know they are real companies with real earnings. What ruined the Internet revolution for most investors was that the story was simply not advanced enough to catch up to the hype. That is why we were told back then that in the new Internet paradigm ideas would be worth more than profits and brick-and-mortar businesses would die. But we have since learned that the foundation, or backbone, of the Internet was very real. Many of the businesses and technological advances that were touted back then have delivered, particularly 3G (now 4G) wireless, high-speed broadband, data storage and e-commerce.

Those investors who stayed invested in their Internet stocks after the bubble burst on March 24, 2000, through the end of the bear market on October 9, 2002, enjoyed a significant rebound. The Dow Jones Composite Internet Index posted a cumulative total return of 505.65% from 9/30/02-6/30/11 (105 months), or an annualized return of 22.84%. The S&P 500 posted a cumulative gain of 92.68%, or an annualized return of 7.78%.

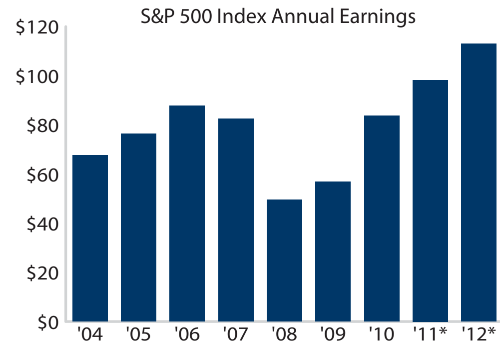
Cloud computing is just beginning. It will take some time for companies, especially those with established IT departments, to embrace the notion of outsourcing some or all of their IT tasks. Among today's cloud users, spending on cloud services is just 33% of the total IT budget, according to a recent survey by CDW. While the argument has been put forth that it will be easier to secure data via the cloud, the potential cost savings are the real hook, particularly for small and medium-sized companies. CDW notes that only 28% of the 1,200 IT professionals it surveyed are actively implementing a cloud computing service. IDC expects spending on cloud services to be more than five times greater than traditional IT outlays through 2014.

Cloud Spending

Forrester Research expects annual spending by companies on cloud computing to grow to $227 billion by 2020, up from approximately $18.6 billion in 2010. A lot of the spending will happen over the next 3-5 years. Bank of America Merrill Lynch estimates that companies will spend $117 billion over that span. In 2010, 124 million adults in the U.S. used at least two devices to connect to the Internet, and that number is expected to grow to 184 million by 2016, according to Forrester.

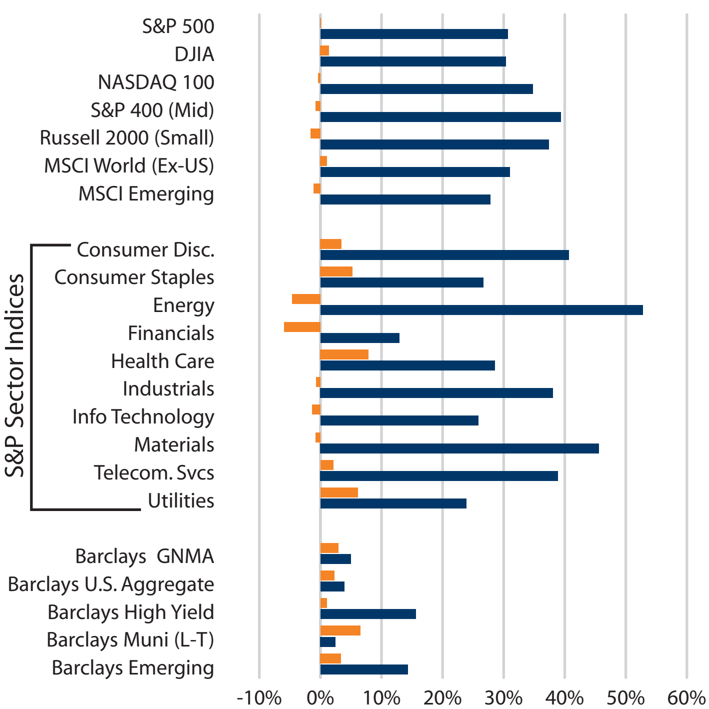
A brief commentary on Earnings

As the chart to the right indicates, the $98.39 in estimated earnings for the S&P 500 in 2011 will easily eclipse the $87.72 in actual earnings posted in 2006 – prior to the subprime meltdown. The fact of the matter is that earnings, until just recently (soft patch), have been ratcheted higher by analysts with each passing quarter. The earnings beat rate, or positive surprises, for the companies in the S&P 500 was 67. 8% in Q1'11 and 67.7% in Q4'10, according to data from Bloomberg. Final earnings topped analysts' expectations by an average of 6.3% over the past 3-4 quarters, according to Standard & Poor's. The upside to higher unemployment is that companies often become lean and mean. Despite increasing outlays on buybacks and dividends, the cash and equivalent levels for the nonfinancial companies in the S&P 500, referred to as S&P Industrials (Old), rose from $940.1 billion to a record $1.1 trillion in Q1'11, according to S&P. Cash holdings stood at $654.6 billion in 2008. The story gets even better. While earnings have been strengthening, P/E ratios have not expanded. The trailing 12-month P/E on the S&P 500 stood at 14.76 on 7/15/11. The historical average is closer to 16.



*Estimated
Source: Standard & Poor's

Total returns for *Q2* and past **12 months** (6/30/11)



A Look Ahead:

The outlook for earnings (year-over-year comparison in $)...

	Q3'11E	Q3'10A	**Q4'11E**	Q4'10A	**2011E**	2010A
Financials	**4.29**	3.92	**4.69**	3.43	**16.68**	14.82
Information Technology	**7.77**	6.70	**9.13**	7.90	**31.29**	26.25
Health Care	**8.32**	7.44	**8.21**	7.15	**32.48**	28.90
Consumer Staples	**5.59**	5.01	**5.76**	5.26	**21.57**	19.45
Consumer Discretionary	**5.04**	4.43	**5.63**	5.05	**20.26**	18.20
Industrials	**5.48**	4.85	**5.78**	5.24	**21.08**	18.41
Telecom. Services	**1.98**	1.84	**1.95**	1.63	**7.83**	7.36
Energy	**12.82**	8.39	**12.81**	9.10	**49.15**	35.21
Utilities	**4.20**	4.11	**2.47**	2.16	**12.57**	12.34
Materials	**4.39**	3.25	**4.09**	3.42	**18.62**	13.33
S&P 500 Index	**25.32**	21.56	**26.40**	21.93	**98.39**	83.77
S&P 400 Index (Mid-Cap)	**14.58**	11.82	**15.53**	11.94	**53.49**	43.92
S&P 600 Index (Small-Cap)	**6.07**	4.86	**6.49**	4.40	**22.85**	17.00

Source: Standard & Poor's (7/6/11)