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Income On Demand

Positive News From the Real Estate Sector!

Plus, the latest on your red-hot portfolio…

Ever since the financial crisis kicked up its heels, I've been saying that one of the big drivers of a solid, sustainable recovery — in the economy and the stock market — will be an improvement in the real estate sector. And while the latest news from the sector doesn't make me do back flips around my office, there certainly are some tasty tidbits.

I'm looking for positive moves in real estate for a simple reason: With improvement in the sector come increased sales and stabilized prices. That, in turn, should put a fire under new lending.

After all, with good sales and reliable prices, homebuyers know what they're buying won't shrink in value overnight. And lenders know the cash they're lending will most likely find its way back to the bank.

But before I get into a few positive real estate-related data points, let's be frank: Even when the real estate market recovers — and it will recover — we're certainly not going to see the kind of pricing frenzy that sparked one of the biggest asset bubbles of all time. Those days are long gone.

In my book, good riddance. Because I've been around the block enough times to know that one of the market characteristics that really worries experienced investors is too much froth in a market. It hides flaws, makes everyone look like a genius and clouds accurate price discovery.

The fact is the real estate bubble was fueled by legions of underqualified borrowers meeting equal numbers of highly motivated lenders with loads of cash and downright lousy lending standards. Throw in a secondary market that was eating up the repackaged, poorly underwritten loans like there was no tomorrow, and it's no wonder the shell game came crashing down.

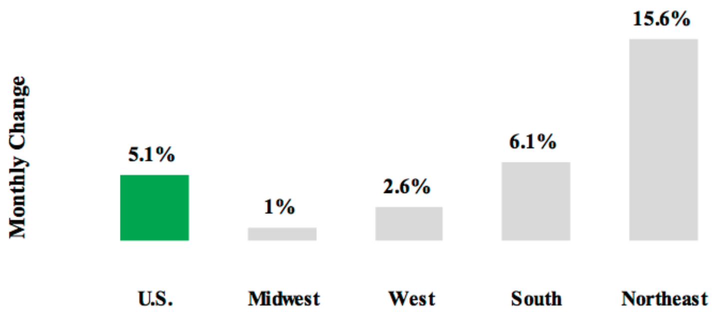
So when the real estate market recovers, you can bet the price action of just a few years ago won't be the norm. No, we'll have to be happy with simple, solid appreciation in the sector.

And while banks have short memories, they aren't that short. So the cash driving the industry — even when back in full swing — won't be sloshing around as much as we saw before this whole mess started.

Rather, the recovery in real estate will begin with baby steps: Small moves in the right direction. And the latest news is just that. Take a look at this chart.

As you can see, this chart, existing home sales in February jumped to the upside compared with January. In fact, home sales were up 2.6% in the West, 6.1% in the South and a whopping 15.6% in the Northeast. All told, existing home sales in the United States increased a solid 5.1%!

Existing Home Sales Jump in February!



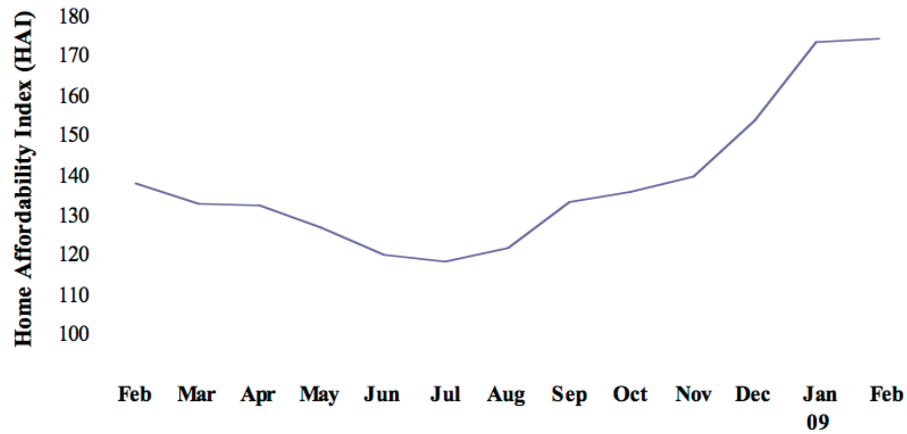
Data source: National Association of Realtors

Over Please…

The news gets better. Sales comparisons with the same period last year — which tend to be less volatile than month-over-month numbers — show some huge bright spots. In fact, while overall home sales in the United States were down 4.6% in February compared with last year, sales in the West were up a stunning 30.4%.

That's right, February home sales in the West — a region that includes the super-important Southern California and Las Vegas real estate markets — *rose nearly a third compared with last year*. Plus, it marked the *eighth straight month* of year-over-year increases for the region.

Home Affordability Rising Fast!



Data source: National Association of Realtors

But that's not all: With the real estate market in the West generating a whopping 1.2 million units in annualized sales, sales activity is now a staggering 38% above its cyclical low point of 870,000 units marked in October 2007.

That means — from a sales angle — a market bottom in this key real estate region is way, way in… and has been for months.

But that's not all: Take a look at the chart above and how home affordability is skyrocketing…

As you can see from this graph of the National Association of Realtors' Housing Affordability Index (HAI), affordability is rising fast. In fact, at a current level of 173, home affordability is now 26% easier than last year's 137 level.

So what does a HAI level of 173 really mean? It's pretty straightforward. An index level of 100 means that the typical family earning the median income in the United States has exactly enough income to qualify for the average mortgage. So with the HAI at a whopping 173, the average U.S. family has 173% of the income necessary to buy an average home. Talk about buying power!

But don't forget — affordability is a double-edged sword: Its natural rise is driven by lower home prices. And while price drops are excellent ways of clearing markets and getting people to buy, you want declines to begin to moderate, eventually stop and then give way to reasonable price appreciation.

So far, that's simply not happening.

As is painfully clear by the Home Price Index chart, U.S. home prices continue to tumble. In fact, according to S&P/Case-Shiller home data through January 2009, 13 of 20 metro areas across the United States booked *record rates of decline*. All told, the 20-city composite benchmark index fell a whopping 19% compared with a year ago. Ouch!

The simple truth is this chart needs to get better before the real estate market can really get on the road to recovery.

Bottom line: Real estate got us into this mess, and it will get us out. And so far, there's some solid positive data points, from both sales and affordability standpoints. But home prices are falling. And while that's a plus for buyers and sales activity in the short run, prices will need to stabilize for the sector — and the economy —

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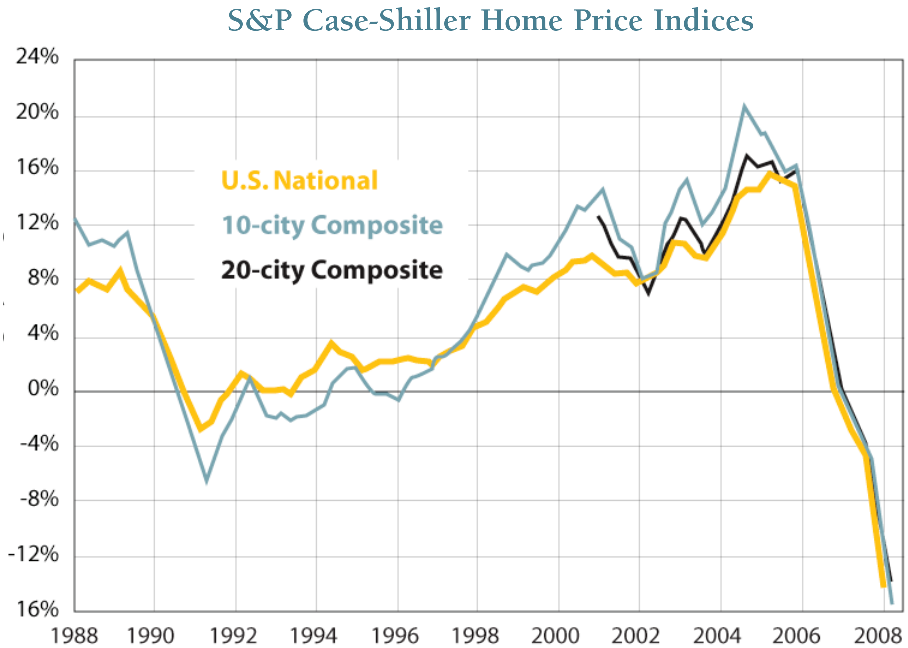


to show any real staying power.

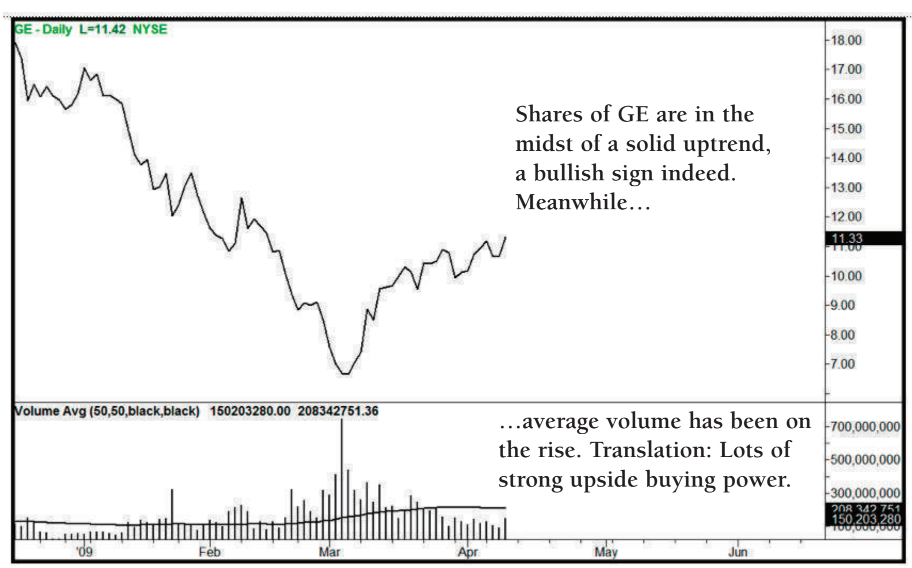
So that's the macro picture. Now it's time to focus on our covered call plays.

The Latest on Your Portfolio

Let's begin with a chart of **General Electric**…

As you can see from the daily chart below, shares of the industrial giant have been on an absolute tear since March.

In fact, from a low of $5.73 on March 4 to a recent high of $11.63 on April 9, the stock has shot up a mind-blowing 103%. That translates to a stunning $5.90 a share!



From a technical standpoint, the shares have blown through near-term resistance at $11.35, which, by the way, was just a penny above our break-even level of $11.34.

Now the stock has a clear shot at $12.90, the next resistance level. From there, it should be clear sailing all the way to $17 and change. That should take us easily above our $15 strike price and straight into maximum profit territory. And since these calls don't expire until June, we have plenty of breathing room as well.

But at the same time, keep in mind we'll probably see a pullback in the days ahead. The stock has run fast and hard, so it only makes sense that it will take a break.

Besides, it's a good idea for GE to take a breather every now and then. Traders in for just the short haul can cash out and make room for longer-term investors. Meanwhile, those looking for a way into the stock get the shares at a small discount. So a dip in price is a good thing… and I'm still feeling great about this play.

The same is also true for our **IBM** play.

IBM's Solid Outlook

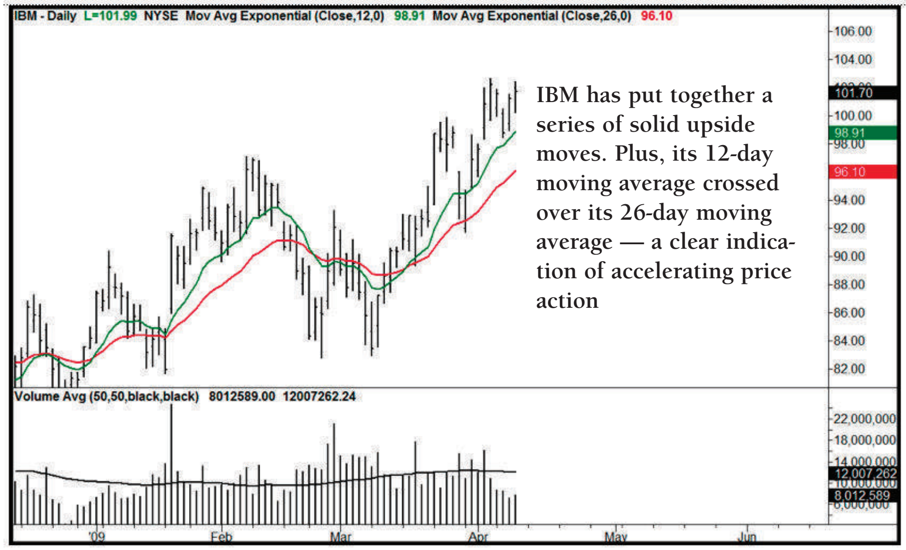
Take a look at the chart of IBM's recent price action on the following page.

First off, notice the nice upside run that IBM shares have put together. By itself, that's solid bullish action.

Now notice something even better: The shares' 12-day moving price average — shown on the chart in green — crossed its 26-day moving average — the red line on the chart — during the middle of last month. Since then, the gap between these two averages has been getting bigger and bigger.

Significant? No doubt about it. Since the moving average line with fewer days is above the moving average line with more days, the stock price is accelerating. And that means it's not just going higher… it's also going higher at a faster rate — a one-two upside punch.

Continued…



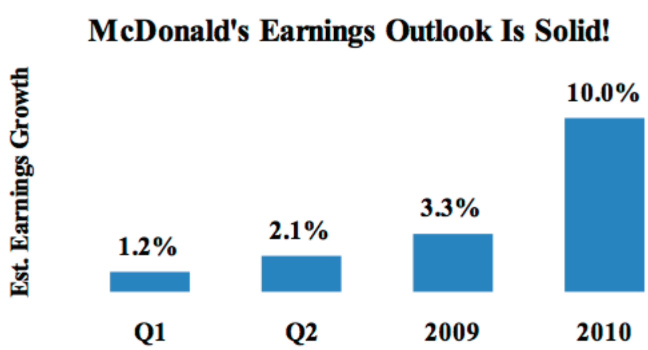
With IBM shares recently trading at $102, this covered call trade is already above our strike price of $100 and firmly in maximum profit territory. All we have to do now is sit back and relax until expiration in July.

But that's not all… **McDonald's** is looking great too!

Great Results for the Golden Arches

I almost fell out of my chair when I took a gander at the latest earnings estimates for restaurant icon McDonald's…

During the first quarter, estimates are calling for



McDonald's to book earnings per share of 82 cents. That's up 1% from last year's 81 cents and shows that this stellar restaurant operator can crank the bottom line even in the most hostile economic environments.

The news gets better. During the second quarter, estimates are calling for a 2% pop in McDonald's earnings, which improve to 3.3% for the year. Then in 2010, we should see a solid 10% increase in the company's bottom line.

With this kind of stellar outlook, it's no wonder our McDonald's covered call play has already met its maximum profit target. All we have to do now is wait for the stock to be called away at $55 a share in June.

Bottom line: From head to toe, your portfolio is in great shape. Both IBM and McDonald's covered call trades are in maximum profit territory, and GE has cleared its break-even level.

In fact, things are working out so well I think it's time to hold off on a recommendation for this month and just work the trades we already have. That also helps us minimize our risk going forward.

Meanwhile, when it comes to the real estate sector, we're far from out of the woods. But recent sales and affordability data points are certainly a step in the right direction. But as I've said before, *tumbling prices need to stabilize* before sustainable progress can be made.

Best wishes,

Wayne Burritt

Editor, ***Income on Demand***