August 17, 2007

7:16 AM EDT

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I really wanted to use the Mr. Toad's Wild Ride subject again since it's so appropriate, but that wouldn't have been original. So instead, I chose a more aptly titled email where I get to eat some of my previous words later in this email.

Eating crow & the projected path

In my last update earlier this week, I discussed a slew of reasons why last Friday's low should hold and we should see a 2-5% rally before another wave of selling hits. Wasn't I right? It did hold, for all of ONE day! That wasn't one of my better calls, but in the grand scheme of things, it wasn't too awful.

But I will say this. If I had to do it all over again, I would make the same statement and react the same way. In the 20 years of research I looked at, that condition held more than 90% of the time with two of the exceptions being October 2000 and August 1998.

Since the former was in the throes of a secular bear market, I can't find many comparisons. The latter has a number of similarities to today like the complete collapse in the credit markets. During that period, the low that was supposed to hold, like last Friday, gave way to a mini crash during the last week of August.

We somewhat saw that mini crash Tuesday through Thursday of this week!

After that collapse, stocks rallied very hard into mid September before rolling over to new lows during the Long Term Capital debacle. Right now, the odds favor a similar path and I do believe we will see at least one major hedge fund, if not two, follow LTCM out of business.

Let's not get ahead of ourselves yet. We'll have plenty of time to discuss all possible scenarios over the coming weeks.

Getting back to my comments from a few days ago, there was so much evidence of an important low being established that we exited our negative positions, locking in another round of nice profits since we began trading the downside at Dow 14,000, about 1200 points ago!

While the market was busy collapsing in July, our Diversified Growth strategy banged out an eye popping gain of more than 4%. Yes, you read that right. It was a PLUS month! It's nice to be able to bank a 10% out performance spread with the market in a short period of time. Talk about a cushion!

Anyway, earlier this week, we saw the major indexes close below last Friday's low and that was the point I knew I was wrong for that set up. Thankfully, with our IT model still negative since Dow 14,000, we did have any positions on to stop out of.

That may all change today or in the coming days. Should we be able to take trades on the long side, I will have some very tight stops to preserve our gains and guard against the very unlikely scenario of another wave of selling right here.

Was it THE bottom

I don't want to spend any time now discussing the plethora of short-term indicators screaming buy, but they are numerous. Stocks are supposed to rally here, across the board.

We got our high volume reversal. We got our rumor mill of secret Fed action with a possible bankruptcy in Countrywide. We got talk of Congress loosening Fannie Mae rules. We got the big funds liquidating anything and everything. It's a lot like August 1998.

And the hedge I mentioned a few issues ago, buying the Japanese Yen, saw its largest one day gain since 1998. In fact, the Yen is up roughly 6% since I wrote about it. And for full disclosure, I exited 100% of it on Thursday.

I spent a lot of time last night going through every major index, sector and country in my universe to identify some of the better opportunities. Usually, I can isolate a few "gems", but right here, most look very similar.

Should the market stage a rally, and once again, that's what I think, I like the Nasdaq 100 as my index with Semiconductors and Telecom as my sectors along the Emerging Markets. For the real risk takers, South Korea looks appealing.

The key now is not finding which security will make the most money; it's managing your downside risk and stopping out with small losses. This is not the time to be a hero!

Thursday looked like a pretty good washout with the dire news backdrop and the exacerbation from monthly options expiration. Next week is supposed to be a strong one for the stock market.

Communication is the key right now

I often find that most financial advisers don't answer their phone or return calls or emails when markets collapse. This is when clients want their hands held. What an idiotic way to conduct business! If you are an adviser or use one, there should be a constant stream of communication, especially now.

While we have done extremely well in this environment, there have been some challenging times earlier this year and during the third quarter of 2006. My level of contact increased 100% then, even though I had to endure a few irate clients calling me some nasty names. It happens.

Make sure you are comfortable with the adviser you are using or pulling the trigger yourself right now. It's no great feat to have made money from March to June. This is the time that tests everyone's mettle. You can certainly contact me directly with any questions or comments, whether or not you are a client.

And finally, clients and prospects always ask me when to act. This period may be the single best opportunity since the bull market began in 2002 to add money to your account or open a new strategy. I URGE you. I IMPLORE you. Do it NOW! PLEASE! Don't

wait like your friends and neighbors for the market to rally sharply before taking action!

The most successful investors are the ones who act now, in the face of turbulent markets and doom and gloom headlines!

Procrastination = Mediocrity

Additional Update

2:12 PM EDT

Just as I was about to hit send this morning, the Fed cut the discount rate 1/2% and the indexes went wild. THIS WAS NOT A RATE CUT!

Rather, it was more of a psychological move by Bernanke to let the markets know they will step in the save the day, if necessary. The discount window is only used by institutions putting up collateral for their loans. The Fed essentially said that they will extend the lending period and allow riskier assets to be put up as collateral.

Most people are viewing this move as a precursor to a rate cut on September 18, the next scheduled Fed meeting.

As expected, the stock market rallied smartly, but I believe it was going to anyway based on the number of indicators flashing buy after yesterday's turnaround. The Fed's move just quickened the upside.

Not much changed in our strategies, except we did some rebalancing in our sector program and added longs in Developed and Emerging Markets. It will be more interesting to see what shakes out next week with very little earnings and economic news.

I would not be surprised to see volatility come way down and a return to semi normalcy.

Have a safe and enjoyable weekend!

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