February 10, 2010

10:19PM EST

Inside this issue

Don't Get Squashed by an Elephant

I've received several questions regarding 1099s and other tax related documents. The Internal Revenue Service (IRS) has changed the yearly 1099 Tax Reporting Statement mailing deadline from January 31 to February 15, as mandated under the Emergency Economic Stabilization Act, signed into law October 3, 2008.

The vast majority of 1099s will be mailed by the 15th, so you can expect to receive them by the 26th. You can also expect to receive a gain/loss worksheet, where applicable. If you do NOT receive the proper tax documents by the end of the month for your taxable account, please contact the office.

Much ado about nothing... That's what I said the night before the big storm was supposed to hit Connecticut this week. 10-20 inches forecasted. 4-5 inches on the ground. It seems like EVERY TIME forecasters call for the storm of the century here, all we get is a whimper. It's the next storm that usually is the whopper, which could come through over the weekend. Is it too much to ask for these nor'easters to miss the big cities and bomb Vermont??? I mean, what good does 3 feet of snow do for Philly? But in Vermont, it's pure heaven for us skiers!!

This morning I decided to leave 30 minutes early for the usual 45 ride to Stamford to do CNBC, planning for all that bad weather. Happily, it only took 45 minutes and my **Squawk Box segment** went off without a hitch. And I stand by my comments during the interview and in every other TV and newsletter opinion that public stimulus, running the printing presses and government bailouts have never, ever led to real recoveries. Economists love to disagree, but they never seem to offer anything factual.

The hallmark of lasting recoveries is private money and investment along with a surge in entrepreneurship. This is usually coupled with tax credits or incentives for small business to invest and hire. The Bush and Obama administrations may have printed trillions of dollars, bailed out Bear, Fannie, Freddie, AIG, GM, GMAC and Chrysler, passed two stimulus packages and infused the major banks with hundreds of billions, but it won't work long-term.

Unless we get the private sector engaged and moving, the nascent recovery will come screeching to a halt as Bernanke & Company are just beginning to remove the punch bowl from the party by ending their trillion plus dollar purchase of mortgage backed securities. Effectively, this has been like letting an elephant sit on top of mortgage rates. What do you think will happen when that elephant stands up and moves somewhere else?

Bottoming Process Continues Building

~~~~~~

The stock market continues to build a bottom to launch another leg higher during the second quarter. As I mentioned last week, the most volatility and largest declines are often seen right before the low, so further weakness this month cannot and should not be ruled out. But price is much closer to the end than the beginning. I won't be surprised if Dow 9800 is revisited or even breached, although that should be the final bout of selling and maybe the perfect buy point.

At this point there is plenty of technical and sentiment evidence to support the bottoming process, such as the usually wrong, mom and pop option traders, various sentiment surveys showing a dramatic shift to bears and short-term mutual fund traders running away from risk. Additionally, last week's decline showed a small slowing of downside momentum that usually presages the final low.

What bothers me is that the investment grade corporate bond market, which peaked in September, is in danger of making lower lows, turning the trend to down. The riskier junk bond market, which assumed a leadership role for all of 2009 and made a new high in early January, has collapsed in recent weeks.

Couple the bond market problems with the fact that most sectors I follow have rolled over to the downside, the stock market certainly has the smell of living on borrowed time. That fits in with my theme that the next rally, as large as it may be, should be the final one before a much more significant correction sets in later in 2010. The sector behavior is important because the more sectors that are healthy, the longer a
~~~~~~

rally can last. Key leadership is vital and unless something changes dramatically, I just don't see where it will come from without a full fledged correction.

The Geithner Countdown

~~~~~~

It's been no secret that I am not fan of Treasury Secretary Tim Geithner. Long time readers remember that I assigned a lot of blame for the collapse of Wall Street on Mr. Geithner when he headed the New York Fed. What I thought was unfathomable was how President Obama could possibly promote this man to a higher office when he basically let Wall Street explode with toxic assets and leverage, and then implode to the detriment of Main Street.

I said I would be shocked if he lasted four years and now it will be interesting to see if he even makes it two years. That was on my on list of **Shockers 2010**. Maybe Goldman Sachs hires him as a "thank you" for the tens of billions he helped them make as a result of the crisis? That would certainly be a shocker! And reverse the trend of former Goldman folks into powerful positions in the government.

I remember when the AIG bailout was being discussed and all of the moving parts involved. Bernanke, Paulson, Geithner, Blankfein, etc. Although I was in favor of saving AIG at the time, given the facts presented, I will clearly and definitely state that if I knew then, what I know now, AIG should have been left to fail.

The financial system and economy would have taken a tremendous blow, but one year later, we would have been on the road to a real and sustainable recovery, not this government sponsored, public rescue of the biggest institutions held together with duct tape and paper clips, much to the detriment of small business. With all good intentions, the Bush administration made a mistake in how AIG was saved. You can add that to the list of screw ups, like allowing five investment banks to leverage 40 times!

What reopened old wounds regarding Geithner was first, his comment on December 23 that "there would be no second wave of the crisis" and then one day later that the U.S. government would unconditionally support Fannie Mae and Freddie Mac. There's no way it was pure coincidence that he chose the quietest time of year when so many investors and media are tending to holiday matters to offer such important comments.

The fact that this man presided over the banks and investment banks and totally dropped the ball is the exact opposite of the meteorologists calling for 10-20 inches here and only getting light snow. Now, he says that another wave of the crisis can't happen? The skeptic in me has just raised the alert level!

Second, and even more infuriating, is something I mentioned during the nationalization of Fannie and Freddie in the summer of 2008. At the time, Paulson and the Bush administration said the cost of the rescue would be contained to $100B at first, with much less being initially deployed. But the more the press dug, the more the public realized that this could become a trillion dollar nightmare in the worst case scenario. I
~~~~~~

think I wrote about a potential $500B price tag when all was said and done.

Now Tim Geithner comes out and pledges unlimited support from the U.S. taxpayer for Fannie and Freddie? How can this be? Where does it end? Does it ever end? These government sponsored enterprises had admirable intentions when they were created, but they ended up poisoned by politics as they became the two largest hedge funds in the world that must eventually be unwound. For now, the government needs to find a way to slowly reduce the size of the entities and their role in the mortgage market.

Long before Tim Geithner steps downs, I fully expect trial balloons to be floated on his replacement. While former New Jersey Governor and Goldman Sachs CEO John Corzine may be the most qualified, it would be hard to believe that people would tolerate it, given the perceived favoritism Goldman has received over the past few years.

Ben Bernanke's Not So Finest Moments

~~~~~~

As long time readers also know, I have been a fan of Ben Bernanke since early 2008 when then "Rip Van Bernanke" finally awoke from his long sleep to take much needed and historic action in the financial markets. While he certainly has to accept some of the blame for being asleep at the switch early on, I commend him for his outside the box thinking and action in attacking the crisis from all sides.

And while I wasn't surprised to see him vilified by several members of Congress during his reappointment hearing to send a very stern and strong warning, it's unreal that you have people like free marketer and fiscal conservative Jim Bunning on the same side of an issue as socialist Bernie Sanders. When was the last time the far right and far left agreed on anything, even the weather, let alone a serious issue? As Charles Dudley Warner so aptly said, *"Politics makes strange bedfellows".*

When I was reviewing my notes for this article, I came across some old comments from the Fed chief that don't exactly put him in the most positive light. Frankly, it makes Bernanke look like he and the Fed had their heads buried in the sand. But in his "defense", I don't believe that he would publicly offer warnings if he did think something was coming. Not from the most powerful banker in the world. I debated listing them, but what the heck.

July 2005 - "I think what is more likely is that house prices will slow, maybe stabilize, might slow consumption spending a bit."

November 2005 - "With respect to their safety, derivatives, for the most part, are traded among very sophisticated financial institutions and individuals who have considerable incentive to understand them and to use them properly."

"the Federal Reserve's responsibility is to make sure that the institutions it regulates have good systems and good procedures for ensuring that their derivatives portfolios
~~~~~~

are well managed and do not create excessive risk in their institutions."

February 2006 - "Housing markets are cooling a bit. Our expectation is that the decline in activity or the slowing in activity will be moderate, that house prices will probably continue to rise."

March 2007 -

"The impact on the broader economy and financial markets of the problems in the subprime markets seems likely to be contained."

May 2007 -

"We do not expect significant spillovers from the subprime market to the rest of the economy or to the financial system."

February 2008 -

"Among the largest banks, the capital ratios remain good and I don't expect any serious problems of that sort among the large, internationally active banks that make up a very substantial part of our banking system."

June 2008 -

"The risk that the economy has entered a substantial downturn appears to have diminished over the past month or so."

July 2008 -

Fannie Mae and Freddie Mac are "adequately capitalized" and "in no danger of failing."

Investment Quotes/Adages To Live By

~~~~~~

"When in doubt, get out!"

"If it's obvious, it's obviously wrong."

-Joe Granville

"It's ok to be wrong, but it's not ok to stay wrong."

"This time is different."

"The markets require the patience of a dozen men."

-Robert Rhea
~~~~~~

"Luck is the residue of effort."

"The most bullish thing a market can do is go up in the face of bad news."

"The most bearish thing a market can do is go down in the face of good news."

"The market can stay irrational longer than you can stay solvent."

-John Maynard Keyes

"Government is best which governs least" - Thomas Jefferson

Inflation is the one form of taxation that can be imposed without legislation.

-Milton Friedman

"You cannot legislate the poor into freedom by legislating the wealthy out of freedom. What one person receives without working for, another person must work for without receiving. The government cannot give to anybody anything that the government does not first take from somebody else. When half of the people get the idea that they do not have to work because the other half is going to take care of them, and when the other half gets the idea that it does no good to work because somebody else is going to get what they work for,that my dear friend, is about the end of any nation. You cannot multiply wealth by dividing it." - Dr. Adrian Rogers, 1931

"Bear markets seem to be divided into three phases: the first being the abandonment of hopes upon which the final uprush of the preceding bull market was predicted; the second, the reflection of decreased earnings power and reduction of dividends, and the third representing distressed liquidation of securities which must be sold to meet living expenses. Each of these phases seems to be divided by a secondary reaction which is often erroneously assumed to be the beginning of a bull market."

- Robert Rhea via Tim Woods

"Free enterprise is a rough and competitive game. Nobody too big to fail. Nobody too small to succeed. It is a hell of a lot better than government control." - Ronald Reagan via Dan Kennedy

"A government big enough to give you everything you want is big enough to take everything you have." - Gerald Ford via Dan Kennedy

"The problem with socialism is that, sooner or later, you run out of other people's money." - Margaret Thatcher via Casey Research

Upcoming TV Appearances

~~~~~~

CNBC's Squawk Box - February 10 at 6:10am

CNBC's Worldwide Exchange - February 11 at 5:30am

CNBC's The Call - February 18 at 11:10am

CNBC's Worldwide Exchange - March 16 at 5:30am

CNBC's Worldwide Exchange - April 27 at 5:30am

You can view most of the past segments by clicking below.

Media Appearances

Friends And Family Plan

~~~~~~

Finally, as you know, our firm and this newsletter continues to grow mostly from your referrals. If you know anyone who is interested in securing their retirement, planning for it or just plain worried about it, please send them here. As always, thanks for thinking of us with your circle of family and friends.

http://www.investfortomorrow.com/newsletter.asp

You can also forward this email to family and friends by hitting the "forward email" hotlink at the bottom of this email.

To Your Financial Success,

Paul Schatz
President
Heritage Capital LLC

1 Bradley Road Suite 202
Woodbridge CT 06525

203.389.3553 Phone
203.389.3550 Fax

www.InvestForTomorrow.com

Important Disclosure Information

Heritage Capital LLC ("Heritage"") composite performance results represent time-weighted actual performance results for continuously managed Heritage accounts, which individual accounts Heritage believes to be representative of its investment management process (i.e. mutual funds and exchange traded funds) for each specific strategy during the corresponding time period. The composite performance results reflect the reinvestment of dividends and other account earnings, and are net of applicable account transaction and custodial charges, and the separate fees assessed directly by each unaffiliated mutual fund and exchange traded fund holding that comprised each account, and the maximum investment advisory fee that the accounts would have incurred (by applying the Heritage's current investment advisory fee of 2.00% as set forth in its current written disclosure statement) during the corresponding time periods.

Please Note: Past performance may not be indicative of future results. Therefore, no current or prospective client should assume that future performance will be profitable, equal the performance results reflected, or equal any corresponding historical benchmark index. The historical index performance results for all historical benchmark indices do not reflect the deduction of transaction and custodial charges, or the deduction of an investment management fee, the incurrence of which would have the effect of decreasing indicated historical performance results. The historical performance results for all indices are provided exclusively for comparison purposes only, so as to provide general comparative information to assist an individual client or prospective client in determining whether the performance of a Heritage program meets, or continues to meet, his/her investment objective(s). A corresponding description of each index is available from Heritage upon request. It should not be assumed that Heritage account holdings will correspond directly to any such comparative benchmark index. The Heritage performance results do not reflect the impact of taxes.

For reasons including variances in the investment management fee incurred, market fluctuation, the date on which a client engaged Heritage's investment management services, and any account contributions or withdrawals, the performance of a specific Heritage client's account may have varied substantially from the indicated portfolio performance results.

In the event that there has been a change in a client's investment objectives or financial situation, he/she/it is encouraged to advise Heritage immediately. Different types of investments and/or investment strategies involve varying levels of risk, and there can be no assurance that any specific investment or investment strategy (including the investments purchased and/or investment strategies devised or undertaken by Heritage) will be profitable.

Information pertaining to Heritage's advisory operations, services, and fees is set forth in Heritage's current disclosure statement, a copy of which is available from Heritage upon request   Performance results have been compiled solely by Heritage, are unaudited, and have not been independently verified. Heritage maintains all information supporting the performance results in accordance with regulatory requirements.