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Waiting for Mr. Farrell

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After last week's issue, my good friend Norm replied, taking a page out of Clara Peller's book, "where's the beef?" He asked me for more market commentary, more charts and more bold opinions. So my response to Norm was, "ask and ye shall receive." Hopefully, this issue quenches the thirst.

After my article on Bob Farrell last week, another good friend, John O., sent me an email letting me know that he plays tennis with Bob all the time and he offered to facilitate an intro. John said to me, "ask and ye shall receive." Hopefully, in the near future, I will meet Bob Farrell, one of the most respected strategists of all time, either by phone or email.
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Similar to last week's edition, it's still snowing in CT with another nice, big storm just beginning. I know you're still cursing me, but spring will be here soon enough and all my snow will be sadly gone.

My 5 year old son has become quite the little powder and bump skier in Vermont, or at least he thinks he is and we've spent some of the greatest father/son time together. When he wakes up or I come home from work, the first thing he asks me is if we can go ski Committed to Ripcord to Second Thoughts to River Run. Those happen to be four trails at Mount Snow. Time is already flying by as the kids grow so the more time I get to spend with them doing fun things, the better!

Barack Obama Meet Bill Clinton

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President Obama delivered the State of the Union last night and you can certainly argue whether it was a good speech or underwhelming, depending on which side of the aisle you sit. I found some things truly fascinating. Late last year, I wrote an article about Obama either digging his heels in with the new Repub House to stand on principle. Or moving taking a page out of Bill Clinton playbook and moving toward the center in hopes of accomplishing some bipartisan work.

Frankly, the only way I thought he had any chance of getting reelected was to follow Clinton's path and reach out to the other side. This has traditionally played very well in the media over the intermediate-term. I have to applaud whichever member of his inner circle spearheaded this effort as it's been a huge success so far.

To me folks like Karl Rove and David Axelrod and James Carville and Mary Matlin are all the same. They follow the same script. They behave the same. They wear the hat they're paid to wear. They are political operatives in a never ending war. And they all know what hot buttons to push with the media and American public to get the job done.

You could see after the crushing Congressional defeat that Obama was at a crossroad. But the extension of the Bush tax cuts, coupled with the deal on the estate tax and payroll tax holiday showed the personality of a man thirsting for reelection over digging in his heels for his agenda. This plays out very well with moderates, but we'll see how he handles the party faithful.

It is extremely interesting that budget cuts have now become front and center after the disastrous November election for the Democrats. And how they very cleverly began using the word "investment" instead of spending and programs. Folks, if you haven't realized it yet, Barack
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Obama's reelection campaign has officially begun!

Turning to the stock market, the pullback or correction that the masses (including me) have been talking about and waiting for has not even come close to materializing. As the number of folks in that camp continues to increase, the likelihood of a real correction diminishes. Remember, most of the time, the market does not accommodate the masses!

At this point, my sense is that stocks will continue to grind higher with a down day here or there until it finally hits an air pocket. That "event" will cause a sharp, scarey and fast drop sometime during the first quarter, but it won't be the end of the bull market, yet.

Besides the fact that the majority is looking for temporary weakness, there are and have been some major warning signs of impending doom. From sentiment to momentum to leadership, there are plenty of reasons to worry. But the market simply has not cooperated. Price is the final arbiter and it certainly looks like Ben Bernanke's QE2 program has some "nice" unintended benefits of higher stock prices and collapsing volatility, for now.

Gold Gearing Up for a Rally

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As I mentioned in my 2011 forecast, after two fantastic years for gold, I expect 2011 to be more of a digestion or consolidation year with a wide and very volatile trading range. I believe we will see $1500 at some point as well as a $100 down day during the year. When all is said and done, I think gold is going to finish 2011 with modest gains, best case scenario.

Several people have questioned why I don't think gold has seen its bull market peak yet. As I mentioned in last week's edition, commodities tend to see inverted "V" tops and long rounded bottoms. That's exactly the opposite of the behavior we usually see in stocks. As a particular commodity gains steam and acceptance, it usually melts up in parabolic fashion.

The chart below shows where gold is today. IF the rally was terminal, it would have blown off to the upside (straight up) and then begin to go straight down. We're not seeing that right now. It's a sideways (trading range) that should eventually resolve itself to the upside.

On the far right of the chart below and the next one, you can see the two possible scenarios for gold in the short-term.   I think the shiny metal
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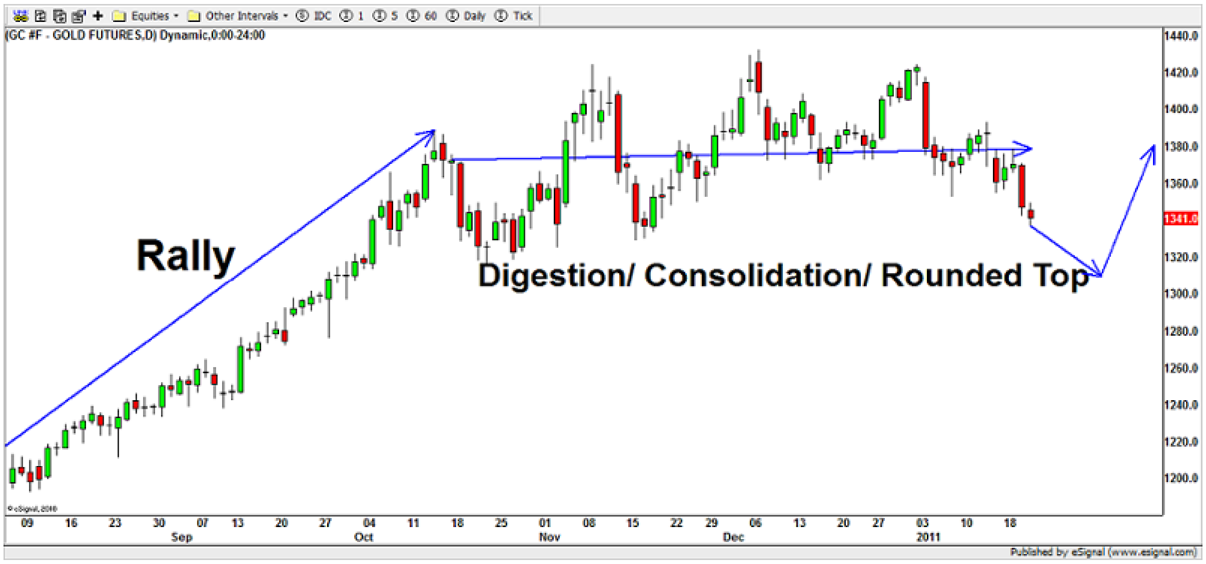
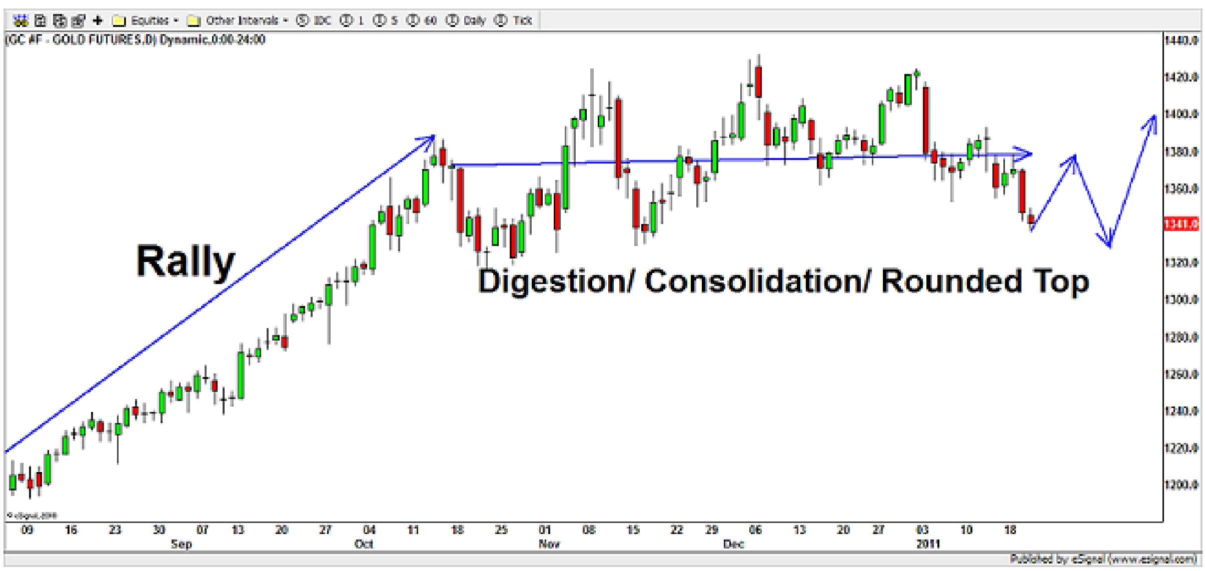
either continues lower into February towards $1300 and then rallies. Or, we see a quick rally now and then another selloff next month before rallying. Either way, I believe the ultimate resolution to this range is a move back to the upper end.





I want to go back to offer examples of how gold behaves near peaks as I discussed above. Before the last rally you can see in the chart above, gold looked a lot like it does right now.

And before that, below, you can see another example of how digestion and consolidation led to another major rally.

Don't get me wrong. This is not infallible, but it does have some solid support behind it. The hardest part is judging what's going on in real time, not hindsight. Many times, the initial top looks like an inverted "V", but never gets going to the downside or stops going down and begins to enter the digestion.

Case in point on the chart above was the peak you see on the far left side that has the makings of an inverted "V". I remember turning negative on gold around $990 as I thought a major top was forming. Several months later after the bears tried and tried to make headway without success, the pattern certainly had changed to that of digestion and consolidation and I slowly went to neutral and then positive.

Update for Heritage Gold Programs

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While on the topic of gold, we recently added our second program to the website under **Strategies.** This program, Intermediate-Term Gold (ITG), is short to intermediate-term in nature and falls in the aggressive category, contrary to our Short-Term Gold Program (STG), which falls in the conservative group.

ITG was launched in September 2009 as a complement to its STG cousin for investors who wanted more of a pure play in the gold and silver mining stock with a much higher risk/reward ratio. So far, it hasn't disappointed with a very strong 30%+ in 2010, but it's not for the faint of heart!

The vast majority of ITG clients are other financial advisors' clients who blend ITG with another strategy or two that dances to a different beat in hopes of smoothing out the volatility. Every 10-14 days, I email a very quick, more technical and unproofed update on our two gold programs, which follows this paragraph. If you are interested in receiving the update, please hit REPLY and let me know.

The XAU index is now oversold on all time horizons, so time-wise, a bottom should be close at hand if we haven't already seen it last week. The correction has been about 15% and the index is about as oversold as it's been since the waterfall decline of 2008. That doesn't preclude more selling, but the bottoming process looks to have begun. Sometimes this takes a "V" shape, like May 2010, while other times it's more complex, like February 2010.

STG took a 50% position on the 20th and that should result in the index moving higher early in the week or a quick stopout as is often the case during the first three days of a trade. As I've discussed before, the highest likelihood for a stopout occurs on day one, day two and then day three of a trade. Once it gets past three days, the odds strongly favor a positive outcome.

ITG's long trade from the 11th continues and is currently experiencing its first real drawdown since late 2009. While I never, ever want to lose money, this is something I have written about before and expected sooner or later. And no, I haven't found a reliable addition to the system that would cushion the blow without sacrificing return. Research shows that in bull markets, these drawdowns usually occur with more frequency that we've seen.

As we've discussed before, gold remains in a trading range that began early in Q4 of 2010. It's not nearly as oversold as the XAU, nor has it seen the price damage done to the gold and silver mining stocks. In the short-term, a move towards the lower $1300s should entice some buyers for at least a reflex rally, if not something bigger.

Ranges like we're seeing now are more indicative of consolidations and digestions rather than terminal bull markets moves. Most times they last 3-6 months, before resuming their uptrend, but it's not unheard of to see them last 9-12 months. My opinion for gold in 2011 remains the same. I
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think the shiny metal will see a wide and volatile range all year with $1500 being seen at some point.

Although the European sovereign debt woes seem to have quieted for now, gold still appears to have a significant bid beneath the market as one of the chosen global currencies. With certain central banks like China, India and Australia in tightening mode, the huge tailwind for gold has lost some steam, temporarily. Until we see some outright central bank selling at lofty levels along with real interest rates above the rate of inflation, gold should remain in a long-term, secular bull market.

Upcoming Appearances

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CNBC's The Call - February 1 at 11:05am

CNBC's Squawk on the Street - February 8 at 9:35am

CNBC's Worldwide Exchange - February 23 at 5:30am

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

Media Appearances

(http://www.investfortomorrow.com/InMedia.asp)

Investment Quotes/Adages To Live By

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"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 Keynes

"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

"Diversification alone is no longer sufficient to temper risk... You need something more to manage risk well."

- Mohamed El-Erian

Friends And Family Plan

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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.

Sign Up Here

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