February 23, 2011

8:39AM EST

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Inside this issue

Libya... One And Done?

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FYI, I will be on CNBC's Worldwide Exchange this Thursday (2/24) from 5:35am to 5:55am. That is, assuming my 4:00am wake up call does the trick after celebrating my wife's birthday tonight. What a difference a few years make! Pre kids, it would have been a serious night out with friends and adult beverages flowing. Now, somehow the kids got to choose the venue, Tengda, but instead of the sushi area, they like the hibatchi room. I know. I know. It's not about me!

For many, many weeks, I have discussed the stock market's need for a pullback. A short-term cleansing to refresh the rally. Unfortunately, far too many others have been talking about it as well, so the market decided not to accommodate, until it wanted to.
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Several weeks ago, I offered that the pullback so many were looking for would probably come out of nowhere with some geopolitical event and would quickly lop 4-7% off the major indices. Today was just that day, following more unrest in the Middle East. This time it was Libya with its big supply of oil. Since I have been writing about this pullback since late last year, I certainly deserve zero in the way of credit for it finally happening. I mean, even a broken clock is right twice a day! Call for something long enough and it's bound to happen at some point.

As I've mentioned before, it's still incredible that the Dow has not closed below its 20 day moving average (average price of the last 20 days) since 12/1 as you can see below. That's historic momentum! I am going to go out on a limb and say that the market will not respond the same way as it did with Egypt and this time it will close below the 20 day moving average in the coming week or so.

But at the same time, I also do not believe this is the start of a real correction (10%+ downside). Corrections typically do not start with a bang like we saw today, just one day removed from the high. Instead, more significant declines usually start slow and small, building towards the large down days, like snowball rolling downhill and gathering momentum. When is a snowball and market going the fastest downhill? The second before it hits the bottom. In this case, we could (and should) see some more downside, but I don't think it's anything serious, yet.

I'll be watching for signs of sector rotation among leadership, both positive and negative, along with any indication that the emerging markets are ready to percolate again. As the major US indices have steadily marched higher since December, which you see from the above chart, emerging markets,chart below, weighted towards the big countries like China, India and Brazil, have totally lost their leadership role and unable to make upside headway.

Equally as important, the performance of the high yield (junk) bond market must be closely watched after the single most dramatic bull market run in history. For the most part, as long as the high yield market is confirming the rally and outperforming on the downside, the structural bull markets in stocks should continue, for now.

As always, please feel free to reach out with any questions or comments by calling the office directly at 203.389.3553 or hitting reply to this email.

Can You Say "Bubble"?

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In the previous issue, I went into detail on how depressed the treasury bond market was and how it was almost impossible to find any bulls. That led me to the contrarian conclusion that treasuries were likely close
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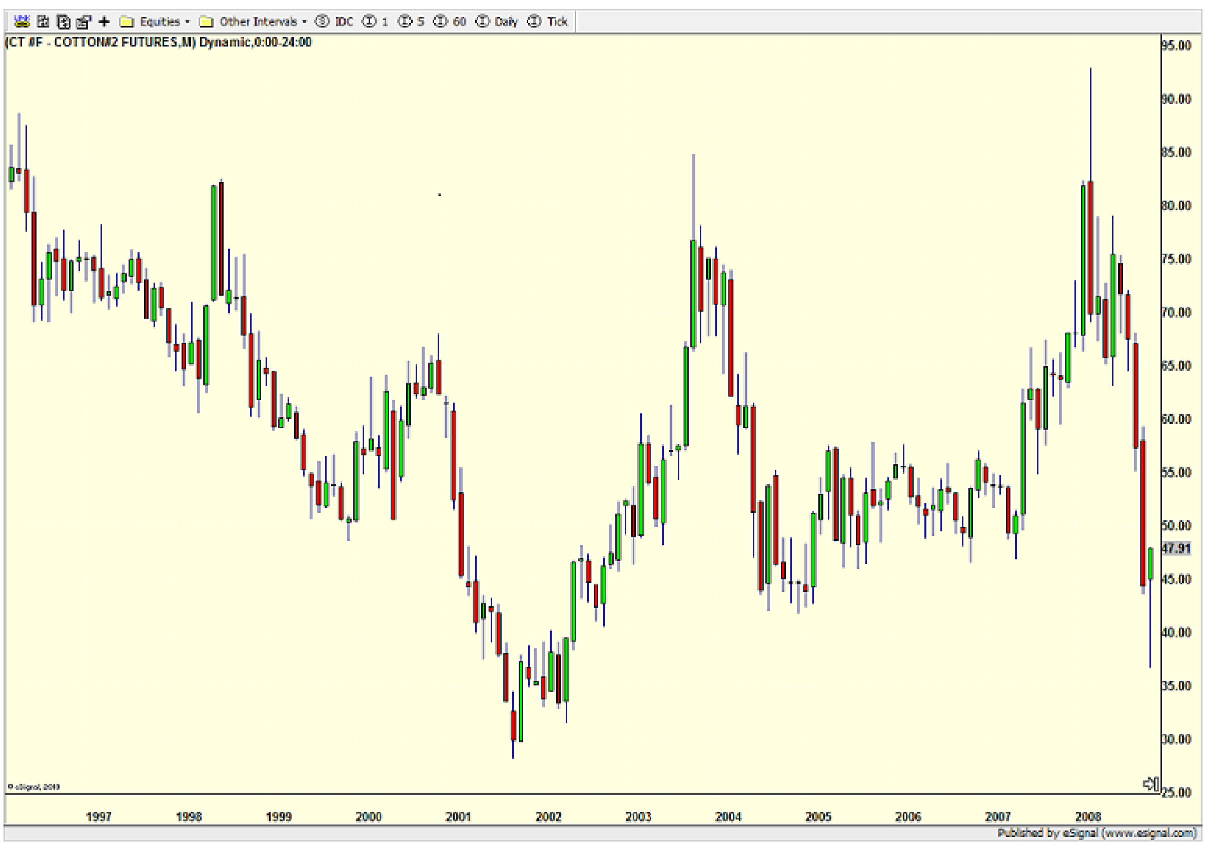
to at least a short-term, if not longer-term, bottom.

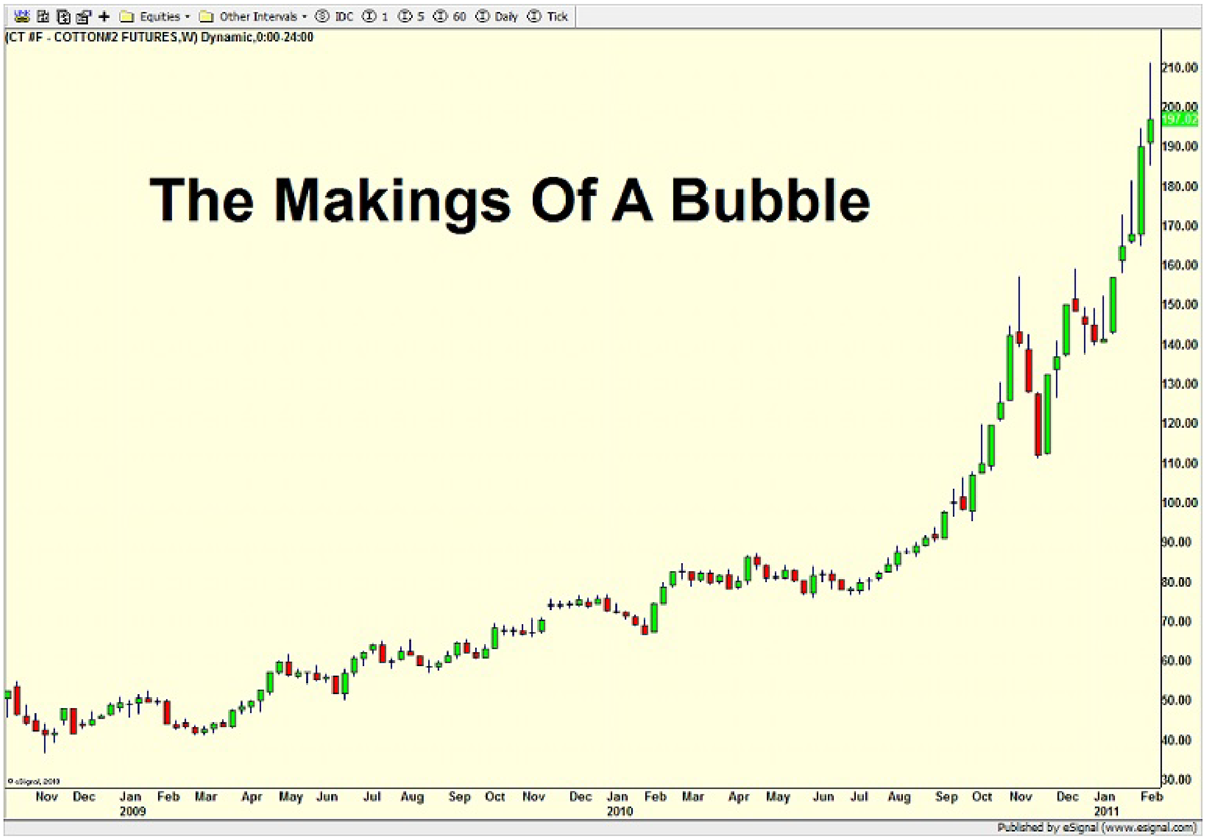
This week, I am going to go to the opposite end of the spectrum and talk about bubbles. In my **Shockers 2011** issue, I spoke about cotton, sugar and coffee being in speculative bubbles that would end very poorly. Let's go into the charts for a peak in cotton. I'll come back to sugar and coffee next week.

The key thing to remember about bubbles is that they always last longer than anyone believes. Declines that appear to be the bubble bursting tend to end and another, even more parabolic, move begins until finally the whole thing comes crashing down. Positioning to profit on the collapse is very difficult since, as we've all learned and heard from John Maynard Keynes, "the market can stay irrational longer than you can stay solvent".

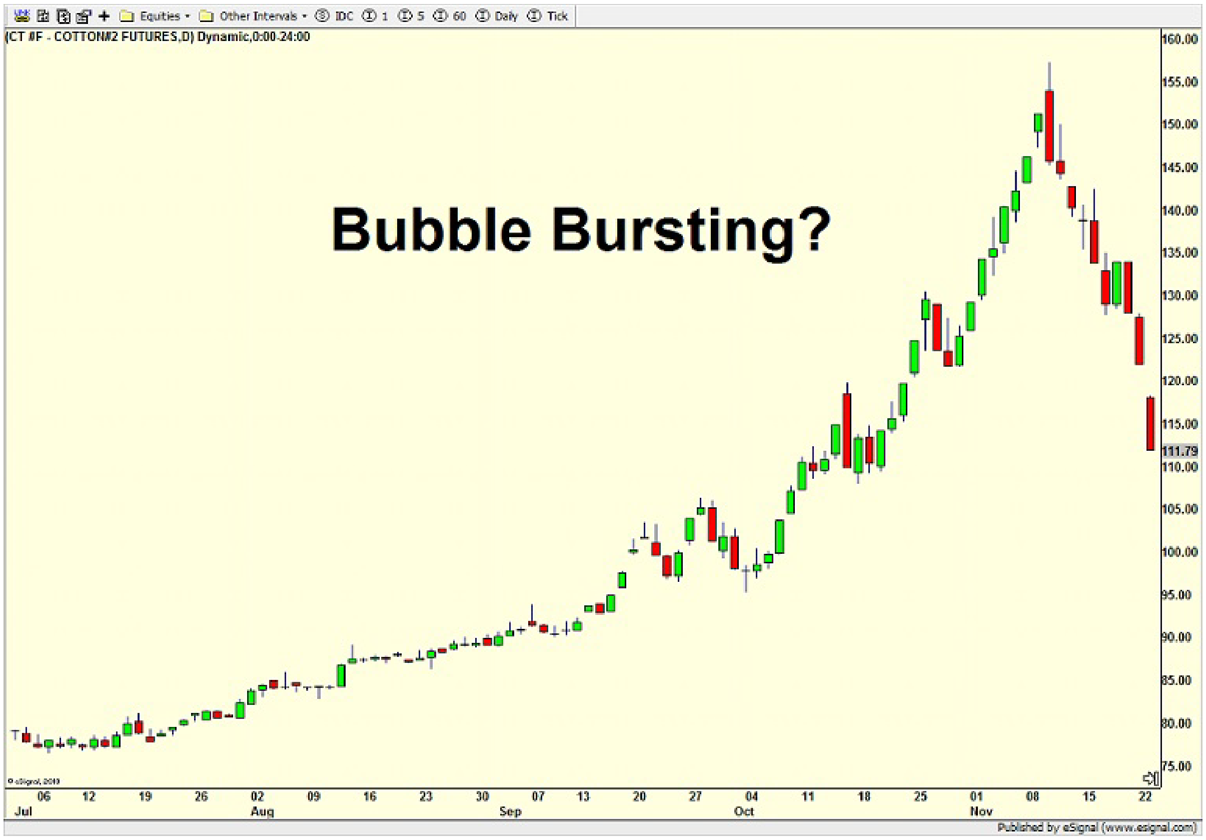
Cotton is a VERY volatile commodity that's known for dramatic, often straight up rises and gravity defying declines. The chart below doesn't even begin to describe the craziness until you pay close attention to the scaling on the right. 30 to 90 and back and back. Try living through that!



Now, multiple moves from 30 to 90 can certainly be classified as bubblesque. But what happened next is unbelievable! From the crash low in 2008 at the far left of the weekly chart, check out where cotton is today. 200!!!



Zeroing in a little more, you can see a daily chart below.



I vividly recall thinking that cotton was heading for a grand collapse from the 150 level in November. All the signs were there!

But someone forgot to tell the commodity!

So once again, cotton has all the signs of a bubble bursting. And in hindsight, it will be clear as day. But how many times can the bears afford to be wrong and totally blown out of the water? That's exactly why bubbles are so easy to spot but so hard to profit from on the way down. They never make it easy!

I stand by my shocker that the bull market in cotton will end very poorly this year, whether the collapse is starting right here and now or later during the first half of 2011.

What's Wrong With This Picture

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Over the past week, there have been marches and protests in Madison, Wisconsin against newly elected Governor Scott Walker's proposal to remove various items from collective bargaining with unions. In exchange for that, he offered to freeze layoffs and furloughs.

Taking a page out of New Jersey's Chris Christie, we are slowly seeing a seachange in state level fiscal policy. And not a moment too soon! For decades, this country has kicked the can down the road until the crisis of 2008 and subsequent budgetary shocks started opening the eyes of the masses.
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I fully expect this new trend to continue across the country as citizens are more than fed up with all the garbage and nonsense going on in government. If we do nothing, there will be a financial crisis the likes of which we have NEVER seen before in America, including the 1930s.

The Wall Street Journal printed an interesting table in the 2/19 - 2/20 edition on page A3 showing how the average public worker is much better compensated than their private sector brethren. That runs counter to what we normally see during emerging and stable economic recoveries.

Below you can see the different categories followed by the average public worker versus private worker. I do not know how the WSJ conducted their research and we all know that numbers can be skewed to fit one's desire, but I think you get the message here. Something needs to change.

Average hourly wages $26.25 / $19.68

Retirement Benefits 99% / 74%

Medical Benefits 99% / 86%

Medical Premiums paid by employee 11% / 20%

Paid Sick Leave 98% / 74%

Paid Holidays 11 / 8

I always find it interesting when a president is riding a new wave of popularity that he decides to weigh in on issues that can only hurt him. According to the WSJ, when asked about Governor Walker's plan, President Obama offered, "seems like more of an assault " on unions. Governor Scott Walker shot back, "When your budget is fixed, you can stick your nose in ours". Touche!

The budget showdown in Washington is in full swing, especially behind closed doors. Those of you who think that politics and financial markets have no correlation and don't mix, you will be in for a rude awakening. The game of chicken is inching ever so closer to the March 4 deadline when at least a short-term spending bill must be passed. Harry Reid proposed a one month measure that freezes spending at current levels, while John Boehner countered that any measure must cut the deficit. The next 10 days should be fun!

Upcoming Appearances

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WTTB's Lighthouse Retirement Hour - February 12 at 12:15pm

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

CNBC's The Call - March 9 at 11:05am

CNBC's Squawk on the Street - March 15 at 9:35am

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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