July 31, 2014

4:41 PM EST

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Inside this issue

Bears Get to Celebrate for a Bit

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As I write this article the stock market closed down 317 points, which is only 1.88% at these lofty levels. That's the biggest one day decline since April, wiping out all of July's gains. Hopefully, you have been reading **www.investfortomorrowblog.com** where I started giving the bears a tiny bit of credibility in mid July, but really agreed with their argument beginning this week. In hindsight that looks like a nice call at the top. The decline that is unfolding should be able to bought before long and should not be thousands of Dow points.

If you don't read the blog regularly, there is a place to sign up to receive emails when something new is posted.

For a long while, I have enjoyed the way the stock market crept higher day after day and week after week, frustrating the heck out of the bears. When you are on the bullish side as I have been, that's awfully fun! The problem
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with markets that grind higher with no end in sight is that when the uptrend finally does cease weeks or even months of gains get wiped away in short order like we are seeing now. Thankfully, whether by luck or skill, cash was dramatically increased in every single portfolio with some strategies going to 100% cash.

Before I continue, I want to repeat a common phrase from the past few years. I do not believe the bull market is over. I do not believe the final peak is in. All this talk of a "bubble" in stocks is PREPOSTEROUS! I don't know any successful money manager who could come to that conclusion here. It doesn't make even the least bit of sense. It's almost as bad as those who opine that the Federal Reserve has been manipulating the stock market higher by directly investing in stocks and futures. Of course the Fed wants a higher stock market! Who doesn't besides the perma bears?

Anyway, enough ranting. As with any forecast or opinion, I could be wrong, but market history remains on the bulls' side. Before the bull market ends, we should see a pullback of 4-7% that leads to another all time high. And after that high, there should be a 10% correction that should lead to the final high. We haven't even seen the 4-7% runs its course yet so there is likely more money to be made for the bulls.

Besides price patterns, the canaries in the market's coal mine have not begun to die which is a good topic for the next Street$marts. We simply do not have the traditional warning signs in place. And those red lights can come a few months before the bull ends or sometimes even two years as we saw in 1998.

What concerns me most right now is that the major sectors that make up the stock market are not screaming buys into the weakness as they have been over the past few years. It will be interesting to see which sectors begin to outperform during the decline and which get taken to the woodshed.

Tomorrow will be an interesting day as it's the first Friday of the month, which means the employment report. Coming off a big earnings week, good GDP report, the Fed and global turmoil, I am keenly watching how stocks and bonds react to an anticipated strong number. A weak number likely sends bonds much higher and stocks in the opposite direction.

As always, don't hesitate to hit REPLY or call the office with any questions.

Vantage Point Yields Crude Conclusion

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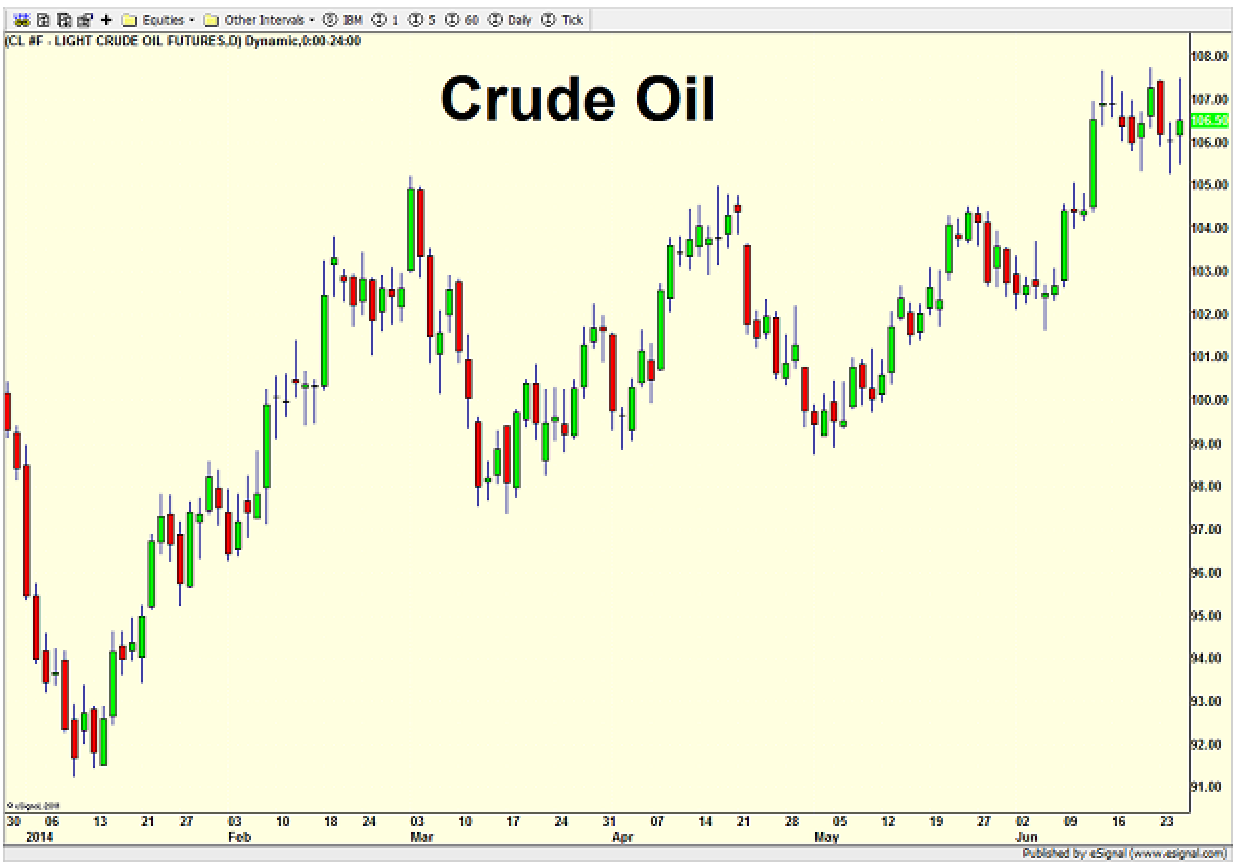
In the previous issue, I offered a few shorter-term scenarios for crude oil and discussed why there is absolutely no inflation whatsoever in energy. I also forecast that oil was in a good position to rally almost immediately to at least $108, if not $115, but that closing in the $102-$13 range would tell me I am wrong and to move on. From the then current price of $104, crude fell quickly and I was wrong. In risk terms, a $2 loss or less than 2% should be manageable for investors. That's the risk/reward way to invest in the short-term.

Turning to where oil is today versus last year and over the past 13 years, you get very different views depending on how long your time horizon is. Starting with oil in 2014 below, and I am going to use round numbers to make it easier, we see that oil began the year at $93 and ran to $107 recently. $14 or 15% certainly looks like a big move over a short period of time. But is it?



Taking a full year view looks very different than just 2014 as we can see below. Last summer, crude oil averaged just about $107 and essentially treaded water on a year over year basis. Factor that into the inflation numbers and there isn't any inflation in what commonly referred to as the "volatile energy number".
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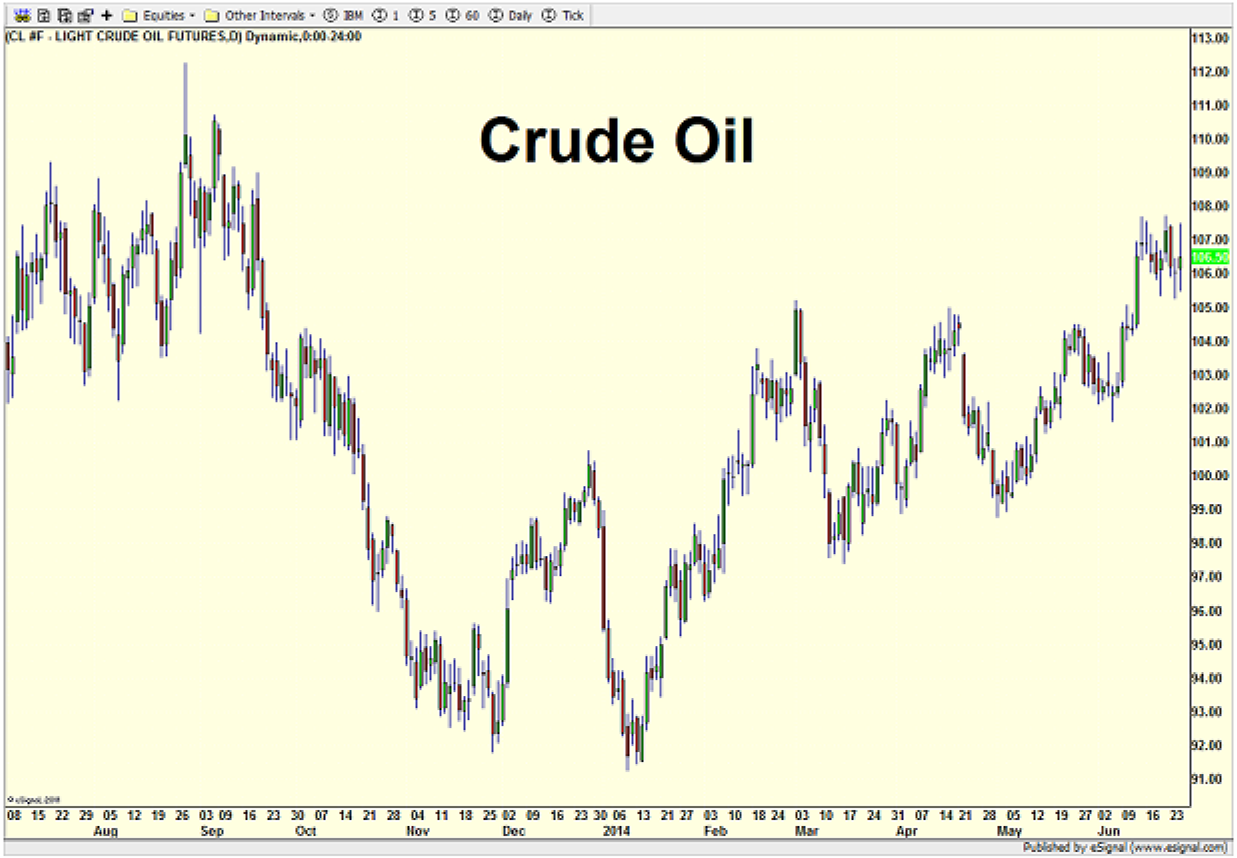
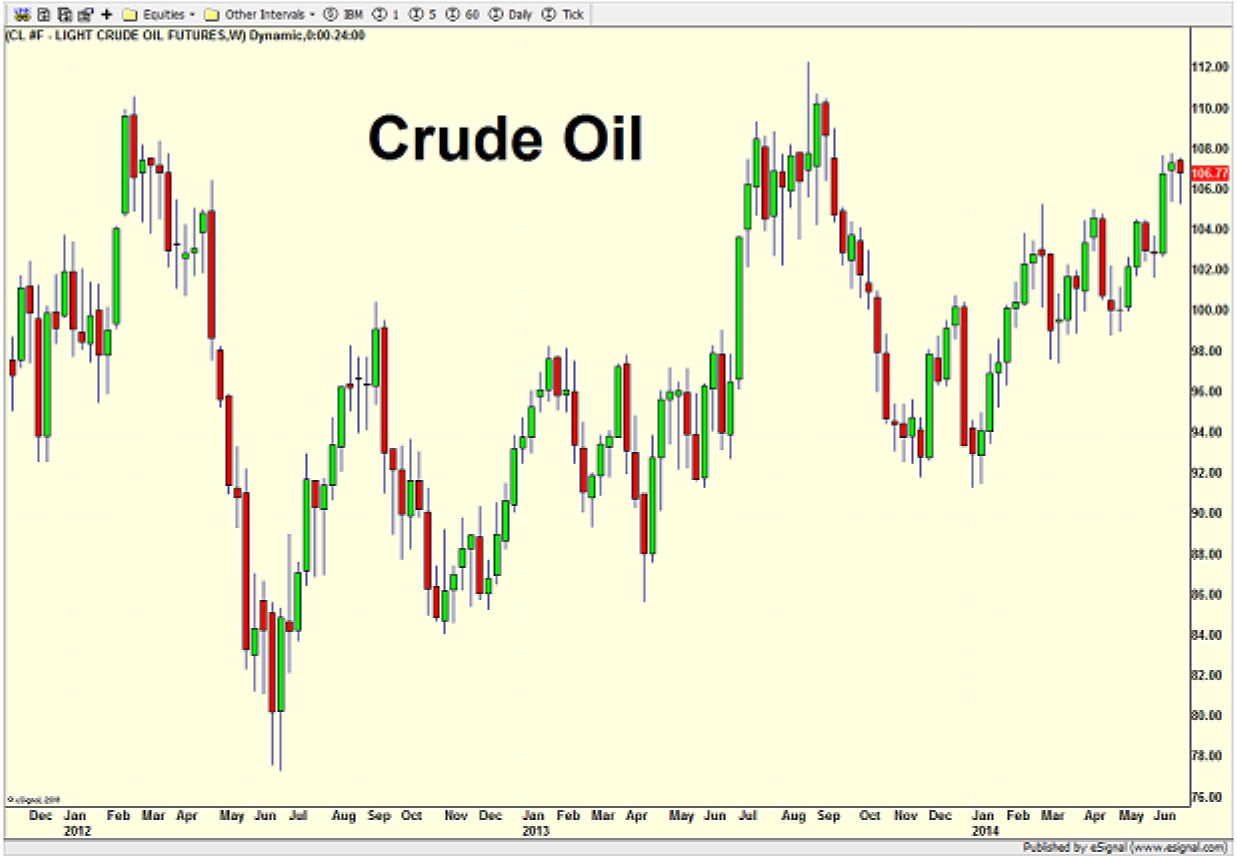
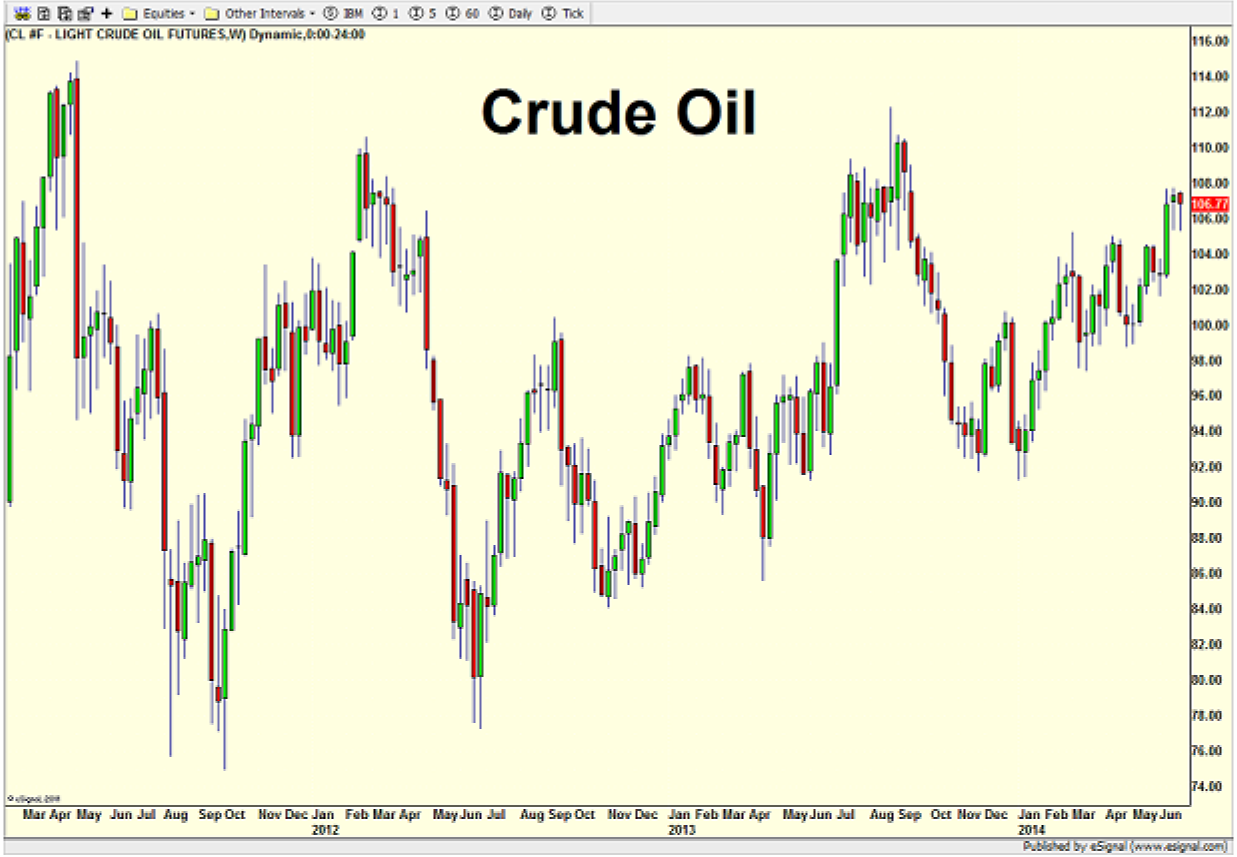
Living through the last 12 months yields celebration when oil plummeted from $113 to $91 and unhappiness when ran back to $107.



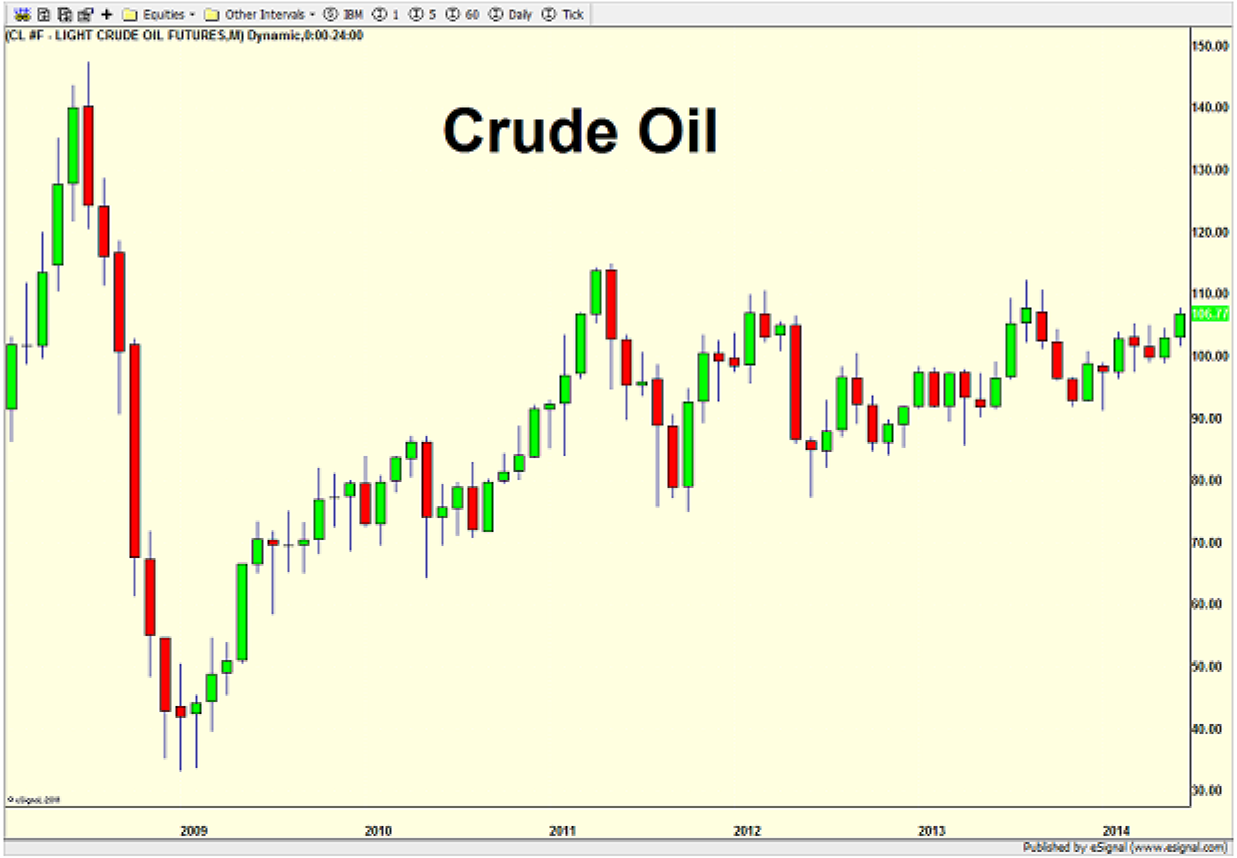
Next, we look at the last two and half years below which also shows fairly stable energy prices overall if you just looked at the far left ($100) and far right ($107). A $7 or 7% increase over two and half years is more than manageable and not very inflationary at all.



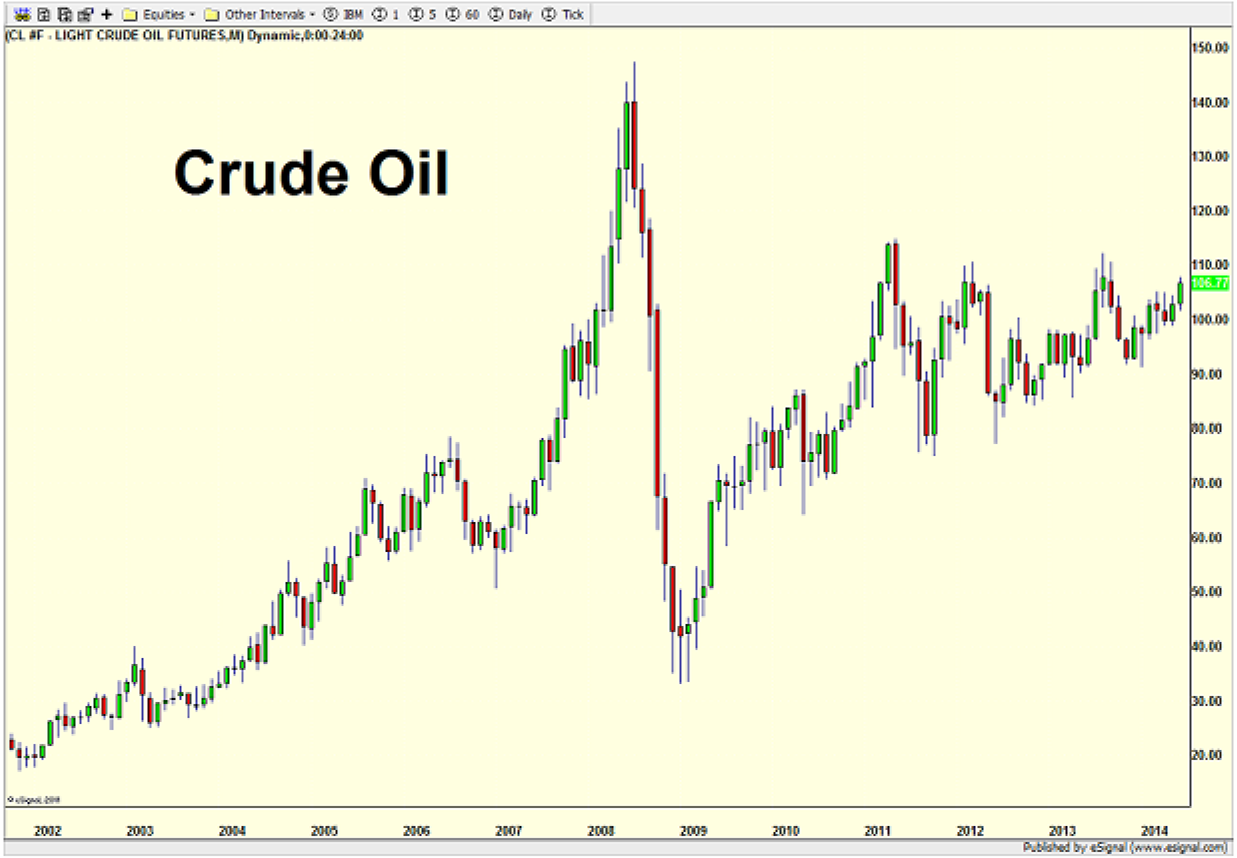
Thrown in for good measure below, adding another year to the equation doesn't change the stability of oil prices. They continue to trade around their average price, plus or minus, over the multi-year time frames. It is very hard to argue that we have any kind of problematic energy inflation.



Now we are into the bigger picture with six years below. This view is good because we see the oil melt up to $147 in 2008 and the subsequent collapse to $35 only a few quarters later on the left side of the chart. It's also interesting to note that ever since the peak and trough six years ago, crude oil inside that band between $147 and $35. In other words, volatility, both upside and downside, has been consistently drained out of the energy market. That certainly runs counter to what we hear and read from the pundits and media, and I will venture to guess that this surprises you as well.



Finally, we can see the past 12+ years of movement in crude oil below. Putting any kind of meaningful average on the chart yields similar conclusions. With the exception of the two year meteoric rise and demise, energy prices have steadily marched higher in a very controlled and gradual fashion at roughly a 30 degree angle. Granted, \$20 to \$107 impacts us all, but over a 12+ year time horizon, adjusting to higher prices is manageable, let alone the number of oil alternatives that continue to enter the market.



Unmanaged Index Funds Are Not "Safe" Investments

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How often have you encountered the following advice? You can't predict the direction of the market so the safest investment is an index fund. To an investment manager, that advice sets one's teeth on edge.

There's nothing "safe" about an index fund. An index fund is a creature of market direction. Whatever the index does, the fund is designed to mirror. Index funds offer no risk management, no ability to invest in top performers, and no guarantee of success. Investing in an unmanaged index fund is a gesture of faith that the economy and the industry segment represented by the index will grow during your investment time frame, and that the index will be positive when you need your money. It doesn't always happen that way.

Historically, index funds work best the longer your investment time frame, with lots of time to recover from down markets. If you happen to be retiring and you need to liquidate portions of an index fund, it matters a great deal whether the index is in an up or down trend. Withdraw in a falling market and you can quickly run out of money. The chart below shows the effect of withdrawing $10,000 a month from $2,500,000 invested in the S&P 500, Nasdaq Composite, 10-Year Treasury Bond index and cash over the period 2000-2012. The best investment? Cash.
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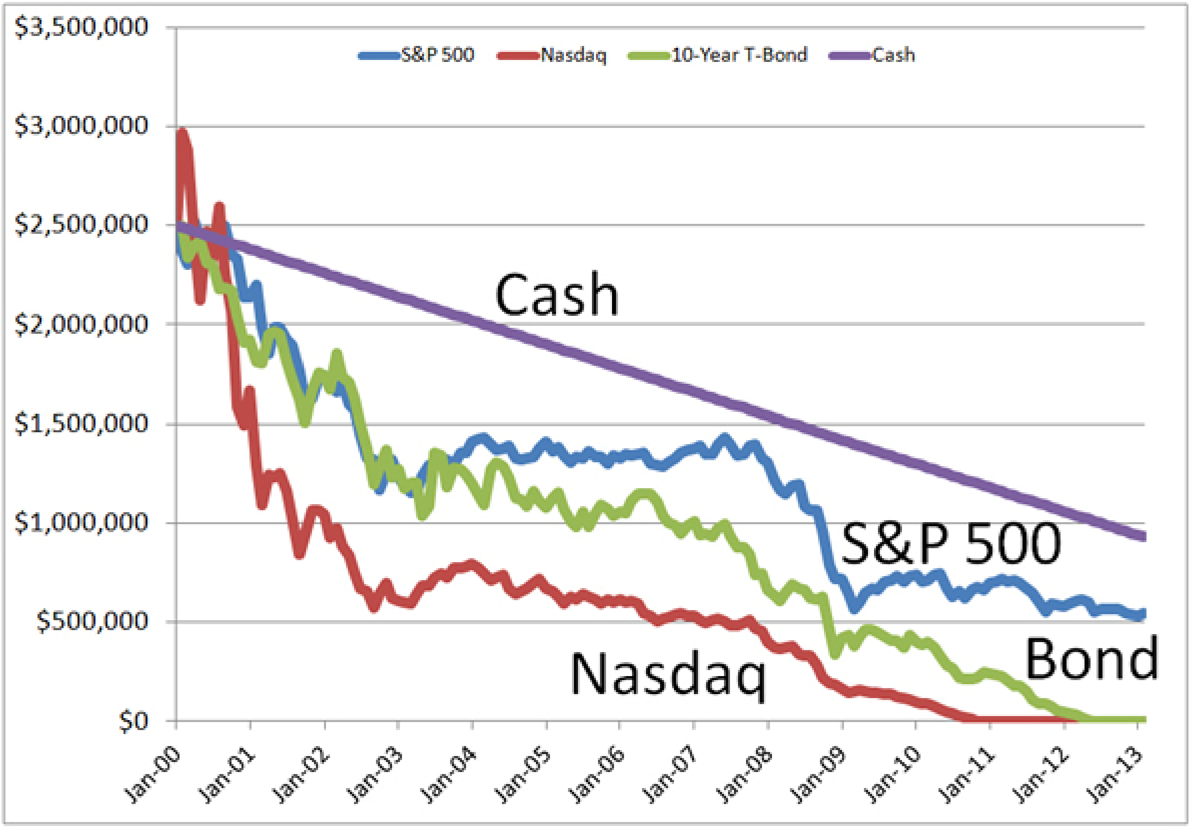
Impact of Withdrawing $10,000 a Month from Index Funds 2000-2012



Data: Yahoo Finance. Past performance is not an indication of future returns. In a different time series, results would differ. The S&P 500, Nasdaq and 10-year Treasury Bond are unmanaged indexes and cannot be invested in directly. The chart above does not reflect transaction costs, which would have the impact of further lowering balances.

According to traditional investment advice, you lower the risk of investing by holding multiple low-correlation index funds covering different asset classes. The concept behind holding uncorrelated assets is that they should not all move in the same direction. When one goes down, hopefully another will increase. But this also fell apart in the time frame shown above.

The popular market segments used in traditional portfolio diversification based on fundamentals and capitalization (large-cap value, large-cap growth, mid-cap value, mid-cap growth, small-cap value, small-cap growth) tend to become highly correlated in market downturns. In the 2008 bear market, indexes based on these segments moved lock-step downward.

Incorporating risk management in a portfolio requires active management. A mixed approach of reducing equity allocations in periods of falling prices and increasing cash positions, and the reverse in rising markets, has the potential to provide investors with the best of both worlds - the preservation of capital offered by cash and the opportunity for appreciation from an equity investment.

With that said, success in active management depends on the ability of the manager to accurately determine the direction of the trend and position assets accordingly. There can be no assurance that an active strategy will be implemented successfully.

Upcoming Appearances

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Yahoo Finance's Breakout - August 14

Fox Business' Money - August 14 at 2:15 pm

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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"The only easy day was yesterday."
- The U.S. Marines

"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, 1984

"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

"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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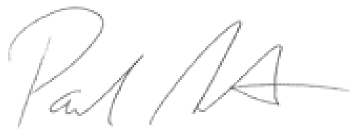
To Your Financial Success,



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