



Stock Market Barometer



Quote of the month:

“We can borrow money for 10 years as the government of the United States because people have confidence in this country at less than 2 percent...The responsible path now is to take advantage of the unique position.” - Timothy Geithner

The Most Influential Financial Newsletter Read By Over 500 Hedge Fund Managers and Thousands of Elite Investors ~ Nov 1 2011

The BIG CHASE Begins! - Mike Swanson (11/01/11)

Boo!

Last night was Halloween but the real scare is happening right now.

No I'm not talking about the fact that stock market dropped yesterday and is poised to gap open this morning. That doesn't matter because I see that just as little pause after the market has gone up almost five weeks in a row.

The real scare is happening on Wall Street where institutional money managers are underperforming the market and according to the statistics there are a lot of them out there. The hedge fund HFRI Weighted Composite index ended down 5.13% for the year at the end of October of as many hedge fund managers got whipsawed in the commodities market during the August-October market correction.

This is bad for hedge fund managers, because the S&P 500 is down less than a percent year to date as of yesterday's close.

So there are a lot of money managers literally sitting out there now with their pants down.

And it isn't just little funds in trouble. Some of the biggest hedge fund names are hurting big time. Take John Paulson for example. Back in 2008 he made \$15 billion by betting against mortgage backed securities. This year his flagship fund is down 50%.

A survey of 150% hedge fund investors by Barclays

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MICHAEL SWANSON

Capital last month found that 35% of them planned to get out of their funds that were underperforming the stock market.

Some of these fund managers have made money year after year, but now suddenly are down this year and their investors have no mercy for them. You can make money for ten years in a row, but if you slip up one year people will take their money out to put it into something they think is hot.

The biggest problem anyone has dealing with investors - whether they be a simple stock broker or billionaire hedge fund manager - is that people do not mind losing money as long as everyone else is, but if the market goes up and they don't make money there will be hell to pay.

As a result most brokers and Wall Street types simply stay bullish on the market all of the time. That's why you get these panic corrections like you saw this summer. Everyone gets positioned on the long-side of the market and then bam! - people get smashed.

What this also means is that most investment decisions made by the professionals are done for emotional reasons too just like they are for the individual investor. There is very little real research done on Wall Street.

That's why the banks went under.

Mutual funds get money from regular people and then just pile that money into stocks without doing much research. The more money they get the less research they do, because they need to play big cap stocks and there are only a couple hundred of them.

If you were playing the market back in 2000 you'll remember the Janus fund was the big fad of the moment back then. It was one of the biggest tech mutual funds and all it did was put most of its money into a dozen big-cap tech stocks. As more money came to them they just bought more and more of these same stocks. But then when the bear market came the fund got killed as these stocks fell into oblivion.

The Janus fund people advertised themselves like they were cutting edge investment experts that understood the "new economy" when in reality they were nothing but momentum players dressed up in suits.

Why do I bring this up now?

Simple.

There is always a theme helping to drive the market moves. In this past correction it was the European debt crisis. That correction came to an end in the first few days of October and the S&P 500 has rallied 20% already since it put in that low.

This has put hedge fund and mutual fund managers

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that have lagged the market all year in a desperate situation right now, because they are under tremendous pressure to catch up with the market. The market is now rallying and they now must CHASE the market higher.

So from now until the end of the year this need to chase will help fuel the market higher. There will buying will help prevent yesterday's drop from turning into a real correction.

Buying will not be done based on careful analysis or real positive fundamental reasons, but a simple need to chase returns.

This is one reason why in the October Power Investor updates I've been so bullish on the market and almost of the stocks we've highlighted in them have done well.

Yes, I think the European debt crisis will return again next year as a problem and bring another big correction with it once the bail-out band aid that has been applied to Greece wears off, but right now that doesn't matter to people. All money managers are going to be thinking about is their jobs and in a rallying market that means they will feel that they MUST buy and CHASE.

Such fear based buying will eventually lead to fear based selling, but it will be the defining characteristic of this stock market for at least the next two months - maybe even three or four months.

Fundamentals don't really matter. All that matters right now is momentum and investor sentiment. Everyone got bearish at the start of October after they sold. That made it time to buy. In a few months everyone will get bullish - they'll rationalize their fear base chasing buy saying that all problems are solved.

But they won't be. But don't think about that now, because no one will until it matters again and right now it doesn't. All that matters it that the market has been going up for the past few weeks, is likely to go up more, and there are too many people who simply cannot afford to miss out so their buying can help fuel the market even higher.

Right now though it is pausing right at long-term resistance. The market went right up to its long-term 150 and 200-day moving averages and stalled out. It's amazing



how these things happen, but they do happen and that's why we pay attention to them.

I'd expect the market to pullback here for a few sessions quickly— which it already is - and digest its gains of October by consolidating around its current levels for the next few weeks to start another real move higher by the end of this month or early December and then maintain a positive trend towards at least the end of this year.

For the most part everything has been going up together. I use TC2000 to analyze the market into over 230 sectors and there are a few of them that are charging up much faster than everything else. They include foreign banks rallying to the tune of 46% in a short-squeeze, toy stores up 40%, oil up 33%, and airlines up 28%. Sectors that are lagging badly and are up less than 10% include drugs, tobacco, and restaurants.

Gold stocks and commodities are lagging too.

So there is an interesting rotation going on where in past rallies commodities and mining stock performed well but so far on this rally the mining stocks aren't.

It could be that some of the big hedge funds that invested in them are being forced to sell. Since the mining market is small in regards to market capitalization it doesn't take that much selling to keep them down.

I will be keeping you updated on the market in some videos this month and should have the next detailed Power Investor report out around November 8th. I know this monthly letter is a little shorter than most of them, but frankly there is not much thinking that needs to be done in this market right now. Simply play dips and acknowledge that we are in a market with little downside risk for the rest of the year.

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