Private Wealth Advisory

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Monkey See, Monkey Do

The efficient market theory, like phrenology, is a load of garbage.

Markets have never been efficient. And any faith that somehow the market knows something you don't is an appeal to a higher power, a market god, that does not exist.

The market failed to predict the Tech Crash, the Housing Crash, the Investment Banks Collapse and the like. Indeed, stocks were still only 16% off their ALL-TIME HIGHS even AFTER the collapse of the entire investment banking industry AND the bailout of half of the US mortgage market (Fannie/ Freddie). <u>Indeed, we had to get within 500 trades of a full-scale systemic meltdown before stocks finally took a nosedive.</u>

That, to me, is truly extraordinary and illustrates the degree to which delusion and inculcated bullishness dominate the stock market. Alas, despite stocks staging one of their worst years on record (2008) both of these (delusions and inculcated bullishness) continue to dominate today.

Indeed, few things illustrate these attributes like our current rally in equities. Sentiment has improved dramatically despite the fact that none of the government's moves/interventions have addressed the core issues plaguing financial markets. These issues are:

1) Lack of confidence in US accounting standards (mark to model AKA imaginary)
2) The insolvency of the US banking system
3) Rising unemployment
4) Structural issues in the job market (we have an environment that cannot create solid, sustainable growth)

Banks have not been forced to come clean about what they own or do not own (this now extends to the US Federal Reserve). Banks remain largely insolvent with more liabilities than assets (ditto the Federal Reserve). Unemployment (without federal gimmickry) is at 20% rising at its fastest pace year over year since the shutdown in production following WWII. And the Stimulus Plan is only creating short-term construction heavy jobs and/or jobs in the public sector (indeed, the Federal Government is now both the only lender AND theonly employer in the market).

And yet, stocks have rallied more than 30%. However, it's worth noting that this rally is running out of steam.

As you can see, the S&P 500 has hit STRONG resistance at the 200-DMA. From a technical standpoint, we could very well see a test of the 50-DMA. And there is the potential for some serious shorting opportunities.

But I'm not recommending any shorts today.

My reasoning is simple. Someone is propping this market up. Someone BIG. For you to understand how, you need to know about stock futures.

Stock futures are a means of betting on where the market will be trading in the future. Unlike regular stock investments in which you purchase the investment the moment you hit "buy," stock futures are investments in which you promise to buy at a specific price on a specific date in the future (hence the name "futures").

Think of it like going to the racetrack: you're betting on what a particular outcome will be at some point in the future. Only you're betting on GE trading at $15 a share on May 28, rather than "Big Brown" winning the Kentucky Derby at 10 to 1.

The futures markets trade around the clock (some of them 24 hours a day). Because of this, you can ALWAYS see exactly where investors are betting that the market will be trading at some future date. Say you're getting bearish about stocks buy see that a bunch of folks just bet $2 billion the S&P 500 will rally… well you might wonder if they know something you don't.

Which is exactly what is going on in today's market. For weeks now, any time stocks showed signs of breaking down (especially in the final minutes of trading), a large volume of bullish futures would be bought. The market would then surge higher as investors believed that someone knew something they didn't. And so, this market rally continues on weaker and weaker volume.

For instance, last Friday seven minutes before the stock market closed, 100,000 S&P futures contracts were traded. Another 100,000 were traded again five minutes before the closing bell. In dollar terms, someone spent $10-20 billion betting the market would rally with only seven minutes to go for stock trading. Investors, thinking someone knew something they didn't, loaded up, pushing the Dow from a loss of 18 points to a gain or 44 points.

Look at the last 30 minutes of trading…

There are plenty of conspiracy theories about who this is. But the reality is that no one actually knows. It could be several large hedge funds. It could be one of the big banks trying to crush the shorts (Goldman Sachs is rumored to have had a huge gold short position last summer right before gold tanker). Or it could be the oft-mentioned but never proven Plunge Protection Team (PPT): a pseudo-fictional governmental group that steps in to keep stocks up whenever they're close to breaking down.

Regardless of who it is, they're BIG, have plenty of CASH and are keeping stock afloat even though the market wants to fall. From a fundamental standpoint, stocks should and WILL fall eventually. But right now, going short is like playing poker with an 800-lb gorilla. Even if you have the winning hand, you can STILL get beaten.

For this reason, I'm not opening any shorts this week. And I'm not comfortable going long while fundamentals are worsening. So we're on the sidelines for now. The rule with trading is never to make a trade until you know the field. Right now, the field is being manipulated (even more than usual). So I'm not comfortable putting any capital at work.

However, that doesn't mean we're not making money. Three out of our four "inflation trade" positions are up. Not bad for one week. And we're just getting started.

Portfolio

Company	**Symbol**	**Buy Date**	**Buy Price**	**Current Price**	**Gain/ Loss**
Gold ETF	GLD	5/6/09	$89.54	$91.09	2%
Gold Miner's ETF	GDX	5/6/09	$36.86	$37.94	3%
Rogers Agri ETN	RJA	5/6/09	$7.62	$7.83	3%
Lehman 20-year+	TBT	5/6/09	$50.11	$49.29	-2%

I'll be watching the market closely over the next week. If anything changes you'll hear from me via an email alert. If nothing develops I'll speak with you next Wednesday in our next issue of *Private Wealth Advisory.* Until then…

Good Investing!

Graham Summers