Private Wealth Advisory

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The "New" Rules of the Game

Welcome to the "new" rules of finance.

As you know, last week stocks were beginning to collapse in a very significant way. By the time Friday rolled around, the S&P 500 looked to have broken the bearish rising wedge pattern that we've been tracking for the past few weeks.

A confirmed breakdown (meaning stocks fall below the trend line and fail to rally back) was the confirmed "sell" signal I've been waiting for to go "all in" shorting this market. To that effect, I began preparing our official "sell" market update on Friday.

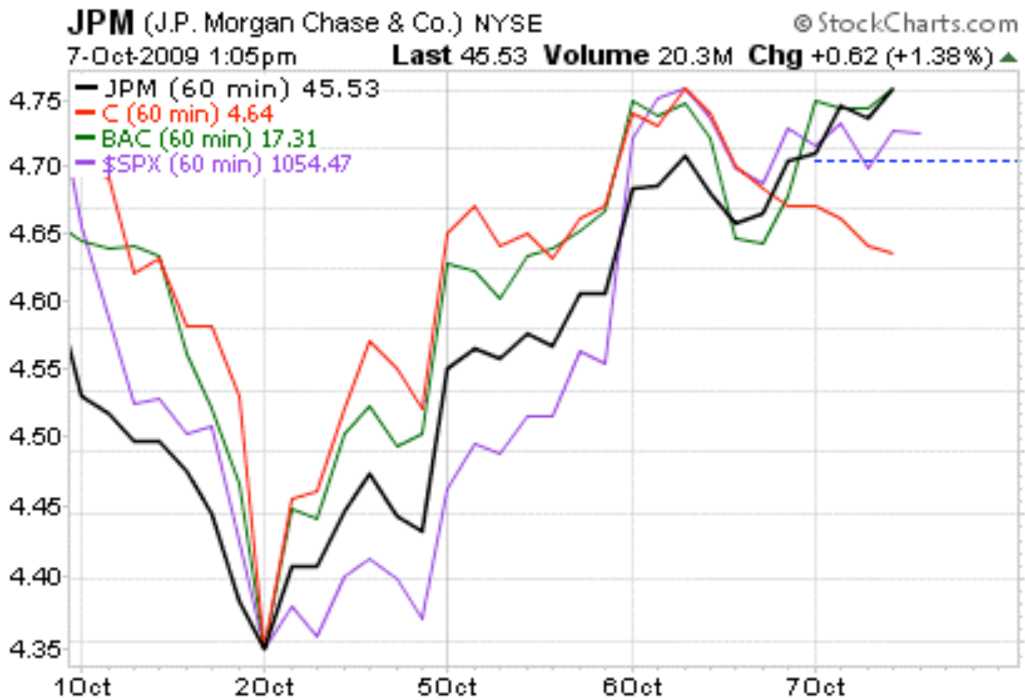
And that's when it happened.

Friday morning, stocks rallied… HARD. As I've noted in previous issues, collapses involve three stages:

1) The initial drop (usually 5-6%)
2) The bounce
3) The "real action" (a large scale correction of 10-30% depending on if it's a correction or a Crash)

Something Doesn't Smell Right…

However, this rally was different in several key ways. Firstly, the reversal began first with bank stocks: the same stocks that were nose-diving Thursday. Look at what happened on Friday October 2: CitiGroup (red), JP Morgan (black), and Bank of America (green) all exploded higher in the first hour of trading. Meanwhile, the S&P 500 (purple), traded sideways for most of the day before finally catching a bid in the last hour of trading.



Looking at this action, it is clear that someone (someone big) piled into banking stocks first thing Friday morning. However, there were NO significant announcements for financial or banking stocks that day AT ALL. Why would banking stocks explode higher— leading the rest of the market higher— on NO NEWS at a time when stocks were literally on the verge of entering a full-scale collapse?

We got the answer on Monday (see the news story below)

Major bank stocks get a boost from analysts

By Alan Fein

(AXcess News) New York - ***Major US bank stocks got a boost Monday morning from analysts*** *with Wells Fargo (NYSE: WFC), Bank of America (NYSE: BAC), CIT and Goldman Sachs (NYSE: GS) trading up as the economy still remains uncertain.*

The increase in market price for big banks came after Goldman Sachs raised its outlook for large banks to outperform regional lenders with Wells Fargo's shares leading the pack, up $1.46, or 5.56%, at $27.74. CIT gained 5 cents, or 4.27%, at $1.22, Bank of America rose 40 cents, or 2.45%, at $16.74 and Goldman Sachs itself climbed $4.56, or 2.54%, at $184.17.

The analysts at Goldman Sachs believe large banks are showing a "dramatic improvement to earning power" verses the regional banks, which Goldman is keeping a 'cautious' outlook on.

Goldman's analysts pointed to 'tangible asset's per share at large banks having increased 29 percent, compared to a 25 percent drop at regional banks, with Wells Fargo the leader at a 70 percent gain.

The explanation here is obvious: Goldman Sachs told their private clients they were about to upgrade bank stocks Friday morning. The “smart” or “informed” money piled in, making a fortune as the shorts got killed (just imagine the profits you could make using options or futures to front-run the entire market). The “dumb” money then invested on Monday when Goldman made its upgrade announcement public. Meanwhile, the “informed” Goldman clients took their profits.

Put another way, Goldman not only manipulated the market, but it actively engaged in insider trading and helping its private clients front-run everyone else. We know this is common practice at the firm: the below article from the *Wall Street Journal* (published August 23, 2009) delves into this Goldman practice in detail:

Goldman's Trading Tips Reward Its Biggest Clients

Goldman Sachs Group Inc. research analyst Marc Irizarry's published rating on mutual-fund manager Janus Capital Group Inc. was a lackluster "neutral" in early April 2008. ***But at an internal meeting that month, the analyst told dozens of Goldman's traders the stock was likely to head higher, company documents show.***

The next day, research-department employees at Goldman called about 50 favored clients of the big securities firm with the same tip, including hedge-fund companies Citadel Investment Group and SAC Capital Advisors, the documents indicate*. Readers of Mr. Irizarry's research didn't find out he was bullish until his written report was issued …*

http://online.wsj.com/article/SB125107135585052521.html

You and I Are the Last to Know

Welcome to the new “rules” of the financial game: where Wall Street is openly permitted to front-run, use insider information, manipulate the markets, AND make fortunes doing it (Goldman had only two losing days for its trading department in 2Q09, a statistical impossibility).

This is why I have not yet notified you that it's time to sell the farm: the market is OPENLY being manipulated higher. I've detailed the manipulations on these pages previously— high frequency program trading, front-running, etc. But last week's trading action took things to a new level. Goldman Sachs is now openly flaunting their financial misconduct. They are literally allowed to commit financial crimes with impunity. Why?

Because the SEC, the federal government, the regulators, and the like have all FAILED to reform the system. They have failed to do anything to rein in the corruption of the financial markets. They have failed to enact any meaningful change. In the words of former SEC Chairman Harvey Pitt (from an interview with CNBC no less):

Those who sit back and think that they can rely either on the government or rating agencies or even third party experts, are making a huge mistake.

Harvey Pitt
Former SEC Chairman

This is why I did not issue an official "sell" last week. It's also why I have yet to notify you to sell this week too (although it's highly likely I will be doing so by the end of this week/ beginning of next). The market was openly gamed right in front of us.

Yet, while Goldman Sachs has succeeded in kicking off a short-rally in stocks… they've completely failed at reversing the market's trend in any real meaningful way:

As you can see, the S&P 500 has broken its rising bearish wedge pattern. It has now risen to re-test the bottom range of this pattern. This is classic "topping" behavior: once a trading range is broken, the range becomes a line of "resistance" (meaning it's difficult for the market to break above it) instead of "support" (meaning the market tends to stay above this level).

The below chart illustrates this point visually.

We are now at THE critical point for the market rally that began March 2009. If the S&P 500 DOES NOT break above the trend-line NOW, then the trend is BROKEN and we have a confirmed "sell" signal and it's time to go "all in" shorting this market.

The below chart gives a close-up of the last week's trading. It shows:

- The trend line of the rising bearish wedge to illustrate closely how the trend has now become a point of "resistance" instead of "support."
- How dramatic Friday's manipulated bounce in stocks has been: we were literally on the edge of the cliff before it happened.
- **How stocks absolutely HAVE to break above the trend line and break to new highs in order for the uptrend to remain intact.**

In simple terms, stocks are completely on borrowed time. If we do not see a MAJOR rally (3-5%) in the S&P 500 within the next 1-2 weeks, then the uptrend is over, and the Crash is imminent. **In other words, some serious buying will have to back up this latest manipulated bounce in order for the uptrend to continue.**

The Hardest Part of Investing

The only solution to this is to wait.

I know I've been saying the same thing now for three weeks. But it's the RIGHT thing to do. As the below chart shows, no one, other than day-traders, has made money from stocks in the last three weeks. Both the rallies and the dips last tops 2-3 days. And as the start of this issue indicates, the only ones making money from this volatility are those "in the know" who are legally permitted to front-run the rest of us with impunity.

On a side note, I want to point out that this kind of volatility (and manipulation) is IDENTICAL to that which occurred last year before the Crash (Sept-Nov '08).

The above chart is of the S&P 500's action for August 2008 (stocks began their total collapse September 2). As you can see, the market began a period of intense volatility during this month: price swings of 2%+ were common. Some of this was the market's response to the Fannie/ Freddie nationalization. But several of these rallies were the products of manipulation much like that of last Friday's.

Bottomline: the market is giving clear signs of "topping" out quite similar to those of last year. Stocks have broken below the rising bearish wedge pattern we've been tracking. They are now rising to re-test the trend line. If they DO NOT break above this line then we have a confirmed "sell" signal and it's time to go "all in" shorting the market.

I hate telling you to wait longer. Indeed, I was LITERALLY writing my "sell now" update on Friday when the market's explosive reversal began.

Having waited a full month to go short the market I can tell you that I WANTED very badly to send out the confirmed "sell" update… but if I had done so we would have lost money as the market exploded in our faces. This illustrates the ultimate maxim for investing:

The market DOES NOT care what you WANT to do.

Investing is all about doing the appropriate action, NOT what you want to do. If you invest based on "wants" you lose money. If you invest based on sound insights and what the market dictates, then you will make money. It's very, very simple, but less than 1 in 1,000 investors get it.

So sit tight regarding our current portfolio and "On Deck" trades. We have entered a critical time for stocks in the last 10 days. If the S&P 500 does NOT break back above its trend line in the next week, then we have a confirmed breakdown of the rising bearish wedge pattern, which means a confirmed "Sell" and time to go "all in" shorting the market.

We'll know the deal within a week. We were literally "there" last week before Goldman Sachs stepped in a kicked off a rally. When you're investing in a market like this (where the "rules" are different for various participants) you HAVE to wait for a confirmed signal, otherwise you risk having the market blow up in your face. Having seen this happen several times this year, I'm not going to allow it to happen again.

However, while things are still in "sit tight" mode for stocks, something wholly different is going on in the gold market.

The Flight From Paper

We traded gold a month ago for a quick 5% gain in the metal and a 17% gain in the mining stocks. When we first invested, I noted that:

*… **gold has formed a long-term inverse head and shoulders formation (two smaller collapses book-ending a major collapse)**. Typically a head and shoulders predicts a*

massive collapse. However, when the head and shoulders is inverse, as is the case for gold today, ***this typically predicts a MAJOR leg up.***

Indeed, any move above the "neckline" of 1,000 would forecast a MAJOR move up to $1,300 or so…

~The $24 Trillion Market Discount
Private Wealth Advisory Issue 17
8/26/09

Well, gold has broken the "neckline":

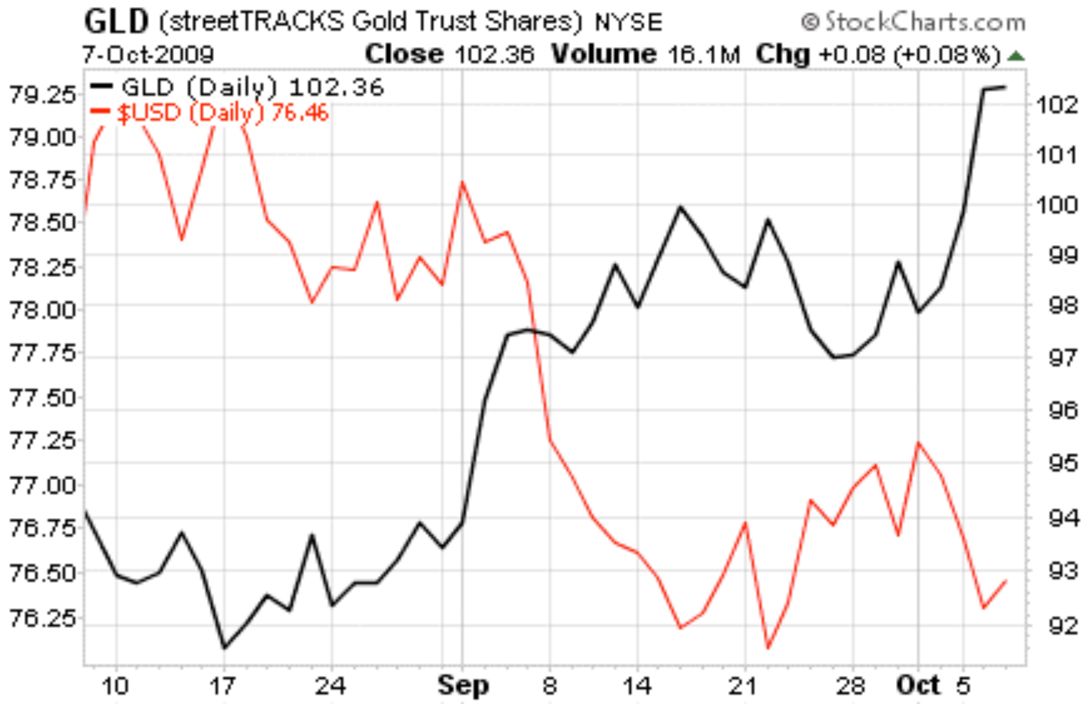
This indicates that the next leg up in the gold bull market has begun. The reason here is simple: investors have begun to realize that every central bank on the planet is hell bent on devaluing their currencies.

Everyone and their mother believes the Fed's actions are hurting the US dollar. But few people have taken noticed that the Europeans don't want a strong euro, just as the Japanese don't want a strong yen, just as the Swiss don't want a strong franc.

Why?

None of these guys want their currencies to appreciate too far against the dollar because most if not ALL of them export to the US. Having a strong currency against a weak dollar means increased production costs against a sales lower price. This means LOWER profitability.

To combat this, countries are either aggressively printing money to stimulate their economies (China, Europe, the UK) or openly manipulating their currencies (Switzerland) in an effort to devalue their money against the dollar. Case in point, this latest breakout in gold happened WITHOUT the dollar falling to a new low:



As you can see, gold broke out dramatically this week. But the dollar failed to fall to a new low. This tells us that investors are fleeing paper money in general, NOT just the dollar. This means that gold mania is now going global as investors flee paper money and pile into the one currency that CANNOT be devalued:

GOLD.

In simple terms, gold has begun its next major leg up. Based on the chart patter, this next leg should take the precious metal to $1,300 or so. So we're buying both the Gold ETF (GLD) and the Gold Miner's Index (GDX) again.

Action to take: Buy the Gold ETF (GLD)

Action to take: Buy the Gold Miner's ETF (GDX)

In conclusion, stocks have broken down below the rising bearish wedge pattern. They have since rallied to retest the upward trend-line thanks in part to manipulation by Goldman Sachs. The issue now is whether or not they break back into the trend-line (signaling that the rally has further room to run) or if they are rejected by the trend-line. If they are rejected, then we have a confirmed “Sell” signal and it is time to go “all in” shorting the market.

Meanwhile, gold has begun its next major leg up. We’re investing accordingly to profit from it.

I continue to monitor the daily fluctuations closely. As soon as it’s time to invest heavily, I’ll notify you via a special update. Until then…

Good Investing!

Graham Summers

OPEN POSITIONS					
Company	**Symbol**	**Buy Date**	**Buy Price**	**Current Price**	**Gain/ Loss**
UltraShort China	FXP	8/11/09	$9.98	**$9.19**	**-8%**
SHORT the Bank ETF	KBE	9/2/09	$21.60	**$23.32**	**-7%**
UltraShort NASDAQ	QID	9/2/09	$26.83	**$23.12**	**-14%**
Utilities ETF	XLU	9/16/09	$30.05	**$29.07**	**-3%**
Powershares Agriculture ETF	DBA	9/16/09	$25.45	**$25.13**	**-1%**
Gold ETF	GLD	10/7/09	$102.36	**NEW**	**BUY!**
Gold Miner’s ETF	GDX	10/7/09	$47.90	**NEW**	**BUY!**

On Deck Portfolio		
Company	**Symbol**	**What We Will Do**
Russell 2000	**IWM**	**Go Short**
Saks	**SKS**	**Go Short**