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Investment Strategy

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U.S. Markets	Close	Net	1 Day %	YTD %
Dow Jones	16272.01	-12.69	-0.08%	-8.70%
Dow Jones Transports	7832.70	47.07	0.60%	-14.30%
Dow Jones Utilities	569.59	-7.24	-1.26%	-7.85%
S&P 500	1923.82	3.79	0.20%	-6.56%
S&P 400 Midcap	1366.44	-2.47	-0.18%	-5.92%
S&P 600 Smallcap	647.03	-3.16	-0.49%	-6.91%
NASDAQ	4627.08	6.92	0.15%	-2.30%
Russell 2000 (Smallcaps)	1097.55	-3.13	-0.28%	-8.89%
BKX (Banking)	69.84	0.02	0.03%	-5.95%
BTK (Biotech)	3429.55	8.70	0.25%	-0.28%
XOI (Oil Index)	1067.60	9.24	0.87%	-20.81%
SOXX (Semiconductor)	595.62	-7.11	-1.18%	-13.28%
XAU (Gold/Silver)	45.20	-1.05	-2.27%	-34.28%

## "Bob Farrell"

In an era gone by, Bob Farrell went on to note, "Economists are unhappy because they do not know what to believe: this month's forecast of a strong economy or last month's forecast of a weak economy. Technicians are unhappy because the market refuses to correct." While currently technicians are not unhappy because the market refuses to correct, they are unhappy because of the trendless nature of the equity markets since the August lows. In fact, the title of Bob Farrell's original note was "Everybody's Unhappy," which certainly seems applicable for investors/traders over the past four weeks. The unhappy crowd can't figure out whether the stock market is trying to bottom or setting up for another new leg to the downside. Consequently, participants are not doing much of anything. That feeling was reflected in most of my institutional meetings last week in NYC. The portfolio managers basically wanted to be "flat" because if they make a "big bet" right here and they are wrong, not only do they have performance risk, but also bonus risk and ultimately job risk at year end. That mind set was noticed this week by the keen-sighted Jason Goepfert of SentimenTrader fame when he wrote:

Macro hedge funds have greatly pulled back on their exposure to the stock market. Looking at a popular hedge fund index and comparing it to returns in the S&P 500, it's clear that funds have pulled back greatly from where they were a couple of months ago, and are showing the least exposure to the market in two years, which has led to mostly positive returns in the months ahead.

And boy, do I hope Jason's data is right because I am tired of exercising patience and not doing much in the equity markets. To that point, I reflected on Bob Farrell's 10 Rules of Investing after recalling his report titled "Everybody's Unhappy." His rules are as timely today as they were 30 years ago! On the second page of today's *Morning Tack* I have reproduced those rules. I suggest you read them. Then read them again. In fact, take them and tape them to your desk because going forward they will save you a lot of money in the investment arena. This morning Europe is better (+1%), Japanese Household spending was better (+2.9% v +1.3%), England's Construction PMI beat estimates (59.9 v 57.5e), there are a bunch of Fed speakers today, but all of this takes a back seat to this morning's employment numbers. The consensus estimates I see are 203K, an unemployment rate of 5.1%, and wages increasing by 0.2% MoM. And that backdrop has the preopening S&P 500 futures better by 7 points at 6:00 a.m.

"Money managers are unhappy because 70% of them are lagging the S&P 500 and see the end of another quarter approaching."

... Bob Farrell, Merrill Lynch's retired legendary strategist

Index	Cur Future	Change	
Dow Jones	16,252	62	
S&P 500	1,925	7.7	
NASDAQ	4,208	20.3	
Volume	ADV/DEC		
1 Day Volume	Volume	Issues	
NYSE	1,015,826,852	1.1	
NASDAQ	2,140,730,000	0.9	
Foreign Markets	Intraday	Net	% Chg
U.K. FTSE 100	6,173	100.48	1.65%
Germany DAX	9,657	147.43	1.55%
Brazil Bovespa	45,313	253.93	0.56%
Japan Nikkei 225	17,725	2.71	0.02%
Hong Kong Hang Seng	21,506	659.79	3.17%
S&P Sectors	Close	% Chg	1 mo %
Consumer Discretionary	593.66	0.73%	2.61%
Consumer Staples	484.82	-0.02%	2.28%
Health Care	772.86	0.89%	-2.43%
Information Technology	663.26	-0.04%	2.33%
Telecom Services	140.14	-0.75%	-1.87%
Energy	451.58	0.06%	-3.20%
Financials	305.75	0.14%	0.48%
Industrials	431.03	-0.17%	0.45%
Materials	253.55	1.06%	-3.59%
Utilities	217.21	-1.19%	4.15%
Key Commodity Prices	Last	Net	
Crude Oil (WTI)/bbl	45.03	0.29	
Natural Gas/mmbtu	2.41	-0.02	
Gasoline (USD/gal)	1.34	-0.02	
Gold/oz.	1106.10	-7.60	
Silver/oz.	14.42	-0.09	
U.S. Dollar Index	96.33	-	
Copper (USD/lb.)	2.32	0.01	
Cotton #2 (USD/lb.)	60.86	0.26	
Market Valuation	2014	2015E	2016E
Consensus S&P 500 EPS	\$113	\$111	\$129
P/E	17.0	17.3	14.9
Earnings Yield		5.8%	6.7%
Equity Risk Premium (10 yr)		3.7%	4.7%
Treasury Yields	90D	10 Yr	30 Yr
	0.02%	2.04%	2.85%

Source: Thomson Reuters Data as of: 7:21 AM



Source: Thomson

## Bob Farrell's 10 Rules of Investing

- 1) Markets tend to return to the mean over time.
- 2) Excesses in one direction will lead to an opposite excess in the other direction.
- 3) There are no new eras – excesses are never permanent.
- 4) Exponential rapidly rising or falling markets usually go further than you think, but they do not correct by going sideways.
- 5) The public buys the most at the top and the least at the bottom.
- 6) Fear and greed are stronger than long-term resolve.
- 7) Markets are strongest when they are broad and weakest when they narrow to a handful of blue-chip names.
- 8) Bear markets have three stages – sharp down, reflexive rebound and a drawn-out fundamental downtrend.
- 9) When all the experts and forecasts agree – something else is going to happen.
- 10) Bull markets are more fun than bear markets.

I would pay particular interest to rule number 8, because given the Dow Theory “sell signal,” that is what I am worried about. It looks something like this chart from 2009:



Source: Stockcharts

**U.S. Markets Index Information:** *U.S. Treasury securities* are guaranteed by the U.S. government and, if held to maturity, offer a fixed rate of return and guaranteed principal value. The *Dow Jones Industrial Average* is an unmanaged index of 30 widely held securities. The *Dow Jones Transportation Average* is the most widely recognized gauge of the American transportation sector. The *Dow Jones Utility Average* keeps track of the performance of 15 prominent utility companies. The *S&P 500* is an unmanaged index of 500 widely held stocks. The *S&P Mid Cap 400 Index* is a capitalization-weighted index that measures the performance of the mid-range sector of the U.S. stock market. The *S&P Small Cap 600 Index* is an unmanaged index of 600 small-cap stocks. The *NASDAQ Composite Index* is an unmanaged index of all stocks traded on the NASDAQ over-the-counter market. The *Russell 2000 index* is an unmanaged index of small cap securities which generally involve greater risks. The *KBW Bank Sector (BKX)* is a capitalization-weighted index composed of 24 geographically diverse stocks representing national money center banks and leading regional institutions. The *NYSE Arca Biotechnology Index (BTK)* is an equal dollar weighted index designed to measure the performance of a cross section of companies in the biotechnology industry that are primarily involved in the use of biological processes to develop products or provide services. The *NYSE Arca Oil Index (XOI)* is a price-weighted index of the leading companies involved in the exploration, production, and development of petroleum. The *PHLX Semiconductor Sector Index (SOXX)* measures the performance of U.S.-traded securities of companies engaged in the semiconductor business, which includes companies engaged in the design, distribution, manufacture, and sales of semiconductors. The *Philadelphia Gold and Silver Index (XAU)* is an index of 16 precious metal mining companies that is traded on the Philadelphia Stock Exchange.

**Futures:** Futures prices are current as of the publication of this report, but will fluctuate. Please contact your financial advisor for updated information.

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