High Desert Investment Advisors

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Serving Your Personal Investment Needs Since 2003

Tuesday, August 2, 2011

Today was one of those days when I would have liked to see a flat to positive close for the day. Needless to say, that was not the case. The market was down pretty hard, and it went down with some volume. What that says is that there was a movement to the sidelines by those traders who had been holding out for the rally – the one that was to be based upon second half GDP growth.

The Commercial Paper data, which I follow as part of our model, seems to be reacting very sharply to what has been going on in Washington D.C. It dropped significantly, probably indicating a reluctance to spend money on inventory, and a caution toward the future, due to all of the uncertainty about the future. This and other economic numbers I follow tend to have some volatility, but when they do move like this, one must take notice.

The economic numbers are forecasting a slowdown after the end of 2011. If this trend continues, it may be possible to slip into another recession, along with negative economic growth, all beginning in this current quarter.

What will precipitate this recession? It is likely to be focused in the European banking system and caused by sovereign debt restructuring (or threat of such restructuring). Sovereign debt is at issue. The concern is the rapid growth of such debt and the ability of specific governments to generate sufficient revenues, in order to make principle and interest payments when they are due. Italy is already feeling the pressure, as interest rates on Italian Government debt are rising. Spain is likely to be the next target. The potential losses from default by one or more of these countries will dwarf the EU reserve fund currently in place to defend against such an event.

That being said, what I am describing here, are only trends based upon current data; that data is then smoothed (averaged) into the future, in order to see where that trend leads. Such a trend is subject to change every time a new set of data is released, and is constantly being updated.

**(It got too late for me to continue and now it is mid-morning Wednesday, August 03, 2011.)

The outline of the above really begs the question of “how much am I going to lose if the market does not turn around and rally?”
Of course, there is no real answer to this question. The answer is subject to change, depending on your criteria for selling your equity positions and going “flat” the stock market.

The modeling process we use is perhaps a week away from recommending a sell order, indicating that the long term trend has not changed as of this date. Effectively, what the model is telling us is that it is too early to know if the trend has changed from an up-trend to a down-trend.

The model strategy is designed to preserve capital as market trends change to a down-trend. It is also programmed to move back into the stock market when those trends return to an up-trend.

RECOMMENDATION:
For now, I think that it is too early to be selling out of equity positions (stocks and mutual funds). The market is very oversold and is likely to have a rally soon. The economic fundamentals are positive, and the debacle in our Nation’s Capital is fading. All of this would suggest that now is a time to be patient. The

caveat to this statement is to be ready – ready to sell when it is clear that the market trend has changed to a down-trend. This trend change could be confirmed within a week, it the change is truly to happen. Needless to say, I will let you know if the trend does change!

NOTE: I know that there is plenty of concern about market conditions and about your investment risk. Please call me or Iris and talk about your concerns. If you want to move your equity investments to the sideline, into cash – if that is what will make you feel more comfortable – let's do that. What is important is that you are comfortable with your investment risk.

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Sincerely,

Dick Brackett
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