WallStreetWindow PowerInvestor

Where We Are In The Bear Market (09/20/2015)

BIG ANNOUNCEMENT.

I have a special free bonus for you. I am releasing a new book titled The Stock Market Bubble Bust of 2015 and Beyond. As a Power Investor member you can get a free kindle copy of this book to download on your computer or reading device today. I have the book on Amazon available for free until Tuesday night just for you to do this. I'm not going to announce the release of this book until Wednesday to give you time to grab it for free first. To get it go here:

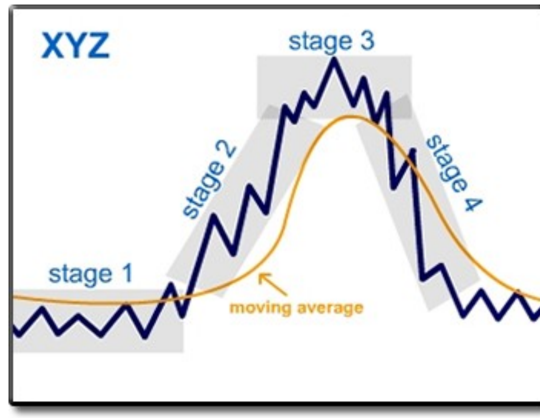
http://www.amazon.com/gp/product/B015KUUJ2I

I will have the link at the end of this report too.

Ok now back to our regular weekly update.

So much for "lift-off." Do you remember that phrase? It had been the media meme promoted by Federal Reserve officials for most of this year. They gave it to Steve LIESman and he started to deliver it to the masses back in January on CNBC. Wall Street analysts and CNBC guests then repeated it over and over again. It was a wonderful propaganda phrase and the masses of stock market bubble bulls ate it up.

What the idea of "lift-off" meant was that the Federal Reserve through its policy



STAGE ANALYSIS OF KEY MARKETS

S&P 500

Long-term: Stage Four Bear Market

Short-term: Bear market rally ends, next move is down.

Gold Long-term: Stage One Base

Short-term: Gold basing now with key resistance at $1,175 area.

DBA ETF

Long-term: Potential Stage One Base

Short-term: Beginning to perform better than the S&P 500.

of zero interest rates had finally achieved a "lift-off" for the US economy. This meant that the US economy was going to begin to really boom in the second half of the year and that the stock market would totally take-off. Bubble bulls believed that "lift-off" meant that the US stock market would breakout to new 52-week highs and surge like a rocket while the Federal Reserve would start to raise rates just enough to confirm that the economy was finally back on track after years of misery, but slow enough that it wouldn't hurt the stock market.

Back in February Steve Liesman and CNBC stock market bulls were claiming that "lift-off" would probably be achieved by July. But then as July came they said the Fed wasn't ready to raise just yet, because the Fed wanted to see more good data for total confirmation and were now "data dependent." You see in the second quarter earnings for corporate America actually shrank by two percentage points. Now the masses didn't think much of this, because CNBC reported that companies beat lowered analyst estimates so they used that as news to excite them. The last thing Wall Street wants is for people to think too much about what they are investing in. What they want is for people to buy and believe.

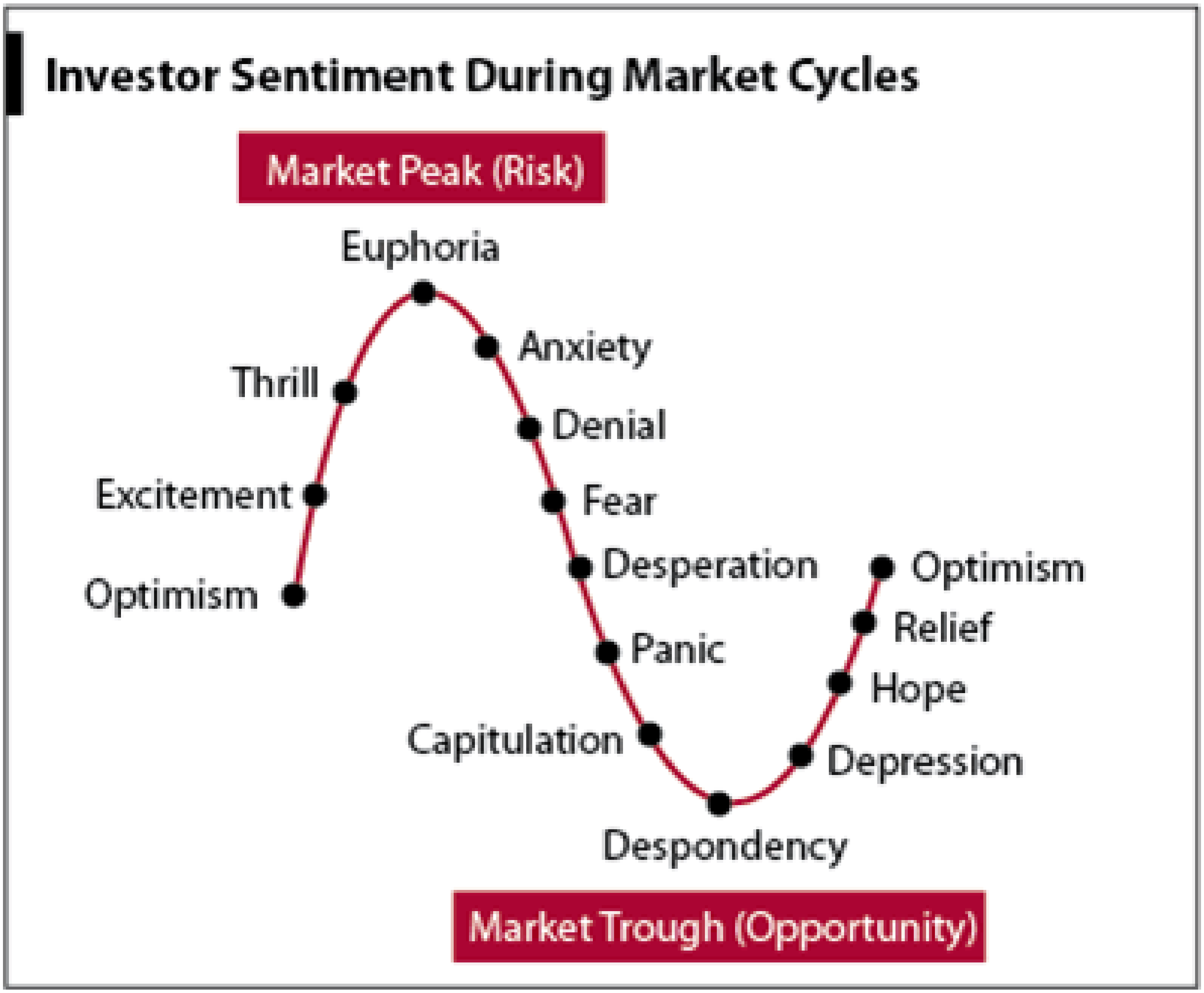
But as August came the phrase "lift-off" still dominated the financial media. And then of course we know what happened next. The US stock failed to breakout and instead broke down at the end of August to begin a new bear market as the US stock market averages fell below their 200-day moving averages. Three days later the DOW gapped down 1,000 points on the open.

And now today the phrase "lift-off" seems like a horrible joke. So it has totally vanished from CNBC reporting. And the masses have completely forgotten about it. The phrase has simply left their consciousness and they make their decisions based on so little real thought that they cannot even remember it.

The point is that the phrases used in the financial media to explain what is happening in the markets are of very little substance. So this year Wall Street economists were predicting a big second half earnings growth based on a belief in the phrase "lift-off." Now suddenly the analysts are guiding down estimates for the third quarter to show that companies earnings shrank again by the tune of 4.4%. This is twice as bad as the shrinkage they had in the second quarter of this year. So "lift-off" has turned into a giant hoax.

You can get the details on these earnings estimates here:

http://www.factset.com/websitefiles/PDFs/earningsinsight/earningsinsight_9.18.15



This isn't the first time the economy has failed to match Wall Street predictions. In fact in each of the past four years economists claimed a second half boom was going to come at the start of the year and each year it didn't come. In fact last year we even saw retail sales decline during the holiday. So in February the economists said everything was slow, because of the weather but would still boom later. And now there is no boom, so I guess it wasn't the weather's fault after all.

In reality what happened is these experts wanted to believe that the stock market would keep going up so they simply assumed that "lift-off" was coming. They wrote the story themselves and believed in it and fed it to the masses. Take a look at the graphic above, because it is very important to understand this to know where we are in this bear market cycle.

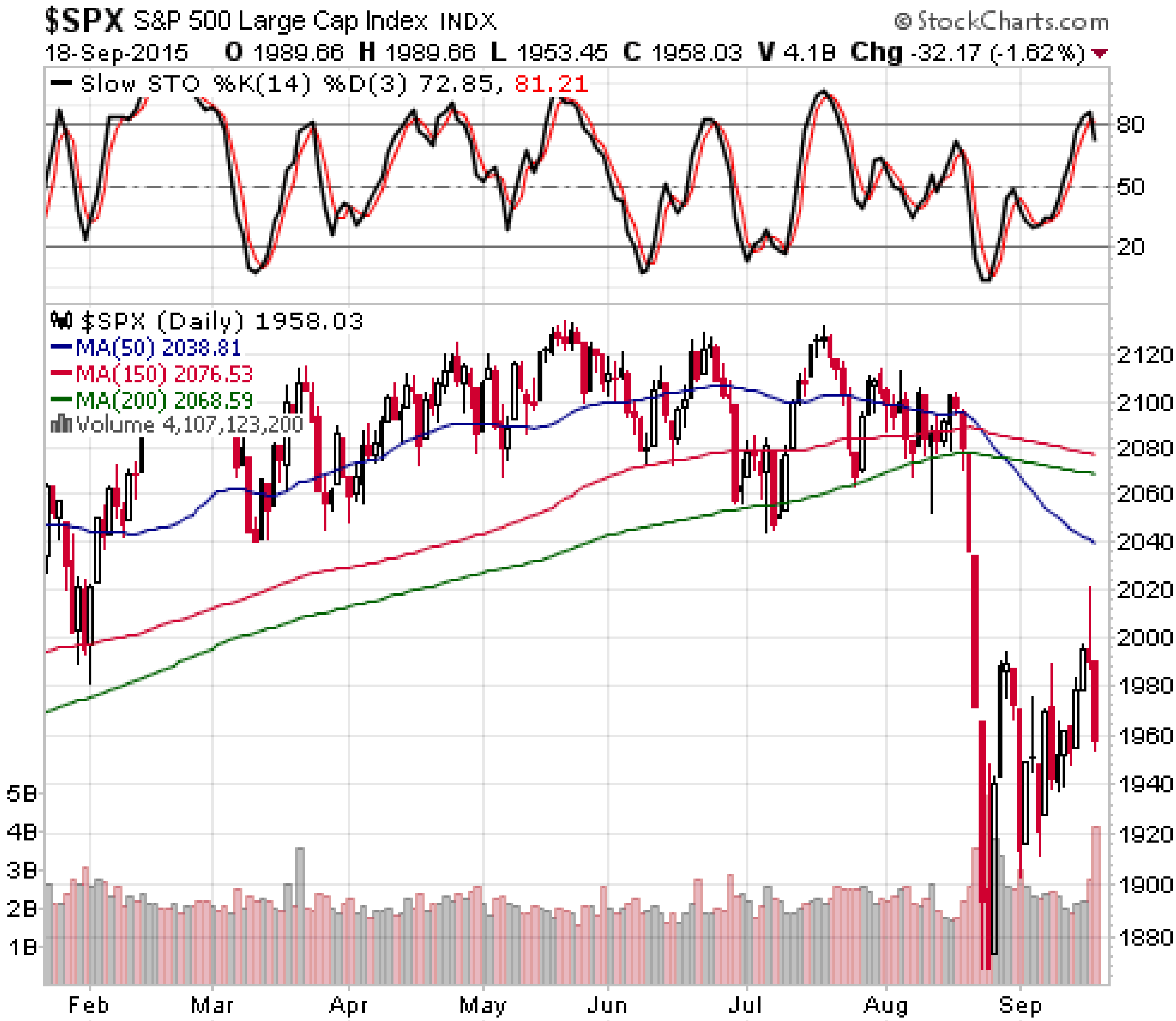
This is the psychological cycle that the masses go through as a stock market cycle plays out. When the last bull market began it wasn't really until 2012 that the masses became excited about the stock market. In fact more individual investors withdrew money from the stock market and put it in bonds from 2009 up till the end of 2012. And then the stairway to heaven rally began as the US stock market went up at a 45 degree angle without any pullback until October of last year. That move caused people to become optimistic, excited, and then even thrilled over the stock market. They became so thrilled by it that they came to believe that stock market valuations no longer meant anything anymore when it came to making investing decisions. They believed that stock market cycles had become abolished and that President Obama and Janet Yellen had perfected management of interest rate policies and the economy so that no bear market or economic recession could possibly ever happen again. With this belief system they now convinced themselves that the stock market would go up forever without ever pulling back again.

It was in May of last year that I was at the Las Vegas Money Show and witnessed in the main conference hall speaker after speaker predict huge gains to come. When one speaker said that the stock market would go up for seven more years the audience stood up and started to cheer and holler. I had never seen that happen before at an investment conference. These people were stomping and carrying on for minutes and the speaker had to tell them to calm down several times so that he could continue talking. He had worked them up into a bull frenzy!

I walked around talking to people there and not a single person had any concerns at all about the stock market. The individual investor who had been cautious on the stock market from 2009-2012 had transformed himself into a bubble bull.

But then last year the market did have a little pullback in October. But that pullback was of such a short duration and the market bounced back up so quickly that the masses of bubble bulls now went into a state of pure euphoria. Now they had confirmation that the stock market not only wouldn't have a real pullback again, but in their mind couldn't.

And this state of euphoria continued even though most stocks in the stock market now began to fall into bear markets as internal deterioration rotted away at the insides of the stock market averages. But CNBC and "Fast Money" boys focused solely on whatever was hot and kept everyone's eyes on the bubbles. So they pumped biotech for a few months. Then financials for a few weeks. And then in July when the market topped out and the only thing still going up were a half dozen tech stocks in the Nasdaq 100 they focused on them and only them. And the bubble bulls continued to believe as they enjoyed feeling euphoric about the market and dreaming big. They did not want to think too much about anything. They believed they no longer had to. All they needed to do was to continue to believe



in order to continue to feel good about the market. They enjoyed their euphoria and to sell would to mean to stop flying high.

But then in August the market fell hard as the S&P 500 and Nasdaq fell below their long-term moving averages in a way that they in fact never had done before in stock market history off of a top.

It happened so quickly that it took everyone by surprise. People simply woke up one morning to see the stock market gap down huge on the open. Their euphoria vanished instantly. And now they went into a state of nervousness. Perhaps the people that had been warning them that a bear market was coming were right some of them may have thought in the back of their minds. People became anxious.

But a few days went by and the market rallied. So now they went into a simple state of denial. CNBC told them that this was just a correction like the ones they saw in 2010 and 2011. In 2010 there was a flash crash that made no sense. So the market shouldn't have fallen then and so it went back up they told themselves. And this was a flash crash again that should not happen they now convinced themselves. All of the signs that this is a bear market they now pushed out of their brains in order to remain in denial. The bubble bull had now transformed himself into a neurotic gullabull who works to deny reality in order to continue to simply feel good about the stock market and his investment positions. He chooses deliberately not to think or work, because making changes in his accounts to adjust to the new stock market environment would mean taking personal responsibility for his investment decisions. And the masses do not want to do that. They want the market to simply go up forever for them and for Janet Yellen to make that happen. So they look for reasons to do nothing and that means they have to block out reality in order exist in denial of the new market trends now in place.

This is in essence what we have seen people do so far this month. They were anxious on the drop in August, but quickly went from a state of anxiety to a state of denial during the bear market rally as they convinced themselves that this was just another correction. And they had plenty of people telling them that and since they saw this on their television boxes it had to be real. But it wasn't.

As the market goes lower the next psychological state people will enter is one of fear. As the stock market goes towards its lows people will continue to hold in hopes that the market will go back up, but they will do so with fear in the back of their minds, because they do know subconsciously that the market could fall into a disaster if it breaks those lows. But they will not want to think too much about it. They will be frozen in fear of making a mistake if they get out and feeling like a failure. Remember the gullabull cannot take responsibility for his own investment decisions. This is his true greatest fear. He fears making a mistake more than he does losing money. So to miss out on a rally for him is the worst thing that could possibly happen to him.

But once the stock market breaks its low of August, which I think it will, most likely in October, the gullabull will enter a phase of desperation as the losses pile up on him.

The masses right now are looking for reasons to believe. And they are totally ignoring market trends and charts to do so. Even those that have read books about technical analysis or listen to people who explain what is happening to them simply ignore what they are hearing, because they feel uncertain about what is happening. One day they see the market up so they start to believe again in the bull market. Or they hear an expert on TV tell them the market is great and they have trouble believing in their own judgment so they sit in fear. In reality what most people really do when it comes to deciding on whether the stock market is bearish or not is simply look at their account balance.

People are willing to hold for a ten percent loss. CNBC tells you that markets fall ten percent and it is no big deal. They say though that a twenty percent drop is the definition of a bear market. And we are not at twenty percent yet.

But once the stock market falls twenty percent and people get statements in the mail showing that they have losses of that size people will then recognize and accept the reality of a bear market. It is at that moment that people will move from holding on in desperation to going into a state of panic.

This is where that dangerous crowd I witnessed at the Las Vegas Money Show is heading to. It is why when I left that conference I wrote a monthly newsletter about it and declared that I had witnessed a dangerous herd form in the stock market.

And it is that herd that is going to generate waves and waves of selling that will smash the stock market once it falls 20%. That level is 1,705 on the S&P 500 and 14,680 for the Dow.

Panic will come once those levels are broken and that selling panic is not likely to last a few days like the drop in August did, but for several weeks as the individual investors go into a selling capitulation.

Think about this. Just in July the masses were in a state of euphoria over the stock market. That psychological state began for them really in November. And now in perhaps a few months we will see them go into panic and capitulation. Most of those people I saw in Vegas last year will end up selling out of the stock market forever.

There are two points I want to make out of this. First of all this bear market is already playing out much more quickly than the last two did. Both of those bear markets lasted over two full years. The average bear market before them though lasted about 15 months. The psychological shifts in the last two bear markets took more time to occur. It took more time for people to go from anxiety to denial and to fear. For example the market declined slowly from October 2007 to January 2008 for almost 90 days before the VIX spiked above 35. In August it did this in four days. Really the fear state in the last bear market did not come until the Fall of 2008. But now we may see that state of the bear market begin next week.

Secondly, most people that invest in the financial markets do so on pure emotion with zero real thought or analysis to what they are doing at all. They simply respond to daily price gyrations and whether their account balance is going up or down and then come up for mere rationalizations to justify their actions. That's why so many people simply believe in slogans such as "lift-off" in order to explain to themselves why they continue to believe that stocks will go up.

It's why people ignore charts and trends even if they have learned how to read them. They see with their eyes, but they only make decisions based on emotion so do not use logic.

This is not a way to make money, because all it does it cause one to repeat the psychological patterns of going from euphoria to capitulation over and over again.

In order to escape that cycle you have to learn how to read market trends and have faith in your own brain and thinking processes and abilities. You have to believe in yourself instead of the Wall Street slogans thrown at you by your television box that everyone else believes in. You have to walk away from the stock market herd and slam the door on it forever and not care what they say about you, because if you do not you will end up on the wrong end of a selling crash with everyone else.

These reports can help you do that. Now as far as the market goes now I am convinced more than ever that we are in a real bear market. We just saw a bear market rally that ended last week on a reversal day on the stock market following the Fed decision when the S&P 500 spiked up to 2,020 only to close at 1,990.

Now that the bear market rally came to an end we can now expect the market to begin towards its lows of August. I cannot predict though what it will do Monday or if the DOW can't pop up 100 or 200 points up first or if it will just simply go straight down. However, if you have no positions against the stock market you can buy any of the short ETF's, such as DXD, SDS, or QID, and place a stop on their lows of last week. You

also can short individual stocks and place stop loss orders on their recent highs. Or buy a put package on long positions you do not want to sell to completely hedge yourself. You can protect yourself from a selling crash that can come when the masses go into a selling frenzy later. And you can position yourself ahead of time to profit from further declines in the stock market. That is what I have done with my own accounts and the model rebalancing portfolio, which is invested 20% each in SDS, DXD, QID and GDX and CEF.

My guess is that we are going to see the market averages go back down to their August lows by the end of this month or the very beginning of October and then have a very short-lived bounce above them for a few days and then simply turn down to go through them to have a drop down to those magic 20% levels of 1,705 on the S&P 500 and 14,680 on the DOW. Perhaps we'll have a bounce off of those levels before the market goes through them, but once it does I think that is when we will see real big selling hit the stock market.

This whole process could play out with some sort of slow decline taking place week after week into the end of this year or with a sudden selling collapse like we saw in October and November of 2008 this fall. There simply is no way that I can predict exactly how things are going to unfold. But we do not need to do that in order to adapt and profit from a bear market drop. All we need to do is accept that we are in a bear market and know that means the market is going to go much lower than anyone expects and position ourselves accordingly. And now frankly is the time to do it if you did not do that back in July.

I have some individual stocks you can bet against in a moment. First I want to tell you what I'm really interested in watching this week in the financial markets. I actually am not that curious about what the US stock market is going to do this week. I'm convinced it's a bear market and that the bear market rally ended last week, so what it does tomorrow doesn't really matter much to me personally.

What I am more curious about is what gold and mining stocks may do this week. You see every time the US stock market goes into a bear market a new bull market always starts in a few sectors of the market or in an entire asset class. In 2000 it was tobacco, utility, and REIT stocks that came out of stage one basing phases to begin a new bull market that spring just as the US stock market rolled over. In 2007 bonds turned up in August. Now gold, silver, and mining stocks have been in a stage one base for the past few months and have actually been outperforming the US stock market averages ever since the Nasdaq peaked on July 20. And that very same day marked what appears to be a capitulation bottom in mining stocks. So take a look at this chart carefully.

The key thing I have my eye on is the gold/S&P 500 relative strength ratio. This ratio has been in a downtrend since gold peaked out in 2011 when it ended its last bull market cycle, but turned up after the Nasdaq topped in July. If gold goes through its last peak of $1,160 while the stock market goes down then this ratio will go through its August peak too. That would mean this ratio will do something it has not done in four years and make a higher high to begin a new uptrend.

Gold's 200-day moving average is at $1,181. If this ratio goes up and gold goes through its 200-day moving average then it will begin a new bull market. Money will simply shift out of the stock market and into gold.

With the Fed's failure to raise interest rates last week all the signs are on the wall that the Fed has trapped itself. Once the stock market goes lower then any notion of them raising rates will disappear for once and for all in the minds of the masses and be replaced with a desperate cry for the Fed to print money to try to make the stock market go back up for them.

The Fed has spent most of this year talking about "lift-off" and trying to convince people that it is going to raise rates at the end of this year. The phrase "lift-off" has now been removed from the CNBC talking points. This fact and the fact that the Fed could not raise rates last week is a sign that it is abandoning its supposedly "tight" monetary policy. This should prove to be a positive for gold and mining stocks.

In 2000 gold started a bull market in the Fall of that year as the stock market declined and the Fed lowered rates in January of 2001. Another decline in the stock market now could also prove to be bullish for gold.

It was last week. After the Fed failed to raise rates gold jumped up and mining stocks rallied over 4%.

Now I do not believe one should be 100% long in this market or 100% short and that is why I have 40% of my money in long positions by having 20% in GDX and 20% in CEF in the model rebalancing portfolio. With the position all of these markets are in right now I believe this is a good time that one could duplicate the model rebalancing portfolio if one wanted to do that with a portion of their money. Remember the key way that the portfolio works is to rebalance the positions using the Friday closing prices so that it maintains the fixed allocation percentage in the ETF's it is invested in.

However, I am very curious to see what gold and the mining stocks do this week. If the gold/spx relative strength ratio breaks out then I will be convinced that the action we saw last week was not just a temporary pop for gold, but the start of a new real bull market. If that happens I'll start to make recommendations in individual mining stocks. It'll actually be an exciting time to buy into precious metals and mining stocks. And just as when a bear market starts the masses think the first dip is just a correction when a new bull market starts no one cares. And that certainly is the case with the metals and mining stocks.

Gold tends to go up first in a commodity cycle. So if gold goes into a new bull market then I expect we'll see other commodities and commodity ETF's such as DBA and RJA follow afterwards. So I'm going to be watching them closely too. Typically in a commodity bull cycle oil and energy go up last so I still do not think they are going to go up until next year and would stay away from oil stocks.

Now there are a lot of people claiming that a giant wave of deflation is coming and I got several emails asking me about that. My answer to that is NEVER EVER base your investment decisions based on what someone is predicting about the economy, because I have never seen anyone be able to predict that with any degree of accuracy at all. I have my own opinions on what the economy is going to do and theories I have read about what reasons a bear market may come are, but in the end I do not make any decisions based upon such ideas, but only based upon the charts and trends.

Personally I think deflation is a giant myth. We saw commodity prices fall for the past few years, but now commercial hedgers are barely short most commodities in the futures market. What is more a falling stock market should be bullish for gold and commodities as it is going to make people call out for more Fed money printing and in a falling stock market and bubble in the bond market that money is likely to flow into gold as a safe haven and drive up commodity prices as a result.

But that's my theory. Let's see what the market does. The bottom line is if the gold/S&P 500 ratio breaks out then we will know that gold is diverging away from the broad US stock market and going up into a new bull market. That's all we need to know. This deflation and inflation debate people like to have is meaningless when it comes to making money.

Don't forget to get my new book. It's free for you until Tuesday night. To get it go here:

http://www.amazon.com/gp/product/B015KUUJ2I

As far as individual stock ideas go. Here are some stocks that provide good entry points now to make bets against them.

I have found that the best stocks to short after a bear market rally are stocks that simply fail to rally with the market and have declining on balance volume, which means that there is more volume on down days than there are on up days. When you combine both of these factors together you have stocks that are lagging the market with signs of distribution. Retailer KSS is one such stock. You could short it now and place a stop loss order on it above

$52.50. You also could purchase January puts on it at a strike price of $47.50. They last trade on Friday for $2.50.

WMT has become one of the worst performing stocks in the DOW as there has been no real recovery this year for the American consumers as was predicted by in January when CNBC talked about economic "lift off." WMT can be shorted now with stop loss order placed above its recent high of $67.00. You also could purchase December puts on WMT with a strike price of $62.50. They last traded on Friday for $2.40.

AMGN was once one of the hottest stocks in the S&P 500 this year as biotech stocks became the final fad sector turned into a bubble by stock market bulls. Now since the Nasdaq peaked in July AMGN has been a laggard and still has a long ways to drop. It can be shorted now with a stop loss order on it placed above its Thursday high of 156.34. You also could buy a Janury put option on AMGN with a strike price of $150.00. They last traded on Friday for $10.00.

I believe all of these stocks are going to get smashed before Thanksgiving along with the overall stock market.

My goal is to hold my short positions through October and probably well into November while being on the lookout now for new uptrends in other sectors and markets to focus on. The increase in market volatility may destroy many stock market bulls who are in denial about what the volatility represents. Remember the spikes in volatility and crazy swings are a part of bear markets, but they also create big opportunities to make money for those that align themselves with no trend of the market.

MODEL REBALANCING ETF PORTFOLIO ALLOCATION

9/19/2015: No changes this week, beyond regular Friday rebalancing.

7/31/2015: Purchase DXD. Portfolio now 20% each SDS, QID, DXD, CEF, GDX.

7/30/2015: Purchase SDS and QID.

7/27/2015: Liquidated DBA position for cash.

5/12/2015: I purchased a 20% position in the agriculture commodity ETF DBA @ 22.44. The model portfolio is now currently invested 40% in cash, 20% DBA, 20% CEF, and 20% GDX. This is the update I posted on the site about this purchase.

http://www.wallstreetwindow.com/powerinvestor/?p=1402

What I am looking to do is own up to 5-6 ETF core ETF positions at any one time with 20% - 18% invested in each one and to maintain that allocation percentage by rebalancing the core positions portfolio every Friday at the closing price.

This is what I plan on doing with the bulk of my real money over the next few years. As for individual stocks I consider them for now as more speculative and outside of the core positions portfolio

For more on how this strategy works read my January monthly newsletter:

http://wallstreetwindow.com/wswmonthly/wswmonthly01012015.pdf

Also see module 7 of my “Bear Market Power Pack” for several videos and academic papers about this market strategy:

http://www.wallstreetwindow.com/powerinvestor/?page_id=1346

For an excel file keeping track of the portfolio go here:

http://wallstreetwindow.com/reports/coreportfoliotrades.xlsx