WallStreetWindow Monthly

The Most Influential Financial Newsletter Read By Over 500 Hedge Fund Managers and Thousands of Elite Investors ~ August 1, 2011

Stock Market Barometer

Quote of the month:

"As for taxes, the Tax Foundation reported that from 1986 through 2009 (the most recent year for which data are available), the share of federal income tax paid by the top 5% of income earners rose from 43% to 59%, while those who paid zero income tax or were net recipients of income from the government rose from 18.5% to 51%. " - William Fleckenstein.

Go Away Debt Default Fears for Now! —Mike Swanson

On Friday the DOW Jones Industrial average closed to post its worst weekly loss in over a year. Negotiations between Republicans and Democrats in Congress and President Obama have dominated the news stations and radio talk shows. There has been hand ringing on CNBC over the issue, with some of the talking heads on that channel blaming the politicians for the losses in the stock market.

However, if you flip and look at the market for Treasury bonds you'll find that Treasury bonds zoomed up in value while yields fell to a low of the year for the 20-year Treasury bond. If bond investors were scared of a debt default then they would be driving interest up instead of down. There are a few reasons why they aren't so worried.

For one thing Credit Suisse calculated that if the US did default on its debt this week then stocks would crash by 30% and the GDP would shrink by 5%. It's simply unimaginable that they would let this happen - especially when they bailed out Wall Street banks to the tune of a trillion dollars three years ago in much less dire circumstances, in fact some argue with good reason that alternatives to the bailout money could have been proposed instead.

Most Wall Street players are confident that Bernanke has now put a "Bernanke put" on the stock market and won't allow the market to fall into a bear market. According to Fortune, Bank of America Merrill Lynch surveyed its 265 big fund managers managing over $800 billion and they all agreed that if the S&P 500 hit 1100 than the Fed would announce a new round of quantitative easing.

So with such confidence in the Fed on the part of Wall Street there really isn't much worry in the bond market. In fact such beliefs may actually be a sign of overconfidence and not fear. I remember people back in 2000 thought that Greenspan would never let the market fall. That belief was backed up by three years of Fed action to help global markets in the wake debt problems in Asia, Russia, and the blow up of the Long-Term Capital Hedge fund so there was reason for people to convince themselves that a "Greenspan put" existed. It existed - it just lost its effectiveness at some point.

But if the financial markets aren't really worried about a debt default then why did stocks fall last week?

Well you have two reasons.

First of all recent economic data points to an economy that is barely growing in what is supposed to be a booming recovery. All the Fed money printing and government spending failed to create a sustainable recovery. Second quarter GDP numbers were released Friday and showed that the economy grew at only a 1.3% annual rate in the second quarter, which is well below the rate of growth needed to lower the unemployment rate.

At the same time the Fed's crazy inflation gauge – which understates inflation by stripping out food and energy costs – went up at the rate of 2.1% in the second quarter. What happened is energy prices went up so much that they helped to drive up the cost of everything anyway. Gas went up to $4.00 a gallon in May, which was its highest level in three years.

The government also lowered its estimate for first quarter GDP growth to 0.40%.

Stagflation anyone?

Consumer sentiment also has fallen to its lowest point in two years.

So we have a stock market that is really caught in the crosswinds of two forces – belief that the Fed will make it go up if it falls again and the reality of a weak economy. Both forces are pushing the market up and down and so far this summer have prevented it from falling into another bear market or having a sustainable rally that lasts more than a few weeks.

All of the recent price action in the market has to be put in context with the sideways phase that the stock market has been going through all year. Yes we saw the market make a new high in April and go up

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for about a week afterwards, but other than that move every time the market averages have gotten near their 52-week highs they have backed off, so with or without the news of possible debt defaults and bad economic numbers this past month, I would have expected the stock market to pullback a bit any-way, because we started the month of July out near its 52-week highs.

Now we are probably near the end of this recent pullback. On Friday all three major market averages ei-ther hit their 200-day moving aver-ages or got near them and bounced. At the same time we saw the put/call ratio close above one and the VIX make a nice jump higher, which indicated that there was some fear among options traders regarding the market. People were either hedging positions or else making bets that more selling was to come.

To me that tells me that for the short-term there isn't much down-side to this market. Get a debt limit agreement and we should get a move back up in the market for a few days.

However, the market is still likely to continue to go sideways a few weeks before it can muster up enough energy to make a run through the highs of the big trading range it has been stuck in for months.

Hopefully this will happen before this month is over or in early Sep-tember. Then we should get a nice Fall rally in the markets.

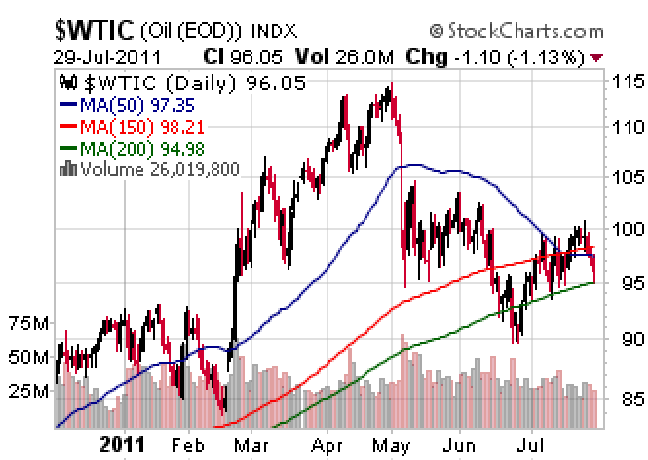
Until then the best thing to do is not to try to trade the broad mar-ket averages, since they are in a choppy environment, but to just try to focus on individual stocks.

So in short this month I'm looking for a short-term rally that lasts for a few days on the back of a debt limit agreement, then some sideways action in the market again for a few weeks, and a breakout to new highs by the end of this month or early September. That means we should get a good buy point this month.

What stocks will likely lead the market going forward? I'd keep a close eye on energy stocks as they have led the market higher all year and will likely continue to do so. Due to the weak economic data we can expect the Fed to keep interest lows and perhaps even start to speak of a QE 3 in some form or an-other by the end of the year. More money printing will continue to help commodities in the long-run.

Sectors & Stocks

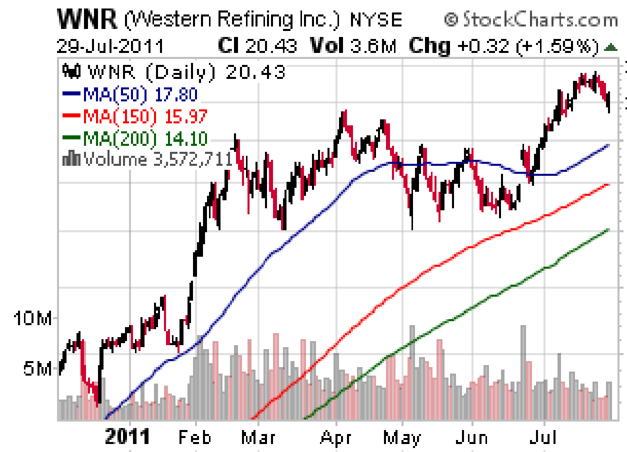
The chart above shows a consolidating market. This trend will eventually be broken, making it clear what course of action should be taken to position ourselves for the next trend. As for now we are looking for opportunity in the sectors and most importantly the stocks outperforming the market. Looking thru some of the best performers for the past month there were several oil stocks that have gotten themselves in a position to potentially be nice trades going forward. Below is a chart of OIL.

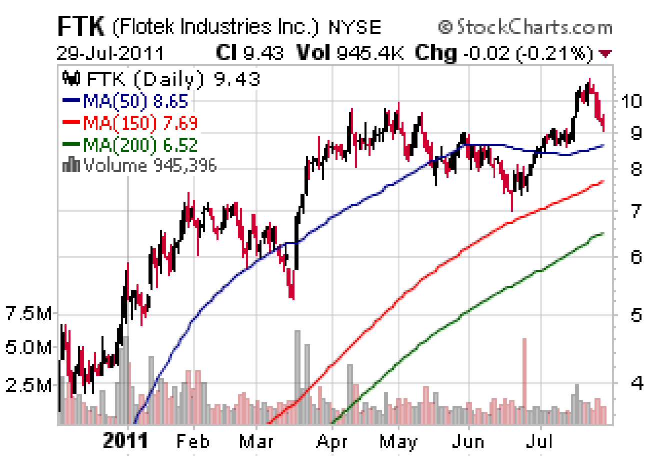


It to is trending sideways and has pulled back the last couple of days to its 200-day MA. One very important thing to watch going forward is the dollar.

Commodities have risen as of late due to the debt crises, if we get a resolution we could get a rally in the dollar putting pressure on commodities. So keep your eye on the dollar as you may look to potentially enter some of these stocks.

The stocks shown below have performed well and may be potential buys on pullbacks .



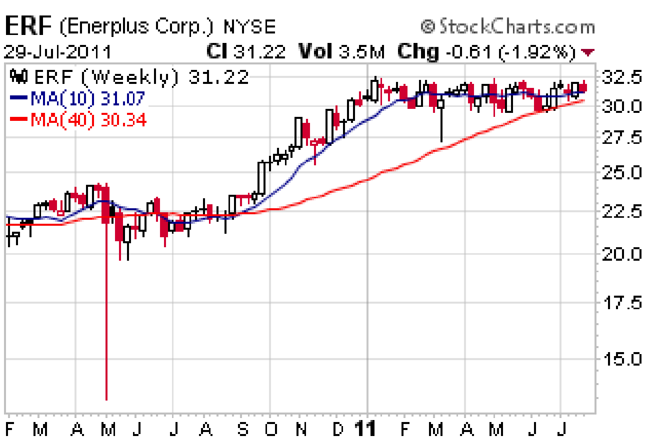


Here are some oil stocks that are well above the long term averages and look to be the leaders of the next major breakout in the markets to come later this year. These stocks should be bought on pull back towards old support > long term moving averages.

MVO

ERF

Consolidating very well and is a buy at breakout.

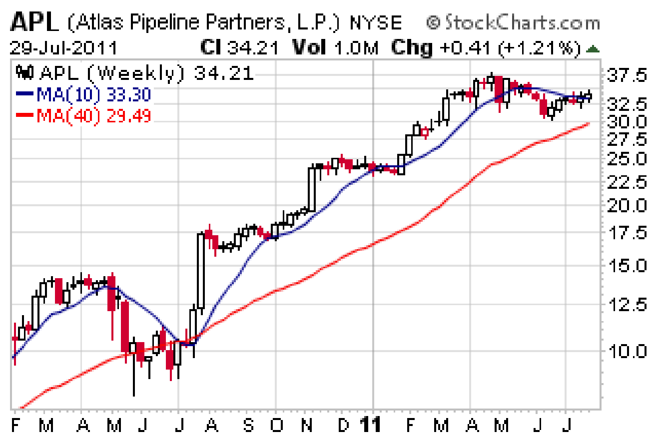


XTXI

Great looking chart pattern with high volume but it's extended and should be bought on pull backs towards 12.00 range.

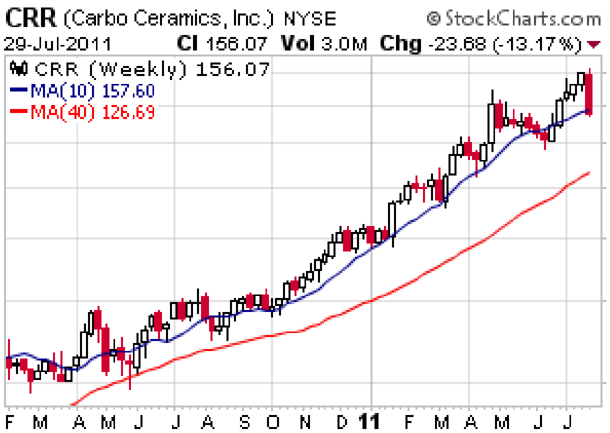
APL

Great looking chart pattern. Consolidating very well and a add on.

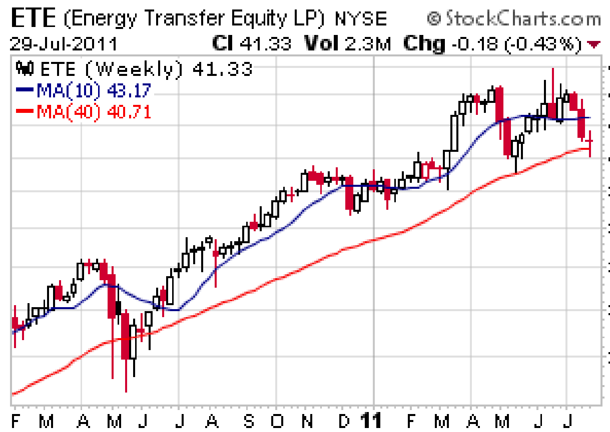


Another great looking chart that's consolidating while the markets pull back

CRR is still extended but is a buy on pull back in the 145 range above the long term moving averages.



ETE is over sold back into the long term moving averages. A buy here placing a stop under May lows.

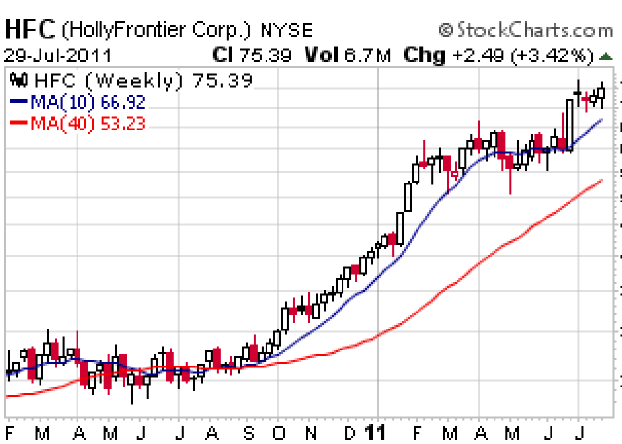


WMB

Need to be a buyer in the 28 > 30 range placing a trailing stop under the long term moving averages

MRO is a in the 30 range placing a stop under the long term moving av-erages.

HFC is extended. Buy on pull backs in the 65 > 66 range.



Others oil related stocks that are trading well on the market pull backs

CVX SM MMP OKS MMLP HP BTE HAL BAI

PTEN WNR CLB WTI NBL RES ENB

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