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Stock Market Barometer

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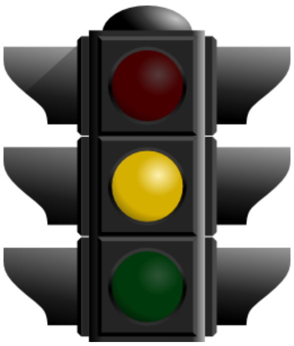
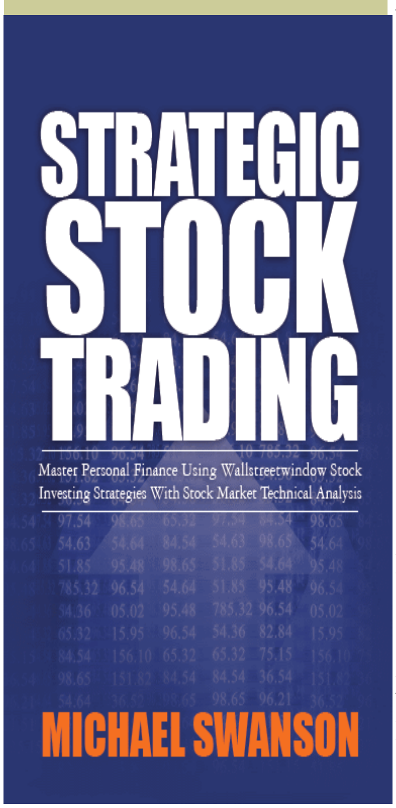


TREND ALERT — Bubble floats up, how high will it go before it pops?



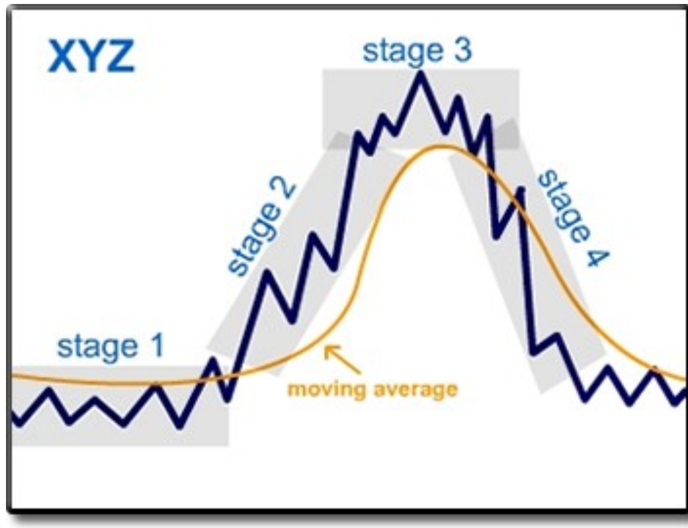
The Federal Reserve Has Made Another Bubble!- Mike Swanson (09/01/2014)

August was a month like many we have seen in the market so far this year. We saw a very little dip to start the month that took the DOW down to its 150 and 200-day moving averages and then a bounce rally back up that took the Nasdaq and S&P 500 up to new highs as the latter closed the month above 2,000. There wasn't a whole lot fear on that dip earlier in the month. Not much at all really. And not according to the Investors Intelligence survey and the action in the VIX . But there was a tremendous amount of excitement on TV at the end of the month.

We are now at a time when everyone is bullish in the stock market and if you express doubts about the stock market all you do is make people angry at you. People want the market to go up forever for them and so they listen to people who tell them that it will. And the truth is most of those that say this are not lying, because they believe this themselves.

How many times have you heard someone say on CNBC that valuations do not matter? Or that the Federal Reserve has now perfected control of interest rates and wants to help the stock market so that it can go up for years on end from here? This has been the message over and over again on that network and in the financial media in general.

Yes, they do have a few bears they put on like Marc Faber and Peter Schiff, but whenever they are put on TV typically CNBC will run several segments afterwards putting on others to say that they are wrong. Sometimes they make fun of them and sometimes they even smear them. But the gold story is different.



Everyone is bearish now and hates gold, because it had a big bear market from 2011 to 2012 and has not had a sustainable rally yet that has lasted for months on end. That time will come soon, but gold is still stuck at the end of its stage one basing phase. I thought it would be breaking out of it by now, but it hasn't yet. It's only a matter of time. Ironically gold stocks have actually performed better than the stock market so far this year, with a gain of 26.3% in the gold stock ETF GDX year to date, but no one cares about them. That's what happens during a stage one base and at the start of a new bull market.

People only get bullish after something has gone up for years like the US stock market has. Gold hasn't gone up for years on end yet so no one cares. They will later though. Gold is acting weaker than the mining stocks, which is a good sign for both, because the action in the mining stocks tends to lead both.

At the start of gold and mining stock bull markets the stocks tend to lead the way. And that is exactly what they are doing now. We saw gold dip a little in August down to the $1,270 level. It wouldn't surprise me if we don't see gold go sideways a bit this month and then dip through that level to make a new bottom like it did at the end of May. But I don't think it matters for the stocks as they are simply going sideways below the critical long-term 250 resistance level on the HUI. Once it is broken they will complete their transition into a new bull market and if gold was going to crash like the naysayers keep saying it will it then they would already have dumped by now.

That means September sets up another good buy time for gold and mining stocks, because once gold starts to rally again you will see the real move higher begin.

And the move is likely to start in a few weeks after some more sideways play or a final quick dip in gold prices.

I keep spending so much time talking about gold with you, because the best time

to invest is at the end of a stage one base and start of a new bull market and the worst time is during a stage three topping phase. But people tend to do the exact opposite. Look I think the US stock market can do ok overall from now and the rest of this year. But we will likely see another dip again begin in September just like we did at the start of this past August to take the DOW back down to its 200-day moving averages.

The stock market has been in a sharp upward channel since 2012. That channel is likely to stay intact into the end of this year, but I am becoming more and more concerned about what will happen once it is broken.

This is why I do not recommend investing in the US stock market right now. Trading is fine. If you want to swing trade and do whatever, go for it. I have trading ideas every week in the Power Investor Service. But eventually a new bear market is going to hit and you are best to invest in places just starting a new bull market that are at cheap valuations and have the real potential to go up for what you are risking then to just buy into the US stock market and hope it goes up forever from here. Instead of thinking about what is happening this week or this month, let's look out further into the future so that we can invest with foresight.

I am a cautious skeptic on the US stock market, but not a bear yet. People like to say that bull markets go through three distinct psychological phases. When they start the pain of the previous bear market causes people to doubt that a new bull market is really starting. Many sold out on the last bear and don't want to buy into another rally and lose again and those that have held their positions are just too beat up mentally to believe there is a new bull market. This is the type of psychology you see in gold and mining stocks now.

Ironically when bull markets start generally speaking they almost always generate huge gains in their first 6-12 months of action. You get a big initial rally that brings huge returns. But because of the widespread fear and worry about the market still a part of the mentality of the masses few position themselves to benefit from it. That's why I'm so adamant about the gold and mining stocks market. Because I think it provides you a chance to get into a new bull market when you probably never have been positioned correctly in the past when one started - or knew what was happening.

After that first psychological phase of a bull market the market tends to slow down. It's still bullish, but the rallies are not as big as they were in the first phase. Corrections come and the market holds up and goes back up. The failure of those corrections to develop into a new bear market eventually causes people to accept the fact that the market is really in a bull market.

They start see things in the news too that backs up this conclusion they have come to about the financial market. They want there to be a reason for their new belief system and they start to see reasons to believe. So in the US stock market many have come to convince themselves several years ago that the financial crisis of 2008 was some sort of anomaly that can never happen again.

In the final phase of a bull market what happens is that things have gone up for so long that people come to expect them to go up forever. So they reach a point where they do not care what price they pay for a stock or the market as a whole, because they believe that it doesn't matter. With the lack of great economic growth in the economy that they can see in their day to day lives they have simply convinced themselves that Obama and Janet Yellen have simply fixed things so that the stock market won't fall again. If you talk to someone really bullish about the stock market right now they tend to worship government action and have total trust in the Federal Reserve.

In the final phase people become wildly bullish. This has showed up this year in wildly bullish sentiment reading and data that shows that a wild level of margin debt built up in the stock market this year.

In the final phase of a bull market sometimes, but not always, you will get an acceleration in the bull market that leads to big gains like you saw in the first part of a bull market. This is what happened at the end of 1999, but didn’t happen in 2007. It is what happened to silver prices when they peaked out in 2011. It is what has been happening in the US stock market this year though.

Really big final move started in 2012. It is the last hurrah of the bulls and will be the final investment bubble for a generation of investors in the market over 65 years old. Unfortunately many of them will fail to get out during the next bear market and hold all of the way down to destroy themselves. But they are happy now. If you can remember there was a bit of fear at the end of 2012. That was when the Congress failed to get a budget agreement together. The stock market fell at the end of December as those worries first became big public news. A few months later the government did shut down over the budget for a few weeks, but it was at the end of 2012 that this issue disturbed investors for a short pe-

riod of time. They got over it quickly and then just ignored it and have in fact ignored all other bad news ever since then.

Since that month way back in December of 2012 the US stock market has been going straight up in an upward channel. It has not had 10% correction ever since. The S&P 500 and the Nasdaq have not even gone below their 200-day moving averages a single time since December of 2012. The DOW did for three days this past February and immediately rallied back up.

At the same time this year very slowly there has been a deterioration in the internals in the stock market. You can see this in the advance/decline line for the Nasdaq. It doesn't show up in the NYSE advance/decline line, because it is being helped by hundreds of ETFs that are in it - and didn't even exist ten years ago.

This is important, because as a bull market comes to an end fewer and fewer stocks and sectors participate in the rallies and as the end gets really close many fall into bear markets of their own way ahead of the US stock market topping out. This is happening right now to casino stocks, housing stocks, and construction stocks.

I am watching all of this very closely, because if it continues and gets worse in the coming months then we will see a new bear market. At this point I don't think the latter is going to happen this year, but it very well could next year. What happens at the end is that only a few stocks end up driving the bull market in its final inning. And when they stop going up the market averages go into bear markets. The fact that slowly fewer sectors and stocks have been participating in the rallies means that things are slowly heading in that direction.

I have been in two big US stock market bear markets now and in three bull markets. This one is acting a little different now than those last two bull markets did, because it is has been going on so long without a real correction. This has very alarming implications, because if the market continues like this for the rest of this year with one or two little dips like it has done so far this year so that it then tops out without having a correction for so long before the final peak then it will all end in some sort of a crash. It's like an airplane flying straight up into the sky. It can only go so high without falling down and that's why pilots don't fly point their airplanes to the moon and try to fly to it.

You see, something that goes straight up tends to go straight down. Corrections are actually good for a stock market. We are in a US stock market balloon that is having too much air blown into it.

This shows up in the stock market valuations by the way. I have talked a lot in the past about the cyclically adjusted P/E ratio and posted several videos about it on my site the other week. It takes the average P/E for the S&P 500 for ten years and adjusts it for inflation. It shows that the stock market in the United States is as highly valued now as it was at the top in 2007 and is the most overvalued stock market in the world now outside of Indonesia.

Now it has been overvalued now for almost two years so people who believe the stock market will go up forever claim that the CAPE ratio doesn't work or that valuations simply do not mean anything anymore. Like someone on Yahoo Finance said recently about Facebook - you can't use valuations to buy it you have to just believe.

The problem with people who dismiss the CAPE ratio is that all other valuation metrics say that the stock market is overvalued too. You should see for yourself and go look at the valuations for all of the DOW 30 stocks and see what you find.

One reader who did this sent me this email the other week:

"In one, or more of your videos you stressed the importance of buying stocks with low PEG ratios. Under 0.50. I was curious as to what the combined PEG ratio was of the DJIA. So I added all thirty PEG ratios together which came to 63.34 then I divided it by 30, which came to 2.11. The lowest was IBM 1.20. The highest was PFE 4.14. My question is do you know if 2.11 PEG ratio is high or what would you consider high?"

Well a 1.0 is considered to be fully valued for a PEG ratio. I got the idea of looking for stocks to buy with PEG ratios under 0.50 from the career of John Templeton and writings of Peter Lynch in his book One Up On Wall Street. This is essentially a method to buy growth stocks at a cheap valuation so that you get the best of both worlds. Yes, with a PEG ratio of 2.11 I think you can consider the DOW to be at a bubble valuation. The other valuation metrics suggest the same thing if you compare them to their historic norms.

Besides the risks of a big drop once this bull market ends as I've outlined already the high valuations in the market pose another big risk and a reason why I simply cannot recommend people invest in the US stock market with the intention of buying and holding. Play for an end of the year rally, but buy and hold at this point is crazy in my opinion.

The Federal Reserve has done it again! I first got started in the stock market in the late 1990's and played internet stocks that the Fed helped to pump up into the stratosphere. Alan Greenspan bailed out the Long-Term Capital Hedge Fund by lowering interest rates and pumping the money supply. The internet bubble was the result.

Everyone knows it couldn't go on forever and when Greenspan started to take back those rate cuts and raise interest rates he said that there would be a "soft landing." There wasn't one. So the stock market collapsed. In response Mr. Greenspan and his Federal Reserve Board members did the only thing they knew to do and that is they lower rates to near zero and printed more money.

It took two years of loose money policies to do it, but in 2002 the stock market bottomed and began a bull market. The Fed though kept rates low for way to long and all that extra money had to go somewhere so it made its way into the real estate market.

A dangerous bubble grew there and it couldn't go on forever so the Federal started to take back its rate cuts. Ben Bernanke became Fed chairman and said there was no overvaluation in the real estate market. He said real estate prices would go up forever. And so did Steve LIESman who proclaimed Bernanke a genius. But they were wrong.

When real estate prices peaked out and dropped they took down the financial system with it. The market crash of 2008 was the result. In response the Federal Reserve lowered rates to zero and began pure money printing in the first quarter of 2009. When they tried to stop printing money the market dumped into the "flash crash" in 2010 and the Fed announced a new money printing program.

That money printing program has brought us yet another bubble in the stock market. The result will be another wreck when it pops and the Fed will most likely panic and print money again like they have done again and again. This time that will make gold prices explode higher.

People say that the stock market can go up forever and the Fed has found a way to manage things correctly, but their confidence in the Fed in 2000 and 2007 was sorely misplaced.

There is talk now in the press about a supposed big debate on how quickly the Fed should raise interest rates. There are a few on the Fed who fear inflation and do worry about the bubble imbalances that the Fed itself has created once again.

The Fed has created a trap. With zero rates and easy money policies it has once again created a bubble in the stock market. If it raises rates it risks popping that bubble and causing another bear market disaster like it did in 2007 and 200. And yet if it keeps rates low it runs the risk of creating inflation.

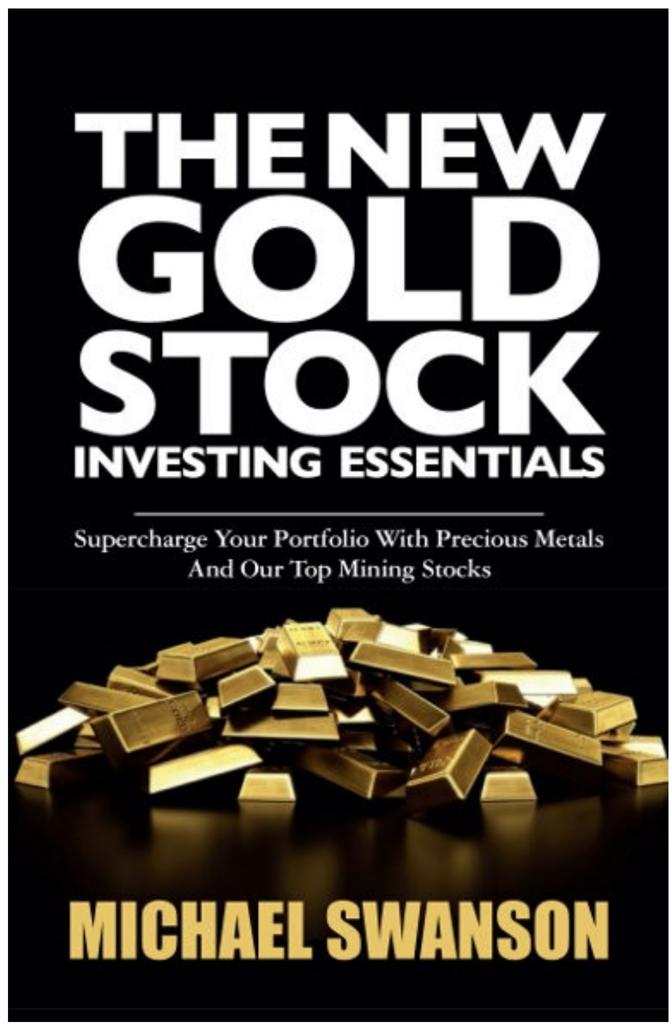
What would you do if you were Janet Yellen? Judging from her statements it appears she is going to try to say and do as little as possible. There is talk that the Fed could raise rates in 2015, but they have no time table on when they will do it and at the next Fed meeting in September she is likely to just release a policy statement saying that the Fed will just look at data points to make decisions.

If she does that this will be her way of just doing and saying nothing. Deep down she doesn't want to do anything, because she doesn't want to risk making a mistake. You can tell how nervous she is when you see her talk on TV and listen to the sound of her voice. She may even be scared.

She is the person and the Federal Reserve is the institution that US stock market bulls are trusting will be able to prevent another bubble disaster from blowing up after they have once again mistakenly created another bubble. Do you have that much trust in them? I don't. If they were smart and wise they would not have allowed another dangerous stock market bubble to appear.

Ben Bernanke, George Bush and Obama did succeed in bailing out Wall Street, but the price has been that they have now put the entire economy at risk again. This time the bailout didn't just help create another stock market bubble, but has fueled a much more dangerous one in US government debt. And that will be a story for tomorrow. Today all people care about is that the stock market is going up. They just expect the bubble will grow and get bigger and bigger for them and they will be able to ride it up to the moon and get out before it pops. Or maybe the masses don't think it will pop and that it will actually take them to the moon.

I'm watching that bubble for signs that it's over. I don't see them yet, but I'm watching carefully. When you play markets that have gone up for five years and overvalued you have to be very cautious. In fact you need to be nervous and fearful.



But when you invest at the start of bull markets you do so with confidence that you bought in at a good price and hope that means big future returns for what you are risking. That's why to me the US stock market is scary and the metals markets and mining stocks are exciting and fun to be a part of and why I am now spending the bulk of my efforts to help you profit in them. This is why I published my book **The New Gold Stock Investing Essentials** this August. If you already bought the book I want to say thanks. And if you reviewed it I want to give you a DOUBLE THANK YOU. If you have not bought it yet then you can get it at Amazon by clicking here.

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