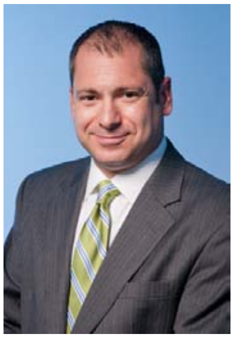

Written by Mitchell O. Goldberg, November 23, 2009.
ClientFirst Strategy, Inc.
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Paranoia...Stocks and the Economy…

Something else to consider…

If you didn't notice, the only thing going up faster than the stock market is investor paranoia. It appears that the big question; "Is the stock market ahead of economic fundamentals?" has reached a crescendo. So, now it is time for an explanation that is more mechanical than economical as to why the stock market rallied and why it can actually continue.

The Negs (those whom are negative on the stock market and/or the economy) will tell you that this current rally is not built on solid underpinnings: unemployment is too high and rising further, more homeowners are behind on their mortgage payments, foreclosures are still rising, banks are failing, revenues are down, earnings growth based on cost cutting cannot last, commercial real estate is about to implode, and the Grand Daddy of them all – **once the Government pulls back on all of its massive stimulus activities, the economy will go into a double dip recession.**

The Posits (those whom are bullish of the stock market and/or the economy) will tell you that the current rally is justified; existing home sales are rising, inventory of unsold homes is near a 2 year low, the first time unemployment claims are trending lower, Mergers and Acquisitions are way up and are removing excess capacity from the economy, the Government stimulus package has barely made its way into the economy, earnings are way up, the credit markets are functioning and corporate debt issuance is on the rise, companies' earnings reports are beating analyst estimates, some companies are rehiring laid off workers, and the Grand Daddy of them all – **GDP is again positive.**

The purpose of this is not to recant a litany of specific economic stats and how one should interpret them, but to put forth an alternative reason for the recent stock market revival that, while making perfect sense to Wall Street insiders, may not have been considered by many investors.

So, what gives?

The Dow Jones Industrial Average of 30 stocks (established in 1896) was meant to reflect the health of the American economy. But changes to it have been made over the years based on its components merging, failing, or otherwise becoming less relevant to investors. *Currently, this heavy weight of indices is confounding economists and is happily outperforming the forecasts of even the most bullish of optimists.*

The Dow has recently risen slightly over 60% from its recent low of 6469.95 set back in March, '09. Too much, some will say. Well, if Citigroup (trading in single digits), General Motors (in bankruptcy and stock is worthless) and Merrill Lynch (acquired by Bank of America and believed to have been the next investment bank after Lehman Bros. to go bust had it not been for B of A) were still part of the index, it wouldn't have been mathematically possible for the index to rise by so much.

Due to the nature of the replacements, Cisco, Kraft, and Travelers, the index was given new firing power in the form of very healthy new components. The help of these new components are a significant reason for the Dow's recent performance.

If you take into consideration the effect that the weak Dollar has on the Dow 30 components' overseas revenues and earnings (a very big positive), the big contribution of the tech sector (5 in the index - IBM, Hewlett Packard, Intel, Microsoft, and Cisco have all reported strong results and forecasts), and the rest of the components being more or less within the sweet spot of the global economic recovery (and reporting strong results as well), it is actually easy to spot why the Dow was able to rise so much…and why it can keep rising. **So, while not even close to all businesses and consumers are enjoying the recovery, the companies that count are.**

The effects of additions and deletions on other indices such as the S&P 500 and NASDAQ 100 are similar. Bottom line; when judging the recent stock market performance, the mechanicals of how indices are comprised and calculated are as relevant, if not more, than whether or not one currently believes the economic recovery moves into expansion or if it double dips.

Moving on:

Now, on to the ClientFirst Strategy, Inc. top 10 possibilities for 2010. We'll see how many on the list come to pass. Of course, being a flexible investment professional, I stand at the ready to make portfolio adjustments at a moments' notice. These are not necessarily hoped for results and by no means are they guarantees. Here we go:

1. The **Dollar** will stay weak through the first quarter of 2010, at which I would expect a change in direction. This should coincide when the Fed potentially raises rates by the end of the March '10 quarter.
2. I expect the **large global companies** to continue to outperform other sectors of the markets.
3. **Institutional money managers** will continue to buy earnings stories regardless of the macro economic picture.
4. Expect the **economy** to continue to surprise on the upside.
5. Expect the **tech sector** to be a leader throughout 2010…NASDAQ Composite could potentially benefit greatly.
6. UBS registered representatives will be calling **JP Morgan** their new employer (or at least someone other than UBS).
7. I expect a **political revival for Republicans** in the 2010 mid-term elections.
8. The major averages should show positive performance for the full year 2010.
9. **The budget deficit** won't be as enormous as investors expect due to the revival in corporate earnings…earnings are taxable, remember? Tax receipts will be higher than many expect. It'll still be enormous!
10. **Inflation will continue to remain low.** This is because "wage push inflation" is the biggest contributor to inflation. With an over supply of available workers, wages should remain low for years to come…bad for workers but good for corporate productivity gains and earnings. Since companies are valued on the earnings they generate, this should potentially be good for investors…refer to # 8.

Thanks for reading this. Please forward this to anyone you know who may find it interesting. Please reply me if you'd like to comment.

Interested in becoming a client? Call me. Let's talk about it.

(Disclosure: This is solely MY opinion. Of course, you are welcome to share your opinions with me too. If you act on any of this without speaking to me first and you lose money, don't blame me. I may be wrong. I reserve the right to change my mind about any of this whenever I want and without warning. We're NOT totally out of the woods yet! Have a great day! ☺)

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