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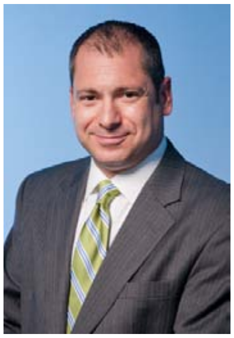

Written by Mitchell O. Goldberg, March 20, 2009
ClientFirst Strategy, Inc.
For immediate release.

"Mark to Market"

Cut through the clutter…and get to the point…

Is this a major stock market reversal or just another sucker's rally?

Wall Street veterans (and we're not all bad!) will tell you that the four most dangerous words in stock market vernacular are "it's different this time". Investors have a strong tendency to extrapolate rising markets well into the future and the same for falling markets. Economists have a term for this kind of tendency; behavioral finance. When we're in the thick of it, we tend to think that the moment we're in is truly unique. Meaning, it's different this time. That's when investors begin positioning their portfolios for the forever trade. **Either investors lose their risk tolerance and bet that that the market will go down forever or they lose their inhibitions and bet that a bull market will rise forever.** They act accordingly by selling in order to satisfy their fear emotion or they buy too much in order to feed their greed emotion. What is lost is the sense of history that everything is cyclical; economics, markets, politics, etc. While it is impossible to measure how oversold or overbought the stock market can get, what we can count on are some investors acting as if the moment, good or bad, will last forever. But alas, the emotion of the moment swings both ways like a pendulum – always. **And when it happens, it moves fast.**

On Tuesday morning of March 10th, 2009, we got a reminder of just how fast the stock market can stage a bear killing reversal. As impressive a rally it is, the reason behind it is what really matters.

What happened on that morning, Federal Reserve Chairman, Ben Bernanke, said not much more than a blurb about how banks may possibly **re-evaluate** the assets on their balance sheets. The futures surged ahead of the opening bell. Stocks staged their first big multi-day rally since November of 2008.

His comments were taken to heart by those who see adjustments to the "Mark to Market" accounting rules as the economy's salvation. But is this issue really important?

"Mark to Market" is a FASB (Financial Accounting Standards Board) rule which dictates how banks value some of the assets on their balance sheets. Asset values should be valued at a price that is agreed upon between willing sellers and willing buyers. It is regarded as the fairest way to value anything. After all, the market will pay what the market will bear, right? **This is supposed to keep financial institutions honest and it gives investors and regulators a fair assessment of the shape that these institutions are in.** Some say that not until banks come clean about the true value of all of the assets on their balance sheets can we ever have confidence in them again.

But what if we find ourselves in a broken economy and a broken financial market? Are the prices agreed upon between buyers and sellers fair or are the prices depressed because of acute distressed selling? What if these assets are worth more than the current depressed market price? What if some "toxic" assets on bank balance sheets are currently valued at zero but should be worth more because they throw off cash flow and will have at least some maturity value? In this case, the anti "Mark to Market" crowd will argue that the rules for this need to be relaxed or adjusted in some way, at least for a little while to get us through this recession. **This, they say, would halt write downs within the banking sector.**

This is important because banks have been getting slammed with stock crushing write downs. When some assets on the balance sheets of banks are written down in value, **banks must come up with cash to make up the difference due to the recorded reduction in value. What if a bank doesn't have the cash? Insolvency happens.** Government (tax payer) bailout money is doled out to potentially insolvent banks (some may have actually reached that point). The bigger problem is that banks can't lend out money to consumers and businesses because they need to hoard cash for the write downs. This causes the economy to get worse due to a lack of credit availability which then causes these "toxic" assets to drop further. This in turn creates more write downs for more banks…less credit availability…weaker economy…more foreclosures…more bankruptcies…etc. It is this vicious cycle that is the ***sum of all fears of the world's central bankers.*** This is why Trillions of Dollars have been thrown at the banks, AIG, Fannie Mae, Freddie Mac, GM, Chrysler, etc.

Does it really matter for the rally that began March 10th whether or not "Mark to Market" is adjusted? Can anyone truly tell which is the right way to go?

Investors have factored into their economic and market forecasts some sort of working compromise on this issue; hence, they bid stock prices and other corporate securities higher. On March 12th, A House sub committee met to address this issue; followed by strong rhetoric that Congress will do something with "Mark to Market" if FASB and SEC don't. Political will on both sides of the aisle seem to be gaining traction. Since it seems like Congress these days gets whatever it wants, investor confidence has had good reason to grow stronger on this issue.

The forceful selling momentum that marked the first 9 weeks of 2009 was like any force of inertia we've seen. The market was falling until something stopped it or moved it in the other direction; easy enough to understand. **That point is called an oversold condition.** When the "Mark to Market" issue came to fore, all it took in this "seller dominated market" was to knock out just a few sellers and for just a few buyers to re-enter in order to **slightly tip the scale to the other side of the fulcrum.** Once one side has more weight, that side will take control. Of course, until the winning side hits the ground, like the heavier kid on a seesaw. Then the whole darn cycle starts all over again. So, it isn't different this time, after all. Not to say that each recession doesn't have its own nuances, but the cycle of boom and bust is still the same old cycle.

In my previous article (January 22, 2009), my reason for the '08 year end rally fading away was because the stock market began the process of discounting the eventual economic recovery from the 2nd half of '09 into 2010. On 60 Minutes (CBS, March 15, 2009), Chairman Bernanke said he sees the recovery in '10. Whoever sent my last email article to him, thank you very much!

Since March 10th:

1. **The mortgage refinance boom** that started in December '08 has grown in size. The newly reduced mortgage statements are just starting to reach homeowner's mail boxes now. That's more money for the economy.
2. Initial unemployment claims is showing **early evidence of leveling off**.*(U.S. Dept. of Labor website) While this figure is still a high 600 K plus, leveling off still needs to precede a decrease; looks like we're getting that now.
3. The big 3 banks, JP Morgan, Citigroup, and BofA all said that **they're profitable on an operating basis so far this year.***(Yahoo Finance, CNBC.com) The zero interest rate policy by the Fed is replenishing bank reserves. This is how the Fed fixed the banking system in **1990** too; another era marked by a crisis in the banking sector.
4. Inflation is low, but not too low. Commodities, which were recently priced to reflect weakening demand, are rising to reflect a potential rise in demand. The **price of gasoline is still low** and we currently have lots in inventory just in time for the summer driving season. No doubt, inflation will become a problem down the road, so it is advisable to have some exposure to commodities.
5. **The BOGS *(Bernanke, Obama, Geithner, and Summers)* Quartet** is singing in unison and in tune. Anyone notice the absence of the endless anti-business talk? Anyone notice the extraordinary steps taken by the Fed and Treasury?
6. Housing is affordable; the most in 40 years.*(NY Times, March 14, 2009) Back to those low mortgage rates; lower principal combined with lower payments WILL alleviate the overhang in housing inventory – my opinion, of course.
7. **Mergers and acquisition activity is up**. Three big takeovers in big pharma (Merck/Schering Plough, Pfizer/Wyeth, and Roche/Genentech) were recently

announced. IBM is in talks to buy Sun Microsystems. Cisco just completed a big bond offering despite tons of cash on their balance sheets.*(Yahoo Finance) Corporate bond issuance has been strong as of late, which portends a big wave of **M&A activity; often a sign of a market turnaround. The strong companies grow market share and the weaklings get gobbled up or disappear. What follows are healthier and more competitive companies and industries – always. Rising corporate earnings typically follow. You know what impact that has on stock prices, right?**

8. General Electric's credit rating was cut only one notch, which wasn't as bad as investors expected. When the stock market goes up on bad news because the news wasn't as bad as expected, that is often a bullish sign for stocks in general. GE announced (March 19, 2008) that it expects its finance unit to be profitable or breakeven in 2009, which came as relief to investors.*(CNBC.com)
9. Oracle beat Wall Street earnings expectations by a wide margin.*(CNBC.com, Bloomberg)
10. AT&T is hiring 3,000 new employees and spending 18 Billion Dollars on tech equipment in order to further build out its wired and wireless networks.*(various news outlets, CNBC.com)
11. Corporate bond prices and preferred stock prices are finally being bid higher as investors' appetite for risk is starting to grow.
12. Some banks are ready or are almost ready to give back TARP money. They wouldn't give it back if they were in dire straits, right? Also, it means that TARP might not be quite as expensive if the Government is getting paid back.*(various news outlets, CNBC.com)

While none of the above is the silver bullet that investors would like, they are at least bullets that are silver tipped. In an extended period of bad news, a little positive news can go a long way. My sense, a lot more is on the way.

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.

Do you know a financial advisor who would like to work in a great environment and who wants to put his/her clients' first? Please let me know. I'm hiring!
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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