

# KAY INVESTMENTS

S E C R E G I S T E R E D I N V E S T M E N T A D V I S O R

July 9, 2009

*Giving money and power to government is like giving whiskey and car keys to teenage boys.* ~ P. J. O'Rourke, American political satirist, journalist, and writer

There is a great divide among financial advisors, economists and investors over the question of whether a new bull market began in March of this year. Those who take the positive position believe in the “green shoots of recovery”, as described by many in government. They believe that the stock market anticipates economic recovery, with improved corporate earnings on the way. Many others are skeptical, however, and cite ugly economic and market statistics to make their case. Lowry’s Institutional, whose market analysis has helped many advisors for decades, takes the skeptical view. The simple summary of their view is that, in all the decades of new bull markets that they have studied, there has never been one that has exhibited the weak internal statistics of this current rally. These important statistics include such things as volume of trading when the market rises versus when it falls, the percentage of stocks overall making new highs, evidence of heavy institutional participation, etc.

John Hussman of the Hussman Funds makes an excellent point about where we stand today – that the market’s sharp rise since March has created a situation where investors now REQUIRE favorable economic developments and will express significant disappointment if those improvements don’t materialize. Based on what I see, the economy is more likely to surprise on the downside than upside. Recoveries are built on new investment, not on government or consumer spending, and corporate investment is not currently in any observable uptrend.

I decided some months ago, as many of you know from these newsletters, to follow a five stage re-entry back into the markets based on objective measures of increasing demand and decreasing supply. At the end of the fifth stage, a new bull market cycle would have proven itself with plenty of future opportunity. Typically, market cycles last 6 or so years on average, from bottom to bottom.

I think that the optimism, if it truly is excessive, is based on expectations that everything is the same as always this time. There is also a certain chatter, based on hope, from the media, from the government and from certain financial institutions that fear any exodus from their investment vehicles.

While I know that bull markets are said to be “built upon a wall of worry”, I feel that much is different in this cycle. This is not an ordinary recession and we are not looking at ordinary government intervention. We have seen severe economic damage in the areas of real estate, finance/banking, government budgets, corporate deleveraging/reorganization, unemployment, bankruptcy and taxation. There is apprehension out there regarding the future inflationary effects of the flood of

newly printed money, the cost impact of the new energy policy and possible new taxes on the way. The damage reminds me of a car in a multicar pile-up. The body damage just doesn't easily pop right back out. Given how much is different, I think it is important, when making market and investment decisions, to take a "show me" attitude. This is the reason for the staged re-entry.

As we redeploy sidelined cash, I will be looking especially for foreign and global opportunities. This is the area of greatest strength in the rally that began in March and the most favorable outlook for stocks in general, going forward.

Please contact me regarding your risk orientation, your investment model or other matters that you would like to discuss.

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