

Market Watch

A Sampling of Advisory Opinion ■ Edited by Anita Peltonen

"The excess liquidity is not only inflating stock prices, but is also debasing the dollar, giving rise to the suspicion that Washington believes the U.S. can export its way out of this recession."

JOHN COLLOPY, Collopy Letter

How to Hold On to This Bull

*State of the Market
by Systems & Forecasts/Signalnet*
150 Great Neck Rd., Great Neck, N.Y. 11021

Oct. 7: The bull continues to charge. The pace of advance should slow down, but our short- and intermediate-term indicators suggest that risk remains below average and profit potential above average.

In a slower-paced market advance, it should become more difficult to gain or hold on to a profit, if you add to positions on days when the market gains more than 1%. On such days, you should add to positions in exchange-traded funds with average or below-average volatility such as SPY (the Standard & Poor's 500 ETF), the consumer-staples SPDR (ticker: XLP) or the health-care SPDR (XLV).

On the other hand, emerging markets (especially Brazil) are favored on a longer-term technical and fundamental basis. If you plan on holding for several months, by all means take your positions. But if you are a shorter-term trader who uses sell-stops, it would be safer to buy on any 3% retracement, because when emerging-market ETFs turn down, they often fall quite rapidly.

—GERALD APPEL, MARVIN APPEL

Sowing Seeds of Another Bubble?

The HCM Market Letter
by Hegemony Capital Management
621 N.W. 53 St., Boca Raton, Fla. 33487

Oct. 7: We still generally concur with a bearish long-term view of the economy... [yet] we do not believe that the equity or credit markets are due for an imminent reversal—and the two are closely linked in today's interconnected, globalized world. Our optimism is squarely based on our experience in the credit markets, which continue to show every sign of healing.

While the initial impetus for this recovery came from government support, the private sector—with the notable exception of the banks—has stepped in to provide financing for many corporations needing loan extensions or refinancing. There are reasons

to be concerned that nonbank financing may become harder to come by in the near future...but abominably low yields and abundant liquidity suggest reasonably healthy borrowers should be able to access capital for a prolonged period of time, something that was not the case beginning a year ago and lasting for six months thereafter. Moreover, low yields are compelling investors to search out investments that offer them what they view as reliable returns without undue risk. This accounts for the ability of corporations in decent financial health, and even some in not-so-decent health, to raise large amounts of capital in 2009 to refinance or extend their existing debt.

The flip side of such a low-interest-rate environment is that it may well sow the seeds for another credit bubble.

The bubble that burst in 2007-08 was

created by the Federal Reserve keeping interest rates too low for too long, and by investors accepting too little return on their capital for too much risk. While the credit markets were clearly grossly undervalued at the depths of the crisis earlier this year, they have quickly moved to a point of fair valuation in many areas, particularly high-quality corporate credit. The danger now is that corporate credit will again overshoot, and offer investors too little return for the risks they are assuming.

Investors need to retain one of the lessons that the crisis should have taught them: in leveraged companies, every layer of the capital structure is a type of debt because there is a risk of default associated with the issuer. Accordingly, even though this is too much to hope [for], it would be much better for the markets if investors would remain

disciplined and insist on being properly compensated for the risks they are assuming when they invest in credit instruments.

The great dilemma the Federal Reserve is facing is when to raise interest rates again.

—MICHAEL LEWITT

Bloated Broad-Market Multiple

The October 2009 Collopy Letter
by Briggs-Picks Securities

250 E. Wisconsin Ave., Milwaukee, Wis. 53202

October: We were listening to a couple of talking heads on TV the other day as they waxed eloquently about this being a trading market fueled by an overly accommodative Fed. And they are on the mark.

Fundamentals do not support the market's current elevated level. The S&P 500 is changing hands at 20 times what seems to be the 2009 consensus earnings estimate of \$54 a share; we think the market's fair value today is 13 times earnings.

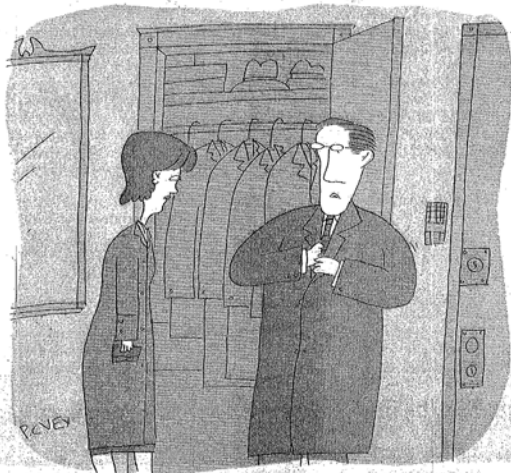
The excess liquidity is not only inflating stock prices, but is also debasing the dollar—giving rise to the suspicion that Washington believes the U.S. can export its way out of this recession.

At the same time, the slipping dollar is encouraging producers of various commodities that trade in dollars to raise prices as a hedge against the lower currency.

The proxy for this liquidity binge is gold, which is trading at new record highs as we write. Higher commodity prices are great for economies that export copper, coal, iron ore, oil and precious metals but not so good for economies that import large amounts of some of these industrial staples—like the U.S.

Sooner or later, our monetary authorities will have to raise short-term rates to protect the dollar. The stock market is not factoring higher rates into current valuations.

JOHN COLLOPY



"Let's go someplace horrible so we'll be happy to get home."

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