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Calm Before The Storm…

By David K. Miller

Have you noticed the shift in the vibe? Since mid-March this year, there has been a disturbance in the Force, as it were. It reminds me of a time, long, long ago, in this very galaxy.

On June 27, 1988, I was talked into watching a much-anticipated boxing match between Mike Tyson and Michael Spinks. I liked Rocky movies, so I figured we'd get some popcorn and beverages and see what a real fight is all about. I was expecting an epic battle, two gloved Gladiators fighting it out. We turned on HBO, gathered around in my apartment and I listened as my better informed friends made predictions about who would win. Then, the first round began, and ended, in 91 seconds.

I learned two things. First, I never want to be hit by Mike Tyson. Second, some fights are over very quickly when one opponent underestimates the other.

Two months ago, Team Obama was snickering at the Republican primary race, wondering just how bloody Mitt Romney would emerge, or if Rick Santorum would be their 'War on Women' poster boy in the general election. Back then, the unemployment rate had dropped, over 200,000 jobs had been created, and the stock market was surging. At the time, we warned you not to get too excited about the rosy economic outlook. Turns out we were right.

Now, it's become clear that the unemployment rate drop is exclusively because of low labor force participation and record joblessness. It's hardly a sign of economic vitality when over 1.2 million souls just give up looking for work. Take any good news on the economy with a seriously large grain of salt.

As for the stock market, it took a renewed recession in Europe, right and left hooks and an upper cut from Greece, Spain, and Italy to reveal that we've only seen the tip of the debt iceberg.

Worse for the markets, the Captains in charge of the ships of state seem to be wedded to the staying on course to oblivion.

End of the World On Hold (Death Star Implodes Instead)

About the only good news is that a new Mayan calendar has been found and Doomsday has been rescheduled. So we got that going for us. I'll keep you posted when we learn the new date that we can safely ignore. Until then, let's revel in the delicious mockery of yet another doomsday prediction failing ahead of schedule.

Anyway, back to the disturbance in the Force. Ever since the Supreme Court looked sideways at the Government's thin argument supporting Obamacare, the fortunes for President Obama's re-election have trended lower and lower. I could literally take up the rest of this month's issue cataloging the Keystone Cops routine that David Axelrod and crew have been acting out, but that would just be mean-spirited.

To put it nicely, they've had a bad couple of months. How bad? Face-in-palms and hair-pulling bad. And, even more than the tower of mashed potatoes that Richard Dreyfus marveled over in 'Close Encounters', this really does mean something.

Let's just say that the GSA Scandal, the Secret Service's penchant for Columbian hookers, and a series of messaging flubs including the War on Women, a big flap with the Catholic Bishops, and a flip-flop on gay marriage, have all sent the campaign into a vicious tailspin.

Uncharacteristically, the Republican presumptive nominee has played all these unforced errors quite deftly. Then again, when your opponent is busy shooting themselves in the foot, it's best to just stand back and let them keep reloading until they're out of ammo, however long it takes.

Not that Romney's team should underestimate Team Obama, but when you think you're going up against the Death Star and you arrive to find that it's imploding on its own, that tells you it's time to upgrade your outlook just a tad.

What To Expect When The Expected Doesn't Happen?

As investors, when the expected doesn't happen, that can tell you a lot about what's coming down the pike. For example, when bad news for a stock causes a minor sell off followed by a rally, that's bullish.

On the other hand, if good news provides only a dead cat bounce, look out below.

After 2008, Team Obama seemed invincible with the fundraising, the speeches, the social media and the fawning media… it was conventional wisdom that whoever the GOP put up against the well-oiled Democrat machine would have the fight of their political lives and probably lose. One more reason to NEVER trust conventional wisdom (Or Doomsday predictions, either, for that matter).

There are implications for the markets if the politically unexpected happens, of course, so it's wise to understand the meaning of the most watched race in American politics… The Wisconsin recall effort of Governor Scott Walker.

Why is that race important? Because it shows us what's likely in the cards for the next round.

No More Poker Face

The Unions and Democrat party went 'all in' to take out Walker for taking on the automatic deduction of dues for Unions - a huge source of funding and political contributions for Democrats. Since February, polling had consistently suggested that the Unions and Democrats were likely to lose on June 5th... and the polls were right.

The Maginot Line of union power has failed in Wisconsin, and battles in Indiana and Ohio will flare up and embattled Governors will likely be emboldened by Walker's survival and double down, too.

If that happens, watch for fireworks in the Presidential race. Despite Obama's significant victory in 2008, if blue states like Wisconsin fall into the GOP column, and the Union piggy bank gets raided, then that just spells DOOM for the Democrats.

On top of the 2010 redistricting fiasco, this isn't just an election cycle loss, it is a veritable Waterloo for Obama and the Progressives. A lot is at stake. Remember that the next President will also nominate at least one Supreme Court justice (Ginsberg is over 80) and tip the balance of the court. Conservatives have a 5 to 4 advantage and making it 6 to 3 would be Double DOOM for the left.

So, yeah, 2012 is kind of a big deal and it started in Wisconsin on June 5th; I think we are seeing which way the dominoes are likely to fall.

The loss in Wisconsin adds salt to fresh wounds in the West Virginia, Arkansas and Kentucky Democrat primary where President Obama lost an average of 42% of the vote to an incarcerated felon, a nobody lawyer, and literally, ‘nobody’, in that order. It should be noted that George H.W. Bush lost re-election in 1992 after losing 37% of the primary vote to Pat Buchannan. Whatever your opinion of Mr. Buchannan, he’s not a felon, a ‘nobody’ lawyer, or nobody at all.

So let’s just say that the aura of invincibility is pierced when a sitting President can’t rally his own base for re-election.

The Great Obama Bubble of 2007 – 2012 RIP?

I posed this question last month and the evidence supporting the hypothesis has grown more substantial.

In investment terms, it is my opinion that the Obama Presidency has been like mania or bubble. There are investment implications of this, as with any crash. The reason is simple; in living memory there has never been a less qualified man elected to the highest office in the land. Without getting into the partisan weeds or conspiracy theories about origin of birth, it is plain to see that prior to winning in 2008, Barack Obama had been a community organizer, a lawyer, a professor, and had been elected, but did not finish, terms in the Illinois legislature and United States Senate.

It is a credit to Team Obama 2008 that he defeated the Clinton Machine and a 23 year Senator and war hero with such thin credentials. Typically, Presidents come from the ranks of Governors and only two have come straight from the Senate without also holding higher office first. What explains Obama’s election, then? In a word, euphoria. The ‘Hope and Change’ vision sold like hot cakes to voters scared of the market crash and burdened with Bush fatigue.

What this means in terms of the bubble metaphor is that manias last as long as the euphoria and suspension of disbelief continues. As with the Dot Com bubble and the sub-prime real estate bubble, once confidence was pierced with the sharp tip of reality, the reversal was sudden and brutal.

In a bubble, naysayers are treated to derision and scorn by the manic believers. In the past 4 years it has been extremely rare to hear any criticism of President Obama from Democrats. That’s why the recent attack by Obama on Romney’s record at Bain Capital has been so astonishing. Democrat Newark Mayor and rising star Cory Booker inexplicably hit Obama on his “nauseating” attacks and the gnashing of teeth and wailing was swift and gut wrenching. While Booker walked back his comments in the manner of a man in a bunker at gun point, 4 other prominent Democrats including the Governor of Massachusetts, Deval Patrick, all distanced themselves from Obama on the issue. The reason why is instructive…

Don’t Bite The Hand That Pays You…

Obama has received hefty financial support from private equity companies, including Bain Capital, but so have all the other Democrats who criticized the President for his attacks on Romney. Not only don’t they want to be thrown under the bus by being perceived by the financial sector as anti-capitalist, they don’t want to go down with Obama’s ship. I’ll leave it to the political pundits to figure out why Team Obama would be this tone deaf and go after key contributors, but it is further evidence that there is not much ‘there’ there in their campaign.

It looks to me like they coasted in on a tsunami wave that favored the Democrat in 2008 and will be washed out by the pullback wave that favors Romney in 2012; if, for no other reason, than the economic malaise that started the cycle persists in spite of ‘Hope and Change’.

American Capitalism 1, Class Warfare 0

The good news for investors is that Team Obama’s shameless plan to pile class warfare on the top of attacks on Romney and ‘Wall Street’ has backfired with gusto. The last thing the US or world economy needs is for an attack on capitalism to take hold and be rewarded at the ballot box. Partisans may disagree, but from an investor's perspective, that fact seems indisputable.

If the markets and the American public--and even Democrats--have indeed pierced the bubble of the Obama Presidency, then this truly could be the calm before the storm in the global economy and the markets. The expected coast to re-election appears to have gotten blindsided by a detour to failure.

It's too soon to know for sure, but barring a major blunder by Team Romney or an 'October Surprise' rabbit out of Team Obama's hat, it looks like this general election may already be over like Tyson and Spinks. That is certainly a minority opinion, but my hunch is that Team Obama has been vastly overestimated and, fair or not, the circumstances of this election do not favor the incumbent.

Regardless of the outcome, the uncertainty created by the unexpected reversal of fortune will likely roil the markets. Any significant negative surprise from here on out will send the stock market plunging.

So, while we got out a big bowl of popcorn and were expecting a long and entertaining bout between Obama and Romney, it seems like we should get ready for a much more rapid resolution. All bets are truly off.

Don't Cry To Me, Wall Street

Here's one thing to keep in mind: the absurd rally in stocks this year is entirely unjustified by any economic data in hand. Tepid growth and high unemployment do not a bull market make. While it's true that the stock market is traditionally a leading indicator with a 6 month jump on other economic measurements, this time that is unlikely to explain the surge in the stock indices.

Keep in mind that ever since the stock market crashed in 2008, the Fed has flooded the financial markets with liquidity from 2 rounds of 'Quantitative Easing' (which is Fed talk for printing endless reams of new money to stave off deflation and doom).

Frankly My Dear, I Don't Give A Damn

There is about a 90% correlation between these Fed easing initiatives and the abrupt rallies in the markets from the lows in 2009 and 2011. Well, when the economic numbers started to improve earlier in the year, 'Daddy Warbucks' Bernanke indicated that a 3rd Quantitative Easing was not in the cards.

When you consider that the rallies since 2009 have been fueled by funny money, then you understand that this year's bull market is not a leading indicator, but lagging traces of inflation funneled into financial assets.

We'd see more inflation on Main Street but the banks have not been lending out the increased money supply and instead have bought bonds. If the funny money is truly cut off, then the odds favor the market taking a significant nose dive.

The added uncertainty from the election year shenanigans, the seemingly endless slow motion train wreck in Europe, and potential fireworks in the Middle East, give every reason to expect a major free fall is in the cards for stocks this year.

Now, sprinkle the OWS Black Bloc in for good measure with riots in Chicago and Oakland, and you have a lit fuse on the powder keg we've been expecting from the Far Left. Obama's troubles will no doubt accelerate the Union funded and organized street terror. The two thwarted OWS-linked terror plots give every indication that we truly are living in the calm before the storm.

Now is NOT the time to complacently hold on to stocks, let's put it that way.

Let's take a look at the market reactions so far…

Don't Look Down

Last month I showed you the following chart with circles marking the rally we caught in the SP 500. I pointed to the wedge forming on the chart and said…

> *"Markets don't go straight in one direction forever. Especially after a run like we've had in stocks this year, the urge of the crowd is to buy any dip in the rally. If price breaks above the downtrend line formed in April, that is a reasonable trade with one caveat – it may reverse quickly if the move stalls."*

And…

> *"As long as price stays above the uptrend line then the trend is up. Price will break above the short term down trend line or below the uptrend line by early May and nimble traders can look to catch a short term trade at that time whichever way it goes."*

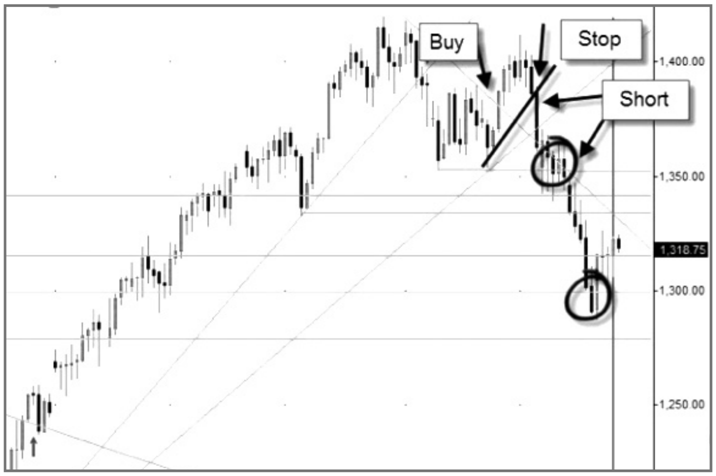
And…

> *"Similarly, there are a lot of frustrated bears who want to short this market and don't understand why it's been going up when there is so much global economic turmoil. Therefore, there could be sufficient selling pressure to break the uptrend line and test the lower price levels down to 1,275 area potentially."*

What Goes Up MUST Come Down…

You'll see that I've marked the buy breakout on the chart below. As that rally broke the uptrend line of the breakout, that was the signal to stop out with a small profit or breakeven, or go short. As a rule, you don't want to just stop and reverse willy-nilly, but in context with what I had said, a failure of that breakout would likely lead to a sell off.

Alternately, when the 1,350 level was breached, that failure of support can be seen as a horizontal 'trend line' breakout to the downside. Notice that price has bounced off the 1,300 level I'd drawn in last month, and price is retracing up.



Of course, the question is, how do you play this?

The uptrend line from October 2011 'til May 2012 has been broken and now the trend is down in the short term. This rally is likely to retrace back up to 38%, 50% or 62% and if it stalls there, sell back down to test the May lows. In terms of this chart, that's 1,335, 1,350, and 1,365 respectively.

Those are Fibonacci Retracement levels, which are time honored calculations that help identify price targets within a trend. For now, I won't go into all the theory behind Fibonacci retracements, but just know that there is a self-fulfilling tendency for them to work because so many traders use them.

In a really strong trend, a 23% retracement will hold, and that's at the 1,319 level where this chart ends. If that holds, then look out below because a test of the 1,250 level would be the next major target for support.

A word of caution: trading these short term swings takes a laser focus as you can see from the fast reversal in early May, from a buy to a strong sell off. If you're going to play these swings then make sure you don't forget to place stops; don't space out or go on vacation to return to a big fat loss.

Given the significance of the 1,350 level and the general tendency for retracements to hit 50%, that is where I would be looking to short this market. As always, I'll look for a trend line break. At the time I'm writing this, there are not enough bars to draw a conclusive trend line so we'll cover that next time.

Our guest contributor this month, John F. Carter, has an analysis of the stock market that you don't want to miss. He's got his finger on the pulse of the market and has a gift for clearly explaining the multiple factors in play. John is also a short-term swing trader and has tried-and-true strategies for timing his trades.

All That Glitters Is NOT Gold (Unless You're Short!)

Last month I showed you this coiled wedge on the gold chart and asked which way it would break out.

And here is what happened…

Gold broke out below the bottom of the wedge for a crystal clear sell signal. The past low is where you'd expect to find support, and sure enough, that was a perfect place to lock profits. I've marked both with circles on the chart.

You can see that once support held in the 1,526 area, Gold retraced up exactly 50% and turned down again at 1,600. That's the pattern I was describing a minute ago in the SP 500.

If you want to catch fast swings like that, consider using an intraday chart, like the 60 minute timeframe.

That way when a retracement holds a particular level, like the 50% in Gold at 1,600, you can get short for a quick swing trade. That will give you a better entry and you won't have to chase the market once it's already held the retracement and turned.

Here's a 60 minute chart that shows a text book example of that kind of swing trade. I've marked the sell with a circle and also the support level where you would look to cover and at least take some profits.

Notice how the gold market came up to the 1,600 level and turned. Once the uptrend line of that retracement broke, the market fell sharply. At that trend line break, you can define the retracement as having held the 50% level and enter the short to play the next move down.

Trading is all about support and resistance levels and previous lows are support where you can expect the buyers to come in and bid up the market.

A Crude and Slippery Slope

Few markets get as many headlines as Crude Oil when it shoots up above $100 a barrel. When prices go up at the pump, eventually someone starts babbling about 'speculators' and evil oil company gouging.

Notice that when Crude sells off sharply they don't give credit to 'speculators', even though they can make money when prices go up or down. That's a rant for another day, though.

What I want to show you is the update on Crude which had a similar false breakout as the SP 500 did.

Had you bought on this chart where I marked with an arrow, you'd have wanted to get out when the trend line of the breakout was broken to the downside. Here's why. The whole reasoning behind a breakout is that you expect prices to continue in the direction of the breakout. When they don't continue and instead reverse, get out. These short term moves are swing trades and not long term investments. You can always get back in, but there is no sense in letting a profitable swing trade go against you.

As with the SP 500, when the breakout failed, you could either have stopped and reversed to short the market, or sold short once the price broke out below the trend line where I marked the circle. As

with the other examples, support at 95 would be an expected place to take profits. You can always trail a stop with a portion of your position and move your stop loss to breakeven if you expect a major trend reversal has occurred.

Bonds Blow Up

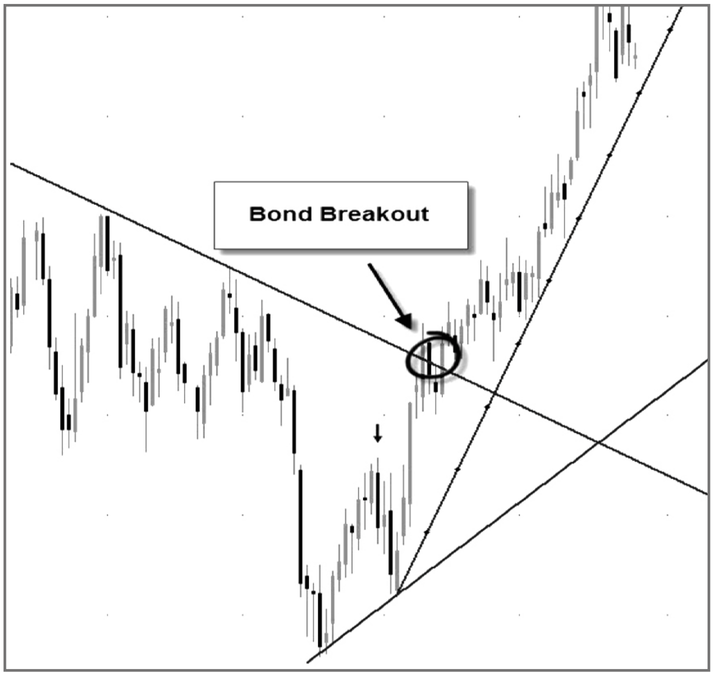
It's worth following up on the Bond market since we got stopped out of the retracement sell that we covered last month.

You'll notice on the chart below that Bonds moved down sharply and retraced in late March, where I marked a sell signal with an arrow. This retracement did move down sharply but it reversed quickly, too. Again, if you trade these retracements on the 60 minute intraday chart you can catch a quick profit even if the move reverses. Not for the faint of heart, to be sure.

A couple things to note in this chart: First, when stocks fall, bonds tend to rise because of a 'flight to quality' effect. More to the point, when a breakout happens and then fails, as the Bonds did in March, that tells you something: the market is going the other way.

In the chart below, you can see that Bonds rallied to break above a down trend line and has sparked a monster rally. No doubt folks who got short when the market broke down scrambled to cover their positions and their buying fueled the rally.

When the market moves that fast with such small retracements, you can see that a trend line drawn below the lows is also very steep. If you want to preserve profits, take profits when the steep trend line is broken and trail a stop so that you can ride a bigger move if you like, but at least move your stop to break even in case the market completely reverses.



EURO TRASHED

One more chart I want to cover this month is the long anticipated Euro break out. We've been stalking this trade for several months and it finally broke down when the European debt crisis flared up for the umpteenth time.

I hope by now you're starting to see the profit potential in identifying wedge price patterns and trading breakouts from them.

On the chart below you'll see a downside breakout short signal at the 1.3000 level. The Euro bounced briefly off of the January low and then proceeded to fall lower. Again, take some profits at support, then trail a stop and move your stop loss to break even.

There are more support levels at 1.2500 and 1.2420, so I'd expect the Euro to bounce more there and give us another opportunity to short on a retracement. Once the retracement begins, calculate a 50% target from the 1.3269 swing high on 4/27 to whatever the low ends up being. If the market bounces off 1.2500 that retracement would be expected to his the 1.288 area.

As with the other examples I showed you, watch the 60 minute chart for the retracement entry signal. The logical place for a stop would be above the 1.288 level, and with resistance at 1.3000 it would make sense to put a stop above that level. Not only is 1.3000 where the breakout originated, but it's also a 62% retracement of the swing. If price retraces above that level, then I would expect the Euro to head higher. That's how I'd play it, anyway.

Take a good look at John F. Carter's article in this month's issue. I watch his market calls like a hawk because he's got an invaluable insight into what makes these markets tick. If you get a chance to put John in your trading and investment corner, jump on it. He's one of the best in the world with his 'Ripple Effect' analysis; it's uncannily accurate.

I had planned on covering the grain markets this month, but the dramatic breakouts in the energy and financial and metals markets jumped to the front of the line. We'll revisit the grains and update these markets again next month.

Until then…

Good Hunting,
David K. Miller

Ripple Trading for the 2nd Half of 2012

John F. Carter

We are approaching the half-way point of 2012, and it's been an interesting ride. The first quarter of the year was easy. Just buy stocks and hold, right? Like the good old days of 1999? And then we started pushing into April and May and things got downright dicey. Why did AAPL stop going up? It was supposed to go to $1000! And why didn't the Facebook IPO save the market? That IPO was so hyped you would have thought it was a promo for a blockbuster movie that was going to knock Avatar from its top spot. And what in the hell is going on in Europe? Can't those guys figure out how to save their union?

Hmmmm . . . Could it be that things really aren't as clear and easy as they seem?

In my last article written in December, 2011, I talked about what was going on in the world, and how it really worked. How banks control everything and how, based on that knowledge—the fact that banks will do anything and everything to keep hold of their power and control—what asset classes were sure to benefit from that reality during the first half of the year.

For me, the no brainer move was buying US Dollars (by buying UUP or shorting FXE, the Euro, which is the inverse of the US Dollar), US Bonds (by buying TLT), and shorting Gold (buying put options on GLD). Now, don't get me wrong. Longer term I am a bonafide gold bull, and I am using this current weakness to buy more of the shiny metal. After all, we can always count on the powers that be to eventually screw up a good thing. Whether they do that in my lifetime or my heirs, I want physical precious metals on hand for my family.

That said, no market goes straight up or straight down. And once it became clear to me what the banks had up their sleeves, I knew it was time to short gold for a temporary move down. Not only to profit from the move... but to hedge my bullion positions. Because I'm not selling those coins!

As I'm writing this, both the dollar and bonds are near their dead highs for the year, and gold is trading close to its lows. And they currently don't show any signs of letting up. Although these investments haven't had the exciting punch of an AAPL move, they have been have been steady, headache free, and they've kept going up while the stock market got hit hard in May. While late investors in AAPL have watched in horror at its recent $100 slide and Facebook investors have been burned, dollars and bonds long have been producing steady returns, and the gold short has been fantastic. And as investors, we want returns. We don't want to be right. We don't want to be validated. We don't want people to pat us on the back. We just want to make money.

For UUP, it's been on the quiet side. After getting in near the $21.50 level in late 2011, it's currently trading just under $23.00. For those that shorted the inverse, FXE, it's made a move from $134 down to $124. For TLT, it took a few months to get the ideal entry of $111.50, but once that level hit, TLT took off and is currently trading near $124. For GLD, after buying puts a few months out on the rally to $165, the ETF is currently trading near $150. Although this is a nice move on the ETF, this move turned into a triple digit gain utilizing put options. For 2012, so far, so good.

So what about the last half of the year? Is it going to be as easy as buying dollars and bonds and kicking back and seeing what happens?

Oh no, no by a long shot.

It's going to get volatile. Heinous, even.

Before I dive into what I think is going to happen next, let's dive into the mind of a successful trader and investor. Because it is going to be important to have these traits in mind as we navigate into the murkier half of the year.

Great Trading and Investing

Great trading, like greatness in any profession or art, is a kind of balancing act. Each trade requires us to split ourselves into two parts: caution and boldness. Caution to be patient, and courage to get in and stay in a winning trade. You need the caution to protect gains once you have them—but not too aggressively so you don't get stopped out on a mere wiggle. And most important is the courage to admit that your trade is wrong and to get the hell out.

Great trading and investing is all of these things, which is why great traders are so rare. This balancing act is the reason so many type-A personalities perform so badly in the markets. Because while they might possess boldness, courage, and decisiveness, they frequently lack the caution, patience, and ability to accept that their first impression was the wrong one. Or, more simply, the ability to concede that, while their setup might have been as attractive as a Swedish au pair, it just didn't go the way they expected it to go. The market doesn't care if the setup was a good one; it's still going to do whatever it wants to do.

It may sound trite, but it's true; something happens at the beginning of a trade: that is, a psychological battle. It's that classic scene of a devil on one shoulder and an angel on the other. One tells you to hang in there with all your might, that's it going to go your way eventually, no matter what the evidence suggests, and the other screams in your ear to preserve your capital, to get out, take a tiny profit, take a tiny loss. Just get out!

It's a powerful sensation, especially for the beginning trader, which is why a clear trading strategy is critical. A trading plan in which you can place your faith is like a pair of mufflers, blocking out the sound of that noisy chorus. Trading without a game plan is like swimming in the Amazon river with a couple of raw steaks strapped to your waist. You might get some good exercise, but the longer you are in the water, the greater your chance of a violent and bloody end.

It's when you're not trading your plan that fear takes grip, and when fear takes grip, it's easy to lose perspective and exit too early, cutting your opportunity for profitability off at the knees. Yet fear also causes traders to do something that seems the total opposite of fear. Fear causes traders to ratchet up their nerve, and stay in the trade long after signs of danger have presented themselves. That is, fear triggers an irrational boldness in the markets. It takes courage to stay in a trade, that much is certain; but the lesson that too many traders learn too late is that it takes just as much courage, if not more so, to get out of a trade that's clearly not working. The greater a trader's nerve, the greater the chance of ruin.

I often recall the classis military maxim of, "Retreat is a perfectly legitimate military tactic." For all the parallels between war and trading, none could be truer than this one. There is no shame in taking a small loss. In fact, when taking a small loss saves you from taking a big one, it should be considered a victory. If things aren't going the way you hoped, preserve your capital and live to fight another day. And always remember, reentry is only a commission away. Go flat, take a walk, clear your head. The market isn't going anywhere.

It sounds simple enough, as if you could simply resolve at the start of every trade to exit neither too early nor too late, to have courage in the right measure at the right times, but it actually requires a tremendous shift in perspective for most traders. We are all geniuses when looking at the charts in hindsight. It's making decisions in real time, clearly not knowing what exactly is going to happen next, that makes or breaks a trader. Anyone can tell you what you should have done.

Great flexibility is required when looking at the markets. There is a certain Zen attitude which is reached by the greatest of traders. In fact, it's is one of the terrific, sometimes hilarious, paradoxes of the trading world, meeting serious traders in their seriously expensive suits, who amidst their talk about the hardcore daily battle between the bears and the bulls, sprinkle in Zen proverbs.

"There's no meaning to a flower unless it blooms." Or, perhaps another, more relevant one might be, "No ego, no pain."

The people who have learned these lessons are the ones who make money in the market because they have learned that when forming an opinion of the market, that's all you are doing: forming an opinion. You must leave room for chance. And when you see that your opinion was the wrong one, have the courage to get out, and the faith to accept another difficult truth: the opportunity will always come around one more time. Again, the markets aren't going anywhere.

Once a trader accepts the constant flow of the market, that it's truly an endless renewal of opportunity, then he understands that there is no need to enter the market on half-convictions. It's much smarter to just sit back and wait until a setup has laid itself out with clarity. Not a 'maybe' or an 'almost.' It's simply there, period.

In the meantime, a trader's main job is to fight off their boredom and stay flat. Traders who take on a position out of boredom then spend their time managing that mediocre trade while good ones pass them by are wasting their time and money. Getting in too early and getting out too late just means that someone else is eating your lunch that day. Your stop loss is another trader's first target.

It's All About Europe

Great. You've not got the right mindset to go confidently into the market.

Now that you do, it's going to be important to keep this in mind as we head into the second half of 2012. With increased volatility comes increased risk and potential frustration. One trick I always like to do? When the markets get more volatile, I cut my position size in half and double my stop loss. This way, I'm still risking the same amount of money in a trade, but I'm more easily able to ride out the whipsaws that destroy most traders accounts.

Now, onto Europe; or what is also known as, "The biggest financial disaster on the planet." To get a feel of what is really going on in Europe, we need to relate the Greece situation to one of the 50 United States.

First off, to say that the euro monetary system is flawed is like saying that the summers in Texas are "warm" when in fact they're damn hot. In fact, saying it's "warm" is a downright lie. In Europe, they have a system that was setup in such a way that each country continues to retain significant sovereign powers – most importantly the ability to exit the system and default on debts in times of stress. In fact, their structure is so shoddy it actually creates incentives to default on their debt and then exit the union - as Greece is considering doing as I'm writing this.

Imagine if the same happened in the US. Let's pick a state, say Virginia. This is nothing against Virginia, but it's a good example because it's economy is about the same size of Greece. Imagine that Virginia gave its citizens full pensions and retirement at age 45, free health care and education, and zero-enforcement against non-payment of taxes. Sounds like a dream, right?

Well clearly, after a while, the money would run out. Virginia, not wanting to upset their citizens, would go to Washington D.C., and demand a bailout. The other states in the union would balk at this, but eventually, for the sake of keeping the financial system in place, the government would cave and grant a bailout.

However, the rest of the states would then demand that Virginia start being fiscally responsible and cut a lot of its benefits. This would of course infuriate Virginians and they would take to the street in protest. They would get so mad, in fact, that they would throw the current government out of office and elect a far left wing official who promises to clean up this mess and keep the benefits coming.

Some wise citizens of Virginia, seeing the writing on the wall, start moving their money out of Virginia and putting it in banks with other states. Remember, in Europe there is no FDIC insurance on deposits. For the ones who stay in Virginia, they are trapped. No banks will lend Virginia money. Virginia has no money to keep up with its benefit program. And dollars are fleeing the state to go into other state banks. The next step? Default on your debt, exit the system, and print your own currency.

That, in a nutshell, is what is going on in Europe right now. Without some form of FDIC insurance and national banking resolution authority, the European Monetary System is hanging by a thread. The system was flawed from the start, but it's taking Greek profligacy (and soon other countries in Southern Europe – Spain is next) to expose the system for what it is. The bottom line is that there is no pain on Greece for them to exit the system. In fact, it would be beneficial for them to do so. They literally have nothing to lose. And this would crush the European Union.

Although the US banking system has its obvious flaws, at least the officials were smart enough to federalize the banking system. This way there isn't any way a single, individual state can threaten the integrity of the entire financial system. There is good reason for the separation of the banking system and the member states. And Europe will never be a successful union until it converts to a state-independent, federalized banking structure. In fact, the only way the European Union can succeed is to force a federal-type structure very quickly. If this doesn't happen, and happen soon, then Europe will continue to drop deeper into a recession - and this will only get worse if and when Greece exits. Their staying is not a good thing - but their leaving is worse.

What is Germany doing about this? Well, they recently were able to sell €4.56 billion ($5.8 billion) of two-year bonds at a 0% coupon interest rate just a few weeks ago. Why would people give Germany money to use for two years at no cost? Because they think Germany might throw up its hands and leave the Eurozone. If Germany left, they would likely denominate their bonds in Deutsche marks, which would rise in value over those of the countries that remained in the euro.

In other words, never a dull moment across the pond.

Ok, so how do we invest in this world and stay sane…and solvent?

Well, my investing themes have not changed much since the beginning of the year. First off, I'm looking for continued upside in the US Dollar. There is nothing to do here but hold onto UUP for more upside exposure. FXE short is still a good idea - but this is going to get volatile. If you don't have the stomach for crazy moves both in your favor and against you, do yourself a favor and just keep the UUP long. It's much less volatile.

I'm not as interested in being long bonds as I was at the beginning of the year. They still have more upside, but they are starting to look tired. I'm moving my stop loss on this trade to 3% below current levels. This way I can lock in profits but still participate in more upside.

For gold, we are essentially at the levels where I expected it to go. This is a good place to take profits and move into something else.

Anything new? There are individual stocks I like, particularly LQDT. This is an internet stock that focuses on liquidating inventory. And as we head into the second half of the year, I'm looking for the economy to struggle. This stock has held up well during this current decline, and it is currently trading near $60. I like it at these levels with a stop just under $50 and an open target for now.

What about shorting US Stocks? Believe it or not, I'm not a fan of this trade . . . yet. I think we are going to get a bigger down move, but I'm not looking for it to hit until we get into 2013. Essentially we have a liquidity crisis right now – meaning there is too much of it. It's just money, lots of money, sitting on balance sheets. This cash has to find a home, and stocks will benefit from this. Remember, never fight the banks, and right now banks continue to inject liquidity into the system.

Yes, at some point it will all come crashing down, but, as Maximus said in the movie Gladiator, "Not Yet."

One of my favorite sayings goes something like, "Markets can stay irrational a lot longer than I can stay solvent." Remember, for the second half of 2012, rationality will have nothing to do with these current markets.

And although the US is doing okay right now, a Europe that goes into a tailspin will impact the entire world, especially the US.

So, dust off your keyboard, get in the right mind set, cut your position size down, use stops, and get ready for some volatility. Because the second half of 2012 will be a lot of things, my friends, but ain't gonna be dull.

IWA Experts' Choices

Senters' Strategies

By Hubert Senters

Entry Date	Company	Symbol	Signal	Entry	Stop Loss	Target	Gain	Position Status
011/21/12	COMPANY z	Z	SHORT/ LONG	PRICE	XXX	YYY	% GAIN / LOSS	OPEN/ CLOSED
6/4/2012	Linkedin	LNKD	SHORT	90.38	103.65	Open		OPEN
5/3/2012	Netflix	NFLX	SHORT/	79.19 or better	97.99 or 25%	68.31		OPEN
3/18/2012	StarBucks	SBUX	Long	53.21	42.95 or 25% stop loss	64.61		Open
1/17/2011	GOLD	GC	Long	1665	1613 or 25% stop Loss	1800	-52	Closed
12/31/2011	Bank Of America	BAC	Long	5.27	4.92	9		Open

Ripple Effect Positions

By John Frederick Carter

Entry Date	Sym	Company	Time Frame	Type	Entry Price	Stop Loss	Target	Exit#1 (1/2)	Exit#2 (1/4)	Exit#3 (1/4)	Avg Gain	Exit Date
06/06/12	LQDT				63.63	51.25	78.50					
06/06/12	QQQ				62.52	59.25	66.50					
5/4/2012	SOYB	Teucrium Soybean Fund	Swing	ETF long	23.50	21.50	27.50					
5/4/2012	LQDT	Liquidity Services INC	Swing	Stock Long	53.75	47.75	85.00					
4/9/2012	TBT	Ultra Short 20+ Year Treasuries	Swing	Stock Long	19.15 (open price)	17.50	21.50					open
3/21/2012	USO	United States Oil Fund	Swing	Stock Long	39.10	36.60	OPEN					OPEN
2/9/2012	SPY	S&P SPDR	Swing	Stock Short	136.50	138.75	133.00				-2.25	CLOSED
2/6/2012	NFLX	Netflix	Swing	Stock Short	129.50	108.50	101.25	112.25	108.50	108.50		CLOSED
1/23/2012	RAX	Rackspace	Swing	Stock Long	42.60	54.50	57.50	52.50	57.50	OPEN		OPEN
1/3/2012	WFC	Wells Fargo	Swing	Stock Long	28.25	25.25	30.25	30.25	Exit Full	Exit Full	2.00	CLOSED
6/12/12												
12/30/2011	NFLX			Stock Long	69.75			94.85	Exit Full	Exit Full	25.10	CLOSED
12/19/2011	SPY			Jan 119 Call Option	2.25			4.90	Exit Full	Exit Full	2.65	CLOSED

Entry Date	Sym	Company	Time Frame	Type	Entry Price	Stop Loss	Target	Exit#1 (1/2)	Exit#2 (1/4)	Exit#3 (1/4)	Avg Gain	Exit Date
12/6/2011	MCD			Jan 90 Call Option	6.50			10.50	Exit Full	Exit Full	4.00	CLOSED
11/22/2011	AMZN			Stock Long	184.25			181.50	Exit Full	Exit Full	-2.75	CLOSED
11/10/2011	TLT			Dec 113 Call Option	3.25			7.30	Exit Full	Exit Full	4.25	CLOSED
11/7/2011	SLV			Stock Short	34.00			28.25	Exit Full	Exit Full	5.75	CLOSED
10/28/2011	FXE			Stock Long	140.50	133.50						OPEN
10/14/2011	USO			Nov 30 Call Option	5.10			7.90	Exit Full	Exit Full	2.80	CLOSED
10/7/2011	GLD			Nov 155 Call Option	5.25			13.10	Exit Full	Exit Full	7.85	CLOSED
10/4/2011	SLV			Stock Long	28.25			33.45	Exit Full	Exit Full	5.20	CLOSED

Current Forex Positions

by Jason Fielder

Pair	Buy	Sell	Hold	Profit/Loss
AUD/CAD			Hold	($92.9) (Closed 4/2/2012)
AUD/JPY				(-313.44)(Closed 6/1/2012)
AUD/NZD			Hold	
AUD/USD				$152.34 (Closed 4/2/2012)
NZD/JPY	62.90 (1/29/12)			$242.28 (Closed 4/2/2012)
NZD/USD	0.7918 (1/15/12)			(-323.95)(Closed 6/1/2012)
USD/CNY			Hold	
EUR/AUD		1.3121 (12/2/11)		$585.37
EUR/TRY		2.3221 (1/6/12)		$272.03
USD/INR			Hold	
USD/KRW			Hold	
USD/MXN		12.9354 (4/2/12)		(-2190.26)(Closed 5/4/2012)
USD/TRY			Hold	
Total:				***$857.40***

The Best Opportunity in Real Estate

By George Ross

"Where is the best opportunity in real estate?" I'm asked that question often. The truth is that there is opportunity in every real estate sector; it depends what kind of investor you are.

If you're a small investor, residential real estate is where there is opportunity to put money in your pocket. Why? Because people always need a place to live. Also, most small investors can't compete with bigger, commercial investors. For the smaller investor, it's best to invest in a market where you can compete effectively. That's the short answer to a broad question.

It's funny, but a lot of people talk about business climates as being bad or good, or apply unrelated terms to describe the current market. I'm sure you have heard of the tech bubble, the stock market bubble, or the real estate bubble.

Cycles, Not Bubbles

But I'm here to tell you right now: There are no bubbles! Let me say it again: There are no bubbles! There are, however, cycles. All asset classes have cycles. It doesn't matter what they are. Take the business cycle in the economy for example; business expands for a while, and then it contracts.

An asset class is the same. The asset is up for a while, and then the economy changes, and then it's down for a while. That's it. Once you know this, you can look at buying or selling decisions from a smarter and more profitable perspective. Now that you know that there have always been cycles and there always will be, you need to know what affects an asset class cycle.

What makes the value rise and fall? This is very important because if you buy an asset at the wrong time in the cycle, you get hurt; you can lose your money. You need to know, as much as possible, where the asset class is in its cycle...Is it rising in value, or falling? Is demand going up or dropping?

This analysis is a more complex process, and there are many variables to consider, with some having more influence on the cycle than others. But, it is possible to develop your skills and knowledge to determine pretty accurately where a given asset is in its cycle.

For example, a tight lending climate, like we have right now, limits the ability of investors to buy. So does a poor economy. Fewer buyers mean less demand. That will cause prices to drop. Or, a rise in mortgage rates may cause also prices to drop. If borrowing costs more, prices will become lower. However, if the location is desirable or rental income is stable and high, the price may not be as impacted as it may be elsewhere.

Implicit is the importance of location as a factor in a property holding and increasing in its value over time. A very desirable location will tend to shield a property from the worst effects of a downturn, but not completely and not every time.

This brings us back to residential real estate. I see a lot of opportunity, but the next question is: "Which type of residential real estate makes the most sense? Condos? Residential apartments? Duplexes?" The answer depends on a lot of factors, but the main one is you.

Your Investor Profile

What's your investor profile? Are you a cash investor or a credit investor? What is the exact amount of money in your budget? Do you plan on holding onto the property as a landlord, or do you plan on flipping it? Can you make the necessary repairs yourself, or must you hire professionals? If you plan to resell the property, how long can you afford to hold onto the property if it doesn't sell?

If you are a credit investor, will you qualify for a loan? Will the rental income cover the mortgage? If it becomes vacant, how long can you afford to pay the mortgage before you have to sell it at a potential loss? Can you afford that? What return on investment (ROI) do you require?

These are the questions you should ask yourself; and you should know exactly what the answers are. Chances are, your budget will determine the type of residential real estate that you will target. Once you know your profile, then you can determine the type of acquisition you will target. Let's assume your goal is to acquire a duplex.

Profile the Market

You will need to analyze the duplex market in the area(s) that fit your investor profile and location.

What are the rents in the area? What is the rental history of the property? Is it stable, or have there been many short term tenants? What are the taxes like? What are the neighborhoods like? Are they desirable? Are businesses and schools closing? Is graffiti visible? What condition are the cars parked along the street? Are there many, or few? (Many may indicate a depressed area because few have jobs, hence their parked cars.) Are there more families in the area, or more single people? Be sure to view the neighborhood in both and night to get a better understanding of the area.

What are wages like there? What are jobs like there? Talk to the tenants if possible, but don't let on that you're considering buying the building. Tell them you're interested in renting in the neighborhood. Ask them how they like their home, things like that. You can learn a lot just by asking a few questions.

You need to look at external factors as well. For instance, are there city plans to widen the street or perform other major work? Is the zoning mixed use or strictly residential? If residential, what is the mix of owners and renters? Does the owner have other duplexes for sale? If so, you may be able to buy two at a deep discount, especially if you have cash. Once you have developed profiles for several target properties, you will have a much clearer idea of where you will be able to buy, and where you shouldn't, and the cash flows you can expect.

Bear in mind, however, that getting the highest possible ROI is great, but don't be led by numbers alone. They don't always tell the whole story; sometimes they conceal the most important factors in the deal. What you expect and what you get can be two very different things.

Know Your Seller

After narrowing your list of properties, find out as much as you can about the seller. Why is he selling? How long has he owned the property? What repairs have been done? Is the seller retiring? If so, you might be able to leverage his desire to retire and get a better price.

Try to establish a rapport with the seller and assess his honesty. Has he put a new roof on the building? Ask him for the receipt. Ask him to verify other claims, such as rental income and vacancy rates. If the seller gives you what you ask for, that's a good sign that he is not trying to hide anything from you. However, if he balks or acts insulted, then a red flag should be waving before your eyes.

This brings me to another rule for investing, no matter what the asset is: Never make a deal with a dishonest or untrustworthy person. Even if the numbers look great, if you can't trust the person giving you those numbers, of what value are they? Sometimes the best investment decision is to walk away from what appears to be a great deal.

Know Your Zone

If the property performs as well or better than you hoped, then everything is great. But what if it doesn't?

Figure out how bad it could possibly get, and how it would affect you. The area between the high and low points is your zone of nirvana. You want to stay within your zone of nirvana.

That's why it's important that your investor profile is accurate and true. And in every deal, always know the worst outcome. Know your tolerances in terms of time and money and potential for loss. Protect yourself like this every time and you'll do fine.

The Gorrie Details

Back to the Good Earth

By James R. Gorrie

"Make your money on Wall Street and bury it on Main Street," went the investment banker saying. But what do you do when Wall Street "hits the wall," so to speak? And Main Street is underwater and underemployed?

Where do you put your money then?

Not to paint too bleak of a picture mind you, but things have changed since the financial meltdown of 2008, By quite a lot, actually…

Not that the Wall Street cats aren't doing well, many still are... Multi-million dollar bonuses for investment bankers haven't been in short supply the past couple of years, so things must be going well, right?

At least they seem to be all right on Wall Street.

The jig is up

Let's face it, Wall Street a lot less of a reliable source of wealth than it used to be and is far less democratic.By that I mean that the mystique and status of the Wall Street investment world has changed…

The mystique has been replaced by derision and scorn from the American public as the curtain has been lifted on the bankers and how they have gamed system... The Facebook phenomenon is only the latest example of what has been standard operating procedure for a long time…

Playing the American public for suckers while manipulating prices. Don't get me wrong; a healthy stock market is crucial to the American economy…

The problem is, it's no longer healthy, and the incestuous relationship between Wall Street and Washington isn't good for the economy, either.

It begets crony capitalism and sows distrust in both the political and financial system from the rest of the country.

Mega bailouts, political protection, and the collusion to pick winners and losers in the economy are what the folks on Main Street see happening on Wall Street.

And it is very personal, After all, when Washington loosened the rules for mortgage qualification, it turned to Wall Street to make the risky loans that resulted from those lowered standards sellable to investors. Like you, me, and millions of others around the world.

And after the crash of both the financial system and the housing market, Washington then fed the Wall Street crowd hundreds of billions of dollars. We all know the story, but the point is, where can you put your money today that will hold at least some value going forward?

What about Treasury bills?

Are T-bills a safe place to park your money? They'd better be since the yields are at historic lows. But even T-bills don't protect your money when inflation and the probability of interest rates rising. Both of those will rob you of your principle while your money is in the bonds for "safekeeping."

That so many investors around the world are now putting their money in US T-bills—and not in the US stock market—speaks volumes about the concerns they have. A brief look at various financial sites and publications will tell you what you already know, That the trust investors had in financial institutions and markets just isn't there anymore.

And the confidence in governments' ability to solve the financial mess that plagues Europe and the US is in short supply as well.

As a result, many investors want to put their money into something tangible with value that they understand.

Back on the farm

And that's why producing farmland is where a lot of investors are finding some level of peace of mind as well as profit. Lots of profit. Prices for farmland in the American Midwest have gone up 30% in the past year alone.

But don't think this strictly a "Green Acres" play where city folk are leaving their urban lives behind, Investors are buying farmland and leasing it to existing farmers to work the land. In a time of rising food prices, farmland is proving to not only show high capital gains, But is also a very stable income play as well.

In fact, farmland is the one area in the real estate market that's booming right now. And it's not just in the US that farmland is in demand.

Working farms in Argentina and Chile are capturing American investors' interest as well. The properties are priced at bargain levels for US investors…

And those countries have a cost of living index that is a fraction of what it is in the US.

But Americans aren't the only ones buying up farmland as fast as they possibly can, So are the Chinese.

The Chinese government is buying great swaths of farmland in Africa, the US and Canada, as well as in New Zealand and Australia.

Like Wang Lung, the protagonist from the classic novel, The Good Earth, the Chinese seem to be clinging to the old notion that all wealth comes from the land.

The Chinese know a good investment when they see it, And they are also well aware of the long term rising cost of food.

Sustenance, they seem to understand, comes from the good earth.

Pearl S. Buck would be proud.

And those are…The Gorrie Details.

Mail Bag

Welcome to the Independent Wealth Alliance letter mailbag. In this section each month we answer questions from IWA members. This is your chance to ask us any investment or trading related questions you have. While we can't offer individual trading or investing advice, feel free to ask myself or our contributors what's on your mind and we'll publish selected answers in the mail bag each month. Write us at mailbag@independentwealthalliance.com

This month we have two questions to feature…

Q. *"What's your take on Facebook's IPO?"*

IPO's are not for the faint of heart. The reality is that any IPO is the 'coming out party' for the early investors and insiders who unload shares on the public that rushes in to make a quick buck. The Dot Com days conditioned many to expect tech stocks to shoot through the roof on IPO and that memory dies hard.

While there may have been some earnings misrepresentations and other hype factors that affected Facebook (FB) dismal IPO, keep in mind that the broad market had been tanking for days when the much anticipated IPO hit.

IWA contributor Hubert Senters recently said that he likes to watch for IPO's to settle down about 50% off their launch day price to buy. He showed a number of stocks including Groupon and LinkedIn that followed that precise pattern. For Facebook, a 50% off sale would be in the $19 range.

With over 900,000,000 people around the world using Facebook, and the way the social media site has become a cultural icon, I would expect FB to be a potentially good long term investment over the next 5 years if it breaks above $38, and it could be worth further due diligence to see if owning FB stock is for you. We may feature the stock in a future issue depending on which way things play out.

Q. *"Why is gold going down when the stock market is selling off so badly?"*

That's a great question. Conventional wisdom is that gold is a hedge against economic turmoil and that gold trades inversely with the stock market. While generally this is true, the fact is that for the last 10 years gold has become a far more speculative commodity and is still well above its historical prices from even just a few years ago.

For now, investors fleeing to quality have chosen the dollar and US bonds over gold. That said, at IWA our credo is to let the market tell us which way to trade, not to worry overly much WHY the market is going a particular direction.

For example, in this month's issue we highlight a very profitable short trade in gold that we'd have missed if we'd been expecting that gold could only go up because of the weak economy and turmoil in Europe.

The data on the chart reflects the sum total of all participants trading decisions and is far more reliable than any other source of information about the markets.

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