

SPECULATION IS FUNGIBLE

FRIDAY, OCTOBER 4, 2002

Market Lore:

Speculative action is fungible. Whether in stocks, bonds, or commodities, excess has similar and measurable characteristics as does its consequent unwinding of suddenly and chronically unsupportable positions.

Any veteran of the formerly notorious Vancouver Stock Exchange would note that no matter how preposterous the story is, as long as the trend is up it will be ardently believed and will enjoy spreading circulation. Then when the trend breaks, sobriety and chagrin prevail until the play is utterly abandoned.

Of course, within the lengthy liquidation process there are brief short squeezes and what has occurred with collapsing Vancouver schemes has occurred in New York a few times lately - a very dynamic rebound that lasts for a day and a half. The week enjoyed another such day and a half winning streak.

The Record:

Last month was widely reported as the worst September since 1937. In looking at the monthly chart, all of the biggest bars have been to the downside. Since 1900, these have also occurred in September 2001, November 2000, April 2000, August 1998, October 1987, May 1940, and September 1931.

The latter is the most pertinent as it was a September of Year 2 after the climax of a new financial era. Ours dropped 12% while the 1931 example clocked a 31% plunge. However, the cumulative declines are similar with the Nasdaq down 77% at the end of 3 Qtr. Year 2 and the Dow (speculative index then) down 75% to the equivalent 3 Qtr. Year 2. Hey, we are just the messengers - not editorial writers or investment bankers. Our product is research, not paper.

The Model:

For 2 Qtr. 2002, the high was expected for March and that it would be the high for the year would be confirmed by the ChartWorks registering important "overboughts" (✓) with a sharp plunge in April (✓). New lows for the bear were expected in June, but were not accomplished until July 23. Then, after some recovery until late August-early September, the decline would resume and set the low for the year around December.

Outlook 2003:

Due to the unprecedented continuation of the boom in the median home and big cars, the economy is not as bad as the action in stocks and credit spreads. On October 2, the WSJ observed: "Tumbling share prices may have hammered portfolios. But, instead of limiting the damage by saving more, many Americans have retreated into an orgy of spending." However, veterans of the markets, rather than contrived economic theories, know that the compulsive action inevitably reaches saturation.

The editor's alert to this failure has been unrequited since April. But the reversal in the treasury curve to steepening and in Fannie's changing fortune suggests that the speculative anomaly could pop.

Every cyclical or secular bear market in history has been eventually accompanied by the equivalent in business activity and we do remain alert to this. In spite of this, the rally out of this hole until around May could merit an increase on equity weighting.

Asset Allocation:

When our boom indicators reversed in February, 2000, the advice was to reduce equity exposure from 60% to 40%. Then, when the models worked out so well on the rally to May, 2001, the advice was to reduce to 35%, which would be the minimum. The Indicators remain unchanged at the very concerning -11 and, should the car and house boom fail, it would drop another notch.

Nevertheless, some technical and historical work has been calling for an important, and possibly cyclical, low for around November-December and it seems appropriate to increase weightings from 35% to 42% equities.

One Model:

The ChartWorks "post-euphoria" patterns following the extravagances of Dow 1929, Gold 1980, and Nikkei 1989 have provided outstanding guidance on the main trend as well as on the intervening trades. We have also called the model "Road Maps" and these have led us to a significant low for the late October to early January window, from which, on each example, a cyclical bull market ensued.

Speculative Match-Up:

The chart of GE 2000 to ? compares with the Dow 1929 to 1932 as follows.

ChartWorks

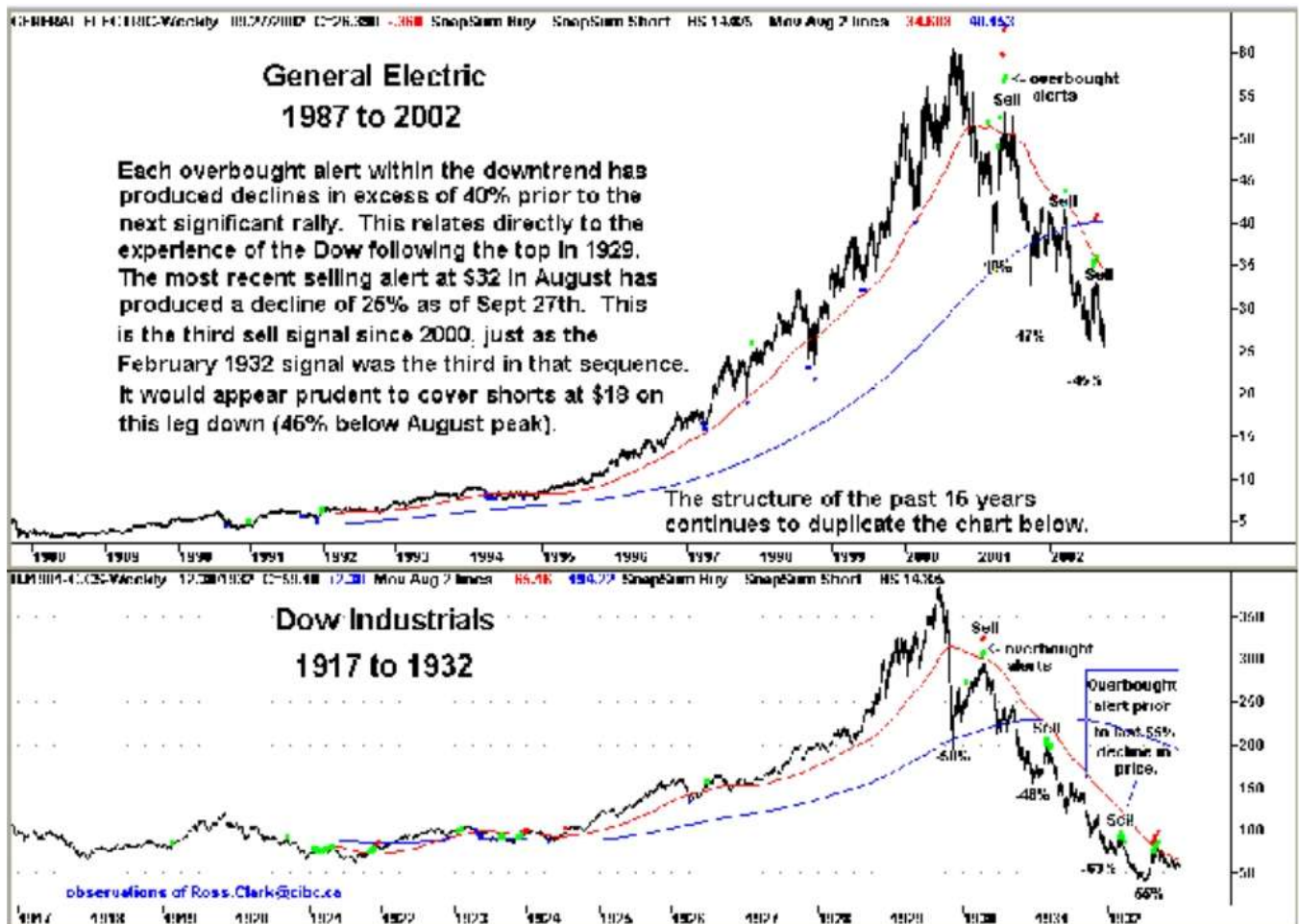
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GENERAL ELECTRIC

The fundamental woes of GE continue. Remember when the pundits on TV said Tyco was the next GE? Well what if GE is the next Tyco? Technically, this stock has been "on track" for us right through the top at \$60.50 on September 1, 2000, the first MACD short sale recommendation at \$58.50 and all the way down.

- For the track record, check the website under Archive ["General Electric 2000 to ??"](#)
- Last "buy" was in Capitulation list of June 27, 2002.
- Last "sell" on overbought alerts on August 1 at 32. "Keeping in mind our target of 12, it's selling time again."
- Using the typical 45% decline following the "overbought", this decline measures to around 18.



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