

ASPERA BULLETIN

Intelligent, Independent Investment Management

Bear Rally Chatter

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919-622-2076
Cary, North Carolina
ken@asperafinancial.com





This market continues to favor traders and thrill seekers. I've talked about fading this market a number of times in the past few months, and, at the margin, that's what I've been doing. The basic rule has been simple: when my wife has had to talk me off the railing of our one-story deck, it's time to buy, and when I start doing Schwarzenegger impressions, it's time to short. Recently, I've been doing Schwarzenegger impressions on the deck railing.

In mid-late November, I added positions in UWM and QLD as the market was again rolling over and the VIX (fear) index was once more spiking towards record levels. Since that time the number of market professionals looking for a bear market rally seems to have grown by the day. I've read quite a few of them just this week talking about a rally into early next year, even those who are very bearish. I'm a bit surprised by the timing of these calls considering that the market has already rallied 20% from its intraday low on November 21st. There's nothing like a good rally to bring out a bunch of predictions for...a rally. The lemmings that went over the cliff are climbing back up for the next jump.

Bear market rallies much greater than 20% aren't exactly common. That certainly doesn't mean that the current rebound can't go significantly higher. Recall, we had a 50% rally during the Great Depression, so there is precedent for very powerful upward moves during bear markets, but these types of moves are very unusual.

In fact, some of the strongest short-term market rallies tend to come during bear markets. It's easy to understand why: fear and greed. On the one hand, the market tends to get oversold in the short-term as fear of a job loss, insolvency, plague, and children who may never leave home grips the masses, and wholesale selling ensues. At the same time, investors who've lost a lot of money are eager to jump on any potential rally that may help them recoup some of their losses in order to help their child with the security deposit on their first apartment. And you never know, the next rally could be the beginning of the next bull market. Who wants to be the idiot who sold at the bottom and kept waiting forever for another chance to buy at those levels?

Back to the present. With a 20% rally already in hand, I have to believe that the easy money from this leg up has been made. That doesn't mean that the market can't go higher, but I'm back at what I call "an inflection point moment." I can't bring myself to add more general market exposure given the move we've already had (though I'm always scouting for individual company opportunities), yet the move up isn't so overdone that there's a clear signal to sell. Unfortunately, I'm just not smart/foolish/prescient/daffy enough to try and call market tops or bottoms, particularly those of a short-term nature. As a result, in this type of

environment I tend to build marginal market long and short exposure as the strength or weakness of the market accelerates.

In keeping with that, I haven't yet sold the QLD or UWM positions, but they will be jettisoned should the market rally much further. In the meantime, I'm willing to give them a little more time as the market has finally been responding well to bad news. I have, however, recently added some modest new short exposure in the real estate area. This is partly due to the fact that this sector has had one of the smartest rebounds during this latest market rally. With the market up 20% from its lows, many real estate ETFs are up closer to 50%. This is a logical pool for bottom fishing given the degree of damage we've already seen, but I'm of the opinion that this sector will see further downside, particularly commercial real estate. The current short position is modest, and my intent is to increase the short side of the portfolio (and reduce longs) should the market rally continue.

This particular rally has been gratifying in that many of our core positions in the commodity, mining, industrial, and precious metal sectors have had nice moves. The recent decline in the U.S. dollar from ridiculous levels hasn't hurt. Many of the names/positions in these sectors are trading at very attractive valuation levels for those willing to look beyond the next few days. I've been gradually adding to this space during the downturn and expect to be very pleased with their performance over the next 5-10 years. In the near term, however, they won't be immune to the next sell-off in the market (at which time I'll be adding to them).

Best,

Ken Bell, CFA, CFP
President
Aspera Financial, LLC

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