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On The Mark Investing

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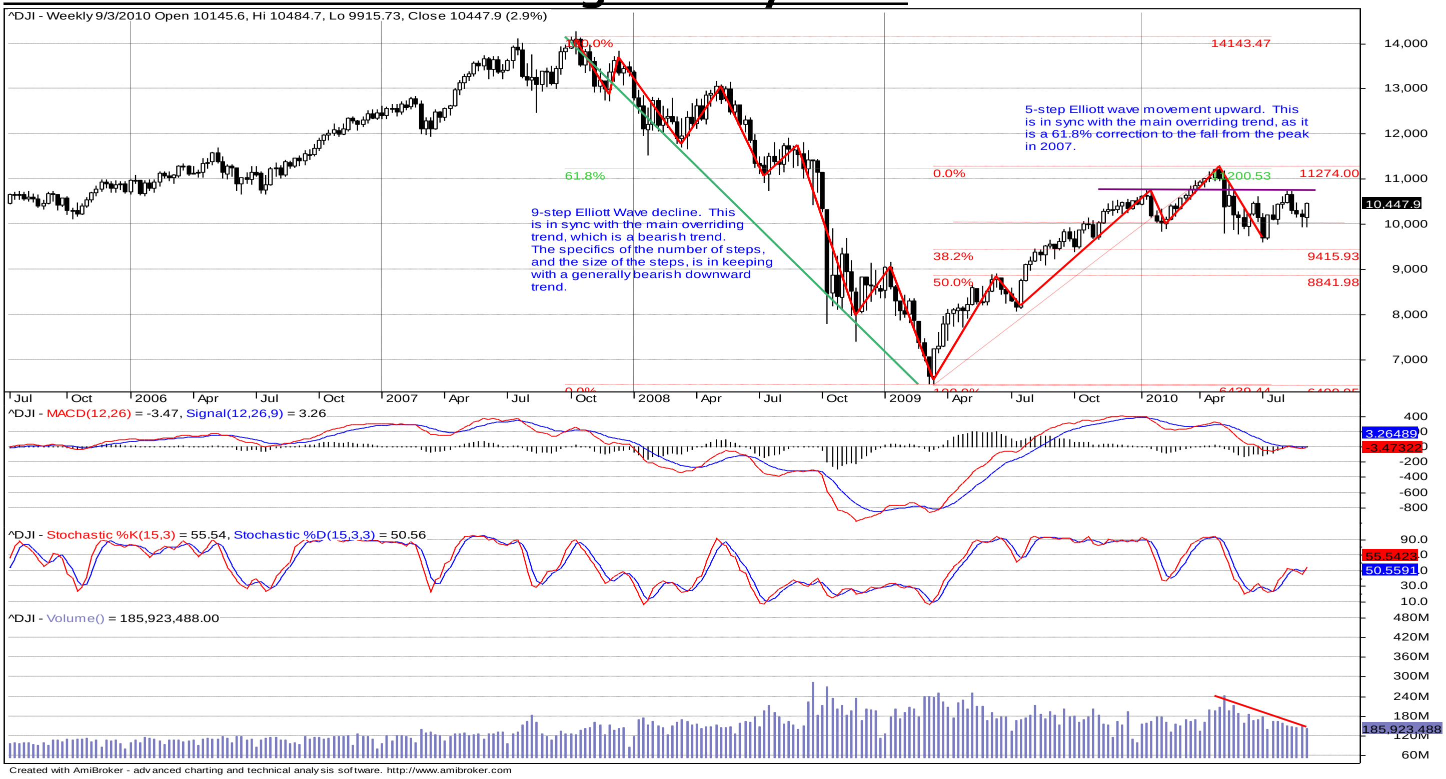
Broad Market Trend using Weekly Data



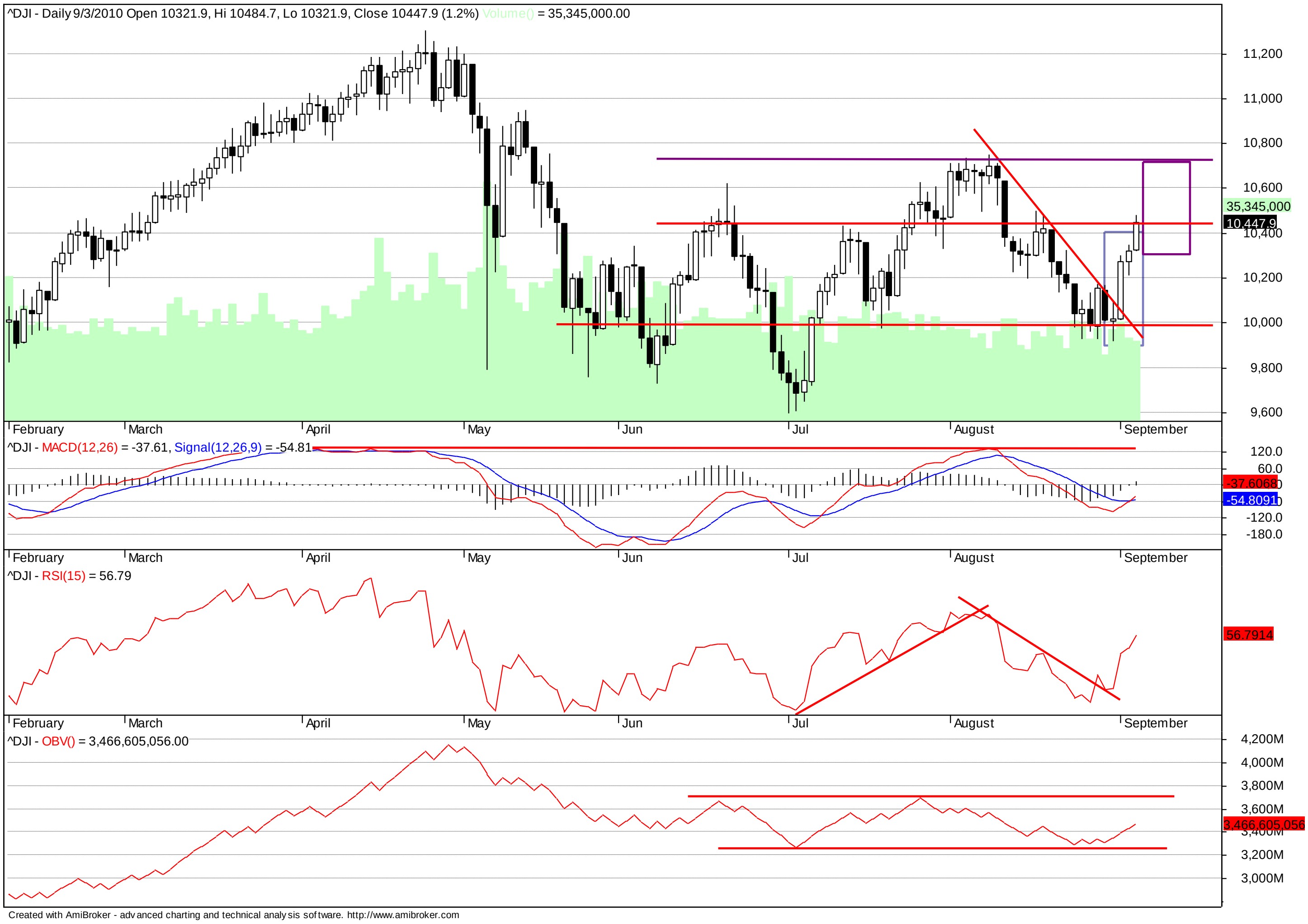
The Dow Jones Industrial Average (^DJI) gained 2.9% last week, finishing at 10,447.

The market is still in a trading range, bounded on the bottom by 10000 and on the top by the PURPLE line at 10700.

Last week I noted "A down market turns into an up market when all of the potential sellers are through selling. We have had a raft of bad economic and political news. The market has reacted with a malaise, drifting sideways-down but for the most part absorbing the news. We could be approaching a point where bad news doesn't move the market downward, but good news would start to move the market upward."

Until the market breaks conclusively out of this 700 point range, it is just a ranging market. The volume has not picked up to any degree, so the odds at this point of follow through above 10700 are very low.

Near-Term Market Trend using Daily data

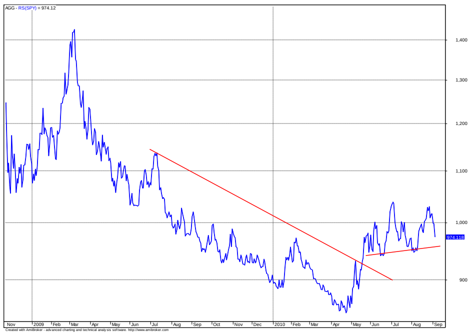


The market spent most of last week in a trading range inside the nice little rectangle that I created (which is now a blue-grey box). Relative Strength has broken its trend line and appears to have the ability to move up further, albeit at a less-steep angle. That would imply further rise in the market. MACD is now at a crossover, where the RED MACD line is moving upward through the signal. When it sits above the signal, that implies that shorter term moving averages are higher than longer term averages, which implies more recent positive movement. Finally the On Balance Volume looks like it can continue to move upward without encountering resistance. All in all, there appears to be room to move further upward.

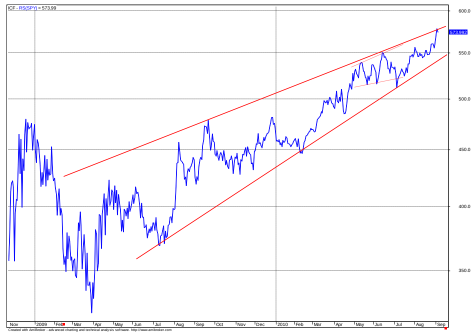
Because volume has not moved upward with price, and because the PURPLE 10700 line has been an upper limit for this ranging market for a variety of reasons, I am assuming a range this week from 10300 to 10700.

<u>Asset Class Behaviors</u>

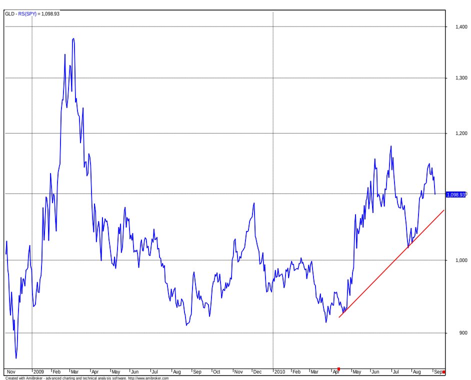
The charts below are <u>not</u> the price of the security. They are the ratio of the price of certain ETFs to the value of the SPY (S&P 500 ETF).



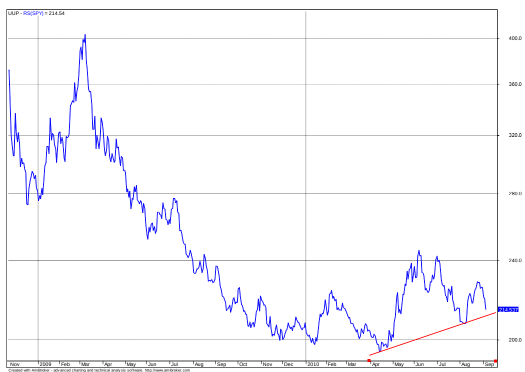
Bonds (AGG) have some near term weakening, but until this breaks the trend line I don't see reason to reduce the present position.



Real Estate (ICF) continues strong relative to the market on the whole. But in a weak market there is risk in the Real Estate play at this time.



Gold (GLD), like Bonds, are retrenching slightly relative to the overall market. Nothing to react to at this point unless the above trend line is penetrated.



Dollar (UUP) is also catching its breath after moving upward relative to the overall market. We'll see in the next week whether this recent drop violates the 6 month trend line and becomes material.

ETF Hedge Fund – Description

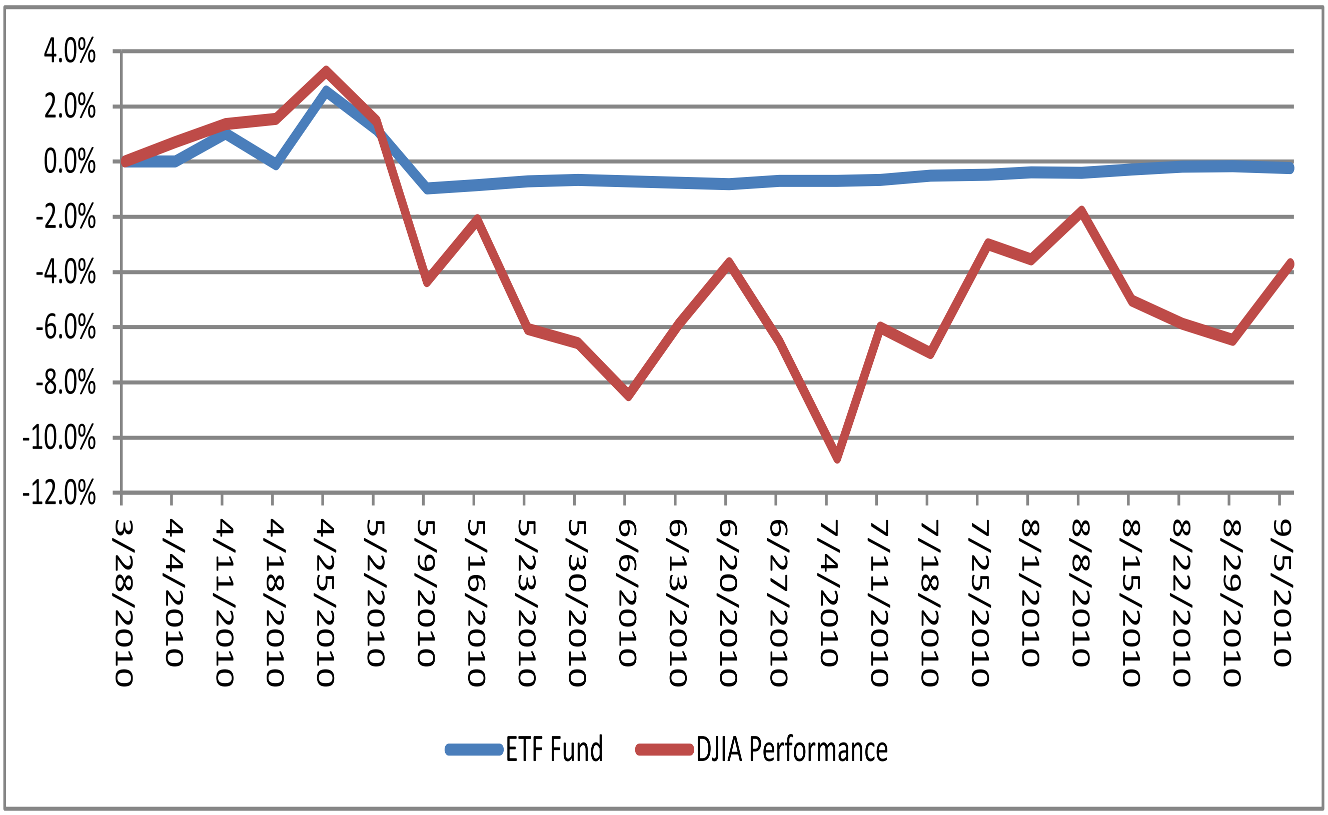
The ETF Hedge Fund consists of a set of loosely-correlated ETFs (Exchange Traded Funds). It is aimed at the conservative investor who is looking to preserve capital, avoid major market downturns, and ride market upturns. Trading occurs no frequently than weekly, and the ETF Hedge Fund has a bias toward conservative money management. ETFs can be bought just like stocks using Schwab, TDAmeritrade, Etrade, or any other electronic brokerage.

An ETF is a commonly traded security that represents a published proportion of underlying securities. For example, the ETF going by the ticker symbol "SPY" consists of a basket of stocks matching the proportion used in the S&P 500 index. ETFs have the advantage of being liquid, traded like stocks, and diversified like a mutual fund since they consist of so many underlying securities.

ETF Hedge Fund – Performance

Performance from inception, 03/28/2010 to Current

The ETF Hedge Fund is down -0.23% before dividends. The DJIA is down -3.71% in the same period.



You can see the moderating effect that properly using uncorrelated assets can have on overall return. Note that in the April timeframe, as the market was moving upward, we took advantage of the trend. In the last 4 months, we are positioned to retain our gains as the inevitable corrections occur.

Were dividend income to be included in the overall results, the ETF Hedge Fund would be positive for the year.

Assumptions in the above chart:

1) You followed all BUY/SELL/STOP LOSS instructions for the security since March 28, 2010
2) Equal amounts were invested each time the security was purchased
3) All shares were sold at the time of the SELL order
4) No commission or transaction fees are included
5) No dividends or capital gain disbursements are included

ETF Hedge Fund – Security Detail

	The BUY/SELL notes below are from mechanical models and used as a reference. Please see notes directly below this table for further clarification and direction.				Current Position Stop Loss	New Position Stop Losses	
Security	**Long-Term**	**Med- Term**	**Short Term**	**Price**	**SELL**	**BUY**	**SELL**
SPY (S&P 500 ETF)	SELL (Jun 30) (103.22)	SELL (May 20) (107.54)	BUY (Sep 3) (110.89)	$110.89			
AGG (Bond ETF)	BUY (Apr 30) (104.89)	BUY (Apr 29) (104.44)	BUY (Apr 15) (104.26)	$108.02	$107.53	$104.75	$104.00
ICF (REIT ETF)	BUY (Jul 7) (55.30)	SELL (Jul 2) (53.66)	BUY (Sep 1) (61.92)	$63.65	$57.97		
GLD (Gold ETF)	BUY (May 24) (116.84)	BUY (May 24) (116.84)	BUY (Aug 3) (115.99)	$121.86	$117.40		
UUP (Dollar ETF)	BUY (Jul 14) (24.25)	SELL (Jul 14) (24.30)	SELL (Sep 2) (23.91)	$23.79			
DOG (S&P Inverse)	SELL (Jun '09) (66.50)	BUY (Aug 20) (51.16)	BUY (Aug 25) (51.95)	$49.87			
MUB (Tax Advantaged Bond)	BUY (Mar 18) (103.49)	BUY (Mar 18) (103.49)	BUY (Apr 16) (103.48)	$106.61	$105.85	$103.40	$102.75

Note these comments:

1) **We only BUY when all three models are in sync and suggest BUY.**
2) General equities (SPY, ICF) are in a short term upward period. If the DJIA moves above 10700, that will be our key to play this in an intermediate term fashion. Until then I am not recommended a BUY unless you want to play this as a daily strategy.
3) The S&P Inverse (DOG) is now flashing a BUY in the short term. In keeping with the intermediate term philosophy, we are not advocating a BUY at this time. But were the market to fall below 10000, we'd probably pick up the long term BUY signal and that would be the time to invest.
4) Bond funds (AGG, MUB) have been bid up such that they are very expensive. You should wait to "buy on the dips" so to speak. So you will see that even though the models say they are BUY, you should wait until the price drops before adding to your holdings.
5) Given that the market is moving sideways, Gold will be a bit unpredictable. It is probably safe to trade at this point as a short-term, day-to-day proposition, but it is unclear that an intermediate-duration trend is underway. So I am not recommending GLD for intermediate-term trading.
6) The US Dollar is in an intermediate-term technical correction cycle and is not good BUY at this point.

Remember to set the stop loss as indicated.

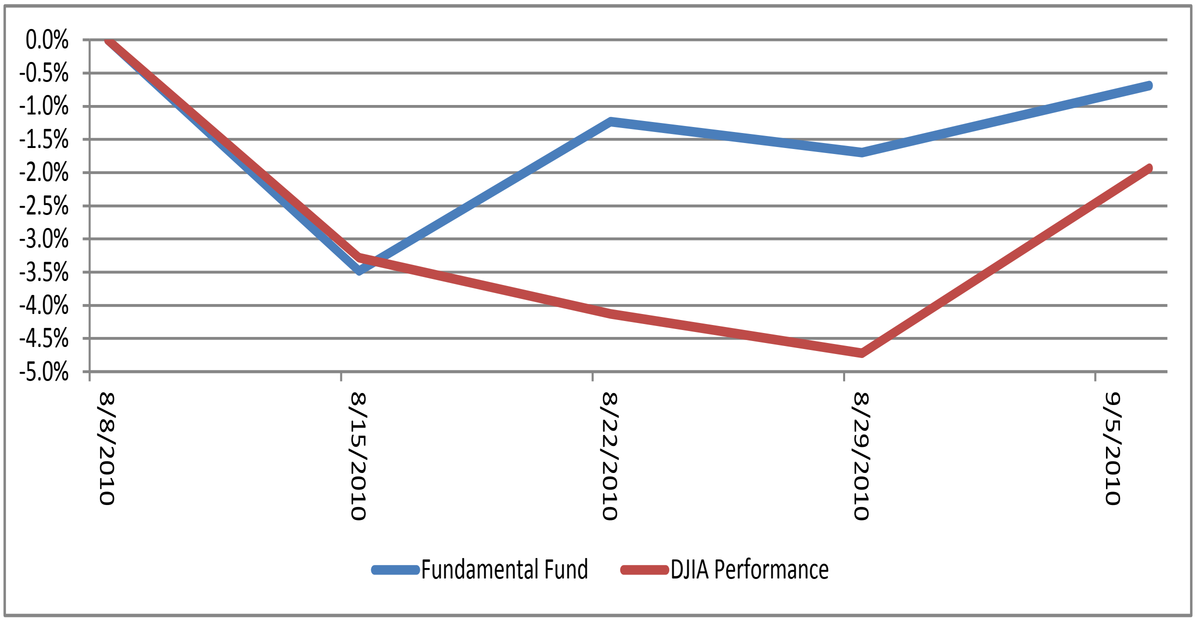
Miley Fundamental Fund – Description

The Miley Fundamental Fund consists of value-based stocks that have been picked by Dan Miley, who is an experienced trader that specializes in a Fundamental Approach that has been outlined in past newsletters. These stocks will then be married up with a Technical timing component, resulting in a set of recommendations that attempt to marry the best of fundamental investing with technical timing.

The Miley Fundamental Fund is designed for Intermediate Term investors that are prepared to wait a bit for good value plays to be realized by the market. This is not designed to be day-traded.

Miley Fundamental Fund – Performance

The Fundamental Fund is down -0.69% before dividends. The DJIA is down -1.93% in the same period.



The Fundamental Fund is designed to achieve greater returns than market over an intermediate period of time. We will need a period of time to determine its success.

Assumptions in the above chart:

1) You followed all BUY/SELL/STOP LOSS instructions for the securities since August 8, 2010
2) Equal amounts were invested each time the security was purchased
3) All shares were sold at the time of the SELL order
4) No commission or transaction fees are included
5) No dividends or capital gain disbursements are included

Miley Fundamental Fund – Security Detail

	The BUY/SELL notes below are from mechanical models and used as a reference. Please see notes directly below this table for further clarification and direction.				Current Position Stop Loss	
Security	**Long-Term**	**Med- Term**	**Short Term**	**Price**	**SELL**	**Recommendation**
Providence Service (PRSC)	BUY (Ju1 1) (13.34)	SELL (Jun 30) (14.00)	BUY (Sep 3) (15.05)	$15.05	12.47	BUY.
First Cash Financial (FCFS)	BUY (Jul 31) (18.79)	BUY (Jun 5) (16.82)	BUY (Sep 3) (25.73)	$25.73	22.91	BUY.
Apple (AAPL)	BUY (Jul 20) (251.89)	SELL (Jul 19) (245.58)	BUY (Sep 3) (258.77)	258.77	236.19	BUY.
Ensign Group (ENSG)	SELL (Jun 30) (16.52)	BUY (Jul 30) (18.00)	SELL (Aug 24) (17.45)	$17.87	$16.69	HOLD.
Almost Family (AFAM)	SELL (Jul 1) (35.01)	SELL (Jul 1) (35.01)	BUY (Jul 23) (24.98)	$25.62	$23.01	BUY.
InterDigital (IDCC)	BUY (Aug 24) (25.30)	SELL (Aug 27) (25.19)	SELL (Aug 11) (26.13)	$25.96		SELL.

Consistent with the belief that we are in a short-term uptrend in the broad market, the mechanized models are indicating BUY opportunities on a number of the securities in this fund.

The Miley Fundamental Fund is value-based, and as a result you have to allow more market volatility in order to give the market time to react to the full value of the stock. You will note that some of the stop loss positions are a bit wider than in the ETF Hedge Fund.

On Fundamentals alone, all stocks in this fund are a good value. However only those stocks with a New Position Buy and a New Position recommended Stop Loss are at BUY status this week. Whether you invest, and how much you invest, should be based on your ability to be comfortable with the underlying risk of a wider stop loss position as well as most recent performance. Make sure you implement a stop loss on all purchases.

Mutual Fund Guidance

Security	Recommendation	Current Price of Proxy	Guidance
Equity Mutual Funds (SPY as a proxy)	(May 24) SELL when SPY was below 110 for 3 days. ($107.71)	$110.89	You should be out of equity funds until this lateral market resolves into a trend.
Bond Mutual Funds (AGG as a proxy)	(May 16) BUY	$108.02	
Money Market	Do not hold cash	N/A	You should be in fully in bond mutual funds at this point.

Rules for 401K Mutual Fund Portfolios

Segment your 401K portfolio offerings into Equity, Bond, and Money Market. Most equity funds (Large Cap, Small Cap, International, Growth, Value) are very tightly correlated and should be considered as a single asset class. Of these, if you have an S&P Index fund, choose this as your Equity fund. Most bond funds (government, mortgage) are tightly correlated. Of these, if you have a government bond fund, choose this as your Bond fund. You typically will not have a Real Estate or Gold option for 401K portfolios.

New Investing Suggestions
None.

The Final Word
The following is an article from the American Association of Independent Investors entitled "Sustaining Wealth in an Uncertain Environment". Lots of good points, I think.

About the author: **Charles Rotblut** , CFA, is a vice president at AAII and editor of the AAII Journal. *Axel Merk is author of the new book "Sustainable Wealth" (John Wiley & Sons, 2010).*

Charles Rotblut (CR): *Many people have seen their portfolios rebound since the bear market, but still do not have the wealth they had a few years ago. What are some steps that someone in this situation should consider if they are trying to figure out what to do with their portfolio now for the next 10, 20, or 30 years?*

Axel Merk (AM): The big challenge facing investors right now is where to place their savings. We have witnessed a major rally across most asset classes from their lows. While the major stock indexes may continue to go up, there is considerable risk that stock prices may experience a significant correction. In parallel, there is a substantial risk that interest rates might go up. There's a substantial risk that inflation might go up. There's also a substantial risk that all the government intervention that has occurred over the past two years is causing distortions, including a disincentive to invest because of erratic policies. All this may impact investments, and investors are spooked.

From my point of view, in this sort of an environment caution should prevail. This may sound counterintuitive—especially if people are desperately trying to make up the money that they previously lost—but being very conservative can be the best strategy.

A strategy that involves being very conservative does not necessarily mean that investors should simply park their money in cash. In fact, in the present environment of increased central bank intervention, even cash may need a diversified approach. Consider what central banks are doing, which is diversifying their reserve holdings. Central banks aren't simply holding one currency; they are diversifying globally in baskets of currencies in an attempt to mitigate the risks associated with any one currency. But at the same time it's not risk-free either. In my view, there is no such thing any more as a risk-free investment. For the individual investor, the lack of a risk-free investment poses some very great challenges and there is no easy answer.

The best thing an individual investor can do is try to be alert, try to be diversified and to allocate assets in a way that provides true diversification. In the fall of 2008, most people came to the harsh realization that allocating their portfolios among growth stocks and value stocks, large cap and small cap, and real estate, did not provide sufficient diversification. As a result, investors need to look for alternative ways to diversify. That, of course, can be very difficult. There are more and more mutual funds out there now that offer additional ways to diversify your investments into low-correlated asset classes. Ultimately, when it comes to diversification, an investor should really look at the return stream that any investment is generating—and not just think 'Oh, it's a slightly different asset class and, therefore, it has to be providing diversification.'

Monitor very closely how different asset classes perform in parallel: One of the best market bubble indicators is when a wide range of different asset classes increasingly move in tandem. That has been happening all the more on the back of policymakers' decisions to throw trillions of dollars at any and all of our financial problems. Many asset classes have become inflated, moving up in lockstep. While everybody feels good as everything goes up, the risk that the bubble may burst also increases. That is the exact time when people may want to consider taking chips off the table, diversifying further or becoming more conservative.

One has to be willing to make these choices realizing that they may not make the decision at the most optimal time. But an investor has to make it in the context of their risk profile and what they can afford to lose and obviously always in the context of whether there are better values elsewhere, better opportunities to deploy your assets.

Sustainable Wealth Principles

Axel advocates that to build sustainable wealth, investors should challenge conventional wisdom, which would have you focus too much on your income and assets (which you cannot control). Rather, investors should take time to focus

on the things they can control: their expenses and liabilities.
Key maxims of sustainable wealth management are:

- Income and asset values can be influenced, but will fluctuate beyond an individual's control;
- An individual, meanwhile, has full control over his expenses and liabilities.

Axel lays these factors out in what he calls the "Sustainable Wealth Grid."

Sustainable Wealth Grid

Income: *Influence*	**Assets:** *Influence*
Expenses: *Control*	**Liabilities:** *Control*

***CR**: In your book, you discuss challenging conventional wisdom when making portfolio decisions. Would you explain what investors should be thinking about in terms of challenging conventional wisdom?*

AM: Despite the uncertainty, it is critical for an investor to remember that they are at the controls. This means it is the investor's responsibility to challenge conventional wisdom and determine what they want to achieve with their portfolio. When you use an investment advisor, for example, work with that person. Financial advisors may be tempted to just use an allocation model, where investors simply give them two or three parameters that are "plugged in." But does it really work? Don't just say 'Oh, I have a high-tech company and a large-cap company and this or that and, therefore, I'm diversified.' Look deeper. Look at where the returns are being generated and whether these returns really are non-correlated.

Emotions play a large role too. The best example is housing. Many people think that home prices are too expensive when they try to look for a house. However, once the house is purchased, investors find a thousand reasons why the neighboring homes are underpriced and should really be much higher.

Investors should always try to distance and personally detach themselves from the investment and try to make a rational decision based on parameters that they looked at when they initially made the decision. That's one way to look at these things.

Another way to look at conventional wisdom is to really develop a picture of how the world is evolving and use that as a filter in your investment process. That doesn't mean that an investor with a strong worldview should put all their eggs in one basket. Sure, if such an investor puts their money where their mouth is and gets it right they can make substantial returns. But should they get it wrong, they can also lose a lot of money. What I like to do is assign probabilities to my various economic views and invest accordingly. In addition, don't be distracted by the mood of the day. Rather, make adjustments based on your life situation, based primarily on the risk that you can afford to take.

This also means that during a bull market, the underperforming assets might be fulfilling a purpose. When assessing any investment, first look at why that investment was made in the first place, and sell the security only if the reason why you bought it doesn't apply anymore.

***CR**: Carrying this a step further, if someone has a view on the direction of the economy and the markets, how do they balance their expectations with keeping risk levels at acceptable levels?*

AM: In order to make those decisions, an investor has to take into consideration, first and foremost, the risks they can take. They should look at their current situation, future cash flows, other assets they have, any future costs they will face and so forth. An investor cannot simply be guided by the fact that things have plummeted or gone up. The moves of the market are really secondary. An investor needs to find good values, assess the types of risks they can take and then make their investment decisions accordingly. Over the medium or long term, if the investments rise, that's great. But if they don't, the investor has only taken the risks they could afford to take.

Now that doesn't change the fact that many people haven't saved enough. But an investor cannot fix that problem by pouring more money into risky assets. The worst thing an investor can do is say 'Oh, I haven't saved enough. Therefore, I have to chase the latest trend and I have to go into this risky investment.'

That's one of the important messages of my book. In the book I refer to Richard Russell [Dow Theory Letters newsletter advisor], who says the difference between the poor investor and the rich investor is that the poor investor will always try to chase the next trend, and will ultimately be bound to invest at the top of any trend and lose a lot of money. Conversely, the wealthy investor has many more streams of income and has plenty of opportunities, so they can afford to miss a rally. A wealthy investor can look for the right value, wait it out and if they see something they like, make the investment. With such a strategy, even the poor investor could become rich: If he just looks for value, looks for the opportunity and only puts down the money when he can afford it, over time, through compounding, that investor can build quite a substantial nest egg.

***CR:** If someone is dependent on income from their investment portfolio—maybe they're taking required minimum distributions—what's your strategy? Should they consider staying in short-term Treasuries and wait for interest rates to get better?*

AM: The Federal Reserve has been the enemy of anybody who has savings. Anyone with savings is not getting rewarded with the current policies. The Federal Reserve wants to keep interest rates low to boost economic growth at any cost. And by having interest rates near zero, investments are not going to provide much income.

Rather than accepting these near-zero interest rates, investors are looking for riskier strategies. This is good if the bonds deliver, but it is not so great if the bonds default. It is a very tempting thing to go into higher-yielding securities, on the fixed-income side in particular. But when you go down in credit quality, you can face very serious risks.

This is why it often does not make sense to try to get just a couple of extra percentage points of yield for taking on tremendous risks. If the issuer defaults, the investor may end up getting close to nothing. Is a 3%, 4%, 5% or 6% premium really enough to compensate for that additional risk? Should an investor buy junk bonds? For many people who are close to retirement age, this simply may not be appropriate.

Conversely, of course, an investor can go out on the yield curve. He can buy longer-dated bonds. However, there is the risk that inflation gets priced into the market. Or if the market requires higher real rates of return because of the government spending, then he may also lose out. That means an investor is just going to get a very lousy return right now and yield-seeking investors may need to stick it out.

***CR:** You talk about personal spending in "Sustainable Wealth," something that is not typically discussed in investment books. Could you explain how personal finances fit into portfolio planning?*

AM: Sure. The other side of the equation everyone has to work on is the cost of living. Nothing gets around it, and it can be a tough choice. For most of us, there's no government bailout waiting around the corner and so if you can't meet your obligations through the asset side or income side of things, then you do have to fine-tune the living expense side.

This is not just an important point; it is ultimately the most important point. Companies don't go bust because of missing revenues; they go bust because their expenses are too high. People don't declare bankruptcy because they don't have income; they go bankrupt because their expenses are too high. Once somebody has an iPhone, cable television or latte at Starbuck's, they want to keep it. It takes both small and large steps. The easiest step, the one thing an investor can control, is expenses. The investment is something a person can make better and worse decisions about, but on the expense side people don't do enough.

***CR:** Let me ask you about taxes. We are looking at a situation right now where, as you know, the Bush tax cuts are expiring and it's uncertain what new tax policies will emerge from Congress. Even though you suggest not investing based on tax policy, taxes still weigh on investors' minds. What are your suggestions?*

AM: As far as taxes, if there's one thing worse than high taxes, it is uncertainty about taxes. We all hate our taxes but the one thing that's really bad for investing, and also for business investment and personal investing, is uncertainty over regulations.

This year people can convert their investments to a Roth IRA account from an IRA account. The key thing about that is in a Roth IRA account an investor is not required to make any withdrawals, unlike standard retirement accounts. What that means is that if an investor does not need to rely on that income stream, he can allow that money to continue to grow tax free. If people don't need to make a withdrawal, then a Roth IRA is a good way to go. Even if you're not the youngest person anymore, you may want to discuss with your tax advisor whether that's a reasonable strategy for you.

Given the massive budget deficit, the government increasingly relies on taxable income to meet its obligations, which is why they are raising tax rates. The cost of borrowing for corporations and the government also may go higher. Investors will demand a higher return to compensate for those taxes. While on the one hand higher taxes will reduce the income an investor is getting, on the flip side, investors will demand higher returns. And of course, if one takes it a bit further, this means the headwinds for corporate America are going to get stronger because the cost of borrowing is going to go up with higher taxes. People always think of higher taxes only from their own perspective. But there's really one perspective for the government, one for individuals, and one for businesses—and these are dynamics that will have a profound impact. Again, clarity is often more relevant in the long run than high taxes alone.

INVESTING IN BOOM AND BUST MARKETS

In his book, "Sustainable Wealth," Axel offers the following suggestions for investing in boom and bust markets.

Boom Markets:

- Diversify your income stream; focus on cash flow.
- Take on more risk, but only if you feel comfortable; ensure other bases are covered.
- Do not expect to find the top; take profits when warranted, don't hang on too long.
- Take some money off the table; recent winners should not make up too large a portion of your portfolio.
- Invest what you can afford to lose; be realistic about this amount.

Bust Markets

- Diversify your income stream; focus on cash flow.
- Consider a steady asset allocation; maintaining that allocation will automatically defend you against busts.
- Take less risk; if market risk increases but your risk profile hasn't, pare down risk.
- Do not expect to find the bottom; markets can overreact, be patient.
- Put money on the table slowly; consider cost averaging.
- Invest what you can afford to lose; this value may change in a bear market.

***CR**: Those are good points. Anything I didn't ask you that you think should be mentioned?*

AM: People always talk about investing, but often overlook the cost side, and the other important aspect: sustainable life balance. Put investing into the context of where you are in life and what you want to do with your life and with your investments. A person should not be a slave to their investments. Rather, investing should be a tool that helps you achieve your goals. If you are stressed about your investments, odds are that you need to change something. Maybe lower the risk profile, maybe look for a different advisor, or maybe look for an advisor if you don't presently use one. At the end of the day, you need to be able to sleep well at night with your investments. If you can't, you should reassess your investment positions

Appendix – Important Details

Rules for Placing Trades

1) When you place a BUY order, you will also place an associated SELL order for the same security. This is designed to keep you free of constantly checking progress of the trade, and it is designed to build the discipline of always having a set of stops in place to control downside risk. This can be automated on TD Ameritrade by using what are referred to as “Conditional Orders”. On Schwab these are referred to as “Bracket Orders”. Lacking these automated tools, once you execute the BUY order you can go in the day after the BUY and manually place the protective stop.
2) All of your orders (BUY and SELL) will be done using Stop Market orders. That is, on a BUY order the market price must rise to a particular price before you BUY. This gives you initial confirmation that the market price is moving in the expected direction. On a SELL order the market price must fall to a particular price before you SELL.

Rules for Adding New Money to Existing Portfolios or Building from Scratch

1) Only add new monies to securities with BUY in Long-Term, Medium Term and Short Term. Otherwise, keep the money in a money market fund.
2) Do not increase the overall size of the portfolio more than 12% a week, in order to limit market risk.
3) Always enter the noted stop loss amount with each investment. Do not enter a purchase without an associated stop loss amount.

Things to be Aware Of….

First, I hold a number of positions in this newsletter.

Second, the information contained herein is based on sources that I deem to be reliable but is neither all-inclusive nor guaranteed for accuracy by me and may be incomplete or condensed. The information and its opinions are subject to change without notice and are for general information only. Past performance is not a guide or guarantee of future performance. The information contained in this report may not be published, broadcast, rewritten or otherwise distributed without my consent. Pursuant to the provisions of Rule 206(4)-1 of the Investment Advisers Act of 1940, all readers are advised that they should not assume that all recommendations made in the future will equal that referred to in this material. Investing in securities involves risks, including the possibility of loss.