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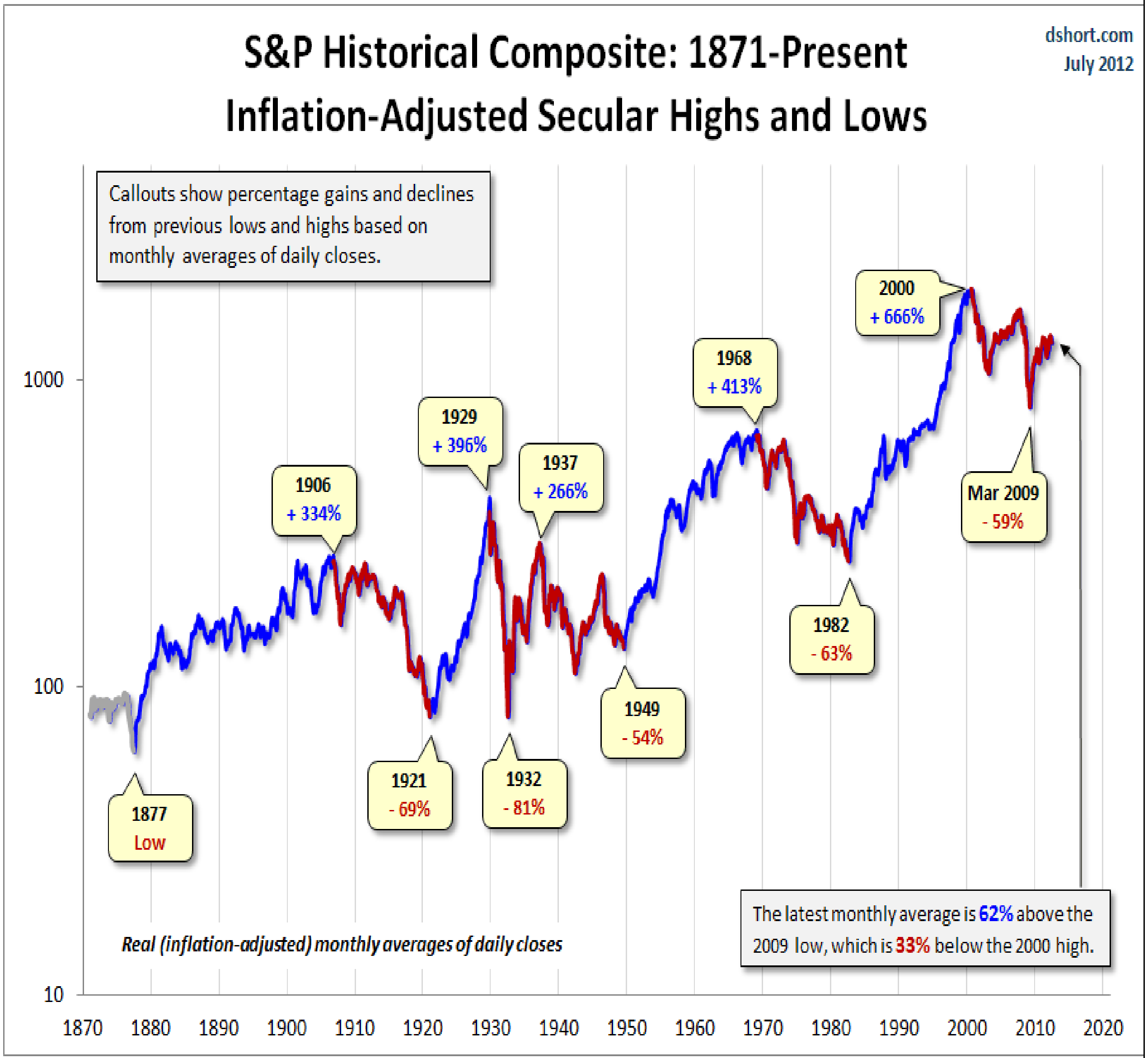
A Historical Perspective: Understanding Where We Are

The current state of the market should influence your investment stance. Since 2000 we've been living in the midst of a bear market. The hope of a reversal of this bearish trend that seemed possible in the latter part of 2007 completely fell apart in 2008. What can we, as investors, learn from this period in history to better prepare ourselves for the short-term and long-term?



A theme seen throughout the market since the downturn is a greater desire for stocks that exude an aurora of safety and stability. What companies are providing products and services that will be demanded even in bad economic times? Food, drug, energy and discount retail companies have been a place many investors run when the markets become choppy.

A perfect example of a 'safe' stock is Altria (MO), which is the U.S. company for Phillip Morris and other tobacco related products. MO and other similar companies have done quite well in the midst of market fluctuations. The reason for this is twofold. First, the business model is very solid. Demand does not fluctuate by much in either good or bad times. Second, the dividend payout is large, consistent and grows from time to time. In a market where volitilitaty sometimes seems like the norm, being assured a dividend yield is very comforting for investors.

For companies like MO that offer rock solid business models and dividends, the idea of buy and hold can be a viable alternative in a bear market. The investment is working for you through dividend distributions and the business model ensures that market dips will only temporarily hold the price down.

Buy and hold though for over 20 years now has been seen to be the rational model for the common investor. Since the early 80's until '00, buy and hold worked pretty darn well. Unless the company was a disaster, it likely appreciated because the direction of the market when rising (or falling) is a very powerful force in lifting stock prices up or down.

This all changed in '00, but we could not fully understand the implications of this shift until after the market collapsed in late 2008. While markets corrected significantly in '00, the setback was not seen as the start of a long-term bear market. The correction was perceived as being more industry specific, since the brunt of the blow was felt throughout technology companies.

Given our current historical perspective, investors should realize that investing in growth stocks is not a bad thing, even though many investors may shun the thought given current market conditions. For those that do venture into stocks that depend on significant company growth to become successful, buy and hold cannot be currently looked at as a viable strategy. Until we break into a new long-term bull market, the risk associated with the buy and hold strategy for this investment class outweighs the possible returns.

A volatile and weak economy plays havoc with most growth stocks. It's more difficult to grow in a time of economic contraction or weak economic growth and a greater share of investors see such companies as not worth the implied risk. Therefore, growth investors must understand the need to place clear exit points for their growth positions. It is equally important to set rules for exiting a position that has realized a profit.

A few easy and popular rules traders use when entering into positions are as follows:

- Cut your losses if a stock falls between 7%-8% below your purchase price after your initial purchase. Maintaining capital is important and hoping that losers turnaround is not a good strategy.
- Make sure the market is in an uptrend when buying. When the market is weak, even good

companies will be pulled down.

- Establish an exit point or points for selling.
- Monitor noticeable changes in the stock's volume. Depending on whether the stock appreciated or depreciated on high volume, it is a cue to investors whether institutions are buying or selling. Both are clear bullish/bearish indicators.

No matter where you stand as an investor, it is important to understand how your investing strategy fits (or doesn't fit) in with the market environment. Make sure to not lose focus of the micro and macro picture.

TheMarketCapitalist.com Portfolio Selection

Company	Ticker	Buy Date	Buy Price	Last Price	Performance	Dividend %	Buy Target
SeaDrill Limited	SDRL	9/7/2011	30.25	36.57	20.89%	8.10%	Up to 38
Weatherford International Ltd.	WFT	9/7/2011	16.31	11.72	-28.14%	0.00%	Up to 26
American Tower Corp.	AMT	9/7/2011	53.75	72.15	34.23%	0.00%	Up to 68
PowerShares Water Resources	PHO	9/7/2011	16.42	18.27	11.27%	0.64%	Up to 22
Cisco Systems, Inc.	CSCO	9/7/2011	15.42	16.31	5.77%	1.20%	Up to 21
Deere & Company	DE	9/7/2011	78.97	77.48	-1.89%	1.90%	Up to 92
Chesapeak Granite Walsh Trust	CHKR	2/3/2011	25.19	22.09	-12.31%	9.30%	Up to 26

Finding Big Yields in a Low Yield World

We're living a yield starved world. Whether it's your savings account, certificate of deposit, or money market account, you're not earning much interest. This is bad, not only because returns are so minimal, but because your money is at best only keeping pace with inflation.

A new alternative has arrived on the scene by the name of peer to peer (p2p) lending. The model is similar to that of a bank's lending system, except the process is direct. At the most basic level, you lend $1,000 directly to someone who is in need of $1,000. Two companies, LendingClub.com and Prosper.com, are currently leading the market in p2p lending.

Yields received by lenders range from mid 5% for loans made to the highest grade borrowers and around 12% for the lowest grade. The borrower's grade is a function of their credit rating. Both sites are configured to encourage loans to multiple people. These block loans reduce risk by dispersing money across multiple parties. Therefore, if one person defaults, the entire payback is not lost.

Stated default rates by A rated borrowers (highest rated) is around 1%. For those rating the lowest, Prosper claims their default rate is roughly 16.5%. Lending Club claims their highest risk borrowers default at a rate of 9.8%. If you contrast these default rates with the junk bond market, the p2p lending alternatives carry a significant amount more risk. Junk bonds historically default at a rate of 2%. Therefore, the importance of diversification is extremely important to mitigate risk.

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Minimum investments are low at both sites. If you're skeptical, but interested, you may want to begin with a low minimum investment and see how things play out. Based on your experience you can then increase your investment. You can start out with a few thousand dollars and then work your way up.

In a world where deposit accounts yields are very low and stock market returns have disappointed for over a decade, p2p lending has and will continue to draw a number of interested parties. Time will tell how well this business model will work for the business operator, lenders and borrowers.

Personal Finance: ***Low Volume Stock Deception***

When considering purchasing a stock or exchange traded fund (ETF), do you consider the stock/fund's average daily volume? For many investors this important aspect is overlooked. Stocks that lack volume are less liquid and therefore carry more risk than stocks with higher volume.

Volume is a measure of how many shares given a specific period of time that have traded. If I purchase 1,000 shares of X company, then I've added 1,000 to the total daily volume for a particular stock. An easy way to remember this concept is that investments that lack volume lack investor interest. If investor interest were high, then many shares would be trading hands frequently.

It is not uncommon to see a number of ETFs and stocks priced below $5 trade with very little daily volume. While this might not be an issue for when you're attempting to establish a position, it can be a disaster when attempting to sell your position.

Low volume securities pose the greatest risk from the sell side. This is because the lack of volume indicates a dearth of buyers. In the case that you need to exit from the investment, you are automatically placed in a bind. You're forced to do one of two things. An order can be placed at the price of the last trade to be completed. Or an order can be placed at a lower price, in hopes of enticing a buyer. Either way, it is blatantly clear the danger posed. The market is generally perceived as being a realm where you can dart in and out of investments at will. While this is true for a large part of the market, many areas are on the fringe and therefore pose an amount of liquidity risk.

A lesser, but still real danger, inherent in investments with low volume is the inability to lock-in profits when price appreciation has occurred. Tight volume can cause prices to jump, but if buyer/seller interest is slim, the idea of locking in gains at the price last traded becomes an illusion. This situation often provides investors with the perception that penny stocks offer a great amount of opportunity.

Lastly, many investors that have purchased stocks in the low dollar range (around $1 or under) and stocks that do not trade on an exchange need to remember that when selling an investment the idea of throwing a market order in and letting the system execute the order will most likely not be possible. The reality is you will need to place a limit order to sell the investment. If you're looking to get out from the investment immediately this will most likely mean placing an ask price below the quoted stock price. This can be unnerving, especially when you find that the lower price still does not cause the sell order to go through. Again, this is because of the stock's low volume.

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