The Big Picture

December 2012

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CURRENT HEALTH OF THE MARKET:
HEALTHY

December 2012

The Big Picture

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The dramatic falls that the markets experienced just after the US election came to a conclusion resulted in many uneducated investors selling at what looks like precisely the wrong time. It's very easy for investors new to the markets to get spooked out when the market is falling and sell on emotion.

Rather than going off how you feel, our take is to let the market tell you what's really going on. You can do that by carefully studying the daily price and volume behaviour of the main indexes and leading stocks. By doing that each and every day, you'll eventually be able to determine whether the behaviour was healthy or unhealthy, helping you to make better-informed investment decisions.

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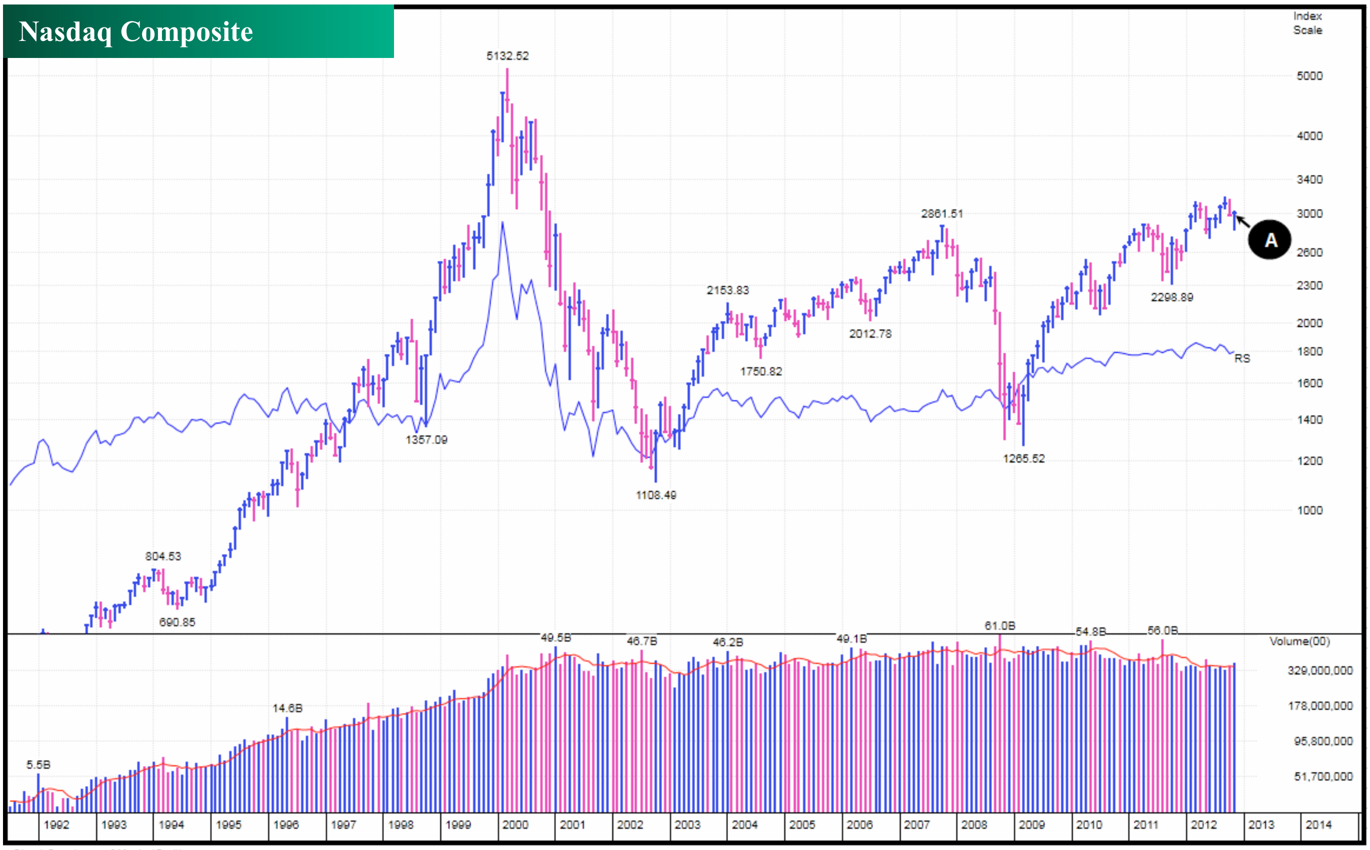

Chart Courtesy of MarketSmith

In November, the major indexes experienced steep falls at the start of the month, followed by a sharp rally in the final two weeks. This is what you call a bullish reversal (Point A) and even though the markets didn't make huge gains, it should still be seen as a constructive month.

The best months for making money

Historically November, December and January have proved to be the best months for making money in the market and because November didn't see large gains, December and January could turn out to be good profit generating months for market participants who are fully invested.

The financial media continue to tell us that the world is about to collapse and the latest buzz word is 'the fiscal cliff'. However as you will see in this edition, we tend to ignore the opinions of others and instead stick to the facts. We believe it's best to let the market tell you what's going on by simply looking at the actions and behaviour of institutional investors. We look to see if they are buying or selling.

> **"Because November didn't see large gains, December and January could turn out to be good profit generating months."**

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It's best to try to get 'in sync'

As you are aware, the big players control approximately 75% of the market's future direction, and so it's best to try to get 'in sync' with their trading activity or it's going to feel like trying to swim against a strong current. If you don't get in sync, you could get hurt. We like to see if the 800 pound gorilla investors are buying, because when they do it strengthens the market. However, if they are selling it weakens it. The other thing we like to keep a close eye on is the action and behaviour of leading stocks.

Why? If the leaders are acting weaker than the general market it's negative. However when leaders are outperforming the market it's positive. It's simple really. When leaders are underperforming, then the market is more likely to head lower, and if leaders are outperforming, then the market is likely to head higher. Are leaders outperforming right now? Yes!

Bull market? Bear market? Where are we?

Many media sources continue to suggest that the stock market is in a bear market cycle. However you can't argue with facts. Take a look at this five year chart of the Nasdaq Composite and you'll see that the bull market that began in March 2009 (Point B) remains intact.

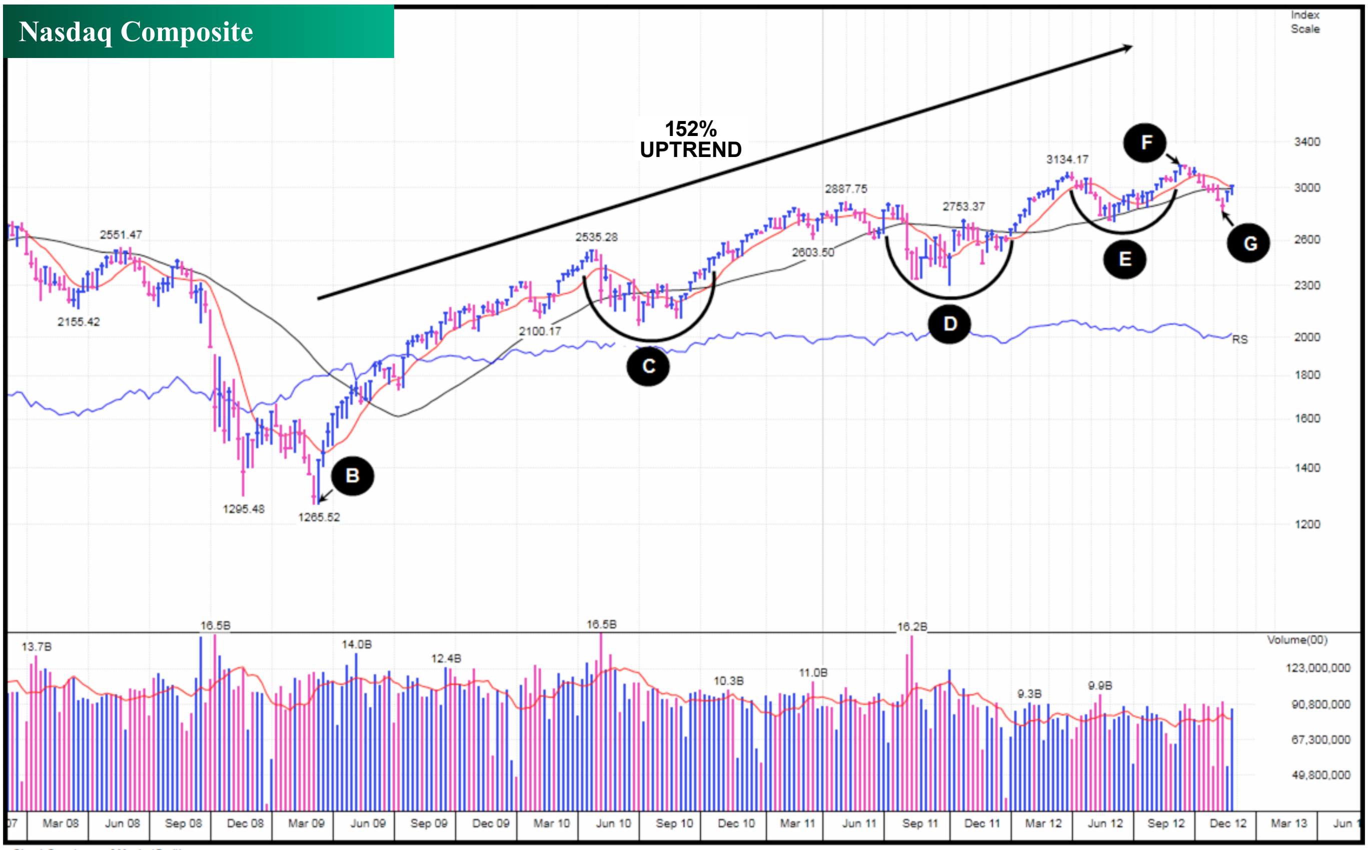

Chart Courtesy of MarketSmith

Since the uptrend began, the Nasdaq has made an impressive 152% return. However, to make that gain it has had to experience three challenging corrections.

The first correction (Point C) occurred from April to November 2010. The second (Point D) is a correction that started in May 2011 and ended in January 2012. The third (Point E), began in late March and ended in September 2012 (Point F). Just after that correction ended, the market has corrected again and it looks as if this retracement found a bottom about two weeks ago on the 16th November (Point G).

"Many media sources continue to suggest that the stock market is in a bear market cycle. However you can't argue with facts."

8 days of gains in the last 10 days = new uptrend

As you can see, on the 12 month chart of the Nasdaq Composite the US tech index has gained eight times in the last ten trading sessions (Point H), helping to confirm that this latest correction has probably found a floor and that we are now on the way back up.

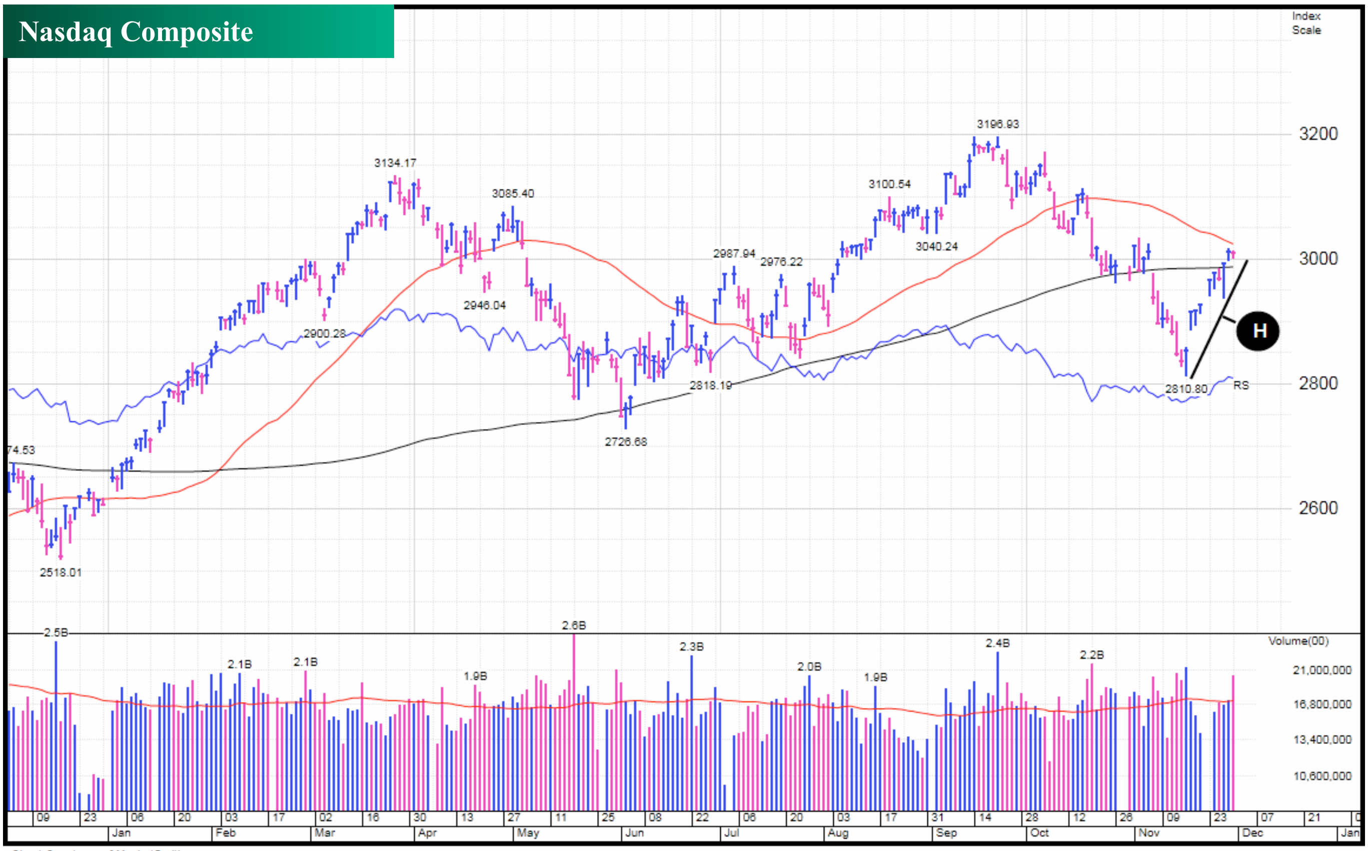

Chart Courtesy of MarketSmith

> “The US tech index has gained eight times in the last ten trading sessions helping to confirm that this latest correction has probably found a floor.”

Back above its 50 day moving average = healthy behaviour

Next take a look at the S&P 600's recent action. Notice on Thursday 29th November, the small cap index bullishly jumped back above its 50 day moving average (point I) helping to confirm that the market has probably clicked back into gear.

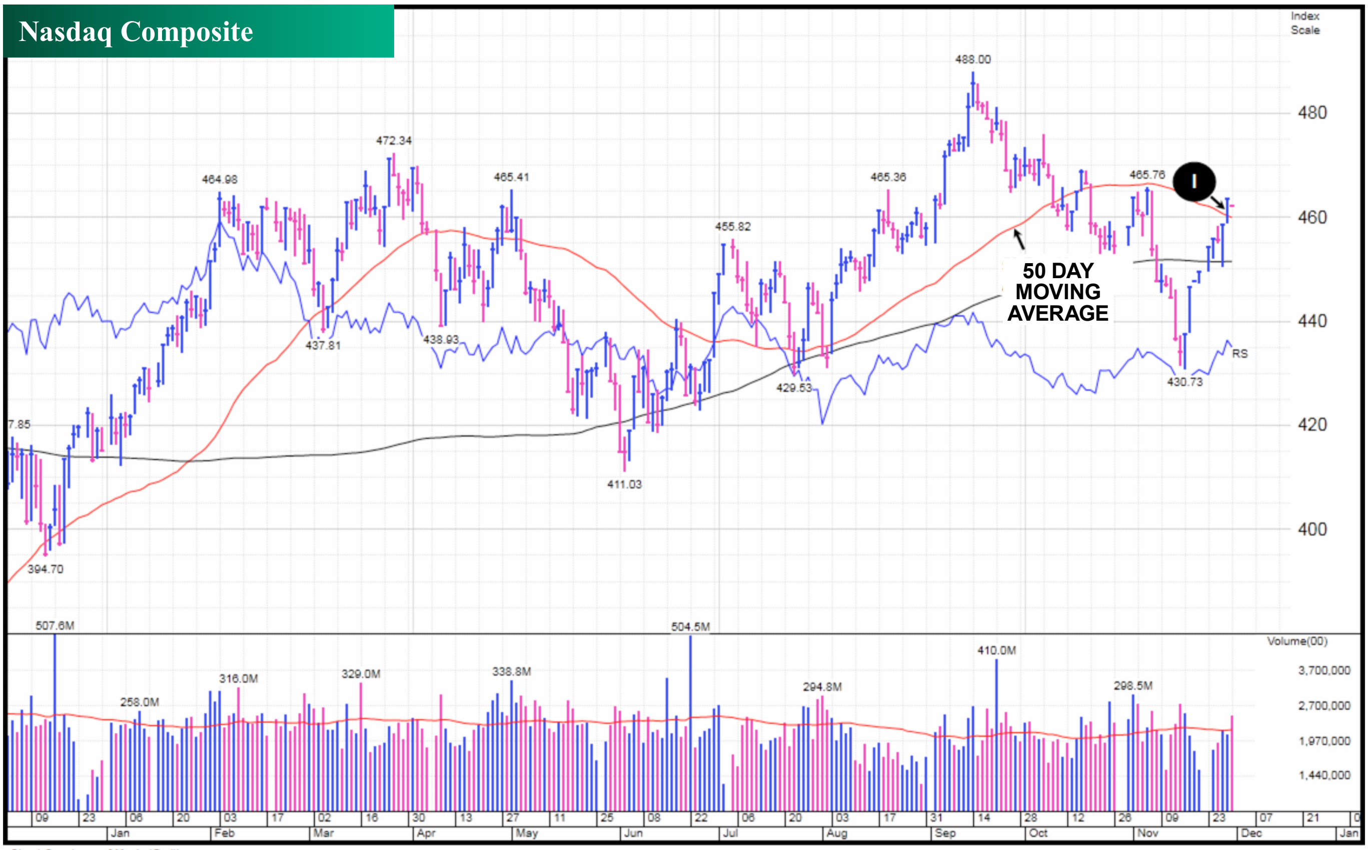

Chart Courtesy of MarketSmith

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Are you on Linkedin?

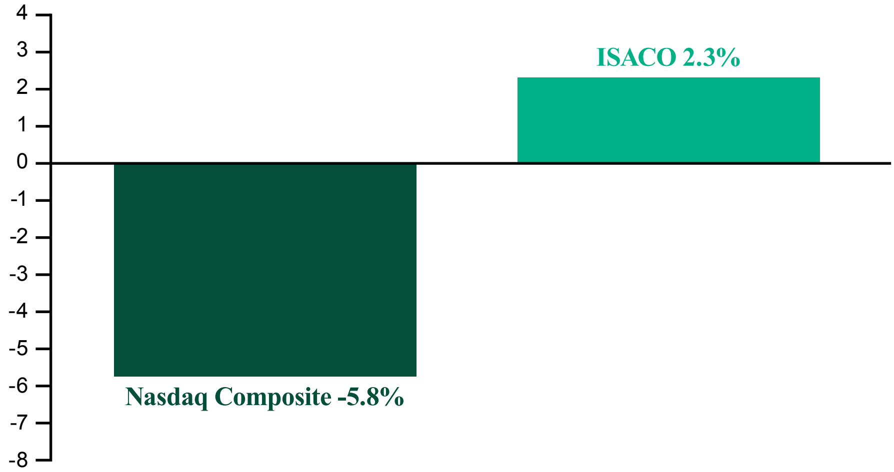
ISACO's two founders would be delighted to connect with you on Linkedin.

You can our find our profiles below.

To link to Stephen Sutherland, click here

To link to Paul Sutherland, click here

Investment performance during latest correction



Fighting the correction, a sign of health

This latest 'mini-correction' began on 21st September when the Nasdaq topped out at 3197. On Friday 30th November, the Nasdaq closed at 3010, which means its dropped 5.8% over the last 9 weeks. However over this same period, our portfolio has seen a gain of 2.3%. This means over the present correction period, we are proud to say we've outperformed the Nasdaq by 8.1%. That's what you call a bullish divergence. It also tells me that we should be staying fully invested in the funds that we currently own because the stocks they own are 'beating' the market.

Evidence of how we beat the market by 8.1%

Next we'll look at why our portfolio has been rising while the market has been falling, by taking a closer look at the two funds we purchased in July this year.

As a reminder, we bought Fund A on 24th July this year at a price of 131. On Saturday 1st December, it was trading at 149. That's a 13.7% gain over the last 18 weeks, easily beating the Nasdaq's 5.1%. The stocks this fund owns have been outperforming the market and, when leading stocks outperform the market, this normally means that the market is about to make a northerly move.

“Strong performing funds tend to get stronger and weak funds tend to get weaker.”

The second fund we recently bought, again on 24th July this year, was purchased at a price of 341. It is currently trading at 383. That means so far we've made a 12.3% return over the last 18 weeks. Just like Fund A, this one has also been outperforming the Nasdaq since we purchased it.

Strong performing funds tend to get stronger

There is no guarantee that these two funds will continue to perform well, however as I've been saying since I bought them, strong performing funds tend to get stronger and weak funds tend to get weaker. A 12.3% and 13.7% return on each fund in three and a half months, especially with the Nasdaq correcting 12.1% recently, demonstrates how strong the investments we choose can be and how quickly they can move once they have upside momentum. This is why we expect both of these funds, as well as the two others we own, to perform well over the remainder of this year and beyond.

Fund C close to a breakout

Take a look at the 12 month chart of another fund we own. This one has carved out a classic cup-with-handle base pattern (Point J) and it looks like it may be making a breakout move. The breakout would be at around the 3.40 price level (Point K).

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Market Indexes

Index	Price Change for the Month	Volume Change for the Month	What this Means
NASDAQ	+1.11%	+0.9%	BULLISH REVERSAL
S&P 500	+0.28%	+6.4%	BULLISH REVERSAL
S&P 600	+0.87%	+1.1%	BULLISH REVERSAL
DJIA	-0.54%	+6.4%	BULLISH REVERSAL

Shadow Investing Intelligence

The table below shows the funds we own:

Holdings	ISIN number	Assets %*
CLASSIFIED	CLASSIFIED	31.45%
CLASSIFIED	CLASSIFIED	25.09%
CLASSIFIED	CLASSIFIED	22.07%
CLASSIFIED	CLASSIFIED	21.39%

*Assets % 1st December 2012

Our view on which way the market is heading is this: we have a bullish stance in the short-term and a bullish stance in the long-term. It's good to remind ourselves how intelligent investors play the market. During bull markets smart investors sit tight and remain fully invested.

Our rule is to never exit a bull market, even when we believe a correction is imminent. We only exit when we believe the bull market has finally run its course. So even though the indexes will occasionally correct during a bull market, we will always sit tight.

If any words or phrases in today's edition seem unfamiliar or puzzling, discover their meaning.

"Our rule is to never exit a bull market, even when we believe a correction is imminent. We only exit when we believe the bull market has finally run its course."

Current Health of the Market

My current stance on the market is healthy. Below is a brief summary of how the market acted each week for the month of October.

As always, I concentrate on the Nasdaq Composite (the market's leading index) and the S&P 600 (the market' second leading index), as their action carries much more weight than the S&P 500 and the Dow.

Week Commencing Monday 29th October

For the week the Nasdaq the markets leading index pulled back 0.19%. The S&P 600 the markets second leading index did better gaining 1.51%. The three day week made the weekly action more difficult to read. It was clear though that the 600 performed better than the Nasdaq, making a small gain after bullishly finding support at its 200 day moving average (Point E). The Nasdaq unfortunately fell for the week but just like the 600, for now it still appears to have support at its 200 day moving average (Point F).

Week Commencing Monday 5th November

For the week the Nasdaq the markets leading index pulled back 2.59%. The S&P 600 the markets second leading index lost 2.94%. Both the Nasdaq and the 600 acted poorly for the week. However when you look under the surface, leading stocks continue to act well which tells me this weakness is probably going to turn out to be temporary in nature. I feel that the market is close to a bottom. I say this because the Nasdaq has tremendous support at these levels which goes all the way back to April 2011 (Point C).

Week Commencing Monday 12th November

For the week the Nasdaq the markets leading index lost 1.78%. The S&P 600 the markets second leading index pulled back 2.30%. This week the Nasdaq (Point C) and S&P 600 both took further hits and with volume coming in above average, indicates another week of institutional selling. The good news is with the increased bearish sentiment and the way top stocks have been acting this week it tells me this retracement could be almost over.

Week Commencing Monday 19th November

For the week the Nasdaq the markets leading index did well rising an impressive 3.99%. The S&P 600 the markets second leading index also pulled out all the stops gaining 3.85%. It was a great week of gains for both the Nasdaq and the 600. We are hoping that next week we see the market follow through to help confirm the start of a new uptrend

Week Commencing Monday 26th November

For the week the Nasdaq the markets leading index gained 1.46%. The S&P 600 the markets second leading index rose 1.73%. The good news is the weekly gains came in on above average volume, indicating the institutional investors were buying. Both indexes now have two weeks of gains under their belt and even though the market has not yet officially 'followed through' the positive action lately appears to imply that a new uptrend has begun.

Summary

Here's a summary of this month's edition:

- November didn't see large gains, so December and January could turn out to be good money making months.
- 8 days of gains in the last 10 days = new uptrend.
- In the last nine weeks, we are proud to say we've outperformed the Nasdaq by 8.1%.
- The two funds we recently purchased continue to go from strength to strength.
- The third fund we own looks as though it could breakout soon.

Please note past performance should not be used as a guide to future performance, which is not guaranteed. Investing in funds should be considered a long-term investment. The value of the investment can go down as well as up and there is no guarantee that you will get back the amount you originally invested.

From all of us here at ISACO we hope you enjoy the month of December and we hope you have a fabulous time over Christmas. ISACO would like you to know that if you are ever unsure about anything we have said or you have any suggestions to help us improve the overall service we provide, please get in touch as we'd love to talk to you and help you in any way we can.

We will always do our best to provide you with the information and personal opinions to help you make the right decisions for your own individual circumstances.

Your friend,
Stephen Sutherland.

ISACO's Chief Investment Strategist and author of 'Liquid Millionaire.'