STOCK MARKET
FORECAST
2010

2010: Stock Market Analysis, Forecast & Advice

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January 5, 2010

Milton Friedman, the noted economist, once opined that stock prices are rational in the long-term, but over the short haul they are far from rational; they are full of noise. In the same vein, we believe the "noise" and "irrationality" to which Friedman referred, makes short-term or micro economic analysis an inexact science at best. For this reason, we have in our stock market reports over years past, focused on the long-term or macro economic picture. As always, our objective is to identify macro economic trends, analyzing and predicting their effect on the markets, while identifying the investments that we believe may be best suited to capitalize on those trends.

Since we began writing our Special Reports in 1999 we have endeavored to be the voice of reason and logic to investors. Our market forecasts have generally proven to be quite accurate—sometimes, uncannily so.* Back in 2000, near the top of the stock market, our prognostications turned bearish. Subsequently, in 2002, we concluded that the market was setting up for an extended period of sub-par performance, albeit with strong interspersed rallies, similar to occurrences in 1901, 1929 and 1966 where, for 16 to 21 years, the Dow Jones averaged only around a 1.5% yearly return!

*** Past performance is not necessarily indicative of future results.**

No, we are not oracles, nor do we have the benefit of divine intervention. And, no, we don't have all the answers. But we do pay very close attention to economic and market history, which we believe can be a very important guide as to the future direction of the markets. **We believe studying the history of the markets is of little use in forecasting day-to-day or short-term market movement, but extremely useful in helping forecast the intermediate to long-term trend of the markets. Why? History is created by the actions of people, and people have generally repeatedly reacted in a predictable fashion since modern civilization began! In our opinion, people do not change; only circumstances and events do!**

Our 2009 Stock Market Forecast

In our stock market report, 2009: Stock Market Analysis and Forecast, we correctly, analyzed, and predicted the outcome for the market in 2009. **You be the judge from the excerpt below keeping in mind the report was written during an extremely bearish period for stocks where the market finally bottomed in March of 2009.** The entire report may be read at: http://cta.visionlp.com/pdf/gen/2009_stock_market_forecast_analysis.pdf

> *No matter how bad deflation gets, the Fed can print money faster than deflation takes hold...... We believe it will not be until the middle part of the year before lower interest rates, quantitative easing, and fiscal stimulus actually take hold initiating a respectable market recovery......We believe the latter part of the second half of 2009 will show improvement as the Fed's quantitative easing and the Federal Government's stimulus finally start to take hold and the market looks ahead in anticipation of the end of the recession and an improvement in corporate earnings. Depending on the success of government actions there's a chance that 2009 may even end up being a positive year for stocks!*

2009 Stock Market Performance in Perspective

The Dow Jones Industrial Average rallied 61% off its March low to return 19% in 2009. The rally from the March low was just one of six of that magnitude in the last 100 years. All previous rallies of this magnitude occurred during past secular bear markets in the 1930s and 1970s. **In fact, according to Ned Davis Research, all previous rallies of this magnitude occurred during periods of turbulence for both the economy and markets and <u>none of the gains were sustained</u>** (*See Secular Bear Markets, below*).

The question begs: Did the strong performance for the stock market in 2009 signal the end of the secular bear market and the beginning of a new secular bull market? This report will give our opinion answering this question and a lot more! We will once again try to be the voice of reason and logic to investors!

Secular Bear Markets

In order to better understand what has and continues to happen in the stock market, it is very important to understand the history and nature of secular bear markets.

A secular bear market is one which rises and falls, making little progress over many years. Secular bear markets have proved to be particularly harmful and unrewarding for buy and hold investors. We have experienced three since the turn of the last century and are currently in our fourth. Average length of previous secular bear markets was 18 years, each lasting anywhere from a minimum of 16 and a maximum of 21 years.

Secular Bear Markets	Market Duration (Years)	Average Yearly Return (Dow)
1906-1921	16	1.58%
1929-1949	21	1.69%
1966-1982	17	1.59%
2000	?	

1906-1921: During the secular bear market of 1906 to 1921 the Dow closed at 94 in 1906. In 1921 it closed at 81. Finally, in 1922 the Dow closed at 98 rising and staying above its 1906 close.

1929-1949: During the secular bear market of 1929 to 1949 the 48% rally of 1929-1932 turned out to be a tragic misfire, leading to a subsequent 86% plunge in market value. Stocks then had sharp rallies and declines for the next 25 years. It was not until 1954 that the Dow broke its 1928 pre-secular bear market high of 300 in 1954 closing at 404.

This secular bear-market in U.S. stocks began in 1966, and didn't end until 1982... 16 years later! As you can see, there were many false-starts along the way, as stocks suffered from repeated selloffs for years...

2000 to 20XX?: In 2000, the Dow closed at 10,786. In 2008, the Dow ended the year at 8,776. In one year, the losses of 2008 wiped out the gains of the previous five years! This is nothing unusual in secular bear markets: The profitable years are typically erased by one or two unprofitable years until the secular bull market begins.

In 2009 the Dow closed at 10,428. The fact is, even with the spectacular rally from its lows in 2009, the Dow is still below 10,768 where it was ten years ago! Additionally, the past decade is the worst in recorded history for the S&P 500 going back to the 1820s. Over the past decade the S&P was down 24% or an average negative return of around 1% including dividends!

It is also very important to recognize, longer term, within secular bear markets, there also exists cyclical bull markets like the one experienced from 2003 through 2007 and in 2009. Some of these cyclical bulls can be quite strong leading investors to believe a new bull market has begun. While these cyclical bulls can last one or even several years, historically speaking, they tend to surrender their gains as the secular bear market re-emerges. **We experienced this most recently in 2008, as the secular bear re-emerged with a vengeance, wiping out all cyclical bull market gains of the past five years, and bringing stocks back to levels of 1997!**

Some of the biggest bear market rallies and cyclical bull markets occurred in the Depression years. After the Dow dropped four years in a row from 1929-1932, falling 89% (248 to 59), it had one of its best performance periods of a cyclical bull market within a secular bear market from 1933 to 1936, rising to 179, only to fall 32% in 1937 to 121. It took another 17 years to breach its 1928 high of 300, reached before the secular bear market started in 1929.

In the secular bear market starting in 1966, the Dow dropped 18% to 785. It was not until 1972 when the Dow finally broke 1,000, rising to 1,020. Then, in 1973 and 1974, the Dow dropped 17% and 28%, respectively, down to 616. The following years, the Dow experienced cyclical bull markets within the secular bear market, but it was not until 1982 before it closed above its 1972 high at 1,047.

We believe a December 31, 2009 Wall Street Journal article, *2009: Banner Year for Stocks*, puts the "banner" year for stocks in proper perspective with the following excerpts:

> *The U.S. stock market is poised to end 2009 with a comeback of historic proportions, with the Dow Jones Industrial Average up 61% from its March nadir and 20% for the year. But the history of such rebounds suggests the biggest gains may already be over, making it hard to expect a blockbuster 2010...Some investors worry that the Dow, with its rapid climb following a precipitous fall, is following patterns seen in the 1930s and 1970s.In those periods, stocks staged robust rallies, only to lose most of those gains and spend years going nowhere. The Dow rose 48% from its low from 1929 to 1930, and then plunged 86% over the next two years. In 1933, the index shot up 64% over 53 trading days. But stocks went on to bounce up and down for years, with sharp gains and declines. After a major slump in 1973 and 1974, stocks began a rally that lasted almost two years. But the market gave back most of those gains.*

Concerning these facts on past secular bear markets we ask, **why should this time be different when the economic fundamentals affecting the stock market in this secular bear market are the worst since the Great Depression?**

Bull Market or Secular Bear Market?

Did the strong performance for the stock market in 2009 signal the end of the secular bear market and the beginning of a new secular bull market? We would love to believe so, but we believe we would only be deluding ourselves! Why? Read on!

Much of corporate earnings in 2009 were attributed to cost cutting. We believe the market rallied extrapolating earnings from cost cutting, which will be unsustainable going forward without a significant increase in sales. With unemployment so high and the consumer still "broke" from the trillions of dollars in losses from real estate and the stock market in 2008, we seriously doubt there will be any substantial increase in corporate sales for years to come!

Consumer wealth has been shredded and wages are falling. The over-indebted U.S. consumer -- whose deleveraging process is still in its early stages, will likely continue to put the brakes on consumption while the savings rate continues to creep up. As long as consumers, who have been busy saving more, keep losing their jobs or remain worried about their job security, they are likely to save more and not spend thus putting a big drag on corporate profits.

With the consumer responsible for supporting nearly two-thirds of the economy, one should be able to see the challenges ahead for the stock market.

We believe the market has gotten ahead of itself based on hopes of a V-shaped recovery that we believe time will prove to look more like a W-shaped recovery once the government's massive liquidity injection ends. In the short-term, markets can be led by false expectations and emotions, but in the long-term fundamentals rule and will ultimately determine market direction. The fundaments still stink!

Most of the problems that caused the market to go down in 2008 are still present and will likely take years more to be solved........they just are not as dire as they were, but they still are very bad.....commercial and residential real estate, high unemployment, a consumer who is broke and saving rather than spending, and tight credit to name a few....... "Less bad" is not what secular bull markets are made of!

One should not be blinded by the market's strong performance in 2009. We are still in a classic secular bear market. As stated previously, the fact is, even with the spectacular rally from its lows in 2009, the Dow is still below where it was ten years ago! Additionally, the past decade is the worst in recorded history for the S&P 500, going back to the 1820s, averaging around a negative 1% per year; and that includes dividends! An investment of $10,000 in stocks starting on Dec. 31, 1999, would have decreased to $9,090 on December 31, 2009. *This past decade should be a poignant reminder that stocks can decline over long periods of time.*

And do not think just because the S&P 500 experienced its worst decade in history that stocks are at good valuations. The long-term price-to-earnings ratio average is about 16. Today it is over priced at 20. Jeremy Grantham, manager of the multi-billion dollar GMO Fund, was described in a February 2009 Barron's article as "...one of the Grandest of thinkers and most eloquent of oracles, Jeremy Grantham has long been the voice of reason in an industry prone to excesses and embellishment."

In a December 2009 Wall Street Journal article Grantham related he believes stocks are 30% overpriced. He expects the stock market to average over the next 7 years only 1.6%. This coincides with our views and is in line with long–term yearly average secular bear market returns.

The Cause Becomes the Cure

The Federal Reserve, through its actions taken at the end of 2008, cutting rates from 1% effectively down to zero, is employing the cause as the cure. The central bank is essentially fighting fire with gasoline or, put another way, their easy money policy is no different than helping a drunk avoid a hangover by providing more liquor! **We think the Fed's actions may forestall, but not solve the problems facing the economy.**

With a historic massive injection of liquidity into the economy, the Fed was successful in 2009 forestalling the problems facing the economy. But in the process we believe the Fed has sown the seeds of our next crisis: inflation. **Consider this: in the next 10 years, the U.S. budget deficit is projected to rise more than in all the previous 233 years combined since the founding of America in 1776.** We believe one does not have to be an analyst to see the inflationary implications of the Fed's actions and its potential negative effect on the U.S. dollar and stock market. Economics 101: An increase in the monetary base leads to an increase in the money supply, which leads to inflation!

The Big Picture

Over the course of the next 10 years or so we fully expect positive years from cyclical bull markets as we saw in 2009 and in previous secular bear markets. However, we believe whatever gains may be realized in rallies or in cyclical bull market years will evaporate as the secular bear market re-emerges as so far has happened in the secular bear market beginning in 2000 (and occurred over 15 to 20 years in other secular bear markets).

Let's not delude ourselves with wishful thinking: why should this time be different when the economic fundamentals affecting the stock market are the worst since the Great Depression? The average length of previous secular bear markets was 18 years, each lasting anywhere from a minimum of 16 and a maximum of 21 years. Thus, if you add 18 years to the start of the current secular bear market, beginning in 2000, and take plus or minus three years on either side, the current secular bear market that began in 2000 may not end until sometime in the 2015 to 2021 time period. With the worst fundamentals since the Great Depression, chances are it won't end until sometime around 2020. Consequently, we believe this secular bear market is only half over!

Accordingly, we believe any gains made in rallies or winning years like 2009 will be lost over the next 10 years. Past performance is not necessarily indicative of future results.

Forecast for 2010

Looking ahead we see reduced corporate profits and a stalled recovery due to high unemployment. How are corporate profits going to substantially rise with high unemployment, reduced consumer spending, and most of the problems causing the market to fall in 2008 not even nearly solved? We believe the reason we saw the market so strong in 2009 was two fold: It recovered from one of the worst sell offs in history and government intervention providing excess liquidity to the markets. We strongly believe the stock market in 2009 and as we go into 2010 is still being driven by excess liquidity and not supported by economic fundamentals necessary for an extended bull market!

It would be very easy to turn bearish on stocks following such a run from its lows in 2009. The problem is there are still several trillion dollars of investor money on the sidelines waiting for an opportunity to get back in. This is one reason why the equity markets have soared beyond expectations.

While we believe the stock market has seen the majority of its gains in 2009 a mildly positive year can't be ruled out as long as the government keeps interest rates artificially low. The market is still on a "sugar high"provided by ultra-low interest rates and the massive amounts of liquidity provided by central banks. However, with the 61% rally the Dow experienced from its lows in 2009, driven by excess liquidity and not sound fundamentals and federal spending clearly out of control, we believe the risks in the stock market are higher than ever. We believe the downside will be significantly greater once interest rates start to go back up or inflation takes hold. If this does occur, as we fully expect, any modest gains can quickly turn into losses as happened in 2008. The market is a discounting mechanism and will factor this in before it occurs making it very difficult to avoid significant declines in stocks!

At this point, to give a more precise prediction for 2010 would be pure conjecture. There is simply too much uncertainty especially with the government artificially propping up the economy. We need to see how the government "plays its hand." Until then, we foresee a volatile two way trader's market with an upside bias.

In this uncertain volatile market environment, we strongly recommend investors properly balance their portfolios with alternative investment strategies that have the flexibility to potentially capitalize equally on rising or falling markets.

The fact is those investors who benefited in the past decade were short-term investors who were able to take advantage of volatility in rising and falling markets. We expect the same to hold true over the next decade!

The Potential Value of Professionally Managed Futures

Reacting to the inflationary implications presented by huge budget deficits amassed here in the U.S. (in the next 10 years, the U.S. budget deficit is projected to rise more than in all the previous 233 years combined since the founding of America in 1776), gold has climbed to record highs. In our opinon, that's not surprising! Gold, given its ties (and inverse relationship) to the U.S. dollar has historically led advances in commodity prices. **We can print money, but we can't print commodities!**

With virtually zero correlation to stocks and the potential ability to capitalize on both rising and falling equity markets, commodities (in particular the energy, metals and grain futures along with other sectors) are gaining popularity among suitable investors as a potentially efficient, alternative asset class!

One way to participate in the commodities markets is through managed futures with professional money managers referred to as Commodity Trading Advisors ("CTAs"). As required by law, CTAs are registered with the Commodity Futures Trading Commission (CFTC) and members of the National Futures Association (NFA), a self regulatory organization authorized by the US Congress in 1982. CTAs are professional money managers who manage investors' assets using investments in the commodities markets, just as a stock mutual fund manager would invest his client's assets in a variety of different stocks. **Professional Commodity Trading Advisors do experience an appreciably higher success rate than the individual amateur trader. The fact is there are numerous Commodity Trading Advisors with attractive returns achieved through prudent money management! Be advised, however, that there are also CTAs who have not experienced attractive returns and you are subject to the risk of loss no matter who is managing your money.**

Our advice for suitable investors is to diversify their portfolios with professionally managed futures. Unlike stocks, managed futures have the versatility and potential to capitalize on both rising and falling markets and correspondingly may be better suited for volatile, secular bear market periods as we are now experiencing. Please be advised that trading futures and options involves substantial risk of loss and is not suitable for all investors. There are no guarantees of profit no matter who is managing your money.

Big Misconception

In our opinion, investors often make no differentiation between commodities and professionally managed futures. Commodities are an asset class. Professionally managed futures are an investment vehicle which uses the commodity futures and options markets in an attempt to capitalize on a rise or fall in commodity prices. In professionally managed futures, performance results are more dependent on the skill of the manager, not the investment vehicle. For example, 2008 was one of the worst years on record for not only stocks, but also commodities: commodities fell 46%. However, professionally managed futures as an asset class were up 14% to 18% according to the Credit Suisse/Tremont Managed Futures Index and the Barclay CTA Index due to Commodity Trading Advisors ("CTAs") capitalizing on significant declines in commodity prices! Please be advised that past performance is not necessarily indicative of future results.

In a brochure published by CME Group entitled, *Managed Futures: Portfolio Diversification Opportunities*, several studies point to the non-correlative nature of commodities versus stocks and the value of professionally managed futures. **"Including up to 20 percent of total investments in managed futures funds," one of the studies suggests (see page 3), "enhances managed portfolio diversity and therefore promotes greater independence from general market moves."** This study can be found in its entirety via the hyperlink below:

http://cta.visionlp.com/pdf/gen/CME%20Managed%20Futures%20FINAL.pdf

Just as an investor would diversify an equity portfolio with stocks from different sectors, we believe for maximum potential risk reduction and increased potential performance one should diversify with a basket of CTAs, each of whom trade different markets and employ different trading strategies. **There have been studies on the actual performance interaction of managed futures, stocks and bonds going back 20 years that helped educate the public about professionally managed futures thus enabling investors to be more objective in making investment decisions. We believe some of the most impressive facts are:**

- Managed futures not only profited in the market meltdown in 2008, but also in every stock market decline except one since 1987! (Source: CME Group: Why Smart Money Trades Managed Futures).

- Managed futures have been positive every year during the worst stock market declines since 1987. (Source: CME Group: *Why Smart Money Trades Managed Futures*).

- A drawdown is a percentage drop in equity before recovery. Investors often use drawdowns in evaluating the risk of an investment. Over the time period of 11/1990 – 02/2008 the worst managed futures drawdown was one-third that of the Dow Jones and seven times less than the NASDAQ's. (Source: CME Group: *Managed Futures: Portfolio Diversification Opportunities*).

- Over the past 27 years, managed futures have outperformend U.S. stocks as measured by the S&P 500 by almost double and International stocks by four fold. (Source: CME Group: *Managed Futures: Portfolio Diversification Opportunities*).

Investors should be aware that trading futures and options involves substantial risk of loss no matter who is managing your money. Past performance is not necessarily indicative of future results.

An attractive feature of a CTA managed futures account is that there is total transparency. Each account is separate in the name of the individual, corporation or entity and not pooled together. Investors have 24/7 access to trading activity and account information via a password protected Web site. Investors receive a trade confirmation with the details of each trade transacted in their account and also receive month-end account statements.

While there are no guarantees or assurances of future performance with any CTA, we believe suitable investors, in the coming years, may stand to benefit with a select group of our recommended money managers. Our reasoning is that even if stocks do have strong gains in any given year, we think they will probably be given back in ensuing years as happened with the stock market gains of 2003-2007 where in one year, 2008, all gains and then some since 2003 were erased. The loss of stock market gains amassed in winning years is typically the case in secular bear markets. On the other hand, unlike stocks, managed futures are more versatile, offering the potential opportunity to capitalize equally on both up or down volatile markets.

Even if our analysis proves off the mark and a new bull market in stocks ensues, we believe our recommended money managers, given their flexible investment approach in both bull and bear markets, can still potentially compliment the stock market!

In order to be better informed about the potential benefits and risks of managed futures we highly recommend reading the brochure, *Modern Portfolio Theory: Dynamic Diversification For Today's Investor*, and PowerPoint, *Understanding Professionally Managed Futures, One of the Fastest Growing Investment Alternatives*.

The brochure is located at: http://cta.visionlp.com/pdf/gen/mpt.pdf

The PowerPoint is located at: http://cta.visionlp.com/mfp_files/frame.htm

Consult your Vision affiliated broker for more information on the CTAs we believe can best meet your affordability, suitability and investment goals. Please be aware that you must read and understand each CTA's disclosure document carefully before investing. Trading futures and options involves substantial risk of loss no matter who is managing your money. Such investments are not suitable for everyone. Past performance is not necessarily indicative of future results.

This piece has been prepared by Vision Financial Markets LLC, a registered Futures Commission Merchant. Futures traders should be aware that daily market volatility might cause loss despite prevailing trends in the stock market. The risks associated with trading futures and options are significantly different than those of stock investing and investors may lose more than their initial investment. While we advocate diversification, please be advised that it will not necessarily provide protection against substantial loss. Past performance is not necessarily indicative of future results.