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Investment Strategy
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"The Boys Are Back in Town"

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Guess who just got back today?
Them wild-eyed boys that had been away
Haven't changed, haven't much to say
But man, I still think them cats are crazy
They were asking if you were around
How you was, where you could be found
Told them you were living downtown
Driving all the old men crazy
The boys are back in town
The boys are back in town

. . . Thin Lizzy (1976)

The boys are indeed back in town as Washington D.C. opened its doors for business as usual last week following a contentious debt ceiling debate and a 16-day shutdown of the government. This outcome had been anticipated in these letters for often-stated reasons, and just like when the "fiscal cliff" was averted, I now expect the media to turn its focus to the next Armageddon. While the self-inflicted crisis took the amateurish rollout of Obamacare out of the headlines, it will likely have a *de minimis* effect on the economy (maybe shave 0.03 – 0.04% off of the official GDP figures). The good news is that except for this week's delayed September employment report, I doubt investors will pay much attention to any of the other economic reports between now and Christmas due to the recent Beltway consternations and their expectation about the potential impact on the economy.

As for the impact on the stock market, it was profound with the S&P 500 (SPX/1744.50), the mid-cap S&P 400, and the small-cap Russell 2000 trading to new all-time highs. While there were some upside non-confirmations (most notably the D-J Industrial Average), the majority of indications confirmed the move higher. For example, the Advance/Decline Line climbed to a new bull market high, the Selling Pressure Index fell to a new reaction low, the short-term "buy signal" I spoke of on October 15th remains in force (when the 14-day Stochastic crossed above its moving average), the Short-Term Trading Index confirms that "buy signal," the number of new highs on the NYSE expanded, and the list goes on. Such metrics caused the "godfather of technical analysis," namely Ralph Acampora, to abandon his bearish "call" of last summer. Recall that like me, Ralph was looking for a short/intermediate-term stock market peak in the mid-July through mid-August timeframe. At the time I was expecting a decline of roughly 10%. And, we were about halfway into that 10% pullback when Vladimir Putin pulled our President out of a tight spot with Putin's Syrian solution. At that point I mainly gave up on my downside "call" and recommended recommitting 15% of the cash that was raised in June. Since then, while the equity markets have been choppy, they have refused to surrender much ground. As stated in last Thursday's *Morning Tack*, "With the debt ceiling debates behind us, the markets can focus on earnings, economics, and the Federal Reserve." To that trifecta, the story is pretty good.

On the earnings front, the bottom up operating earnings estimate for the SPX is currently $107.58, leaving the SPX's P/E ratio at almost 16x. Next year's estimate is $121.66. If the SPX continues to trade at that P/E multiple it renders a price target of 1946. Moreover, so far of the 190 companies that have reported earnings, 60.5% of those companies have beaten estimates and 50.9% have beaten revenue estimates. As far as economics, as stated the numbers are probably going to be ignored for a few months because of the shutdown. However, I believe GDP growth will accelerate to 3% in 2014 driven by a capital expenditure cycle because companies like GM are running their plants flat out 24/7 and the equipment is wearing out. Finally, with Janet Yellen at the helm of the Fed it should be steady as you go. That implies no tapering and plenty of liquidity. And, a number of other things are going right in this country.

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While the politicians do not want to broadcast it, the latest monthly CBO report shows tax revenues up 13% year/year and individual income tax payments up an amazing 15.8%. Further, payroll taxes are better by 11.6%, all of which have cut the CBO's 2013 estimate of the deficit to $642 billion. Part of the reason for that deficit reduction is because median family annual incomes have stabilized for the first time since the recession to an inflation-adjusted $51,017. Another reason is that the U.S. is on track to overtake Russia as the world's largest producer of oil and natural gas. Of course the reason for that energy leap is the technologies of fracking and horizontal drilling. Interestingly, the research firm IHS Global Insights notes fracking has added the equivalent of $1,200 to real household disposable income on average in 2012 and estimates that figure will grow to $3,500 by 2025. Further, fracking added $283 billion to economic growth last year and is expected to add $533 billion in 2025 with an attendant federal/state tax payment of $138 billion. The relative resulting "cheap" energy estimates are causing foreign companies to invest, or are planning to invest, billions of dollars in plants that would churn out chemicals, fertilizers, plastics, metals, etc. Obviously, the American Industrial Renaissance (AIR) is happening. A few of the ways to participate in this renaissance is through Rich Bernstein and either of the mutual funds he manages for Eaton Vance, Richard Bernstein Equity Strategy Fund (ERBAX/$13.62) and the Richard Bernstein All Asset Strategy Fund (EARAX/$12.24). As for a pure play (100%) on AIR, there is First Trust's Richard Bernstein TS American Industrial Renaissance ETF (FWRVLX/$10.17).

Another theme we have embraced for the past two years has been the recovery in housing. Recently many investors have cooled on this theme due to the rise in mortgage rates. However, as can be seen in the chart on page 3, mortgage rates have declined over the past few weeks. A second derivative way to get at the burgeoning housing theme is via Strong Buy-rated Weyerhaeuser (WY/$30.11). As our fundamental analyst writes in the commentary for our Analysts' Current Favorites product, released earlier today:

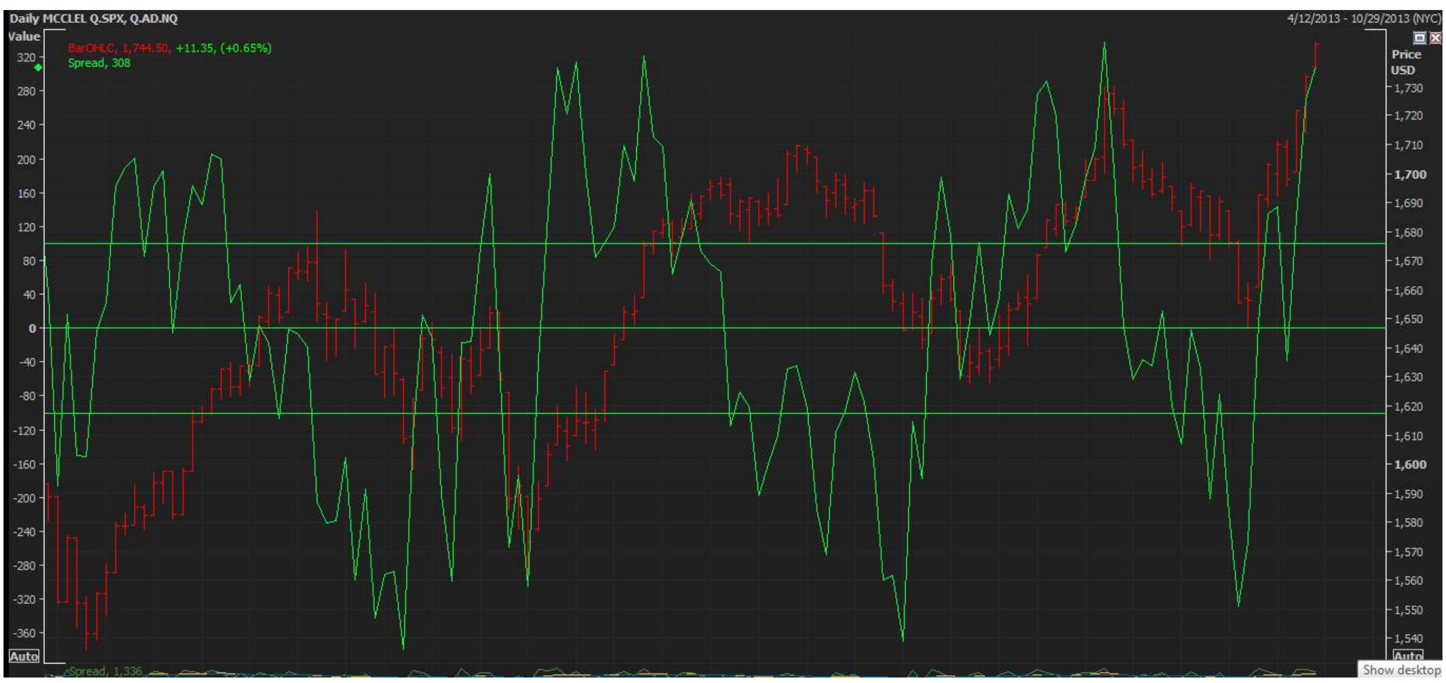
> We believe: 1) the embedded value of Weyerhaeuser's homebuilding platform is underappreciated relative to other public builder valuations (most notably, the 17,700 lots it controls in California); 2) the recent underperformance of WY shares has created a buying opportunity; and 3) in the context of our REIT coverage, there are relatively few opportunities to find similar long-term earnings/cash flow growth stories. In our view, Weyerhaeuser's homebuilding platform (one of the 20 largest in the country), significant wood products business, and immense timberland portfolio position it as a compelling alternative to pure-play homebuilders in this housing recovery. Weyerhaeuser is targeting a payout of 75% of FAD over the cycle and is well positioned to raise its dividend as the housing recovery gains momentum. The company has already boosted its dividend by 33% since October (WY shares currently yield ~3%).

The call for this week: According to the weight of the evidence, the primary stock market trend remains "up!" Indeed, last Thursday's gain, while not a 90% Upside Day, was indeed an 80% Upside Day as the market breadth, and total points gained, were decidedly positive. Manifestly, since 1940 there have only been 45 other days when 80% of issues and volume were positive and the SPX closed at a new 52-week high (like happened last week). Of those, only seven occurred two days in a row. According to the must have SentimenTrader folks, "To get more precedents, let's look for any time that both the percentage of up issues and volume were both above 75%, with the last one occurring on a day the S&P closed at a new high. In 73 years, there have been 17 precedents. A week later, there were only three negative returns, and two of those were less than -0.5%. Three months later, there was essentially only one negative return, as was the case six months later was well. Average returns were about double what a random return was during the study period." Verily, the only current negatives are the short-term overbought condition (see chart on page 3) and the upside non-confirmations.

Source: Bespoke Investment Group.

Red = S&P 500

Green = overbought McClellan Oscillator



Source: Thomson Reuters.

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Market Perform (MP3) Expected to perform in line with the underlying country index.
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Underperform (Sell)	7%	1%	0%	20%	3%	0%	0%	0%

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