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KEY TAKEAWAYS

- ⇒ *Fiscal cliff dialogue means market risk decreasing*
- ⇒ *Is everyone declaring a special dividend?*
- ⇒ *The January Effect draws near and draws profits*
- ⇒ *Some trends from this year will carry over which isn't so great*
- ⇒ *Systemic changes could be precursor to economic growth aid*

KEY STATISTICS

Index	Close	YTD
DJIA	13135	6.8%
S&P 500	1414	12.6%
NASDAQ	2971	14.2%
Russell 2K	824	10.9%

(figures are rounded)

Market Ready Now

When you play the game of “chicken”, the loser is usually the one that flinches first. If the fiscal cliff dance between Obama and House Majority Leader Boehner is chicken, then Boehner lost. Moreover, the winner is the stock market.

In a news report over the weekend, it appeared that Boehner caved in the issue of higher taxes for the wealthy. If that philosophy moves ahead, eve with additional, other wacky proposed spending cuts, debt limit raises and tax deduction ideas move forward, at least some of the uncertainty in stocks is removed. Again, while the end result of the policy changes may still not be good for us, dialogue is a good thing.

Which brings us to 3 of our favorite words: *The January Effect*. More on that in a moment. We need to touch upon something we noted a few times last week in our *Market Monitor* (daily blogs.)

We talk a lot about seasonality because most investors' gains occur during big, but short runs in the market, and oftentimes, these big runs occur from December – January. This year it is a little different than most because of the fiscal cliff concerns. In some cases, we have seen some small cap stocks and penny stocks generate have a bit of a run. Still, it has not been a scenario where a rising tide lifts all boats, in this segment.

To combat the concern regarding the potential of significantly higher dividend tax rates in 2013 and to generate interest in their companies, we have seen large cap stocks declare special dividends recently, in addition to initiating or continuing stock buybacks. Not to be outdone, small cap stocks have joined the fray. For example, Rentech (NYSE – RTK - \$2.94, a stock we featured nine months ago and last week, declared a special dividend of \$0.19 (a 6.6% rate). The larger cap-RCM Technologies (NASDAQ – RCMT - \$6.63) really went overboard and declared a \$1.00 special dividend with the same record and distribution dates. Based on Friday's trading, that is a 15% special dividend rate. (cont'd)

Weird Moves

This is all highly unusual stuff. Normally, at this time of year we are all about the *January Effect* and how for the most part, some quick, easy money can be made by savvy traders.

What is (usually) great about the last 2 weeks of December is that virtually all the institutional window dressing/selling has passed. Plus, all selling for tax purposes or the selling of small cap losers by individuals has passed. As a result, many small cap stocks are temporarily low prompting portfolio managers and individual investors alike are buying stocks for 2-6 month holding periods.

This year, the selling is behind us, but the buying and volume gains have not really occurred yet as investors remain concerned about the likely rise in capital gains taxes for 2013.

The January Effect

Still, with 2 weeks left in the year, and the probable agreement to stave off the fiscal mess on the horizon, investors and traders should start making their list and checking it twice. Even with the fiscal cliff, the timing is primed for followers of the *January Effect*.

There are multiple definitions associated with the *January Effect*, and this year's fiscal cliff phenomenon may prompt the inauguration of a new name for it as well. In a nutshell, the *January Effect* is an historical Wall Street moniker for the belief that small cap stocks outperform large caps from January through June, with the trigger based upon catalysts mentioned above. In fact, this event has occurred for 27 of the past 33 years, which is an 82% accuracy rate!

One example of the *January Effect's* real impact is the list of *January Effect Stocks*, produced annually by the well-regarded Ned Davis Research. It is generated by screening for the smallest 10% of the stocks in the S&P 1500-stock index that also are among the 10% of stocks furthest from their calendar-year closing high. From 1996 through 2009, the portfolio returned an average of 8.6% from mid-December through the end of January, well above the 1.2% gain of the S&P 500.

Check out his list. It is usually very interesting. In the meantime, as you begin to build your list of potential buys, be sure to fill it with the big losers of 2012 and recent momentum plays of stocks that have just hit new 52-week highs. As you begin to build your list of potential buys, be sure to fill it with the big losers of 2012 and recent momentum plays of stocks that have just hit new 52-week highs. We will start to give you some of our own *January Effect* stocking stuffers later this week.

An Observation

It is really remarkable that the stock market has held up and enjoyed strong gains this year, despite all of the poor, underlying fundamentals of the both the domestic and global economy. It goes to show just how much a low-growth, low interest rate environment still means to investors. Equities remain one of the better sources of investment capital. Yet, with the poor corporate finance, investment banking and trading characteristics, plus greater regulation, it makes one think twice about what this will all look like in 5 years.

In the meantime, publicly traded companies, unable to eke out any “real” top-line growth, have opted for



greater efficiencies to generate higher income growth rates. Since many have been sitting on large cash piles, and have been reticent to spend to grow their businesses due to fears of an even worse economic scenario, we have witnessed different methods of trying to woo investors. This has included what certainly appears to be an unprecedented number of companies enacting and executing stock buybacks and declaring special dividends.

In some cases, there is a sleight of hand occurring, where troubled firms are hiding behind the ruse of dividends and buybacks to mask the underlying funda-

mental problems in which they face.

Separately, many OTCBB firms and others that have seen trading and funding dry up due in part to over-regulation, are scrambling to up-list their shares.

Some of these trends (buybacks and uplistings) will continue into next year and it is likely that the moves will have a more muted effect as the year progresses. Momentum and short-term trading especially in sideways markets should continue to rule the day, until we can see some real economic growth. It will be interesting to see how crowdfunding plays a role in the speculative investment world next year. I suspect that we could see a return to more speculation which is not really a good thing if the deal quality is poor. I am hopeful that a new exchange/marketplace, or a different system of the entire investment process is explored, to foster growth of new, small businesses hiring people to spur economic growth and fill our coffers with cash.

Until next week....



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1498 Reisterstown Road, Suite 286
Baltimore Maryland 21208
Phone: 410.609.7100
info@goldmanresearch.com
www.goldmanresearch.com

Analyst: Robert Goldman

Rob Goldman founded Goldman Small Cap Research in 2009. Rob has over 20 years of investment and company research experience as a senior research analyst and as a portfolio and mutual fund manager. During his tenure as a sell-side analyst, Rob was a senior member of Piper Jaffray's Technology and Communications teams. Prior to joining Piper, Rob led Josephthal & Co.'s Washington-based Emerging Growth Research Group. In addition to his sell-side experience Rob served as Chief Investment Officer of a boutique investment management firm and Blue and White Investment Management, where he managed Small Cap Growth portfolios and *The Blue and White Fund*.

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