The Goldman Guide

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INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *The bull is done for a multitude of reasons*
- ⇒ *Valuations are high, performance is poor*
- ⇒ *Check out market strategists year-end forecasts for the S&P 500*
- ⇒ *Our 2015 small cap picks are killing it*
- ⇒ *How to use covered calls with small caps*

THE MAJOR INDICES

Index	Close	2015
DJIA	18010	1.1%
S&P 500	2107	2.3%
NASDAQ	5070	7.1%
Russell 2000	1246	3.4%

(figures are rounded)

Smarter Than The Average Bear

Yogi Bear, the iconic cartoon character, had a famous catch-phrase: “I’m smarter than average bear.” As most of you are aware, oftentimes he was not only smarter than the average bear but the Ranger as well.

Unless you are in the “Neutral” camp regarding stocks, odds are that you and Yogi Bear have a lot in common. If you are bullish on stocks, you obviously are ignoring the warning signs and think you are smarter than the average market bear. If you are bearish on the market, it is likely that you think you are one step ahead of everyone else, just like Yogi was way ahead of Ranger Smith. It goes with the territory. Bears always think they have magic intel or insights. Plus, just as Yogi Bear was always showing off his brainiac bear skills by stealing picnic baskets, brainy bearish investors steal market value by engaging in short selling or going directly after perceived “weak” stocks.

As for me, I am pragmatic. I generally believe that we usually operate in a secular bull market that endures short to intermediate term corrective phases and even bear phases that are not as long-lasting as the bullish terms. Most bulls are eternally optimistic and most bears are eternally negative and we see it today with wild prognostications on both sides.

As for the unabashed bulls, they are like a river in Egypt: “(De) Nile.” They ignore the tell-tale signs. The bears must still be grumpy from hibernation since they see only catastrophes in the global economy ahead.

History Suggests the Bull is Nearly Done

Sometimes we get so caught up in the here and now, and what is on the come that we take for granted what we have already experienced. This situation is precisely why one must pragmatic and unemotional when assessing the current situation.

One of the people I respect the most in the industry is Laszlo Birinyi and I am pleased that I was able to have even a small, short term relationship back in the day. One of Birinyi Associates' online publications, TickerSense, published a great piece on the market on Friday and I am sharing highlights of that blog right now.

Interestingly, last week, I was looking at how far the market has risen and what the prospects were in mid-October, as compared to today, as part of a piece I was going to pen that illustrated the nightclub has to shut down for a while. I will address that in a moment, but here is even more interesting and useful data, courtesy of Birinyi Associates.

Secular Bull Markets

Start	End	Perc Chg	Days
06/26/62	02/09/66	80%	1,324
10/03/74	11/28/80	125%	2,248
08/12/82	08/25/87	228%	1,839
10/11/90	07/17/98	302%	2,836
10/09/02	10/09/07	102%	1,826
03/09/09	**05/27/15**	**214%**	**2,270**
Average:		175%	2,057

Today's investors are spoiled and clearly do not realize how great we have had it since the bull market began in March 2009. According to Birinyi, ever the eternal bull, we have had 6 secular bull markets since 1962. The current bull market, at 2,270 days, is the second longest of the six, and has enjoyed the third best gain, at 213%. As of today, we have already exceeded the average bull market length, which should be cause for consternation. After all, the longest bull market, in the 1990's was fueled by the internet bubble. Perhaps we are winding now as well, at least for a spell.

Since we live in an instant gratification world, it is no shock that investors don't seem to appreciate anything. Six and one half months ago, the recent market low on the S&P 500 Index was 1820. Today, it stands at 2107, a nearly 16% gain, and that ain't nothing.

Valuation is High, Performance is Poor

As illustrated in the chart below, courtesy of Finviz.com, the healthcare space is up over 26% during this period.

Even ardent bulls have to sit back and see that with a drop of 0.7% in GDP for the first quarter of 2015 business is tough all over. Moreover, year-over-year quarterly earnings may not see positive levels until later in the year. If the dollar wasn't so strong it would have a bigger effect on attracting investment funds here. It already is negatively impacting multinationals and too many investment dollars are flowing out of domestic funds to funds abroad. Throw in a fair value valuation for stocks and we think we are heading into "correction city" before gains occur later in the year as earnings growth returns.

The bottom line is that against the backdrop of "fair" valuations, inconsistent economic growth, and more Fed concerns, it is hard to be anything more than moderate bullish for the interim. As illustrated in the Finviz.com table below, the average forward P/E for the 9 S&P industry groups is 16.9, which is not cheap. Hell, with anemic growth, how can the market justify an average PEG of 2.6x for these groups? By the way, anyone ever note how health care has dominated stocks' performance? These 9 groups are up an average of 2.66% year-to-date, but without the 12.4% health care run, the average returns is actually an anemic 1.45%.

Are Strategists Too Optimistic?

Stock Group Valuation

Name	Stocks	Market Cap ($, mil)	P/E	Forward P/E	PEG	Float Short
Conglomerates	17	$22,021	31.26	24.16	5.79	1.74%
Basic Materials	620	$5,413,822	18.8	18.79	3.38	3.42%
Healthcare	720	$4,566,267	27.05	18.45	2.38	4.25%
Services	854	$5,318,301	23.37	18.14	1.56	4.23%
Technology	869	$6,568,223	22.71	17.06	1.75	2.95%
Consumer Goods	366	$4,541,742	20.6	16.32	1.84	2.25%
Industrial Goods	361	$2,051,707	22.88	16.3	2.15	2.95%
Utilities	118	$906,090	17.82	15.11	2.92	2.59%
Financial	1162	$7,330,238	16.3	7.35	1.63	1.30%

Source: Finviz.com

Another gem from Birinyi from Friday is a list of strategists year-end S&P 500 Index targets. The list includes 19 chief strategist forecasts from major Wall Street firms. (I worked with 2 of them in previous lives.) Interestingly, despite the negative items we outlined above, all but one has a target higher than the recent S&P 500 Index close, and he is from Goldman Sachs. Two others project a 2350 close, which would mean a 11.5% rise from here. The average of all 19 is 2,232 which equates to a 8.4% gain from 12/31/14 and a 5.9% rise from current levels.

On December 15, 2014, we forecasted a 5% peak gain in the S&P 500 for 2015. That would take it to 2162, a modest 2.6% move from the 2107 close. Not only will I stick with my number as a peak projection but I will even go so far as to say that we will be below this figure by year-end, plus or minus 20 points. I just think that we could drop several percentage points before a solid rally, just as we experienced in 2014.

Say What?

Yahoo Finance

http://finance.yahoo.com/video/amusement-parks-busy-summer-cedar-125420907.html

The premise is sound but FUN, SEAS, and SIX are valued at 25x 2015 EPS, with upside to 10%. Check back in Dec..

Marketwatch

http://www.marketwatch.com/story/three-times-rotten-a-recovery-have-never-seen-this-many-dips-2015-05-29?link=MW_home_latest_news

I don't know why economists are making excuses in reporting. Can't we just agree the economy sucks, which is obviously bad for stocks?

Bloomberg

http://www.bloomberg.com/news/articles/2015-05-29/guess-who-in-d-c-helped-these-stocks-double-hint-not-the-fed

FDA and orphan drugs are on fire.

The New York Post

http://nypost.com/2015/05/30/how-the-us-created-the-camp-where-isis-was-born/

Oh crap.

BizJournals.com

http://www.bizjournals.com/bizjournals/washingtonbureau/2015/05/why-the-economy-could-benefit-if-the-supreme-court.html

Fresh and interesting perspective.
http://nypost.com/2015/05/30/how-the-us-created-the-camp-where-isis-was-born/

Just the Stats!

By the Numbers

For the first five months of the year, the DJIA and S&P 500 Index are up around 1% and 2%, respectively, while NASDAQ kicks butt, up over 7%. Meanwhile, the Russell 2000 has given us a respectable 3%+ performance. Looking at last week's figures, volume was pretty impressive-more so than in recent weeks. <u>In fact, on Friday, volume on the S&P 500 of 3.9 billion shares was the largest since April 30th, when the index traded 4.5 billion hares and dropped 1% (ironically from the 2107 level to 2085.)</u>

We continue to see slow shifts on the negative side with respect to divergence in the 52 week high/low figures and advance/declines. As of May, the YTD highs for both combined are 196 versus 171 combined lows, which is lower than in April. As you have likely surmised, may's performance was anything but stellar for stocks. Total advances for the month were 812 versus 3314 decliners, a difference of nearly four times.

AAII Sentiment Survey (courtesy of AAII.com, figures rounded)

More of the same but a little relenting, perhaps ahead of hope that June is better than May…still, it is now 8 weeks of over 45% Neutral.

Last Week	Long Term Avg
Bullish 27%	39%
Neutral 48%	31%
Bearish 25%	30%

Lipper Fund Flows Survey (courtesy of Lipper.com)
(as of 5/20/15)

Z'BigNews

Orbotech (NASDAQ—ORBK—$20.90—NR) was tabbed as our small cap stock pick of the year and featured again last week as we thought the valuation warranted another table pounding. The stock did not disappoint and broke through the $20 mark for the first time in 8 years on news of a new order. Volume was huge and the stock reached a peak return for the week of 10%. More upside is still in the cards, in our view.

Skechers USA (NYSE—SKX—$105.87—NR) continues to "run" higher as the company announced it has the #2 brand position in America's athletic footwear market. We were on the stock early and it has not disappointed, with the shares up 58%. Start taking a little off the table, if you have not already done so.

We probably should have pulled the trigger on **1-800 Flowers (NASDAQ—FLWS—$9.51—NR)** a couple of weeks ago, but now looks like the run is over. Therefore, we are removing the stock from our "Pick 'em" list. Ditto for **SkullCandy (NASDAQ—SKUL—$7.50—NR)**, a stock that did so well for us earlier in 2015 has been rotten of late. We had it under review and in hindsight dropped the ball by not removing it earlier.

Liberator Medical (NASDAQ—LBMH—$2.62) has stunk up the joint, down 11% since our feature a little while back. Have a little faith, baby. We think this is just a blip.

Speaking of blips, our short term trading idea off of the VIX and a market downturn was anything but profitable as VelocityShares Daily 2x VIX ETN (NYSE—TVIX—$0.89—NR) has gone the wrong way. Never fear, as this is still a great day-trading and risky vehicle when things are headed south.

Speaking of short term trading, **Plasmatech BioPharma (NASDAQ—PTBI—$7.85—NR)**, the Soros company did what we thought—went up big a few times and is now essentially back where it started a few weeks ago, in the $7.00 range.

More Stats

GSCR 2015 Picks and Pans					
The Goldman Guide: Big Cap Picks					
Stock	Pick/Pan	Profile Date	Orig Price	5/29/2015	Return
DOD	Pick	1/2/2015	$15.35	$15.57	1.4%
T	Pick	1/2/2015	$33.87	$34.54	2.0%
VZ	Pick	1/2/2015	$46.96	$49.44	5.3%
CVX	Pick	1/2/2015	$112.58	$103.00	-8.5%
AAPL	Pick	1/2/2015	$109.33	$130.28	19.2%
Big Cap Avg					*3.9%*
S&P 500					2.3%
Source:	GSCR, Yahoo!Finance				

Now that the first five months of the year are in the books, it is time that we see how our Guide-profiled stocks have fared. For better relative comparison, we have segmented our profiled picks into three categories for now: Big Cap, India, and Small Cap. As we introduce more short term trading ideas and ETFs, we will add these categories with the appropriate benchmarks for performance comparison, later on in the year.

As you can see, our big cap picks, aided in large part by powerhouse **Apple (NASDAQ—AAPL—NR)** has been solid and canceled out the drop in **Chevron (NYSE—CVX—NR)**. Meanwhile, India has been no China, and our picks have been nothing to write home about.

GSCR 2015 Picks and Pans					
The Goldman Guide: India Picks					
Stock	Pick/Pan	Profile Date	Orig Price	5/29/2015	Return
PIN	Pick	1/9/2015	$21.53	$21.77	1.1%
IBN	Pick	1/9/2015	$11.55	$10.56	-8.6%
TTM	Pick	1/9/2015	$43.83	$38.30	-12.6%
India Avg					*-6.7%*
Emerging Mkts ETF (NYSE - EEM)			$39.27	$41.12	4.7%
Source:	GSCR, Yahoo!Finance				

Strong Small Cap Gains

We are pleased to report that our picks trounced the index, with help from gains led by SKX, ORBK, VLTC (which is down from recent highs), ZIXI, and GLUU. Note the changes to the list in the footnotes below.

GSCR 2015 Picks and Pans

The Goldman Guide: Small Cap Picks

Stock	Pick/Pan	Profile Date	Orig Price	5/29/2015	Return
MSO	*Pan*	*1/16/2015*	*$4.77*	*$5.20*	*9.0%*
ZIXI	Pick	1/16/2015	$3.71	$4.59	23.7%
ELY	Pick	1/23/2015	$7.92	$9.44	19.2%
FLWS^	Pick	1/30/2015	$7.89	$9.51	20.5%
HRB#	Pick	2/6/2015	$35.38	$31.55	-10.8%
JGW	Pick	2/6/2015	$10.24	$9.38	-8.4%
ORBK	Pick	2/13/2015	$15.87	$20.90	31.7%
INTT	Pick	2/20/2015	$4.16	$4.64	11.5%
CVU#	Pick	2/20/2015	$11.87	$11.14	-6.1%
LCI	Pick	2/20/2015	$63.23	$55.63	-12.0%
LPSN#	Pick	2/27/2015	$11.54	$9.42	-18.4%
SKX	Pick	3/6/2015	$66.79	$105.87	58.5%
VA#	Pick	3/13/2015	$34.77	$28.53	-17.9%
GLUU	Pick	3/20/2015	$4.95	$6.48	30.9%
SKUL^	Pick	3/27/2015	$10.85	$7.50	-30.9%
VLTC	Pick	4/2/2015	$2.63	$6.56	149.4%
LBMH	Pick	5/3/2015	$2.94	$2.62	-10.9%
GCA	Pick	5/24/2015	$7.84	$7.73	-1.4%
SC Buy Avg*					13.45%
RUT 2000					3.4%

Source: GSCR, Yahoo!Finance

*excludes pans and FNRG which has been suspended
**Our NT target on FLWS was $10
***Our NT target on VLTC was $5
# denotes no longer pick as of 5/1/15
^ denotes no longer pick as of 5/31/15

The Investor Academy

Beginning with this issue, we are featuring a teach-in section called *The Investor Academy.* Depending upon the topic, this segment can be viewed as Investing 101 or serve as secrets of a former Wall Street insider that leverages our many years of experience in senior positions on Wall Street, including analyst and mutual fund manager.

Stock Buybacks Are No Longer a Good Thing

Aside from the obvious low economic growth and high P/E multiples for equities, one of the problems with the current bull market is that a series of stealth events has likely prolonged its duration and its magnitude. Unfortunately, these events may soon come to a close and take the bull market with it.

The first cause for concern is the stock buyback. Stock buybacks have been a steady feature of the stock rally which has definitely had an impact on stocks as companies that comprise the S&P 500 Index have spent hundreds of billions in stock buybacks over the past 6 years. With fears over the commencement of a market correction, management teams may elect to soon put the brakes on their buyback plans. If that were to occur, investors would surely recognize that liquidity, volume, and prices would drop, further exacerbating a stock market decline and potentially protracting a downturn.

Another byproduct of a stock buyback suspension is its impact on financial reporting. When a company buys back its shares in the open market that stock is returned to its treasury and the number of shares outstanding is reduced by that number. So, when a company reports financials that demonstrate a decline in shares outstanding from the year-ago period, EPS could be raised not by operating performance but simple math. Fewer shares in the share count results in a higher earnings per share. Once a buyback plan is suspended, that incremental EPS gain is lost, making it harder to outperform EPS recorded in prior periods.

The Investor Academy

Most small cap investors and traders do not think of options when buying or selling stocks in the small cap space and there is generally lot of fear inappropriately associated with the word 'options'.

The fact is that option strategies can be used in a simple way to generate income for short-term – intermediate-term holdings which can add to returns. How? Use covered calls. It is not as difficult as it sounds.

For those not familiar or those needing a review here is what is involved simplest terms:

⇒ *Buy* 100 shares of stock XYZ
⇒ *Sell* 1 Call Contract of stock XYZ (1 contract = 100 shares of underlying security)

After the transaction, the investor will own the stock and generate the income of the trade price of the option contract. One crucial element to remember is that 1 contract equals 100 shares of the underlying stock. So, the investor needs to buy 200 shares for 2 contracts, 300 for 3 contracts, etc. to ***cover*** the total number of call contracts.

A sound tactic is to sell 'out of the money' calls at a strike price equivalent to what you are willing to take profits and sell the underlying security. This mechanism is automatically in place, as the buyer of the call could 'exercise' or buy the stock from the contract if it moves above the strike, which is in essence *your* target price.

As a result, the worst-case scenario is that you sell the stock at your low-end target price and the best-case scenario is that you generate income from the call option sale, enhancing your return on investment.

The Investor Academy (cont'd)

We recommend incorporating the following criteria when using a covered call strategy.

⇒ Buy stock with price under $10
⇒ Stock has demonstrated upward momentum with at least 25% increase off of 52-week low
⇒ Technical Analysis illustrating short, intermediate, and long term bullish indication
⇒ Consensus Analyst Opinion of **Buy** or Better
⇒ Out-of-the-money strike price at least 6 months from expiration and above $50 premium for sale. (Remember premium from sale = ask price x 100)

By using these screens, the stock price would have to rise above $10 before buyers would begin to exercise. Additionally, if and when this exercise would happen, it does not necessarily mean that the contract(s)) an individual holds will be exercised; it is the 'luck of the draw'. Plus, you can always reverse the transaction by buying the same month and strike price call and selling the underlying shares to back out completely, although we would not recommend it.

If the call contract you sold does get exercised, the 100 shares of the underlying stock you own are sold at the strike of $10 and that is what you generate on the sale.

As an example, if you bought 100 shares of XYZ at $9.35, you will earn $65 from the sale of the stock, and income of $50 from the original sale of the call, which could nearly double your profit margin on the entire transaction.

Remember, these trades *are not free*, so make sure you know how much your broker charges before you go charging ahead.

Have a great week!

The Goldman Guide

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