

“The Joy of Cooking”

Directions: In a large bowl, combine the following contents with a hugely confused investor population. Toss lightly. Just before roasting the turkey, spoon ingredients loosely into the body cavity of the turkey and do not overstuff. Truss all the opening so that no investors can escape. Use skewers if necessary.

Ingredients: Bread crumbs, watered down stock, enriched money supply, artificially low interest rates, depreciating currencies, malted securities, financial sausage, derivative yeast to increase expansion, roasted European chestnuts, governmental regulations to retard spoilage, and unelected czars to further enhance the mixture.

Selecting the Turkey: When it comes time to pick out the bird, we always remember the old stock market “saw” about poker games. In every poker game there is always a loser, also known as the “turkey.” If you have been playing poker for over 30 minutes, and you haven’t figured out who is the turkey, YOU are likely the turkey!

Stuffing the Bird: Always wait to stuff the bird until just before roasting. This may not be convenient, but it is by far the safest procedure. Fill the bird only about three quarters full, since the stuffing assuredly will expand.

Roasting: In timing the meat, remember that many factors are involved. The age of the bird, how fat it is and whether it is fresh. Generally the bigger the bird the longer it takes to cook. Keep in mind that all parts of the bird do not cook at the same time. We suggest a thermometer to test when it is done.

So wrote our dear departed friend, Stanley D. Salvigsen, decades ago from his perch as president of Comstock Partners. Stan began his investment career in 1964 as an analyst with the Value Line Investment Survey. Subsequently, he was an equity strategist at a succession of firms, including Dreyfus, Oppenheimer, C. J. Lawrence, and Merrill Lynch. Stan wrote the most engaging, entertaining, colorful, and insightful strategy reports I have read in my 41 years in this business. Select titles of his reports were: “That Ain’t Mud on Your Boots Partner,” “Revenge of the Nerds,” “Homesick,” and my favorite “Surf’s Up!” “Surf’s Up” showed pictures of a plethora of landside observers watching the few daring surfers willing to brave the 40-foot waves of Waimea Bay. Stan likened those surfers to the investors who had the courage to buy stocks in the summer of 1982 and ride the “big bull waves” that were likely going to occur as interest rates declined from 22%. It was a tempestuous time when my pleas to investors to buy stocks fell on deaf ears as their mantra was, “Why should I buy stocks when I can get 22% in a money market?” My response was, “That’s exactly why you should buy stocks!” Stan died of a heart attack in 1996 at the tender age of 53 in the offices of one of his best friends. Truly, a Wall Street icon who is still missed by many for his keen-sighted strategy reports.

Last week another Wall Street icon “fell,” but this time not because of death. Rather, Legg Mason’s Bill Miller “fell” due to market hubris. I worshiped Bill Miller’s prose from Richmond, Virginia until I moved to Baltimore and met him in the early 1990s. In subsequent meetings I found that his investment philosophy consisted of, “The man with the last dollar wins.” The idea was that if you average down in a declining stock, provided it’s not Enron-like, you inevitably “win” when that stock bottoms and rallies. Of course that strategy worked during the 18-year secular bull market that began in the summer of 1982 . . . until it didn’t.

Interestingly, in 1982 Bill Miller inherited Legg Mason’s Value Trust (LMVTX/\$36.09) from another portfolio manager named Ernie Kiehne. “Keen Ernie’s” investment style was to watch companies with large revenues and then buy their shares when the net margins began to expand. That style left Ernie with large holdings in companies like supermarkets, which didn’t really “work” in the early 1980s and therefore he was removed from command of the fund. Enter Bill Miller at the start of the great bull market that began in the summer of 1982. Yet, while brilliant, Miller was anything but a value investor, often preferring growth stocks like AOL (AOL/\$14.73) over value stocks. Plainly, that strategy also worked until it didn’t. Subsequently, he gave back all of his years of outperformance in the 2007 – 2009 debacle. To be sure, the strategy of “The man with the last dollar wins” collapsed in that decline, which lopped ~58% off of the S&P 500 (SPX/1215.65).

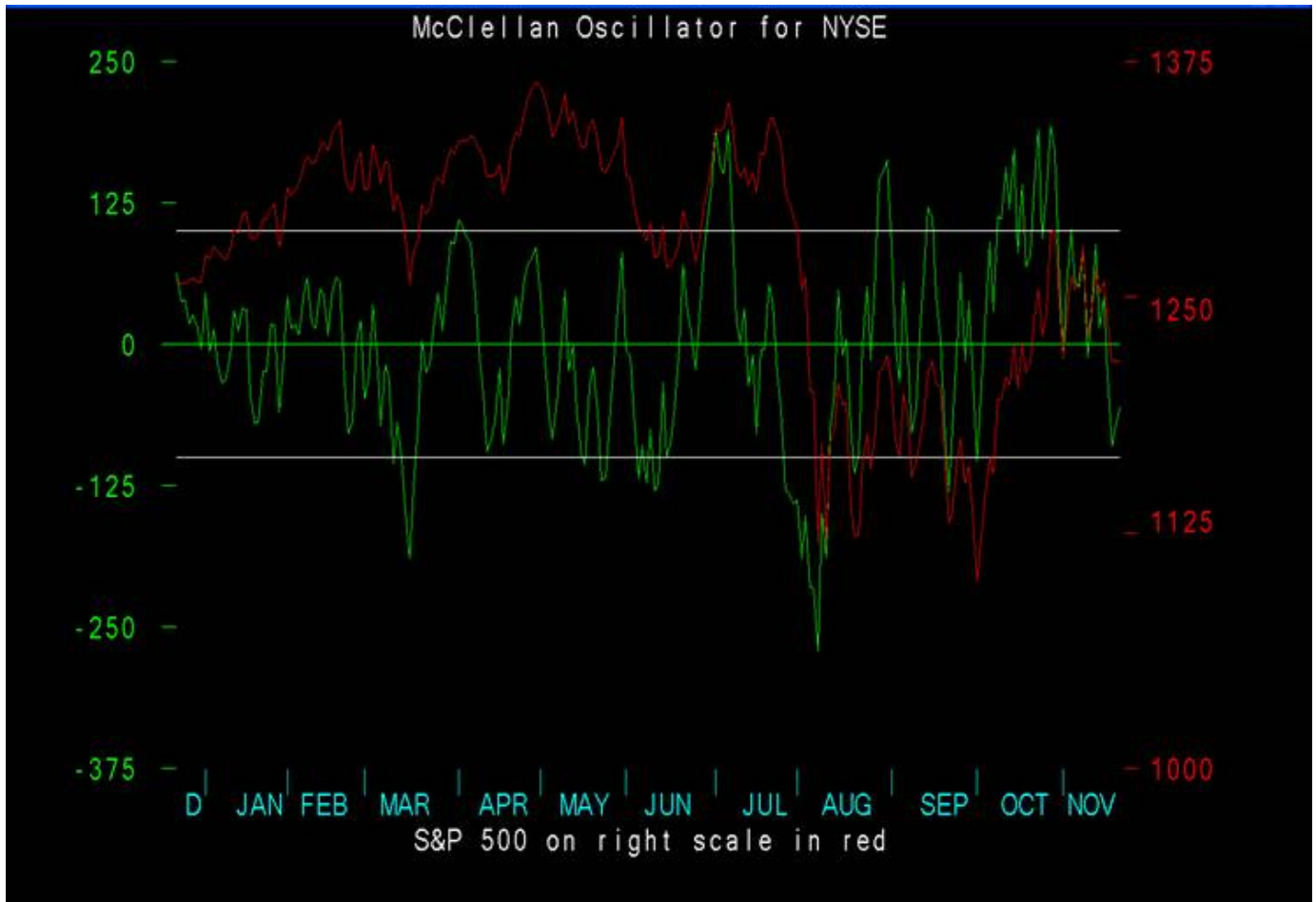
I revisit the Bill Miller saga this morning not to kick a man when he is down, but to reinforce the quote from the book “The Intelligent Investor” where Benjamin Graham tells us, “The essence of investment management is the management of risks, not the management of returns. All good portfolio management begins [*and ends*] with this tenet!” Clearly, Bill Miller deviated from that tenet as he rode many of his investments to substantial losses. Last week, such losses were pointed out to me by a Raymond James

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Financial Advisor who “pinged” me with the question, “Hey Jeff, we bought NII Holdings (NIHD/\$23.41/Strong Buy), based on your recommendation, around \$40.00 and we are now down some 50% in those investments. What’s the story?” After giving our fundamental analyst’s response that NIHD collects its revenues in the Brazilian currency, but reports its earnings in U.S. Dollars; and, that the rally in the U.S.\$, *vis-à-vis* the Brazilian Real has really hurt NII’s earnings. Then I reminded my emailer that since the first Dow Theory “sell signal,” of September 1999, I have been adamant about not letting ANYTHING go more than 15% - 20% against you. That doesn’t mean I always sell a position at down 15% - 20%, but at that “uncle point” I take some kind of action. Sometimes it is to sell, other times it is to hedge the position to prevent the “Big Loss.” Indeed, the essence of investment management is management of risks, not the management of returns!

Another investment position I have recently been queried about is EV Energy Partners (EVEP/\$65.27/Strong Buy), which over the past few weeks has declined from \$78 per share into last Friday’s closing price of \$65.27. There are some reasons for the decline. Firstly, and most importantly, rumors are swirling that the Obama administration is stopping energy operations in the Utica Shale Basin for environmental reasons. This is not true! What did happen was the Obama administration stopped new land leasing in the Utica for environmental reasons. Yet, the companies that already own mineral rights should still be able to drill. Secondly, a lot of “hot money” had piled into EVEP in anticipation of a Chesapeake Energy (CHK/\$24.33/Market Perform) joint venture (JV) announcement. When EVEP didn’t rally on that announcement, the “hot money” sold. Consequently, there is no near-term catalyst for EVEP. The company’s drilling results in the Utica are likely months away. EVEP’s JV announcement isn’t due until 2H12 and then there is always the potential of a stock overhang. Operationally, however, our energy team doesn’t know of anything wrong.

The call for this week: Last Friday CNBC’s Maria Bartiromo asked me what was going to happen with this week’s Super Committee decision? After jokingly responding that if past is prelude if the Super Committee doesn’t arrive at a decision they will appoint a SuperDuper Committee, I then stated, “I don’t think the Super Committee will reach a consensus.” I also opined, “I believe there is a wink and a nod between President Obama and Speaker John Boehner to not implement the mandatory ‘cuts’ and let the 2012 Presidential election resolve the debate between increased taxes and spending cuts.” Quite frankly, I don’t know of any member of Congress that will stand for major military base closings in his (or her) state. Meanwhile, earnings continue to surprise with S&P 500 earnings up ~22% y/y, while revenues improved ~11.7% y/y. Such reports make it increasingly uncomfortable for the underinvested crowd; and the world remains profoundly underinvested in U.S. equities. Accordingly, I think stocks will continue to grind higher, provided we don’t talk ourselves into a recession. The reasons for that view are: 1) underinvested portfolio managers playing “catch up” (read: performance anxiety); 2) the upside seasonal bias; 3) low stock valuations; 4) improving economic trends; 5) still depressed sentiment readings; and 6) the knowledge that we have now entered the best performing six months of the year for stocks. Consistent with this view, I think the buying of inexpensive beta makes sense. To parse that theme, I screened our Analysts’ Current Favorites List, excluding the banks, looking for companies with less than an 18x P/E multiple (based on forward earnings estimates) and with more than a 1.20 Beta. Then I overlaid my proprietary technical algorithms and came away with the following names, all of which are rated Strong Buy by our fundamental analysts: Energy XII (EXXI/\$30.25); National Oilwell Varco (NOV/\$67.50); VeriFone (PAY/\$42.97); and ValueClick (VCLK/\$16.07), which I offer for your consideration. Regrettably, the SPX has violated my long-standing pivot point of 1217, bringing into view 1206 and then 1191; and while it was not “decisive” as of last week, it looks like it is going to be decisive this morning. The approximate cause for this morning’s futures fade is our dysfunctional government punctuated by the Super Committee’s failure to reach a decision. On the positive side, there is a “ton” of internal energy that has been rebuilt over the past few weeks following our near-term overbought “cautionary call” of 10/29/11 in a report titled “Crescendo.” Additionally, if the equity markets open where the futures are indicating, the McClellan Oscillator should be in oversold territory, as can be seen in the chart on page 3.



Source: Bloomberg.

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	Coverage Universe Rating Distribution			Investment Banking Distribution		
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