

The Starboard Side Report

The week ending October 02, 2009

The seasonal correction that we have been expecting appears to be in full swing. According to Bespoke Investment Group, the S&P 500 just had the fourth worst October start on record.

S&P 500 on 1st Day of October

Date	% Chg
10/1/1998	-3.01
10/1/1934	-2.75
10/3/1955	-2.70
10/1/2009	-2.58
10/3/1966	-2.17
10/1/1931	-1.85
10/1/1956	-1.43
10/1/1962	-1.39
10/1/1975	-1.12
10/2/1933	-1.03
10/1/1976	-1.02

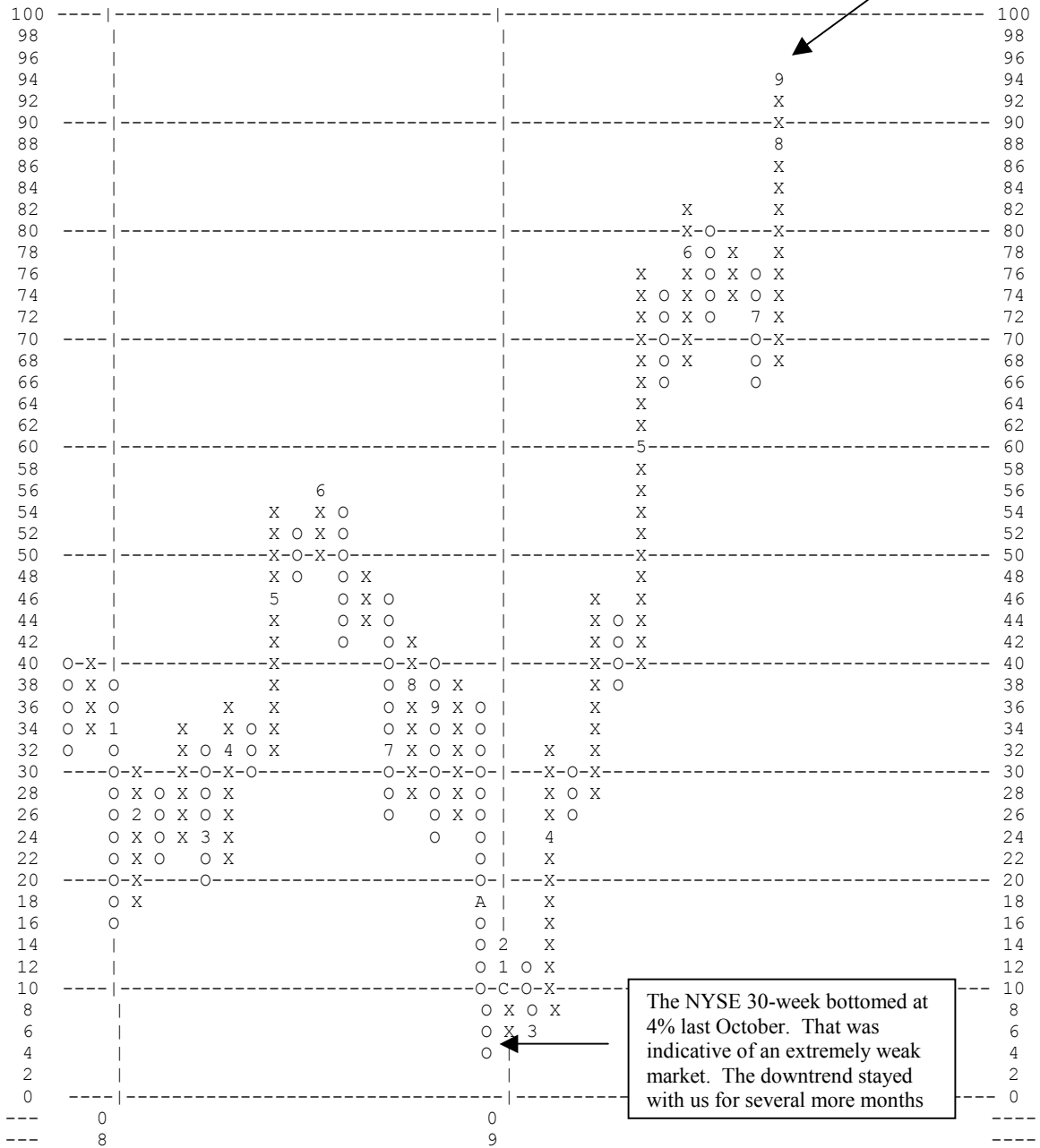
Source: Bespoke Investment Group

The good news is that after the other nine worst starts listed above, the market was able to shake-off the decline and head to a higher-high by the end of the year (11.7% above the Sept. closing price on average). That bodes well for this being just a temporary pullback in the context of a more significant up trend. In addition, it means we should not read too much into the bad start to October.

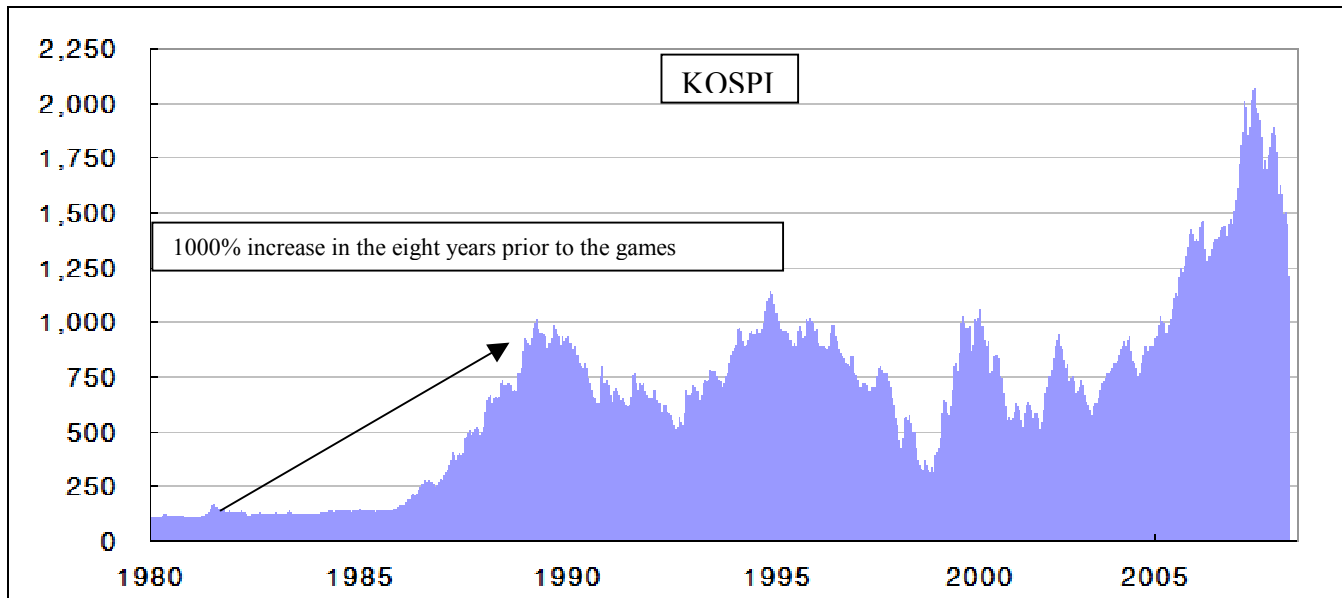
One valuable long-term technical indicator we track is the percentage of stocks on the NYSE that are trading above their own 30-week moving average (see chart on following page). This is a great barometer for the underlying health of the market. When it reaches an extreme level it often means that the easy money has been made, but that directional trend in force still has more room to run. On September 16th, this 30-week number breached the 94% level for only the eighth time since 1970. August of 1997 was the last time it was surpassed. Two things become clear after studying the other seven moves above 94%. First, the market uses a lot of energy getting to this level, so a short-term correction follows rather quickly. On average, we have seen a 5% decline within a few weeks of getting to the 94% level (the correction range has been 3% to 11% over a one month period). Second, the rallies that have pushed the market to that point have been so strong that they *always* resulted in a higher-high on the S&P 500 within six months. On average, the rally that followed the pullback phase was 13% above the prior peak. We continue to feel the evidence points to a strong close to the year and/or a good first quarter of 2010 after we get through this bout of turbulence.

30 Wk For NYSE (30NYSE)
 Updated Through- 10/01/2009 (89.230 Down 3.066)
 Bull Confirmed 94% Xs on 07/16/2009

Historically, 94% has meant that we're in the late innings, but the party is not over yet.



It is rather fitting that an emerging market has won the right to host the 2016 Olympic Games. We believe emerging economies, like that of Brazil, will continue to earn global respect in the years ahead as the US and Europe dig out of their financial holes. According to the *Financial Times*, Rio de Janeiro's capital spending budget for the 2016 Summer Games is \$11.1 billion. The average of the other three finalists (Chicago, Tokyo and Madrid) was only \$2.5 billion. This makes it clear that the Olympics are a significant economic event for an emerging market country. The past two emerging markets to get the Summer Olympics were South Korea in 1988 and China in 2008. We went back and analyzed the Korean Composite Stock Price Index (KOSPI) and the Chinese H share market as measured by the FTSE/Xinhua China 25 Index (FXI). Between 1980 and April 1989, the KOSPI surged ten fold, whereas the FXI had a 500% rally in the six years following the selection of Beijing in 2001. The market indexes seem to indicate that the most significant impact isn't felt until three or four years before the actual event. Therefore, it seems we still have some time before the biggest impact will be felt in the Brazilian economy. However, we feel this is still a big positive for Brazil on a net basis.



Source: Wikipedia



The Brazilian stock market has had some pretty amazing gains already this decade, so expecting 500-1000% returns may be on the optimistic side. However, the first chart below shows a strong bull market still intact despite the crash last year. Even more impressive is the relative strength of Brazil versus the US market over the past six years as seen in the second chart below.



One final chart on Brazil is a new small capitalization fund launched earlier this year by Van Eck Associates. Our research vendor Dorsey Wright has compiled data on the Market Vectors Brazil Small Cap Fund back to 2005. We believe small cap stocks in Brazil are an undiscovered asset class that offers great potential in the years ahead for US investors. This was true even before the Olympic announcement today. Brazil is the fifth most populous nation in the world and its tenth largest economy. Interest rates are still double digits, but have been declining rapidly over the past five years. The long-term interest rate cycle in Brazil looks similar to the US in the 1980's. Lower interest rates should be go news for Brazil's rapidly growing middle class. Unlike the Bovespa Stock Index, which is mostly global industrial companies, the Brazil Small Cap ETF is 38% consumer related. As negative as we are on the US consumer, we feel emerging market consumers such as those in Brazil are in very good shape to boost consumption in the years ahead.

Market Vectors Brazil Small-Cap ETF (BRF)
 Updated Through- 10/02/2009 (39.756 Up 0.576)- View History
IYY RS = Buy, 10/02/2009; col=Xs Score 6.00
 Trend Chart Broke a Double Top on 09/14/2009

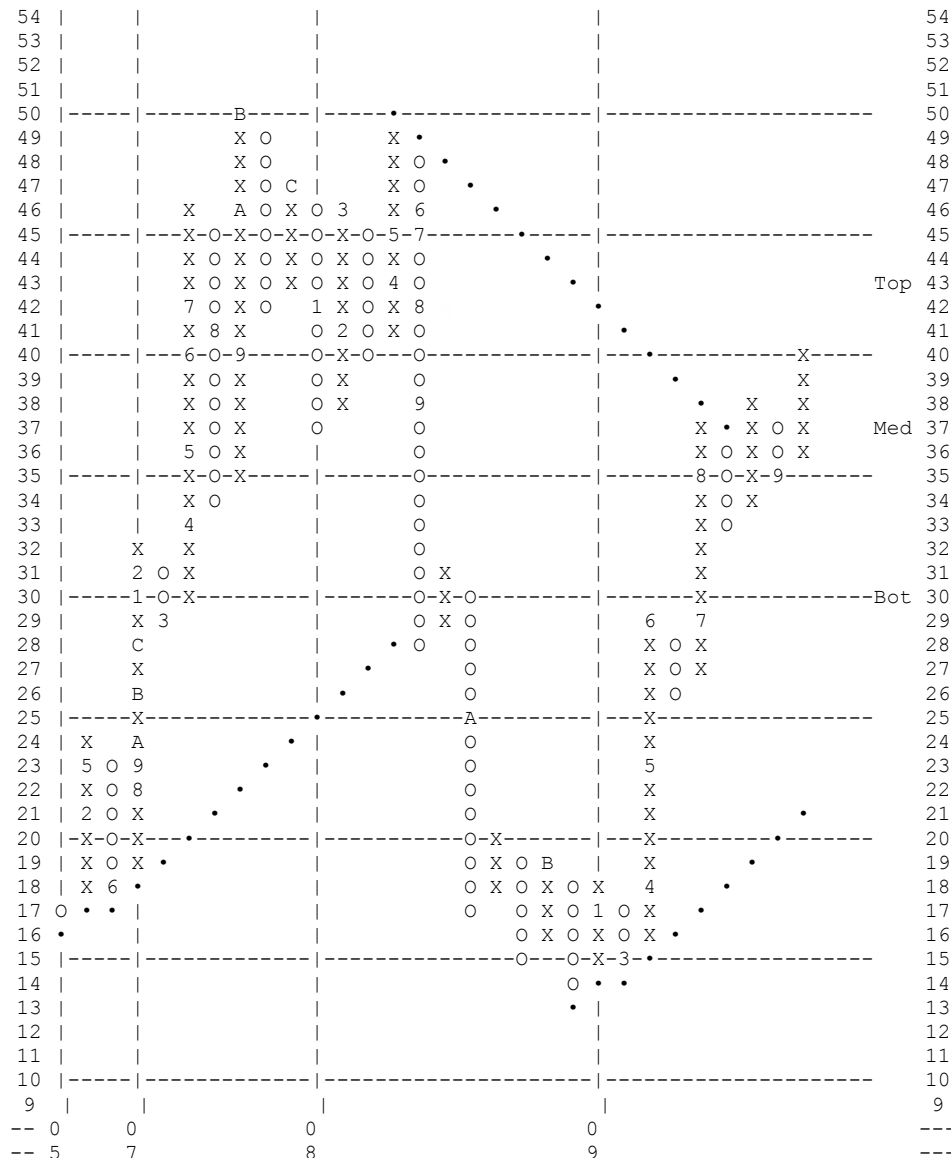


Chart has broken through its down trend line, given a double top buy signal and just gone back to a relative strength buy signal versus the US market. All in all this is just about as good a technical set-up as there is.