

Laurel Kenner and Victor Niederhoffer
Columnists

WORLDLY INVESTOR

January 2 —February 28, 2001



Nothing but Net in 2001

By Victor Niederhoffer and Laurel Kenner

Columnists

01/02/2001 10:22 AM

The market ended the year 2000 in beautifully symmetric opposition to the year before. In 1999, the Dow, Nasdaq and S&P 500 all ended at new highs, up 25%, 86% and 20%, respectively, while bonds lost 13%.

In 2000, the S&P 500 and Nasdaq both ended near their lows, down 10% and 39%, respectively. The Dow managed to lose only 6%. Bonds returned 20%.

What a difference a year makes. In 1999, Jeff Bezos was *Time* magazine's Person of the Year, sitting atop Amazon.com (AMZN), the biggest retailer by market value in the world. In 2000, his stock fell 80%.

The Daily Speculations Woman of the Year in 2000 is Hillary Clinton. So far as we know, she didn't trade cattle futures as she did in 1980 when she made a 10,000% return in six months by shorting beef despite her bullishness. Nevertheless, she received hearty endorsements this year from the Sultan of Speculation, George Soros, and the world's most famous investor, Warren Buffett.

Mr. Soros pulled the plug on his big Quantum hedge fund this year after taking a bath on tech stocks, while Mr. Buffett won't buy tech shares because he can't understand them. This was Mr. Buffett's year: his Berkshire Hathaway (BRK/A) shares hit a low on March 10, the precise day on which the Nasdaq Composite peaked, and have since risen 72%.

We can only hope that the pro value guidance of these great tennis and bridge players will ensure that the First Speculatrix's returns in 2000 did not pale in comparison with her previous foray into the markets.

Celebrating Diversity

There have been numerous excellent summaries of what the market did in 2000, and there is little useful that we can add, especially since history too often does not repeat itself. However, one aspect that we have not seen any comments about that provides a base of operations for the New Year is the extraordinary divergence in the performance of individual companies last year.

As the chronically bearish columnist at the leading financial weekly, Alan Abelson feels that 2001 will be even worse than the previous year.

Elsewhere, however, the weekly reported a Ned Davis study showing that even though the S&P 500 was down 10% last year the number of stocks rising was greater than the number falling. Mr. Davis used only stocks that existed in the S&P 500 as of the beginning of the year, avoiding the survival bias that too often plagues studies of this nature.

An even more striking example of divergence is found in the Nasdaq 100. Even though the index fell 37% in 2000, about a third of the members gained more than 10%. The reason this is significant, aside from the fact that it shows the breakdown of the standard Sharpe market model this year, is that instead of acting in concert with each other and being wafted about similarly with the market's tides, stocks

actually competed against each other. It was a market of stocks rather than a stock market.

Less Initial Reaction

The descriptive précis above is an example of the kind of armchair quarterbacking that makes market writers seem so much wiser than they actually are. It predicts nothing. Yet the description of what happened last year at least provides the latitude and longitude of where we were, giving a reference point for a reasonable prediction.

The stock market suffered a tremendous erosion of value last year. About \$1.8 trillion evaporated. What caused it?

In ecological terms, the carrying capacity of the market environment was too small for all the new initial public offerings that came down the pike in 1999 and early 2000.

The numbers of Internet IPOs tell the story best. In both 1997 and 1998, there were 40; in 1999, there were 400. In 2000, before the Internet IPO market essentially shut down in the second half, there were 100.

After a lag to digest and use the funds raised, the supply of Internet stocks reached a level that was much too high for the savings of the economy and the amount of revenue from advertising and consumer purchases to support.

Once supply became too great for demand, Internet stocks started falling. The decline spilled over into all other tech stocks. Finally, value stocks started competing with techs the same way that a fish that loses weight becomes prey for bigger fish in a tank. As the value stocks became fatter, their appetites increased, and this caused further declines in the Internet stocks that made them even more vulnerable to further predation. The spiral led down and down toward the very extinction of the species, a fate almost concluded by the end of 2000.

Feeling Meeker

The carnage in the Internet sector was almost beyond belief. Consider that of the 275 members of the Bloomberg US Internet Index, one-third fell 80% or wider in 2000. The rogues gallery includes such names as eToys (ETYS), down 99%; Internet Capital Group (ICGE), down 99%; Ask Jeeves (ASKJ), down 98%; Priceline.com (PCLN), down 97%; Webvan (WBVN), down 97% and Yahoo! (YHOO), down 86%.

Many of the stocks came highly recommended by the big brokerage houses. According to the *New York Times*, Mary Meeker, the famed Morgan Stanley Internet analyst, has "outperform" rating on 11 Internet stocks, and they are down an average of 83%. The situation is similar at many of the other firms.

According to Web Mergers, 130 Net companies closed their doors in 2000, many of which never even made it to the IPO market. Some of the noted dot-goners, according to Investors Business Daily, are Digital Entertainment Network, Fastv.com, 1stup.com, Furniture.com and Icast.com.

Former Dot-Commers in a Pickle

Some Internet executives at once high-flying firms, whose paper net worth was once in the tens of millions, found themselves out of work and in such terrible straits that they are now working in subordinate positions at Web sites specializing in pornography.

For example, Scott Bingham, formerly of Egreeting Network Inc., in October joined the marketing

department of Picklepoint.com, which, according to Investors Business Daily, "offers pornographic content on the Web for free. He saw nothing else available." How consistent this is with the desire of those in the middle of the pecking order to maintain their ability to grow, prosper and reproduce.

Where does this leave us? The same factors that caused the decline in Internet stocks can reverse. Such an outcome wouldn't surprise field ecologists accustomed to observing cyclical swings in such populations as lynx and lemmings.

Projections call for a 40% to 50% a year increase in Internet business and general use over the next five years. The carrying capacity is increasing, increasing the supply of available food, while the reduced density means there will be less competition for it.

There have been virtually no Internet IPOs in the last six months. On the contrary, one after another has been canceled.

A Broadband View of the Market

Under the circumstances, we can do nothing but recommend the Internet.

We presented a list of 10 ravaged Internet companies with recent insider buying in our column last week:

Ameritrade (AMTD)
Cobalt (CBLT)
Doubleclick (DCLK)
Etrade (EGRP)
Expedia (EXPE)
ITXC Corp. (ITXC)
Psinet (PSIX)
Razorfish (RAZF)
Rhythms Netconnections (RTHM)
24/7 Media (TFSM)

They are about unchanged since we recommended them. We repeat our recommendation, and add the following companies where insiders have stepped up to the plate and bought shares in the last two months:

Globix (GBIX)
Internet.com (INTM)
Lifeminders (LFMN)
MarchFirst (MRCH)
New ERA of Networks (NEON)
Safeguard Scientifics (SFE)
USinternetworking (USIX)
Walt Disney Internet Group (DIG)

We add them to our list, and intend to buy them to add to our holdings of the previous 10 we already own.

We make this our recommended portfolio for the year 2001. We advise that these be bought on full margin, with a reserve of about 25%. If a decline does occur, we would recommend a reduction of one-

third of the core position so as to always maintain a 25% cushion.

We will monitor our results and report on them in coming columns.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.05	Down 1	-6.2	3.4
S&P 500	0.94	Down 1	-10	0.6
Nasdaq	0.95	Down 1	-39	-6.9
Europe STOXX-50	1.07	Down 1	-3.9	-1.1
Dollar/euro	0.86	Up 1	-9.1	4.8
Nikkei	0.79	Down 3	-27	-5.3
Dollar/yen	0.92	Down 5	-16	-2.1
Gold	0.74	UnChg	-5.5	0.5
Oil	1.29	Up 1	50	-3.8
Bond Futures	1.19	Down 4	16	-0.1
2-Yr Note Futures	1.12	Up 1	2.2	0.3
Bund Futures	1.14	Up 1	5.3	0.03

*Victor Niederhoffer is a private speculator specializing in futures and options trading. His positions often change during the day based on shifting market expectations and volatilities. He is the author of the best-selling *The Education of a Speculator*, which is available [here](#).*

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Positions can change at any time.

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The Fed's Material Misreading of the Economy

By Victor Niederhoffer and Laurel Kenner

Columnists

01/03/2001 09:11 AM

Note to readers: In today's column, we present commentary by regular Daily Speculations contributor, Mark M. McNabb, a finance professor at Virginia Tech University.

The year started out with a reprise of 2000. Bonds had one of their best days ever, and the Nadsaq had one of its worst days.

The stock market vigilantes are in control at present, and they are trying to show Doc Greenspan the error of his political wavering about cutting rates in the face of all the negative news about the economy.

The 2.6% loss in S&P 500 futures was the worst beginning of the year ever, as well as the biggest post-holiday decline. The only hopeful sign is that the market likes to fake everyone out by doing exactly the opposite at the beginning of a period as it does at the end.

Here's the Beef

Happily, the Daily Spec computers are wildly bullish once again, after an expected down open today. Looking at the 13 most similar occasions to yesterday's action, the computers disgorge that in 12 of 13 occasions the market was substantially higher seven days later, with the average percentage change coming to a gain of some 3%, with about 1 1/2 times as much variability about that change. Highs in bonds in conjunction with big declines in stocks have always been the time to take out the canes.

Also bullish is the break in the S&P futures below the magic number of 1,300. Round numbers never hold in futures, and breaks such as this tend to awaken the market's desire for completion so that it moves to a consonant level.

As we start the New Year, we issue a bullish seven-day forecast for the market with a nice catalytic rise in the three days preceding the employment announcement this Friday. What a fine opportunity that would be for Doc Greenspan to save face and do something positive for the economy that seemingly has nothing to do with the stock market, which he has tried to bear down for many years.

Our 2001 portfolio of 19 Internet stocks with insider buying performed in line with the market, falling 4%. Under the circumstances, we need the respite of some incisive analysis of where the economy stands vis-à-vis the Fed and the stock market, and we have called on Mark McNabb, the barbecue-loving finance professor at Virginia Tech, for a special two-part analysis. Don't forget to read Part II, which will be posted later today.

Misreading Between the Lines

The consensus in the business press is that the Federal Open Market Committee has performed a remarkable job in the last decade with restraint and only reasoned intervention. A contrary view would be that the economy performed admirably during most of the recent decade and gave the Fed a holiday.

Looking back through the years, recall that the Fed induced a recession (at least two quarters of negative growth in real GDP) in 1991 when it maintained short-term rates of 7% when the CPI-urban index was

rapidly falling from 9% to under 2% -- before the Iraqi invasion and oil-price shock.

The Fed's decision-makers are only as good as the team of highly trained economic forecasters within the bank. In 1990, most dismissed the CPI numbers under 1% at the end of the summer as the temporary effect of market psychology (hysteria?) and then proceeded to dismiss three quarters of rapidly declining growth around 1% in nominal GDP as well as the near-40% tumble in market indexes. The Fed thought the economy was growing too fast, but in retrospect, the internal data it relied on was flawed, wrong, analyzed poorly, or ignored.

Reversal of Fed Policy

The Fed realized the error by December 1990, just weeks before the US-led invasion to reclaim Kuwait from Iraq and secure low-cost energy for the world. It then aggressively cut short-term rates 250 basis points over the next 12 months and 150 basis points more in the following six months. Short-term rates fell to 3% by summer of 1992 -- too late to avoid three quarters of flat to negative real GDP growth.

During this easing, the inflation index peaked for one month at 18% due to the energy price shock in December 1990, dropped below 5% two months after the start of the Persian Gulf War and then fell to under 4% in the next 12 months and to less than 3% 12 months later.

Prelude to a Bull

This steady decline would be contrary to basic economic thinking. The rate of inflation peaked in 1991 and has trended under 3% since 1994, even as the Fed was accommodating growth and not fighting inflation. The return of short-term interest rates to a level near their "natural level" of 5% in 1995 set the stage for a great bull market without inflation.

The forces that significantly diminished inflation included the restructuring of corporations (begun in the 1980s with the assistance of junk debt) that allowed the manufacturing sector to produce more by replacing labor with technology and capital, the globalization of our economy, and our nation's desire to compete without significant trade barriers, letting consumers and corporations seek the highest value for the least price. These factors suppressed the ability of domestic producers to raise prices.

Other factors included increased opportunities across the private economy that gave individuals, especially women and minorities, the desire to enter business at unprecedented levels in our history.

New technologies in communications and media, such as fiber-optics, networking, business-productivity software, Internet commerce and wireless, came in the aftermath of the Cold War as a large number of our most technically proficient minds moved out of defense-related industries and into the commercial world. The result of these forces was a long-awaited productivity boom that didn't receive notice from the Fed until 1999.

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A Front-Row Seat for the Rate Cut Heard 'Round the World

By Victor Niederhoffer and Laurel Kenner

Columnists

01/04/2001 12:00 AM

Part One of two. Be sure to check out Part Two featuring an excerpt of a late-night exchange between Vic and reader on the eve of the cut.

New York, Jan. 3. 9:30 a.m. S&P 500 futures start the game at 1296, not taking any chances. Nasdaq e-minis not too far from a two-year low at 2180, but will run like the wind if Greenspan hits one.

Rumors during the day that Greenspan is ready caused an early 1% rally. But strikeouts in the morning, stocks dug into lows.

12:15 p.m. Nasdaq futures at 2136.

1:00 p.m. Nasdaq futures rally to 2193. A murmur ripples through the crowd.

1:13 p.m. **THE FED LOWERS THE FED FUNDS RATE! THE FED LOWERS THE FED FUNDS RATE! THE FED LOWERS THE FED FUNDS RATE! ALAN GREENSPAN LOWERED THE FED FUNDS RATE FROM 6.5% TO 6%! THE FED LOWERED THE FED FUNDS RATE AND STOCKS ARE GOING CRAZY!**

Yes, ladies and gentlemen, after 533 consecutive days of tightening involving six consecutive increases in the federal funds rate, with the economy and markets in shambles, the old-hearted people at the Fed finally bowed to the stock market vigilantes and vox populi, thereby revealing the extent of weakness in the economy.

Fed Moves					
Start of Policy Shift	Starting Rate	# of Easings	# of Tightenings	# Days Before Next Change	S&P Cash Day Before Move
11/1/1978	9.50%		5	575	93.15
5/29/1980	13%	1		119	112.06
9/25/1980	10%		4	402	130.37
11/1/1981	14%	9		890	121.89
4/9/1984	8.50%		1	225	155.48
11/20/1984	9%	7		1357	271.15
8/8/1988	6%		3	861	326.82
12/17/1990	7%	7		1145	480.71
2/4/1994	3%		7	517	547.26
7/6/1995	6%	3		628	790.89
3/25/1997	5.25%		1	553	1048.69
9/29/1998	5.50%	3		274	1351.45

6/30/1999	4.75%		6	553	1283.27
1/3/2001	6.50%				
Average # Easings: 5					
Average # Tightenings: 4					
Average Time Before Change: 623 days (1.75 years)					

Without any ax to grind, the employment numbers to be released on Friday will doubtless convey a starkly weakening economy. No longer will there be a need to add hundreds of thousands of Internet jobs and the like to the numbers to make it seem like we're going through the roof.

Having seen these numbers in advance, Alan Greenspan finally thought it politically expedient to throw in the towel.

Stocks staged their biggest rally of all time. Nasdaq futures rose 25% from low to high, and closed up 17% on the day. The S&P's 60-point move was the second-greatest ever. About \$700 billion was added to the market's value, judging by the move in the Wilshire 5000 Index, which includes all U.S.-headquartered stocks.

In consistent moves this morning in Asia, South Korea rallied 7%, Taiwan rose 5% and Hong Kong gained 4%.

Regrettably, the market is so rational these days that in one minute it does what used to take five years to accomplish. It used to be that when the Fed signaled a change in direction of easings or tightenings, something it has done on 13 occasions in the past 22 years, bonds would go up strongly when they eased. But now in one minute, bonds anticipate not only that short-term rates will fall for the next two years, but that afterward the Fed will have to start easing again. And they go down instead of up. Yesterday, bonds had their worst decline in a year, falling more than 2 points.

The stock market, one second after the news was released to the public, rallied to the high of Nasdaq 2650 from 2170.

But then it was over.

Looking at the table of stock market performance during recent easings, we see no evidence that stocks go up at a higher rate than they do during tightenings. And after a big rally of this nature, the market has to spend a bit of time digesting.

Yes, the rate reduction heard around the world saved the day and the beginning of the year, just like Bobby Thomson's home run won the playoff for the Giants on Oct. 3, 1951 (a day that, according to our correspondents was not a Jewish high holiday). But the Giants went on to lose the World Series. Let us hope that the outcome will not be similar here due to the Machiavellian doings at the old-hearted Fed.

After yesterday's remarkable rally, we were relieved to hear that everybody knew it was coming. We're reluctant to join the chorus, mindful as we are of reader Bill Haynes' "Guaranteed to Happen" saying: "The market analysts who make a famously accurate prediction will be wrong on their next three predictions." Also, as Bipin C. Pathak writes, "One cannot analyze an irrational entity (such as the Fed) rationally."

But as we have had precious little opportunity lately to issue our patented self-congratulatory evaluations, perhaps our readers will excuse us for noting what we wrote yesterday morning: "Happily, the Daily Spec computers are wildly bullish once again, after an expected down open today.... Highs in bonds in conjunction with big declines in stocks have always been times to take out the canes."

We also said that it would be a fine opportunity for Doc Greenspan to "save face and do something positive for the economy that seemingly has nothing to do with the stock market, which he has tried to bear down for many years." And then we ran Virginia Tech professor Mark McNabb's compelling case for a Fed rate cut.

What can we possibly do for an encore? Our Daily Speculations computers are now neutral to slightly bearish.

Go to Part Two.

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Analyzing the Many Faces of the Market

By Victor Niederhoffer and Laurel Kenner

Columnists

01/05/2001 09:03 AM

(Editor's Note: Brett N. Steenbarger, Ph.D. is a licensed clinical psychologist and periodic guest contributor to the Daily Speculations column.)

Would the real stock market please stand up? Is it the NYSE Composite Index (\$NYA), which stands only about 5% from an all-time high, or is it the Nasdaq Composite Index (\$COMPQ), which practically needs to double to achieve the same feat -- even after the recent Fed-inspired rise?

Perhaps the real market is what is actively traded: the S&P 500 Index (\$SPX), which -- off roughly 15% from its peak -- is acting as a hybrid of old and new economies. Or maybe the market is better captured by an unweighted index such as the Value Line Index, which treats all issues equally.

These are more than semantic quibbles. If I use past data to infer possible future investment trends, my results will be highly dependent upon my data. If I looked at NYSE data during December, for example, I found hundreds of stocks making new annual highs at the same time that hundreds of stocks were making new annual lows, a truly bifurcated market.

Such was not the picture on the Nasdaq, where new lows soared to a multiyear extreme, far eclipsing new highs. Similarly, if I followed trendlines or chart patterns over that period, the two indices gave a very different read of the market, as did any multivariate modeling approach that employed past price change as a predictor.

Just as troublesome, a historical look quickly establishes that the indices themselves have undergone significant changes in recent years. With the addition of Microsoft (MSFT), Intel (INTC), and Hewlett Packard (HWP), the Dow Jones Industrial Average (\$INDU) increased its weighting in technology and reduced its exposure to basic industry. The S&P 500 Index, weighted by the capitalization of its issues, was dominated by oil stocks in the early 1980s and then by technology in early 2000. In an important sense, the market today is not the market of yesterday, even when using a single index for analysis.

Employ All Three Majors

How, then, can you analyze the market if there are multiple reference points, each of which is ever changing?

Carl Swenlin, creator of the technical analysis site decisionpoint.com and editor of the Decision Point advisory service, addresses this issue by cumulating data across all three major stock exchanges. He computes advance-decline, new high/low, price momentum, and other indicators for the entire universe of stocks traded, hoping to yield a better sense of perspective. "No one else has Total Market indicators," Swenlin told me recently, "and I thought it would provide a unique view that would be useful. The idea was to provide as broad a view of the market as possible."

Swenlin takes the concept a step further and derives indicators by aggregating price change, momentum, and other technical indicators from the components of each of the averages. "You can't generalize indicators like the NYSE or Nasdaq Advance-Dcline Lines-or any other indicator for that matter-to all market indices," he asserted. "Indicators should be derived from the individual stocks in the specific

index whenever possible. Indexes like the S&P are strongly influenced by a few mondo-cap stocks, and you can't see the internal strength or weakness of the index without creating indicators from the component stocks."

At the Decision Point site, Swenlin creates composite indicators from the components of the S&P 500, S&P 100, Dow, and Nasdaq 100 indices. "They are amazingly useful if you trade these indexes," Swenlin observed, "and give the individual indexes context in broader market analysis."

When we cumulate statistics for the New York Stock Exchange, Nasdaq, and American Stock Exchanges, an interesting picture emerges. For example, a weekly tally of advancing versus declining stocks, which largely eliminates the downward bias in the daily series, shows that we hit a dual peak in October 1987 and April 1998, followed by a precipitous fall that has lasted to the present. Indeed, the cumulative weekly advance-decline line for the total market is now below its prior cyclical trough of 1990, almost entirely due to the Nasdaq carnage.

Latest Bull Run Less Widespread

A less dramatic, but similar pattern can be seen in the cumulative weekly tally of stocks making new annual highs versus those making new lows. This line was in a steady uptrend from 1986 to June 1998 and has been declining ever since. This suggests that the entire bull thrust from October 1998 through March 2000 was far more selective than its predecessors, taking fewer stocks to new highs.

Finally, a cumulated 60-day NYSE Short-Term Trading Index (\$TRIN), constructed by aggregating volume and advance/decline statistics across the three exchanges, reveals that volume has been more concentrated in declining stocks in late 2000 than at any time since the traumatic decline of 1987. The relative strength of the NYSE Composite Index is masking the reality that we have witnessed selling of historic proportions during 2000.

These cumulated TRIN readings are especially instructive because they incorporate an important reality: the shift in trading volume toward the Nasdaq over the past several years. Any effort to analyze the market using NYSE statistics systematically underestimated market strength during the late 1990s and now is underestimating weakness since March, 2000.

What can we take away from this little exercise in cumulated data? If history offers any precedent, we are at the tail end of a major selling wave at a time of falling interest rates. This has yielded a nice market rally, which should continue. On the other hand, it appears that the great bull market dating back to 1982 reached its maximum point of momentum in early 1998 and now has become a much more selective affair. Indeed this scenario appears to be playing itself out since March, 2000, with defensive sectors (drugs, healthcare, utilities, energy) serving as a near mirror image to the technology stocks.

Indeed, in just the past few days we have seen a historic rally in the Nasdaq and an eye-opening decline in the Dow Utility (\$UTIL) stocks. Meanwhile, the NYSE Composite Average sits a bit more than midway through its recent price range. After a dramatic, broad advance followed by a massive tech collapse, the market seems determined to continue to throw the bulls and bears a continued curve ball of rotating, sideways, selective action.

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Time to Pick Up Those Struggling Net Stocks?

By Victor Niederhoffer and Laurel Kenner

Columnists

01/08/2001 09:12 AM

The incredibly inhospitable situation of the market today, particularly for tech and Internet stocks, brings to mind the primordial soup that preceded life on earth. Volcanic eruptions, violent thunderstorms, baleful ultraviolet light and a choking atmosphere of methane and ammonia permitted only the existence of simple organic compounds.

At some point, a spark of life led to progressively more complicated molecules and thence to ambitious amphibians that climbed out of the water to fill every available ecological niche.

A similar situation exists in the market today. The destruction of 2000 reduced many Internet and tech stocks to simple penny stocks struggling for life. Half of the companies in the Nasdaq 100 are down 30% in the last six months, and half the 202 companies in the Bloomberg U.S. Internet Index are down 70%. But a mysterious spark has put Web stocks in the news again.

Even the Mafia have Internet stocks on their palettes. In a series of conversations clandestinely taped by the FBI, the wise guys themselves want to cash in on Net riches, *The Daily News* reported over the weekend. "These (expletive) kids will teach you things you'd never believe," said Joseph "Tin Ear" Sclafani. Gangster Reynolds Maragni had plans for illegally selling Viagra without a prescription. "We're going to open a Web site, sell it right over the Internet. I'll make \$4-\$5 million a week. I got the kid to write the program," Maragni said from a luxurious Miami hotel suite right out of the HBO television series "Sopranos."

Of course, it's not all easy money, even for the Soprano crowd. There was much talk on the tapes about trying to scrape up cash for a girlfriend's breast implants, a wife throwing clothes on the lawn, and Maragni's pleas to his ex-wife to "Come and get your daughters, I can't take it no more. I'm 50 years old, I can't breathe."

Joining the wise guys recently are the old guys from the leading financial weekly. They're hot on Internet stocks now. You see, "lots of smart financiers are beginning to look around the battered Internet sector for bargains," the publication reported. Among those appealed to for inspiration are Bill Hambrecht, founder of Hambrecht & Quist, Alan Patricof and the Sultan of Speculation, George Soros himself.

A Net Stock Advocate

Winner of the Daily Speculations "Hunt with the Hounds, Run With the Hares" award is Greg Kyle, the author of a book entitled *The 100 Best Internet Stocks to Own* as well as a compilation for *Barron's* of a list of Internet stocks to avoid because they're rapidly burning through their cash. In the same issue, Kyle points to stamps.com and Fashionmall.com as two promising outfits selling for less than their cash on hand.

Kyle's book, published last year, is available at all the major airports, and contains the kind of wisdom and analysis that makes us nod with delight that people with his depth of experience exist and are actually willing to share their knowledge. It's filled with metrics like acquisition costs, customers, market expenses/sales, market value/visitor, market revenue/ page view and burn rate. We feel

incredible gratitude that Kyle shared his insights with the unwashed like us and that many of these 100 stocks are down more than 90% since the book was published last April.

Therein lies the opportunity. Insiders -- corporate officers and directors -- have been buying many of these stocks recently. This is a radical change from the situation of the last 12 months, where at least 95% of the transactions in Nasdaq 100 stocks were from the sell side.

If insiders are willing to invest more money in these companies, with the knowledge that any profits they make from trades closed within one year must be given back to the company, that would seem a favorable augury -- especially considering that the vast majority of the insiders must have a high preponderance of their wealth already tied up in these companies.

Our Own Net Advocacy

On Dec. 26, we issued a recommendation to buy Internet stocks. We pointed to ecological arguments related to the reduced density, increased carrying capacity and predator-prey relations that made us bullish, and we listed 11 stocks with recent insider buying that were on Kyle's 100 best list. They were:

Ameritrade (AMTD)
Cylink (CYLK)
Cobalt (CBLT)
Doubleclick (DCLK)
Etrade (EGRP)
Expedia (EXPE)
ITXC Corp. (ITXC)
Psinet (PSIX)
Razorfish (RAZF)
Rhythms Netconnections (RTHM)
24/7 Media (TFSM)

We suggested purchase on full margin for them. On average they are up 23% from year-end, which would make it 46% for the week with full margin.

Using the kind of reasoning that the media accorded a certain prominent female guru guest on the last "Wall Street Week," wherein credit is given for a call to reduce stock holdings to 65% from 70% last March and five subsequent predictions for a 10% rise in the market for 2000 are forgotten, we are tempted to add another 10% to our recommendations and call it a year. After all, many of our readers were probably away on vacation, and might not have had a chance to avail themselves of the privilege of buying these issues until the close on Tuesday, when the market was down 9%. Out of a natural modesty, we will eschew the temptation.

The situation involving insider buying of Internet stocks is not simple. Each line in the thousands reported by the usual sources contains a world of hopes, dreams and fears that would doubtless make a thrilling novel. Among the buys listed, one notes that the price paid is often 10% or less of the market price at the time. These were obviously options- or compensation-related.

On other occasions, massive filings to sell shares amount to hundreds of times the market value of the few sporadic buys. It's hard to know what to do with such situations, as often these filings to sell are merely efforts to register stocks held by officials on the chance they will need to sell or use them as collateral in the future, especially if the price should return to former stratospheric levels.

Other times, the amount of insider buying comes to only a few hundred dollars that may have been loaned by the company. In other instances, the insider might be trying to send a signal to armchair detectives like ourselves who study their trades with a gimlet eye, ready to spread the word that they're bullish, thereby helping push the stock up so the insider's massive pre-existing holdings will benefit.

We are not privy to the range of emotions and financial decision-making behind each trade, nor do we have the ability to interview each of the insiders, or their company chairs or spokesmen. Nor do we understand the fundamentals of each stock nearly as well as Mr. Kyle or his ersatz imitators. But we have done our best to ferret out the wheat from the chaff, and are happy to report in that regard that we can add four recommendations from Kyle's 100 Best list: MyPoints.com (MYPT), Prodigy Communications (PRGY), TD Waterhouse (TWE) and Wit Capital (WITC).

At the same time, we will take the liberty of deleting Expedia (EXPE) from our list because the Shadow's eyes have detected insider selling. In the interest of keeping the portfolio manageable, we also are deleting Globix (GBIX), internet.com (INTM), LifeMinders (LFMN), marchFirst (MRCH), New Era of Networks (NEON), Safeguard Scientifics (SFE), and Usinternetworking (USIX), which we recommended on Jan. 2.

Here is the current 15-stock portfolio.

Ameritrade (AMTD)
 Cylink (CYLK)
 Cobalt (CBLT)
 Doubleclick (DCLK)
 Etrade (EGRP)
 Expedia (EXPE)
 ITXC Corp. (ITXC)
 MyPoints.com (MYPT)
 Prodigy Communications (PRGY)
 Psinet (PSIX)
 Razorfish (RAZF)
 Rhythms Netconnections (RTHM)
 TD Waterhouse (TWE)
 24/7 Media (TFSM)
 Wit Capital Group (WITC)

As indicated, we did buy a few thousand shares of each of the companies on the original list, and we intend to buy the four new ones recommended today once our readers have had a chance at buying to join us, selling to fade us or watching to participate with us vicariously on a level playing field.

The reasoning here is not restricted to Internet stocks, but would apply to all such beaten-down groups in tech where the IPO pipelines of supply have depleted lately and the carrying capacity of the market is increasing drastically. Expect to see hundreds of templates for buying such stocks sluice through the media in the coming weeks.

Like the guest on "Wall Street Week," we are highly, and in our case, wildly, bullish. The Daily Spec computers are always most sanguine when stocks and interest rates both are down. The primordial soup of the market appears ripe for a profusion of life and growth.

Speculator's Scorecard			
Days Up/Days	# Days in Latest	% Change	% Change

	Down Ratio (YTD)	Streak (YTD)	YTD	(last 10 days)
Dow	1.03	Down 2	-7.3	0.2
S&P 500	0.93	Down 2	-12	-0.6
Nasdaq	0.94	Down 2	-41	-4.3
Europe STOXX-50	1.05	Down 1	-5.0	0.9
Dollar/euro	0.88	Up 2	-7.5	3.5
Nikkei	0.80	Up 1	-27	3.3
Dollar/yen	0.92	Down 2	-18	-3.6
Gold	0.74	Up 1	-6.9	-2.1
Oil	1.30	Down 1	57	6.8
Bond Futures	1.21	Up 2	17	0.00
2-Yr Note Futures	1.14	Up 2	3.1	0.7
Bund Futures	1.16	Up 1	6.3	1.1

*Victor Niederhoffer is a private speculator specializing in futures and options trading. His positions often change during the day based on shifting market expectations and volatilities. He is the author of the best-selling *The Education of a Speculator*, which is available [here](#).*

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Picking a Software Winner with Value Line's Help

By Victor Niederhoffer and Laurel Kenner

Columnists

01/09/2001 09:42 AM

Only a Beethoven or a Jules Verne could have delivered a script for the end of the world that rivaled the one staged by the Mistress of Markets yesterday.

After a sharp decline from a small up open, the market plunged early in the day. A brief rally fizzled, whereupon stocks fell into a gut-wrenching decline with lightning storms from General Electric (GE), volcanic eruptions from the building industry, and crashing meteorites hurled from entertainment industry constellations like Disney (DIS) and Viacom (VIA).

By 3 p.m., stocks managed to drop below the lows that preceded last Wednesday's Federal Reserve rate cut. As Henry Worthington Fowler described it in his 1870 book, *Ten Years in Wall Street*:

An appalling stillness like that which precedes a tornado followed.... A crowd of ruined operators reeled and surged up the rostrum, half-crazed by their losses and stupefied or maddened by drink, while the whole room rang with yells and curses.

Music is the universal language, and the despair of 3 p.m. yesterday was captured by Beethoven in the development section of the Fifth Symphony's first movement. A series of chords exchanged by the winds in high registers and the horns down low becomes both softer and progressively more agitated, suggesting a person gasping for breath, until at last the music trails off into pianissimo pulses like a dying patient's heartbeats.

But then, out of the clear blue sky, some big orders came in. And in one beautiful hour, Nasdaq futures rallied from 2175 to 2325. A favorable sales report from Amazon.com after the close sent the contract to 2362, up 8% from its end-of-world level.

James Lackey, a day trader from Florida and a past winner of our contest for market proverbs, captured the turnaround.

"All of a sudden huge buyers came in, in Amgen (AMGN) and Biogen (BGEN). Then the Nasdaq rallied around 25 points off the low. The Nasdaq highflyers, like Juniper (JNPR), Ciena (CIEN), Check Point Software (CHKP) and Broadcom (BRCM), actually went up while the Dow was making new lows. That is the first time since August that we have seen tech relative strength like this.

I knew that I should be long. I was scared. I waited for stocks to go positive. When stocks go positive after a big down day there is always a short squeeze, a high probability trade. I was long Juniper, Ciena, PMC-Sierra (PMCS), Broadcom and anything that went positive on the day."

Mr. Lackey concludes: *"Today was a bottom. I promise."*

The Daily Speculations Duo is dedicated to providing our readers with a meal for a lifetime, not just to entertainment even when we can quote a Beethoven or Fowler score. We have checked through the last six years of data to see if it is indeed true that when stocks go from minus to plus on the day after a big

down day there is a tendency for continued rallies. Regrettably, we could only find 10 observations that fit the bill, and six of these were down by the close that day as well as one day later. Thus, the intuition of Mr. Lackey worked for him yesterday but might not be appropriate for all seasons.

We were privileged to spend some time over the weekend with Sam Eisenstadt, who for 56 years has been the linchpin of Value Line's record as the world's greatest stock picker. At a chronological age that makes Doc Greenspan look like a kid, a creative age with more curiosity than most kids and a physical age where his gait is much livelier than that of a certain squash player-turned-columnist, Sam is an inspiring example of how to stay young-hearted as the century mark approaches. With Sam as research chairman, Value Line has managed to stay quite lively, and has not hesitated to add such new industries as e-commerce to the 3,500-plus companies it covers.

As most investors know, stocks ranked 1 or 2 for timeliness by Value Line have managed over the past 35 years to beat the market by 10 or 15 percentage points a year. Unfortunately, the timeliness rankings are highly correlated with the last 12 months' performance. Most Internet stocks are now ranked 4 or 5 because they fell so sharply during that period.

However, we are happy to report that a software company called Inprise (INPR), the former Boland International, has received a 2 ranking from Value Line. It also has a few characteristics that make it attractive to us: It has insider buying, it's down 58% from its 12-month high, and it's in an industry with high growth forecasts. We hereby add it to our recommended list.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.02	Down 3	-7.6	-0.1
S&P 500	0.92	Down 3	-12	-0.8
Nasdaq	0.93	Down 3	-41	-4.8
Europe STOXX-50	1.05	Down 2	-5.7	0.2
Dollar/euro	0.87	Down 1	-8.2	2.8
Nikkei	Mkt Closed	Mkt Closed	Mkt Closed	Mkt Closed
Dollar/yen	0.93	Up 1	-17	-2.9
Gold	0.75	Up 2	-6.8	-2.0
Oil	1.29	Down 2	53	4.4
Bond Futures	1.21	UnChg	17	0.00
2-Yr Note Futures	1.15	Up 3	3.3	0.8
Bund Futures	1.15	Down 1	6.3	1.0

*Victor Niederhoffer is a private speculator specializing in futures and options trading. His positions often change during the day based on shifting market expectations and volatilities. He is the author of the best-selling *The Education of a Speculator*, which is available [here](#).*

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Markets Poised for an Opposite Move

By Victor Niederhoffer and Laurel Kenner

Columnists

01/10/2001 02:50 PM

The markets are poised to do exactly the opposite of what they did previously both in the short run and the long run.

Yesterday, there was a nice up-opening, a rally to midday, and then an end-of-day decline on fear about earnings, to end exactly unchanged on the day. Continuing the theme, the markets opened sharply down today, with Nasdaq futures quickly moving to limit down, and then a similar sharp rally to up 1% on the day in the S&P 500 and up 3% on the day in Nasdaq.

Today's up-move to noon started out similarly to yesterday's rally to noon. But then an announcement by Cisco Systems (CSCO) at 12:30 p.m. that yes, the company would be affected by the business slowdown, dropped the market a quick 1% to down on the day as we write.

It looks so similar to yesterday. So our guess is that instead of weakness to the next open there will be strength.

Warm Winds From Afar

A key feature of last year's move was the drastic declines of certain Asian and South American countries. In retrospect, many of these countries forewarned the fall in US stocks, especially Nasdaq.

But guess what? Many of these countries are already registering sharp advances this year. Some representative countries with their declines last year and this year to date appear below:

Country	Last Year	Year to date
Argentina	-10%	19%
Brazil	-10%	12%
Mexico	-22%	2%
Singapore	-20%	2%
South Korea	-43%	14%
Taiwan	-46%	15%
Thailand	-46%	9%

The wind generally moves from high-pressure areas to low-pressure areas. We hypothesize that this year the high-pressure areas are in Asia and South America. These countries traditionally are more volatile. As such, like California in the old days, they are likely to be at the cusp when changes in taste occur.

In retrospect, the crash of October 1997 and the weakness of the US markets at the end of last year were forecasted by the 50% declines in many hot areas. As sage onlookers see the money to be made in these countries, they will spread the word that there's ebullience out there. And the information could be transmitted to waiting bulls the same way news about a new hot industry is disseminated through the usual channels.

Duncan Coker, a philosopher from the volatile climes of Aspen, Colo., who before becoming a stock trader served an apprenticeship in marketing containers, thereby giving him exposure to a wide birth of American industry, adds the following philosophical thought from Shakespeare:

"Perhaps," he writes, "it is the winds themselves that link markets."

The winds did sing it to me: and the thunder, That deep and dreadful organ-pipe, pronounced the name of Prosper! (The Tempest)

The book *Wall Street Picks 2001*, published by Dearborn, has expert recommendations and analyses on 50 hot stocks for 2001. One of them, Techne Corp. (TECH) recommended as a bonus pick by Sally Anderson of Kopp Investment Advisers appears beautiful indeed. It produces biological products used in research and diagnostics, a field that should benefit from the research necessary to replace all the drugs coming into the pipeline in future years.

It's our kind of stock, since it's down some 60% from its 12-month high. It also has the rare virtue of being ranked 1 for technical performance and 2 for timeliness by Value Line. Added to that, its last insider trade, admittedly a small one and occurring in September, was a buy. All things considered, that's five pluses for it in our book. We intend to buy the stock and add it to our recommended list.

The updated list follows:

Ameritrade (AMTD)
Cobalt (CBLT)
Cylink (CYLK)
DoubleClick (DCLK)
Walt Disney Internet Group (DIG)
E*Trade (EGRP)
Inprise (INPR)
ITXC (ITXC)
MyPoint.com (MYPT)
Prodigy (PRGY)
Psinet (PSIX)
Razorfish (RAZF)
Rhythms Netconnections (RTHM)
Techne (TECH)
TFSM (24/7 Media)
TD Waterhouse (TWE)
Wit Capital (WITC)

As of the recommendation dates, the portfolio is up 18% -- or 36% if bought on full-margin, as we advised.

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Medicated Bulls Recharging

By Victor Niederhoffer and Laurel Kenner

Columnists

01/11/2001 10:37 AM

The Wall Street canyons that house the NYSE and the virtual electronic Nasdaq corridors that culminate in the giant neon readout in Times Square witnessed a terrific battle yesterday between the bearish forces of ephemeral profit warnings and the bullish forces of growth.

The victory yesterday was in doubt until the last hour, when a surge in computer and Internet stocks carried the Nasdaq up 8% from its lows, with the other markets registering strong but attenuated gains.

Particularly impressive was a 5% rise in the Internet indexes that wafted our own 2001 Net portfolio to up 27% from the dates we recommended the stocks in the Dec. 26 through Jan. 8 period.

Thirsty S&P Slaked

Symptomatic of the renewed vigor of the bulls, Wednesday's close was the first occasion since Nov. 6 when the S&P futures managed to span three consecutive days without a decline. Such a two-month period without a drink appears to be the longest dry period in the last six years.

Like the policemen in the Gilbert & Sullivan opera, *The Pirates of Penzance*, the market has "with cat-like tread" been stealing up on the enemy. After hitting 1,315 and falling to 1,310 five times in the last two days, the S&P 500 surged to close at 1,327. (All results reported are for the forward-looking futures rather than the lagging index.)

Yesterday's finish leaves the futures just 8 points below the magical level of unchanged for the year, which many use as a bellwether for what's going to happen the rest of the year.

The Nasdaq, for its part, had a typical day. It fell quickly to 2,261, limit down, then rallied to close at 2,441. It's now within 90 points of the high it achieved after the Fed cut interest rates on Jan. 3, and up 2.8% for the year. Compared with the 1.7% year-to-date decline in the Dow industrials, that's a nice divergence of about 5 percentage points for growth vs. value.

Rallying Despite Warnings

The market's surge in the face of a sales warning from Cisco Systems (CSCO), one of the great principalities of the growth kingdom and the second-most highly valued company in the Nasdaq 100, has us thinking about how epidemics end.

Some contagions, in disease and in markets, are stopped by a magic bullet. New vaccines virtually ended polio and tuberculosis; penicillin made it possible to avoid the long degeneration of syphilis; Federal Reserve rate cuts resuscitated the global market after the Russians defaulted in 1998.

In other instances, the deadly disease loses its power over the population when the body's immune system, an amazing 24/7 laboratory of feverish experimentation, comes up with its own weapon. In 17th century England, for example, the plague mysteriously began losing its killing power just when it looked as though none would escape.

The plague took the lives of 100,000 Londoners in the single terrible year of 1665, and continued well into 1666. But as Daniel Defoe writes in *A Journal of the Plague Year*, an account of the epidemic published in 1722:

"The plague being come to its crisis, its fury began to assuage. People recovered faster and more in number than they used to; and indeed, if it had not been so, what had been the condition of London? It was wonderful; even the physicians themselves were surprised at it. Wherever they visited they found their patients better in a few days, everybody was recovering."

Cisco CEO John Chambers said the company would be hurt by the economy's slowdown, and he wished the Fed had cut rates last month when orders had started suddenly declining. His remark took the Nasdaq down a quick 125 points in the hour after noon. But the patient quickly recovered, closing at a new high for the day.

As Vic's former partner Steve Wisdom observed: "As Nasdaq fell at first, a few companies 'warned.' Then after a while it seemed that there were several warnings every day as the 'epidemic' peaked. Now it seems they've developed 'immunity' and the warnings don't hit the stocks as much."

It Ain't Just Warnings

Regrettably, there are a couple of other clouds on the sky beyond earnings warnings. Bonds dropped almost a full point to \$110.86 yesterday, a half-point above their lowest level in a month. Such minimums in bonds in conjunction with rallies in stocks always raise the warning needles of the analog computers the Specs use to supplement the digital numbers issuing forth from their bank of Gateways.

Also somewhat discouraging has been the decline in the VIX, a measure of the volatility of the stock market indexes traded on the Chicago Board Options Exchange, from 34.77 on Monday to a gnat's eyelash above 30. Levels above 30 are traditionally very bullish, as they show a level of fear that is inconsistent with the market's normal long-term variability, which has averaged some 20% a year for the last 10 years.

As to whether the population of stocks is sufficiently immunized or not, the crystal balls are clouded. The situation is particularly difficult before any three-day weekend, and this one occurs after the release of the always volatile -- but usually bullish -- Producer Price Index.

One thing for sure. The market will fluctuate in a fashion designed to separate the weak from their chips to the benefit of the strong.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.02	Up 1	-7.8	-1.8
S&P 500	0.93	Up 2	-11	-1.2
Nasdaq	0.95	Up 2	-38	-0.6
Europe STOXX-50	1.03	Down 4	-7.9	-3.6
Dollar/euro	0.86	Down 3	-9.3	0.8
Nikkei	0.78	Down 2	-29	-3.9
Dollar/yen	0.93	Up 1	-18	-2.1
Gold	0.74	Down 2	-8.1	-3.8
Oil	1.31	Up 2	66	11

Bond Futures	1.19	Down 2	15	-0.3
2-Yr Note Futures	1.13	Down 2	2.8	0.5
Bund Futures	1.13	Down 3	5.7	0.6

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Market Psychology Questionnaire

By Victor Niederhoffer and Laurel Kenner
Columnists

01/12/2001 09:14 AM

Editor's Note: Brett N. Steenbarger, Ph.D. is a licensed clinical psychologist and periodic guest contributor to the Daily Speculations column.

Many traders are worried that their psychological issues will sabotage their forays into the market. Their concerns borrow directly from Freud: emotional problems, they believe, are the result of past, unresolved conflicts.

The late Abraham Maslow, however, proposed a radical alternative. Emotional concerns stem, not from the presence of conflicts, but from the absence of meaningful life challenges.

Perhaps a questionnaire can best illustrate the idea. Below are 24 emotional states. Before moving on in the article, use the scale below to indicate how often you have experienced each state in the past two weeks of trading. Focus specifically on how you have felt while trading the markets.

1 = almost never 2 = rarely 3 = sometimes 4 = often 5 = almost always

1) Happy _____	9) Joyful _____	17) Cheery _____
2) Pleased _____	10) Content _____	18) Satisfied _____
3) Energetic _____	11) Enthusiastic _____	19) Lively _____
4) Affectionate _____	12) Caring _____	20) Warm _____
5) Sad _____	13) Melancholy _____	21) Depressed _____
6) Nervous _____	14) Stressed _____	22) Edgy _____
7) Frustrated _____	15) Angry _____	23) Irritated _____
8) Regretful _____	16) Guilty _____	24) Self Doubting _____

To score the questionnaire, add your responses to the three items in each row. The first four rows, in order, represent Happiness, Contentment, Energy Level and Affection. These are four basic dimensions of psychological well-being.

The last four rows represent Depression, Anxiety, Anger and Guilt. These are the basic dimensions of psychological distress.

When we compare our total scores for the first four rows with our scores for the last four rows, we have an index of psychological balance. This offers a snapshot of the degree to which our sources of distress are balanced by sources of well-being.

Interfering Distress Signal

How balanced are you during your trading? If your distress scores equals or exceeds your well-being score, you're probably trading with a fair degree of emotional interference.

As it turns out, Maslow was correct. Stress-related illnesses and long-term emotional problems are as much a function of an absence of well-being as a surplus of distress. Research suggests that people who have high levels of positive *and* negative emotional experience are actually less likely to suffer from adjustment problems than those who have low stress, but also low well-being.

We can endure much pain when it is balanced with joy, contentment, vigor and affection. Without well-being, however, we lapse into negativity and neurosis.

Maslow, however, went further. In his paper "Lessons from the Peak Experience," he stated:

"When I started to explore the psychology of health, I picked out the finest, healthiest people, the best specimens of mankind I could find, and studied them to see what they were like. They were very different, in some ways startlingly different from the average...I found that these individuals tended to report having had something like mystic experiences, moments of great awe, moments of the most intense happiness, or even rapture, ecstasy, or bliss. These moments were of pure, positive happiness, when all doubts, all fears, all inhibitions, all tensions, all weaknesses, were left behind."

Psychological health, Maslow found, is not the mere absence of illness. It is the presence of the capacity for peak experiences: the ability to lose oneself in experiences of well-being.

"What is happiness?" Nietzsche reflected. "The feeling that power increases -- that resistance is being overcome." Peak experiences, the modern existentialist Colin Wilson recognized "are in direct proportion to the intensity of the will."

Work Flowing

To a certain point, effortful, goal-oriented activity is tiring. If we can extend ourselves beyond the initial point of fatigue, however, an interesting phenomenon arises. We reach a point of emotional second wind, a point described by the psychologist Csikszentmihalyi as "flow." We're in the zone; we lose track of time. We're no longer working; the work is flowing through us.

A common theme emerges from the books written by great traders. Each one emphasizes extensive homework before the trade: keeping a journal, making a plan, analyzing winning and losing trades, immersing yourself in the markets. Such extensive practice and preparation has a psychological function, as well as an educational one. It trains the mind for flow. It cultivates the capacity for peak experience by training the speculator to work beyond the point of fatigue, to the point of emotional second wind.

Great traders are distinguished by great efforts. They don't make great trades. The really great trades flow through them.

And why do other traders fail miserably? Is it because of their repressed conflicts and desires for self-destruction? Wilson suggests not, and instead offers a different explanation: "Crises or difficulties can often produce a sense of meaning when more pleasant stimuli have failed."

Seeking New Highs

If traders cannot generate peak experiences through creative work effort, they may seek an alternate route. By overtrading and assuming undue risk, they attempt to counterfeit authentic well-being. Unwilling to live without peak experiences, they -- like the addict -- engage in an ever-spiraling search for emotional highs.

"Each has his own happiness in his hands," Goethe wrote. "As the artist handles the rude clay, he seeks to reshape it into a figure; yet it is the same with this art as with all others: only the capacity for it is innate; the art itself must be learned and painstakingly practiced."

Whether in squash, trading, or scientific pursuit, painstaking practice is the mother of well-being, the fountainhead of peak experience, and the source of all greatness. Buried deep within the literature of psychology is a gymnasium for the mind, a treasure-trove of techniques for cultivating will and the capacity for directed effort. The future belongs to the body-builders of mind.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.03	Up 2	-7.7	-2.4
S&P 500	0.94	Up 3	-9.7	-0.6
Nasdaq	0.96	Up 3	-35	3.2
Europe STOXX-50	1.04	Up 1	-6.4	-2.9
Dollar/euro	0.87	Up 1	-8.1	2.3
Nikkei	0.78	Down 3	-30	-5.3
Dollar/yen	0.92	Down 1	-19	-3.1
Gold	0.73	Down 3	-8.2	-2.9
Oil	1.30	Down 1	65	14
Bond Futures	1.18	Down 3	15	-1.0
2-Yr Note Futures	1.13	UnChg	2.8	0.6
Bund Futures	1.12	Down 4	5.6	0.7

Brett N. Steenbarger, Ph.D. is a licensed clinical psychologist and Associate Professor of Psychiatry and Behavioral Sciences at the SUNY Upstate Medical University in Syracuse, N.Y. His primary research interest is multivariate behavioral modeling of the stock market. He welcomes comments and questions at steenbab@aol.com.

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The Speculators' Net Portfolio Surges

By Victor Niederhoffer and Laurel Kenner

Columnists

01/16/2001 12:00 AM

What are the reasons behind the 142% gain in our portfolio of 15 Internet stocks in the first two weeks of the year 2001?

Since we recommended these stocks three times starting Dec. 26, the annualized returns are quite good.

Two keys:

- Low-priced, beaten-down small-cap stocks in general did well. Stocks in the S&P SmallCap 600 Index that closed below \$5 at year-end are up an average of 26% in 2001.
- Internet indexes have done well. The Inter@ctive Week Internet Index (\$IIX) is up 7% year to date.

And what is the backdrop that brought these stocks down so far and prepared them for such a spectacular rise? The four key reasons are:

- 1) **Embarrassment.** Investment managers who held beaten-down Internet stocks didn't want to be seen with them at the end of 2000, so they sold them wholesale before the end of the year.
- 2) **Tax selling.** Since these stocks declined so much last year, investors sold them before the end of the year to realize losses for tax purposes.
- 3) **Low expectations.** Investors gave up on them. And anything that was good since year-end has led to a positive revision of expectations.
- 4) **Insider Buying.** Insiders have been net sellers of almost all Nasdaq 100 stocks for at least two years. We found a group that insiders were willing to throw good money at even after the terrible decline. They must have been true believers, and their hopes were doubtless fortified in many cases by knowledge that a buyer lurked in the wings who was ready, willing and able to offer them a lot more than they paid.

While each factor doubtless contributed to the success, the ecological theory we originally presented overrides all of them. These were all stocks in an industry with great carrying capacity, and they had no opinion leaders or mavens to communicate their virtues to other people. Their predators had become numerous, fat and unprepared for the resurgence of the population. The IPO pipeline of competitors had been empty for six months, thereby taking the edge off the battle for resources.

Thus, when the Internet stocks started rising at the beginning of the year, it was open sesame. The food for them was there. Their enemies were off guard. And the competitors were too few in number to stand up to them.

The question, however, is will they continue to rise?

Looking Back, Looking Forward

To see the future, it is helpful to look at the past. The most striking thing about 2001 to date has been the divergence of bonds and stocks. Bonds are down 2.3%, and the Nasdaq 100 is up 7%. It is rare for the two measures to be out of sync. In fact, during the last 20 years, the correlation between the change of the S&P 500 and bond futures during the same year has been 0.6%.

Also, the dollar is down some 10% against the euro over the past month. This indicates capitulation by the Europeans -- the same kind of capitulation that the mutual funds and end-of-worlders were talking about at year-end. How could the New Year bring anything but a change in grounding?

The largest divergence in returns occurred last year. Not only was one market up and the other down, a very rare event that occurred only once in the previous 20 years, but the difference in performance of 20 percentage points was the largest by far in that period.

What does it foretell for the future when such a divergence occurs? The Daily Spec computers have now been taken out of the woodshed and Fisherman Vic's qualitative incursions are but a distant bad dream. As we write, the computers are humming incessantly with billions of calculations.

The conclusion: The recent decline in bonds in conjunction with the rise in stocks, one of the most startling divergences of the last six years, has not happened enough to yield a non-random prediction. The same is true for the recent decline in the Chicago Board of Trade's Volatility Index (\$VIX) from 34% to 27%. For sure, however, these two moves are not overly healthy.

Bonds Are Breaking

We note, for example, that after four consecutive declines of at least half a point in price, bonds are down wider than 2 1/2 points on the week. Such a freefall is very rare, happening perhaps once a year over the last six years as of the end of a week. And yet on the eight most similar occasions to the present, the expectations for stocks were down 1% two or three days later, with a subsequent rise of about twice that level.

In short, there is nothing bullish or bearish for stocks at this time. While the Spec computers are not wildly optimistic, as they were in the last two weeks, they are not pessimistic either. The outcome, as usual, will be determined by outside factors, and one of them will be the Federal Open Market Committee meeting on Jan. 31.

Under the circumstances, we will note that January is generally the best month of the year for the S&P 500. At present, despite all the bullishness, it is down 0.1%. Not a stellar performance, considering that mavens are now beginning to talk up stocks amid the gloom, as well as the possibility for tax reductions and Social Security privatizations under President Bush.

Stock Talk!

After a month-long hiatus, we revived Stock Talk! in honor of the 17th annual national Martin Luther King Day holiday. The 455th session was held at the Congress of Racial Equality's celebration of the holiday. The CORE award winners, B.B. King and Charlton Heston, stressed the importance of reaching out to all communities to create a universal feeling of brotherhood among all races.

The same applies to all stocks. The rise in the Internet Index is gradually spreading to other industries -- telecom, semiconductor and computer software. Almost every good stock in these industries that was beaten down in 2000, with reasonably good forecasted earnings for 2001 and a modicum of insider buying, is up substantially from year-end.

We fortuitously have participated in this bounce with our recommended stocks. And in the spirit of universal brotherhood that the more than 1,000 celebrants at CORE's King Day dinner, we will reach out to other industries to find three stocks that might be wafted upward by the dream of equal opportunity for rises in all stocks, a dream that we believe would have been as dear to Dr. King's heart as his favorite opera music, which was performed at the dinner and reception.

To remedy our failings of last year, we are going to stay much more closely in touch with our recommendations. So far, we have recommended 15 Internet stocks and two non-Internet stocks. The following table shows the performance of our Internet stocks to date:

Company	YTD % Change
Ameritrade (AMTD)	39.29
Cobalt Group (CBLT)	183.33
Cylink (CYLK)	33.33
DoubleClick (DCLK)	34.09
Disney (Walt) Internet Group (DIG)	30.88
E*Trade Group (EGRP)	61.86
ITXC (ITXC)	27.03
MyPoints.com (MYPT)	45.16
Prodigy Communications (PRGY)	13
Psinet (PSIX)	286.93
Razorfish (RAZF)	30.77
Rhythms Netconnections (RTHM)	83.33
24/7 Media (TFSM)	158.85
TD Waterhouse (TWE)	4.7
Wit Capital Group (WITC)	37.29

The two non-Internet stocks -- Inprise (INPR) and Techne (TECH) are up 15% and 12%, respectively. We hereby put them in what we're calling our Other Worldly portfolio. The Internet stocks have been in our portfolio for an average of two weeks, while we chose Inprise last Tuesday and Wednesday.

In looking for additional non-Internet picks, we found stock after stock that is up spectacularly. Many of the obvious plays in similar industry ecologies, as semiconductors already have been lofted to returns that make us queasy.

Nevertheless, some companies in industries that are still out of favor have not yet reached the firmament, at least in our opinion.

We ran a screen of 100 stocks that Value Line predicts will rise most over the next three to five years that are also rated middling to good at present in "timeliness," the firm's 1-to-5 ranking system. We came up with three that have not already hit the roof this year. We add them to our recommended Other Worldly portfolio:

CommScope (CTV)
-1999 Close: 40 5/16

-2000 Close: 16 9/16
 -High: 50 1/8
 -Price: 21 1/16

PetSmart (PETM)
 -1999 Close: 5 3/4
 -2000 Close: 2 7/8
 -High: 5 3/4
 -Price: 3 7/32

Westell Technologies (WSTL)
 -1999 Close: 10 3/4
 -2000 Close: 3 1/16
 -High: 40 3/4
 -Price: 3 29/32

Togetherness in Privatization

A key part of Dr. King's dream was a time when people of all races, religions, classes and stations in life put aside their differences and joined in the spirit of togetherness. A very fit Mayor Giuliani, who left a private performance at the Met to attend, emphasized his desire to reach out in his own celebratory remarks at the dinner.

In this context, the results of a recent Zogby poll were presented at the dinner, showing that almost 40% of Gore voters favor the partial private investment of Social Security taxes. Such sentiment must be considered highly bullish for the market.

The average Chilean worker is now retiring with greater wealth than his American counterparts. And there is now almost 100% support in Chile for the privatization. What a boon to the US stock market and, even more important, to the attitude of Americans toward business, that would be here.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.02	Down 1	-8.5	-2.4
S&P 500	0.93	Down 1	-10	-0.1
Nasdaq	0.95	Down 1	-35	6.3
Europe STOXX-50	1.05	Up 2	-5.7	-1.8
Dollar/euro	0.86	Down 1	-8.2	1.0
Nikkei	0.78	UnChg	-30	-4.2
Dollar/yen	0.91	Down 2	-19	-3.3
Gold	0.74	Up 1	-8.2	-2.9
Oil	1.31	Up 1	69	12
Bond Futures	1.17	Down 4	14	-1.6
2-Yr Note Futures	1.12	Down 1	2.5	0.3
Bund Futures	1.11	Down 5	5.3	0.05

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the best-selling [The Education of a Speculator](#), which is available [here](#).

Laurel Kenner is a financial writer in New York City. Formerly head of US stock market coverage at Bloomberg News, she previously reported on police, politics and aerospace during her 17-year news career.

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Finally the Market Laughs With You, Not at You

By Victor Niederhoffer and Laurel Kenner

Columnists

01/17/2001 12:00 AM

The world has joked incessantly for over 50 centuries.

--W.S. Gilbert, *His Excellency: The Played-Out Humorist* (1894)

The market has been playing a very pleasant joke on its investors, speculators and traders so far this year.

At inception, it pretended to do exactly what it did last year. The S&P 500 was down 3% to 1300. Bonds were up 2 points. Tech was down 6%, and Internet, 13%.

Subsequently, the S&P rose 3%. Bonds fell a few points. Tech is up 16% and Internets are up 22%. Our own recommended Internet portfolio is up 188%.

The pivot point came when Old Doc Greenspan lowered the fed funds rate by an unusual half-point, at an unusual between-meeting time. The Nasdaq immediately rallied some 25% in the next second, then gave back more than two-thirds of that during trading in the next two days.

But now the joke. As of the open today, a strong sales forecast from Juniper Networks (JNPR) has sent both indexes back to within striking distance of where they were after the Doc acted.

The larger point is that the Mistress of Markets herself is prone to jokes. And many of these jokes are improbable, symmetric, and incongruous, in the tradition of the mathematics that makes jokes and markets funny.

Philosophy Florida Style

A rather brilliant report on the market as a joke was generated in the heat of battle by a philosophical day trader from Florida, James Lackey. His sage analysis provides a meal for all seasons in the best tradition of the Daily Spec:

"Get the joke." My father loves when I use that line. He is the type that says, How can you sell something that you do not own, referring to short sales. I learned that line from my old friend Tony Forte, an old Wall Street veteran who is now in heaven. When I was a brand new trader, guys would yell, "I can't believe the stock is going down on good news." I was new, but I would say, "Nobody cares," and Tony Forte would say, "Ya see, Lack gets the joke." He took me under his wing only for a short time until I realized that Wall Street is telling jokes all day long, and it was my job to get the joke. Then Tony Forte sent me out in the speculation world to learn my own style of comedy.

Telling jokes is harder than writing them. It is all in the timing.. Trading well is all about timing. Quick little one-liners are good for small laughs and small profits. Huge detailed stories have the potential to bring the house down, huge profits, but considerably more risk.

Get the joke means, not only why is that guy saying that, but what does he mean by that. Asking him is the simple way. The best way is to get to know him.

On the cusp of the Juniper earnings announcement, stocks are scheduled to go through the roof at the open today, thrusting the S&P 500 to up on the year. That's a pleasant joke in itself. The barbecue-loving professor Mark McNabb of Virginia Tech got a belly laugh out of that one, as he's long Juniper and Cisco Systems (CSCO). He's expecting wildfire in the networking sector "at least for five minutes," and hopes that the food chain in chips and suppliers and couplers should be a great joke today, as his touchy-feely indicators suggest that "the shorts may have been playing many of the others in case Juniper was not so good."

The Day for Vishay

The good jokes in tech recently stimulated the Spec Duo to call up Vishay Intertechnology (VISH), the largest manufacturer of passive electronic components in the U.S. and Europe, and one of the largest in the active components used in chips. Vic uses their products every day in his hobby of creating feedback circuits. But his interest was piqued more by the decline in their stock price to 16 1/2 from a recent high of 62. That's always a source of innocent merriment for us, especially when it brings the P/E down to 4. (Long-term growth is projected at 16% a year.)

The problem is that business was so good that the recent slowdown in chip purchases by telecoms and chipmakers caused Vishay to guide earnings estimates down by 10% or 20%. That brought the stock back to where it sold in 1997. What a paradox to note that the earnings in 1997 were some 15% of the current base levels. The guess here, based on the interview with Vishay's chief financial officer, is that the quarterly comparison in the last two quarters of 2001 will be quite strong. And shortly thereafter, or even before, we would not be surprised to see an ascent back to the old highs in the three- to five-year time frame.

We aren't recommending a buy right now, but Vishay should provide a barrel of laughs sometime in the future.

Company	YTD % Change
Ameritrade (AMTD)	40.18
Cobalt Group (CBLT)	266.67
Cylink (CYLK)	44.93
DoubleClick (DCLK)	38.64
Disney (Walt) Internet Group (DIG)	30.88
E*Trade Group (EGRP)	66.10
ITXC (ITXC)	35.14
MyPoints.com (MYPT)	70.97
Prodigy Communications (PRGY)	18
Psinet (PSIX)	382.58
Razorfish (RAZF)	51.92
Rhythms Netconnections (RTHM)	94.44
24/7 Media (TFSM)	229.44
TD Waterhouse (TWE)	4.27
Wit Capital Group (WITC)	36.44
Average Move	94

With Full Margin, as Recommended: 188

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.03	Up 1	-1.2	0.1
S&P 500	0.94	Up 1	0.5	3.4
Nasdaq	0.94	Down 2	6.0	14
Europe STOXX-50	1.05	Down 1	-2.5	-1.1
Dollar/euro	0.85	Down 2	.01	-0.9
Nikkei	0.80	Up 3	-1.5	-1.5
Dollar/yen	0.92	Up 1	-2.6	-2.8
Gold	0.73	Down 2	-3.1	-2.1
Oil	1.29	Down 1	11.1	9.4
Bond Futures	1.17	Up 1	14	-1.4
2-Yr Note Futures	1.13	Up 1	0.3	-0.1
Bund Futures	1.11	Down 1	-.09	-0.9

Victor Niederhoffer is a private speculator specializing in futures and options trading. His positions often change during the day based on shifting market expectations and volatilities. He is the author of the best-selling The Education of a Speculator, which is available [here](#).

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Attempt to Hobble Ty Cobb Mirrors Gates Case

By Victor Niederhoffer and Laurel Kenner

Columnists

01/18/2001 05:54 PM

In many ways he was resented by a lot of people because he was so doggone good.

-- Davy Jones discussing Ty Cobb, from *The Glory of Their Times* by Lawrence S. Ritter.

The overnight swing of IBM (IBM) above 100 for the first time since Dec. 5 creates a heroic environment for stocks, echoed in the refusal of S&P 500 futures to fall more than five points for seven consecutive trading days.

Regrettably, both events have been bearish for the market in recent years. The Daily Spec computers are flashing negative.

Accordingly, a special meeting of Stock Talk! was held outside the Lucille Lortel Theatre in Manhattan last night to protest the performance of "Cobb," Lee Blessing's loathsome play about the greatest baseball player who ever lived. The play depicts Cobb as an angry, racist, gun-loving drunk who spiked and slashed his way to a .367 lifetime batting average.

Sam Crawford, the greatest hitter of the dead-ball era, who played the outfield with Cobb for 13 years from 1905 through 1917, put things in perspective in his interview with Ritter in *The Glory of Their Times*: "Cobb never tried to spike anybody. The base line belongs to the runner. Infielders are supposed to watch out and take care of themselves."

Such books as Richard Bak's *Ty Cobb* quote Cobb's opponents echoing Crawford. But for the same reasons that great companies must be destroyed in order to justify the prevailing belief that humans are small, Cobb himself must be sacrificed to the pillar of envy and smallness.

Cobb and Gates

Indeed, "Cobb" could have been written by Judge Penfield Jackson himself, whose complete lack of trust in Microsoft (MSFT) "let him overcome his aversion to a structural remedy," according to an excellent article in the Jan. 15 issue of the *New Yorker*.

You see, Jackson believes Gates & Co.'s crime was hubris. The judge thinks Gates has a Napoleonic concept of himself and his company, an arrogance that derives from power and unalloyed success with no leavening hard experiences, no reverses. (The current film "Anti-Trust" gives the Hollywood version of this view.)

There's nothing small about Gates or Cobb. Gates is still the world's richest man. Cobb's lifetime average is the highest of any Major League Baseball player. He stole 891 bases, scored 2,246 runs and won a home run title in the dead-ball era. He was a great fielder. He was the kind of player who could beat the opponent single-handedly.

In short, Cobb was the Microsoft of his day. And Vic still remembers with glee that he was often called "The Ty Cobb of Squash," even though it was meant as an insult even 100 years ago when Vic played

the game.

Apparently, the old diabolical idea is back: hatred of the good for being good, for believing it is good. As long as this idea permeates our civilization, both moral and market, it will be hard for stocks to ascend. For greatness in stock performance belongs to those who provide a heroic product at a heroic profit.

Holding Off on the Chips

Our computers, meanwhile, are showing an expected 1.5% decline in the next week or two on the 17 most similar occasions to the present vis-à-vis a long absence of a terrible decline.

Under the circumstances, we will eschew our planned review of the semiconductor industry today. We had planned to recommend Cirrus Logic (CRUS), Conexant Systems (CNXT), Motorola (MOT), Xilinx (XLNX) and KLA-Tencor (KLAC).

The markets are much too exuberant for our taste -- both on a qualitative and quantitative basis. The big rise in both stocks and bonds as well as the absence of even a small decline in the last eight days is highly negative.

Taking one consideration with another, it is our unhappy lot to recommend the full hedging of both our Internet and Other Worldly portfolio. We are doing the same.

One way to hedge the Internet portfolio is to sell one or all of the three American stock exchange indexes that are available for trading. The broad-based Internet security trades under the symbol HHH (HHH). The Internet architecture security trades under the symbol IAH (IAH). The Internet infrastructure security trades under the symbol IIH (IIH). For those who want to hedge their Internet position, they might wish to divide shorts among these three Holders.

To hedge the Other Worldly portfolio, consider shorting the Spiders (SPY), the S&P 500 futures or some equivalent basket.

Bear in mind, however, that to the best of our knowledge -- and the studies of Mark Hulbert, the dean of performance evaluations, there is no one in history who has ever made money on their short-sale recommendations over a reasonable time period. And there is no reason to believe that the same would not apply to us.

Postscript:

This just in from reader Larry Ritter, who, frankly, knows a lot more about baseball than we do:

I hereby give my official imprimatur to today's column (even though Cobb was NOT "the greatest ballplayer who ever lived.") Many vote for Mr. George Herman Ruth and a few for Mr. Honus Wagner. Hope all goes well.

Larry

Internet Portfolio			
Company	Dec. 29 Close	Jan. 17 Close	% Change YTD
Ameritrade (AMTD)	7	9 7/8	41.07
Cobalt Group (CBLT)	1 1/8	4	255.56

Cylink (CYLK)	2 1/16	3 5/16	53.62
DoubleClick (DCLK)	11	14 11/16	33.52
Disney Internet Group (DIG)	4 1/4	5 5/16	25
E*Trade Group (EGRP)	7 3/8	12 9/16	70.34
ITXC (ITXC)	6 15/16	10	44.14
MyPoints.com (MYPT)	31/32	1 11/16	74.19
Prodigy Comm. (PRGY)	3 1/8	3 7/8	24
Psinet (PSIX)	0.7188	3 1/8	334.75
Razorfish (RAZF)	1 5/8	2 15/32	51.92
Rhythms Netconnections (RTHM)	1 1/8	1 21/32	47.22
TD Waterhouse (TWE)	14 5/8	15 7/16	5.56
24/7 Media (TSFM)	1/2	1 3/4	229.44
Wit Soundview (WITC)	3 11/16	4 31/32	34.75
Average Move			88
With full margin as recommended:			176

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.02	Down 1	1.9	-3.3
S&P 500	0.95	Up 2	0.7	-1.3
Nasdaq	0.95	Up 1	8.6	2.5
Europe STOXX-50	1.05	Up 1	-0.09	2.2
Dollar/euro	0.85	Down 3	-0.7	0.4
Nikkei	0.81	Up 4	-0.9	-0.9
Dollar/yen	0.91	Down 1	-3.8	-4.6
Gold	0.73	UnChg	-3.2	-1.7
Oil	1.28	Down 2	8.0	3.7
Bond Futures	1.18	Up 2	-0.5	-0.4
2-Yr Note Futures	1.13	Up 2	0.4	0.1
Bund Futures	1.12	Up 1	0.1	-0.7

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Disclosure: Victor Niederhoffer is long most of the Internet stocks in the Daily Speculator Internet Portfolio, and is short S&P futures at the time of writing. His positions change at all times. He currently

holds long positions in Cobalt (CBLT), Cylink (CYLK), DoubleClick (DCLK), ETrade Group (EGRP), Expedia (EXPE), ITCX (ITXC), Psinet (PSIX), Razorfish (RAZF), Rhythm Netconnections (RTHM) and 24/7 Media (TFSM).

Laurel Kenner does not own or control any of the stocks mentioned in this article.

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Honing Your Craft with Better Tools

By Victor Niederhoffer and Laurel Kenner

Columnists

01/19/2001 09:22 AM

(Editor's Note: Brett N. Steenbarger, Ph.D. is a licensed clinical psychologist and periodic guest contributor to the Daily Speculations column. This is the first in a three-part series covering online resources and tools for active traders.)

During my college days, the best psychologist role models were the basketball coaches. Even at a competitive hoops school like Duke University, there were always a few cupcakes on the schedule, especially early in the year. And nothing is more difficult than practicing for an easy opponent. It is human nature to ease up, take the short cuts.

The coaches realized this, and also recognized that the best competitors compete against themselves. It doesn't matter if the opponent is Notre Dame University or the Little Sisters of the Poor. The warlike competitor always has a worthy foe in himself.

So there was a very special drill reserved for those half-speed practices: No one could go home until he had made ten straight foul shots. If the practices were especially lethargic, no one could go home until *everyone* had made their foul shots.

Duke University basketball of 1972 is not Duke basketball in 2001. We lost plenty of games and were never rated in the top 20. *But we made our foul shots.* When the pressure was on and a free throw could make the difference in the outcome, we were money in the bank. Week after week practicing those free throws under self-imposed pressure, we had been tested under fire.

Creating Your Own Challenge

If you read Jack Schwager's "Market Wizard" books, the same competitive themes emerge. The greats test themselves under pressure and, during peaceful times, create their own challenges. They search for patterns to trade and they re-search. They are ever-improving their craft.

A true craftsman, however, must have tools worthy of the trade. If you are going to hone your craft, you need resources that will inform and challenge you. Thankfully, with the boom of the online medium, there are many high quality resources available to speculators who would improve themselves. In this series of articles, I hope to share some of these with you.

A trader's most basic resource is a real-time data feed. Immersion in the movements of the market provides an intimacy that cannot be duplicated by simply following end-of-day data.

What, however, if you cannot afford hundreds of dollars per month for real-time data and charting? A worthy option is Ask Research (www.askresearch.com). This real-time charting service (indices are free; stocks are \$25/month) allows users to manipulate bars from 1 minute to 60 minutes to daily and incorporates a number of the most popular technical indicators and studies, such as the NYSE TICK, a unique money-flow index, and moving averages. Most impressive of all, Ask Research updates itself every 30 seconds during the trading day, with no need to manually refresh the screen.

Ask and You Shall Receive

Scott Ruppert, managing partner at Ask Research, points out that "our daily charts are updated with each trade for price and technical indicators. A trader can see exactly where a stock is trading at that instant compared to where it was four days ago or four years ago, in price as well as indicator levels. We also appear to be the only charting site that allows a user to adjust the technical indicator parameters to their investment objectives and to stock volatility."

My own experience with Ask Research confirms Ruppert's assertion that his service is "a faster, more customizable service than others."

Some of my favorite services for self-improvement are those that educate traders. A standout is Teach Trade (www.teachtrade.com), which features well-known pit trader Lewis Borsellino and is edited by Patricia Crisafulli. Borsellino conducts a "morning meeting" each day in which he sets the context and strategy for trading. This includes anticipated targets, support and resistance levels, and important news events. Throughout the day, the morning strategy is updated with commentary and specific trade ideas from Borsellino and site co-founder Brad Sullivan. These are provided at no charge to those who register with the site.

When I asked about the unique features of Teach Trade, Borsellino responded enthusiastically. "What's unique about our site is that it's 'for traders, by traders.' By that I mean the commentary on the site—dynamically updated all day—is from traders who are trading all day, every day... Throughout the day we comment on the stock index futures markets, what we see in the Pit, the action we see on the screen, how we view the market and how we'd play that day's trade. We're not looking to replace a trader's own thinking. Rather, we want to be a part of a trader's decision-making process."

My experience with Teach Trade is that it provides a vantage point unlike that of other sites. The commentary is front-line—who is buying, who is selling—and it is delivered to the subscriber in real time via a pop-up window. "The window alerts users each time we post an update on the Stock Index Futures (S&P, Nasdaq, and Dow)," Borsellino explained. "Users tell us that this is the number-one advantage to using our site. We understand that traders are watching their charts, their analytics. We don't want them to have to take their eyes off the market."

Trading Places

Perhaps the largest educational trading site is TradingMarkets.com, which charges \$15-\$35 for its subscription service but also has a great assortment of trading products for sale. The site contains a variety of features, including commentary on market action throughout the day, updated indicators based on the research of Larry Connors and others, and a host of trade ideas from such active traders as Jeff Cooper and Dave Landry. I have been most impressed by the site's online courses and detailed commentary on how to select stocks for buying and shorting.

Steve Miller, President of TradingMarkets.com, notes that the site is unique in that "We don't tell people what to buy and sell, but how to find this out on their own." He explains that the real-time "TradersWire" "is the only service in the world that gives up-to-the-second price action alerts, combined with actionable trading analysis" via a scrolling applet." Noting that a sister site, beginningtrader.com, has been developed to provide education to those new to trading, Miller explained that, "Ongoing education and training by successful traders is our strongest feature."

A feature common to these services is their ability to deliver information in real time. This teaches traders to process market information in the heat of market action. When the next major market move occurs, traders who have honed their skills under fire will be able to make their "free throws." In the

next installment in this series, we will hear from Daily Speculations readers and their favorite tools and resources for mastering their craft.

Brett N. Steenbarger, Ph.D. is a licensed clinical psychologist and Associate Professor of Psychiatry and Behavioral Sciences at the SUNY Upstate Medical University in Syracuse, NY. His primary research interest is multivariate behavioral modeling of the stock market. He welcomes comments and questions at steenbab@aol.com. He does not hold a position in any of the stocks or services discussed in this column. Positions may change at any time.

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Warren Buffett Hathaway of Downplaying Tech and the Knicks

By Victor Niederhoffer and Laurel Kenner

Columnists

01/22/2001 09:52 AM

Vic happened to be in Seattle on Friday night to see the Minnesota Timberwolves beat the SuperSonics 98-93 at KeyArena stadium, and found himself sitting directly in back of the World's Oddest Couple: Bill Gates and Warren Buffett.

As Vic watched the ex-Knicks center Patrick Ewing score his 4 points for the game -- slightly below his six-point average for the 11 games he's played this year for the Sonics -- he couldn't help overhearing Warren as he tutored Bill on the fine points of sports and investing.

Warren: Sure, the Knicks seem to be doing fine without Ewing. They're in second place in their division now, and the Sonics are in fifth place. But Ewing exemplifies the value approach, Bill. He's old, he's tired, he's sluggish. But he's got name recognition. Without him, you watch, the Knicks are due for a fall.

Just like your own stock, Bill. Sure, Microsoft (MSFT) has had an unusual bounce lately. What is it, up 41% year to date? But what you young folks don't understand is that investors have always lost money on tech companies. Why, I remember the early days of the airplane industry...it was before your time... most of those stocks don't even exist any more. If it had been up to me, I would've shot those scoundrels Orville and Wilbur before they got off the ground a second time.

Bill: (We couldn't hear clearly, but he seemed to be offering condolences to Buffett for the 5% drop in Berkshire-Hathaway (BRK/A) shares in 2001.)

Warren: How soon people forget their lessons. That Nasdaq 100, now -- it's up 13% this year. Well, practically none of those stocks will exist in 100 years. You mark my words, Bill. Technology, it's just a new-fangled outrage on humanity.

At my own shop, we will not go into businesses where technology is crucial to the investment decision. I know about as much about semiconductors or integrated circuits as I do of the mating habits of the chimpanzees. I liked things better in the days before computers and wireless, when there was only black-and-white TV in 11-inch sets.

What chance do I have of understanding Genentech (DNA) or Cisco (CSCO)? Technology is way over my head. I can't understand it, I don't want to understand it. I just want to eat my burgers and drink my Coke (KO) and play my bridge.

Bill: Well, a lot of people thanked you last year, Warren, when techs crashed.

Warren: That was nothing. I'm hoping for a real crash, like in 1973. A friend described me as being "in a state of ecstasy" then. I was running around like a young colt. When I got up, I felt like I wanted to tap-dance.

Bill, why don't you use that extra cash you're sitting on to buy back some of your stock the same way

Coke and so many of the other companies whose boards I sit on have been doing? Why plow that cash back into investment when tech is dead? Why be a risk taker when there are good companies producing things like shoes and candy and trading stamps? People will always pay a premium price for necessities like these.

Bill: What did you do with all those Green Stamps, Warren?

Warren: I keep 'em in the hall closet. Bill, we should go on a two-week cruise. Hillary's going to give a talk on how to profit in the market, and I got invited because I endorsed her. I've been feeling kind of down lately, because although I did pretty well last year, I'm never going to make the 10,000% return that Hill made on cattle futures. No wonder she doesn't trust the masses to invest their own Social Security contributions.

Bill: (Points to elderly gentleman in front row with local TV celebrities.)

Warren: Alan Greenspan! I can't figure out what he's up to. He was doing so well with puncturing the Nasdaq bubble. Heck, those stocks still have ridiculously high P/Es. Why did he stop raising rates just when the going was good? HEY, ALAN!

(At that point, Vic woke up in a cold sweat. Warren, Bill, the Sonics...it had all been only a bad dream. Throwing on a bathrobe, he ran to the phone and called Laurel.)

Vic: How much are we up on that Internet portfolio we recommended at worldlyinvestor.com at the start of the year?

Laurel: (mumbling) Who died? Yes, I'll meet the margin call tomorrow. I'll take the French toast. The check is in the mail. Oh, it's you, Vic. Let me turn on my terminal. We're up 82%, or 164% on the full margin we recommended.

Internet Portfolio			
Company	Dec. 29 Close*	Jan. 17 Close	% Change YTD
Ameritrade (AMTD)	7	9 7/16	34.82
Cobalt Group (CBLT)	1 1/8	3 15/16	250
Cylink (CYLK)	2 1/16	4 3/16	94.2
DoubleClick (DCLK)	11	15 1/4	38.64
Disney Internet Group (DIG)	4 1/4	5 5/16	25
E*Trade Group (EGRP)	7 3/8	12 9/16	70.34
ITXC (ITXC)	6 15/16	11 1/4	62.16
MyPoints.com* (MYPT)	31/32	1 5/16	35.48
Prodigy Comm.* (PRGY)	3 1/8	5	60
Psinet (PSIX)	0.7188	2 19/32	260.84
Razorfish (RAZF)	1 5/8	2 5/16	42.31
Rhythms Netconnections (RTHM)	1 1/8	1 17/32	36.11
TD Waterhouse* (TWE)	14 5/8	15 3/8	5.13
24/7 Media (TSFM)	1/2	1 17/32	188.26

Wit Soundview (WITC)	3 11/16	4 15/16	33.9
Average Move			86
With full margin as recommended:			164
*Priced as of 1/5			

That doesn't count the hedge we advised Thursday afternoon. We advised people to short the three American Stock Exchange Internet-related exchange-traded funds to the full amount of the dollar value involved at Friday's open.

(The broad-based Internet security trades under the symbol HHH (HHH). The Internet architecture security trades under the symbol IAH (IAH). The Internet infrastructure security trades under the symbol IIH (IIH).)

Vic: Hopefully the gain from the short covered the commissions and bid-asked spread involved.

Laurel: Vic, should we tell people to sell? I mean, 164% in three weeks...

Vic: Well, it's not just us, you know. And it's not that we were "due" after being so cold during the fourth quarter. Almost all beaten-down stocks have displayed fantastic rallies in the first three weeks of this year.

I was talking with my friend Dick Sears, who created an index of the tech stocks recommended by George Gilder. The site is www.gtindex.com. The Gilder stocks are up 53% from their Dec. 21 low, after losing two-thirds of their value between March 6 and Dec. 21.

Laurel: That's wild, but listen to this: Remember those 43 below-\$5 NYSE stocks we recommended on Oct. 4 and Oct. 5? They're up 39% since our call. I bought 15 of them myself, and they're up 40% this year. And the smaller portfolio of below-\$5 stocks we published Oct. 12, the ones that paid dividends and had insider buying, is up 41%.

Vic: Everything switched with the New Year, just like we predicted in our MSN MoneyCentral column on Dec. 28. The 10-worst Nasdaq 100 performers of 2000 are up an average of 41% in the first three weeks of 2001. They were all down 79% or more last year.

Laurel: How long are we going to hold onto the Internet portfolio, then?

Vic: I'm in a dilemma, especially since bonds had yet another terrible decline on Friday after a few days of reprieve.

Too many investors have a stop on how much they will accept as a loss. Too few have a stop on how much they will accept as a win before calling it a day. The situation is particularly vivid in all its tragedy at any casino, where player after player quits after losing 80% of their chips, but few would even consider quitting when they double their money.

On the other hand, I keep thinking of Peter Lynch. He reports in his books that over and over he tended to sell stocks too early on the way up, being happy with a two-bagger when stocks such as Wal-Mart eventually would have turned into 100-baggers.

The problem with the "wisdom" of Peter Lynch, in my book, is that he doesn't read any books. Nor to the best of my knowledge does he ever put any statistics on the table that would give his readers a meal for a lifetime. In fact, the best I can come up with of lasting value in his books is that he admires the rapier-like analytical abilities of the chief columnist at the old-hearted financial weekly, and that he admires his wife's ability to pick great brands on her frequent trips to the shopping mall.

With guidance such as this, it's hard to pick the wheat from the chaff. While there undoubtedly are some things of value in what he discusses, I can't tell if his advice to wait for multi-baggers is tested, intuitive, or a hypothesis appropriate for describing his own records.

Laurel: By the way, I meant to tell you -- corporate insiders recently have been selling many of our Internet picks. Considering that most of these stocks had declined 90% or more from their highs, this is somewhat distressing. While one can always sympathize with an insider's need to raise cash --

Vic: Yes, I have been there many times myself --

Laurel: -- to me, it's not an intuitively healthy sign when a company official, doubtless for diversification or divorce settlements or college tuition-only, heads for the exit signs.

Vic: But we don't have to make that intuitive judgment in what we do. We had four or five reasons for recommending these stocks in the first place, and one of them was insider buying. Now that reason has been removed.

The six stocks among our 15 recommended with recent insider selling are E*TRADE Group (EGRP), ITXC Corp. (ITXC), MyPoints.com (MYPT), Wit Capital (WITC), DoubleClick (DCLK) and Ameritrade (AMTD). Let's recommend the sale of these issues. I'm going to be selling my own holdings of them on a leisurely manner over the next three days.

Laurel: What should we tell people to do with the money they raise from the sales?

Vic: I don't think they should do anything with it right now. I think the end of the month will be a better time to consider buying something. Until then, I would hold the money in cash.

In the interim, I'm going to reduce the dollar amount of my hedge so that it equals the remaining value of the 10 stocks still held. I'll be selling the stocks with limit orders so as not to lose that extra little edge.

*Victor Niederhoffer is a private speculator specializing in futures and options trading. His positions often change during the day based on shifting market expectations and volatilities. He is the author of the best-selling *The Education of a Speculator*, which is available [here](#).*

Laurel Kenner is a financial writer in New York City. Formerly head of US stock market coverage at Bloomberg News, she previously reported on police, politics and aerospace during her 17-year news career.

They hold positions in some of the companies discussed. Positions can change at any time.



Pacify Yourself With Profits in Case Market Heads South

By Victor Niederhoffer and Laurel Kenner

Columnists

01/23/2001 09:43 AM

To the tune of "Some Enchanted Evening," from the 1949 stage musical *South Pacific* (music by Richard Rodgers, lyrics by Oscar Hammerstein II)

1. Some infernal evening
After a Fed-rate cut
After all your stocks have
Set new highs for the year

Then somehow you fear
A down day's in store
Your stocks aren't going to
Go up any more.

2. Some infernal evening
Greenspan may be laughing
You may hear him laughing
Within a long dry speech

And night after night
As strange as it seems
The sound of his laughter
Will ring in your dreams

Who can predict it?
Who can tell you why?
Bears give their reasons
Nasdaq's far too high.

The massive turnaround in beaten-up stocks this year is unprecedented. One-tenth of all Nasdaq stocks, led by BMC Software (BMCS), are up more than 48%, and one-half of them are up more than 25% in 2001.

Under the circumstances, we found ourselves singing "Some Enchanted Evening" on the way back from dinner last night. The wait captains at the restaurant are beginning to nibble on stocks again, after suffering losses last year.

One retro analyst after another is retrospectively noting the turnaround in the depressed issues of last year and making equivocal noises about how this is a normal, persisting tendency.

Music to a Bear's Ear

How distressing. How bearish. Such euphoria always makes us sing "Some Enchanted Evening," but with the kind of dark overtones in which lyricists such as Sondheim and Gilbert found their natural

métier.

The absence of a big decline has added to the euphoria. S&P 500 futures have managed to avoid a drop of wider than 8 points for 11 trading days. Such long runs have been highly bearish in the past.

The straws in the wind are getting more numerous. Bond prices hover near two-month lows. The Chicago Board Option Exchange's Volatility Index (\$VIX) has quietly fallen from 35 to a bit above 25. IBM (IBM) has broken above 100, thereby requiring its attraction for the round number.

Furthermore, Dr. Brett Steenbarger, the Daily Speculations market psychologist, says the preponderance of advances over declines among individual stocks is slight at present, despite the strong advances in the averages. His diagnosis: The market is suffering from split personality. His statistical studies of such cases indicate a serious risk of decline.

As is usually the case, since we tend to be bottom-fishers, we find ourselves holding an inordinate number of the stocks that have gone up the most this year, including BMC Software and several two- and three-baggers among the Internet issues. Yesterday, we advised selling five of the 15 stocks in our Internet portfolio.

Time to Harvest Profits

With all the expectations surrounding the coming Fed-rate cuts, we are planning to cut our remaining holdings by 50%. (Last week we sold short an Internet "basket" security traded on the Amex under the symbol (HHH), and we will be reducing that hedge by a corresponding dollar amount.)

In short, our recommended portfolio of Internet stocks is down to a third of the levels originally recommended. And we are hedged to the full amount of the remaining position, thereby locking in our 180% profit. In our other worldly portfolio, we are maintaining our positions in the six issues recommended but are hedged with S&P futures to the full extent of that position.

The five remaining issues are: Techne (TECH), up 29%; Borland Software (BORL), up 22%; Westell Technologies (WSTL), up 14%; Commscope (CTV), down 2.7%; and Petsmart (PETM), down 8.9%.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.02	Down 2	-1.9	-0.4
S&P 500	0.96	Up 1	1.7	3.6
Nasdaq	0.96	Down 1	11.6	15
Europe STOXX-50	1.04	Up 1	-1.2	0.7
Dollar/euro	0.86	Up 1	-0.4	-1.4
Nikkei	0.83	Up 7	1.8	1.2
Dollar/yen	0.93	Up 3	-0.09	-0.8
Gold	0.75	Up 3	-1.9	-0.5
Oil	1.28	Down 1	16.2	14
Bond Futures	1.17	Down 2	-1.4	-2.3
2-Yr Note Futures	1.13	UnChg	0.5	-0.5
Bund Futures	1.10	Down 2	-0.2	-1.1

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Awash in Profits, Speculators Turn Negative

By Victor Niederhoffer and Laurel Kenner

Columnists

01/24/2001 10:33 AM

The path to market glory is fraught with peril. Always below there is the Hospitable One, with room for yet another soul.

Today's guides to the river Styx and beyond are not the likes of Hermes, but the voluptuous media mavens and the withered old sages who eat everything young.

Day trading can lead all too often to the Hot Place. For those lucky enough to reach Charon's gateway with a penny fare still in their pocket after paying the crushing vig on their trades, brokers are all too willing to ferry them across. Those without a penny must wander about till they find the pauper's entrance. And Cerebrus, the three-headed dog, will keep the new entrants from returning to the land of the living.

Thus, we were reluctant to advise selling the market short. After all, Rule #1 is "Never sell short," because it goes against the 10 million percent-per-century returns available to a random buy-and-hold strategy.

The Sultan of Speculation himself, Mr. George Soros, often told Vic that he lost more money selling short than in any other activity in his illustrious career. And the Dean of Evaluation, Mark Hulbert, concluded that among the hundreds of advisers he has audited, not one short seller has beat buy-and-hold.

Thus, it was with great reluctance that we suggested anything other than a buy-and-hold strategy to our loyal readers. But we ourselves have not been unwilling to give the underworld the hope of seeing us whirl around.

Too Much, Too Fast

Too many portfolios, including all of ours, are going up much too fast. Our research picks, for example, recommended Nov. 28, are up 50% year to date. Our basket of below-\$5 NYSE stocks recommended Oct. 4 and Oct. 5, are up 31% on the year. BMC Software (BMCS), which we recommended in July and again in October last year, is up 117%, the best performance among the S&P 500.

The reasons we tempt the Evil One with our short-sale recommendation are multifarious. For one, the often-bearish Employment Cost Index number is due on Thursday. The declines that have preceded the release of this number are so scary that it makes us shudder to report them.

Similarly, the Chicago Board Options Exchange's Volatility Index (\$VIX) has fallen from above 35 to a shade above 23 as of the close yesterday. One of our timeless systems involves buying the market when VIX is above 30 and closing out the position when it falls below 25.

Along the same lines is the failure of the market to show even a chimera of a good-sized decline in the last 12 trading days. The S&P 500 futures are at the highest since Dec. 13. Yesterday, the market moved to above the highs it achieved in the seconds after Doc Greenspan released the magic bullet of a rate cut on Jan. 3. Such returns fulfill the destiny of the market.

And regardless of the quantitative numbers, we are not pleased when bonds close at a seven-week low, as they did yesterday.

Putting all things together, and considering that the rate of profit on all our recommended portfolios (and our own performance itself) is unsustainably high, we are intending to sell yet another half of the remaining Internet portfolio today, thereby reducing our position in Internet stocks to one-sixth of its original level. We will reduce our hedge accordingly, locking in a profit of 160% or so during three weeks.

Calling Nearly All Portfolios: Time to Sell

At the same time, we are hereby officially suggesting that all of the year 2000 portfolios on which we posted bullish analytics, all guidances we reported last year on the recommendations of great traders ranging from the Shakespeare of Markets on down, and all stocks we recommended last year, be closed out today from our hypothetical and actual track records. We will be moving in the same direction with all those stocks in our portfolio that are not in the control of others.

One exception: since our Other Worldly portfolio is hedged, we are not recommending the sale of those five stocks (Borland Software (BORL), which changed its name from Inprise on Jan. 22; Commscope (CTV); Petsmart (PETM), Techne (TECH) and Westell (WSTL).

Internet Portfolio			
Company	Dec. 29 Close	Jan. 22 Close	% Change YTD
Ameritrade (AMTD)	7	9 7/32	31.70
Cobalt Group (CBLT)	1 1/8	3 15/16	250
Cylink (CYLK)	2 5/32	3 13/16	76.81
DoubleClick (DCLK)	11	17 5/16	57.39
Disney Internet Group (DIG)	4 1/4	5 1/2	29.41
E*Trade Group (EGRP)	7 3/8	13 1/16	77.12
ITXC (ITXC)	6 15/16	14	101.80
MyPoints.com* (MYPT)	31/32	1 9/32	32.36
Prodigy Comm.* (PRGY)	3 1/8	4 1/2	44
Psinet (PSIX)	23/32	2 1/8	195.63
Razorfish (RAZF)	1 5/8	2 9/16	57.69
Rhythms Netconnections (RTHM)	1 1/8	1 5/8	44.44
TD Waterhouse* (TWE)	14 5/8	15 7/16	5.56
24/7 Media (TSFM)	17/32	1 23/32	223.56
Wit Soundview (WITC)	3 11/16	5 3/16	40.68
Average Move			85
With full margin as recommended:			174
*Priced as of 1/5			
"NOTE: SELL RECOMMENDATIONS issued 1/21 on E*Trade, ITXC, MyPoints.com, Wit Capital, DoubleClick, Ameritrade. These stocks will be removed from portfolio 1/24."			

Bear in mind that our own record is fraught with getting in and out of positions too early. Like the many old-hearted people, we cannot resist subjecting to the Rabelaisian hurly-burly of our column, we too can remember the poverty-stricken days. We too would find it almost impossible to climb the stairs from the bottom again, and thus, our bullish goals tend to fall short of the heights.

Like most writers and market commentators, we are far too human -- and far too fallible. When we do make a prediction, most of the time the likely outcomes are not significantly different from chance. Last year, we were far too expansive. We reported much too often on ideas that doubtless made their creators millions but were all too likely to end up being unprofitable for those who tagged along.

We counted too many anomalies, and compounded the mischief by regularly reporting on current stocks that displayed those seeming anomalies. The law of ever-changing cycles frequently worked to make things that did well in the past ready to go the opposite way just after we uncovered them.

Above all, we were much too bullish last year. Our standard mantra of buy and hold, which has been good for most of the last century, was not good last year, especially for Nasdaq stocks.

Extraordinary, Unsustainable Profits

This year, we had a very good idea. Luck, and being due for a win, probably had as much to do with our success as our own skill. It is highly unlikely that we will ever repeat this coup. Almost all the ideas we had for this year have been extraordinarily, and unsustainably profitable. And the general reversal of fortunes this year, whereby last year's worst have become this year's best, has worked to waft almost all stocks and portfolios we were bullish about to extraordinary gains.

Just a few weeks ago readers were urging Laurel to trade Vic in for a new partner who knew something about catching fish and good stocks. She stuck with Vic, of course. And now we're kindly being asked for our pre-dawn picks. Even if it were possible to provide them, which it's not, those picks would be of no value.

There is one value, however, we believe we can contribute. We can provide a meal for a lifetime rather than a meal for a day. We can provide a rudder and a framework for analyzing the ever-changing and all-encompassing forces that affect that market, whether from anthropology, ecology, economics, electricity, genetics, geology, meteorology, music, oceanography, sports, statistics or what have you.

We will attempt to stick more to our knitting in the future, and we will not be giving stock recommendations again -- until, that is, the market declines a few days in a row.

Keep in mind that following in the footsteps of guides such as ourselves is guaranteed to prevent you from reaching the Elysian fields. Perhaps as compensation it will increase the chances of your having a penny for Charon.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	1.02	Up 1	-1.3	0.7
S&P 500	0.96	Up 2	3.0	4.6
Nasdaq	0.96	Up 1	14.9	16
Europe STOXX-50	1.04	Down 1	-1.2	2.1
Dollar/euro	0.86	Up 2	-0.3	-0.6

Nikkei	0.82	Down 1	1.4	2.7
Dollar/yen	0.93	Down 1	-2.4	-0.5
Gold	0.74	Down 1	-2.1	-0.4
Oil	1.27	Down 2	15.3.1	12
Bond Futures	1.16	Down 3	-1.9	-2.6
2-Yr Note Futures	1.12	Down 1	0.4	-0.4
Bund Futures	1.11	Up 1	-0.04	-0.6

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Drawing a Conclusion From a Draw in the Markets

By Victor Niederhoffer and Laurel Kenner

Columnists

01/25/2001 10:17 AM

The markets ended in a draw yesterday, with the Dow and S&P 500 each ending within a tick or two of unchanged. Indeed, for the last 13 trading days, the Dow has closed within half a percent of 10,600, and the S&P futures haven't declined by wider than eight points.

Such outcomes always made Vic's checker's teacher, Tom Wiswell, very happy. "A draw is a win for both players," he liked to say, "since they both avoided defeat."

The problem is that the Mistress of Markets is not pleased with such paltry fluctuations. She adores extraordinary moves and extremes of optimism and pessimism so she can induce the players to churn their accounts, thereby paying for the massive overhead needed to keep the infrastructure fit and lubricated.

The Mistress Loves Distress

Regrettably, the thought of the bearish down moves that have followed such long episodes without a meaningful decline had us lying awake with dismal headaches. The punishment for failing to sacrifice to a god what is their due is often terrible. The Trojans learned this to their cost in the *Iliad* when they were too cheap to make the required tribute. Hopefully, the Mistress of Markets will not be as vengeful.

As a final tribute to the Mistress of Markets, we are implementing the sale of yet another half of the remaining portion of our Internet portfolio, and reducing the hedge accordingly, thereby bringing our own holdings to 1/12 the initial amounts.

Internet Portfolio				
Company	Dec. 29 Close	Jan. 22 Close	% Change YTD	Action on 1/23
Ameritrade (AMTD)	7	10 7/8	55.36	Sell
Cobalt Group (CBLT)	1 1/8	3 7/8	244.44	Reduce to 1/4
Cylink (CYLK)	2 5/32	3 9/16	65.22	Reduce to 1/4
DoubleClick (DCLK)	11	16 7/8	53.41	Sell
Disney Internet Group (DIG)	4 1/4	5 11/16	33.82	Reduce to 1/4
E*Trade Group (EGRP)	7 3/8	13 31/32	89.41	Sell
ITXC (ITXC)	6 15/16	13	87.39	Sell
MyPoints.com* (MYPT)	31/32	1 3/8	41.94	Reduce to 1/4
Prodigy Comm.* (PRGY)	3 1/8	4 3/8	40	Reduce to 1/4
Psinet (PSIX)	23/32	2 23/32	278.23	Reduce to 1/4
Razorfish (RAZF)	1 5/8	2 9/16	57.69	Reduce to 1/4
Rhythms Netconnections (RTHM)	1 1/8	1 7/8	66.67	Reduce to 1/4
TD Waterhouse* (TWE)	14 5/8	16	9.40	Reduce to 1/4

24/7 Media (TSFM)	17/32	1 25/32	235.33	Reduce to 1/4
Wit Soundview (WITC)	3 11/16	5 5/16	44.07	Sell
Average Move			93	
With full margin as recommended:			186	
*Priced as of 1/5				
"NOTE: SELL RECOMMENDATIONS issued 1/21 on E*Trade, ITXC, MyPoints.com, Wit Capital, DoubleClick, Ameritrade. These stocks will be removed from portfolio 1/24."				
"ADVISE REDUCING remaining positions to 1/4 of original, HEDGE by selling Internet Holdrs (HHH) to dollar value of portfolio"				

Earning Triple-Digit Returns to Break Even

One person who has not failed to ante up to the Mistress is a day trader from Florida who started the year with an account of \$100,000. He writes: "I paid over \$400,000 in commission alone last year in my account. There was another \$100,000 in ECN fees and SEC tax. So I had to make \$500,000 just to break even."

Needless to say, his letter did not help our insomnia or our headaches. We worried about the certainty of ruination that must inevitably result from such a structure. As Daily Speculations market psychologist Dr. Brett was busy putting out some fires with some patients in Syracuse, he could not opine. We therefore turned to our collection of gambling proverbs, and two immediately came to mind:

- The House will grind through a sack of gold.
- *The only one that can grind is the House.*

Put in simple terms, the ultimate outcome of playing in such a game is inevitable. The House will have all the gambler's money, and he will have none. The gravitational impact of the house take cannot be overcome.

These points are well covered in most books on gambling and probability. The necessary outcome is predicted in one of Vic's favorite adages: "All gamblers die broke," which one of Vic's friends, a hedge-fund operator in Las Vegas, has been able to turn to his advantage.

After the World Series of poker, the winners often celebrate at a gala dinner. Vic's friend, who has made a fortune for many of the owners and entertainers at the major casinos there, is invited to attend. After an appropriate interval of celebration, he likes to say, "Vic Niederhoffer, a thoughtful speculator from the other world, has a proverb: *All gamblers die broke. Their last years are destined to be miserable.*"

He reports that the initial reaction is always stunned disbelief and denial -- and then, silence, as none around the table can deliver a counter-example. The next day, his phone invariably rings and he has another client for his hedge fund.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	0.82	Down 1	-1.3	0.4

S&P 500	1.86	Up 3	3.3	3.9
Nasdaq	1.22	Up 2	16	13
Europe STOXX-50	0.82	Up 1	-0.1	4.2
Dollar/euro	1.00	Down 1	-1.9	-1.7
Nikkei	1.11	Down 2	0.8	3.4
Dollar/yen	0.67	Down 2	-3.2	-1.5
Gold	0.75	Down 2	-2.8	-0.1
Oil	1.00	Down 3	13	3.0
Bond Futures	0.46	Down 4	-2.1	-2.0
2-Yr Note Futures	0.80	Down 2	0.4	-0.2
Bund Futures	0.58	Down 1	-0.2	-0.5

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Laurel Kenner is a financial writer in New York City. Formerly head of US stock market coverage at Bloomberg News, she previously reported on police, politics and aerospace during her 17-year news career.

They hold positions in some of the companies mentioned in this column. Positions can change at any time.

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The Luck of the Maestro, Part II

By Victor Niederhoffer and Laurel Kenner

Columnists

01/26/2001 10:01 AM

(Editor's Note: This is Part II of a two-part book review of Bob Woodward's Maestro by bond expert Paul DeRosa, Ph.D. [Click Here](#) for Part I.)

How Power Gathers

The complete chronology of Alan Greenspan's term as Fed chairman is presented by Robert Woodward in his book, *Maestro*. Woodward, a Washington journalist of some renown, dwells mainly on the 89% of Greenspan's job that is not economics. Like other writers infatuated with Washington, Woodward is concerned with how power is gathered and wielded rather than the thoughts that motivate it. He has written a book about economic policymaking rather than economic policy.

Consistent with this slant, Woodward provides only brief glimpses of Greenspan's life before Washington. The 50-odd years he spent becoming a musician, pursuing a Ph.D., debating Ayn Rand and building a consulting business are important only as prelude to Greenspan's emergence at the seat of government.

The themes of Woodward's narrative are Greenspan's relations with the executive branch, his efforts to manage the other members of the Board of Governors, and his general method for operating in the Washington environment. Woodward makes little effort to discern Greenspan's economic framework, which isn't too surprising since Woodward himself has never covered the economic or financial beat and probably isn't comfortable in the world of economics.

As to Greenspan's political modus operandi, it can be summarized with ease: Give every adversary his full say; listen politely to everyone; and be swayed by no one. This sounds simple enough, and as Woodward documents, it works time and again, but one suspects it is something that relies on the Greenspan magic and that few other people could adopt.

Secretarial Relations

The chairman's relations with the five secretaries of the Treasury with whom he has served have been somewhat more complex. The formal powers of the Treasury secretary are a fraction of those inherent in the Federal Reserve chairmanship, and as a result the person serving as Treasury secretary is more or less effective to the extent he can influence high government officials, especially the Fed chairman.

Greenspan's best working relationship appears to have been with Robert Rubin. As Woodward tells it, Greenspan had entered into a "gentlemen's agreement" with Rubin's predecessor, Lloyd Bentsen, by which he would provide low interest rates in return for a fiscal package that reduced the federal budget deficit by \$140 billion. The Clinton administration, at no small risk to itself, delivered on its side of the bargain, but Greenspan responded by doubling the level of the Federal-funds rate in the ensuing year. It fell to Rubin to forestall war between the White House and the Federal Reserve.

Rubin's approach to this problem provides a telling contrast to that of Nicholas Brady, George Bush's Treasury secretary, in a similar confrontation. Rather than give in to the adversarial reflex, Rubin tried to appreciate Greenspan's objectives and the benefits low inflation and low bond rates might bring to Clinton's administration. He defused the situation by appointing two Democrats to the Board of

Governors but continued to work productively with Greenspan.

Brady, desperate for lower interest rates in 1991, indulged in undergraduate mind games with Greenspan, and let the situation deteriorate to a point where Republicans hold Greenspan responsible for their loss of the 1992 election -- something Ross Perot will be relieved to hear.

For those readers who believe that individuals rather than forces determine the course of government, Woodward's book will provide a feast. Virtually every chapter relates some incident of the relationships among the powerful and it is all delivered with the fluency one would expect from a journalist of Woodward's standing. What is missing is any sense of evaluation. Greenspan is widely held to be brilliant; Woodward can do nothing but agree. The Fed chairman handled the Asia currency crisis with a deft touch, but didn't his failure to raise interest rates in 1996 cause it in the first place?

More importantly, Woodward has no appreciation for the gamble Greenspan took in allowing stock prices to become so grossly inflated in the years after 1996. The only hope of fulfilling the earnings expectations embedded in those prices was a US economy that would grow for an extended period at a rate not seen since the 19th century. In countenancing the stock boom Greenspan implicitly enlisted in the New Economy brigade and put his faith in the power of technology to overcome regulation's icy grip.

Still a Mystery

Despite his best efforts, neither Greenspan nor anyone else has yet to uncover evidence that the productivity revolution extends much beyond the computer industry itself. His enlistment, then, was largely an act of faith. Or perhaps it was the act of a man comfortable in the Washington establishment, who didn't feel like living with the friction that a more restrictive policy was certain to create.

In either case, the foundations of the chairman's policy began to crumble in the spring of 2000. Woodward's obvious admiration for a successful Washington operator makes it impossible for the reader of *Maestro* to place Greenspan in the history of Federal Reserve chairmen.

Like Olympic divers, central bankers are judged not only on the quality of their execution but also on the difficulty of their dives. Alan Greenspan has done well executing a series of swan dives and jackknives, but it was Paul Volker who pulled off the triple somersault with reverse twist. It takes a trained eye to perceive the difference, which is why Olympic divers are judged by other divers rather than by writers.

(Paul DeRosa began his career in the securities industry as the money market economist in Citibank's bond trading division. He later became the bank's chief proprietary bond trader and subsequent was named head of Citibank's financial derivative and capital markets businesses in North America. In 1986, Dr. DeRosa joined E.F. Hutton Co. as co-head of bond trading with particularly responsibility for mortgage trading and finance. In 1989, Dr. DeRosa helped to establish Eastbridge Holdings Inc., a bond and currency trading company in New York, where he eventually served as CEO. Dr. DeRosa holds a Ph.D. in economics from Columbia and has served as a staff economist for the Federal Reserve Bank of New York.)

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Bear-Baiting in the Grisly Market

By Victor Niederhoffer and Laurel Kenner

Columnists

01/29/2001 09:09 AM

The Puritans hated bear-baiting, not because it gave pain to the bear, but because it gave pleasure to the spectators. Macaulay, History of England.

At great cost to their personal safety and wealth, Laurel and Vic have been betting on bear-baiting since March of last year.

Every day of the week, they climb downstairs into a basement room, where dogs of every breed nip at the heels of a chained, muzzled bear. The dog owners call out their fighting records before the match, and the bears often go berserk with rage. The fights are cruel.

We're not talking about one of those old Bowery dives where sailors were given chloral hydrate before being robbed. In fact, bear-baiting mostly disappeared around the Civil War, replaced by terrier matches with the rats that were to be found in abundance around Lower East Side betting establishments. Nowadays, we wouldn't put up with such cruelty to animals.

No, we're talking about the stock market.

Bearing Witness

After their sport was banned for good, bear owners thought the market would be an ideal venue, and they're always attempting comebacks. They tried in October 1987, October 1990 and October 1997. But they had no real success until last year, when the bears came back to play havoc with the Nasdaq.

The Naz dogs of California lineage had the worst time of it. They were lucky to escape with half their limbs.

The fights are still going on this year, but things are different. One dog company after another has been reporting the kind of bad earnings that the bears would have eaten them for just last year, and living to see the morning. Last year, when those dogs lost their footing in the bear's presence, the owners had a dead animal on their hand. This year, even weak dogs are staying alive. Not only that, they're being showered with gold coins.

Take, for example, how the market has been treating some of the tech dogs:

- JDS Uniphase (JDSU), Jan. 25: Says 2001 sales may be disappointing.
Reaction: Up 8%.
- Intel (INTC), Jan. 17: Analysts cut earnings estimates after company says it will spend more on equipment this year.
Reaction: Up 18% in next seven days.
- Teradyne (TER), Jan. 17: Warns it will miss fourth-quarter estimates.
Reaction: Up 8% in two days.

- Advanced Micro Devices (AMD), Jan. 17: Misses lowered estimates.
Reaction: Up 22%.
- Xilinx (XLNX), Jan. 17: Sales fall short of reduced estimates.
Reaction: Up 12%.
- Gateway (GTW), Jan. 11: Cuts 2001 growth targets for second time; Profit is one-third of forecast.
Reaction: Up 15%.

Dogmatic View

And then there are those Internet dogs. One, Webvan (WBVN), is so emaciated that it has lost 96 pounds in the past year. Every day, it loses more calories and dollars than the air it breathes in. Yet this year, it is steadily regaining weight.

Same story with XDOGS Inc. (XDGI), a company that sells outdoor clothing over the Internet. It, too, lost 96 pounds in the past year, but has doubled in size in 2001.

Would you believe that Vic secretly has an ownership interest in many of the Internet dogs? And he's made lots of money from them. He's been selling them furtively, and it's all perfectly legal.

He originally owned 15 dogs. Then, when no one was looking, he sold six of them at triple the price he paid late last year. And the bear just stood idly by. Refused to swat at those dogs. Refused to snarl at them.

Then Vic started selling shares in the remaining dogs. First a half interest. Then another half. Then another half.

Then he went into a gambling room in New York's worst hellhole, right next to Wall Street, and he dutched the remaining ones. That is, he hedged his bets by selling a basket of Internet securities (HHH).

It's a trick he learned from a bookie and a racetrack gambler named Pittsburgh Phil. They taught Vic that you can bet on the other side so even if your dogs get eaten up you don't lose.

Getting the Dogs Fixed

Needless to say, the authorities are trying to put an end to these games. But they're doing it by going after the dog owners. Fact is, a judge from Washington, name of Jackson, ordered the Gates dogs (MSFT) to be cut apart into three pieces, and he threatened to fine Gates his whole net worth.

Jackson worked with an old Doc in Washington in the crackdown on dog owners. The Doc forced the barkeepers to raise the entry fee to 6%, 7% and 8% just to get into the ring. None of the dogs could get a running start. The owners lost half of what they had.

But then, wouldn't you know it, the Doc heard that an ambush was in the works for him. So after pretending he wasn't going to change, he surprised everyone and let things go back to the way they were. And it looks like Old Judge Jackson is going to be put into retirement, after *The New Yorker* wrote an expose about his bias against bear-baiting.

The devil carries a long spoon, however, and even as we speak he may be meeting with his lieutenants. Don't ever count him out. Especially remember that if he returns, he likes to torture you by giving you hope. Just like the old bunco game operators would let the player win steadily for awhile and then deal

him a "27," which meant he had to put up in cash a sum equal to his total winnings to stay in the game. The mark always did put it up, and he always lost that hand.

Inside Info

Keep the devil in mind as we offer you a Mephistophelean bargain. Yes, it's another Internet stock. And appropriately, it's a dog in which Gates has a \$50 million interest. Better yet, Aether Systems (AETH) also is in for \$10 million. Almost all the Wall Street analysts hate it. The company just said Jan. 16 it would fire 11% of its workforce because of the economic slowdown.

But a couple of insiders each bought more than 660,000 shares at the end of the year, and we have found that that's one of the very few tells that work in dens of iniquity. And insider buys are rare lately, exceedingly rare. What's more, the stock hasn't jumped this year the way Vic's first set of dogs have. We therefore recommend Usinternetworking (USIX).

We also recommend Ivax (IVX), if it falls a few points below the current level of 36. Neil Flanzraich, the president, has been buying, and his buys have served as good signals in the past.

One of the ways the devil gives mortals hope is to go up three weeks in a row on occasion, the way he did as of last Friday. That has happened only 30 times in the last six years, and it has been relatively bearish. So beware. We therefore suggest waiting to buy both Usinternetworking and Ivax until the close on Wednesday, Jan. 31, when the Doc in Washington has left the stage and the month is over.

In another room in the gambling den, AT&T (T) will be reporting earnings tomorrow, and will hold a conference call at 8:30 a.m. Last week, it was reported that Mr. John C. Malone sold 1 million shares on Dec. 12. Last time he sold a million shares, on June 20, the stock fell 49% through the end of the year. He sold 3 million last January, and he's still got 26 million left.

Another AT&T director, Amos Hostetter, *bought* a total of 4 million shares in November and December.

Place your bets, ladies and gentlemen.

End Note: Vic visited the bear's den over the weekend. Walked right into Humbug Square in Atlanta, which was the capital of bear-baiting before the Civil War. General Sherman burned it down and put an end to it. Now the square is the site of an exhibit called "The World of Coca-Cola," which Vic attended accompanied by the great tax attorney and merger maker Lee Henkel in celebration of his 50th wedding anniversary.

Speculator's Scorecard				
	Days Up/Days Down Ratio (YTD)	# Days in Latest Streak (YTD)	% Change YTD	% Change (last 10 days)
Dow	0.83	Down 1	-1.2	1.3
S&P 500	1.44	Down 2	2.6	2.8
Nasdaq	1.20	Up 1	13	5.9
Europe STOXX-50	0.83	Down 1	0.0	1.9
Dollar/euro	1.00	Up 1	-1.9	-2.8
Nikkei	0.91	Down 4	-0.7	2.6
Dollar/yen	0.69	Down 1	-2.8	0.6
Gold	0.77	Down 1	-3.4	-0.5
Oil	1.20	Up 2	16	3.5

Bond Futures	0.50	Down 1	-1.8	-0.1
2-Yr Note Futures	1.00	Up 2	0.4	0.1
Bund Futures	0.75	Up 2	-0.1	-0.2

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Garden of Eden Market Ripe for Snakebite

By Victor Niederhoffer and Laurel Kenner

Columnists

01/30/2001 10:10 AM

Two passages, one leading into Elysium, the other into Tarturus.
Broughton, *Letters* (1599)

The market has been moving in recent days as if it has already landed in the Elysian Fields. Every day, another year-to-date high. Another bad earnings report disregarded. Another mutual fund manager joining the bullish camp. Another analyst pointing out that we are in a falling interest-rate environment.

Our own Internet portfolio, now fully hedged, is up 112% (up 224% if bought on margin as advised) and our Other Worldly five-stock portfolio is up 21%, both in just a few weeks.

Yet we have doubts as to whether the market will continue in this perfect state of happiness today and tomorrow.

S&P 500 futures are up 2% in the past six days, bonds down 3%. Such divergences are usually not bullish. Nor is the absence of a big decline since Jan. 5. Nor is the end of the month.

Apple Defies Gravity

As the Fed gets ready to lower the funds rate once again tomorrow at the conclusion of its two-day meeting, we remind ourselves of Rule No. 1: Never sell short; and Rule No. 2: When in doubt, go back to Rule 1.

Nevertheless, we can't help noting that Apple (AAPL) has risen 52% since we recommended it on Dec. 18. The gain is about in line with everything else we've recommended in the last month. For those lucky enough to have followed our guidance, we might advise considering taking profits on the stock.

Of course, we are sticking to our higher purpose of guiding readers so that they never are without a nickel to pay Charon for the ferry ride across to the other world. We'll refrain from more specific advice, concentrating on meals for a lifetime rather than a meal for a day. That is, until Wednesday's close, when we plan to be highly bullish again.

Today, we're tempted to go fishing. Instead, we will turn to one of the experts who have kindly been inspiring us this past year, making this column a linchpin for the discerning reader to tap into the ever-changing, dispersed and specialized knowledge that dwarfs what we, or any columnist in the world who doesn't tap into and encourage readers' feedback, might provide.

Flicking Off Risk

This expert, the young-hearted 70-something Bill Haynes of California, was in the midst of a discussion about a Web site (www.riskgrade.com) that evaluates the relative risk of a particular investment compared with a wide segment of the market. Bill, a former fighter pilot and aerospace engineer who knows something about risk-taking, asked: "How is that advantageous for an investor?"

Evaluating risk alone isn't likely to help much, and by the time you're done comparing other important

qualities to the broad market sample, the chances of finding a golden stock among the dross are close to zero, Bill wrote. And circumstances may have changed by the time comparisons are performed.

His own approach, he writes, is to track rapidly developing technology and investigate the companies at the cutting edge. "Usually there is one, perhaps two, rarely more than three that are leaders. I look into their history, the company Web site, their corporate leaders and statements, their patent portfolio and the prospects for fairly near-term breakthroughs. Also, are the big guys in related fields investing in them? If I see the potential for a real PR blast developing and boosting the stock up multiples, I buy it. Then I hold on to it."

That technique made Bill an early investor in Qualcomm (QCOM). Right now, he is holding Geron Corp. (GERN). "I really think this is the pack leader in what I expect will be an exploding biopharmaceutical market in the next few years." The stock is at 19 5/8 now, down from a high of 75 7/8 last March. Bill expects "spectacular returns from one or more truly fantastic but real possibilities: cancer cure (all types), human-life extension and farm-animal-cloning technology licensing."

He also owns SpaceHab (SPAB), which makes laboratory modules for NASA's space shuttles. The company's most intriguing project, though, is a communications center that will be part of the International Space Station, where SpaceHab's civilian astronauts will conduct streaming video programs for the public's enjoyment.

Incapable Apes

Bill's *idée fixe* is somewhat similar to that covered in books such as *The Gorilla Game*, by Geoffrey Moore, and *Quantum Companies*, by David Silver. The idea behind these methodologies is to find the market leader in an exploding market, one with proprietary technology that customers decide would be too expensive to switch from.

It's easy to recognize retrospectively, from the comfort of the armchair, that Intel (INTC), Microsoft (MSFT) and Cisco Systems (CSCO) were destined for gorilladom. But *The Gorilla Game* also names Etoys (ETYS) and Priceline.com (PCLN) as not just gorillas of the future, but godzillas. Both have lost wider than 95% of their value in the past year.

Companies recommended by tech guru George Gilder lost 70% to 80% of their value last year, and they had gorilla characteristics. The roller-coaster performance of the Gilder picks are tracked on Dick Sears' non-commercial site, www.gtindex.com.

Clearly, it's not so easy. But someone like Haynes, who knows his fields and goes to all that extra work, is likely to have more success than someone who relies on retrofitted formulas that were designed for finding the gorillas of the 1990s.

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Nasdaq	1.30	Up 2	15	8.1
Europe STOXX-50	0.92	Up 1	0.3	1.4
Dollar/euro	0.92	Down 1	-2.5	-3.4
Nikkei	1.00	Up 1	0.4	2.5

Dollar/yen	0.77	Up 1	-2.3	1.1
Gold	0.77	UnChg	-3.4	-0.2
Oil	1.09	Down 1	13	1.0
Bond Futures	0.47	Down 2	-2.1	-0.5
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Ugly Facts Meet Hypotheses

By Victor Niederhoffer and Laurel Kenner

Columnists

01/31/2001 10:10 AM

Whenever you can, count. Statistics are the only tools by which an opening can be cut through the formidable thicket of difficulties that bars the path of those who pursue science.

-- Francis Galton

The markets have been providing a thicket of difficulties in recent days for the young-hearted as well as the Spec Duo.

The divergence between the super-performance of the Dow, the fine performance of the S&P 500 and the lackluster performance of the Nasdaq during the past two weeks is enough to put a cane in the hands of the young and a spring in the step of the old.

Consider: The Dow yesterday registered its largest rise since Jan. 3. The S&P had its 15th consecutive trading without a decline of wider than 0.5%, a record. The Nasdaq, on the other hand, is unchanged from the 2,700 level of nine days ago.

Rather than burying the head in the sand or, worse yet, resorting to the easiest thing in the world for market commentators, description, we will take out the needle and index card as recommended by Francis Galton (he was too much the Victorian gentleman to offend sensibilities by counting publicly with a pencil and paper) and count.

For many too many days, we have been reporting the relatively bearish significance of new highs in the market in conjunction with the absence of a good-sized decline. Yes, the face is red, and yesterday's large up-move in bonds changes the scale of evidence considerably.

Ugly Facts

So let's turn first to something new, an event that comes only 12 times a year: the last trading day of the month. The folklore is that a certain washed-up hedge-fund operator liked to sell the market at the end of the month and that this created bearish waves. Counting, however, leads only to what Huxley calls "the great tragedy of science -- the slaying of a beautiful hypothesis by an ugly fact."

Turns out that the actual move on the last 72 end-of-month trading days is about as close to zero as could be: up 48% of the time, with an expectation of a loss of 0.1%. The only non-random phenomenon evident from the record is that things tend to get a little dodgy near the end of the day. That's exactly when the Fed will be announcing its politico-economic decision on rates, adding to the unpredictability of it all.

Continuing the counting, but this time classifying by ends of months after strong up-days -- as transpired to our cost yesterday -- a slightly more bullish tendency emerges.

Turning to the divergence between the S&P and Nasdaq, we count 40 occasions like yesterday, when the S&P was up substantially and the Nasdaq was down. The realizations in the next few trading days are slightly bullish for Nasdaq and slightly bearish for the S&P. Same results vis-à-vis the divergence over the last five trading days.

Next we turn to an interesting numerical hypothesis kindly submitted by one of our good readers, Mr. John Lamberg, a program developer from Minnesota. "Three minutes for a lunch of three chili dogs, nine minutes per e-mail and 36 months per trade. Good things must come in threes (or multiples thereof)."

How to test this rich hypothesis?

Three-Dog Day

Let's start with the 144 occasions the market ate three hot dogs in a row by going up three nice days in a row. The same way it would be if it were to defy our expectations and go up today. In subsequent days, the market is slightly bearish.

This sounds promising, and we will be asking Mr. Lamberg for further uplifting insights on using and fine-tuning his hypothesis.

All this is overridden today by the important announcement of how much the Fed will be reducing the funds rate, scheduled for today at about 2:15 p.m. New York time. Last time the Federal Open Market Committee made an announcement, on Dec. 19, the market promptly declined 4% in the next hour. But looking back over the last 30 announcements, the average change is exactly zero.

Thus, after all the counting we will close with a qualitative assessment. The market is unusually optimistic right now. Every commentator, and his sisters and his brothers and his cousins and his aunts, is bullish right now because the Fed is in a rate-cutting mode. The expectation is for a strong half-point reduction today.

Granted that a half-point cut is likely. But the Fed likes to maintain its Delphic aura, thereby increasing its power and purse, by mixing seemingly bullish reductions with ominous verbiage.

A Wish to Fish the Pier

Recognizing this, we've been tempted for the past couple of days to leave the market alone and go down to North Carolina for some fishing. But we were dissuaded by this late-breaking dispatch, relayed by a young-hearted correspondent, Mr. Peter Daniels: "The fishing has been stopped on the Outer Banks for the last 24 hours. The Fishing Hotspot is None -- all areas are stopped." As Mr. Daniels observed, "I guess the fish are waiting on Greenspan today."

Taking one consideration with another, we're issuing yet another negative forecast for today -- to be followed, of course, by fantastic bullishness after the fear is put back.

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Dollar/euro	1.00	Up 1	-1.6	-1.6
Nikkei	0.92	Down 1	0.3	1.8
Dollar/yen	0.85	Up 2	-1.5	1.1
Gold	0.85	Up 1	-2.3	0.9

Oil	1.09	UnChg	13	2.0
Bond Futures	0.53	Up 1	-1.1	0.3
2-Yr Note Futures	1.10	Up 1	0.5	0.2
Bund Futures	0.92	Up 4	0.3	0.4

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