The Mania Chronicles

Reflections of a Skeptic through the Mania and Beyond

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Chapter One: The Building of a Mania

Period of October 1998 through August 1999

Though the longest bull market in U.S. history closed at new highs on July 20, 1998, recent world developments have draped a pall over Wall Street just a few short weeks later. By early October, the S&P 500 is down 19 percent, the Dow down 17 percent, and the Nasdaq, having punched through a 2000 print at its July high, has taken a 25 percent beating. While the market has rewarded investors with impressive gains since the early 80's - even more so since 1995 - there is a contemplative sense that this great period of U.S. economic expansion, and thus the stock market ascent, has reached its limit.

The concerns are not frivolous. As the world has progressed into a global economy, individual economic meltdowns ricochet across the boundaries and onto the shores of other countries. The economies of Asian countries, Indonesia, South Korea, Malaysia, Thailand, the Philippines, Hong Kong, and Japan have fallen like dominoes in a burst bubble aftermath. Russia has defaulted its debt and devalued the ruble. Consequently, the markets are wild and whippy as people all over the world, it seems, are rushing to the safety of cash and U.S. Treasury bonds.

There are troubles here at home too. Profits for 900 companies on *Business Week's* Corporate Scoreboard dropped four percent in the third quarter as compared to a year earlier. A glut of crude oil has reduced the earnings of coal, oil, and gas companies, while imports of cheap steel have knocked profits for that industry. And there is the not so inconsequential problem of computer chip supply – which is to say – there's not enough demand for it. Overcapacity of microchips has taken its toll on semiconductor profits; they are down 45 percent. As the U.S. economy slows, pink slips have been issued across a multitude of industries – manufacturing, finance, computers, telecommunications, and oil services.

Main Street America is obviously feeling the pinch, yet it's nothing compared to the chokehold gripping Wall Street. Though it's rather hushed at the moment, the private hedge fund, Long Term Capital Management, is in big trouble. Brilliant, greedy, smug in their own perceived infallibility, and over-leveraged through derivatives beyond any sane measure of risk, Long Term has found itself the wrong way in nearly every position it is involved - and they never wager small. The current global market volatility is precisely the trade Long Term seeks to short, but they have seriously underestimated how dicey it can get, how long it will last, and how much pain they can tolerate.

A private hedge fund's predicament shouldn't cause even a blip on the market's radar, and indeed, most Americans know nothing of any *real* financial crisis, much less ever heard of this obscure hedge operation, Long Term Capital Management. But the problem is that Wall Street's most notorious banks, enamored by Long Term's heretofore-spectacular success, had also believed Long Term too big and too smart to fail. They have been quickly reminded that the market is like the ocean - it respects no individual. Worse, they have met the sickening realization of the extent they are adversely exposed to Long Term's sinking ship, and now they too, are racking up heavy losses on a daily basis.

Wall Street is white-knuckled and praying for an easing of U.S. monetary policy. While cutting U.S. interest rates can't fix the rickety financial architectures, nor cure the economic diseases plaguing the globe, it will provide liquidity, mildly bolster foreign currencies, and hand a psychological trump card to the investing public. It is the easiest solution, as opposed to enacting difficult, though necessary, financial reforms. More telling, it is one tactic Alan Greenspan is well inclined to employ, and Wall Street knows it.

As is their wont to do, the Federal Reserve Board cut interest rates 25 basis points in response to the pleas of Wall Street campaigners in late September. Wall Street insiders and apparently even the Fed itself feared a world financial system collapse. If a well-timed interest rate cut would help the markets settle down allowing Long Term to stay with their trades, become solvent again, and perhaps even change the stock market's course from due south back to due north . . . well, what's a little interest rate finagling? Wouldn't everyone be better off?

Investors remained a bit timid to step back in after the September easing, but on October 15th, the day before options expiration, the Fed released a memo at 3:04 in the afternoon announcing another 25 basis point cut. Market participants now clearly understood the Fed's stance. It would do whatever it deemed necessary to restore confidence in the financial markets. The surprise move sparked a panicked buying frenzy for equities by options traders, short sellers and speculative longs because the historically bullish seasonal period was fast approaching, technical traders were very pleased with their charts, and best of all, the Fed had just flashed a green light to get long the stock market.


Dow Jones Industrial Average Index, Weekly
The collapse of Long Term Capital Management and the Russian debt default had people spooked
9000.00
7899.52
7000.00
6000.00
5000.00
4000.00
Jul Oct 1995 Jan Apr Jul Oct 1996 Jan Apr Jul Oct 1997 Jan Apr Jul Oct 1998 Jan Apr Jul Oct


S&P 500 Index (CBOE), Weekly
and wondering if at long last, the bull market was over.
But they had no reason to worry;
1200.00
984.32
800.00
600.00
Jul Oct 1995 Jan Apr Jul Oct 1996 Jan Apr Jul Oct 1997 Jan Apr Jul Oct 1998 Jan Apr Jul Oct


Nasdaq Combined Composite Indx, Weekly
afterall, who could have known?
These lows were merely the launch for a moonshot.
2000.00
1800.00
1600.00
1492.49
1400.00
1200.00
1000.00
800.00
Jul Oct 1995 Jan Apr Jul Oct 1996 Jan Apr Jul Oct 1997 Jan Apr Jul Oct 1998 Jan Apr Jul Oct

Alan Greenspan Rides in on a White Horse . . . *(October 16, 1998)* The Federal Reserve has now become a cross between the Hong Kong Monetary Authority and the Ministry of Finance in Japan. We too, now have an official price-keeping operation. From last Thursday's lows to yesterday's highs, the S&P 500 has rocketed 17 percent, the effect of this most recent manipulation.

My objection isn't to the cut itself. The economy is weak and everybody knew that ultimately, the Fed was going to act. My complaint is the *timing* of the move and what it means. The Fed's timing was for one reason only: to manipulate the daylights out of the U.S. stock market. What else can you call it when it eases at a time guaranteed to produce an epic rally – this one launching a five percent move in five minutes? The announcement came just forty-five minutes before the close prior to an options expiration day; that, in my opinion, is a blatant move, the sole purpose to juice the market. Once you know a market is being manipulated, you lose faith in it. It is the same as not being able to trust someone who has lied to you.

It’s rather apparent to me that this surprise cut is yet another bailout in progress. Why else would the Fed have done it? Obviously someone is in a lot of trouble. In all likelihood, a big bank or money manager has an equity derivative book that is horribly offside, in addition to facing trouble in other derivatives. So the Fed has launched an assault on the stock market, jamming it higher and thus, at today’s expiration the massive equity derivative book isn’t nearly the loser it would have been.

We know the Fed intervenes in the currency markets. We know that it intervenes in the fix-income markets. We know that other governments intervene in the gold markets. And now we know that the Fed intervenes in the stock market and is therefore in the business of manipulating all markets. Once you begin to step in, there is no turning back – you have to keep going. They’ve created the moral hazard through bailouts like this, diminishing and socializing the risk of speculation. It’s the principal reason why the public feels that it cannot lose money in the stock market over time.

Markets in Party Mode . . . *(November 4, 1998)* In addition to a gargantuan amount of short covering, it appears that we are trying to speculate ourselves to prosperity through flights to speculative and trash names. The more speculative the name, the better it performs. Internet stocks are strong and Yahoo! (YHOO) is now up 150 percent from the low it touched back in August.

It Don’t Matter to Me . . . *(November 5, 1998)* Let’s look at what matters on Wall Street and what doesn’t. The truth is - nothing matters. The only thing that propels stock prices these days is the game called *Make the Number*. Here’s how it works: Presume ABC stock starts the quarter at $10, and by some great act of levitation, goes to $50. Say the estimate is a whopping two cents, the stock will continue higher, because how much they make has no bearing on how much the stock should sell for. All that matters is, do they make or beat the number at that moment in time? If by some odd happenstance they miss the number, it is deemed to be OK, under two circumstances:

First, it is OK if they miss the number due to an extraordinary charge, for example a merger or writing off old research and development costs, or employee severance, or anything else they can make up. Second, it’s OK to miss if things are about to get better. How do we know if things are about to get better? We don’t. But as long as we can make up a big story that things will get better, then it is OK to miss the number. The only time it isn’t OK is if you miss with no explanation, or hide it with some accounting nonsense.

Then we move on to the next quarter, where the stock is free to go up five or ten fold again. As long as we can make or beat the number again, the stock never will have to come down. So stocks can go up forever as long as you can steer Wall Street to the number. We have created a wonderful, financial perpetual-motion machine.

Let’s not pretend that it has anything to do with investing; for example finding companies with barriers to entry or new products, or sound management. We don’t need an understanding of the world or have to know whether the U.S. economy is contracting or expanding, or if the geopolitical environment is friendly or if we have any currency risks, etc., etc. Don’t bother thinking about that, because it doesn’t matter. All that matters is, can you make the number?

In the Land of Make-Believe . . . *(November 10, 1998)* Speculation continues to run hot and heavy. The star of the day goes to EBAY, which was up $28 to $131. Just 32 days ago the stock was at $25. Wire-to-wire melt ups levitated Microsoft (MSFT), IBM (IBM), some of the semiconductor capital equipment and the biggest speculative joke in chipland, Micron (MU). It was quite a day for fairy tales. Speaking of which, the Internet stocks were on fire. Yahoo (YHOO) was up about six percent while other Internet want-to-be's like K-Tel and Egghead Software (EGGS) charged higher as well. Some of these names have had years' worth of moves compressed into a month. This is truly one of the most breathtaking things that I have ever seen. It wasn't this crazy in Tokyo, folks.

Fed Does It Again . . . *(November 17, 1998)* The drunks at the FOMC did the irresponsible thing again by cutting rates. The same drunk who discussed irrational exuberance back at 6300 has seen fit to slash rates by a total of 75 basis points now succeeding in getting the largest-of-all-time bubble moving higher even more quickly. With this latest quarter percent cut, they made the following statement, "Although conditions in financial markets have settled down materially since mid-October, unusual strains remain."

Sure. We have complete unbridled speculation in the Internet sector, the Nasdaq 100 is up 52 percent year to date and we've seen total melt-ups in some of these narrow indexes; the SOX is up almost 100 percent since its October lows. And these morons at the Fed are talking about unsettled conditions.

My friend Colin Negrych was quoted on Bloomberg about Fed Chairman Alan Greenspan: "He appears to be trying to print enough money to make the consequences of his multiple errors over the decade his successor's problems. When you dig yourself into a hole, you can stop digging, but when you blow a bubble, you can't stop blowing, at least until your retirement is imminent."

Down the road, when we have the worst financial fallout since the Depression, you will know whom to blame. The irresponsible fools at the Fed have spoken and we, and all of our kids, are going to live with the consequences.

The Internet index is now up over 100 percent since the October 8th low, just thirty-five trading days ago. The Tuesday and Wednesday prior to the Thanksgiving Day holiday – the 23rd and the 24th – saw many spectacular moves in Internet related stocks.

It's Like the Belmont Stakes . . . *(November 23, 1998)* Amazon (AMZN) was the first to $200/share although it's been in a tight race with Yahoo (YHOO) for the trophy. Yahoo had been in the lead, but Amazon closed the gap and was the first one to trade over the mark. Though Amazon.com was the first to $200, Yahoo wound up winning the high-price-of-the-day game, closing at $221-plus versus $218 for AMZN. Literally, over the course of the day, you could watch these two stocks trade side-by-side and it was as though speculators were buying one stock against the price of the other. EBAY tried to keep up but closed the day at $192, up $46. It failed to make $200, but what the hell - that's why we have tomorrow, right? [EBAY closed at $210 the next day.]

Talk Trashy to Me . . . *(November 30, 1998)* Although I wasn't in on Friday, [following the Thanksgiving holiday] I can't help but comment on some of the activity. We had the Internet trash stocks, some from the crop of a couple of years ago, going absolutely berserk. Some of them were up over 100 percent on that day alone. If you wanted to be on the top 15 gainers on the OTC market, you had to be up about 46 percent.

The stock market has now reclaimed all lost ground from the fall's swoon and is back to the highs of the summer. The public has noticed the sharp recovery and is anxious to be a part of a strong bull move. As individuals jump into the fray, they believe they are wisely investing because in their minds, participation in the stock market is always an investment. It's not. In this environment, it's gambling in a pyramid scheme, but few have the experience to know this.

Investing, Informed Speculation and Gambling . . . *(December 1998)* Let's clarify the distinction between investing, informed speculation, and uninformed speculation and gambling. Value Investing is the process of doing research to identify opportunities that have a favorable risk-reward ratio. It is about probability management. It's about finding attractive entry points to buy sound businesses cheaply enough so that if you are wrong, as we all are on occasion, you are protected in not losing too much. And yet, if you are right, you enjoy a large payday. The gains are large enough to offset the occasional loss because your losses have been kept manageable because your investment had inherently low downside risk.

Next, there is informed speculation. You have done a lot of work, but the investment is nevertheless, very risky. Short selling falls into this category, that is, provided you have done your homework and know a lot about short selling. By definition, short selling is riskier because loss is potentially unlimited, and of course, we are presently battling a mania where anything flies on a wink and a nod.

You can be an informed speculator on the long side as well. For example, after doing your homework, you may think that a takeover is on the horizon. Though you've researched, it is still speculation. Small-stock investing or venture type investing also falls into this category.

Finally, there is uninformed speculation, which is what is happening today. Hundreds of millions of people are "playing the stock market." I'm not trying to say that I'm any smarter than anyone out there, but the reason is simple that I call it uninformed speculation. I get questions all the time from individual investors asking about certain companies that they own. I ask them if they know anything about the company itself. Market cap? Revenues? They never know. Just hearing about a company and then buying its stock does not constitute research. Peter Lynch has made the point in the past that people should buy things that they are familiar with. Unfortunately that is where people have stopped, failing to take the next step. Lynch says to buy things you are familiar with and understand due to research. How can an individual consider himself an investor when he doesn't know the basic fundamentals of a company, much less earnings, prospects, management's capabilities, and any barriers to entry?

This is the environment. It is total rank speculation and therefore it isn't surprising that any stock can be kited up to any price. The business and economic conditions are not favorable for value investment and what has become so exasperating is that presently companies have taken to lying about their prospects in order to prop their stock prices. Research analysts believe the lie or don't know any better because they don't do any homework, and then, when the company hits the wall, analysts complain that the company misled them. The company then turns around and blames Asia. It's all such a joke.

As long as companies are willing to say anything or give the right body language, folks jump on the stock. This is gambling. The moral of this story is that you should not trust analysts. They're just Wall Street's cheerleaders. They are out to sell stock and help the corporate finance departments. Wall Street research is a perfect oxymoron and it's getting worse every year. They're not there to help you.

I'll grant that there are some good analysts; most of them though, can't talk about or don't know what is really going on and few have been tested by tough times as the market and the economy have been great for so long. You need to make note of a good analyst because he will make you real money over time; however, in this environment, they're vilified for ever asserting something negative even if it is accurate. Also remember that you cannot trust corporate management either until they **prove** to you that they value truth and their business more than their own stock price.

And just for the record, there is nothing wrong with speculation, per se. It goes on in various forms all the time. The problem arises when the percentage of speculative activity becomes far too high. What is "too high?" I can't tell you an exact number. It's kind of like pornography; you know it when you see it. Right now, in my opinion, some huge percentage of what is going on is speculation. It isn't just in the Internet stocks; people are chasing price action all over the tape, wherever they can.

When speculation is this ubiquitous, it changes the psychology and becomes unhealthy and dangerous. I am not against speculation, but when the entire market becomes a speculative mania, it always leads to a ***decade*** of trouble and that, of course, is the problem. While it seems like so much fun, when the party is over, everyone will realize that it was an egregious mistake. Ask the Japanese. This forms the basis of my entire complaint; the aftermath of a bubble bursting is a problem for everyone. If I choose to stay out of what I perceive to be a bubble and I miss out by being wrong, tough luck for me. But if by being irresponsible, the authorities allow a bubble to take place, everybody has to pay in the aftermath. That isn't right.

According to the Purchasing Manager's survey, manufacturing has been in a contraction for the previous six months. Consumer confidence, while high relative to historical standards, has fallen from its summer peak. In the political arena, the United States Congress is in the process of impeaching President Clinton for lying under oath about his relationship with White House intern, Monica Lewinsky. The whole scenario is a drag on investor, business and consumer confidence. Though equity valuations are at or near record highs, several high profile - in fact, twelve of thirty Dow composite companies - have warned of revenue and earnings shortfalls.

Ode to the Consumer . . . *(December 11, 1998)* In the real world, things get worse, but in the stock market, things just get better. What's keeping things together right now is the consumer, spending more than he makes, I guess because he thinks that he can get rich in the stock market. A lot of people have ridiculed the personal savings rate numbers because they're not well concocted. While that is true, at least the methodology's been consistent over the last 50 years, and consequently the savings rate has gone from 7.8 percent at the high to minus 0.2 percent. It may not be the best number but it's very clear that the savings rate is down dramatically.

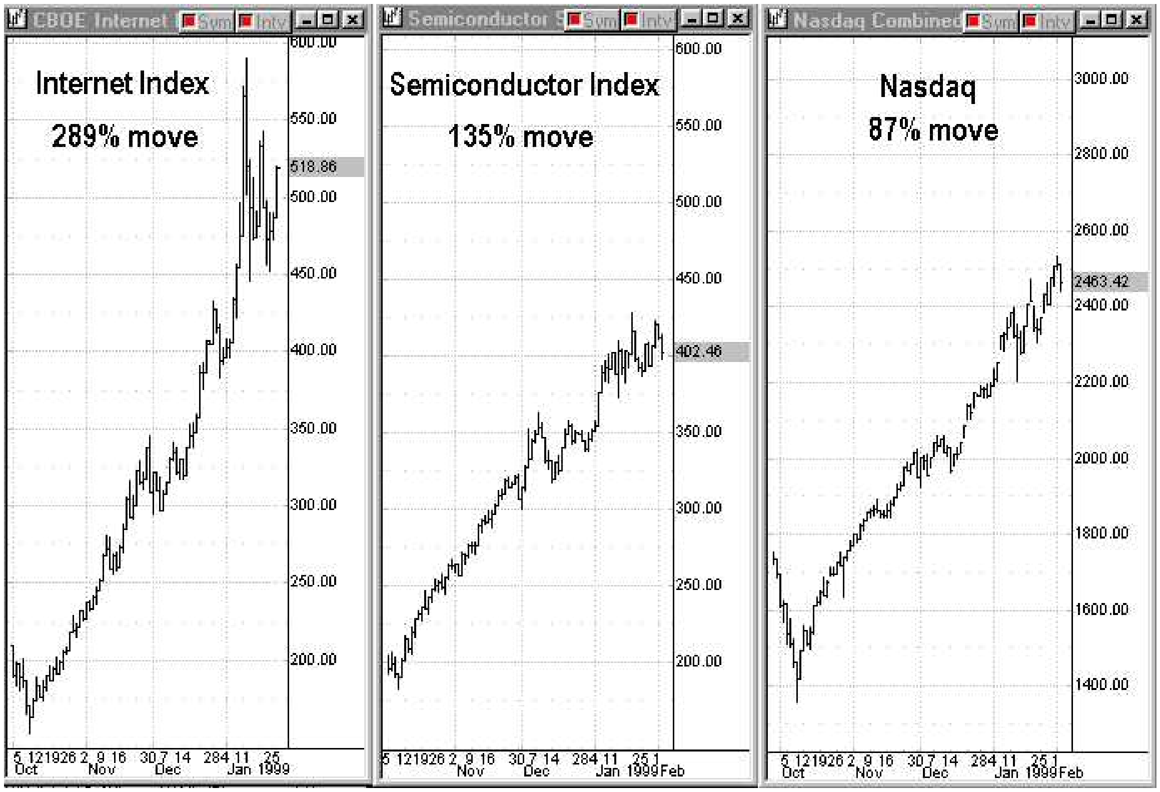
Tis the Season . . . *(January 8, 1999)* We're now in the favorable flow of funds season and imaginations are running wild. When speculators decided that they didn't care about any of the bad news, it gave the green light for everyone to go crazy. The Internets are just nuts. Amazon.com (AMZN) was up 40 points for a 60-point move in two days. The stock actually traded at $40 in November just to allow a visual of the sized moves we're seeing. However, after opening up a gargantuan amount, it finished the day up only about a buck. Going into the close it had been down as much as $5, so maybe it is due for a decent size pullback one of these days – even though I know that's not allowed.

Here's an interesting development. Broadcast.com (BCST) was up about 95 points when it was halted. The Nasdaq asked the company for comments about why the stock was up as much as it was, but the company said it didn't have anything to say about that, so it backed off some. Still, it's breathtaking when you see a stock trading at $230 per share up $95 on the day. [During the following session it was revealed why that move had happened.] The company, which had nothing to say about the stock's moon shot previously, decided to divulge that it was planning a two for one stock split. That made it good for another 87 points, which in turn, ignited all of the net stocks – YHOO up 72 points, Go2Net (GNET) up 54, Mindspring (MSPG) and Inktomi (INKT) both up 22. Amazon was a laggard, up only 24.

Semi's Rule . . . *(January 8, 1999)* Stocks within the Semiconductor index are now higher than they were when the business was booming back in 1995. But never let a few facts get in the way of a good party. People seem to have determined that the semiconductor business got so bad and now it is just slightly better so it must be getting ready to start a whole new cycle; the third or fourth new cycle in the last three years by their proclamation, though there hasn't been even one.

What this proves is that all stocks, in essence, have become Internet stocks. I have focused mostly upon technology, but we have examples of other companies: JC Penney (JCP) announced disappointing results yet was down only a dollar. Because folks have speculated so successfully in Internet stocks, and no unsavory news has hurt them, people now think all stocks can be bought, no matter what the price, regardless fundamentals, and that not only will they not get hurt, they will make money. I've been a little slow to realize this thesis that appears to be at work now, but that is it.

Save it for Posterity . . . *(January 8, 1999)* You folks at home should save the clippings of these moves from the newspaper, because when this bubble finishes, you won't see it again in your lifetime. It'll be a long, long time before we have another speculative period even remotely similar after this one melts down.

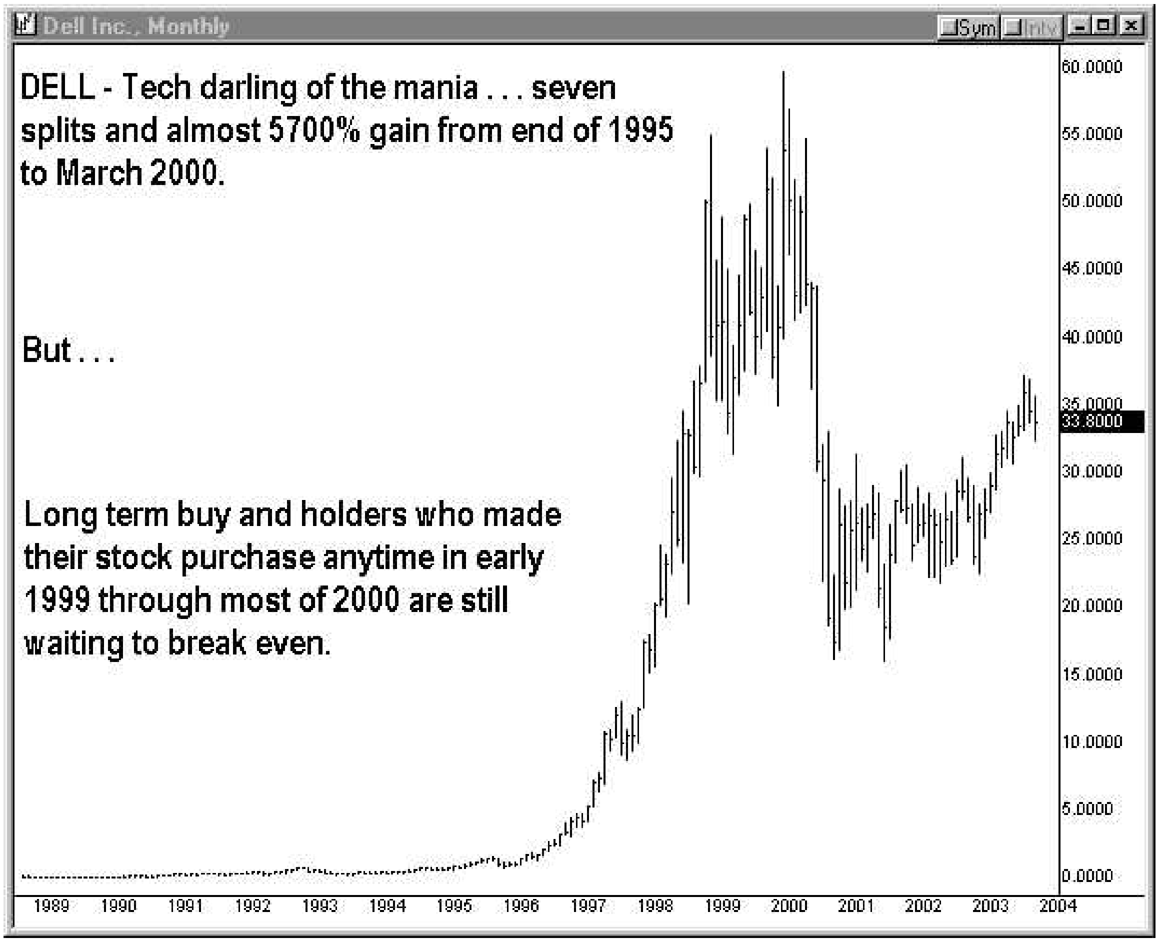


Doing the Splits . . . *(January 26, 1999)* Bill Clinton's motto, "It's the economy, stupid," wasn't quite right. It should have been, "It's the stocks splits, stupid." Xerox (XRX) announced a stock split, and the stock was up $11 in the early going; IBM (IBM) announced its stock split about an hour and a half into one trading session, and that got its stock going. McDonald's (MCD) and Merck (MRK) both jumped into the fray and announced two for one splits, which immediately moved MRK shares from down $0.50 to up $3.00 in just over five minutes. When Microsoft (MSFT) announced its blowout earnings, it wasn't enough to hold the stock up, and it promptly sold off over $10.00. Yet as soon as the company announced a stock split, it got back the $10.00 and more. Then people remembered that Yahoo is going to be splitting soon, and we shortly find ourselves in another wire-to-wire melt up.

So it is apparent that now, stock splits are the only thing that matter.

What Will They Think of Next? . . . *(January 26, 1999)* I guess we can expect that now every stock trading over about $20 is going to announce a stock split, and we can double the Dow on the back of just creating more pieces of paper. I mean, why not? It's about as intelligent as anything else that's going on in the stock market these days.

Dell-irium . . . *(March 8, 1999)* The most important company in Western civilization, Dell (DELL), had its 2-for-1 stock split today. In honor of this solemn occasion but due to the fact that I've been venting pretty heavily, I'll try to be brief. Dell is now higher than it was the day when it announced that its revenue growth, contrary to expectations, had slowed from the 50 percent into the 35 percent region. Its P/E is now back closer to 100. All this for a maker of commodity goods - plastic wrapped around chips. Dell is a $120 billion company that has nine percent market share of a $140 billion market. The fact that people now have two pieces of little paper instead of one big one has run the stock from $39 to $45 and counting.



Bear Attacks . . . *(March 12, 1999)* I was dumbfounded to watch Joe Kernen go after Bob Olstein of Olstein Financial Reports on CNBC's Squawk Box early this morning. Bob was going through accounting machinations and the book cooking that has been going on at Lucent (LU), warning folks about how illusory their earnings and earnings growth has been. Kernen promptly took him to task by saying, "Well, we know all that. Nobody cares - the price is where it is." Joe went on to make the point that anyone who talks about these things - and then the stock goes up - is just plain wrong. Therefore, anyone who has been negative is simply wrong because the market has gone up.

None of us knows where the market is going; none of us even claim to. We make our best educated guesses but the market is the market. What some of us try to do is research specific areas and point out potential faults. People have been slow to recognize a lot of those faults because of the ongoing mania in the market itself. What invariably happens to a stock like Lucent, where there are problems, is that one day we walk in, and the thing gets shredded. What is so lopsided about this environment is that no one ever takes to task the bulls who were busily touting the stock when all these things were supposedly known. The stock gets crushed and people just go their merry way.

Facts are facts. . . I guess if Joe Kernen had his way, everyone would always say everything is wonderful, and then no one would have any idea of which stocks to potentially avoid. It's absolutely ridiculous to try to muzzle people for bringing up facts - not opinions, but facts. It is getting completely of hand when people are personally attacked for being bearish on any subject. Enough of this lopsided treatment where the bulls can constantly be wrong on the facts, and when the stock prices implode, no one takes them to task and meanwhile, the bears are always being called on the carpet. That stock prices have not reacted to facts is testimony that we're in a mania where nothing matters. These are knowable business problems and eventually, they will matter - the key word being “eventually.” None of us knows the timing, obviously.

You are going to see so many examples of companies where you can say, “Well gee, we knew this and it can't be a problem because we knew it.” In a mania, nothing's a problem until everything's a problem, and then you have a total implosion. At that point, all you wish is that you had abandoned ship. We haven't seen that part of it played out, but I can absolutely guarantee you that it will happen - I just don't know when.

World Developments Dicey . . . *(March 23, 1999)* We've got problems in the Balkans and in the Middle East with Hussein. The Japanese are shooting bullets at North Korean vessels today too, so we've got a lot of dicey things going on. We've been trying to keep abreast of them for a while, though no one has much cared. In the old days, before we had stock splits and Internet stocks, these things mattered.

Still crazy for splits . . . *(March 2 9, 1999)* I must make just one more comment about the ridiculous religious fanaticism that is associated with stock splits. People continue to believe that a pizza with 12 slices is worth more than one with four, even though it doesn't change anything.

Microsoft has been the latest beneficiary of this split rage. Now, Microsoft has been and is a great company, but let's look at what we have here. Today, we have the happy event of Microsoft's (MSFT) long-awaited split. There are now over 5.6 billion shares of Microsoft fully diluted outstanding, and the stock is approaching $100, yet all the splitsters are probably looking for the next split. To put these big numbers in perspective, today's $3 move in Microsoft adds approximately the same value as one year's worth of revenues to its market capitalization. Microsoft's valuation now equals about $530 billion - which is approximately six percent of the gross domestic product of the U.S. It is hard to imagine how $18 billion in revenues could be worth this, especially when one thinks about the continuing collapse in the price of TV sets - I mean PCs!

Dot.com Foolery . . . *(March 29, 1999)* Finally, we can discuss the Internet stocks, which are in many ways the ultimate greater fool stocks. Nobody's making any money in these things and it's quite likely that no one will. There are very few barriers to entry. What it's all about is destroying profitability for businesses as middlemen are stripped out. It's a tremendous boon for the consumer, but it's not clear how anyone's going to make a whole hell of a lot of money, at least certainly not all these hundreds of companies with multi-billion-dollar valuations.

What people want on the Internet is stuff for free and things that are easier and cheaper. So far, I don't see anyone out there who's making a great deal of money, and anyone who's even close to making money has a valuation that is so absurd as to never make any sense. I'm sure I'll alienate some people with all this, but I thought it would be worthwhile to deconstruct some of the myths as to why stocks are such a great investment these days.

Roll Out a Red Carpet . . . *(March 30, 1999)* The IPO du jour today was a company called Priceline.com (PCLN). The stock opened at $85 and closed at $69, so some of the initial buyers didn't do so well. At $85, it had a market cap of over $12 billion, a staggering number for an IPO, even one that has as good an idea as this one appears to have.

Internet names did get a bit of a bid after Priceline became public. Obviously the logic is that if Priceline's worth $12 billion, then XYZinternetgiveaway.com is worth some big price. And if that one's worth some big price, then something else is worth another big price. The Internet stocks are all recursive, in that if one is worth a certain price, then another one is worth even more, and the next one is used to justify that one, and so on and so forth. In this way, Internet valuations are just a perpetual motion machine that, at the moment, seems to know no bounds.

IPO Machine in Motion . . . *(March 30, 1999)* Presently, it appears that there are over 250 IPO's in registration and my guess is that the overwhelming majority of them has something to do with the Internet. So all you Internet bulls out there, get ready. There's a whole lot more supply on the way. One thing you can always count on from Wall Street - it will create supply to meet any level of demand. My prediction is that somewhere in the next three months this Internet stock mania is going to be on borrowed time, because Wall Street will create a trillion dollars worth of paper if you give it an opportunity. After all, it takes about 15 minutes to start up one of these companies.

Jam Them Higher . . . *(March 30, 1999)* In a little bit of unreality this morning, both AOL and Amazon had their price targets raised. That's the newest form of research in the mania; we don't talk about fundamentals, we raise our price targets. Does anybody think it's a coincidence that all these Internet stocks are having their price targets raised right at the end of the quarter? Nah - I didn't think so either.

Yep, it's the end of the month, end of the quarter and the name of the game here is Heavy-duty Window Dressing. Usually the third and the second-to-the-last days are the most powerful. Most of the time they are not so blatant as to mark them up on the last day since the SEC and everyone else has figured that out, but it's really staggering to me that people at home probably have no idea of the complete disrespect with which their money is "managed" these days by mutual funds. Not to say that they are doing all of this, but I suspect that someday, after huge amounts of money are lost, Congress will decide to investigate market manipulation and this is where they're going to find some game. Of course, we'll never know for sure until somebody does look into it, and maybe it's not happening, but if it looks like a duck and quacks like a duck, my guess is, it's a duck.

Risky Business . . . *(March 30, 1999)* One thing that has been totally lost in today's mania is any concept of risk and reward. I think it's kind of funny that no present day, self-respecting stock market speculator playing a game of black jack would ever consider hitting a 19 or a 20, especially if the dealer had a 5 or a 6 – just to pick an example. Intuition says there are rules of probability in gambling so people tend to come up with some form of risk management or attempts to put probability in their own favor, whether it's counting cards, blackjack or something else along those lines.

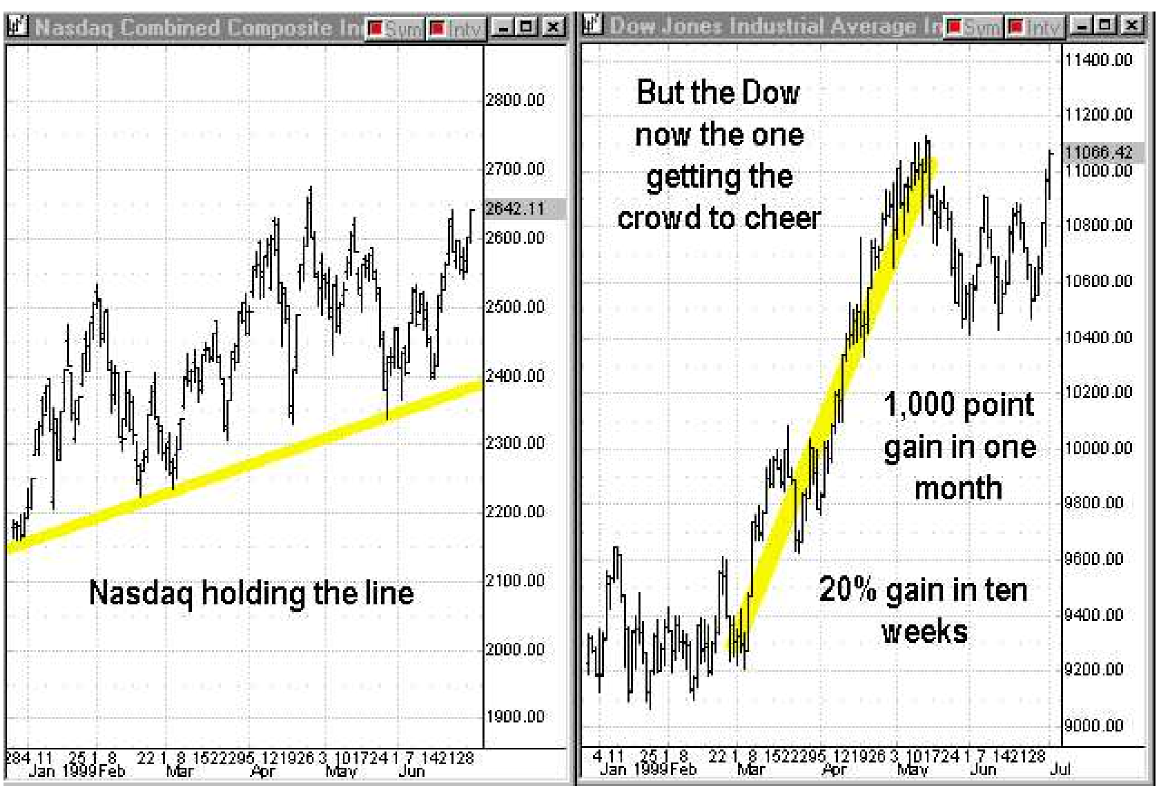
People approach gambling with some regard for the risk of losing their money, yet they approach the stock market with reckless abandon as if nothing bad could ever happen. It's the same kind of disconnect taking place when you look at the Dow 10,000 party hats then you look at the deteriorating state of affairs in Yugoslavia and the Middle East. I guess because people are having so much fun in chasing dot.coms, splits, and all the other goofy concepts that pass for brilliance these days – and have been well-rewarded thus far, I'll concede - they feel that they can safely ignore all the lessons of risk management.

Investment portfolios are fat, CNBC is gaining viewership by the moment, and their financial journalists have become celebrities. Any popular analyst's commentary or recommendations on a CNBC program easily moves the market, while stock chatrooms anoint and swear by their own faceless gurus.

The publishers of business magazines are doing their part too. They can't seem to find enough young adults starting or running their own dot.com venture to feature in their glossy pages. Everyone is a Bill Gates and Paul Allen these days.

It's a moot point at this juncture – and it will be for a long time to come - but stocks are expensive. The average PE of the S&P 100 is around 32, nearly twice the average since World War II; but according to those who have to justify the multiples on stocks, this is not a problem because it's a New Economy. Inflation is low, unemployment is mild, and corporate profits are green this year in comparison to the negative five percent for 1998. People are living better than they ever have before, although they're doing it by increasing their debt, spending more than they make. They've mentally collateralized debt obligations with their bulging stock and retirement portfolios and their appreciating housing values. Still, they're always on the lookout for that next parabolic stock because the chances at winning in the market are better than the lottery or Vegas.

The hot tape of the previous six months continues only a few days into April before running into the speed bumps of bearish fundamentals. It's a perfect opportunity to move some money around. As the Nasdaq cools, the Dow is chased 1,000 points higher in less than a month during April.



Floating Belly Up . . . (*April 1, 1999)* [Fleckism: "Dead Fish" – a Wall Street analyst who floats with the current] Yesterday our favorite, nameless dead fish, who's been very enamored of raising price targets as his form of analysis, was pounding the table on Silicon Graphics (SGI), which managed to preannounce last night. Today, it opened down about 30 percent.

Somebody asked me if I couldn't come up with more live fish in technology. I'm sorry to say I've about exhausted the supply of those I know. I asked my friend Fred Hickey, editor of *The High Tech Strategist* newsletter, if I was missing anybody. All I got out of him was ribald laughter. So we'll keep trying to look for live fish in technology, and I'll continue to point them out as I see them in other areas but don't hold your breath.

It's Just a Wheel of Fortune . . . *(April 5, 1999)* I've heard many stories from brokers who are being asked the following question: What do I buy? I need to make some money to buy a new car or purchase something. So rather
invest and make money, the stock market has become a place where folks think they can go to make a quick hit - to do something they can't afford to do. It's sort of like going to Vegas and saying, "OK, now which number should I bet on at the roulette table? I need to make some money to make my house payment."

I can't stress strongly enough that what goes on in the stock market today has absolutely nothing to do with what's going on in the economy or in the businesses. The market has been completely turned into just pieces of paper and bears no relationship to the real world. I could make the Raps much shorter simply saying, "the market opened, stocks went up and it doesn't matter what the fundamental events were, because every day the same thing happens, the market opens and stocks go up." But if I did that, you regular readers would have to go somewhere else for a few yuks.

Not by the Book . . . *(April 7, 1999)* Today's *Wall Street Journal* had a really good lead article about cooking the books. The article, "SEC Case Claims Profit Management by Grace," focused on W.R. Grace (GRA). One of the interesting things about the article was that W.R. Grace appeared to rationalize its actions by offering the excuse that "everybody does it." Sad to say, that's part of the problem.

Behold Buffett . . . It calls to mind what Warren Buffett recently wrote in his recent year annual report to Berkshire Hathaway shareholders about the shenanigans in accounting:

> *"Many major corporations still play things straight, but a significant and growing number of otherwise high -grade managers - CEOs you'd be happy to have as s pouses for your children or as trustees in your will - have come to view it's OK to manipulate earnings to satisfy what they believe are Wall Street's desires. Indeed, many CEOs think this kind of manipulation is not only OK, but actually their duty."*
>
> He then added, *"These managers say their shareholders will be hurt if their currency for doing deals - that is, their stock - is not fully priced, and they argue that in using accounting shenanigans to get the figures they want, they are only doing what ever yone else does. Once such an 'everybody's doing it' attitude takes hold, ethical misgivings vanish."*

The estimable Mr. Buffett's annual shareholder reports are always cause for conversation and thought. Buffett is the value investor's investor and while that methodology - by comparison - presently isn't working so well, few can hold a candle to his investment success.

Buffett hit the proverbial nail on the head about the misleading usage of stock options for payment to employees by corporations. Increasingly, companies reward their employees stock options in lieu of higher pay or benefits. Stock options allow the holder to then buy a fixed number of his company's shares at a fixed price in what is a rising market. It's a real boon for the workers . . . but it's even better to be the boss.

According to the AFL-CIO, the primary union federation in the U.S., the average American chief executive has now been taking home 419 times the wage of the average factory worker thanks in large part to share options. By comparison, in 1980, that executive made 42 times as much.

Rewarding such large sums of options to executives constitutes what is likely the largest peacetime transfer of wealth in history. Could the reward of options in a rising market entice company heads and spokespersons to speak glowingly of their future business prospects? Of course it would, but the analyst community and general investing public is largely dismissing this legal compensation racket.

Still, the point survives that even though there is no mandate they be reported as such, options are a liability against corporate profits. In 1995, corporate lobbyists defeated the Financial Accounting Standards Board (FASB) in the requirement that companies apply the expense of employee stock options on their balance sheets. Technology firms tend to be quite generous with options at this particular moment, and the outstanding liabilities against profits, which few either understand or talk about, are enormous.

And what did Buffett have to say about it?

> *"Accounting principles offer management a choice: pay employees in one form and count the cost, or pay them in another form and ignore the cost. Small wonder then that the use of options has mushroomed. If options aren't a form of compensation, what are they? If compensation isn't an expense, what is it? And, if expenses shouldn't go into the calculation of earnings, where in the world should they go?"*

Tech is taking a nasty spill after a preannouncement of an earnings miss by Compaq Computer in early April. Articles in the *Wall Street Journal* have profiled how PC sales are slowing and price pressures are detracting from companies' bottom lines. The horrible quarterly results of retail stores heavily dependent upon computer sales, CompUSA for instance, have been among the first signs of an oncoming debacle for computer manufacturers. As individual stocks in computer related sectors are sold, the Internet stocks catch a bid for a last hurrah of this particular leg of the rally that has been in progress since the October low.

Speculators Seek Safety . . . *(April 12, 1999)* The interesting thing is - and I'm saying this with a smile on my face - there was a flight to safety in the Internet stocks. They went berserk this morning when everything else was getting pounded. I guess the fact that stocks can go down has been lost on the Internet speculators. There's no point is going into how much they all were up, because they were just going ballistic.

Internet Insanity . . . *(April 12, 1999)* Today was the finest example I think that I have ever seen - and maybe that anybody has ever seen - for defining chaos in the stock market. The big-cap tech stocks were sold all day long, as were things connected with PCs, semiconductors and semiconductor capital equipment -with good reason, I might add. And away from that, the Internets were up 15 to 20 percent – unimaginable price moves, really. I won't name them all, so many of them were extraordinary, but to go through the list, 15 to 20 percent gains were fairly common, ten percent gains were not uncommon, and five percent gains were everywhere. I don't see how this internet craze can continue without some meaningful reversal. In the past when they've climbed so rapidly, there have been sessions that they've been whacked by 30 or 40 percent. I wouldn't be surprised to see that happen in the not-too-distant-future.

Spin Wins Again . . . *(April 22, 1999)* Compliments of IBM, Wall Street threw a big party in hardware stocks today as Big Blue's numbers were better than expected. Without going into all the gory details, I think that Lou Gerstner is headed for the Betty Crocker Memorial Prestidigitation award. In essence, the reason why the numbers were so much better than folks expected was that last year IBM did not break its hardware out by segment. Now it does. It turns out that last year, on a couple of billion dollars in revenues, it lost $500 million. Recall that last year there was a big channel-stuffing problem, precipitated by IBM and Compaq, so IBM had a very poor first quarter in terms of hardware revenues. But no one dreamed that it could have lost that much money.

Most growth stocks in tech companies are measured sequentially, not year-over-year, but in this environment we can pick and choose however we want. So that was the proximate cause for today's party, completely taking away all fears that have been raised over the last several months by virtually every manufacturer and seller of PCs. Even if one looks at what IBM did, it was nothing to refute the ongoing problem. Spin won again, facts got tossed out the window, and we had a big party.

Doing Business on a Wink, Blink and a Nod . . . *(April 23, 1999)* Away from certain technology problems, most of the companies have been able to come in and meet the nice low estimates that have been set by the obliging analysts. That is the game that has been going on ever since real earnings growth slowed a couple of years ago. The company sets a nice low number, the analysts wink and say, "If you make the number, no matter how you get there, it's OK by us. But if you don't make it, and you make us look bad, then we're going to hate you."

Just Charge It . . . *(April 23, 1999)* That's what companies like Compaq (CPQ) did, and they finally ran out of ammo and got caught. We've got the same sort of accounting sleights of hand going on at many companies. Today Xilinx (XLNX) was forced to come out and restate its earnings for the last few years. It is going to change the way it accounts for sales into and out of the distribution channel, and take a one-time charge. So what earnings you thought you had a while back, you don't have now. That's where all the financial engineering ultimately ends up - in a one-time charge down the road. I'm sure that Compaq will be making one, and someday Gateway (GTW) and IBM (IBM) and all the rest of these guys will be doing it too - including companies away from technology.

Data Game . . . *(April 29, 1999)* We had a supposedly important economic statistic this morning, the employment cost index. The reason it's important is because Greenspan supposedly likes it. Anybody who thinks government numbers are going to show anything untoward doesn't really understand the present administration, as the economic data is so massaged. If you look at the CPI calculations and the way that they're calculated, there's no way we'll ever see inflation because price hikes are always adjusted for "improvements."

These people have an agenda not to show any inflation. That's not to say we have a whole lot now as generalized CPI inflation is not raging, but it's certainly not as low as the government makes it out to be - just ask anybody who writes checks for things. Having said all that, the last place anybody's going to see it is in the employment cost index, because everybody's getting paid with stock options.

So the thinking is, we have a tight labor market and no inflation and that's what makes everyone feel so good. But I submit to you that the inflation that exists is largely bound up in the stock market and the housing market. We've had plenty of inflation - it's just gone into paper assets. By the way, just think of where the employment rate would be if people didn't have stocks to day trade and actually had to get jobs. So the rosy economic scenario is nothing other than a $15 trillion stock market. That's really the whole story.

As long as we're on the subject of the ECI and government statistics, has anybody noticed that any time and for whatever reason the market gets in trouble and we have an economic statistic coming out, it always manages to be just what the doctor prescribed? I'm sure that's just a coincidence, but it has happened about 100 times in a row.

The Dow is pushing to surpass the 11,000 mark at the end of April. The Internets have taken a sizable tumble but are stabilizing, and there is the ongoing battle of wills over the computer industry. Additionally, people have great longings to get in on IPO’s. There’s a big one coming up: Goldman Sachs.

Poetic Pricing . . . *(May 3, 1999)* So the Dow jammed to 11,000 right on the day that Goldman was set to do its IPO pricing, and it's perfectly poetic that Goldman would get its deal done at what looks to be a very fat price. As long as we're on the subject of fat prices, Warren Buffett, who was hosting his annual meeting today, had this to say about the IPO market after he had been specifically queried about the Goldman deal:

> *"An IPO is sold when the seller wants to sell it. To think that, among thousands and thousands and thousands of choices for securities, that the most attractive thing on a given day would be to buy the stock of something that a knowledgeable seller has decided, among all the choices they have as the days to be sold, that they're going to sell that day, I mean, it is almost a mathematical impossibility."*

Buffett is commenting on the fact that the sellers of Goldman Sachs, who have waited since the Dow was zero to now get to 11,000 to share a piece with the public, might know more than the buyers. That's generally been the case with IPO's throughout history, as they are not particularly good investments. The last couple of years, of course, when we've had the Internet craze, a lot of people have made a lot of money. But, of course, in that instance we're not talking about investing - we're talking about speculating for the most part.

Deflating the Inflation Myth . . . *(May 14, 1999)* The notion that there's no inflation is, of course, bunk because all the inflation is in the stock market. We've talked about asset inflation before; it tends to be more rare than CPI inflation, but that's what we have.

Since the Fed cut interest rates last fall, the equity market has moved straight up, and the bond market has fallen straight down. As a reference point, at this mid May point, the ten year note, more important to the mortgage market and the banking system than is the 30-year bond, yields 5.72 percent; the yield was 4.5 percent in December, a 20 percent hike in the cost of financing, a fairly substantial move. The bond market, a free market contemplating inflation, is raising interest rates in spite of the Fed.

Yet, the Fed is performing coupon passes, that is, injecting liquidity into the system by purchasing government bonds. This has nearly the same effect as lowering interest rates because suddenly, banks have more money to lend borrowers.

Not Enough Money for Both . . . *(May 14, 1999)* The problem, as I've maintained all along, is that bonds are going to keep being shredded until equities are. There's not enough money to run both markets and the economy, and folks have no interest in buying short-dated paper at 5 1/2 percent when they think they can make 30 percent a week in the stock market. With the bond down on inflation fears, what did our sterling Fed do today? Yes, another coupon pass. I don't know for certain, but I believe that makes it about eight coupon passes in the last two weeks.

Pass the Coupons Please . . . *(May 20, 1999)* The Fed, once again, came in and talked out of both sides of its mouth, doing its umpteenth coupon pass in the last week. So they continue to say one thing and do something else. Why might they be doing that? Maybe they finally realize they have a stock market bubble on their hands and they'd like it to keep from getting out of control. There have been rumors of potential currency problems in Argentina, so this has coincided with Rubin stepping down. Whether Rubin is stepping down because he has to get out of the way before trouble hits, or people are starting to worry about trouble because he's leaving, we don't know. But it may be one reason why the Fed is trying to have it both ways. Bubble management is tricky business.

Special Speech . . . *(May 17, 1999)* I'd like to share portions of a story from Reuters, which covered a speech that Paul Volker made Friday at a Credit Suisse-First Boston Conference on mergers and acquisitions.

> The article stated, *"Volker acknowledged that the U.S. economy had changed largely due to technology that has increased U.S. productivity. This has allowed U.S. corporations to boost output and profits without inflationary price hikes. 'This expansion has violated everything I know about the economy,' Volker said of the second-longest expansion on record, in which the economy has grown at a robust clip while inflation has stayed tame. 'Part of the explanation is we are doing so well because the rest of the world is doing so poorly . . . inflation has been so good because commodity prices are depressed and everyone else has excess capacity utilization,' the former Fed chief said."*

I certainly know how Paul Volker feels when he talks about the fact that the expansion has violated everything he knows about the economy. But what follows is the most important thing he said, and is exactly what I believe:

> *"The fate of the world economy is now totally dependent on the growth of the U.S. economy, which is dependent on the stock market, whose growth is dependent on about 50 stocks, half of which have never reported any earnings,"* Volker said.

That is a very potent statement from a man who, in my opinion, gets complete credit for slaying the inflation of the late '70s and setting the stage for all the things that Greenspan has subsequently mismanaged. Volker is one of the last true central bankers and I value his comments very highly. I recommend that folks read those quotes a few times and make sure that they sink in.

Whenever Greenspan speaks, the media and the market scrutinize every word for any signal that the Fed plans to take back the fall rate cuts and what, is the obsession, will be their bias going forward? Symmetrical, asymmetrical? How will the market react? Greenspan has been very careful to warn the equity markets of interest rate hikes, though surprise cuts, as they have shown, are fair game. Martin Mayer, author of <u>The Fed</u> contemplated the deleterious effect that a 25 basis-point hike had on the equities market in 1994. As a result it seems that Greenspan self-imposed an edict as to how he relates to the financial markets :

> *"Though he has denied it, I will argue that this experience was the push that moved Greenspan to a belief in "transparency" – in letting the money markets know much more about what the Fed was doing and wanted to do, and about what the banks were doing and its impact on the value of their portfolios.*
>
> *"In any event, the customs changed. Rather than letting the market draw its own conclusions about the FOMC decision from what the open market desk did in New York, the Fed began a custom of informing everybody during the FOMC's periodic two-day meeting in Washington not only what Fed Funds rate the desk would seek in the weeks ahead, but what the committee's expectations were for future changes in the rate."*

Easy Al on the Hill . . . (*June 16, 1999)* Tomorrow we'll hear from the man who brought you the mania. Easy Al's going to get on the Hill and try to jawbone away his mistakes because he's terrified to do what he should do and raise rates. The Fed appears to be cognizant these days of the fact that a mania has been unleashed, but obviously it doesn't understand how big it is or it probably would have done something by now.

Easy Al's Moral Hazard . . . *(June 17, 1999)* As soon as the text of what Easy Al had to say was released, I took a quick read of it. The bottom line: He said he was going to raise rates pretty soon, but went on to talk about how hard it was to identify a bubble and paid some lip service to asset prices. The way I read it, he basically said that if a bubble bursts, "don't worry, I'll take care of it," thereby once again increasing the moral hazard for investors.

It is a Bubble . . . *(June 17, 1999)* Greenspan's statement that you can't tell about a bubble is complete nonsense. If you read a few history books, many people understood that it was a bubble in the late `20s, and that it was a bubble in Tokyo. By definition, those who believe in a bubble have to be in a minority or it can't occur. Greenspan made clear one of my long-held beliefs - <u>that in a social democracy all roads lead to inflation.</u> You can see that in the Fed's response to all problems in the last few years, and you can see it in Greenspan's testimony, where he makes it clear that they've been very reluctant to take back the 75 basis points even though they admit it's no longer needed. Actually, my friend Colin Negrych said it best as follows:

> *"Greenspan's comment, `To spot a bubble in advance requires a judgment that hundreds of thousands of informed investors have it all wrong,' is laughable. All these hundreds of thousands of investors wanted to be informed about was whether Greenspan would continue to defer to them. He did."*

Another Fed Surprise . . . *(June 30, 1999)* The Fed gave us the 25 basis point hike, but to my surprise, decided that was going to be it - it was going to go back to neutral. I never expect anything terribly responsible out of Greenspan, but occasionally he surprises even me with his willingness to be irresponsible.

If you recall, in his most recent speech before Congress, Greenspan admitted that the 75 basis points the Fed gave us were probably no longer needed. But now he's afraid to take them back, even with a lot of precursors of inflation heating up: housing prices are going crazy, labor is as tight as hell, and the cost of most things is up other than basic commodities. And while we're on that subject, basic commodities are starting to pick up. Oil was up strong today and the CRB, the Goldman Sachs index, the commodity indexes and copper are all starting to break out. So the inflation genie potentially is about to get out of the bottle and if it weren't for the fact that everyone's getting paid in stock options, wage rates and labor would be ratcheting up too.

A rate hike won't stop us from swinging into recession in a heartbeat once the stock market cracks, but for anyone to think that the Fed is going to get away with just 25 basis points is absurd, because 25 basis points is not going to change anything.

Breathless Anticipation . . . *(July 8, 1999)* The big news of the day is the earnings report of both General Electric (GE) and Yahoo! (YHOO). Once again we had both companies "beat expectations." I'd like to comment some more on the concept of "versus expectations." This proves as eloquently as anything that what goes on in the stock market today has nothing to do with fundamentals, and is complete rank speculation, as if there weren't lots of other examples. "Earnings versus expectations" is all the TV, which aids and abets this mania, discusses. That and the whisper expectation. It's all that matters.

How about FASB 000? . . . *(July 8, 1999)* In an effort to simplify all of this, I propose that we come up with a new FASB regulation, and call it FASB 000. We will only discuss company revenues. We won't worry about EBITDA [earnings before interest, taxes, depreciation and amortization], we won't worry about before write-offs, we won't have any extraordinary charges or restructuring charges - we'll just have revenues. That will simplify everyone's life. It will free up the money that's being spent currently on accounting and auditing to be used for even more share buybacks. We won't have to worry about book value dilution due to paying people in stock and then buying it back and having it wind up helping earnings. We'll just throw away all that stuff.

Then, if we really want to get a peek at a company, if it's an Internet company we can look at the page views or the number of customers. If we want to analyze a steel company, we can have them tell us how many ingots they sold this week. Nordstrom can concentrate on how many dresses they've sold; the airlines can say how many seats they've sold; hotels can talk about how many rooms they've sold - and that will be our snapshot for the businesses.

That would be perfectly in line with the total lunacy that passes for research in this day and age, since nobody does any research; all they do is chase momentum. I think that the FASB would go along with that, because it's basically just a lap dog for corporate America and it will make life a lot easier. Corporate America would have a lot less to lie about. So that's my proposal. I think we should forward it on to those in charge and just dispense with all this other nonsense and make life simple - sort of like a flat tax in terms of simplicity.

Back to Those Earnings . . . *(July 8, 1999)* So returning to the news that highlights the preposterousness of all this, last night Yahoo beat the number. What I want to know is, how come the number was set at eight cents, down 25 percent from last quarter, so that if the company reported flat earnings that was deemed a major victory? If this is supposedly one of the greatest growth stories of all time, which is what the valuation implies, how come flat sequential earnings is such an accomplishment? On the other hand, if all of Yahoo's revenues were profits, as in my proposal above, the company still would be trading north of 60 times revenues (revenues equal earnings).

Speaking of Getting into Trouble . . . *(July 9, 1999)* Here's some interesting information about Waste Management, which imploded the other day on a warning. As the dead fish were recommending the stock a few months back, insiders sold about $57 million worth of stock into that little flurry. This also reinforces two other points: a) how dead fish don't do their jobs and b) how management takes any and all advantage of opportunities that present themselves. Of course, those dead fish who now recommend selling Waste Management after they recommended buying it before, will go find something else to recommend and of course everyone will jump on it like it's a good idea.

Comparing the '80s and '90s . . . *(July 9, 1999)* This time reminds me a lot of the early '80s. In the way of interpersonal full disclosure, I left the computer business in 1979 to get into the brokerage business because I thought stocks were cheap and there would eventually be a big bull market. I remember it being so clear in July of 1982 that fundamentals didn't matter and the only thing that mattered was the fact that stocks only went down, so no one cared. It made me question my focus on fundamentals for the last couple of months before the bull market started. In the early '80s it didn't really matter how cheap stocks were or how much value was there. Nobody really cared because a) they were getting good money in the money funds and b) stocks never went up.

The professionals had to be market timers because when there was a surge in the market or in a particular stock, they had to take advantage of it. I believed at the time that before the bull market ran its course, market timing would be completely discredited. Obviously it has been discredited because now everyone’s time horizon for owning stocks is *forever*. Having said that, what people really like to do between holding some of their stocks forever is, they like to trade them like mad based on the price action.

Yet, just as in the early '80s, when there was a complete disregard for value when stocks were very low-risk propositions because there was so-o-o much value, today there is a total disregard for risk because people think that since stocks have been going up, they will only go up. Therefore, the only thing that matters is market action. Everything is very similar to what it was in the summer of 1982, only precisely in the opposite direction. Euphoria reigns supreme; stocks represent absolutely no value and still, people believe them to be without risk.

Instant replay . . . *(July 9, 1999)* Part of this, I think, comes from watching Bubblevision. People believe that because they have a computer and they have the TV telling them what to do, they can't get hurt. I think that Bubblevision has aided and abetted the market in the sense that earnings are reported as to how they compare to what was expected. There's absolutely no mention whatsoever of what the business is, what the margins are, what the barriers to entry are, what the earnings power is versus the market cap - nothing fundamental is ever discussed. Rather it's simply about action, expectations and psychology.

In terms of the way it’s chronicled, it’s as though the stock market is a subsidiary of CNBC or a sporting event. I remember going to Japan in late 1990 after the market had broken badly and finding out that during their bull craze, people tuned into radio show that broadcast stock trades. I wondered at how absurd that was. Little did I know that here in America, a decade later we were going to make a radio play-by-play seem extremely tame.

My suspicion is that before the bear market is over, which hasn't commenced as yet, no one will care about price action or technical analysis. The only thing that will matter will be fundamentals, and occasionally taking profits and it's going to be interesting to see how that develops.

Irving Fisher was Right? . . . *(August 23, 1999)* In an absolutely staggering display of bravado on CNBC this morning, Jim Glassman, *(author, Dow 36,000)* a fellow at the American Enterprise Institute, made the case that paying 100 times earnings for stocks is no big deal because they are always going to grow. He stated that "Irving Fisher was right, stocks worked out for the long term." Glassman was referring to Irving Fisher, who said that stocks were on a permanently high plateau just before the stock market crashed in 1929.

In fact, stocks have worked out pretty well for the last seventy years, but that belies the point: The reason why people are supposed to control their risk when they run portfolios is because you don't always know when life is going to issue its margin calls. And if you had been brilliant enough to follow Dr. Fisher's advice in 1929, you might have needed that money along the way, like during the Depression, when you lost your job.

The point that all of these people who rationalize new era valuations fail to take into consideration is that many different types of risk does exist. If you buy at a stupidly high price, you may, being a human and subject to human emotions, find yourself forced, compelled, or tricked into selling at a bad price. This is why you should look to gain an advantage by buying at more attractive prices, rather than paying a stupidly high price, and trying to sell at an even more inflated price later. The risk side of the equation is something that new era proponents frequently miss.

It is widely and correctly assumed that the Fed will increase interest rates another 25 basis points during its August meeting. The market doesn't mind. The Dow marched right on up to a new high in the days before and one day after the perfunctory August 25th hike.

And We Have Liftoff . . . *(August 24, 1999)* At its usual time, the Fed gave us the good news about our 25 basis point rate hike. CNBC's coverage of such an important event had all of the feeling of NASA watching the first moon launch. There was so much anticipation and analysis, and of course, we got the live call from someone who was close to the Fed. It is amazing to watch the hoopla attendant to the stock market. I said a long time ago stock speculation was a national pastime, and even though that's a decent analogy, it's not quite forceful enough. The stock market is watched every day with as much interest as was Neil Armstrong stepping onto the moon back in the late 60s.

Big Buy for Cisco . . . *(August 26, 1999)* In another staggering piece of news, Cisco Systems announced that it was going to buy a startup networking company for about $7 billion. Relative to the level of sales, that's a breathtaking number. What's even more to behold is that on the news of this latest acquisition, the stock got a lift for it, at least in the early going.

It's also noteworthy that Michael Dell managed to make himself a gargantuan amount of money as he invested $30 million in the company about a month ago. I couldn't tell from the press reports what he made because I don't know what the valuation was, but it certainly could have been as much as a couple of billion bucks. Hey, when you're hot, you're hot.

The Economist, a world-renowned newspaper, has become increasingly critical of Alan Greenspan's timidity in curbing the inflation of the stock market bubble. Although the Fed has now taken back two of the three fall of '98 rate cuts in June and August of '99, The Economist ran an editorial opinion column in late August stating,

> *"A prudent central bank would have tightened policy more aggressively by now. Even after this week's rise, American short-term interest rates are still a quarter of a point lower than they were a year ago, before the Fed eased in response to the financial jitters caused by Russia's default. So long as a buoyant stock market and rampant credit expansion continue to boost growth, it will take more than a few small interest rate rises to slow America's boom. Indeed, such timid moves may falsely reassure Wall Street that the Fed has everything safely under control – encouraging the stock market to ever-giddier heights. A vulnerable dollar, a stock market that on most measures looks hugely overvalued, a monstrous overhang of personal and corporate debt: all combine to make it more likely that America's boom will end in a hard landing. To avoid this will test the revered (if opaque) Mr. Greenspan to the limit. But his dilemma is largely of his own making: it reflects a failure to tackle America's economic imbalances earlier, before they had become so severe."*

The Nasdaq has more than doubled since it took off from the October 1998 lows less than a year ago, but it pales in comparison to how far and how fast they're going to run stocks in the approaching months. The next chapter asks, "How Big Can this Get?" The answer is well known in hindsight, yet at the time, few could have guessed.

The mania is in full bloom and the bubble just grows with each passing day. People do the craziest things in the pursuit of a buck. In the next chapter you'll see what Fleck did to capture tiny slices of the mass mania. The stories from readers all over the world were so telling and poignant that he began collecting and chronicling the wildest tales for the readership. He called them – quite perfectly – "The Mania Chronicles."

Chapter two details the most incredible days, the blowoff of the bubble, from the fall season of 1999 to March of 2000, just before the Nasdaq sees its top tick. It's a time when anyone who is conscious knows there's money to be had in the stock market, so consequently, everyone is in the process of getting in.

The answer to "how big can it get?" question: