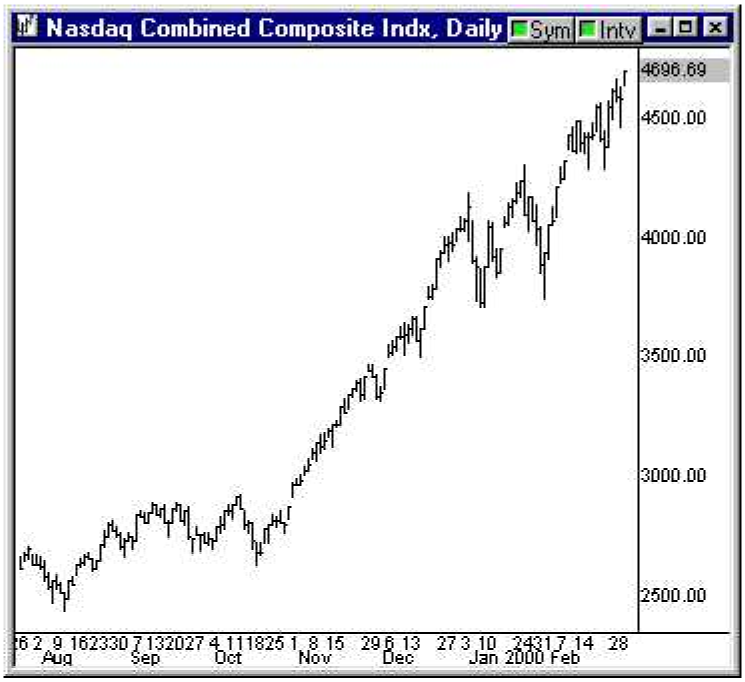
Chapter Two: How Big Can This Get?

Period of September 1999 through February 2000



On September 21, 1999, a 7.6 earthquake struck Taiwan. Taiwan is home to companies who manufacture ten percent of the world's DRAM supply, 22 percent of desktop PC's, 40 percent of computer notebooks, almost half of the modems, 60 percent of all motherboards, and nearly 70 percent of desktop scanners. The effect to the PC industry was of utmost concern and speculators scrambled to saddle up with who might benefit versus who might suffer. For example, American chipmaker Micron (MU) was immediately bid up ten percent on the supposition that DRAM prices would be moving higher, while box maker stocks were beaten for the same reason.

The market has been fairly subdued throughout the late summer and early fall as the fallout from the earthquake and disappointing earnings results are weighed. Still, the market doesn't go down "well" even if it can't get going on the upside just yet. It's as though folks are simply waiting to get all the bad news out of the way to get into the favorable seasonal period – late fall, early winter. If it seems that way, then maybe it's true. Everyone knows the market goes up after October, right?

Kudos for Levitt . . . *(October 8, 1999)* I'd just like to give a tip of the hat to Art Levitt, who continues to try to clean up what's going on in Wall Street. The SEC is going to issue some specific regulations on selective disclosure. Thank God somebody's cracking down on some of this monkey business that's going on.

But it's Business as Usual for GE . . . *(October 8, 1999)* GE came out and beat the number, as usual, in its managed earnings state. Maybe Levitt should take a look at GE if he wants to get a good example of managed earnings. I know it's a stock that everyone likes but you can't tell me, given its far-flung businesses and all the different things the company is in, that its growth rate is this smooth. It's just like Cisco. This stuff is not supposed to be allowed to go on, and yet it does. One of these days, people will be very upset about it.

Intel Scrapes a Knee . . . (October 13, 1999) Everyone now knows that Intel didn't make the earnings estimates that Wall Street had been led to believe. What's interesting is that everyone was excited that Intel was expected to pre-announce better than expected numbers, so from July thru late September, the stock has been ramped from the low $50s to $90. And yet, the company didn't even make the estimate. But this morning, all the analysts were pounding the table, reiterating their $95 price targets, because the company gave stronger guidance.

Now regardless of whether you like Intel as an idea, you have to be struck by the fact that analysts are recommending a company that missed revenue estimates in the first two quarters and missed earnings estimates in this quarter. Everyone feels good because the company "was more aggressive in its guidance." Ladies and gentlemen, last quarter's guidance was wrong when it came to the margins and at the end of the day it's about earnings, not revenues. We constantly hear these stories, "well, if not for this, if not for that," but the bottom line is if it weren't for expenses, revenues would be earnings.

With the exception of Drew Peck at Cowen & Co., who was cautious because of the company's transition problems and the fact that microprocessors have then become a commodity, most of the other dead fish were out pounding the table on this wonderful buying opportunity. So it continues to be a case where the analysts get their fundamentals wrong but raise their stock prices anyway because that's what research has become in this day and age.

I submit that anybody who's really trying to do any objective homework can figure out what's going on. Go read the *Barron's* article of a couple of weeks ago that got dismissed by Wall Street. It was actually quite good and it elaborates on this story. Intel has historically been a great manufacturing company and it's given us a lot of great products. But as an investment, to me it makes no sense given the price of the business and the current state of the business.

Corporate fundamentals are, obviously, only a bit part of what determines market direction and price action. While the fundamentals have been the primary focus of attention for this month, there are other issues to note. One of these is the involvement of large mutual funds. The rating of a fund manager is based upon how well the fund compares to the S&P 500 and to that of its peers in the same category. The game to outperform the index and competing funds was already well in place before the beginning of the epic ramp in the Nasdaq Composite Index.

Mutual Fund Madness . . . *(October 14, 1999)* When I voice my disgust for what investors are, I don't mean to imply that the public is doing this to themselves. In all likelihood it's the idiots who run the mutual funds that they have plowed into. As I say this, I realize that there are a lot of sane mutual fund managers out there trying to buy value stocks. Their lives have been made miserable because things that are cheap only get cheaper and things that represent value continue to get destroyed. Meanwhile, the absolutely crazy stuff keeps going up.

Why, you might ask? Because money is being managed by people who "don't own it." And that means the risks for the owners of the capital are different from the risks the fund managers take. If a fund manager sells and the market goes up, the manager is out of a job. However, if managers are totally invested for their clients and the market collapses, they feel that they are not doing any worse than anybody else is.

So there exists this perverse set of circumstances in which these supposed professionals feel that they can't afford to let stocks go up without them, yet they can all go down together. As a result, the huge chunk of fund managers are all piling into the same things and all behaving in a completely irresponsible fashion because they think that's what they have to do to keep their jobs. This is precisely what happened in the late `20s and that didn't turn out so well either.

Drunkenness and irresponsibility are the order of the day. When we look back on this period, Wall Street is going to have a black eye that will take a long time to remove.

Microsoft Numbers Don't Compute . . . *(October 20, 1999)* The big news was Microsoft and the even bigger news was how wildly bullish the company was on the conference call. Words like "awesome" were tossed about freely, and both the press and Bubblevision were quick to pick up on all the wonderful things that Microsoft had to say. The problem is that when one looks at the numbers, they don't quite fit the rhetoric.

Now, why is this important, you ask? First, let me say that Microsoft is a great company and I am not short it. But the main question that I would have is, if things were so awesomely awesome, why did revenues fall sequentially? If you go back to the spring of 1995, just before Windows was launched, to the September quarter that was just reported, revenues have always gone up. In this particular quarter, revenues fell 6.7 percent and that is a little startling. More importantly, if you look at the deferred revenue line (an accounting feature somewhat unique to Microsoft) instead of growing, as has always been the case, it declined for the first time ever! Why would those two "first-time" events occur in such an awesomely phenomenal quarter?

Just the Facts . . . *(October 20, 1999)* If this were any other company but Microsoft, it would look as though it went out of its way to make the numbers look better than they were. Historically, Microsoft has let the numbers do the talking. This time, the company did the talking. Usually the call is quite subdued and not so promotional. I will leave it to the reader to deduce why Microsoft would make the call so wildly bullish when in fact its numbers don't support it. Yet, when Microsoft speaks, everyone listens and spin counts far more than the facts at the moment. However, since I'm a professional debunker, it’s my job to do just that.

One thing I should point out again is that insiders at a lot of these companies obviously have a vested interest in putting as good a foot forward as they can. They all have options and more importantly, the rest of the people in the company have options. So the stock price has become a very important asset, maybe more important than any other asset at a company, at least in some folks' minds. That is a motive, I think, when managements do whatever they can to try to make sure the stock prices don't go down.

IBM moves Dow lower . . . *(October 21, 1999)* Maria woke up to nuclear winter this morning. The TV finally started talking about something that we have been discussing for a month, and should have been obvious to anyone who's been paying attention. Of course, it took IBM admitting to the facts to get everyone to focus on the situation, but that's the way it goes in this environment - nothing ever seems to be discounted until the moment one of the companies admits it. Obviously, Big Lou, our favorite financial prestidigitator, ran out of things he could do to engineer better numbers and the fundamentals have won the day.

For a short time it seemed that the facts were going to matter. The market opened with a giant thud. The Dow was quickly down a couple of hundred points on the opening and that set the lows in the early going. From there, we had a saw-tooth rally and setback, rally and setback, all day long, with bonds on the decline whenever stocks would go up. However, once the bond market closed, the stock market went nuts on the upside in one of the most brazen displays of denial or bravado that I’ve seen during my 20 years in the business. Everything in technology went berserk. The internet stocks were the strongest. Chip stocks went wild, as did PC and PC-related stocks. It’s as though IBM was in the food business; nobody cared at all.

I'm told that one of the deadest of all the dead fish came out and made sort of a bullish semiconductor call and said that Y2K would have no impact. I guess he figures that all these pieces of hardware where companies are having troubles run on noodles or something like that. So it continues to be the case that any stupid thing will fly as long as it's bullish. And if the facts turn out to be bearish, as soon as they become known they are immediately dismissed as old news.

Earlier in the month the Fed changed its bias from neutral to an inclination to tighten interest rates. A couple weeks later, Chairman Greenspan issued some quasi-hawkish remarks the evening before the release of a higher PPI number. An already jittery market faltered at this bit of unwelcome data and its attendant implications, but with the benefit of hindsight and a completed chart, it's clear that all of the aforementioned was quickly discounted and forgotten.

Markets serve as a medium for buyers and sellers to come to a collective agreement regarding the value of tradable assets. In terms of corporate stock, share prices are based upon all that is known about a company's prospects for business, earnings, and future growth. Presently, investors either believe that many tech companies are going to soon enjoy enormous growth or something entirely else has gripped the market. In this moment in time, it is the latter and its name is Easy Credit, Easy Money.

While the Fed's printing press is about to kick into high gear, additional credit is widely available outside of federal control and it's finding its way into the market. Cheap financing is available for just about anything the consumer wishes to purchase. Online brokerages offer incredibly low commission for online trading and margin use is scantly recognized as even a remote risk to personal capital assets.

The motion of stock moving up everyday is infecting investor psychology. Everyone wants to buy the stocks that go up everyday and every bit of bad news is interpreted – as well as hyped – as a buying opportunity.

As the market edged up out of the October slump, it needed just a little push to overcome the hurdle of an eighteen-week trading range. In what was likely a combination of deliberate stock ramping for typical month end games and Alan Greenspan's dinner speech embracing all things technology before the business council in Boca Raton, Florida, the market gapped higher the next day, October 29. It was precisely what was needed to give a technical buy signal. The opening gap broke through the upper trading band, encouraging the index to climb nearly 20 percent higher before taking a couple days rest at the end of November.

It was during this wild period that Fleck began recording “The Mania Chronicles,” some of the more interesting real life stories from stock market observers and participants. There’s just nothing quite like them to effectively capture the essence of the day in such simplistic terms. The best of the Chronicles are interspersed throughout the remainder of this chapter and the next in boxed sections. This following vignette was the first of many to merit inclusion in the Chronicles.

The Mania Chronicles

Bring on the exuberance . . . I have to share an absolutely staggering article by Dr. Irwin Kellner posted on the CBS MarketWatch site Nov. 9. If I didn't know better I would swear that Kellner was trying to be tongue-and-cheek. This is absolutely the most bombastic, arrogant piece I have ever read concerning the stock market. It makes the things I see pure novices doing, which I think are ridiculous, seem completely rational. This is exactly the kind of thing that you would think you would never see, but ultimately comes at the top of the biggest bubble of all time.

"Hey there, Mr. Greenspan, you don't scare us.

"We're the stock market and we're ready for whatever you and your colleagues decide to dish out, so go ahead and take your best shot.

"If you decide to raise interest rates next week, that's fine. We can deal with it.

"And should you think it's unnecessary to boost rates, that's even better.

"In other words - whatever you and your band of merry central bankers decide to do on Nov. 16 is OK with the stock market. And, to paraphrase that great economist, `engine' Charlie Wilson, ‘what's good for the stock market is good for America.’

"While economists, Fed watchers and the media are obsessing over whether or not you will hike rates come the 16th, read our lips - it really doesn't matter what you do.

"Here's the reason: If you should decide to raise the federal funds rate by a quarter of a point, that would only bring it back to where it was back on Sept. 30 of last year, before you cut it three times, a quarter of a point each time.

"No big deal. At 5.50 percent, this was not an impediment to rising stock prices; equities had a pretty good year in 1998, you will recall.

"Besides, you're not going to raise rates again for the rest of this century. Indeed, we're willing to wager that you won't even be thinking about a rate hike until spring in the new millennium - if then.

"Care to know why? Because you've already told us that you plan to inject some $50 billion extra into the financial system to help tide the banks over any cash needs they might have arising from their customers' concerns over Y2K.

"It wouldn't make sense to put money in with one hand and take it out with the other, would it?

"Also, the economy will be so distorted by Y2K-related activity, it will be virtually impossible for you to discern the underlying trends.

"There's so much precautionary inventory building going on now that there's bound to be a slowdown come first-quarter 2000.

"Indeed, you won't know until spring whether the economy is roaring ahead or throttling back; a rate hike would be unwise until the Y2K fog lifts.

"So if you do raise rates next week, we're going to assume that will be it for at least four months, if not more. That's a buy signal, if we ever saw one.

"Of course, should you pass on a rate hike, that's all the more reason to throw caution to the winds and snap up whatever's available.

"Yes, Mr. Greenspan, we're going to start our New Year party early no matter what you do on the 16th.

"It's called exuberance, get used to it."

Well, he's at least got one thing right, for sure. And that is, the Fed's 25 basis points is certainly not going to be any big deal after everything we've witnessed in the last year, with this tripling of the Nasdaq 100 and the sensational moves of all the indices.

Despite the pompousness of his sermon, Kellner's comments about the infusion of fresh cash and its resulting "buy signal" were right on the mark. The $50 billion that he suggested, however, was entirely too modest. The Fed is pumping money out like water through a fire hose. Take $50 billion times three or four; that's closer to the correct figures.

Tough talk, no action . . . *(November 4, 1999)* Even though Greenspan's talked tough and the Fed has raised the cost of money, it has been liberally throwing money into the system, as one can see by looking at the monetary base and other monetary aggregates. I guess this is the main reason why we continue to party, because the merry pranksters at the Fed have no stomach for doing one of the jobs for which they were appointed - that is, keeping things stable.

Berry boosts bulls . . . And in the scheme of how bubbleonians view things these days, the *Washington Post* carried an article by the bulls' favorite Fed pundit, John Berry, saying in essence that all the rate hikes were done for the rest of the year. That precipitated a wild party once again on the opening. The S&P opened up a little more than a percent, and the Nasdaq 100 opened up its customary about a percent and a half.

Pass the champagne . . . A friend sent an email that sums up the present environment and comments on the John Berry article as follows: "Expect silly season in the asset markets to get worse. If Berry is correct, then a fair assumption would be the Fed wants to create a `no fear environment' until after Y2K. Damn the bubbles, pass the champagne. This ‘leak,’ plus stories being fed to big-brain newsletter writers by the most senior Fed officials are the modern equivalent of central banking. The motivation is easy to understand - this fed loves applause - and nobody wants to be accused of having left anything undone in preventing a problem on the order that some expect for Y2K. If there is no problem, the Fed is a helpful genius. If there is, well, the Fed did all it could. Hell is at hand."

No Messing With the Margin . . . *(November 8, 1999)* Maybe bubbleonians feel they got an all clear signal as the merry pranksters at the Fed were quoted in the *Wall Street Journal* saying they had absolutely no intention of raising margin requirements. God forbid that they should do anything that might dampen the speculative enthusiasm.

A twenty percent gain in a major index isn’t something that just creeps along. There are tremendous gains in individual stocks as the excitement of making money in a rising market invites others to join. The following Rap excerpts are condensed for brevity but the content should help you to quickly recall the “feel” of those days.

How This Market Moves . . . *(November 3, 1999)* Sox up 5 percent. Last week bank index up nearly 20 percent in eight days. Sox has now run 20 percent in five days. Lot of stocks up north of $12-14. Everyday occurrence to see groups of stocks moving 10-20 percent, all are companies that now have $5-20 billion market caps yet they didn't even exist 18 months ago.

(November 10, 1999) Another stunning display of monster moves as happens virtually every day. Liberate Technology (LBRT) up about $34, mere 50-percent move, Next Level Communications (NXTV)up $31, about 150-percent move and iBasis Technology up $24, over 150-percent gain. QualComm (QCOM), the one that goes up a gazillion points a day, up about $20.

Really not possible to give an accurate, succinct description of how crazy things are. Something gets in motion, just continues to move in that direction as folks chase anything that's moving, trying to make money as greed overwhelms every other emotion (save the complete terror that the shorts labor under).

(November 17, 1999) Three stocks loosely related to China go absolutely berserk because China.com (CHNA) has gone berserk. Other day China.com went from $60 to $120 in one day. Traded today as high as $140. So on back of that, had few wannabes go ballistic. China Pacific (???) traded from between 14 cents and $12 3/8. China Resources (??) traded in last two days a range from $5 to $50. China Prosperity (??) yesterday traded from approximately $1 - $11; today traded between $11-$80.

Quite clear what going on has zero to do with fundamentals or investing and has everything to do with massive liquidity injection Fed putting in to forestall Y2K problems alongside general mania in force.

(November 22, 1999) Standout stocks to upside - surprise, surprise - Internet stocks, some real leapers today. Number of nouveau Internet stocks up $10-15, especially optical boys. Standouts include Brocade (BRCD) up $46, Foundry Networks (FDRY) up $30 and SDL (SDLI) up $23. In old-guard department, CMGI was up $18, while Yahoo (YHOO), DoubleClick (DCLK) and eBay (EBAY) all up $8.

The Mania Chronicles

If it wasn’t so Sick it would be Funny . . . From a Yahoo message board post: "I'm going to retire at 25 cause of AMZN. HA HA HA HA!!! I'm a junior at CS Hayward and I plan to live fat after AMZN splits a few more times in the upcoming years!!!! ALL YOU AMZN LONGS PARTY AT MY HOUSE...DEC 2003. We can all discuss how filthy rich each of us are and burn thousands of dollars on my BBQ Grill!!!! P.S. See you guys in a few years!!!!"

So this is how the market is moving and the reality of it is that no one particular day is any more spectacular than another. There are gigantic moves in choice stocks in every technology and Internet sector on a daily basis. One day the brokerages fly, next the semiconductors, then the Internet portals have their day. There could be a paragraph like those above, noting the incredible leaps, for nearly every day in November and on through December of 1999. The media loves to show their charts; they talk about the strength of economy and business, and they’re making stars of the analysts touting the stocks of the day. But the real obsession at this point is with regard to the Fed. Will they raise interest rates again on the 16^{th}?

Even this Fed will Raise Rates . . . *(November 10, 1999)* I'm sure even these irresponsible new-era types will finally get around to giving us a 25-basis-point hike at the next meeting, taking back the last of its 75 basis points of easing from last year. The Nasdaq 100 is up over 160 percent, the Nasdaq itself is up over 130 percent, the Dow is up over 35 percent and the more speculative indexes are up even more. Meanwhile, we've got the lowest unemployment in 25 years, jobs are going begging, people are paying bounties to find employees and we've got incipient signs of inflation, even with the government-cooked statistics. This ought to be something that even these guys can see.

Of course, I don't think the 25-basis-point rate hike is going to be a significant event in ending the mania. When you look at the action right now, and the speculation and euphoria that we have attempted to describe, the best way to sum it up is, we are so close to the action and yet so far. Even if it's a modest amount of time, God knows how many points it could ultimately be.

The aftermath of this only gets worse. The craziness and warping of the economy continues to get larger as more businesses and peoples' lives are changed as expectations get ratcheted up due to the mania. So even if the Fed acts semi-responsibly and raises rates 25 basis points next week, I don't think that it will matter.

Nothing will matter in ending the mania until we reach exhaustion, and then anything will be a good enough excuse to take it down. Who knows exactly when that will be or from how high, but surely we must be getting closer. This type of insanity continues unabated every day and it just gets logarithmically wilder every day.

Show Us the Money . . . Some folks are confused as to how come Greenspan talks tough, periodically mentioning a bubble and talks about raising rates - yet, the stock market still goes ballistic? Well, the Fed can do two things: It can change the cost of money, or it can change the quantity of money. Old Easy Al doesn't know about restricting the quantity of money, all he knows is that he periodically raises what it costs. There's a big difference between making money slightly more expensive and making it not available, which will make it more expensive. But just making it more expensive does not necessarily do much of anything.

To put some of that into perspective, since Sept. 20 of this year, the broad aggregate of money supply has exploded $147 billion. That would take us to an annual rate of an astounding 14.3 percent growth. But for a broader analysis of what's gone on in the money supply, we should step back to Feb. 26, 1996 when M3 was about $4.7 trillion. As of Oct. 25 this year, it was $6.3 trillion. A bit of mathematical equation shows us what has happened and it predicts a doubling of the money supply about every eight years. So there's mathematical proof - as though we didn't see it in the stock market - that Easy Al has engaged in one of the most expansive/exponential money-printing campaigns of modern times.

Any News is Good News . . . *(November 16, 1999)* The best way to describe the early action and the lead-up to the FOMC meeting was: People felt that either the Fed wouldn't hike now because there's no inflation or the Fed wouldn't hike next year because it's an election year. Either way, it's good news because it won't happen or if so, it'll be the last one.

This was the third rate hike. The federal funds rate of 5.50% is now back at the rate it was before the fed began lowering it in response to "the crisis" on Wall Street a year before. What's the scorecard? From the October closing lows, the Dow has gained 42 percent, the S&P 500 48 percent, the Nasdaq Composite is up 132 percent, and the Nasdaq 100 index is up 160 percent. Of course, by the time we see a top in just under four more months for the Nasdaq, it'll have gained another 56 percent while the Nasdaq 100 index is still good for another 60 percent sprint.

1-2-3-hike . . . The old folklore of "three steps and a stumble" was meant to describe what stocks did after three rate hikes, i.e. stumble. I guess new-era proponents want to change it to "three steps and a moon shot," thinking that the markets should blast off on rate hikes. We already know that they blast off on rate cuts.

Lou in a Skirt . . . *(November 18, 1999)* We got the results last night from Hewlett Packard, and they have been spun into momentous good news because the company met the new lowered number. Now what you probably wouldn't know from the reading the newspapers is that for the first time in at least this decade, but the first time I can remember for Hewlett-Packard since the company has been doing conference calls, it did not give out order rate data.

This was another one of those results with a lot of curiosity in them. Receivables were up a significant amount, which really helped the earnings and the tax rates that the company just a month ago had suggested would be at one rate, magically dropped a couple hundred basis points, which helped out as well. The company then talked optimistically going forward but wouldn't support it with the order rate.

For those of you who like this inside baseball stuff, I urge you to listen to the conference replay. You can hear Fred Hickey discuss the results with new H-P CEO Carly Fiorina, a.k.a. Lou Gerstner in a skirt. You won't want to listen to the entire boring call but Fred's is the last question and you can hear him go one-on-one with management as they try to dance around the question of why they stopped giving out good, hard data.

I bring this up to illuminate the practice of spin, spin and spin, and how come there were no other analysts, save Kevin McCarthy at DLJ, who were willing to note that there might have been a problem. Hear for yourself all the dead fish being dead fish and listen to one analyst actually being an analyst.

There doesn't seem to be many bears around these days. Only a few other than Fleck will openly recognize that what is happening with the market is an aberration; it most assuredly is not the hallmark of a New Economy that the talking heads would have us believe. Occasionally, Fleck hands his mike over to another dissenting voice for corroboration . . .

Tech in Another World . . . *(November 24, 1999)* I believe we're in a murky state between a bear market for most stocks and a blow-off for tech stocks. This particular state was recently best described by Richard Russell. Russell has been writing *The Dow Theory Letters* market commentary since the mid-1950s, so he's seen quite a lot. Here's what he has to say about it:

> *"A bull market begins to die when the smartest investors in the nation realize that business has reached the point where 'it can't get any better.' When it can't get any better, there's only one thing that can happen - it will get worse - but that may take time.* ***It's <u>that</u> period that we are in now, and that's why this period has been so difficult to analyze and understand.*** *(Emphasis added.)*
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> *"The figures for last week were so poor that when I saw them, I did a double-take. For the week ending Nov. 12, there were 1,547 advances and 1,899 declines. There were 186 new highs and 341 new lows. Those are abysmally rotten statistics for a week when the Dow and the transports both ended higher. The techs and particularly the Internet stocks are in a fantasy world of their own."*

Yearning for Yahoo . . . *(December, 1999)* I'd like to make one comment on the latest S&P 500 inductee. Yahoo was up about $28, giving it a market cap north of $72 billion. That would make it approximately the 33rd largest company in the S&P 500, ahead of American Express, Dupont, Ford, McDonalds, Disney, Pepsi, GM - you know, a few small companies.

Not that fundamentals make much difference, but it's another amusing anecdote to how wacko things are for a company that makes in essence pennies and is dependent on the stock market IPO machine to create new companies to be able to pay Yahoo money. To pick a comparison, Yahoo's valuation is over twice that of Merrill-Lynch, which in itself is no bull-market piker.

Yahoo Stays Strong . . . *(December 7, 1999)* The big star of the day continued to be Yahoo. At one point it traded up about 72 points to 352 shortly before the close, where it ended at 346 5/8. This gives Yahoo a market cap of over $90 billion. In the last six days, its market cap has **increased** more than its entire market cap was as recently as August! Today was the last day to buy Yahoo before it officially becomes an S&P 500 member, so they'll probably leave it for dead and jump on something else immediately. It does go to show that there's nothing like an S&P induction, as Yahoo has added roughly $35 billion of market cap since it was given the nod. Yahoo's gain proves the point for the umpteenth time that none of this is about investing; it's really just some cross between a video game and gambling.

Speaking of Ridiculous Valuations . . . *(December 7, 1999)* I haven't mentioned them for a long time because it's been a totally meaningless exercise. Everyone knows scores of absurd valuation stories but I was struck by the fact that when one looks at the combined revenue of Cisco and Microsoft, it's around $35 billion for the last 12 months. And yet the market cap of those two companies is around $850 billion, or about ten percent of the GDP of the U.S. gross domestic product.

It's kind of interesting to take a look at Boeing, a world-class manufacturer (although it's been having some difficulties lately) with only one real competitor. This company has $60 billion in revenues for the last 12 months, yet has a $35-billion market cap. So Boeing is a world-class company like Cisco and Microsoft, has revenues 50 percent higher than they do collectively and yet has a valuation that is about 3-4 percent of those two. We can look at a multitude of similar examples, but this one has struck me lately and I thought it would help put things in perspective.

Biggest Leaper Ever . . . *(December 9, 1999)* Today's leaper du jour was the biggest explosion in stock market history. VA Linux, which was filed at $11 and priced at $32, opened at $299, traded as high as $320 and then closed at $250. Just another example in long string of stunning rises in an IPO for a company that hasn't that much to offer except a lot of hype and imagination.

Tongue in Cheek . . . *(December 15, 1999)* A dead fish raised his price target of eBay this morning to $230 from its current price yesterday of about $150. You'll all want to know why, of course. It's because he believes that the stock should trade at 105 times its 2005 earnings estimate. Now, I don't see how anybody can say that; I can't possibly imagine more than a 102 or 103 times 2004 estimates. I mean, 105 times 2005 - that's just ridiculous, isn't it?

The Mania Chronicles

Where Cheap Money Goes . . . Here's a tale that Dennis Gartman told late last week. It's the perfect period piece to capture the mood of the present environment:

"As a final aside for the year, we went to our local branch bank yesterday to transact some business, and spent some time chatting with the branch manager. She doesn't know what business we're in, so when we asked her if she'd seen any increase in personal loans; she replied that yes, indeed she had. Apparently, the personal loan demand at her branch had escalated rather substantively.

"She then proffered that the sole reason for the sharp rise in personal loans was the investment in the stock market. She said that local doctors, lawyers, farmers, auto dealers . . . all of the leading figures of the local economy (and their wives) had been in recently to borrow money to `put into the market.'

“We asked her how long this had been going on, and she said that the branch had been making personal, signature loans like that for some while, but that the demand had really escalated in the past several months and has really become `hot' in the past several weeks. She wondered if it was too late for her to join in the market's enthusiasm!

“We said, `We don't know,' and left bemused and afraid.”

The anticipation of Y2K manifestations turned out to be much more drama than the reality. What was a boring and tedious problem for companies – get all the computers to accept the rollover of 1999, a year ending in 99 to accept the year 2000, a year ending in 00 – was turned into a sensational story about all the things that could go wrong. Granted, it certainly would be a big headache if corporate computers couldn’t reconcile with the date change and messed up databases and lines of code for accounting, billing, taxation, payrolls and what not. But that story somehow got pushed into the background in favor of tall tales and myths: air traffic control computers would malfunction, bank computers might erase records of individual balances, water supplies would be cut off, nuclear plants potentially could melt down, etc.

Cooler heads prevailed. If American genius could bring information technology to the point it had thus far come, surely it could figure out how to overcome a glitch in a two digit numerical code. And yes, of course - and thankfully, diligent people did a huge amount of work to bring computers up to speed. New “Y2K compliant” models replaced older systems or new software fixed the bug.

Predictably, at the stroke of midnight on January 1, 2000, computers still worked fine, lights turned on, there had been no runs on banks, no nuclear bombs went off, no planes crashed, and no one had panicked – except the Federal Reserve Board.

Supreme Speculation . . . *(January 3, 2000)* The equity environment of the last two weeks continued to be speculation, speculation and more speculation. On the back of that, we have been able to power the stock market to about a $17-trillion market cap, about twice GDP. World equity markets now are at about $35 trillion, bigger than world GDP, which is between $25-30 trillion.

Of course, the primary responsibility for that mania lies at the doorstep of the Fed - Easy Al and the Merry Pranksters. They did it by absolutely jamming the daylights out of the financial system with liquidity injections over their fears about Y2K. The monetary base expanded about 17 percent last year and went absolutely berserk during the last three months of the year. The last two weeks alone expanded at a 39-percent annualized rate.

Fed No Friend to Bonds . . . *(January 3, 2000)* The group that took it in the chops the most over all of that liquidity was the fixed-income folks. Last year the 30-year bond was down a little over 14 percent, which is the worst performance ever. The second-worst performance was in 1994, when Greenspan was taking out the liquidity that he'd put in at the beginning of the decade. Two of the worst bond years in history have occurred in the last six years with Easy Al at the helm, so I can't see how any fixed-income investors can be big friends of the Fed.

Another Dead Fish Story . . . *(January 4, 2000)* In the continuation of the mindless trend that's been going on for some time now, we had a dead fish raise his price target for Yahoo to $600 [$300 split adjusted]. That these dead fish continually raise price targets with very little to no justification is just ridiculous and it’s pretty silly that we actually call these people “analysts.”

Working for Peanuts . . . *(January 5, 2000)* Speaking of the Fed, it was amazing to see some of the comments in the press over Greenspan's appointment. To paraphrase Greenspan, when the reappointment was announced yesterday, he said he had a real intellectual fascination with testing theories in the marketplace. He then specifically admitted, "It's a lot like eating peanuts: When you start, you can't stop." I can't believe the guy can go on record saying something like that, but I guess that given his actions, it all kind of fits.

Greenspan received his fourth nod for the helm of the Federal Reserve Board amid lavish praises and camaraderie from President Clinton. The President complimented him for his "wise and steady leadership [that] has inspired confidence not only here in America but all around the world." He then praised him as one of the few economists who had championed the power of technology to boost growth, "I've been thinking of taking Alan.com public," he quipped.

The "peanuts" remark refers to Mr. Greenspan's own explanation as to the question regarding the reasons, at age 73, that he wished to remain in that capacity,

> *"There is a certain, really quite unimaginable intellectual interest that one gets from working in the context where you have to put broad theoretical and fairly complex conceptual issues t o a test in the marketplace. It's a type of activity which forces economists like ourselves to be acutely aware of the fact that our actions have consequences. And it's crucially important for us to try to determine in advance what those consequences are.*
>
> *"And that is a challenge, which I must say to you, is, as I said to the President before, it's like eating peanuts. You keep doing it, keep doing it, and you never get tired, because the future is always ultimately unknowable."*

In separate Washington Post articles by John Burgess and John Berry regarding the nomination, both unwittingly made remarks that reflected the jovial nature of the time. In reference to the peanuts bit, Burgess observed, "Once you've tasted the thrill of having the $9 trillion-a-year economy as a lab to test your theories about how interest rates affect the general well-being, it's hard to stop."

And Berry seemed to have believed that Greenspan had eradicated the business cycle, "In the process, the central bank has gained credibility with investors that it can be trusted not to allow a return to the boom-and-bust business cycles that have marked much of the nation's history." Of course, we know in hindsight that if investors believed in the omnipotence of one Alan Greenspan - a mere mortal, to that extent, they had been quite misled.

However, at this present time, January 2000, it is quite imaginable that investors do, in fact, believe just that. The first trading day of the New Year opened with a big gap to the upside, which was met with a rush of sellers. The dip buyers showed up but the voracity of that day's decline spooked folks enough to take the Nasdaq down a full ten percent over the next three days. Never fear, a good sale must be bought and ten percent marks the first bounce level. The market traded higher for the next two weeks but then succumbed to another sell off at month's end, rendering January a very volatile and slightly losing month for Nasdaq participants. The Dow finished down five percent as well, topping out at 11750 on January 14, 2000.

The Mania Chronicles

A regular reader who owns a pawnshop sent an email explaining, "Had a guy come into my pawn shop wanting to borrow $4,500 some time ago to put into the market. Imagine borrowing money at pawnshop rates to beat the market - now that's confidence."

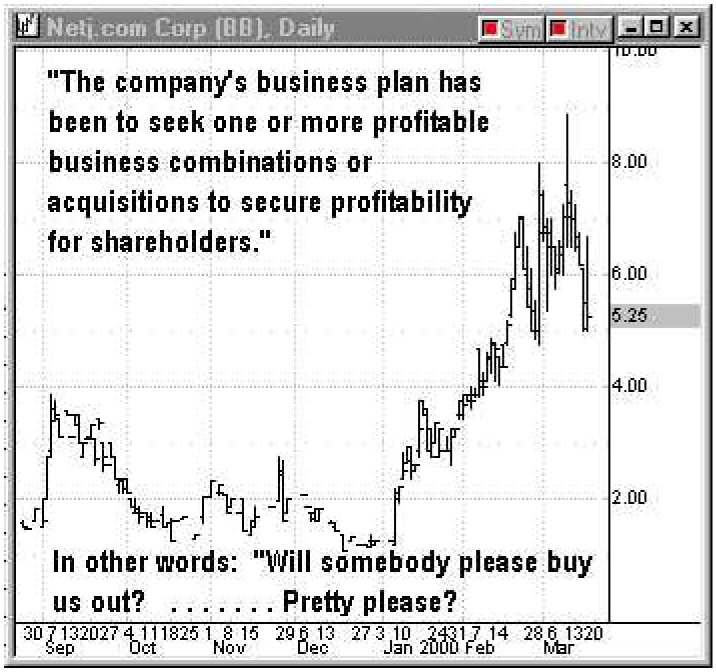
In Today's Slice of the Mania . . . *(January 12, 2000)* Someone pointed out to me that the stock of a little company called NetJ.com in the last five days has gone from about $1 1/4 to $3 and has a market cap of about $20 million. What was most hilarious was the description of the company as it reads on Bloomberg: "NetJ.com Corp. currently has no business operations. The company is seeking to acquire or merge with a business or company."

So there you go: $20 million and counting for something that is none other than a pure piece of paper.

Yahoo.com's Company Profile

NetJ.com Corp. has had no business for some time. The Company's business plan has been to seek one or more profitable business combinations or acquisitions to secure profitability for shareholders. It has had no day-to-day operations up to the present time. NetJ.com's officers and directors have devoted only insubstantial time and attention to its affairs, for the reason that only such attention has been required. The Company had identified previous possible acquisition targets in news releases during the year 2000.

For the nine months ended 9/30/01, the Company reported no revenues. Net loss declined 66% to $331 thousand. Results reflect the Company's lack of active operations. None of NetJ.com's possible acquisitions materialized and none are currently pending.



Over the counter bulletin board stocks provided a faster car for traders addicted to the stock ramp race. The extraordinary movements in penny stocks lend credibility to the cliché that a rising tide lifts all boats – and the debris that floats alongside them. The OTC's are the lowest common denominators in the stock market world, and speculation in these ranks are clue that everything else has become too expensive for the infatuated nonprofessional speculator to participate in any meaningful or otherwise profitable way.

More Stories from the Mania Chronicles

A reader sent this tale about a friend of his who is about to retire as a blue-collar worker from a Midwest company after 40 years of work. He liquidated his retirement plan, brought it over to his broker and dumped it all into a brokerage fund-sponsored Internet fund.

These are real-life examples of the massive speculation and the total disregard for risk that is going on in every-day America. We know the market is speculative, we can see the debt statistics, but I think when you see real stories like this, you realize how crazy it is. This is what happens in an insane bubble: Folks go from very conservative a decade ago and taking almost no risk, to moving into stocks that have some merit. Then at the end of the day in a mania, they own nothing but the most speculative and illiquid pieces of paper they can find. And often times it's 100 percent of their portfolio and in many cases it's even more because they're using margin and running up their debts.

This is how folks wind up losing more money than they started with, even though the market goes up tenfold and maybe only corrects 50 or 60 percent, just to pick some numbers as opposed to an example. When the average person in the street is doing this, it has huge economic ramifications when it unwinds.

Buffett on Long-Term Investing . . . *(January 20, 2000)* In a recent interview with *Fortune* magazine Warren Buffett said, "The key to investing is not assessing how much an industry is going to affect society, or how much it will grow, but rather determining competitive advantage of any given company, and above all, the durability of that advantage."

In other words, you have to look at businesses, see if they have an edge and whether they can keep it. The sole purpose in having an edge is to make money because at the end of the day, it's why we go into business - to make profits. To again quote Buffett:

> *"Sure, you and I can sell each other's stocks at higher and higher prices," he said during a speech. "Let's say the Fortune 500 was just one business and that the people in this room each owned a piece of it. In that case, we could sit here and sell each other pieces at ever ascending prices. You personally might outsmart the next fellow by buying low and selling high, but no money would leave the game when that happened: you'd simply take out what he put in. Meanwhile, the experience of the group wouldn't have been affected a whit, because its fate would still be tied to its profits. The absolute most that the owners of a business, in aggregate, can get out of it in the end - between now and judgment day - is what the business earns over time."*

This is why I have talked about earnings and the warping of earnings through accounting games, and why I have tried to tie earnings to the underlying businesses. Because if you don't do that, everything is just speculation, which is of course what this environment is all about. New-era types and bubbleonians take umbrage at that, but they are so mesmerized by the action that most of them don't even know that what they're doing is not investing.

The Mania Chronicles

A reader wrote: "The 19-year-old check-out clerk at the grocery store in my neighborhood was telling me about his Red Hat and was BITCHING that it wasn't going up anymore! I guess a couple-hundred-percent gain in a few months is pretty bad these days. Another fellow I hunt with was recently telling me how he told a friend of his to pull his money from his investment advisor because the guy only got him a 30-percent return last year! This guy also told me that Microsoft would keep doubling every year... forever."

New-Era Analysis . . . *(January 21, 2000)* Here's a Bloomberg story of a brokerage firm, which shall remain nameless, that had the following to say: "We are raising our 12-month target on NTAP shares to $150 a share, or 64 times trailing revenues. We cannot, of course, support this target on any traditional valuation metric, but if one starts with the premise that current technology valuations are justifiable, then it's not hard to argue for another doubling in NTAP's shares."

Software and Oil Don't Mix . . . *(January 21, 2000)* A feature in the news today was oil prices. Folks seem to notice now that oil is trading in the high 20s. This morning, someone on Bubblevision said that we needn't worry about the price of oil because it doesn't impact the economy very much. The quote was something to the effect that you don't use much energy writing software. While it is true that in this decade, oil consumption in terms of barrels has grown less than 20 percent as fast as the economy, we still are using an incredible amount of it. As should be obvious, people don't buy anywhere near as much software - to follow up on that new-era analogy - as they do gasoline for the tank.

Oil has a tremendous impact in the economy, old or new. Amazon and Homegrocer.com can't deliver their products without it, just to state the obvious. So the rationalization of all potential problems continues.

Dell Warns . . . *(January 26, 2000)* After the Rap had gone to the editor, Dell pre-announced a massive earnings disappointment. Its results will now be flat year over year. So maybe that's why the tech tape was so heavy today - someone knew this was coming, although, I should add that it wasn't so hard to know.

But Delights Dead Fish . . . *(January 27, 200 0)* Dell, after going out 36 1/4 in after-hours trading, got up to almost 41 in the early going, as every dead fish on the planet who didn't see the problem coming, wound up upgrading the stock. More about that in a moment.

Holding the Line on Tech . . . So it would appear that the battle lines were established this morning. Wall Street drew a line in the sand, determined to support tech. That's what it's all about - protecting a position so they can make the prices go up to bring in more money for buying stocks. Wall Street appeared determined not to let the tape go down on bad news as that would end the party.

If this rally fails, assuming we don't get a huge gain from here, it will be very important. Wall Street and the dipsters are making a very high-stakes commitment to the fact that they can turn the tape here and now. It seems like suicide to me, but the fact that they've won time and time again means that there's nothing that they won't try.

January ended with a thud. With the Fed likely to again raise the discount interest rate during their meeting on February 2, market participants realized the risks in holding expensive stocks were escalating.

Energy prices were weighing on the market as well; the cost per gallon of gasoline had hiked around 30 percent while heating oil had doubled over the prices of a year ago.

To round it all out, big names Qualcomm (QCOM), EMC (EMC), Compaq (CPQ) and then Dell (DELL) all issued troubling news regarding earnings or revenues.

The Mania Chronicles

"I am a broker at an independent brokerage firm in Southern California. A broker friend of mine who handles accounts for brokers in the firm who are out, got an interesting voice mail that I think you'd find very funny. The guy called up to say he was in Hawaii at 2 a.m. and wanted to buy stocks in the morning `because we had just had a correction.' This was the morning after the day the Nasdaq experienced its heaviest volume on record, Jan. 24.

"Anyway, after this `correction' - his words - he wanted to buy stocks and was calling my friend because his broker was unavailable and he just had to buy. He wasn't specific on what we wanted to buy (I don't think it mattered) and he wanted to put the purchases on his credit card."

I think the illuminating part of that mania chronicle, as with so many of them, is that it reflects the stories we keep seeing about credit card debt, margin debt, lines of credit people have used - all to buy stocks. I've received many, many more of these than I've shared and that seems to be the most staggering thing - the absolutely rampant use of leverage in all forms by people who arguably are the least equipped to use it. It's damned difficult for the pros to use leverage, as we've seen, like the Long Term Capital blowup. But the people who do other things besides investments for a living are being seduced into trying it.

A financial investor north of the border said: "A client called me two weeks ago to tell me she wanted to withdraw all her money from her retirement account to buy a stock that someone at work told her about. I asked her what the name of the stock was or the symbol. She told the stock was called Nasdaq. This lady is a nurse and doesn't even know what a stock exchange is, but she knows she will make a lot of money from this stock. After trying to dissuade her, she took out 30 percent and she is going to talk to her friend to get the actual name so she can invest. The craziness is alive and well in Canada."

More Stories from the Mania

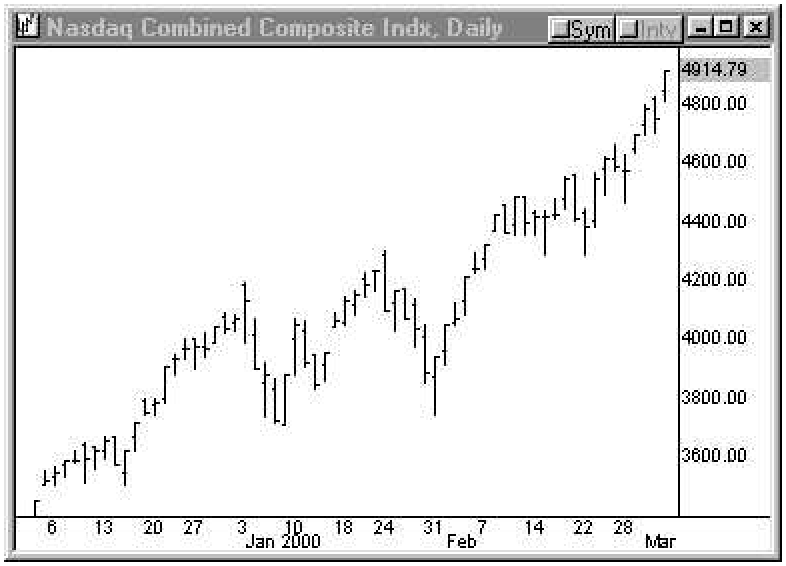
"Today my 16-year-old niece explained to me the wondrous concept of compounding. Additionally, according to my niece, her teacher issued that by investing in `technology stocks,' a `reasonable rate of return' for the foreseeable future should be on the order of 50 percent annually."

"I am an agent for a large insurance company and have a client who is about 30 years old. His grandfather bought him a paid-up life policy when he was a 5-year-old boy. My client never had to pay a dime into this policy again, had earned 7 1/2 percent plus a substantial dividend every year. Both gains are tax-free. It is a great policy.

"Well, he owned Lucent for a while, but when it took a hit on its earnings warning, his stockbroker talked him into getting every dime he had and buying more Lucent at this new steal of a price. He cleaned out this policy and who knows what else he had saved, then loaded up on Lucent."

The Nasdaq Composite had been in decline for the last six trading days of January, shaving 555 points from the high to the low. As if in answer to the downside work that had been done, the bull crowd showed that they were still in firm control as February began, powering the Nasdaq higher by 680 points over the next seven trading days.

During this period, on February 2, 2000, the Fed raised the discount rate by another 25 basis points – the fourth hike. Same song . . . the Fed is ahead of the curve, same dance . . . the market goes up in relief and jubilation.



But then, Fleck says it better . . .

(February 7, 200 0) The market was terrified of the Fed last week, as the Nasdaq managed about a nine percent gain, its biggest increase in about 25 years. The Nasdaq 100 was up about 12 percent, the Sox was up 16 percent and the Morgan Stanley high-tech index was up about 13 percent. Greenspan really knocked the hell out of the equity markets.

The Mania Chronicles

I have in the past referred jokingly to bubbleonians' view of corporate America by saying,

"We don't care if you lie. In fact, we love it. Just don't get caught."

I always thought that was somewhat tongue in cheek. But a reader emailed a couple of posts from a particular thread on Silicon Investor. It seems this isn't just a joke on my part. It is, in fact, how folks feel.

One post read: "Also SI is reporting 61 cents for Intel versus the 69 cents they reported? Why the discrepancy? Did Intel have to fudge a little to beat the numbers? Even if they did, it is a testament to Intel protecting their shareholders."

Another one read: "I really don't know what Intel did, but looking at the stock price, it appears they pulled a muck-up quarter out of gutter to the benefit of the shareholders. To this end they should be trusted and commended. It appears they will pull out all the stops."

So the moral of the story is, shareholders seem to cheer anything that "makes the numbers" and pushes the stock price higher. There's apparently no concern about things that may impair the company in the longer run?

(February 9, 2000) Cisco reported a fine quarter and predictably the stock went berserk, although the best trades were seen overnight, in the wee hours this morning. At one point, Cisco was up nearly $10. I won't bother to tell you that would have been over 150 times earnings or over 40 times revenues. But what might be interesting is that in overnight trade, Cisco added to its market capitalization three years' worth of revenues. Was the quarter that great?

How high is too high? . . . It begs the question of how many points are too many? Can a stock ever reach too high a price? Bubblevision was discussing that Cisco might be the first company to hit a trillion-dollar market cap.

Well, in this mania anything's possible. Cisco managed to get over $500 billion, putting it in a league only with Microsoft. But folks, the whole world's GDP is only slightly above $30 trillion. Can a company with $12 billion in revenues - or even $15 billion or $20 billion - really be worth a trillion dollars, 3 percent of world GDP? U.S. GDP is only $9 trillion, so could one company with that amount of revenues be worth one-tenth of the U.S. economy?

When we look back on this, those are the kinds of big numbers that will cause people to say, how did anyone ever think those things were possible?

In the Mania Chronicles

I have a longer piece to share from a regular reader. It's one of the most insightful emails that I've received out of the 20,000 I've seen in the last four years.

"I work with a bubblehead at a medium-sized media company. I have been a contrarian since 1996, when I thought most stocks were about 50 percent overpriced as opposed to now, where I think they are about 77 percent overpriced - and I have been consistently wrong year after year about the coming crash. Working with the bubblehead, however, has given me great insight as to why I am wrong again and again.

"This bubblehead bought some stock in a dog biomedical company that has never earned a thin penny in its life. At $14 a share, nothing but a risky drug called Campath in the pipeline, and -3.50 per share in earnings, I told her I would walk away. The stock then zooms in one month, for no real reason, to over $30 per share and I have to listen to this bubblehead tell me what an idiot I am every day. Now she has applied for a mortgage on her home and has taken cash advances from two Visa cards to buy - you guessed it - even more of the stock!! Her plan is to have the house paid in full within the next couple of years.

"And that is when it hit me - this is why the bubble continues to grow. Bubbleheads keep saying to us `levelheads,' `Hey, you were wrong for the past four years - you said a crash was coming and it never came - so you are probably wrong about the future too.' The `winning `keeps them at the table' - it's like a fever, something you might see in a casino. The mania continues to grow because idiots are willing to actually borrow money to invest.

"The problem I see is that as these jerks keep pushing the market up, the greater will be the damage when the whole house of cards comes crashing down. Thanks to my bubblehead I have to pray every night that she is right and I am wrong, because now if I'm ever right, the market will probably take us all out in one fell swoop.

"Like it or not, we contrarians are, for all practical purposes, `co-invested' with our bubblehead friends."

Our reader has made a terrific point. We are all in this together, bubbleheads and levelheads alike. That is one of the unfortunate ironies of the process. As the mania has occurred, folks who don't believe in it have not benefited from it, but when it unwinds, everyone is going to pay a big price.

As the Dow and S&P diverge from the Nasdaq, volatility has become hallmark in terms of how the market trades. The volatility isn't just a day-to-day phenomenon; wild swings occur throughout the trading day on a regular basis as well. The further that the markets diverge – rather the Nasdaq climbs - the more spectacular the sight is to behold. Of course, these moves are only a prelude of what is to come after the top and on into the bear market but the escalation of such occurrences offers one more clue that the end for this bubble creeps closer.

Panic Selling Drives Tech Stocks all the way back to Monday's Prices . . . *(Friday, February 11, 2000)* For no particular reason that I could discern, the selling began slowly this morning, picked up steam throughout the day, and then accelerated in the final hour. With about a half an hour to go, we hit the lows with the Dow down nearly 300 points. It's amazing that once again, the Dow was down more of a percentage basis than the Nasdaq. Going back to about the end of October, the Dow is essentially flat while the Nasdaq's up about 40 percent, so the Nasdaq has plenty of downside room once it starts heading in that direction.

Abby Plus Maria Equals Big Rally . . . *(February 14, 2000)* In carryover of our weakness of Friday, the rest of the world was weaker last night. However, since we've had our ten percent correction, Abbey Joseph Cohen and Maria put their heads together and decided that it was time to buy. That was the broadcast early this morning on Bubblevision, so I'm told. In addition, Joey *(Battipaglia)* raised his yearend price targets for the Nasdaq to 5,000 from 4,250.

You Go Girls . . . It's just amazing what ten percent down can do in terms of convincing people it's time now to go higher once again - as if it's somewhere in the U.S. Constitution that ten percent is all the farther that a market can slide.

In the "Can You Believe What She Just Said?" Department . . . *(February 14, 2000)*
And speaking of Abby Joe, her firm released a study in the Wall Street Journal that "suggests that business-to-business uses of the Internet will push the economy to 'a permanently higher level of output' while inflation will be unchanged. It adds 'equity markets will benefit most due to higher output and increased profits, although less-favored businesses will suffer reduced profit margins.'"

I guess we'll know which ones are less favored because they'll be the stocks that go down. It reminds me of the remark about equity prices being on "a permanently high plateau," as forecasted by Irving Fischer in late 1929.

Love Those Message Board Posts

Here's where you go to get free investment advice in the New Economy. St iber is lamenting his/her lack of finesse in nailing the buy and sells just right, and had been wondering if he should dip a toe into CMGI, or had it already run too far? Then, there is the friendly advice given back:

Stiber: "Well, from past experience, whenever I buy a stock, it is at the peak, whenever I don't buy, it keeps going up, and whenever I sell, it goes up powerfully (INSP and CHKP come to mind)."

Lisa6: "Well, CMGI basically is my past experience. I bought it on the way up at 113, watched it peak @126 and then plummet straight down. I just kept thinking, 'wow, am I bad at this investment stuff!' But I had done enough homework, on these boards and off, to know that there was something special about this company and I held, and have been handsomely rewarded. My advice is, if you're looking even semi-long-term, don't worry about your timing on this stock. Hold long enough and it will make you money.

The Joke's On Us . . . *(February 14, 2000)* I got an email from a knowledgeable bond market observer, stating:

> *"Remember all the talk of a 'giant sucking sound' of liquidity being taken from the market by the Fed post Y2K? Well... MZM... Poole's favorite indicator of monetary conditions (he being a monetarist in olden days) just hit a new hig h. M3-M1 (lagged), my personal favorite monetary indicator, also just posted a new high. The financial system is bulging with an incomprehensible amount of monetary stimulus. This monetary condition . . . is not the stuff of bond rallies or economic slo wdowns. Print money. Accept applause. Print money. Accept applause. The Fed is a complete joke."*

The Mania Chronicles

"The small town in which I live has an ancient but beautiful city hall. The elevators in this building are still run by elevator operators, and the other day an elderly man working in this capacity smiled broadly and suggested that I buy Juniper Networks. He'd `made a bundle' and had no interest in ever selling. Ever. Instantly I was struck by the irony of this situation as it related to 1929, thought it over and called my broker. I'm now 100 percent in cash, and I think the crash you've been predicting now is just around the corner."

Caught on the Message Boards

I want to share a couple of posts from SI from yesterday. The first one read: "Hey SSP, since the time I quit my job today ($11 per hour) at 1 p.m., I've made $1,400 on the computer! MAMH! MBCH! PAGE! TNRG! Now I have to explain this to my wife! I hope I don't have to use violence! LOL! "

And the reply post: "Right now I'm only long TNRG! I quit my job today too! I will be trying to make a couple of hundred dollars a day trading stocks! With the help of all these great guys on Golden Lists, I think I can realize some good profits! I think PAGE will continuously go up in price, but like I said I only want to make a couple hundred bucks a day and may sell real quick!! After hours looked good on PAGE. MBCH, I made $2,000 on Friday! Got back in today at 34 cents (30,000 shares). Hope it goes to 50 cents tomorrow and I WILL SELL QUICK!! MAMH I like because my friend is in it!!!"

It was a big problem back in the 1920's and it's become an ominous symptom of this bubble as well. Margin debt is moving higher at an unprecedented pace. It's a form of leverage, allowing an investor to trade 50 percent more money than his account's tangible value to speculate in the open markets (In the 20's margin allowance was 90 percent of one's account's worth). What one has is not enough if there's extra money available – even if it does come with a price tag – to buy even more shares. But the problem with margin debt is that once all the money is in and the market runs out of buyers, prices start to fall. Most people, in their newfound professions of trading (or "investing" – as so many of them believe that this is what their market participation is), have never seen more than a ten to fifteen percent correction and lack the trading experience to know when to cut and run or which dip is going to bite them. Until now, every dip has been an opportunity to get in, but one of these days, the market is not going to go higher. Instead, it is going to fall precipitously.

Margin calls mean a loss of capital. As the account's worth shrinks due to falling prices, the borrowed money for equities gets recalled by the loaning broker, but the stock prices are much less now than what they were when the stock was purchased. The lending broker has to be paid and players selling out to meet margin calls - when no one is buying – sets the scene for gut wrenching losses.

When we started this section of market memoirs, October 1999, public margin debt was $182 billion. That alone was a 40 percent increase over the same period the year before. Now, in February of 2000, that indebtedness has taken an even sharper upturn of growth to $265 billion. At the height of this mania, in March of 2000, that figure will climb to $278.5 billion – a $96 billion dollar increase in six months! For a bit of perspective, consider that in the year 1996, the total average monthly margin debt was just over $84 billion. Furthermore, margin debt as a percentage of total market capitalization is just above 1.5 percent. This is A) a greater share of total market capitalization than at any point since 1929 and B) the closest it has come in recent years to levels registered on October 1, 1987 – just a couple weeks before another well-known market meltdown, Black Monday, October 19, 1987.

When reforms were made during the Great Depression, one piece of legislation, the Securities and Exchange Act (1934), empowered the Fed to regulate broker loans for the purchase of stock and speculation. The current rules, in place since 1974, provide that investors may borrow up to 50 percent for equity, mutual fund and convertible bond purchases, up to 85 percent of municipal bond values and up to 95 percent of the value for U.S. Treasury securities.

A quiet debate was revived in and among financial circles that raising margin requirements would help to curtail the speculative fever, thus reduce risk to individuals using margin and the broader market from margin induced selling. In the past, financier George Soros and Stanley Fischer, deputy director at the International Monetary Fund, had both advocated that the Fed release a little air out of the credit bubble by raising margin requirements. But Greenspan had always resisted this suggestion claiming that he did not want to infringe upon people who needed to borrow money to participate in the stock market.

During the Senate Banking Committee confirmation hearings on January 26, 2000, Senator Charles Schumer (D-NY) candidly explained the concerns and recommendations of market-affiliated people from his district. He correctly cited escalating margin debt numbers and comparisons, foreseeable dangers to individuals and the broad markets, and then directly asked the Fed Chairman why, if he had considered raising requirements, had he not done so.

> *"I've talked to a good number of people in New York in the markets and elsewhere. T hey are truly troubled by this. And when I – the rate of increase of some of these stocks that seem to have no relationship to reality. That's not the blue chips. That's not the existing 'dot coms.' And that's not even some of the new ones that have a great idea.*
>
> *"But it seems people just come up with the idea of a company, put 'dot com' after the name and just ride the rollercoaster. But the small investor is often left holding the bag. The big investors ride them on the way up; they're out; they're not as heavily borrowed on the margin as the small investor. I don't see any other solution. As mentioned, I've talked to a lot of people in the markets. They are very troubled by this. They say a solution is margin – you know, is to raise the margin r equirement to help tamp things down without taking away – you know, without creating a really major problem.*
>
> *"So my real question is, because I know you've considered it, why haven't you done it? What is your objection to it? And what would be an alterna tive strategy rather than sort of standing by and going, 'isn't this a shame' or 'aren't we worried about this.'"*

But Alan Greenspan, in his characteristic circuitous verbiage, countered to the Senator once again that raising margin requirements would discriminate against the small investor and that studies had "suggested that the level of stock prices have nothing to do with margin requirements." Furthermore, he stated that the Fed was well aware of the numbers, that they had "moved up at a pace which has created a good deal of evaluation on our part and obviously other supervisory regulators, and there's been considerable conversation going on with respect to addressing this issue because it goes beyond the mere issue of stocks."

To which Schumer asked, "Is there an alternative to doing either nothing or raising the margin requirements? Is there a better way to deal with this?"

> *Greenspan replied, "I would prefer – the answer is that we obviously have also been discussing other alternatives that there are , and you have to be careful. It's very easy to invent all sorts of new schemes*

that allegedly are going to do something and when put into practice turn out to be less than perfect, if I may use such a term. I don't want to suggest that we are about to do anything at this stage, but I would confirm that we obviously do a good deal of thinking about the whole process."

Mr. Schumer was undoubtedly left dissatisfied with Greenspan's reply. Two days after the hearing, Schumer asked Banking Committee Chairman Phil Gramm (R-TX) to conduct separate hearings on the subject of margin debt. Those hearings were undertaken on March 21, 2000. So far, nothing has changed.

Greenspan Clueless . . . (February 17, 2000) Over at the House Banking Committee, Alan Greenspan was once again demonstrating a total lack of understanding of what makes markets work. When queried on changing margin requirements, he stated that they would have no effect on prices. My rhetorical question is, if changing margin requirements has no impact, how come commodity exchanges do it regularly?

Hit 'em Where it Hurts . . . f*rom a January 25, 2000 Rap regarding margin issues* - It's interesting that Greenspan doesn't seem to notice what the folks at the New York Merc have noticed about heating oil. This morning, Joanie pointed out:

"Y'all know about the cold snap and the resulting surge in prices which led crude along, right? Well, they busted heating oil 11 percent yesterday in the blink of an eye. How did they do that? (Al.com, pay attention here) Besides the call for milder temperatures, they had the audacity to raise margin requirements for February heating oil - are you ready - by a steep 80 percent, effective on the close yesterday. This margin hike is on the heels of a 25-percent margin hike last Friday on crude and products future trade. So, if you want to weed out the speculators, hit 'em in the pocketbook, right?"

It just goes to show you that raising margin requirements does cool speculation, and it's a much more effective tool than raising interest rates.

From the Mania Chronicles

A reader writes: "Recently, I was on vacation in rural New Mexico. I stopped into a Native American Indian store in the middle of nowhere, hoping to buy a souvenir. The place was nothing more than a roadside shack. Inside the place was an elderly Native American woman, and almost nothing else except for one item: a brand new color television, which via the outside satellite dish was tuned into CNBC.

I asked the woman if she invested. She smiled broadly and showed me a large packet of mutual fund and brokerage statements. She told me that she used to drive two hours each

Friday night to a tribal casino, but now she was more interested in the stock market. That revelation was less than comforting to me."

So as these chronicles continue to make clear, we have managed to get into every nook and cranny on the planet in terms of herding folks into the market.

At some point, the consequences of this dramatic misallocation of capital will result in substantial suffering, and folks will say, how could we not have known? And sadly, the answer will be, because you chose not to know.

More Bubble Trouble . . . *(February 17, 2000)* It is striking to note that Japan continues to be mired in the aftermath of its own speculative bubble, even though it has been ten years and counting. While there has been a certain speculation in Japan's over-the-counter market, its stock market is still down 50 percent from the highs and the economy is still a mess. The moral of that story is that when you have bubble in your country, it takes a very, very long time to right it.

It's been over a decade in Tokyo, and it took well over a decade to repair from the 1929 bubble. That is why prudent central bankers try to prevent them in the first place. They are much easier to prevent than to fix afterward. This is also why I continue to drone on about the dangers, and why I have held Greenspan in such low regard. In my opinion, the aftermath of our bubble will be far worse than Japan's, because this bubble is so much bigger.

The Mania Chronicles

From a reader who is a money manager:

"I've got a client who has very successfully run a business for the past ten years and has become fairly wealthy. He asked me what I do, so I told him how I like sure things such as cash takeovers with room. I told him about a few we had in the works and said he wanted that type of investment. We sent him the paperwork for an account.

"In the week and a half it took to get his paperwork back and the account opened, he started buying high techs at another firm. I talked to him Thursday and he told me about the $3 stocks he sold for $4.50. The $15 stock he sold for $22. Everything is 'e' this and dot-com that. He has $150,000 in trading stocks and asked me which high-tech fund he should put, get this, $500,000 into! This guy had all his money in government bonds up until January, and now he wants high-tech funds!?!?!

"Then he said the ultimate to me - 'I've learned a lot over the past month. I've really got the hang of this stock trading stuff already. I know what I'm doing. I've already made more in one month more than I made on all my money in the bank last year!' I told him I was still buying my boring takeovers. He wasn't interested. Fifteen percent isn't good enough anymore. He's swinging for the fences. He wanted a 'real mover.' He told me I didn't know what I was doing and I was out of touch, I had to get where the action was.

That's great, one month of experience (read - luck) and he is the expert and my 15 years' experience is worthless."

This little nugget illuminates both greed and the fact that, unfortunately, some people have apparently confused a bubble with brains.

Caught on the Silicon Investor Board
February 20 , 2000

"It is good that interest rates are rising. The rates are killing off the old, indolent, inefficient, rust bucket, 19th century leftover corporations whose continuing existence has been held together only by a benign environment. It would take an instantaneous Fed funds rate of 30 percent to slow the new economy corporations because that's what their effective growth rate of wealth is."

Dead Fish on Display . . . (*February 24, 2000)* This morning, the dead-fish society had its best on parade. We had analysts crowing about the Gateway meeting yesterday. The rationale: Gateway was positive about its earnings outlook for 2004, among other things. This is a company that can't give accurate guidance for the next quarter.

And one of our favorite fish from the Dead Fish Hall of Fame - the one with a former $150 price target on Micron - came out and upped his recommendation on Intel this morning. It's interesting to note that this leading proponent of Windows 2000 driving DRAM demand, hasn't mentioned that DRAM prices have plunged to a new low of $4.60, down from $8 recently - one of the fastest declines on record.

There's today's example of analysts completing ignoring the obvious to tout stocks and try to break charts out.

And today was a complete speculative orgy, where the participants displayed utter disdain for any thought that the market might at some point ever take their money instead of making them rich. We've seen the creation of a perverse environment where many of the worst companies or companies executing in the poorest fashion see their stock prices go berserk, while good companies at fair prices continue to sink.

This has become a giant game of chicken between the public (and the fund managers they have chosen) and the capital markets. While it's not debatable who will get hurt in the long run by being macho, the present-day displays of bravado are truly a sight to behold. Of course, the game has been aided and abetted by Wall Street manipulation on the part of the dead-fish community and the big mutual fun/hedge fund boys, not to mention corporate America's playing the earnings' bastardization game.

The Mania Chronicles

Surely, everyone is "in":

"I was installing a network card in my neighbor's PC so he could hook up a second PC to his cable modem, and he started talking stocks. He said to me: 'I'm not greedy, I just want my 15 to 20 percent a year.'

Guess why he wants the extra PC hooked up??? Seems his 76-year-old father wants to start trading stocks on the Internet."

And in the continuing saga of everyone being in – and not just in America, but clear across the pond - here's one from Germany:

"A friend of mine told me that recently his 60-year-old mother started to invest in the stock market. Her strategy: She picks from the television ticker a stock that has suffered quite a loss over the past couple of days and buys it. She has no clue what kind of business the stock is into. Her only criterion is that the stock is listed on the 'Neuer Markt' (the German equivalent to the Nasdaq). She doesn't even know how to pronounce the names of the shares, as she is not familiar with English.

Finally, can you come up with a better example of how the economy is being warped because everyone is "in?"

"A family friend, who is a mid-level insurance salesman, just informed us that he is quitting his job of 11 years. He is 41 years old, married, with three kids. He told us he is preparing to move his family from here in Ohio to a tiny town high in the Rocky Mountains, where his new job will be that of a day trader. That will be his only way to pay the bills.

"He's armed with about $100,000 in life savings, a laptop computer, and an online discount brokerage account. Apparently, he says he was motivated by a late-night 'trade your way to riches' infomercial, which convinced him he could move to the mountains, trade by day, and live the life he's always wanted. He made his first foray into the stock market a few weeks ago, when he bought a stock at 50 cents and sold it the next day at $3. He said he gave notice at his job the next day.

Fed Fodder . . . *(February 25, 2000)* Richard Russell had a great synopsis of what the Fed has fomented, and so I thought I would share it here with readers:

> *"What happened is the Fed flooded the banks with reserves as it prepared for a disastrous Y2K. When Y2K never happened, the Fed didn't have the guts to shrink the reserves. The Nasdaq went wild and the Fed still didn't have the guts to do anything but feebly mess with the Fed Funds. Now Greenspan knows the Nasdaq is in a dangerous bubble, but he's too frightened to pierce the bubble. Didn't he tell the Senate Banking Committee that you can't even tell if it's a bubble until AFTER the EVENT. Come on Alan, you've backed yourself into a corner. No margin boosts, c'mon, stop kidding yourself, you're going*

to have to do something or take the consequences. Those little 1/4 point boosts in the Fed Funds don't work.

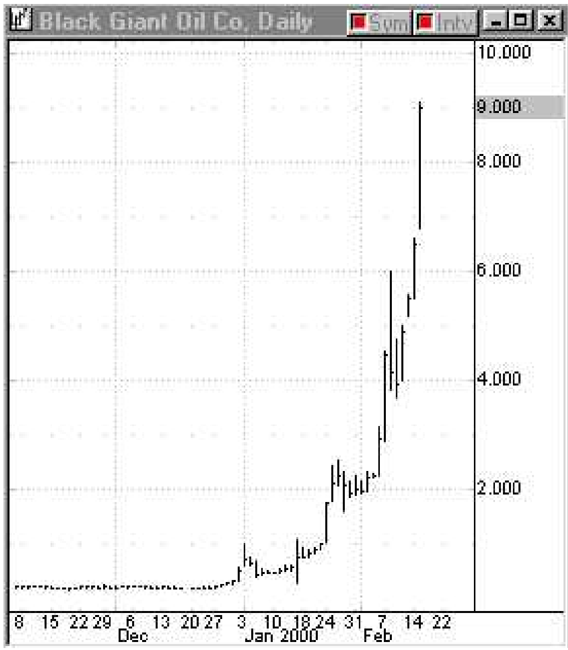
"But the bear is doing the real work, and you're not going to like what the bear is doing at all (assuming that you and the bunch at the Fed even recognize what's going on). It's the worse of possible worlds for you, Alan, the Nasdaq in a dangerous bubble and the rest of the stocks in a vicious bear market. Fun's over - this thing is getting serious and pretty soon you won't know whether to raise rates or lower them."

From the Mania Chronicles

A reader writes: "I was at a gas station here in Southern California recently and overheard a conversation that you'd like. A clerk who was finishing his shift for the day went into the back office. The other clerk asked if he was heading over to the casino (an Indian casino was across the freeway). He said no, that he was going to watch CNBC and do some trading for a while. Thought that said it all..."

And here's one from another reader who offers "a note from Native American land, where we are no strangers to economic bubbles."

"I think I have come across the deal of all deals, the bulletin board dry hole turned cyber chic. After drilling their last dry hole, a company named Black Giant Oil here in our great state has decided that there is much more oil on Wall Street than there is in Oklahoma and the best way to recover it is to change the name of their company to Broadband and Wireless Int. Check it out, from BGOC to BBAN in one day and from $2 to $12 in no time. The rumors are flying, references to McCaw and CSCO are whispered in the same breath. This has to be a sign. The end must be near. If only my pockets were deep enough and there was stock to borrow. Enough said."



Another reader penned this "Open letter to Flim Flam Al and his bunko artists at the BLS:"

"Dear Al, "Thanks for the great news. I was beginning to worry that inflation was starting to rear its ugly head. You see, Al, for the past three years, my rent has increased every six months because of supply and demand. (By the way Al, I leave in the D.C. area, your own backyard. And of course, I can't deduct the rent because of the powerful NRA lobbyists.)

"Since I'm single, I do all my own grocery shopping, and of course everything I buy has gotten more expensive in the last six months. Also, I can now fill my gas tank with a 20 instead of a 10. But I know food and energy aren't important, so just ignore my babbling, Al. On the bright side, more SUVs are stacking up at the local car dealers, so maybe I'm in less danger of getting crushed by one.

"On a personal note, Al, would you please call my dentist and my HMO provider, because they have insisted on raising their rates. Will you tell them there's no inflation? Oh, just between you and me, Al, I'm self-employed and I can't storm into my employer's office and demand a pay raise, so thankfully I can't contribute to wage inflation.

"Thanks for listening, Uncle Al."

Sox Explodes . . . *(February 29, 2000)* Intel notwithstanding, the Sox was where it was at today. It exploded by ten percent, up 104 points. Just to put that number in perspective and bore you with a few fundamental details, at the end of 1995 the Sox index was about 200. The index now stands at 1170. What's interesting is that semiconductor revenues worldwide at the end of 1995 were just about even with where they were at the end of 1999. In other words, even though this index is up sixfold, semiconductor revenues are about the same as they were in 1995. I guess the logic must be that they were just too darned cheap back in 1995.

But one must remember that this is month end, so maybe some of the power in the Sox index, as well as other favorites, was related to guys making sure their portfolio looked dandy for the end of the month - who knows?

In the Mania Chronicles

"I have a 15-year-old son. Recently while shuffling him and one of his high-school-freshman pals around, I overheard an amazing conversation between the two boys. Seems my son's pal was in a rush to get home so he could check on his high-tech stocks. He opined that from his reading of the charts, he was certain that they would be making their next explosive move up, and he wanted to buy some more! "From the mouths of babes..."

And here's another from a reader who offers a staggering example of how leverage is being utilized:

"I work in credit card customer service and have been stunned by the number of people using their promotional balance transfer checks to make deposits into their brokerage accounts, especially at on-line trading firms. They call me late at night anxious to confirm the transfer of funds, with the obvious intent of trading right from the opening bell. The teaser rates on the cards start quite low but within six months they'll be paying at their usual merchandise APR.

A few times I've asked, `Are you a Bull or a Bear?' but I don't bother anymore. While it's no surprise these folks aren't rushing to buy puts, none of those 'investors' even knew it was possible to make money in a declining market. God help us all."

The top is coming. Chapter three brings the full detail of the days surrounding an astonishing spectacle – Nasdaq 5000 – and the beginning of its landslide along with a few more incredible stories from The Mania Chronicles.