YAHOO! FINANCE

Why You Can't Trust Wall Street's Predictions for 2012

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By Simon Maierhofer | ETFguide – Tue, Dec 27, 2011 10:01 PM EST

It takes years to build trust and only an instant to destroy it. When it comes to market forecasting, trust is essential. Can you trust Wall Street's 2012 forecasts?

What if You Trusted Wall Street's 2011 Forecast?

'Five Wall Street heavyweights say it's time for individual investors to shun the perceived safety of bonds and get over their fear of the U.S. stock market so they can take advantage of what they predict will be a third straight year of solid gains for stocks in 2011.'

Before you go out and buy stocks, beware that you just read the 2011 outlook printed on the front page of USA Today's December 17, 2010 edition. USA Today wasn't the only one distributing Wall Street's Kool Aid.

'Outlook 2011 - 10 strategists see the S&P 500 finishing next year at 1,373' - Barrons, December 18, 2010

'Long way from dog days: 2011 might see record Dow' - AP, December 17, 2011

'Greenspan says U.S. economy is gaining momentum, may expend 3.5% next year' - Bloomberg, December 17, 2010

2011 Casualty Report

Wall Street's bullish outlook paid off for the first 34 trading days of 2011, but starting in mid-February the major U.S. indexes a la Dow Jones (DJI: ^DJI - News), S&P 500 (SNP: ^GSPC - News) and Nasdaq (Nasdaq: ^IXIC - News) suffered a series of set backs.

As the chart of the S&P 500 below shows, there was one major high and one major low along with a number of minor highs and lows within a general trading range.

What was Wall Street's advice right before the May high and the October low? Buckle up, enjoy the ride and get ready to make a brand new New Year's resolution.

Guilty on All Counts

The S&P 500 topped on May 2 at 1,370.58. Ironically that was the same day Osama Bin Laden's death hit the wire (so much for news driving the market). Here are some headlines found right before the May high:

'World revs up U.S. profits' - Wall Street Journal

'GE CEO Immelt says global economy is improving' - AP

'The S&P 500 breaks out' - Yahoo Breakout

'The Dow's going to 20,000' - Yahoo

'Sales Growth the big surprise on Wall Street' - AP

'Buffett says odds of another U.S. banking crisis low' - AP

Quite to the contrary, the May 1 ETF Profit Strategy Newsletter recommended to go short at 1,369 with a tight stop-loss. This trade was in line with the outlook provided in the April 3 ETF Profit Strategy update: 'In terms of resistance levels, the 1,369 - 1,382 range is a strong candidate for a reversal of potentially historic proportions.'

Over the next few weeks, the newsletter recommended to lock in profits a couple of times, but most importantly reaffirmed its recommendation to go short before the summer meltdown occurred.

The Perfect SeeSaw

From July 7 to October 4 the S&P lost 20%. On September 23, the ETF Profit Strategy Newsletter foretold that: 'From its May high at 1,370 to its eventual low, the S&P will likely have lost about 300 points (22%). This kind of move validates a counter trend rally. The plan is to square short positions and buy long positions around 1,088. The rally, once underway, will probably re-inspire a certain degree of confidence into the market before it runs out of steam. The most likely target for this rally is S&P 1,266 - 1,282.'

By now you probably guessed that Wall Street's take on the market was different. Here's a brief sample of headlines:

'Think the economy is bad? You haven't seen anything' - CNBC, October 3

'S&P enters bear market territory' - Reuters, October 4

'S&P falls to the bears' - TheStreet, October 4

What effect did Wall Street's guidance and the media's cheerleading have? On October 2, two days before the onset of a massive 20%, 18 day trading rally, the Associated Press reported that: 'Wild market ride is driving people out of stocks.'

Thanks to the lethal Wall Street/media combo, many investors sold at the worst time, again.

Asset-Overreaching Incompetence

Wall Street had the same rotten timing when it came to gold (NYSEArca: GLD - News) and silver (NYSEArca: SLV - News).

Silver spiked to nearly $50 on April 28. On April 27, the Wall Street Journal reported that: 'Silver rush spreads to stock market. Investors have turned to precious metals amid worries about inflation and the weakness in the U.S dollar. The metals are increasingly considered attractive as a permanent store of value that doesn't diminish like paper currencies.'

The April 25 ETF Profit Strategy update pointed out silver's gap up open and warned that: 'The gap up open may have been an exhaustion gap and cautions that a historic reversal may have occurred.'

The Next Profit Opportunity

The October 4 low proved to be a great buying opportunity. Since the S&P reached my target range of 1,250 - 1,300 however, the performance has become stale. Via the November 30 ETF Profit Strategy Newsletter I assumed that: 'Based on seasonality and today's volume it appears that higher prices are likely. I would like to see a slow grind within the 1,226 - 1,xxx (reserved for subscribers) range. This would suggest a virtually untradeable December followed by another great opportunity.'

This 'great opportunity' is not here quite yet, but a quick glance at VIX shows that volatility creates a double bottom in December/January, which usually coincides with a January top of some sort for stocks.

The ETF Profit Strategy Newsletter identifies the up side target of this rally and the must hold support along with a concise, easy to understand short, mid and long-term forecast.

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