02 August 30th 2011 CNBC Mad Money Jim Cramer Stock Market Show Opening

I'm Jim Cramer and welcome to my world.   Other people want to make friends I'm just trying to make you some money. My job is to entertain, to coach, to educated, to teach. So call me at 1 800 743 CNBC. Investing ain't easy but it can be a whole lot easier and much less daunting then you probably think with a little instruction.

The whole business to manage your money is made much more confusing and difficult because of all the arcane terminology.   I call the authentic Wall Street gibberish. And if you're not clued in it can sound like the pros are speaking an entirely different language. You gotta remember that there's an entire industry of people who want you happily convinced that investing, frankly, is too hard, head scratching. That ordinary people like you and me can't do it and the safest thing is to give your money to a "pro." Now maybe that is the right thing to do for some of you, particularly the time constraint. But if you can put in the effort, now I know it would be if you put in one hour of homework per week per stock, then at least I know you can beat these professionals.

The fact of the matter is that many the pros all after your fees, more interested in taking your money thann making you money and that often means keeping you a little bit ignorant about the market so that you'll stay in your stock chains. I like to compare them to the Wizard of Oz. They don't want to peak at the man behind the curtain. They don't want you to understand, because if you did, then you might very well take control of your own finances, pick your own stocks, and not pay someone else potentially exorbitant fees to do things the you are perfectly capable doing yourself and that's where I come in.

Tonight I'm pulling back the curtain. I'm explaining everything because while authentic Wall Street gibberish can sound complex, even impenetrable, it's not rocket science. Not brain surgery. You don't need to go to business school or work at an investment bank to understand it. You can comprehend all the mystical sounding vocabulary that we throw around as long as you have a translator, a coach like me who can explain what the darn words mean. I want you think it me as a defector. Someone who used to play for the other team, imagine five hundred million dollars of already rich people's money in my old hedge fund, but who's now playing for you, teaching you how to navigate your way through the minefield of the stock market every week night on mad money. Forget that Da Vinci Code. Forget them enigma. To be great investor you got a break the wall street code and I'm here to help you crack it.

That's why tonight I'm giving you my wall street gibberish to plain English Dictionary. Consider this a glossary of the most important terms you absolutely must understand if you're going to actively manage your own portfolio. Words and concepts that many people in the financial industry don't want you to get your heads around since then you might actually feel empowered enough to pull your money out of their mutual funds and stop handing over your fees and commissions. Even if you're a pro, you may not know enough. So I why not take advantage of my 30-plus years investing experience and give yourself an extra edge?

Let's start with a couple of extremely important ideas that go hand in hand. These are the things that baffled me. I had them first explained after 10 years of listening to Wall Street week with the great, late Lulu Kaiser, the two terms cyclical and secular. You hear these all the time, all day, yet no one but me ever bothers to explain what they mean even though they are crucial when it comes to picking the right stocks. Cyclical has nothing to do with the spin cycle or your washing machine or Wagner's Ring cycle (some good class music there) and secular isn't about the separation of church and state or public versus parochial schools.

We say company is cyclical if it needs a strong economy in order to have its earnings grow. It's cyclical because it depends on the business cycle. So who's cyclical? US Steel, they need the economy. New Core, right? They fall in this category. Caterpillar. Raw material companies, Dupont... These companies, even though they're well-run, all of them, are all hostages to the vicissitudes of the economy. When it heats up, oh man, when it heats up I gotta tell you there's no stopping them. You know what they do? They earn a ton of money and we're willing to pay more for those earnings but when it slows down...sell, sell, sell, sell, sell, sell...when we shift into recession mode, they earn less money, and investors pay less for the shares.

A secular growth company on the other hand is one where the earnings keep coming regardless of the economy's overall health. Think of anything you can eat, drink, smoke, brush your teeth with, use for medication, okay? You see you got consumer staples like Procter & Colgate, the foods like General Mills and Kellogg. Tobacco like alger. Drug stocks like Pfizer or Burke. These are the classic recession-resistant stock so you want to buy when the economy slows down and investors flock to stocks that can generate safe yet consistant earnings. You don't stop eating food or brushing your teeth just because of a recession but then again you also know that these stocks don't outperform the others, don't do better when the economy's in full speed motion.

So why is the secular versus cyclical distinction so important? Why is it the first piece of Wall Street jargon that I'm translating for you tonight? Because it helps you figure out how much money companies will earn. Because it matters to the big institutional money managers. Those are the guys who have so much money to throw around that they're buying and selling actually drives stocks up and down. That's who moves the stock. That's the anatomy of the game. That's basically the single biggest determiner of where prices go in the short term. The whole hedge fund playbook is about when to buy and when to sell cyclical stocks and when to buy or when to sell secular growth stocks, based on how economies in this country and around the world are doing. This is what drives their decision-making process.

Remember about 50 percent of any individual stock comes from its sector, its performance, fifty percent of it, which is just a fancy word for the segment of the economy a stock falls into... like tech or energy or machinery or health care, finance. And when it comes to sectors, much of their moves are driven by whether they fall into this secular growth or cyclical camp. You don't want to own much in the way of cyclicals when the economy slowing, when it's breaking. Those stocks are simply going to get crushed. They always do. There's nothing you can do about it. It is etched in stone. By the same token, when business heats up and the cyclicals are doing well, nobody wants to own those boring consistent, recession-proof stocks. It's the smoke stocks, the soap stocks. You will not make money in those stocks. You could lose it even though you think they're consistent growth. And this can help you understand another the opaque piece of investment strategy, what's known as a rotation. That's just when money flows out of one of the cyclical groups into a secular growth. That's just what happens, we call them rotations. It has nothing to do a volleyball.

Now this is probably completely antithetical to what you've been told about the right way to invest. The conventional wisdom is if you're going to pick your own stocks, something which by the way the conventional wisdom regards as being the height of idiocy and lunacy because you're not supposed to be able to beat the market, then you should find high quality companies and stick with them through thick and thin. That's the conventional wisdom and eventually if you hold out long enough maybe you'll make some money. This is the brain dead philosophy of buy and hold but I spend so much time trying to debunk the strategy that is not work for ten, has not worked for twenty years, but they never seem to think it goes out of style. It's a zombie ideology that refuses to die, even though it's been utterly discredited by the actual imperical performance in the market, as I explain in getting back to even in the first three chapters just to try to get you to start dealing with the volatile, tough market that we are in.

Once you recognize how powerful the secular versus cyclical distinction is, you can see why buy and hold was just downright, outright silly. If you're gonna own stocks through thick and thin no matter what, then you need to be prepared to lose money in the cyclicals when they're out favor. Most people can't do that. You need to be ready to tread water or decline a little in the secular stocks while the cyclicals are roaring. Why take the pain when you can avoid it and most people can't take the pain, so they sell at the bottom. It doesn't mean you should play the rotation game and only own the group that's in style, not at all.

Remember the need for diversification, another important piece of investing vocabulary. Simply means making sure you don't have all your eggs in one sector basket. To me you're diversified when no more than 20 percent in your portfolio's in any single sector. That way you won't get annihilated for example a sector rotation takes down your cyclical stocks because you have some secular growth names that are going to hold out much better or even make you money at the same time.

Here's the bottom line. Yes investing isn't easy. But it doesn't have to be mystifying. You just need to learn the languag,e know the difference between cyclical and secular, recognize a sector rotation when you see one, and always stay diversified.

Jason in New York. Jason.

>>Hi, Jim. How are you doing? This is me, Jason, from Harlem.

Hey how are you, Jason? Good to have you on the show.

>> Great to be here. I have a question. When investing in international stocks or ETFs do you evaluate them like you would US companies?

Yes, provided, and this is a great question, Jason, provided they have ADRs. You need American depositary receipts. Why? I need to be able to compare their SEC filings with ours. If they don't have SEC filings, I absolutely don't even think about them. Jason, they're too hard, they're too opaque. If they have ADRs, I'll make the compares and we'll be fine. Stephen, California. Steve.

>>Hey Jim. Booyah, California in Los Angeles.

My old hometown. How can I help?

>>Well I first want to thank you for getting me back in the game. I've been on the sideline for years but discovered your show and I am reading your new book and I'm back in so thank you.

That's what I want. Because you gotta get the dividends going, you can beat banks, you can beat the stocks that don't have the dividends and you can certainly beat cash. How can I help?

>>That's what I'm looking at. I'm look at stocks that have good yields for my IRA .

Good. Smart.

>> And I'm reading your chapter on dividends, and I want to try to figure out the difference between an accidental high-yield achiever or something that's too good to be true. I've been doing the homework and I've got a couple stock that they look like they should be bought but I'm nervous about them.

>> Okay, you gotta go back to cash flow. You can't measure stock based on the earnings or else you would've sold ATT a long time ago cuz it doesn't look like its earning the dividend. You would have sold a lot of these very special master limit partnerships I like. You need to look at the cash flow not the earnings. The earnings aren't telling the truth. Go through the chapter in getting back even on cash flow and you'll understand it. It'll take me half hour, that's a very hard chapter. But that's what you use. Bill in New York. Bill

>>Booyah Jim.

Booyah Bill.

>>Some time ago you mentioned that the market was going up and that foreign money was coming into the market. How do you know where the money is coming from, be it Europe, Asia. For the sidelines, how do you measure it and its significance?

Federal Reserve actually releases figures about whether money's coming in from foreigners or not. That's how you measure it.   What I also like to look at is when the currency gets strong you tend to see a lot of money coming from overseas because remember the foreigners want both. They want double-whammy performance. They want a stock to go up and they want the currency to go up. So when you see the dollar go up and the stock market stabilizes, that tends to bring new money in, but the Market has to stabilize or else the money doesn't come. They're not just gonna make a bet on currency if it looks like the stocks are gonna go down.

Mastering the language of the market is key to mastering your domain. Don't let Wall Street gibberish get the best of you. Always stay diversified. Stay with Cramer too.