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Bull Bear Review^sm *with*

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- **Mild correction is sign of more upside to come**
- **1st quarter of '08 may be hard on the bulls**

In my October 2nd posting I was looking for a market correction starting October 11th and lasting through the 26th. The high in the S&P500 cash index was made on October 11 and the index has since corrected about 3%. I am pleased that, so far, this correction has been mild, orderly, and what one would expect in a rising market. We may have to contend with further weakness through the end of October but, at least for now, very little technical damage has been done. The market continues to slough off bad news, and after the October lows are in I look for one more run to new highs by the end of the year.

The bulls may be facing the perfect storm by the 1st quarter of 2008. If the price of oil simply remains constant it will be trading 80% above year ago levels by January. Once oil reaches this relative level, it has predictive value according to Steve Leeb. In his book, *The Oil Factor*, he shows that it's this relative level of oil prices that may cause the markets to drop. Additionally, a large number of variable rate mortgages are due to reset January through March. Higher gas and mortgage payments may be enough to slow consumer spending. Add the fact that there is an important 3.3-year cycle low due at that time and we may see our first 20% correction in five years.

On The Upside

There is lots of cash sitting in corporate coffers, hedge funds and Sovereign Wealth Trust. This **liquidity** should provide support during market corrections and buying power now that it appears that the Fed has turned to an easing stance.

Weekly Trend is up. Stops on a weekly close only basis for the S&P 500, Dow Jones Industrials, and Nasdaq 100 indexes are 1,505, 13,650 and 2,085 respectively.

The **commercials** started covering their record long position three weeks ago, but had very little change during the past two weeks. What they did during last Tuesday, Wednesday and Thursday's drive to new highs will be reflected in this Fridays report. My guess is that they continued to cover their long position.

On the Downside

From June of 2006 until late May of 2007, the 3-month T-Bill was yielding more than the 10- and 30-year bond rates. This is what is called an **inverted yield curve** and is an important "red flag" because this condition has resulted in a recession seven out of the last eight occurrences. There has

BULL BEAR REVIEW 10-17-2007 SPX 1,533 NDX 2,166 DJI 13,850

Bull (up)	Bear (down)
Liquidity and Free Cash Flow	Inverted Yield Curve
Commercials Net Long	Housing Market Fall Out
Stocks in Weekly Up Trend	Seasonals Down Through October
	Cycles Down Through October
	Rising World Interest Rates
	Advisor Sentiment Extreme
	Major Cyclical low due early 1st quarter

not been a recession since 1950 that was not preceded by a 10- to 20-percent decline in the stock market. July 19 through August 16th the major indexes corrected 10 plus percent. Will a recession follow?

The **housing market fall out** remains the wild card. What we know about the housing market cycles are that the average length of time from peak to trough is 27 months. This down move started in January of 2006 and therefore likely has another 7 months. In the past 40 years, private residential construction has never contracted to this extent with out triggering a recession. Housing inventories are at a 16-year high (10 months at the current rate of sales). Existing home sales are at a 5-year low. Both new and existing home sales are down 10.6 percent verses year ago levels. Building activity is down 24% from year ago levels. This is becoming an old story and many believe the market has discounted it. However, this story will likely come to the forefront again the first quarter of 2008, as a very large number of variable rate home loans will adjust upward.

Jim Stack is doing a good job of tracking the unwinding of the housing bubble. Go to www.investech.com to find three great charts that tell the story. Jim updates these charts regularly. Go to www.lenderimplode.com to track the demise of the sub prime industry.

Seasonals are down through October.

Cycles are down mid October to late October.

Advisor Sentiment is negative. Investor Intelligences reports 62% of advisors bullish and only 19.6% bearish. This is a five year extreme and, while not a good short term indicator, has preceded many market tops.

Restrictive Monetary Policy by China's Central Bank could be a showstopper. China has a problem with speculation in its' stock market. The central planners are aware of the problem and are trying to quell enthusiasm with higher interest rates and restrictive monetary policies. There will be some fall out worldwide when their market corrects.

The 3.3-year **cycle low** is due late in 2007 early 2008. This cycle low has marked many significant lows over the past twenty-five years including the 1987 crash low.

Your Bull Bear Review Analyst,

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