



## Bull Bear Review<sup>sm</sup> with Michael J. Chapman, CFP



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317-705-1999

03/27/07

- **Stock Indexes follow thru to upside**
- **Utilities Index hits new high**
- **Trends turn neutral**

Was March 13<sup>th</sup> the end of the correction? Lows were made March 6<sup>th</sup> close to the 200 day moving average then retested on the 13<sup>th</sup>. On March 21 the S&P 500 index had a 1.8% move to the upside on large volume. This took out all down trends and was confirmation for the bulls that a short term low has been made. Next stop new highs?

I was looking for this down move to last until mid / late May. However, Mr. Market is whom we have to listen to and right now we appear to be in the very early stages of the next up move. The verdict is still out for a couple more weeks but, as you can see in my "balance of evidence" below, the weight is shifting back to the bull.

Ben Bernanke made a slight shift to fed policy March 21 by deleting the part that implied a bias towards higher fed funds rates. This may explain why the 10-

and 30-year bonds broke their up trends and are now declining (Long rates moving higher). The long bond market senses that the fed, if forced to choose between inflation and recession, will choose inflation; i.e. they will keep the liquidity as high as possible. In 1987 I watched as bonds declined (rates rose) from April to August as the stock market continued to rise the entire time. Of course, the stock market then proceeded to catch up with bonds by crashing. Feelings of Deja vu.

### On The Upside

According to Thomson Financial, 2006 was a record year for global merger and acquisition activity, hitting 3.77 trillion and topping the record set in 2000 of 3.44 trillion. This trend has continued into 2007. A recent *Fortune Magazine* article discussed the ten largest private equity firms. By their calculations these top ten firms have \$250 Billion in cash. They will borrow up to 10 times that amount when doing their deals (hence the term "leveraged buy out"). Which means they have buying power of \$2.5 Trillion. This should add tremendous **liquidity** to the market thus driving it higher during good times and supporting it during sell offs.

**BULL BEAR REVIEW 03-27-2007**

**Bull (up)**

**Liquidity and Free Cash Flow**

**Leeb Oil Index**

**Seasonals (Up Nov. 1 thru April 30)**

**Commitment of Traders**

**SPX 1,429 NDX 1,795 DJI 12,400**

**Bear (down)**

**Inverted Yield Curve**

**Housing Market Fall Out**

**Pattern (Time & Price )**

**Major Cyclical low due late 4<sup>th</sup> quarter**

**Oil prices** are \$62/brrl. However, because the price of oil moved up sharply from February to August of 2006 we are still trading below year ago levels. The price of oil verses one year ago has been lower for the last sixteen weeks. Stephan Leeb, editor of the *The Complete Investor*, notes that, “Over the past 30 years, stocks have never fallen more than 5% during the 6 months following a drop in price below year ago levels.”

There is a strong up **seasonal** from November 1 through April 30th.

**The Dow Jones Industrial Utility index is in an up trend** and just made new highs. This index normally tops before other indexes top not after.

## **On the Downside**

Three-month treasury bills are yielding more then the ten and thirty year treasury bonds and have been since June of 2006. 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 not been a recession since 1950 that was not preceded by a 10 to 20 percent decline in the stock market.

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 12 months. In the past 40 years private residential construction has never contracted to this extent with out triggering a recession. February new-home sales in the U.S. fell to seven-year lows (Bloomberg March 26). Housing inventories are at a 16-year high (8.1 months at the current rate of sales).

Robert Prechter’s Elliott Wave International report is showing a completed wave **pattern** through February 22, 2007. The next move using their approach is strongly lower. The last three out of four calls they have made have been correct on direction but wrong on the degree of the drop. They correctly called the May 2006 highs to the day but were calling for a much greater move down then the 8 percent.

The 3.3-year **cycle low** is due late in 2007. 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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