PETER ELIADES' STOCKMARKET CYCLES

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December 1, 2006
End of Week # 1668

DJIA	12194.13
CI	1719
NCI	1643
Ratio	1.047

—THE CYCLES—

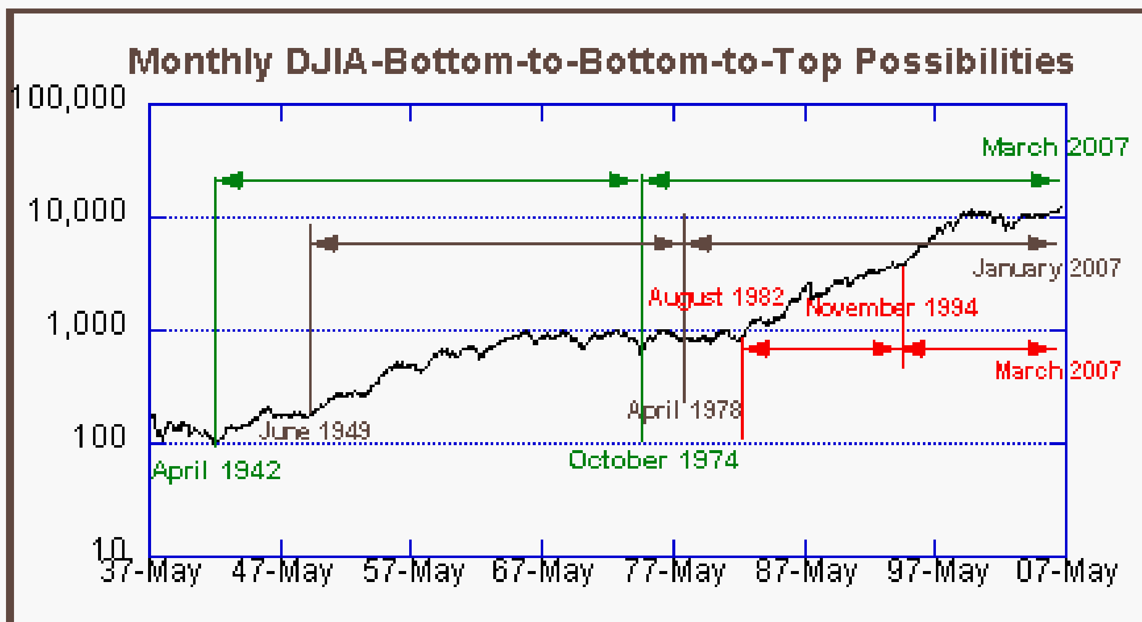
Over the past several months in these newsletters, we have been pointing out an apparently growing number of patterns that appear to be converging in the late 2006 early 2007 time zone. If the stock market were declining into the time zone encompassed between the last quarter of 2006 and the first quarter of 2007, we could make a strong argument that a very important market bottom was being registered. In our October 5th, 2006 newsletter, we noted a combination of a large number of periodic time patterns. Most of these numbers were a multiple of the number 4 and, because the 4 year cycle has been so consistent, it was a simple process to combine two 4 year cycles to form an 8 year cycle, three 4 year cycles to form a 12 year cycle, four 4 year cycles to form a 16 year cycle, and even eight 4 year cycles to form a 32 year cycle.

Our presentation of all those combinations of 4 year cycles was used in association with the George Lindsay theory that virtually all important market tops display a bottom-to-bottom-to-top pattern and we theorized for several reasons that it was possible that these large numbers of combinations of 4 year cycle multiples could well be doing exactly that, namely combining to form a very important market top. We will discuss several reasons in the technical section why we believe there is a better chance that a top of great importance will be formed between the last quarter of 2006 and the first quarter of 2007, but in this cycle section we want to continue with the presentation of these potential bottom-to-bottom-to-top patterns that we believe are telling a significant story.

The front page chart in today's newsletter represents a depiction of three separate potential bottom-to-bottom-to-top patterns. The longest pattern on the front page chart begins at the April 1942 market low, one of the most significant lows of the 20th century. If we measure the distance between that very major low and what might be considered another of the two or three most important lows of the 20th-century, namely October 1974, then measure the same distance forward from October 1974, we would arrive at March 2007. The exact date would be March 12th, 2007. For those of you receive the newsletter via e-mail, that pattern is depicted by dark green lines and arrows.

The next pattern on the front page chart is one we have not discussed before. The June 1949 market bottom was notable, not because there was a large decline into that time period, but because it was a springboard for a market rally that would, in effect, last for almost 17 years. If we measure the distance from that June 1949 springboard bottom to the important market low that occurred in March-April 1978, there is a time span of between 10,487-10,520 days, depending on whether the March 1st, 1978 bottom is used or the April 3rd, 1978 bottom is used. Using the March 1st, 1978 bottom would result in a bottom-to-bottom-to-top resolution on November 16th, 2006. Using the secondary low which occurred on April 3rd, 1978 would result in a resolution on January 21st, 2007. Those of you who have color charts will note that this pattern is depicted by brown lines and arrows.

The final pattern scheduled to resolve in the first quarter of 2007 was discussed in our October 5th, 2006 newsletter although we did not depict the pattern in that newsletter. August 1982 certainly qualifies as one of the most important market bottoms of the past 50 years or longer. It was that bottom which began the explosive move that would fuel an ultimate 17-



18 year rally of historical proportions in the United States equity markets. In this case we count the time span between that 1982 bottom and the November 1994 bottom of the Dow Jones Industrial Average which acted as a springboard for one of the greatest five-six year rallies in market history. It encompassed a period of 4489 calendar days. If we add an additional 4489 calendar days to the November 23rd, 1994 bottom in the Dow, it results in reaching the date of March 9th, 2007. Note that the March 9th date is only one trading day away from the March 12th, 2007 date that marked the potential resolution of the 32 year pattern discussed above. This pattern is marked in red for those of you who have the chart in color.

In addition to all these resolutions that are theoretically due in the first quarter of 2007, we would like to quickly review both the 25 Year and a 75 year patterns discussed in the August 4th, 2006 newsletter. We should begin by quoting our August 5th, 2005 newsletter where we wrote:

> *... every resolution of the 25 Year cycle has been an exact resolution and has marked a low point which the market has never since penetrated. More specifically, the lows of 1907, 1932, 1957, and 1982 have been exact bottoms and the market has never again moved below those levels. That makes the prospects for the year 2007 very interesting. First of all, it argues that there will be no important bottom in the year 2006 unless it occurs very late in the year and it joins forces with a very early 2007 resolution of the 25 Year cycle bottom. Remember that in the past, if the two cycles [the 4 year and 25 year] had different resolutions, it was the 25 year cycle that ruled. The larger question that looms, of course, is whether the 25 Year cycle will be as important a bottom this time around as it has been in the past. It is our contention that if that is to occur, that cycle resolution will be preceded by a devastating decline and a long period of investor bearishness.*

There are 20 trading days remaining in the year 2006. It is very highly unlikely that there will be a devastating decline over that time period. We are not aware of any devastating declines that have ever occurred between Thanksgiving and Christmas and we are confident this year will be no different.

There is a chance, of course, that the 25 year cycle will cause a severe decline into the first quarter of 2007. It is our contention, however, that the more probable course of action will be to see the current rally which has carried many of the market averages to new all-time highs continue into the first quarter of 2007. Should that occur, then we face the possibility of adding two more very long term potential bottom-to-bottom-to-top patterns that would be due to resolve in 2007, probably in the first quarter of that year. That would mean that between the fourth quarter of 2006 and the first quarter of 2007 there would be potential resolutions of bottom-to-bottom-to-top patterns of two years, four years, eight years, 12 years, 16 years, 25 years, 32 years, and 75 years. A culmination of that many patterns within such a relatively short time zone would mean that we could be facing one of the most important six month time periods in market history. We will look forward to facing those resolutions along with our subscribers.

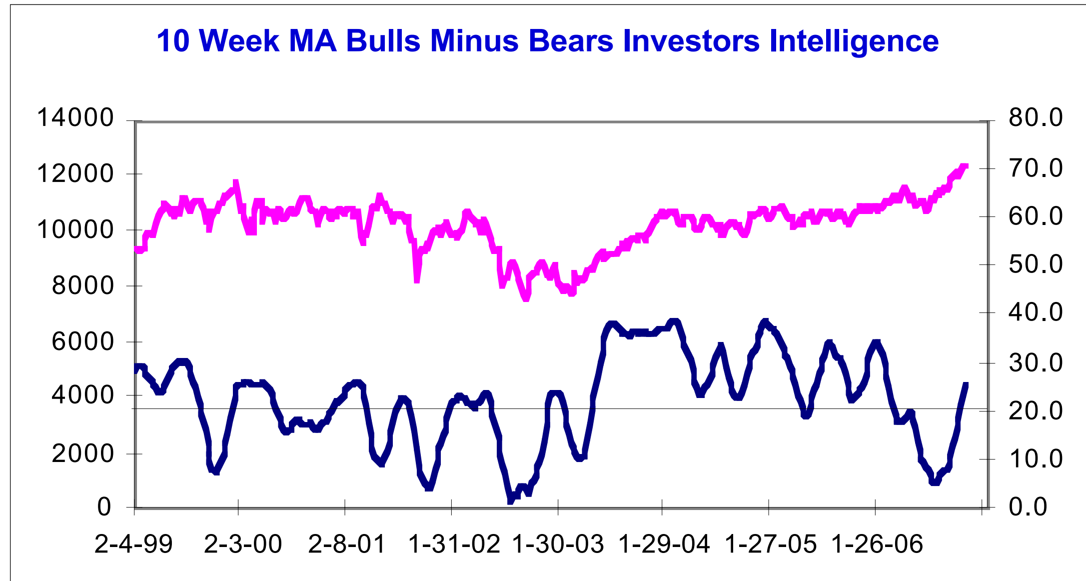
We discussed the 75 year cycle in our August 4th, 2006 newsletter but will quickly review it for new subscribers. If we were to show you a long term chart of stock prices going back to the 19th century, as we did in our August newsletter, there are at least two market bottoms that stand out dramatically on the chart. Those are the bottoms of 1857 and 1932, 75 years apart. As it turns out, although the data is sparse, we can make a case using British stock prices prior to 1800 that there was also an important market bottom around 1784, just under 75 years before the 1857 bottom, and another market bottom around 1707, just over 75 years before the 1784 bottom. This group of periodicities points to the year 2007 as the next potential year for the resolution of the pattern. The fact that the market is making new all-time highs on some of the major indexes as we approach the end of 2006 suggests the possibility that both the 25 Year and the 75 year cycle, which are due to resolve in 2007, could result in a George Lindsay bottom-to-bottom-to-top configuration rather than resolving in an important market low.

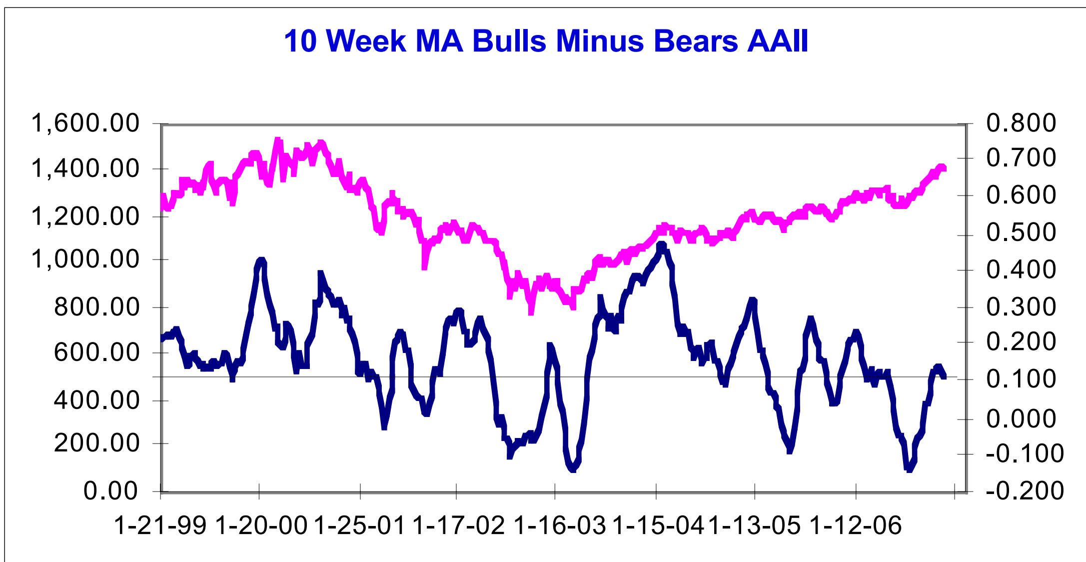
The bottom line is that an amazing number of intermediate to long-term to very long term market patterns appear to be pointing towards a convergence of potentially great importance, with the focus of that convergence occurring sometime between the middle of the fourth quarter of 2006 and the end of the first quarter of 2007. In other words, it should not surprise us if the market has already made an important high but it should also not surprise us to see a final high occur as late as March 2007. We believe the market is living in an endangered time zone and, although we will present evidence in the technical section that the top has not yet occurred, we should be prepared at any market downturn to concede the possibility the market has registered a very important high.

—TECHNICAL INDICATORS—

We follow two main services that provide sentiment readings that are useful in judging market sentiment. By far, the veteran in the service of documenting market sentiment is Investors Intelligence (30 Church St., PO Box 2046, New Rochelle, NY 10801) . The sentiment surveys were begun by Abe Cohen almost 50 years ago. The surveys began as a bi-weekly service but by 1969, sentiment surveys were reported weekly.The company has been headed up for the past few decades by Michael Burke, a very talented market analyst in his own right who seldom gets credit for his own market insights because he so often quotes the insights of others.

The other service we follow is the American Association of Individual Investors (AAII). They releas their sentiment readings to the public on Thursday of each week. It is important to note the differences between these two services. The weekly sentiment readings from Investors Intelligence are compiled from newsletters and, although the list of newsletters monitored usually increases from year to year, the opinions are garnered





from the same consistent basket of newsletters each week. We believe that system is at least theoretically superior to the system employed by AAII because their data are compiled from online responses of the lay investors who visit their web site. There is no way of knowing how uniform and consistent people are in responding to that survey. In other words, it is possible that very few people who responded four weeks ago are among the group which responded during the current week. In that respect, the numbers could take on a lesser significance. We should also note that, although the AAII data has been compiled on a weekly basis since 1987, the methodology used to gather the data changed rather significantly in the year 2000. Prior to that time, responses were mailed in by group members. In the year 2000, the method of gathering responses moved online. A cursory glance of the data might lead one to believe that the character and personality and consistency of those responding changed to a certain degree in the year 2000. For that reason, we have a tendency to give more credence to the Investors Intelligence numbers. The only potential weakness from their sentiment survey is that it involves a certain amount of subjectivity because the great majority of newsletters do not announce within their newsletters whether they are bearish, bullish, or looking for a correction within a bullish overall pattern. Inasmuch as those are the three categories that are reported by Investors Intelligence, the reader of those newsletters must sometimes make a judgment as to which category the newsletter writer fits into. In any event, the fact that their survey is always drawn from the same basket of newsletter writers provides us with a consistency that AAII is simply unable to provide. One of the most important aspects of judging market sentiment occurs when a newsletter writer changes his opinion. That change in opinion is always reflected in their data and, even though contrary changes in the opinion from two different newsletter writers may offset each other, we know that changes from bearish to bullish opinions and vice versa are always reflecting the opinion of the same sampling universe. That is not the case with AAII. The one potential advantage of the AAII sentiment figures is that there is no subjectivity involved. Those who take their survey simply state outright whether they are bullish or bearish on the outlook for the market. No subjective interpretations need be made.

With that background, let's attempt to analyze the current readings from those services .

We thought it might prove interesting to compare the sentiment readings from both of the above services going back over an identical period of almost seven years. This time span covers the major market top reached in the year 2000 and the subsequent bear and bull markets. Both charts represent the same types of readings from the two data services. The chart is constructed by calculating the weekly difference between the

percentage of bulls and the percentage of bears. These data were compiled into a 10 week moving average in order to smooth the data. The Investors Intelligence chart is accompanied by the weekly closing price of the Dow Jones Industrial Average while the AAII chart is accompanied by the weekly closing price of the S&P 500.

The broad horizontal lines on each of the charts represent the average of all the readings during the time span of the chart. Although there are some very obvious differences between the two charts, perhaps the two things that strike the eye first are the relatively smoother readings resulting from the Investors Intelligence data and the overall similarity between the two data sets. Perhaps the most remarkable aspect of the Investors Intelligence data is that it has never moved below the zero level over the almost seven years covered by the chart. If this leads you to believe that the area around the zero level has always been a good contrary opinion level for being bullish, we would caution you against that conclusion. This has been a most remarkable time period in that the market has gone through a full 4 year cycle from October 2002 through October 2006 without one **weekly** reading from Investors Intelligence showing a plurality of bears over bulls. We wish to emphasize that point because it is a truly remarkable statistic. Perhaps we can put that statistic in perspective. In the year 1994 which turned out to be a base building year prior to a spectacular five-year flight into the ionosphere by stock prices, there was a plurality of bears over bulls in 43 of the 52 weekly reports from Investors Intelligence. Of those 43 weeks, 39 of the readings were registered in consecutive order. That is the type of sentiment that is generally seen prior to important market bottoms or prior to base-building periods that act as springboards for long term bull markets.

Notice that the data from both services reached their highest readings early in the year 2004. In fact, in both cases the 2004 bullish sentiment was greater than the bullish sentiment at the very major market tops that were reached in the year 2000. Perhaps another surprising statistic (which we regrettably admit we did not recognize in real time) is the relatively extremely low readings registered at the July-August lows of this year. In fact, the 10 week moving average of bulls minus bears reached a level of minus 14.1% on August 3rd, 2006 and that was the lowest reading in the almost seven year history of the data with the exception of the minus 14.6% reading registered on March 13th, 2003 when the Dow was at the 7700 level and the S&P was around 800. Notice also that, although the corresponding reading from Investors Intelligence was not relatively as low as the AAII reading, it was, nevertheless, also the lowest reading since late 2002-early 2003.

Finally, notice that the latest readings do not appear to have reached levels that have been dangerous in the past. That is certainly true with the AAII readings. The Investors Intelligence readings currently are close to some of the levels registered during the year 2000 when the market was making a major top. In fact the latest reading of 25.3 from the Investors Intelligence data matches up quite closely with the 25.9 peak reading during January-February 2000 when the Dow was establishing what was then its all-time high and forming a top which would last for over six years. In other words, although current levels suggest there is a good reason to look for further upside progress, there is also reason to be vigilant in terms of preparing for a market top based on the Investors Intelligence data from the year 2000.

—MARKET PROJECTIONS—

In our last newsletter we noted that the New York Composite Index had generated an upside projection which had already been slightly exceeded. When all longer-term upside projections are reached, it is still possible for indexes to generate even higher projections after some short-term declines. Those of you acquainted with our projection offset techniques know that a short-term decline followed by a rally that moves above the offset of that decline can continue to generate at least slightly higher upside projections. That has occurred on the New York Composite Index and there is now in fact a projection outstanding up to 9004-9038 that we gave on our daily update on Wednesday, November 29th. That index closed today, Friday, at 8,949.07. Despite today's decline, that projection remains in effect through today's close.

—MUTUAL FUNDS—

Rydex switchers purchased the Rydex Tempest Fund, now called the Rydex Inverse Dynamic S&P 500 Fund, on November 8th at 33.74 and sold the fund on November 14th at 33.41 for a loss of 1%. Fidelity Select switchers remain in Fidelity Select Gold fund which we purchased on July 20th at 33.73. The fund closed today at 38.43. We have two different specific model portfolios-one for Fidelity Select switchers and one for Rydex Group switchers. How you distribute your own portfolio is up to you as an individual.

NOTE: We would like to remind subscribers that we are now managing money through the use of mutual fund timing. This relieves you of the stress of wondering whether you missed a signal or whether you will reach your fund in time to make a switch. Our management company is called, appropriately enough, "Stockmarket Cycles Management, Inc." If you would like additional information regarding this service, please call the office (800) 888-4351 or e-mail us at *suedavy_smc@comcast.net* anytime.

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