



Summary

Cycles Research issued a 200% long position for stocks on December 1. CR issued a buy on gold as of the close on April 9th. A buy signal was issued on bonds by interim message on June 24th.

Analysis

Q1 Will Likely Bring a Top

There are five reasons to expect a Q1 top:

- 2010 is a year ending in zero. As we know from Edgar Laurence Smith's study of the decennial pattern, 65% of all years ending in zero have been down years in the stock market. The last one was 2000.
- The 24 and 40-month cycle tops in February.
- The month of March has been a turning point in each month except one since 2000.
- There are several monthly time counts that expire in March and there are at least 4 in April.
- My intermediate cycles top on March 9th and then go sideways into March 26th, and then fall into June.
- Ben Bernanke was on the cover of Time as man of the year (see the bonds section).

The decennial pattern was described by Smith in his book, Tides and the Affairs of Men. This study tells us that years ending in 5 have typically been the strongest. The pattern also suggests that years ending in 7 bring crises; this was helpful in the CR prediction of a real estate crisis beginning in 2007. Years ending in 9 frequently bring tops in the equity market.

The second point is based upon the findings of Richard Moge and the Foundation for the Study of Cycles. Research shows that these have been the two most reliable rhythms in the US market since 1780. The combination of the pair is depicted below:

Monthly DJIA 24 And 40-Month Cycles In 2010



Daily S&P 500



Value Line, and the Market is Smarter Than We Are

Sam Eisenstadt, 84, the creator of the Value Line Investment Survey's timeliness ranking system, has been fired after 63 years of employment. The business was begun by Arnold Bernhard, a journalist. Mr. Eisenstadt once explained to me that VLIS was begun with Bernhard's idea that a stock was worth its cash flow, a 'value line.' This is the cash flow line in the graph at the top of the page that was fit to the price. Eisenstadt later developed the ranking system, which attempted to measure the difference between earnings and price change. Stocks that had an earnings trend that was far above the price trend were ranked number 1 while those of lesser rank were 2, 3, 4, or 5. The system was tested by Prof. F. Black at the U. of Chicago and was deemed to be valid, refuting the efficient market hypothesis. The story of this dismissal reminded me of an occurrence that was known to analysts as 'the shock of the week.' Each week, the editor would select an especially attractive stock from the 1-ranked group. The analyst that covered the stock was then tasked with the stock of the week, which came to be known as the 'shock of the week.' In the old days, analysts could change the rank of a stock by placing a buy or a sell which would raise or lower the rank by one level. Well, in order to avoid the 'shock of the week', analysts lowered the 1-ranked stocks to 2-ranked stocks by placing a sell recommendation on them. When management discovered this, they asked Sam to run a back test of the value added by the analyst recommendations. The net result of the recommendations over the years was zero; the value added by the analyst recommendations was nil. So, the analyst recommendations were dropped. The system was wiser than 50 analysts, and the market was wiser than all of us.

In Case You Are Wondering Why It Is Taking the Administration So Long to Find Solutions for the Economy:

From web radio, the host read a list of Cabinet members that actually had worked in the private sector or had owned businesses. The percentage of cabinet members with such experience sorted by administration from Teddy Roosevelt are:

PRESIDENT	PERCENTAGE
Roosevelt	38%
Taft	40
Wilson	52
Harding	49
Coolidge	48
Hoover	42
Roosevelt	50
Truman	50
Eisenhower	57
Kennedy	30
Johnson	47
Nixon	53
Ford	42
Reagan	56
Bush	51
Clinton	39
Bush	55
Obama	8

And Now For Some Contrary Opinion Forecasting for 2010

I always enjoy the Erste Bank asset allocation conference in December. The opinion polls taken at these meetings produce interesting results. Last year, the majority (90%) chose Japan and the US to be the leading stock markets in 2009 while only 10% selected Brazil; the result was the reverse. The opinion on the oil price was too low, and only 15% were correct on the value of the \$; Most respondents were too bullish.

In 2010, 39% chose the Brazilian stock market to rise the most. China was in last place, selected by 12%. Regarding gold, 24% think that it will trade in the \$900-\$1100 range while 20% chose the \$1100-\$1300 range. In 2009, attendees did get interest rates right, so contrary opinion might not apply to this market in 2010. Here are some of the results.

Stock Market	Percent
Brazil	39%
Japan	19
USA	14
China	13
Russia	9
Europe	6

Oil Price	Percent
\$30-\$50	7%
50-70	19
70-100	57
100-150	10
>150	7

Euro	Percent
<1.10	3%
1.10-1.25	6
1.25-1.35	14
1.35-1.50	37
1.50-1.60	34

10-Year Rates	Percent
<3%	14%
3-4	32
4-5	30
5-6	17
6-7	4
>7	3

If contrary opinion works in 2010 as it did in 2009, then the Russian, Chinese and European stock markets will be strong, and Brazil will be weak. Oil will soar over \$100, and gold will either be under \$900 or over \$1300. The euro will be less than \$1.35 or higher than \$1.60.

Turning Points

Combining short-term cycles with the dates below, it appears that the market will rise from the 4th to the 7th or the 8th. From the 11th to the 21st, cycles rise. The turning point on the 15th will likely bring a 1-to-2-day correction in this uptrend. Cycles are mixed from the 21st to the 29th, so this period is likely a corrective consolidation.

The highest-probability S&P and DJIA turning points (+ or – 1 day) for the month are
(The stronger turning points are starred:

4* 21

8 29*

15*

The highest-probability NASDAQ turning points (+ or - 1 day) for the month are
(The stronger turning points are starred*):

4* 21

8 28*

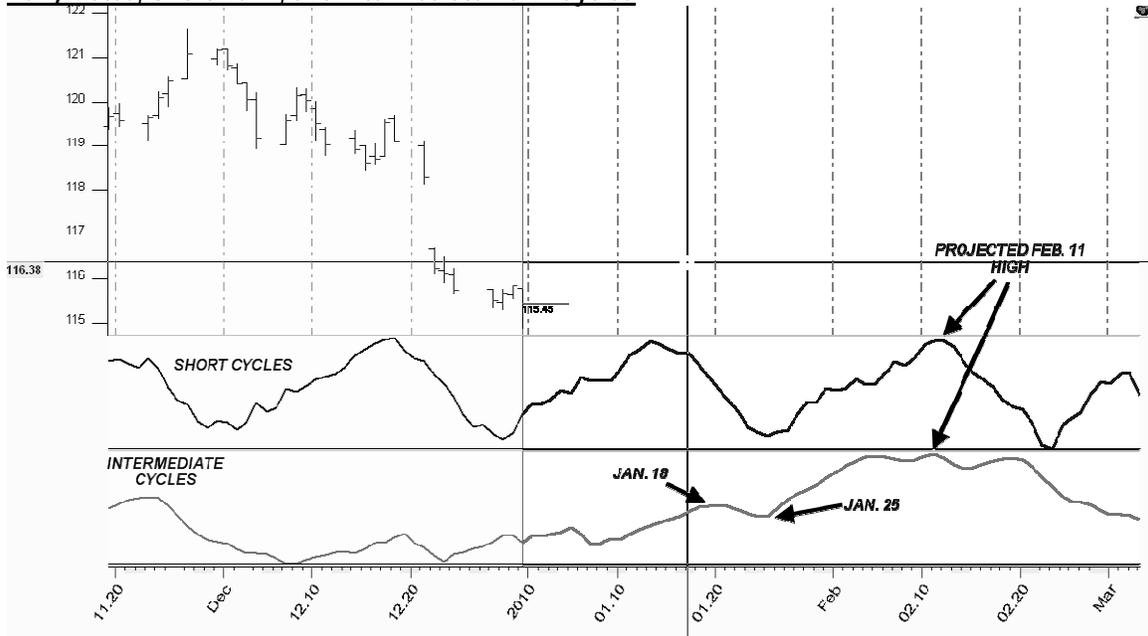
15*

Bonds

The decline in notes in December was much greater in magnitude than anticipated. The cycle composite shows both the short and the long cycles topping near the 19th. Note that the intermediate cycle then bottomed on the 23rd but price kept falling into the 29th. The fact that the magnitude of the December drop was large and that notes kept falling after the cycle low tells us that a longer cycle is pressing down as the annual cycle enters a topping phase. The intermediate cycle composite tops on January 18th, bottoms a week later and then hits a high on February 11th. The graph below the Daily Notes graph shows that the February 11th date falls in the annual topping phase that stretches from January 18th to March 18th.

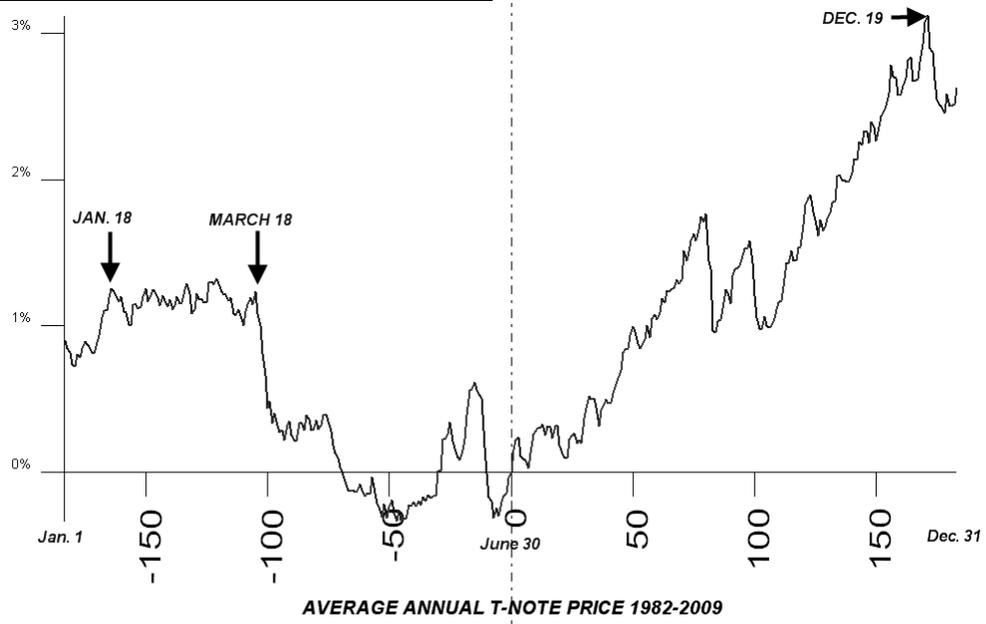
Bond holdings should be reduced on the current rally. The high for the quarter is likely in mid-January or mid-February.

Daily Notes, Short-Term, and Intermediate-Term Cycles



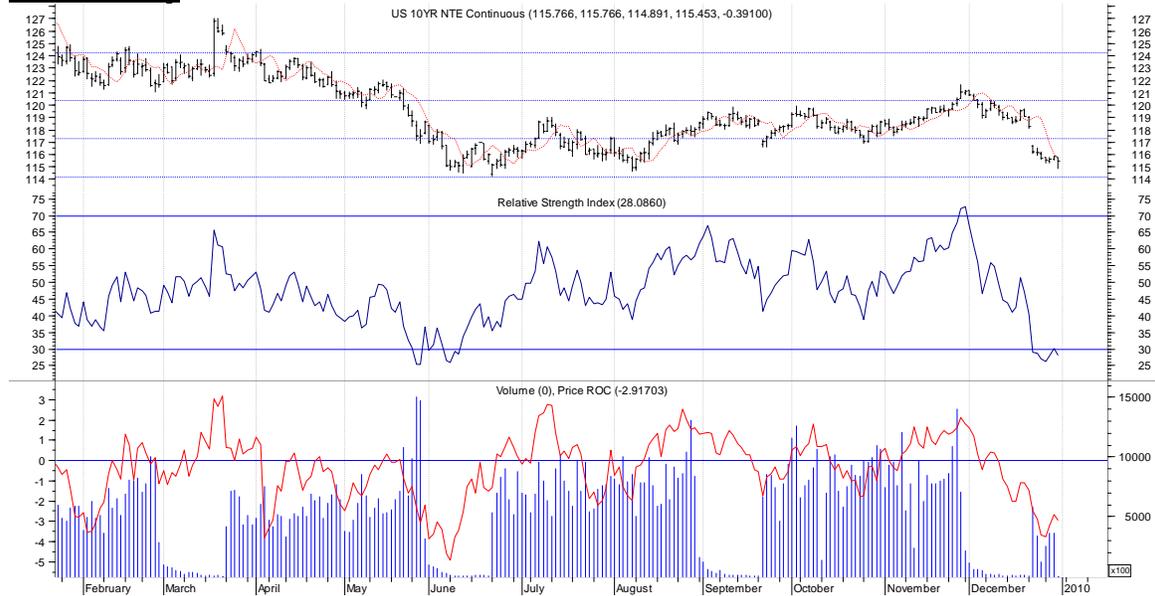
Note that the December 18, 2009 high was only one day off of the average annual high as depicted below. Curiously, this was also the high day in 2008.

Average Annual Note Cycle With Average Turning Points



The daily graph shows that notes are oversold and that the initial decline from the November 27 high to the December 15th low is now about equal to the decline from December 18th. This technical condition, combined with the cycle upturn will likely be enough to lift notes. In addition, July is the only month with fewer turning points than January, so bonds are unlikely to make a major shift.

US Notes Daily



Ben Bernanke was on the cover of Time Magazine as man of the year. Those who are familiar with Paul McRae Montgomery's (Montgomery Capital Management in Virginia, USA) research of magazine covers know what this suggests. It is likely that the investment tone suggested by the cover story will reverse within 3 to 4 months with an 80% probability. Appearances by Fed chiefs have occurred at major turning points in the past. Paul Volcker was on the cover of Time in 1982 in a negative light, a point that proved to be an excellent buying opportunity for bonds. In March of 1986, he was on the cover of Newsweek as 'the second most powerful man in America.' The US note topped in mid-April 1986 at 93.5 and bottomed in October 1987 at 75.0.

The recent story called him the most powerful man on the planet, implying that a situation will occur in 2010 that he will be powerless to stop. The magazine cover is a sentiment confirmation of the cycle high.

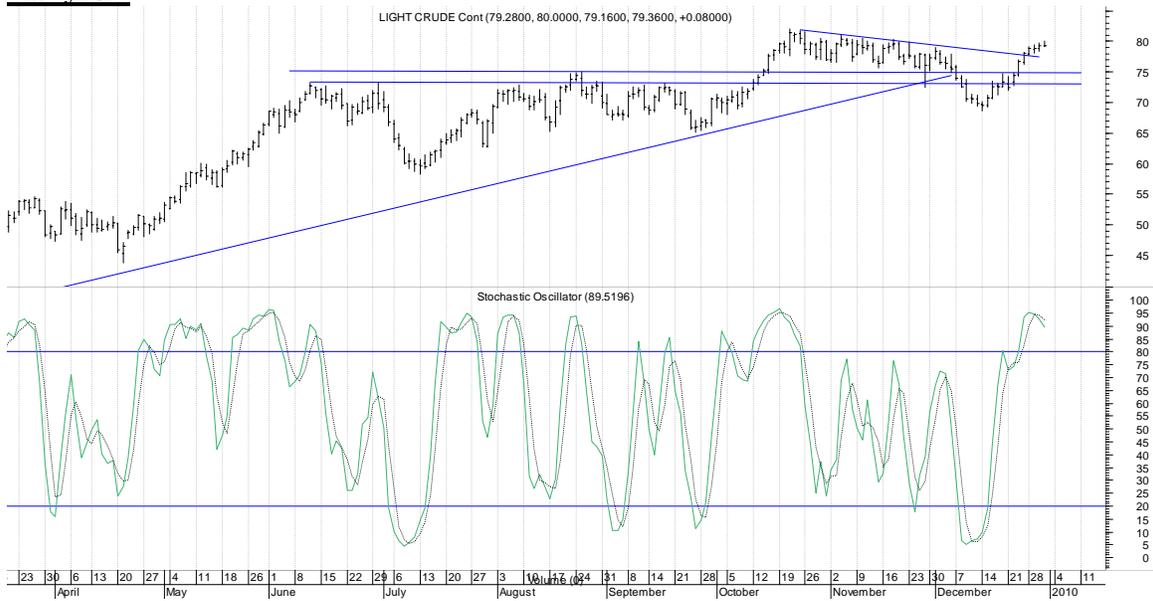
Sectors and Groups

The tech and health care sectors continue to be strong. The relative strength of the financial sector continues to fall.

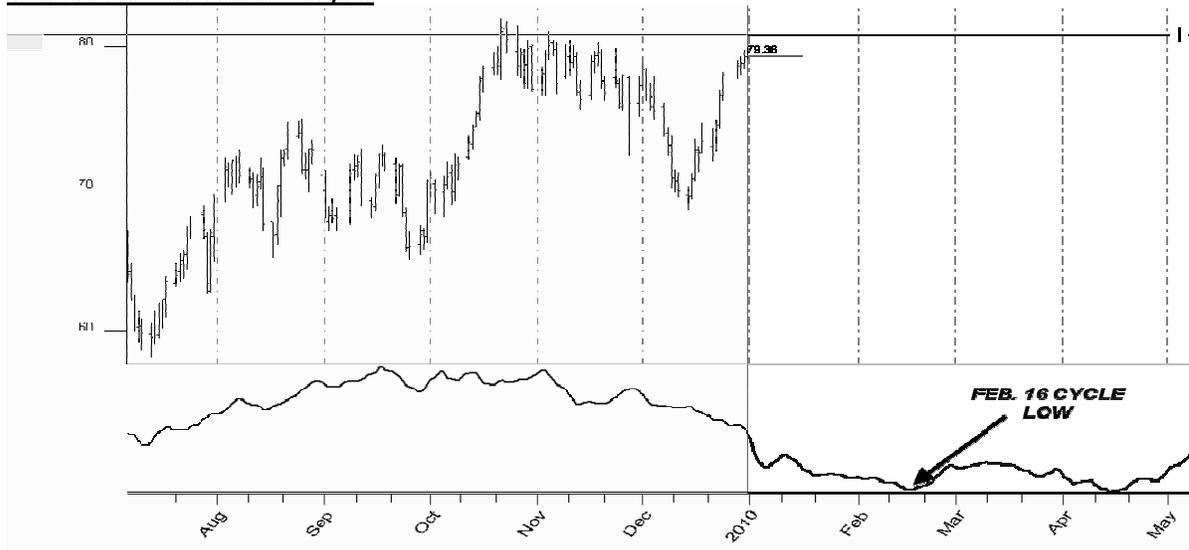
Energy

Oil was much stronger than expected and has rallied back into resistance. Cycles suggest that oil can trade up into the latter part of this week, but that the price is likely to then complete correction by falling into late into mid February. The daily graph below shows that oil is overbought and is at the old high. I think that oil is about to get back in line with the cycle in the second graph. .

Daily Oil



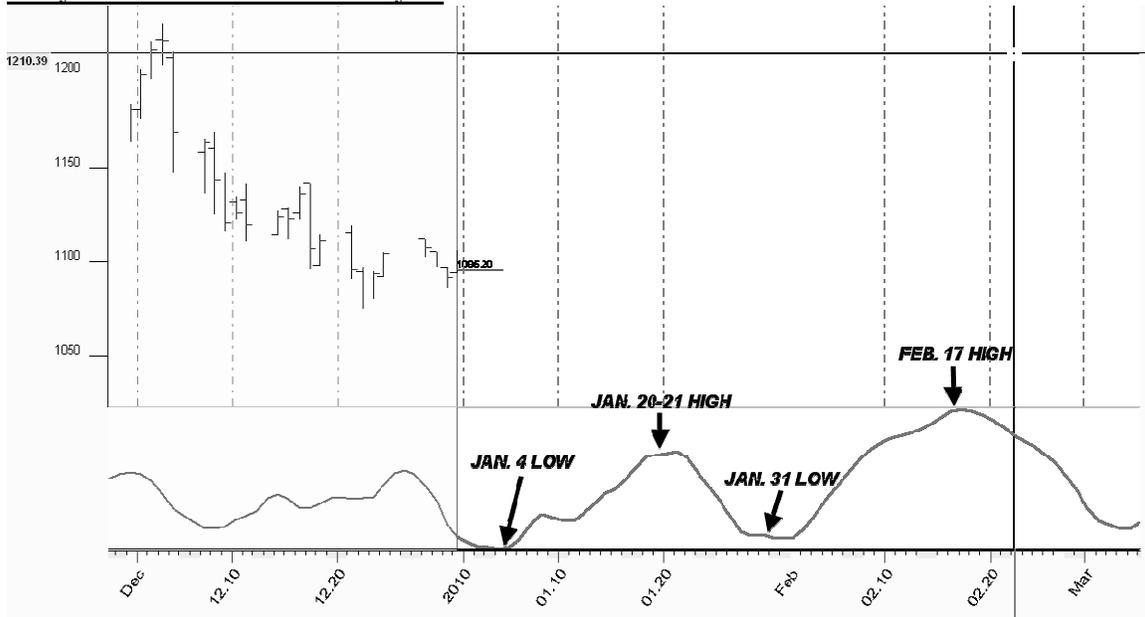
Oil and Intermediate-Term Cycle



Gold

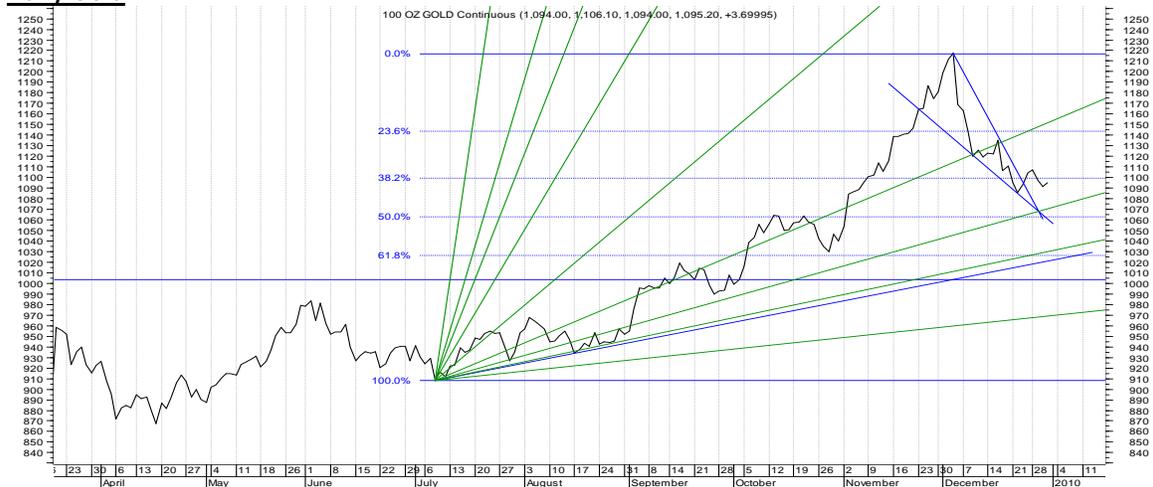
Gold was weaker than expected in December. But, the cycle depicted below has bottomed, and the technical picture that is described below the cycle graph is positive for the short-term. Most highs in gold occur in Q1. The average annual high is in January, and the cycle below points to the 20th-21st, but the annual high can push forward into February or March during bull markets. Note that the cycle below also peaks in mid-February. I think that this is the more likely time for a significant high. Price-wise, the high that was projected from the technical breakout is still \$1300. It does not appear that we have enough time to reach that level by January; February seems more likely.

Daily Gold and Intermediate Cycle



The daily graph below shows that gold has broken out of a falling wedge. It stopped falling at the 38% retracement area, which is also the 23.6% retracement from the October 2008 low to the last high (line not shown). At \$1065, there is another retracement level and a Gann fan line (green line) that provide further support.

Daily Gold



Looking at the gold market from another angle, we see that most major turns have occurred in February and in March.

Gold Turning Points Using a 5% Filter

MONTH	HIGHS	LOWS
JAN	6.9%	5.7%
FEB	12.6%	12.6%
MAR	11.5%	11.5%
APR	9.2%	6.9%
MAY	4.6%	6.9%
JUNE	9.2%	9.2%
JULY	10.3%	9.2%
AUG	9.2%	11.5%
SEPT	8.0%	5.7%
OCT	5.7%	5.7%
NOV	2.3%	6.9%
DEC	10.3%	5.7%

Individual Stocks

PORTFOLIO

Stock	Buy Price	Buy Date	Current Price
Bond ETF- TLT	92.73	June 24	89.89
Pro Shares Ultra Gold ETF-UGL	30.59	April 9	44.68
US Natural Gas Fund ETF- UNG	12.87	July 31	10.08
Ultra S&P Proshares- SSO	36.9	December 1	38.24

Strategy

Investors continue to hold strong stocks. Reduce those with lagging relative strength. Traders refer to the turning points section of the report.

The Prediction Market

I had not gone to StrategyPage.com for some time. The Predictions Market at this site lists many world situations, an end date for the prediction, and the percentages of respondents agreeing or disagreeing with the prediction. The market opinions have been 88.79% accurate. Following is a selection of predictions. The latest readings are not positive for the current US administration.

SITUATION	RESULT
Within the next 6 months, Israel will make a major incursion into the Gaza strip, involving missile attacks and ground troops, that lasts over 72 hours. (2/10/2010)	True
A weapon of mass destruction will be used in a terrorist attack somewhere in the world by the end of 2013. (12/31/2013)	True
Shots fired near President Obama. 01/20/2012	True
Republicans gain at least 30 seats in the House in the 2010 mid-term elections. 11/05/2010	True
Sarah Palin will run for president in 2012. 09/30/2012	True
A Monthly Average Of US Dollar Inflation Will Exceed A 16% Annualized Rate For Some Month Before Years End 2012. 12/31/2012	True

What the Media is Not Telling Us

- Once again I refer to Jim Dunnigan's Strategypage.com. There is a recorded 28-minute interview entitled, The Aftermath of the Fort Hood Massacre – 12/11/2009. The stated purpose was that Austin Bay and Jim discuss the Fort Hood shooting and what changes it might prompt internally within the U.S. Military. The most interesting part was the fact that the shooter could not have been suffering from stress. His work reviews were poor and he had a third of the usual workload. What became clear is that the warning signals were flashing but no one wanted to pull the plug, fearing anti-something backlash. <http://www.strategypage.com/strategytalk/default.aspx>
- At Copenhagen, one speaker received a standing ovation-Hugo Chavez. He criticized capitalism and the USA. That should tell you all that you need is to know about the attendees.
- The Washington Post reported that former detainees of the U.S. prison in Guantanamo Bay, Cuba, have led the growing assertiveness of the al-Qaeda branch that claimed responsibility for the attempted Christmas Day bombing of a U.S. airliner. <http://www.washingtonpost.com/wp-dyn/content/article/2009/12/29/AR2009122902289.html?wpisrc=newsletter>
- The USA influence in Iraq has touched off a debate in the Middle East about the difference between policing and imprisonment in the West and in the Middle East. When the details about Abu Ghraib prison, better conditions than in any Arab nation and no torture, became public, the censors were unable to stop the public call for change.

What They Are Not Telling You About Healthcare

The N.Y. Times reported that states with expanded health coverage are pushing back against the Senate overhaul bill, arguing that it unfairly penalizes them in favor of states that have done little or nothing to extend benefits to the uninsured. These states, including Arizona, California, New Jersey, New York and Wisconsin, say they cannot afford to subsidize other states' expansion of healthcare. And people try to tell me that this is not socialism.

Don't Worry-Be Happy

Despite the economic numbers, there are ongoing signs that the American people are waking up. The announcement by Alabama Rep. Parker Griffith that he is switching to the Republican Party is another response from America to the administration along with the governorship losses in Va. And N.J. Griffith warned the Democratic Party to plot a more moderate centrist course.

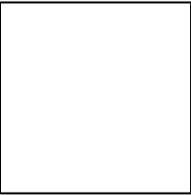
And there are signs that the economic process of writing off of worthless debt and its accompanying fall in prices is trying to take place. Colorado's minimum wage will drop slightly in the New Year, the first decrease in any state's minimum wage since the federal minimum was adopted in 1938. Colorado's wage is falling 3 cents an hour, from \$7.28 to the federal level of \$7.25. That's because Colorado is one of 10 states that tie the state minimum wage to inflation. The goal is to protect low-wage workers from having unchanged paychecks as the cost of living goes up. But Colorado's provision also allows wage declines, and the state's consumer price index fell 0.6 percent last year, so the minimum wage is going down. The lower consumer price index, attributed to lower fuel prices, would have forced the wage down 4 cents an hour, but no state can go below the federal minimum of \$7.25

Quote of the Month

"The farther backward you look, the further forward you see."
-Winston Churchill

Book Reviews

This Time is Different by Carmen M. Reinhart and Kenneth S. Rogoff. In the words of Niall Ferguson, *"This is simply the best empirical investigation of financial crises ever published."* When I browsed the introduction to this fine volume, I found a graph that expressed sovereign external debt from 1800 to 2008, expressed as a percentage of countries in external default or restructuring, weighted by their share of world income. The authors, from Princeton, do their best to place the study of crises upon some common yardsticks, such as the graph that I described. It is not always possible to do so, therefore a bank run has to be defined a bit subjectively. For example, following a banking crisis, government debt rises for about 3 years by 86%. There is a chapter devoted to cycles of sovereign default. The authors cite the important and ephemeral role of confidence in the recurring nature of such crises. If you are a financial historian, this must be read.



CFRS Portfolio

The CFRS model portfolio rose 17.43% in Q3 versus a rise of 14.98% for the S&P.
Looking at the returns on an annualized basis from January 1, 1996 through September 30, 2009:

S&P Annual Return: 4.0%

Portfolio Annual Return: 21.0%

*Disclaimer: The methods utilized have proven profitable in the past but no guarantee can be made of future performance nor is any liability accepted.
See the website at cyclesresearch.com.*

The report is sent on or prior to the open of the first trading day of the new month, unless otherwise stated. If you do contact us by e-mail, kindly give your full name. We cannot query the database by e-mail address. Thank you.

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