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Inside this issue

[Turning Lemons In To Lemonade?!?!](#)

[The Lone Bull On Wall Street](#)

[Refer a Friend](#)

Turning Lemons In To Lemonade?!?!

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**As many of you know, I am a list maker. I have my list of things to do around the house. I have my list of research items to test in the financial markets. I have my list of things I need to do at the office. And I have my list of topics to include in this newsletter. And that's only the first page of my lists!**

**And while my wife once bought me a Palm Pilot to keep me organized, I somehow regressed back to those old Post It notes. I even have a little white spiral notebook where I stick those Post It notes and make more lists. So today I decided I was going to knock out six things on my office list before I went home, which was totally doable given that it wasn't even lunch yet.**

**I was humming along early in the afternoon and decided to update all of my investment models and indicators that use weekly and monthly data. As I walked out of my office over to the desk where that PC resides, I got that "deer in the headlights" feeling as I looked down at the carpet.**

**The medium green color had a wide swath of dark green. The "oh no" thought raced through my mind as I slowly walked over to see that the brand new 6 gallon water bottle I had just put in the cooler was only 1/4 full with water streaming out of the bottom all over the floor.**

**It wasn't bad enough that I just paid \$3.50 a gallon for home heating oil, but now my office had a mini flood and I had to figure out how to get it cleaned up pronto. Many old Wall Street Journals later on the floor and I got back to my list, but I didn't get my 6 items checked off. Such is life sometimes.**

**I was once quoted in a national newspaper as saying, "when the market gives you lemons, you make lemonade"; something I am certain never came out of my mouth. But as with my mishap earlier in the day, I came in with a plan, much like I do every day and week in the market, but sometimes the powers that be force you to adapt and adjust on the fly.**

**Having a plan in the markets as well as life is certainly no guarantee of success, but it surely enhances your chances to succeed and puts you way ahead of the masses who simply react rather than "proact".**

## **The Lone Bull On Wall Street**

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Now that I set up a nice segue (or maybe I didn't), let's spend some time on the financial markets and my plan. My original intent was to discuss some big picture items with the economy, but I think it's best to divide this into two emails and focus our attention on the markets tonight and the economy in a few days.

Since the dramatic low we saw on January 22 and 23, I spelled out three possible scenarios for stocks. Thankfully so far, the stock market has followed the path I labeled as most likely. We were watching for a 2-4 week rally that had to finish up by the end of February for a variety of technical reasons.

Although it wasn't an "easy" rally as we saw many violent moves in both directions, the major indices moved higher into early February, back off and rallied again into the last week of the month, all on weak volume. Then comes the harder part.

It has been and remains my preferred scenario that stocks use the first few weeks of March to revisit the panic bottom we saw as that rogue trader from Societe Generale had his positions liquidated around the globe during the M.L. King holiday. Now, a retest of a prior low can come in many forms as it does its best to confound the masses and convince people that a whole other wave of selling is about to be unleashed.

If you go back and look at a chart during that time, you will notice the absolute low from that day is much lower than the close that day. A common

question I get is do we have to retest the lowest low or just the closing low. The answer is, as you might have guessed, both can qualify.

I have been using the behavior in 1987, 1990 and 1998 as similar periods to today and there was not consistent theme. While I firmly believe the fundamental backdrop is eerily similar to 1990, the stock market acts much more like 1987 and 1998 when we saw a decent rally following the panic low.

Another question I get is must all of the major indices revisit those lows. The answer is no. The Nasdaq Composite has already scored a new closing low and is within one bad day of the old lows, while the S&P Mid Cap is substantially above both of its lows. In 1987 and 1998, some indices made slightly lower lows, and others did not.

The markets cannot always be black and white, no matter how hard I tell them they have to! And we have to remain flexible as the potential is there for the best buying opportunity of the year.

So I remain on guard for a continuation of extreme volatility with the likelihood of one more nasty bout of selling in the next few weeks. Should that occur, I expect another feeling of panic and despair to dominate the markets and convince the masses we are headed for another 2000 - 2002 bear market.

It will be that event where the smart money will be gobbling up shares in anticipation of a very powerful rally into spring and summer, worst case. Yes, I believe that even if we are in a longer-term bear market, which I don't, the second quarter is going to be a strong one for stocks. From low to high, we should see at least a 10% rally.

The best case scenario is that we see enough capitulation with enormous volume, margin calls, widespread fear that we actually launch a new bull market that lasts at least through year-end. Should that happen, we could see a 15-20% rally from low to high, taking the major indices into positive territory for 2008.

The keys to watch over the next few weeks are overall market volume, reactions to bad news which will dominate long after the horse leaves the starting gate, sector leadership and skepticism about any rally that begins.

Just yesterday, we heard Intel warn about profit growth, yet by the close of trading, the stock was EVEN on the day with more than 124 million shares trading hands! If the market was anywhere near as weak as it was in January, we would have seen a complete rout.

Before I begin to close this edition, we've all heard from the suddenly chatty Federal Reserve about all the things that ail our economy and their efforts to overcome them. Talk about sending up a trial balloon for more dramatic rate cuts!

I don't know if Big Ben is going to do another emergency cut this week, but there is NO DOUBT that at least another 1/2%, if not 3/4%, is going to get chopped off the Fed Fund rate on March 18 with even more to come. When all is said and done, short-term rates will be well below 2%, adding more fuel to the stock market.

Lastly, a fair question I am sure someone is going to ask is how will I know if I am wrong. After all, I have been wrong before and will be wrong again (and again). If the major indices approach the intra day lows from January without accelerating and without volume increasing and without much fear and despair, then I am likely wrong on my very bullish outlook. That slow and steady drip would continue for some time with meager and failing rallies along the way.

We are getting close to a great opportunity! Patience should be rewarded much sooner than later if you have dry powder to act. The best advice I can offer is to ignore the constant barrage of gloom and doom in the media. It happens at every major stock market bottom.

Folks, I want to hear from you! I enjoy exchanging emails and readers challenging my opinion. That's good and healthy dialogue. Please feel free to hit reply with your questions and comments or pick up the phone and call me directly at 203.389.3553. I promise; I don't bite!

Refer a Friend

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