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The Death of the U.S. Economy

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**It's BADDDDDD out there, huh? Not an hour goes by, let alone a day, when I don't see another headline confirming the gloom and doom. I mean, it's REALLY bad! In fact, we've already stockpiled our supply of pencils and apples to sell on the streets. I don't know how anyone can possibly sleep with the dire news backdrop.**

**Let's see. We've got:**

**a severe credit crunch unfolding**

**some banks on the verge of solvency**

**housing bust**

**an economy on the brink of recession**

**inflation**

**war in Iraq**

**Please reread those problems again. You agree, right? How could you not! It certainly sounds like a country on the verge of depression. And of course, let's not forget the chorus of the U.S. no longer being the world economic leader.**

**Folks, those were the headlines 17 years ago in December 1990!**

**Back then, the credit crunch last several years, while the pundits continually called for severe economic conditions. That was during the infamous savings and loan crisis when the government created The Resolution Trust Company to bail out the system.**

**I remember working at Shearson Lehman and hearing rumors almost every day that Chase Manhattan was only days away from declaring insolvency. And that would certainly spell disaster for our entire country.**

**Housing prices peaked just before the 1987 crash and were in steady decline for 4 - 6 years, depending on which study you review. Crude oil had spiked and the experts were certain that \$40 oil would lead to recession, while \$50 oil would mean a severe recession and the unthinkable \$70 oil equaled depression. Inflation was going to be epic!**

**And who could forget the best selling book by Ravi Batra, The Great Depression of 1990! And all this was in the midst of an impending war with the fourth largest army on earth, well equipped with biological and chemical weapons!**

**Yeah, it was unbelievably bad back then.**

**The Dow Jones Industrial Average just hit 2400. The S&P 500 kissed 300 and the Nasdaq saw 325. And they NEVER went below those levels again!**

**Imagine that. With the constant stream of bad news and horrific headlines, the good ole U.S stock market took off like a rocket in early 1991, going essentially straight up for years, not days or months.**

**The Dow climbed to 11,000 within 9 years, while the S&P 500 ran above 1500. But the real winner was the Nasdaq that surged to 5000. Those moves are mind boggling!**

**I guess rumors of the death of the U.S financial system had been greatly exaggerated!**

**Does any of this sound familiar? It should since it's going on right now. We have a housing bust resulting from ill conceived financial engineering by the banks and brokerages. There's a credit crunch that's only just begun. The economic data seemingly gets worse each day and headline inflation is the worst in 30 years. And let's not forget the war in Iraq.**

Every single poll I have seen this month shows the same thing. The U.S. consumer has NEVER been more negative or more concerned or worried about the state of the economy that right now. Think about that. People are about as down as they could be without a bear market in stocks.

That's incredible to me since I cannot remember any time in history where accepted recession forecasts ever came true. Sure, we can have slow or no growth, but the masses have never, ever correctly predicted a recession. Imagine this. Consumers are more negative about the economy now than at any time during the 2000 - 2002 bear market and the 1987 stock market crash.

We are living history in the making. What's even more unreal is that the stock market doesn't seem to care. Yes, it had two 10% declines this year, but it's essentially flat to up for 2007. (That's the market, not our own strategies!)

Surely, if housing, the credit crunch, inflation and recession were becoming so prevalent, the stock market would be in much worse shape than it is right now. But it's been pretty resilient if you ask me!

And even if it corrected another 5 - 8% from here next quarter, I would have the same opinion. Unless sentiment dramatically changes, I do not believe the U.S. economy will fall into recession in 2008.

## What's Not to Love

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As far as the stock market goes, last week I had these comments,

I believe any weakness we see over the next week, likely due from either Lehman's or Morgan Stanley's earnings or the inflation reports is a buying opportunity for the rest of 2007.

Sentiment still supports additional price appreciation and we have seen significant buying from corporate insiders. We are also approaching the most positive seasonal period and all this adds up to a rally.

Those feelings remain today. Having sidestepped all of the summer 10% decline and a good portion of the fall 10% decline, our portfolios held a large amount of cash until early November when we put roughly 50% to work. After the market's reaction to the disappointing news from the Fed, we added more money and the final chunk was added early this week.

This brings our portfolios to fully invested for the first time since early July. It doesn't mean that stocks have to go up right now, although we certainly believe they will. But it does indicate that reward far outweighs risk over the intermediate-term.

For those who listened and reacted when I last sent an email to add money to your account or open a new strategy, I truly believe you acted prudently by "buying" into scary headlines and a stock market correction, exactly what smart money does!

The stock market is now in its most seasonally positive time of the year. Buying by corporate insiders is at historically high levels. As long as the major indexes continue to make a series of higher lows, meaning the August bottom was the lowest, followed by the November low a bit higher and the December low even higher, stocks should be on solid footing.

By almost every measure I use to gauge sentiment, investors are extremely negative on the prospects for equities, while smart money remains positive. Since the masses are usually wrong, these are the right ingredients for a rally into the new year and possibly longer.

Savvy investors are beginning to bargain hunt in the financial space to balance off good holdings in technology. We continue to favor energy, utilities and pharma as well.

It's now way past my bedtime and I am sure there are many typos that I won't catch. Although there are usually typos I don't catch when I write this during the day!

In case this is my last update of 2007, I thank you for reading and your continued support, confidence and trust.

I wish you and your families a very happy, healthy and prosperous New Year!

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