Exceptional Bear Market Letter

August 29, 2009

Precipitous decline by October, likely a CRASH

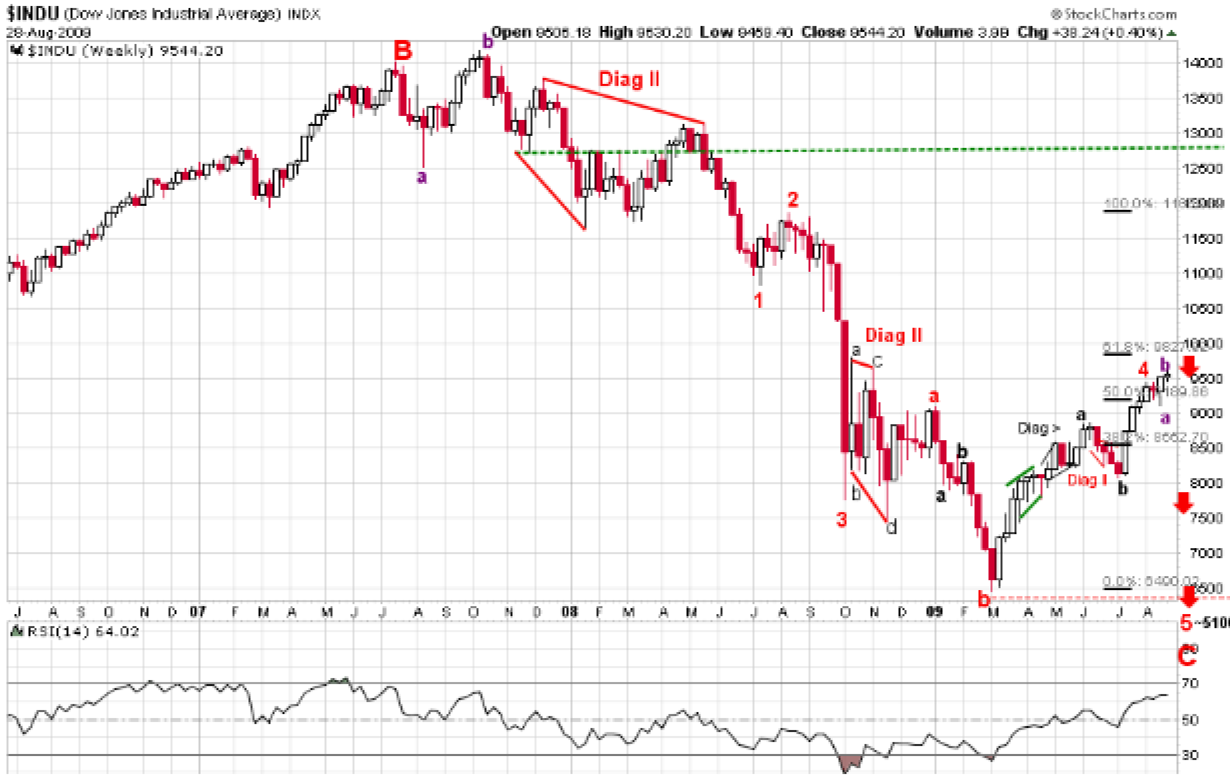
An extraordinary opportunity for tremendous gain or excrcuciating pain.

There are few investors left to be *erroneously* convinced that the economy is beginning to recover. Consumers are *usually wrong* at tops and bottoms, consumer confidence, which rose from 47.4 to 54.1 in August, is a *contrary indicator*. Similarly contrary, is Investors' Intelligence survey of advisory services which showed 51% Bullish against only 19% Bearish. The last time the spread was this wide was in November 2007, just before the top of the previous Bear Market Rally. Is it different this time? Not likely! Only the slightly higher serial *b transitions* that account for the slight upside. Even a sharp rise in new homes was met with a big yawn, while in July a similar jump in sales sent the S&P up 2.3% in a day.

We know that corporate insiders, *the smart money, have gotten out of the market in record numbers during the last six weeks.* While in March the US Equity Market was undervalued for the first time since 1988, on the basis of 10-year average earnings, the S&P is now 23% overvalued. Since the market makes wide swings from overvaluation to undervaluation, we can expect gross undervaluation as a requisite for the *real rally* to begin. This false rally is spent, and what appeared to be indices continuing to creep up, was in reality setting the stage for a *sudden collapse*.

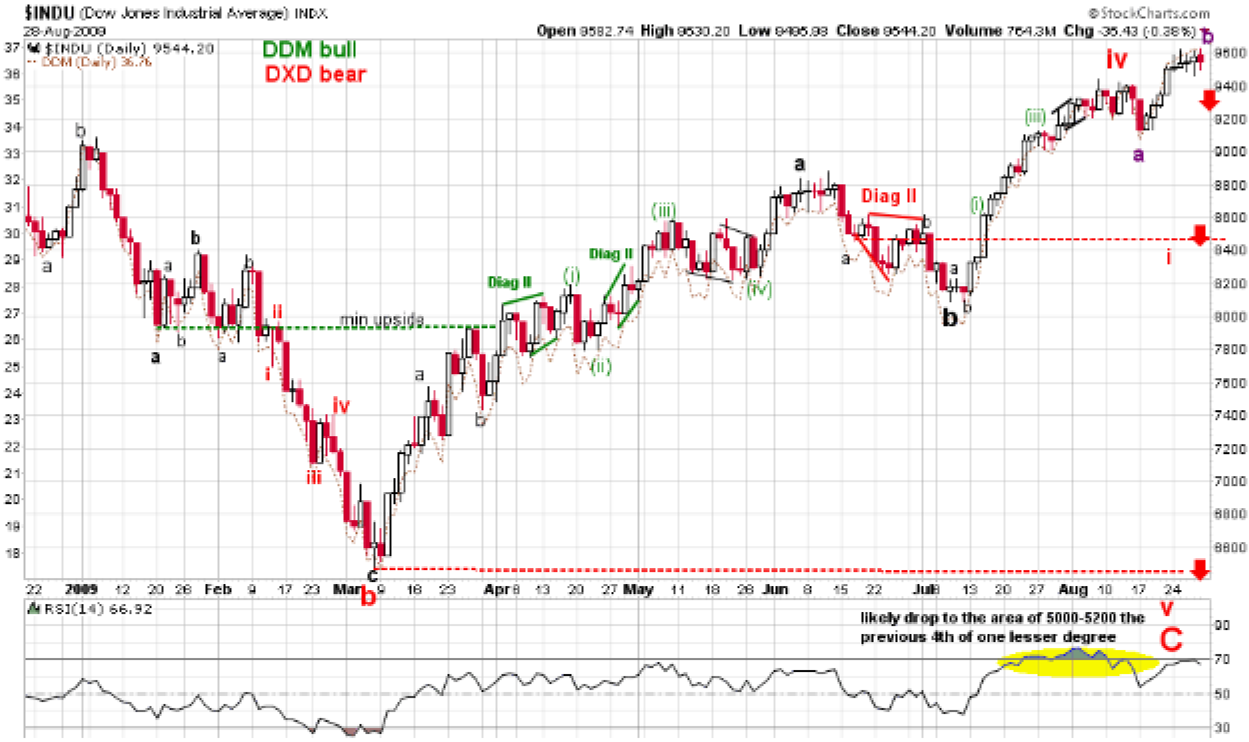
Meanwhile what passed for the Market's resounding approval of Mr. Bernanke's re-appointment was more likely just another example of Market Manipulation intended to deceive the public, and sway public opinion. The Fed has gotten good at timing futures purchases to coincide with major announcements, whihc is always given credence by the press. And what to make of *"break out"* in government-backed enterprises: AIG, Citibank, Fannie Mae, Freddie Mac and Bank of America last week? AIG stcok rose 53% to $50, while Barron's estimates negative shareholder equity of $7 per share. Yet another example of this blatant attempt to deceive. Decption is always destructive.

In the 1987 Crash the Fed first made use of Futures, when the Crash had already run its course. Like now, they believed they had saved the day, with this fool-proof method. It gave the Fed a false sense of security, on which they continue to rely on today. It is highly unlikely that this strategy will work at the *beginning of a Crash*; anymore than 1987's *portfolio insurance.* Portfolio insurance rather than insuring portfolios exacerbated their losses in the crash. This time, the crash should easily dwarf 1987's 35% free fall.

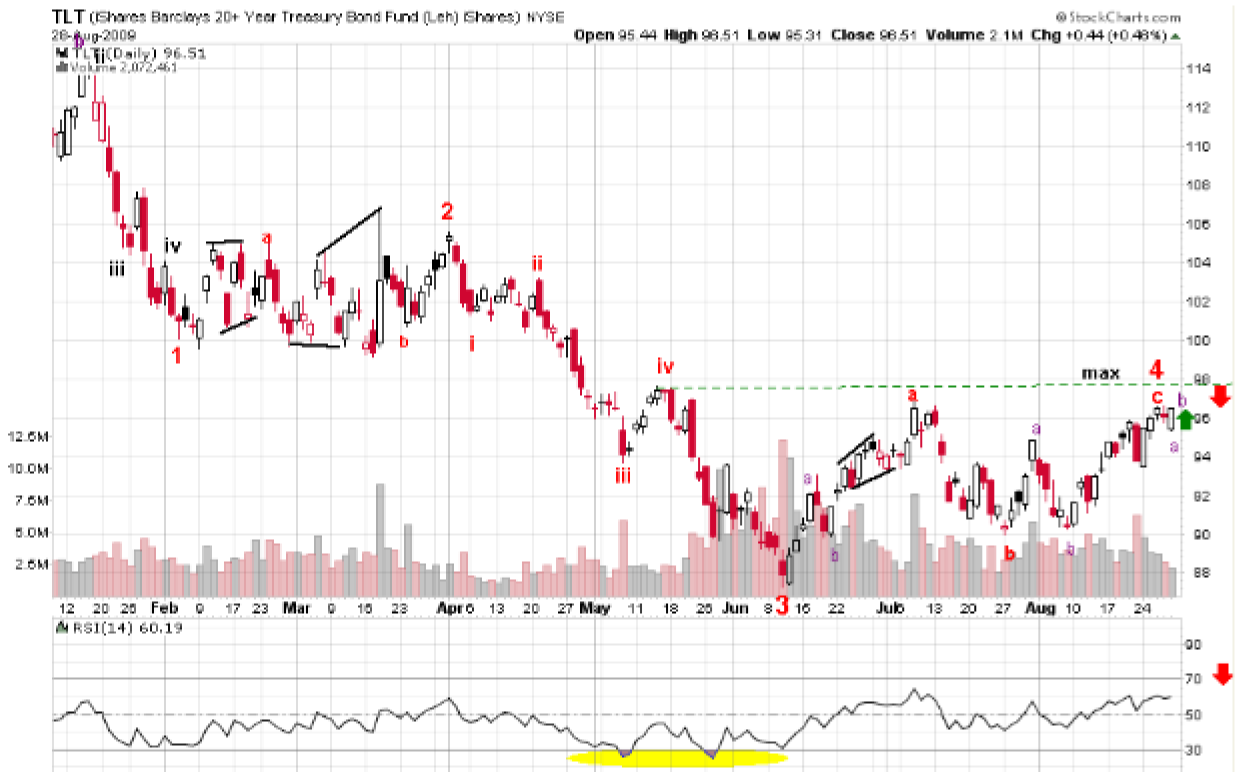


When a *Diag II* occurs at the top like this, the likely minimum downside is *at least* 5 times the length of the 3rd wave within the *Diag II*. Measuring on the perpendicular this would indicate a plunge of 5(2,250) points from roughly 14,000 which results in a ballpark trough of 2750. This is just a 1.8% deviation from our lower estimate of ~2700 to the second previous 4th wave - a *71% plunge* from where we are now.

In actuality we had a preview of the plunge ahead with Shanghai's 20% plummet earlier this month. This is the Market once hoped to lead the world out of recession, when in fact it will likely lead to a precipitous decline and likely Crash in world markets. Five times the longest leg of the *Diag II* measured to the perpendicular (52.5), subtracted from the high equals a number far lower than zero. In the absence of government intervention, China is *most certainly a CRASH to near zero.*



In the **Dow** the stage is set for a drop to the area of 8500 in wave i



Bonds are in the ***b*** transition down to **i.**

Wave (ii) in the **dollar index** has just one more day to go. Likely coinciding with the plunge in stocks is a *meteoric rise in the dollar*. *When we sell stocks, we buy dollars* or their equivalents.

After so much credence in a recovery rally, the last thing the market expects is a Crash – *that's precisely when they occur.* ***At the very minimum we have a 45% decline by the first week in October. This is an extraordinarily high probability gain/low probability loss entry point for inverse funds and short sales.***

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Regards,

Eduardo Mirahyes
Exceptional Bear

The <u>true</u> Wave Count