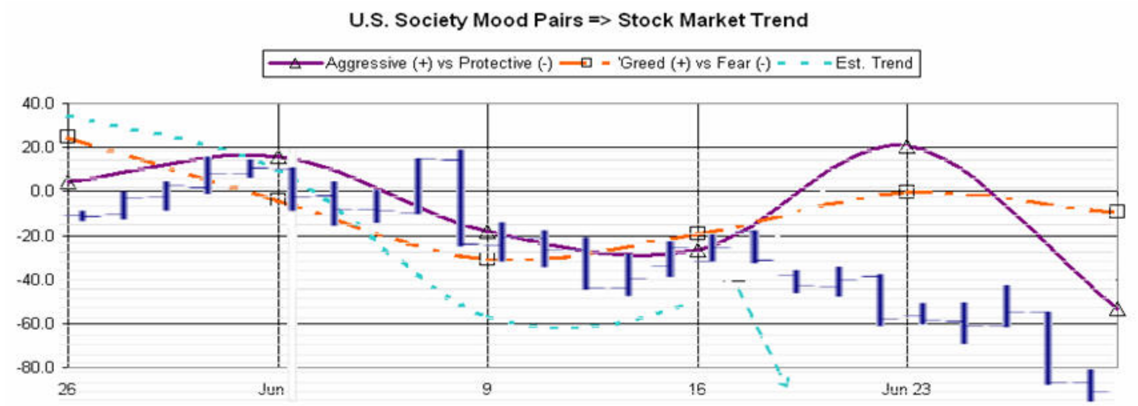
July *MoodCompass* Supplement –
Why There Never Was Going to Be a Crash This Month

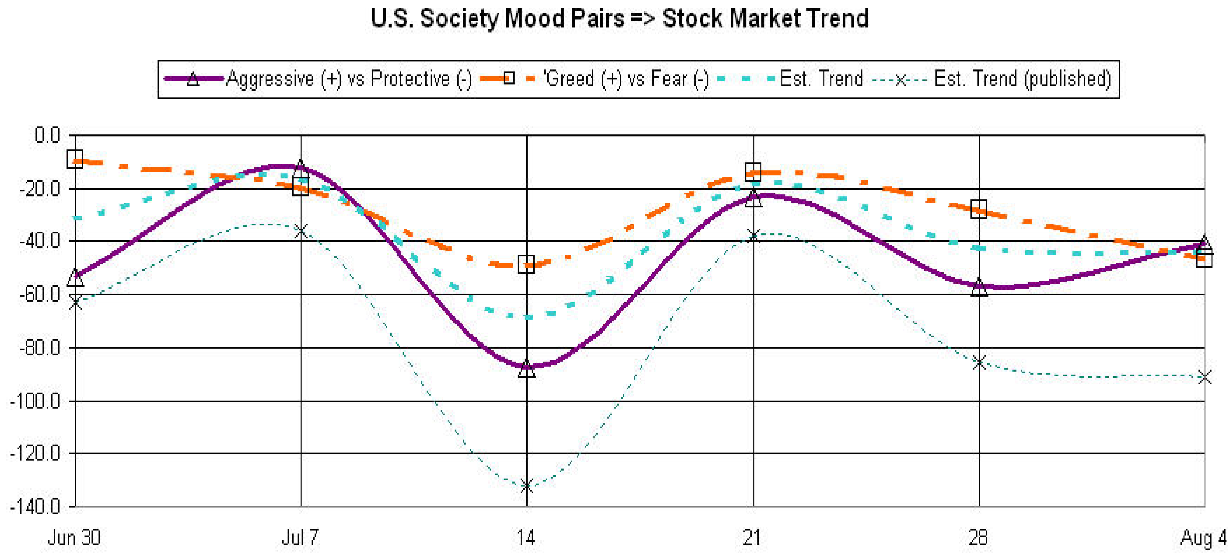
In the July issue of *MoodCompass*, we presented a crash scenario in the U.S. markets for July 7-11. While the call on extreme geopolitical tension was correct, and bearish sentiment in the markets is at an extreme, the markets did not crash. In reviewing what went into our forecast for the week, we have determined that the system and the models were correct. However, "operator error" caused the model to be misrepresented (an incorrect spreadsheet cell was selected for the estimated trend line in the S&P model). The result was a call for a crash that should never have been made. The purpose of this supplement is to show the nature of the error, what should have been presented, and hopefully repair any injuries to our model's credibility.

In the July issue, we presented the following chart highlighting our success with the June forecast:



The "estimated trend" line is calculated as simply the average of the values of the other two lines except in rare special cases such as the one depicted by the sharply down arrow on the right side of the chart. When preparing the June issue, we began experimenting with an alternate model to avoid having to manually decide these special cases and manually draw in a trend line such as in the above chart. We have abandoned this project for the time being, but unfortunately left the spreadsheet column that calculates the estimated trend line set to the experimental calculations. The calculated estimated trend line (through June 16) in the chart above is in error. It should have been simply the average of the other two lines, or halfway in between them. As you can see, the actual price data would have been an even better fit that way than it already was. However, because it was very close anyway, the error was not noticed.

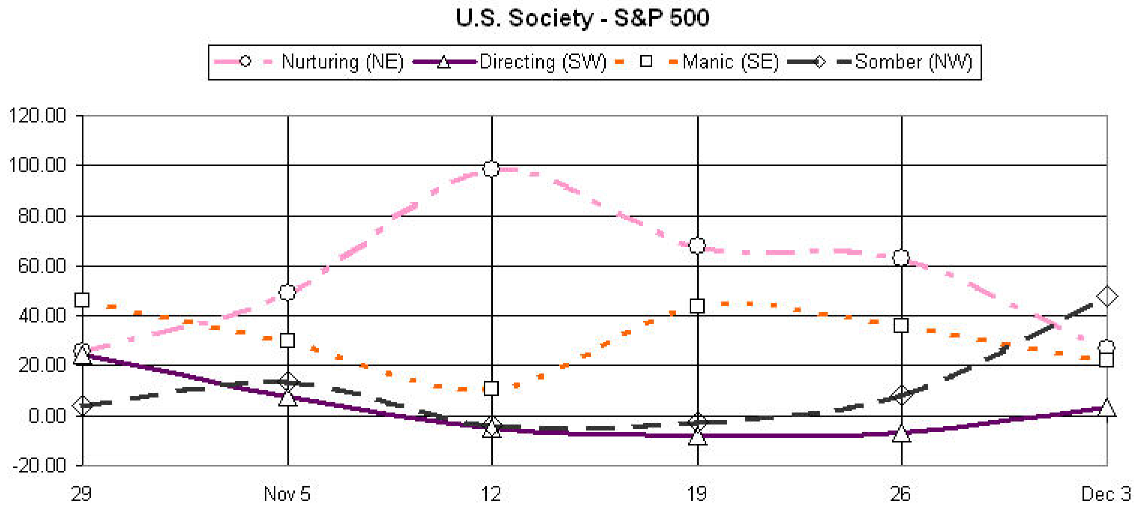
Below is the estimated trend for July. It includes the originally published estimated trend line as well as the corrected one.

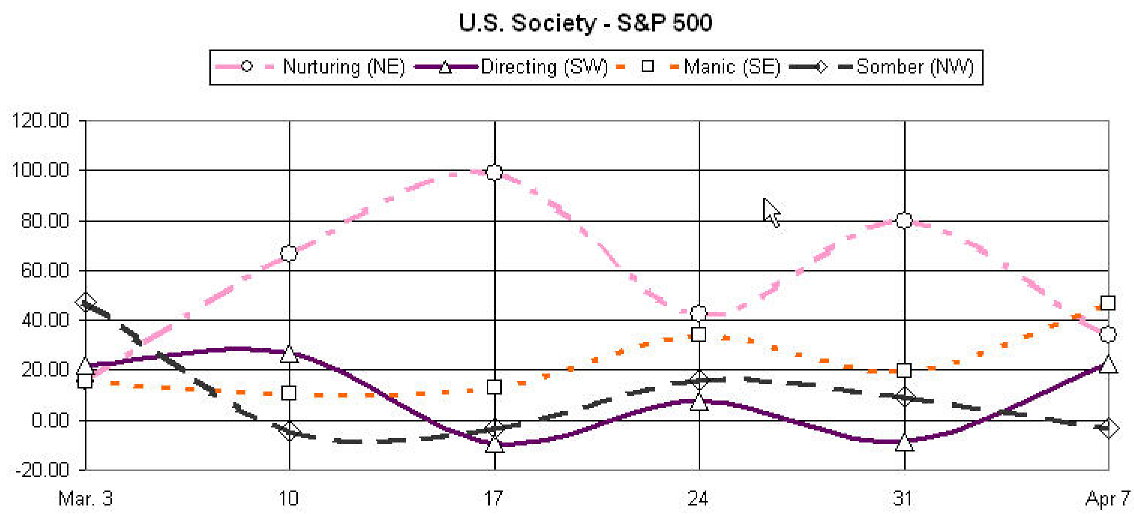


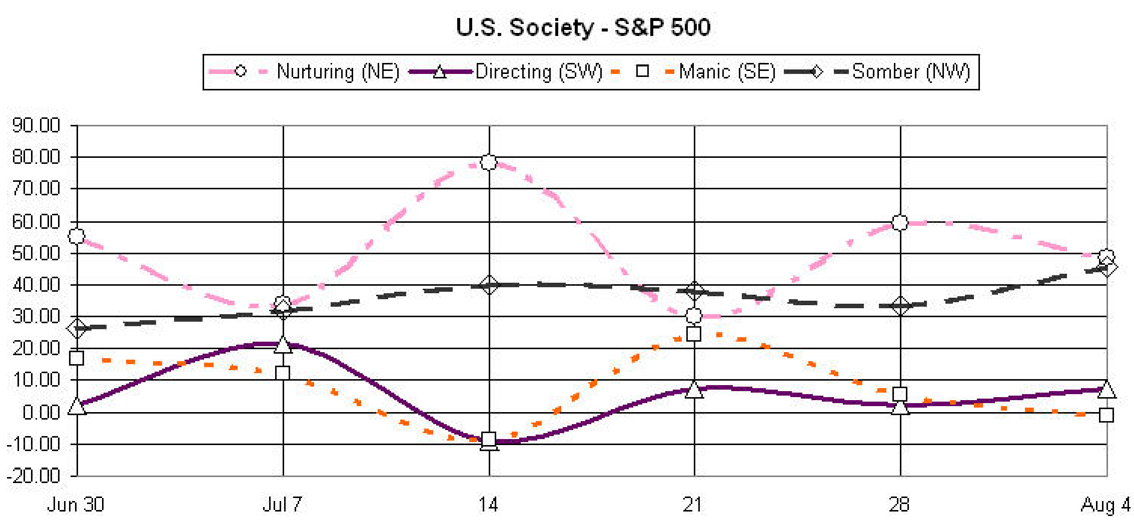
While the error here perhaps should have been obvious, its extremity fit well into the extreme nature of the geopolitical situation and economic stress that was indicated for July. In other words, the situation appeared so bad that a crash subjectively seemed appropriate and the error went unnoticed. While there may or may not end up being a crash in July or at any time, there is nothing showing up in our models to indicate anything more than another mediocre down month in the stock market.

Another indicator which at first glance supported the sharply down call is the pattern in the Moodlines. As shown in the charts below, a similar pattern appears in the notorious months of November 2007 and March 2008. In both November and March, S&P short term bottoms coincided with a high *Nurturing* vs. *Directing*, and short term tops coincided with a smaller difference between the two. This fact assisted us in developing the current model that converts the *Moodlines* to an estimated trend. We have data presented in the Moodline format since July 2007. So far, this pattern type has only shown up for those two months and for July 2008. However, as will be seen, there is something distinct about July that indicates it is less likely to have severe movements.

November 2007, March 2008, and July 2008
High Nurturing / Low Directing U.S. Society/S&P Patterns







The July pattern most closely resembles March, but with one important distinction. Running through the July pattern is an elevated *Somber* line. High *Somber* by itself is characteristic of down to sideways markets. Qualitatively it coincides with delusion, denial, cloudy thinking, lethargy, fear (but not panic). Its denial quality finds it often associated with bear market rallies. Superimposed on a pattern, *Somber* is like a dampening agent to the overall pattern, i.e. the pattern is "muffled." The net result is an overall directional pattern (high *Nurturing* coincides with extreme downward price pressure, and low *Nurturing* upward), however this will be "muffled" with sideways and countertrend movements intraweek.

We hope this clarifies our outlook on July. While it is a significant month as far as the development of the global economic downturn and concurrent geopolitical tensions, as far as the stock market is concerned, it's bearish, but not especially catastrophic. As far as social mood is concerned, there should be moments on par with March and November in terms of pessimism and the drive towards "seeking safety."