ROBERT PRECHTER

THE ELLIOTT WAVE THEORIST

STOCK MARKET INTEREST RATES PRECIOUS METALS

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A Major Stock Market Low is Still Due in 2003-2004

The Elliott Wave Theorist's cyclic and Fibonacci projections have long pointed to the year 2003 (with leeway to 2004) for a major low in the stock market. This low should mark Supercycle wave (a) of Grand Supercycle wave ⓦ. This bottom is expected to be of the magnitude of those registered in 1932, 1842, 1784 (±8) and 1722.

Several years have appeared to be good candidates for the bull market top, but none of them panned out. At this point, time is running out, and if our low is to come to pass, very little guesswork remains. This report will present a review of my cycle and Fibonacci studies to bring you up to date on the dramatic potential that lies directly ahead.

Kondratieff Cycle

In the early 1980s, there was serious debate about the timing of the previous Kondratieff cycle low. Was it 1932 or 1942? Today, of course, no one believes that the Kondratieff cycle exists, as they are convinced that economic cycles have been tamed by the Federal Reserve Board, and the trend is always up.

In May 1983, *The Elliott Wave Theorist* looked at the history of that cycle and the evidence of stock market action and concluded as follows: "Based on its previous low in 1896, the most recent Kondratieff cycle bottom…may have occurred as late as 1949, which places the next bottom around **2003**." Ever since EWT came to that conclusion, additional evidence has strengthened the case.

Should we rely on the Kondratieff cycle? Here is how *At the Crest of the Tidal Wave* answered that question:

> Most economists dismiss cycles altogether and appear particularly to relish denying the existence of the Kondratieff cycle. I take a strong position on the opposite side. While the time length for the Kondratieff cycle is usually cited as "50 to 60 years, averaging about 54 years in length," the record of stock prices reveals that this cycle has recently been quite precise. Price lows occurred in 1896, **53** years before 1949, and in 1842, **54** years before 1896, and (possibly) 1788, **54** years before 1842. Sparse data indicates that the latter date could have been any of several years between 1778 and 1788 (see discussion in Chapter 2). The cycle that occurred in the 1700s in British stock prices appears to have been longer, at **[56-66]** years, lasting from 1722 to [1778 to 1788]. The answer, then, is that if the cycle is still operating, our timing projection should be fairly reliable. The earliest likely year for a bottom is **2002**, the best fit is **2003**, and match of the longest cycle on record would place the low as far out as **2011**.

Figure 1 displays the history of the Kondratieff cycle against the Dow Jones Industrial Average.

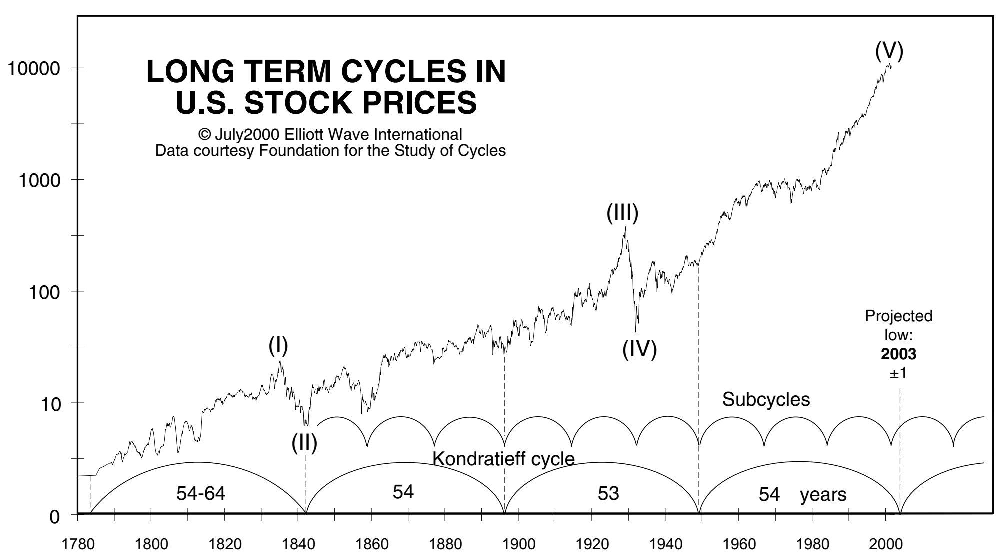

Figure 1

Figure 2 shows a close-up of the last two cycles against the PPI-adjusted DJIA, revealing why I dated the cycle bottom later than other cycle-watchers. The 1929 high and subsequent crash occurred early in the down portion of the cycle, which is why Kondratieff cycle enthusiasts were thrown off about the position of the previous cycle bottom. Inflation-adjusted stock prices scraped bottom until the cycle finally ceased exerting downside pressure. For the record, 1948 was the end of the cycle in PPI-adjusted terms, while 1949 was the end of the cycle in nominal terms, so the proper designation for the low is 1948-1949.

With all-time highs being achieved this year (in fact, two indexes are at an all-time high as this is written), most people would think that the idea of a major stock market low three years from now is absurd. In fact, though, three of the last four Kondratieff-related stock market bottoms occurred within a few short years of an all-time high stock market peak: 1720-1722: *2 years*; 1835-1842: *7 years*; 1929-1932: *3 years*. In two of the four the cases (1722 and 1835), the stock market topped extremely late in the Kondratieff cycle and then crashed. This is the prospect we face today.

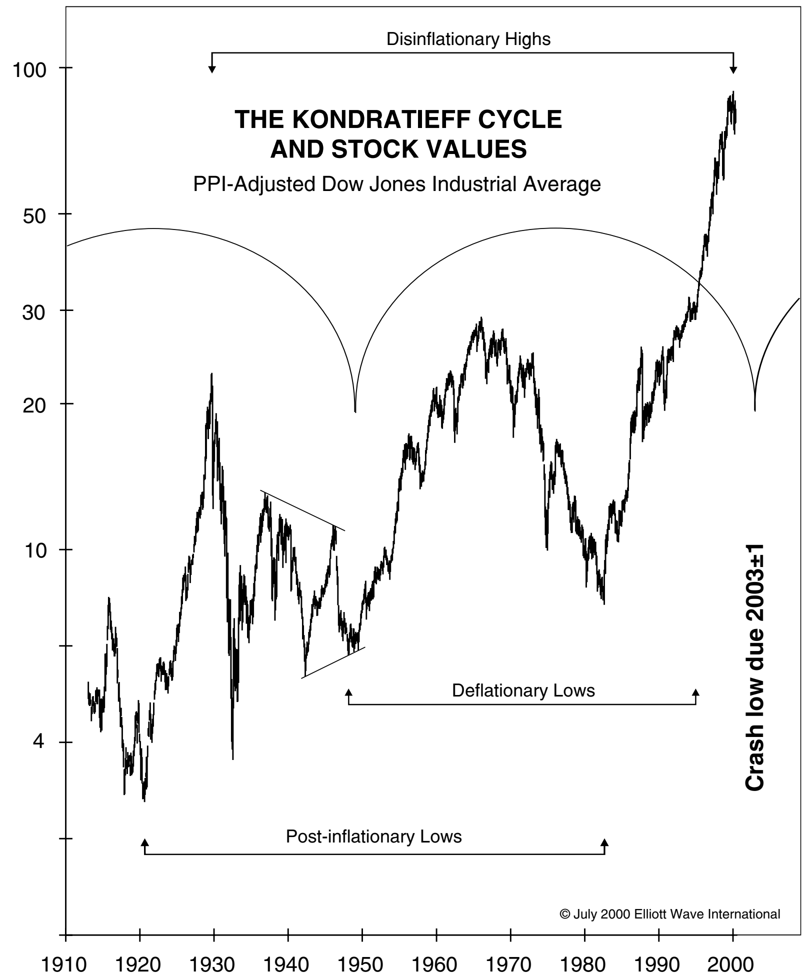

Figure 2

The Benner-Fibonacci Cycle

A.J. Frost worked out a pattern of cyclic repetition that has a basis in the Fibonacci sequence. We presented the idea in Chapter 4 of *Elliott Wave Principle* in 1978. In that book, we showed the progression of the cycles through 1987, which we forecast as the next important low. *At the Crest of the Tidal Wave* presented the extended progression, calling for the next low in 2003, coincident with the projected Kondratieff cycle low. Figure 3 shows the entire Benner-Fibonacci cycle chart from 1895 through 2003.

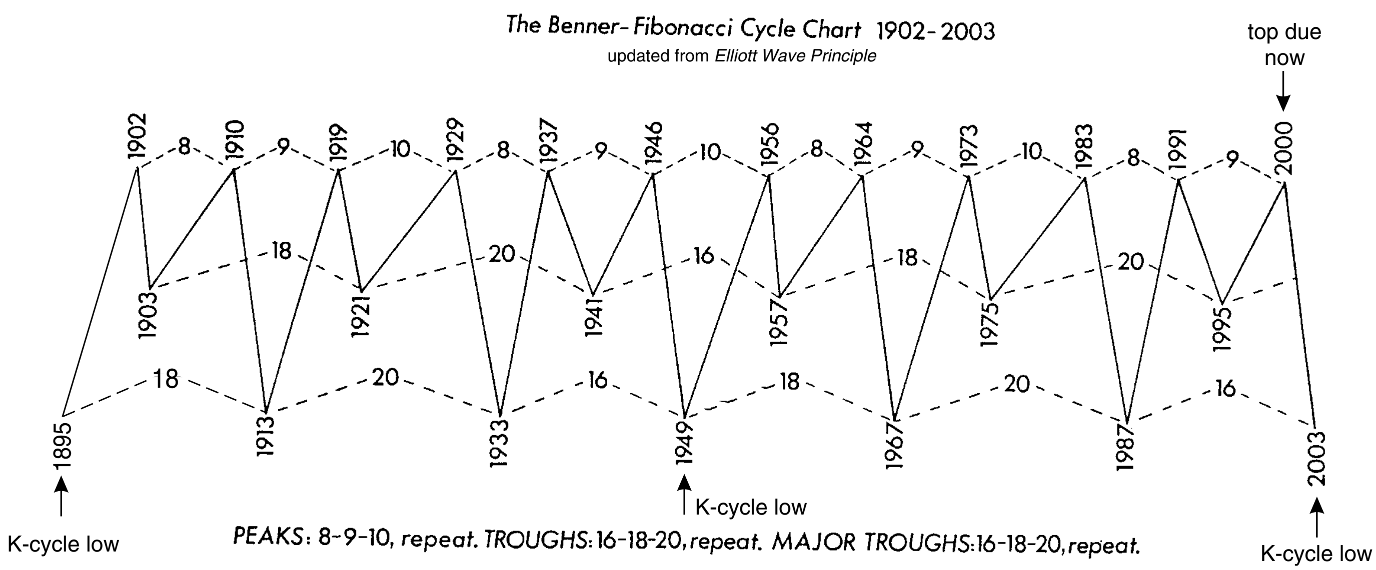

Figure 3

At least as interesting as the next projected bottom is the fact that Benner-Fibonacci cycles also project a *top* in the year 2000, i.e., *now*. For the record, note that the 1896 low occurred a year after the cycle bottomed, the 1974 low occurred a month prior to the projected bottom in 1975, and the 1994 low occurred several months early. No cyclic model is perfect, but these projections have nevertheless been quite a good guide.

Fibonacci Durations

Figure 4 shows the Fibonacci web of peaks that began in 1966. From there to the top in 1987 took **21** years. Had the current Kondratieff cycle acted like the previous one, that year would have been the high in stock prices. However, following the crash, the market resumed its upward path and has now climbed an additional **13** years, for a total of **34** years from the 1966 high. Thus, two Fibonacci durations related to tops end in 2000. As you can see in Figure 5, this feat has produced a secondary Fibonacci result, which is that wave V from 1974 now subdivides into two phases of advance lasting a Fibonacci **13** years each.

Figure 6 shows that a remarkable four Fibonacci durations related to stock market bottoms all end in 2003. That year is **13** years from 1990, when the three-year bear market in the Value Line index ended, completing the largest setback within the two-decade stock mania. It is **21** years from 1982, the bottom of the 16-year bear market in the inflation-adjusted Dow. It is **55** years from 1948, the end of the 19-year bear-market triangle in the inflation-adjusted DJIA. It is **144** years from 1859, the end of Supercycle wave (II). This is a remarkable cluster of dates all pointing to the same year.

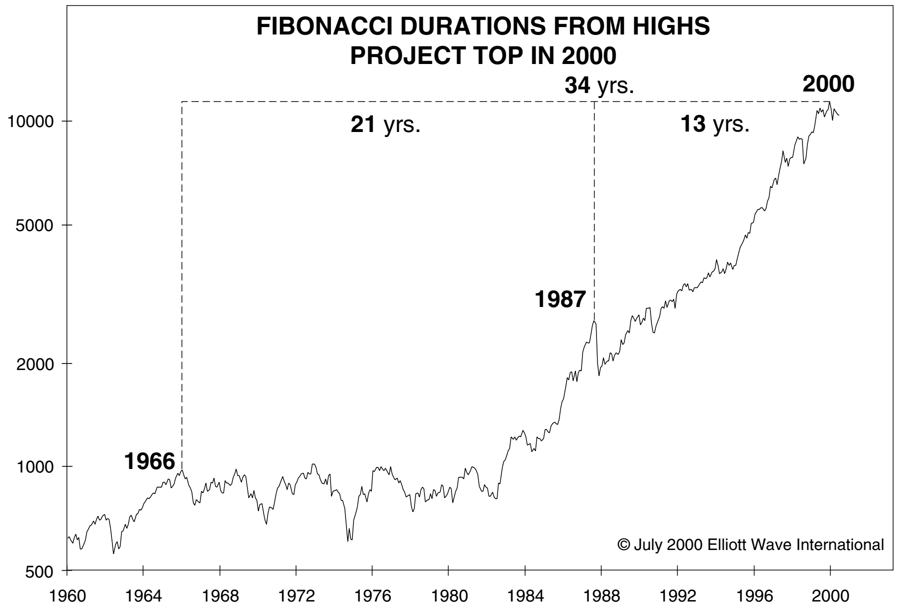

Figure 4

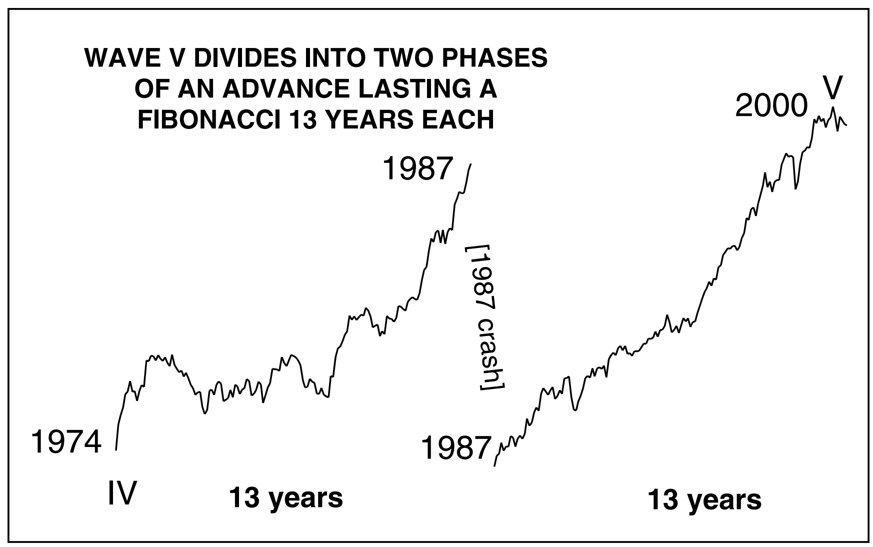

Figure 5

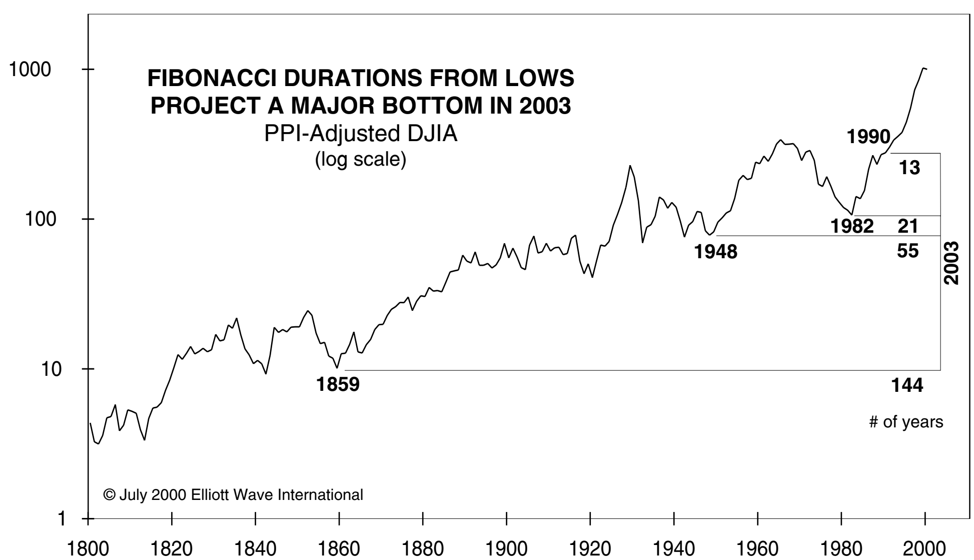

Figure 6

Together, these clusters project a major high in the year **2000** and a major low in the year **2003**. Notice that these Fibonacci durations, while unrelated to the Benner-Fibonacci cycles and the Kondratieff cycle, *nevertheless indicate the same years for a major top and bottom.*

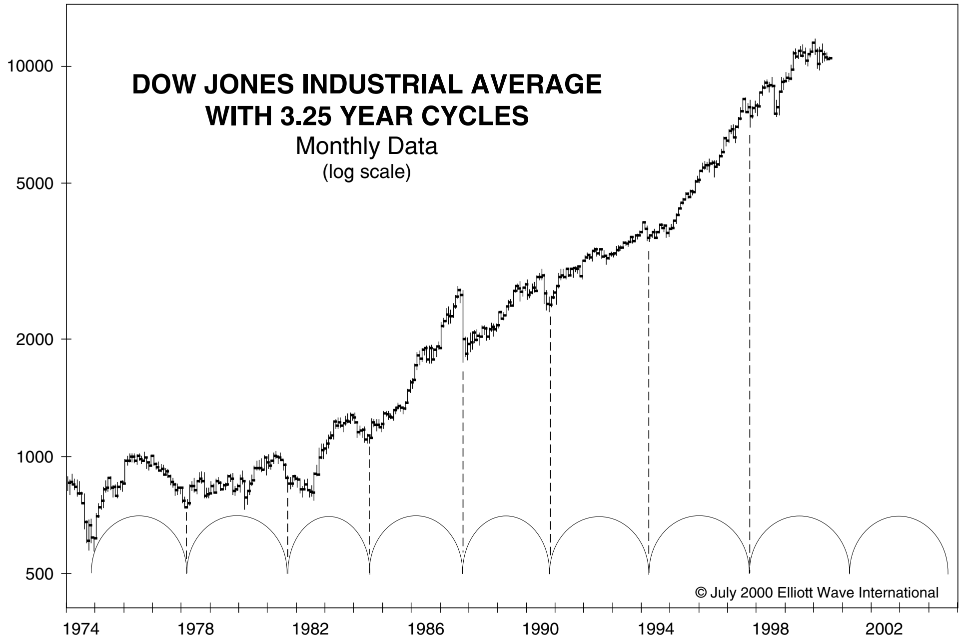

Figure 7

The 3-Year Cycle

Back in 1978, I predicted in *Elliott Wave Principle* that the 4-year cycle would shrink to 3.5 years because a whole new Elliott wave of Cycle degree was due to begin. The cycle shrank immediately thereafter, averaging 3.25 years in length, with bottoms in 1978, 1981, 1984, 1987, 1990, 1994 (January) and 1997. The next two bottoms are due at **year-end 2000**, ±2 months and in the first half of **2004**. See Figure 7.

Only One Year's Leeway

Several considerations suggest that the low could occur as late as 2004, which is a small allowance given the substantial length of the Kondratieff cycle. The 3.25-year cycle is ideally due to bottom in early 2004, as detailed above. The Decennial Pattern is an average of the market's action each decade. It would be nothing more than a statistical artifact were it not for the fact that the market has tended to follow the pattern in each individual decade. The pattern bottoms in the second year of the decade, with little upside progress until the middle of the fourth year. In two recent decades, the zero and fourth years, rather than the second year, have marked lows: 1970/1974 and 1990/1994. It could happen again. Alternatively, recall that the market tested its 1932 low in 1933 with an 80% retracement of the first wave up. If 2003 marks the bottom, 2004 could include a deep setback to test that low. As you can see in Figure 8, downside pressure from the Decennial pattern ends just shy of midway through the "4" year. The economy typically lags the stock market, so if stocks collapse into 2003, the severest year of the resulting depression should be 2004, so *some* measures will probably bottom then. Finally, because the preceding

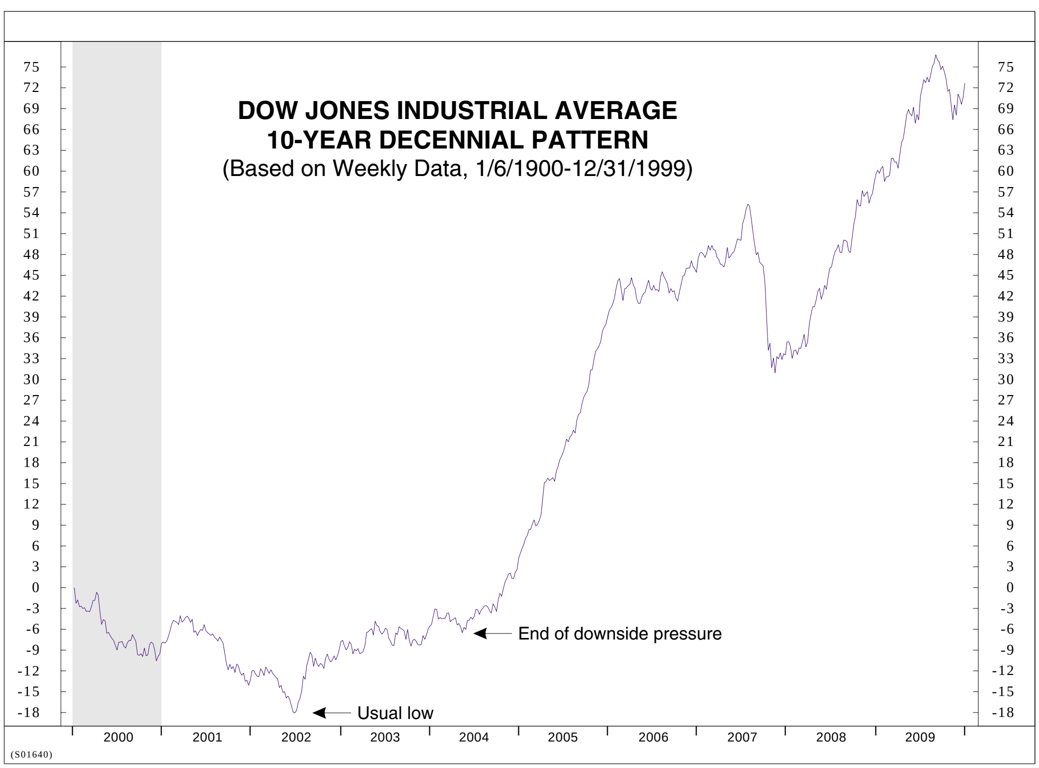

Figure 8

Kondratieff cycle lasted only 53 years to 1949 (or 52 years to 1948), the current cycle might stretch to 2004 to maintain the 54-year average.

The 20-year cycle bottoms in 2002, as you can see in Figure 9. There seems to be too little time for the stock market to bottom that quickly, but the 1720-1722 experience (see discussion below) shows that it is possible. My guess is that the pressure from this cycle will simply make the year leading up to its low the most powerful portion of the decline.

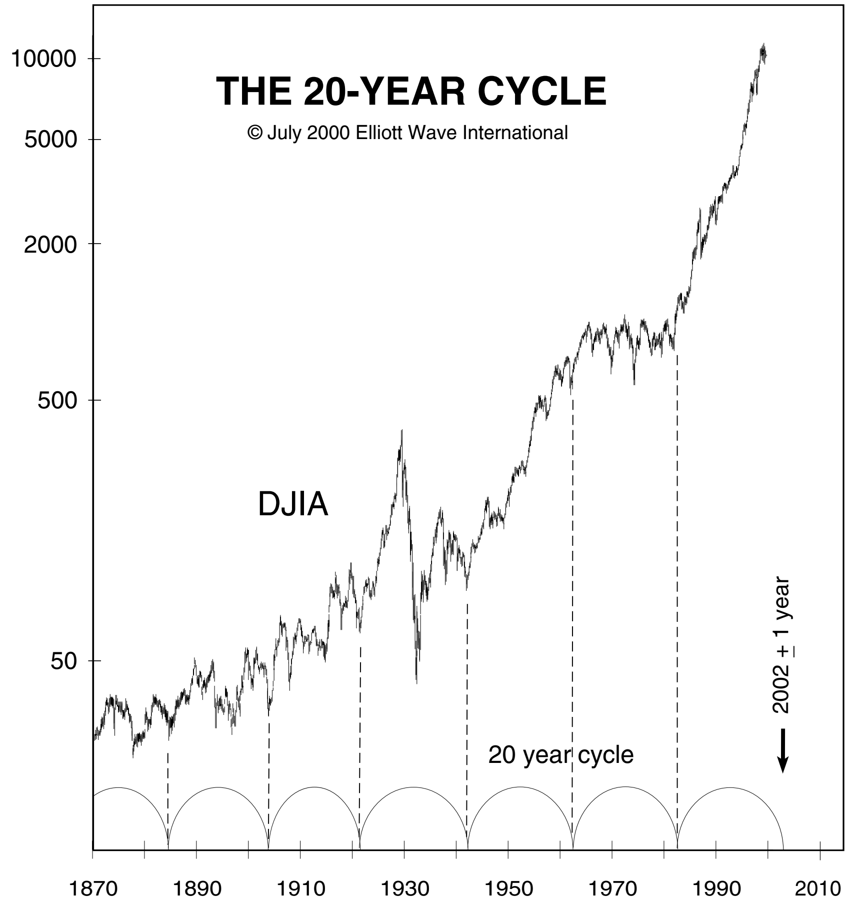

Figure 9

Probable Depth and Results

Kondratieff cycle stock market collapses of the past three centuries have ranged from 46% to 98%. In 1720-1722, the average stock on the London exchange, properly factoring in those that dropped to zero, fell 98%. The decline that ended in 1784 is difficult to assess, as the crash of 1720-1722 dampened stock speculation for a century. The depression of the early 1790s was severe, covering the Americas and Europe, so regardless of the exact figures, it was clearly a disaster for whatever stock owners there were. In 1835-1842, a reconstructed average of U.S. stocks fell 78%. The smallest decline, which occurred from 1889 to1896, was not preceded by excessive stock speculation. Moreover, it took place within the middle of a strongly advancing third Elliott wave that lasted from 1859 to 1929. It is remarkable that in the middle of this most powerful structure, and without stocks reaching absurd heights beforehand, the Kondratieff cycle still managed to cut an average of major stock prices in half. In 1929-1932, the Dow fell 89%. Even this substantial figure does not take into account the many company names that were flying high in 1928 but no longer existed in 1933. Figure 10 summarizes these declines. *The decline that lies immediately ahead will be in the range of these percentages*.

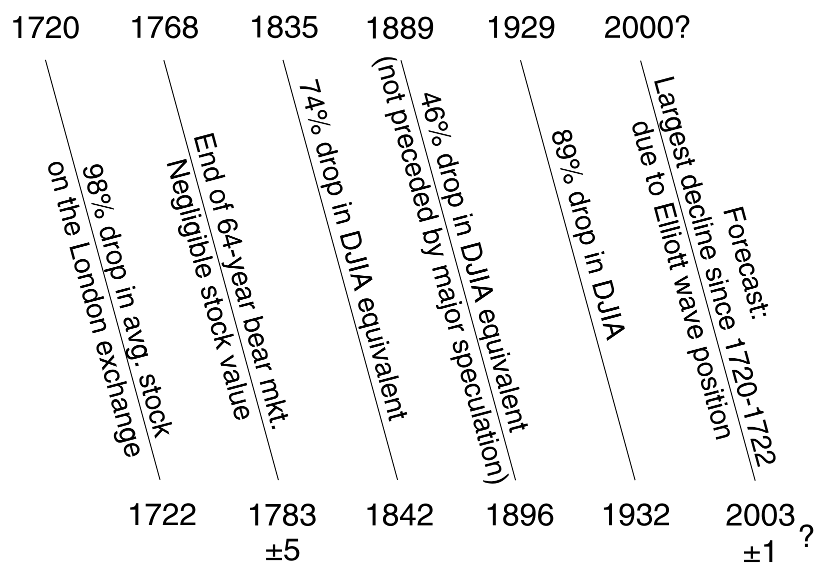

Figure 10

The last time a Grand Supercycle peaked out was in 1720. Thus, the only decline among the past four Kondratieff cycle collapses that coincided with the kickoff of a Grand Supercycle bear market was 1720-1722, the 98% wipe-out. *That is the degree of wave ending today*. The extent of the 1990s stock mania, with its legions of pricey shares of companies having no actual worth, brings us to a year that resembles none more than 1720, which ended the South Sea Bubble in England. The situation today is certainly set up to produce a similar result, as shares valued in the billions of dollars today are often of companies that not only have no earnings but persistently lose money. The number of stocks poised to go to zero is so large that the coming bear market should have little difficulty producing an experience more akin to that of 1720-1722 than to any Kondratieff cycle decline since. Figure 5-12 in *At the Crest of the Tidal Wave* presents a full picture of the forecasted Grand Supercycle as I see it.

Each Supercycle collapse and every Kondratieff cycle bottom has produced a depression in the economy. A severe depression took place in the 1720s, 1790s, 1840s, 1896-1897 and the 1930s. There is little question that the upcoming decline will have the same result.

For most people, cash will be a good friend during the coming stock price fall. However, today's market is unique in that it offers so many ways to profit from falling prices, whether via special "bear" funds, liquid derivatives or short-side portfolio management. To the speculator properly positioned, the next three to four years should offer the most profit potential in the shortest amount of time in the history of the stock market.

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