

Capital Management Associates, Inc.

Investment Management.....Financial Planning.....Estate Planning.....Tax Strategy

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December 7, 2007

CMA Update: Stocks Continue Advance Towards Year End

The stock market had a superb recovery last week on the heels of a lot of financial press "doom and gloom" about sub prime loan foreclosures, a credit crunch, weak dollar, and soaring oil prices. That was probably the "trough" or low point in market despondency about the US economic outlook. The press has been setting up consumer expectations that the seeds of a recession are already sown.

This week, a few surprises...pleasant ones...have occurred to turn the tide of investor sentiment to more positive footings. As the US FED has reduced interest rates, Canada and Britain have cut interest rates with us, which has stabilized the US dollar in foreign exchange markets...it (US\$) has even strengthened a few percent against the C\$ and Brit Pound this past week.

The US Treasury and White house have put into place an adjustable rate mortgage "rate freeze" to forestall a lot, (very many), of potential mortgage delinquency and foreclosures next year. 2008 is also an election year and I think it is safe to say that neither the Dems or Reps want any nasty downside to the US economy in 08. That being said, the Administration, Dems, Treasury and FED will work at the limit of their capacity to aid the US economy and housing sector from further deterioration, and that is Bullish for stocks. It is very bullish for financial stocks, for cyclical discretionary stocks, and for companies having US export volume and foreign income....with the US \$ currently low against most currencies.

This current interest rate easing policy of the FED has a lot more to go, perhaps bringing rates down another full percent from where they are now. The housing market has to be restarted next year, and home buyer affordability is not just the cost or price of the home...it is the cost of financing...the mortgage rate. I think the FED understands that to halt a contracting housing market and alleviate the building inventory of unsold homes, several things have to happen:

- 1) The US economy cannot contract to produce a rise in unemployment,
- 2) Mortgage rates have to become more affordable in the 5% range, under tighter or more stringent loan underwriting standards coming out,
- 3) Banks need access to more liquidity in 2008 to carry them through the mortgage loan write off period of sub prime.....banks are the only principal lenders to the US economy they will be kept financially healthy regardless of "moral hazard" issues, and

4) If banks are agreeing to the White House and Treasury sub prime rate fix, then bank funding costs...the FED Funds Rate and Discount Rate will remain low for as long as inflation stays tame.

All this said....The "Bulls are Back". The combination of the 2008 election year, FED rate cuts, weak US dollar aiding exports and US inbound tourism, sub prime adjustable rate fix, and rather huge Bearish Consensus Sentiment Index on stocks...54%...(thank you press), is setting up the stage for a big stock rally thru year end and into 2008.

We added a few new stock holdings this week, before it took off for upside on Wednesday for a near 400 point DOW run thru Friday's close. The market sold off GE to below \$37, DELL to \$24, EMC TO \$19, and Walgreens to \$36, which were near 2-4 year lows...and we bought them well. I really like GE and DELL here because of the huge foreign market business positions they have. WAG is a great stock to hold anytime for the long term, especially now as it is down at a 4 year low.

We replenished our position in Amgen, after it sold down \$3 making it a very attractive price to hold AMGN now...it is the largest biotech company and has 18% foreign sales. We increased investment positions in every holding a little, if the stock price was moving up with the market this week. This included: BRCM, DRE, JOE, ALK, COH, EL, GLW, JPM, LLY, MMM, SHO, AHT, BAC, LHO, AVP, BCS. Holdings that were not moving up or have relatively low foreign sales revenue were cut or eliminated. These include: BGP, ALL, HR, L XK, MOT, JCP, KSS.

If you have any questions about your portfolios or about the stocks we are holding, please call Chuck Dushek or Greg Nickum at CMA.

Sincerely,

Chuck Dushek