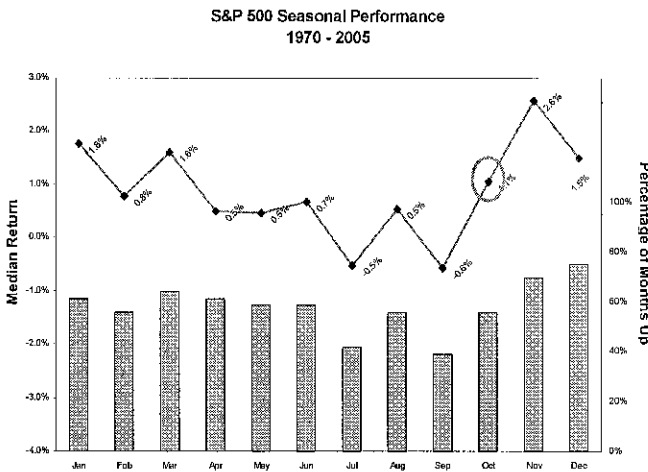


October

October ranks as the year's fifth best month and is the most volatile when measured by standard deviation of returns and monthly high/low range. This risk can be attributed to the severe declines that occurred during Octobers in 1929, 1987, and 1997, as well as the brutal declines of the mid 1970s. However, October is the best month of the year during mid term election years, with an average return of 2.1%. From a historical perspective, the average and median return for the month of October since 1970 is 0.9% and 1.1% respectively on the S&P 500.

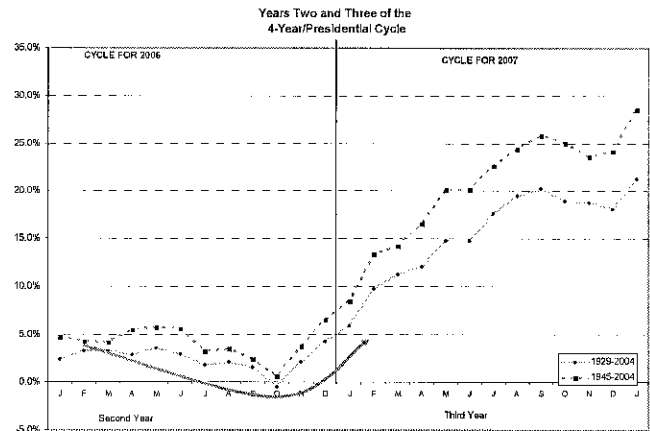
S&P 500 Seasonal Performance: 1970-2005



Source: Lehman Brothers, Factset

As of the close on September 28th, the S&P 500 is up 2.6% for the month. This is the best September since 1998. To see if strength from September can translate into further gains in October, we segmented and examined the monthly returns. When September returns are positive, October has a 59% probability of being up with median returns of 0.7%. However, when September returns are negative, October has even a better chance of doing well. The median return increases to 1.2%, with a 64% probability of being up.

Four Year Presidential Cycle: Years Two and Three



Source: Lehman Brothers, Factset

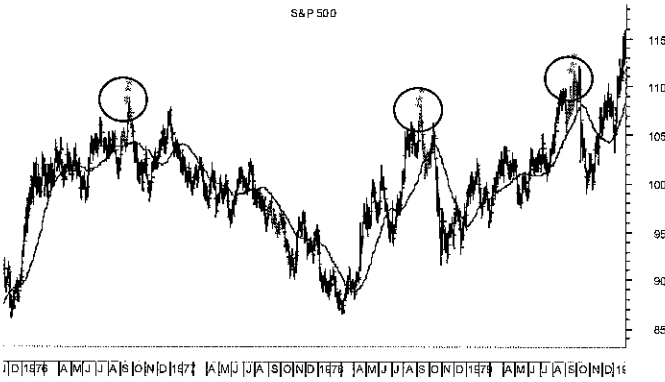
This year, the market broke out during the month of September, a month that historically performs poorly. To see the implications of September breakouts, we ran a trading system that went long the S&P 500 when the index made a yearly high (250 trading days), and closed the position 65 trading days later. We found the best month to buy a yearly high is January, followed by November and December. The bottom three months are August, July, and May. September ranks as the 9th best month to follow this strategy, and works 72% of the time. An important note is September's statistics has some underlining information that implies one should avoid chasing the market higher. The drawdown or the pain one needs to sit through is the worst of all the twelve months. Also, the average win to loss ratio is the lowest of the 12 months. However, October has the best average gain to loss ratio and ranks as the fourth best month to follow this strategy. The main take away from this exercise is to avoid a potential bull trap set in September and wait for further confirmation.

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Investors should consider this report as only a single factor in making their investment decision.

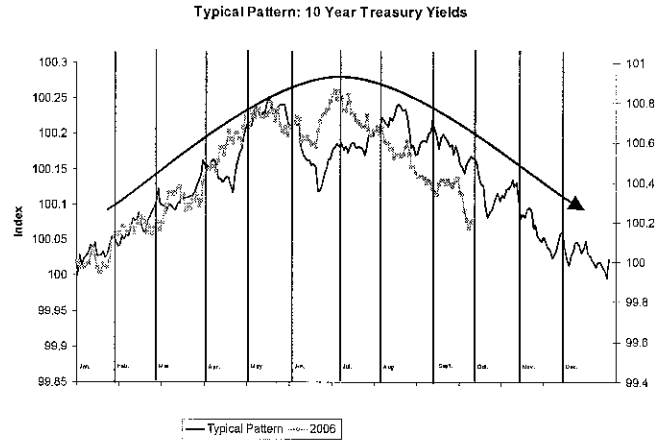
PLEASE SEE ANALYST(S) CERTIFICATION(S) AND IMPORTANT DISCLOSURES ON PAGE 7

Historical Perspective S&P 500: Examples of Failed September Breakouts ('76, '78, & '79)

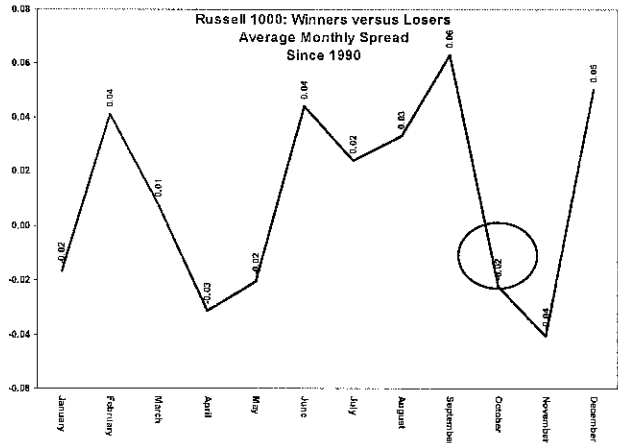


Source: Lehman Brothers, Metastock

Daily Trading Patterns: 10 Year Treasury Yield



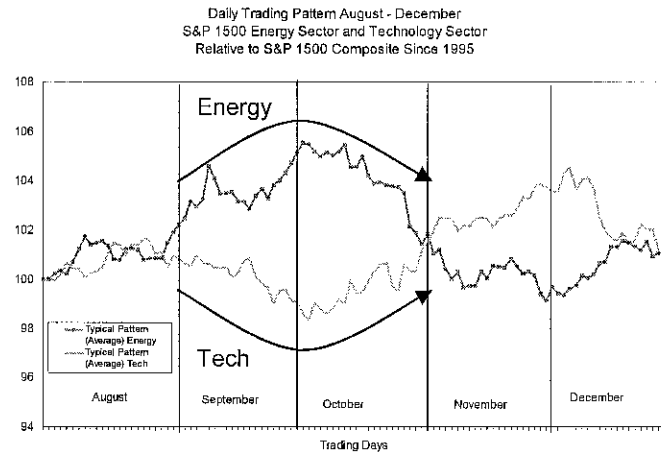
Winners vs. Losers



Winners: top decile measured by rolling twelve month return.
Losers: bottom decile measured by rolling twelve month return.
Source: Lehman Brothers, Factset, Clarifi Modelstation

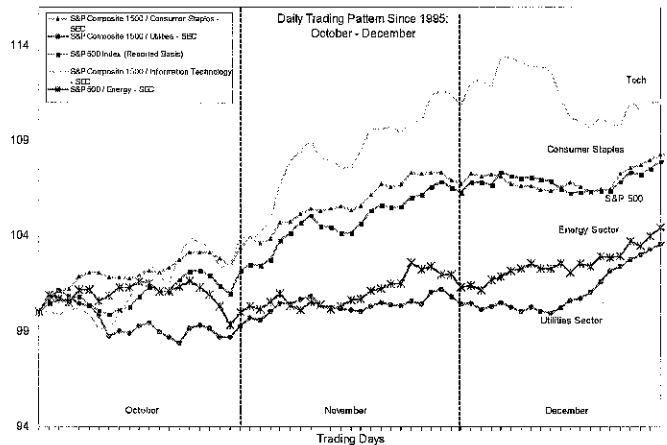
Last month we suggested rotating into oversold, neglected Technology names and out of the over-owned Energy stocks. Seasonally this is still valid. In addition, this time of year begins the strongest three month seasonal patch for the majority of the sectors. Energy and Utilities are the worst performing sectors for the month of October as well as for the next three months, while Technology is the top performer. Consumer Discretionary ranks as the third best sector for the next three months and within this sector the seasonal pattern for retail is favorable. Retail, as measured by the S&P 1500 Retail Industry Group, outperforms the S&P 1500 during the next three months, with the November being the seasonal sweet spot.

Daily Trading Patterns: Technology and Energy



Source: Lehman Brothers, Factset

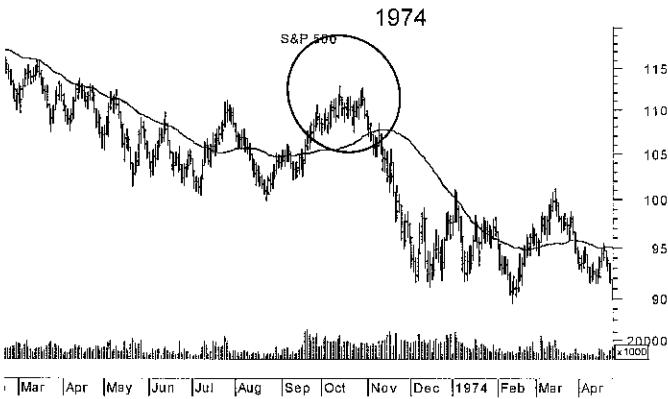
Daily Trading Patterns: Next Three Months



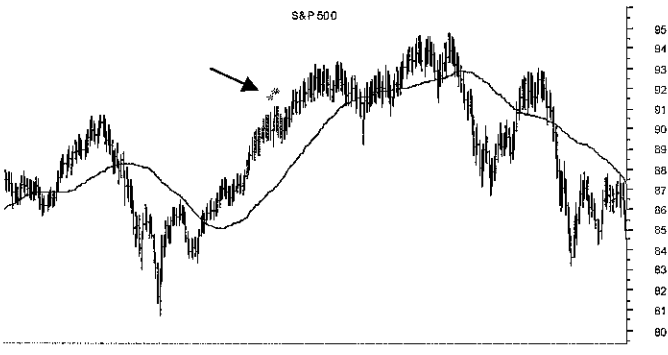
Source: Lehman Brothers, Factset

Treasury Yields are following their typical seasonal pattern this year: rising yields for the first half of, followed by a decline during the second half. The annual small cap/large cap cycle begins to see the large cap relative outperformance slow during October and November and clearly favors small caps once again starting in January. Twelve month momentum losers outperform 12 month momentum winners in October and November.

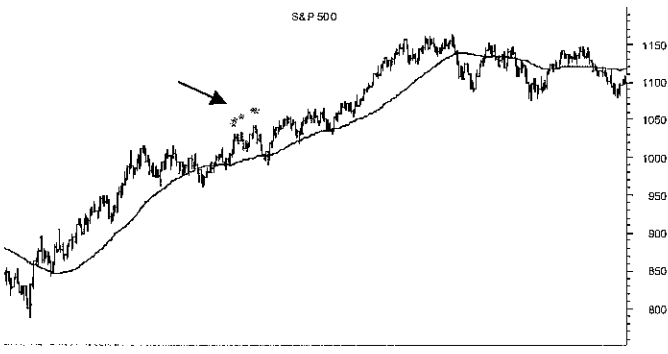
Historical Perspective: Best October Since 1970



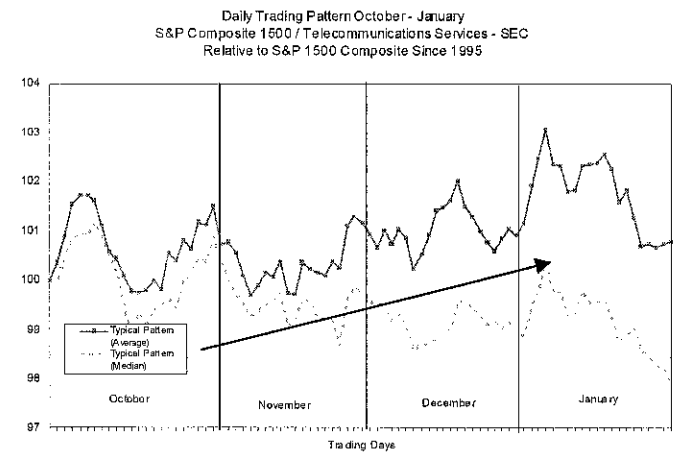
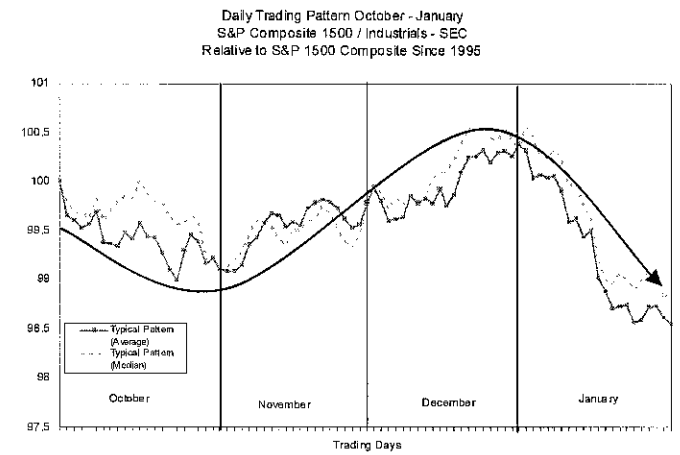
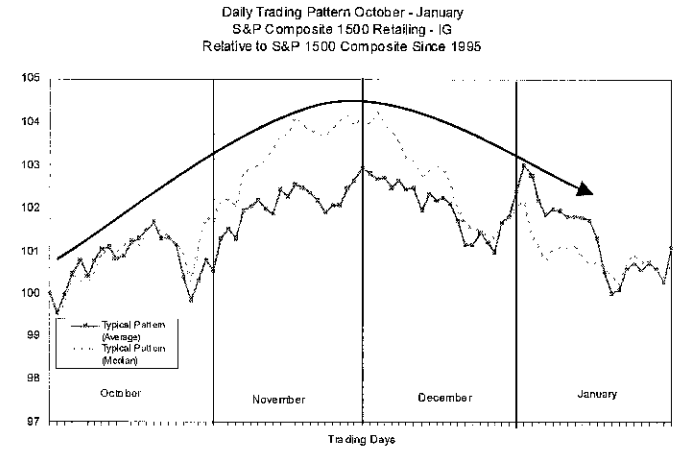
Historical Perspective S&P 500: Example of Successful Yearly High in September (1965).



Historical Perspective S&P 500: The Last Time the S&P 500 Made a Yearly High in September (2003)

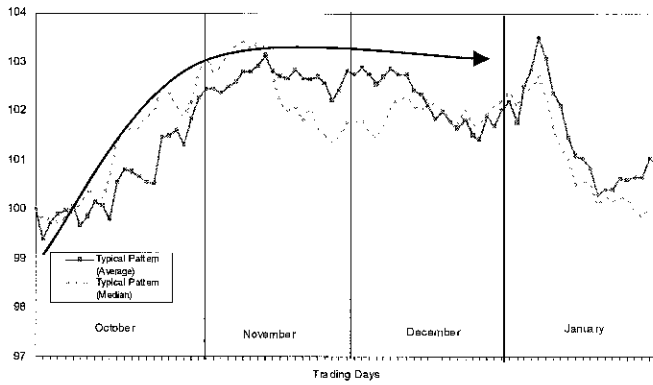


Group Highlights:

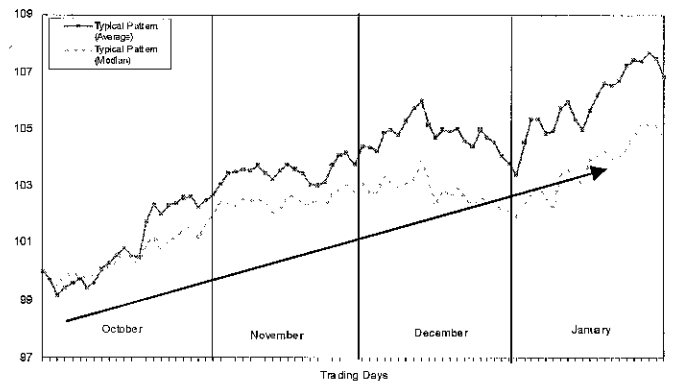


Source: Lehman Brothers, Factset

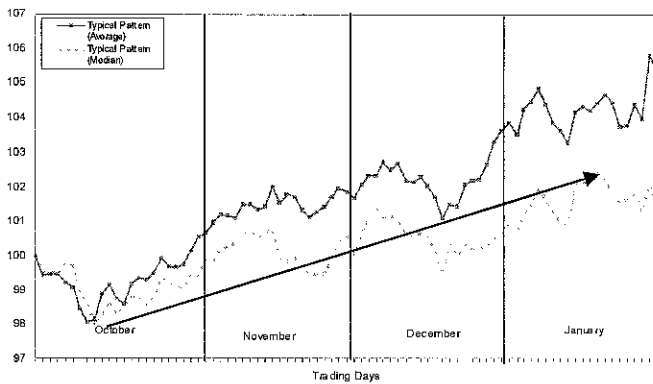
Daily Trading Pattern October - January
S&P Composite 1500 / Transportation - IG
Relative to S&P 1500 Composite Since 1995



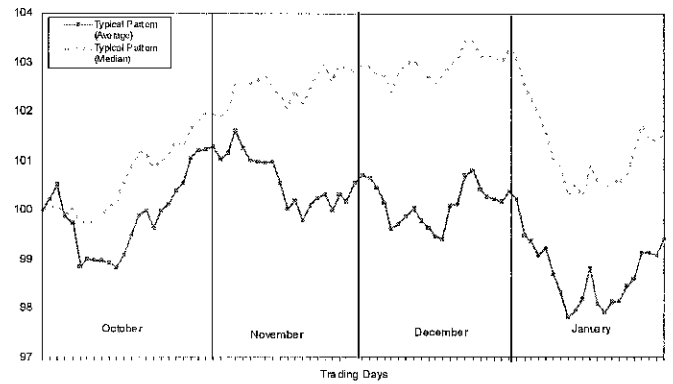
Daily Trading Pattern October - January
S&P Composite 1500 / Software & Services - IG
Relative to S&P 1500 Composite Since 1995



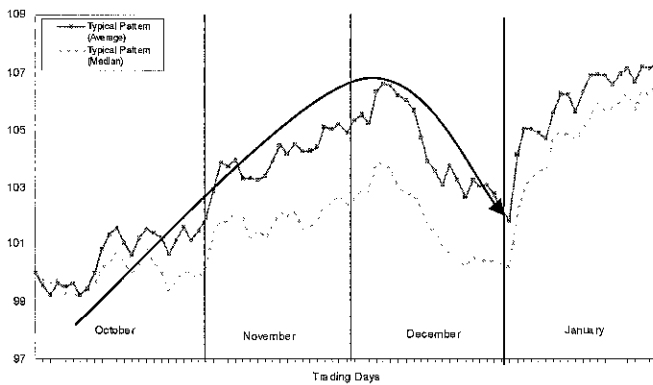
Daily Trading Pattern October - January
S&P Composite 1500 / Hotels, Resorts & Cruiselines - SUB
Relative to S&P 1500 Composite Since 1995



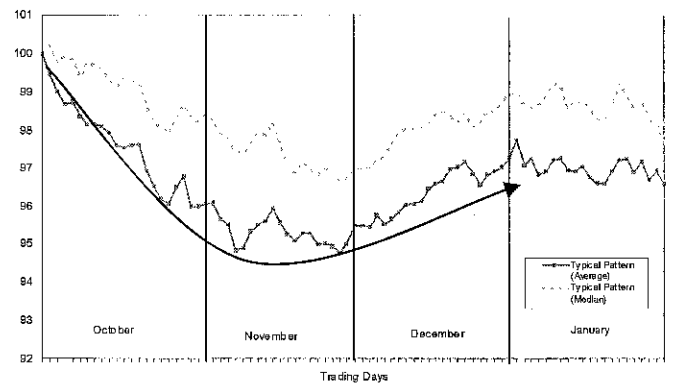
Daily Trading Pattern October - January
S&P Composite 1500 / Commercial Banks - IND
Relative to S&P 1500 Composite Since 1995



Daily Trading Pattern October - January
S&P Composite 1500 / Technology Hardware & Equipment - IG
Relative to S&P 1500 Composite Since 1995



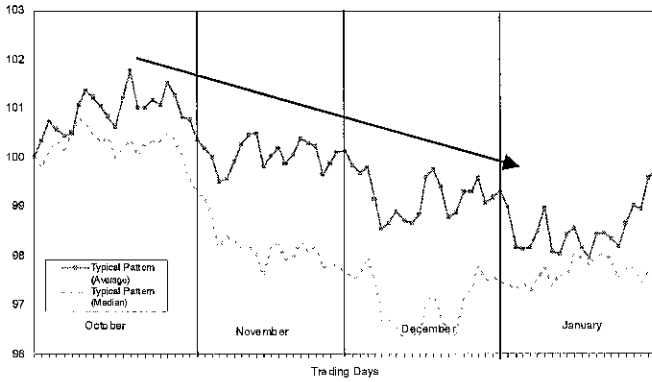
Daily Trading Pattern October - January
MSCI US REIT Index
Relative to S&P 1500 Composite Since 1995



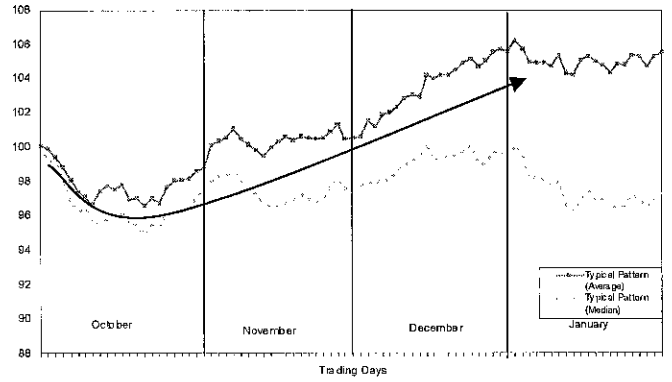
Source: Lehman Brothers, Factset

Source: Lehman Brothers, Factset

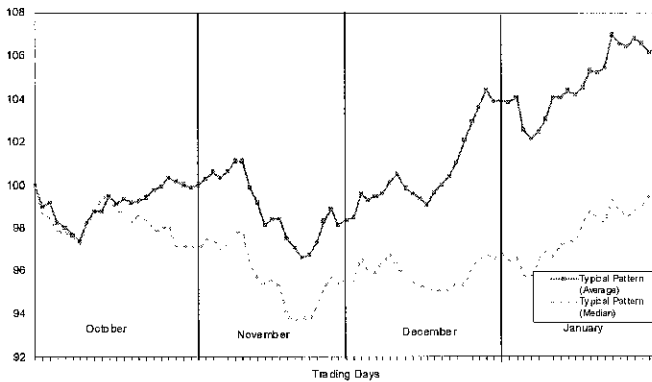
Daily Trading Pattern October - January
S&P Composite 1500 / Pharmaceuticals - IND
Relative to S&P 1500 Composite Since 1995



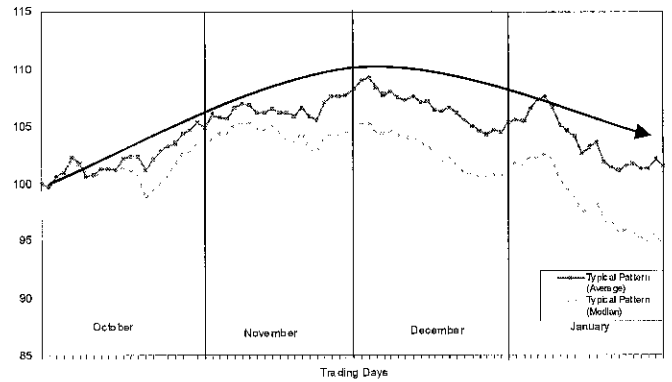
Daily Trading Pattern October - January
S&P Composite 1500 / Homebuilding - SUB
Relative to S&P 1500 Composite Since 1995



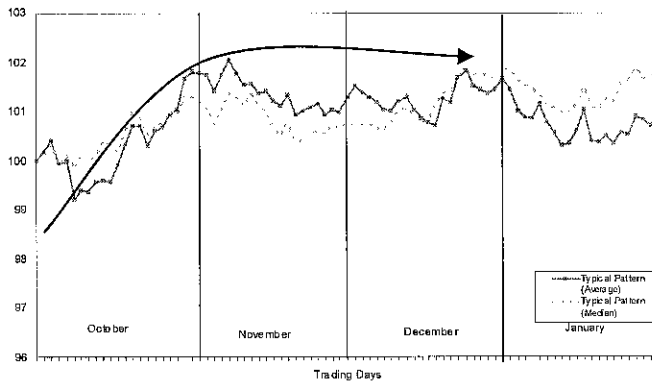
Daily Trading Pattern October - January
AMEX Biotechnology Index
Relative to S&P 1500 Composite Since 1995



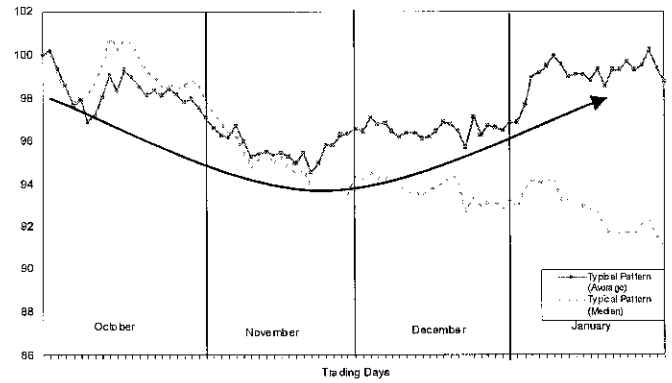
Daily Trading Pattern October - January
S&P Composite 1500 / Airlines - IND
Relative to S&P 1500 Composite Since 1995



Daily Trading Pattern October - January
S&P Composite 1500 / Financials - SEC
Relative to S&P 1500 Composite Since 1995



Daily Trading Pattern October - January
S&P Composite 1500 / Automobile Manufacturers - SUB
Relative to S&P 1500 Composite Since 1995



Source: Lehman Brothers, Factset

Source: Lehman Brothers, Factset

Seasonal ETF Recommendations:

Long: XLK, SWH, XLP, XLF, PPH, IWN,

Short: XLE, OIH, PXE, XLU, XLB, XME

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