Fourth Quarter 2007
Yearend Comments

THE MARKET

The overall market finished poorly in the 4th quarter 2007 as illustrated by a 3.3% drop (as adjusted for dividend reinvestment) in the S&P 500 and 4% drop in the Dow Jones Industrial Average. For full year 2007, the S&P 500 rose by 5.4% (including the effects of dividends) and the Dow by 6.6%. Since mid-year and even while the senior averages (DOW and S&P 500) where making or approaching all-time highs, the market internals were steadily deteriorating. For example, the number of operating companies making new 52-week highs have shown a pattern of decline from each major rally peak – 428 new highs at the February 28th top, 276 new highs at the July 19th top, and 151 new highs at the October 9th top. I find it noteworthy that since early October, new 52 weeks lows have consistently exceeded new highs. Additionally, the "operating-companies-only" advance-decline line still sits below late March levels, another sign of a market becoming increasingly selective and loosing momentum.

In recognition of waning market momentum, the fourth quarter strategy has been to reduce risk, build cash positions and emphasize investments with high yield. For example, the riskiest position owned during the year, the non-dividend paying Profunds Biotechnology special purpose mutual fund was profitably liquidated by mid-November and diverted to the Fidelity money market fund for the time being. This volatile fund has since dropped nearly 15% from top tic. On the other hand, positions in ultra-high yield stocks and exchange-traded-funds, the Nuveen Multi-Strategy Income and Growth Fund and Blackrock Enhanced Dividend Achievers have been initiated as unfavorable market conditions of the 4th quarter drove the price of these securities down to more than 10% below "net-asset-value", while their annualized dividend yields have risen to in excess of 10%.

Declining markets create excellent opportunities if the investor is positioned properly and alert to the opportunities. I think the current market environment is no exception, as I would expect the monetary easing cycle currently being implemented by the Federal Reserve Board to eventually take hold at some point in 2008. But I also think that "eventually" is not going to arrive until market sentiment deteriorates from current bullishness and the market works its way into an extreme oversold condition, not present at this time. Therefore, it is more likely than not that the next "high-odds" buying opportunity will present itself sometime during the 1st quarter of 2008 at a level below the bottom of the current trading range – that level being 12,700 on the Dow Jones Industrial Average and 1,420 on the S&P 500, with sharp intervening rallying attempts not withstanding. So, patience is a virtue at this time. Meanwhile, income yield in clients' accounts through the ownership of high-yield securities and from the implementation of call writing programs currently is at an all-time high.

STOCK SPECIFICS.

The 50% club – those stocks that I believe have the greatest appreciation potential in the next 18 months:

TIBCO Software – this company provides services that large companies must have, there is no alternative option if they want to compete in the global economy – enterprise software applications that make their businesses run more efficiently. Sales growth accelerated in the 4th quarter 2007 and sales have increased by 118% since 2003. Profits for Q4 also reached a record. Cash flow is 40% higher than reported net profits due to the write-off of non-cash expenses, and has been used to buy-back more than 12% of outstanding shares during 2007. The company competes directly with BEA Systems, (a larger but similar software provider) that was subject of a takeover offer by Oracle Systems during the year, but the deal was rejected by BEA management as being too low. A comparative analysis of TIBCO indicates a potential takeover value to be in excess of $11 per share for this $8 stock. I think the stock could easily trade higher than $11/share if fundamentals continue in accelerate. But for the time being, it's a good Company in a temporarily less-than-inspiring market environment that will likely give us ample opportunity to add to position sizes. I love this stock – can you tell?

Canadian Income Trusts – this is a simple mathematical calculation for many of the energy trusts. For example, take Harvest Energy (as Henny Youngman would say, please….) which currently yields an eye-popping 16.5% that is adequately covered by current income levels. So in a year-and-a half, at today's price of $20.75 per share, you pick up 24% just on the dividend alone. And then at some point with the refining operation set to run full out until at least the end of 2008 (the operation was partially shutdown in Oct./Nov. 2007 for periodic maintenance and negatively affected operating performance for a couple of months), and with 350 natural gas well sites identified and ready to be drilled at the first sign of a resurgence of currently lethargic natural gas prices, the stock should rally back up to its 2007 price peak of $33/share, for a move of 57%, in addition to the juicy dividend yield. This group was beaten down in December 2007, likely due to year-end tax selling and a generally weak stock market. A sharp bounce in the early part of 2008, as tax selling is no longer a factor, wouldn't surprise me in the least!

Time Warner – Fundamentals have been and are projected to continue to be excellent for this multi-faceted company with cash flows nearly double that of reported earnings. The company has aggressively bought back shares in recent years and promises to continue to do so, although a move to $24 per share (the 50% threshold) will require some catalyst(s) – perhaps spin-offs of some of its divisions (AOL, to be precise) and a generally healthier market environment. But the stock price remains fundamentally on the bargain counter.

Companies that will benefit from lower interest rates and a steep yield curve (ie. the gap between short-term and long-term yields), and Federal Reserve Board's in-process operation of monetary easing – banks, economically sensitive companies, possibly homebuilders (gulp, if my nervous system can stand it!).

MISCELLANEOUS COMMENTS

I think the sub-prime mess will be worked out in due time, but there could be some negative surprises along the way that could affect market sentiment. Possibly a surprise chapter 11 bankruptcy announcement of a major institution, hedge fund blowup, or other similar event. It could ultimately be that the announcement of that negative event paves the way for the market bottom that I referred to above…….With Citigroup being bailed out by a $6 billion dollar foreign investor at an interest rate of 11% puts that once great company is now in the class of sub-prime itself! …… I think the move in foreign markets is due for a reversal in the next few months. Chart patterns in the Shanghai, S. Korean, Indian, and Hong Kong indices indicate in-process downside reversals after parabolic run-ups and I would be extremely careful of bottom-fishing in this overcrowded trade. Looks dangerous to me…… I am looking forward to the launch of a website for **21ST CENTURY** sometime in the next few months. It is currently under construction…….I invite all clients to review **21ST CENTURY'S** most recent disclosure form ADV – Part II. Please call the office and I would be happy to send you an updated copy.

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21ST CENTURY EQUITY ADVISORS CORPORATION
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