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Global Strategy and Investment Trends by David Fuller www.fullermoney.com

Please note: This is a compilation of Comment of the Day for Subscribers, which appeared on the www.fullermoney.com website during the last week. Subscribers are encouraged to login at their convenience, to read the daily coverage and use the many other site facilities, including the Library of charts.

Monday 4th February 2008

Insider Buys Exceed Sales, Signalling Market Bottom - This is an informative article by Michael Tsang and Alexis Xydias for Bloomberg. Here is the opening:

August Busch III, an AT&T Inc. board member since 1980, bought $2.27 million of shares in the biggest U.S. phone company last month, his largest purchase on record. Monsanto Co. director William Parfet added to his holdings in the world's No. 1 seed producer for the first time in eight years.

Chief executive officers, directors and other senior officials in corporate America are buying more of their companies' shares than they're selling for the first time since 1995, prompting growing confidence the stock market is poised to rally for the rest of the year.

The last seven times insiders bought more than they sold, between 1988 and 1995, the Standard & Poor's 500 Index rallied an average 21 percent in the following 12 months, according to data compiled by the Washington Service. The purchases show executives believe the worst may be over after stocks suffered the biggest January drop in 18 years on signs the economy is in a recession.

``If it's so bad, how come these guys are gobbling up their own companies' stock? That's the telltale indicator,'' said Fritz Meyer, 57, the Denver-based senior market strategist at AIM Advisors Inc., which manages about $166 billion. ``Companies are in the best possible position to assess the economic outlook.''

My view - This is in line with what I observed and commented on during the Davos bun fight. Economists sounded as if they were auditioning for parts in the next Hollywood splat film. They all work in banks, where the black of art of deception is perfected, to the point of destruction every 15 years or so.

In contrast, the CEOs were bubbling with enthusiasm. And why not, we might ask, with those severance packages. Some may be partying on the Titanic, but in full knowledge that a private lifeboat with all mod cons awaits them.

What about the recent insider buying as an indicator for the US stock market?

It can only be a positive sign, although I doubt anyone knows the depth of conviction among most CEOs regarding current share valuations and future prospects for the companies they manage. One often needs to deconstruct data, in terms of cause and effect, and while the Bloomberg article cites an impressive track record for insider buying, the converse is apparently not so accurate.

For instance, I can remember people doubting the excellent global bull trend from 2003 - 2006, particularly in the earlier stages, on the basis that corporate insiders were selling throughout. I can only guess as to why - perhaps they were exercising share options and then selling to raise cash, and they may have been more cautious because of the previous recession.

In contrast, while many people feel that the US is actually in recession today, until or unless this is confirmed by lagging data, the global economy is still synchronised in a period of GDP expansion, albeit at a somewhat slower pace than in 2006.

The Bloomberg article also included this eyebrow-raising statistic: "The amount of short selling -- when traders sell borrowed shares expecting to buy them back after prices fall -- grew to 3.7 percent of the total shares on the NYSE last month, the highest since at least 1931." That is reason enough for a sharp rally following the selling climax on 22nd January. (*See also my comments in response to Email of the day (1) below*.)

Email of the day (1) - On Richard Russell's latest market call:

"Thought you might be interested in Richard Russell's Dow Theory Letter from yesterday. I remember noting that Richard declared the start of the primary bear market early (and correctly) and now is declaring (early again) the end based mostly on the action in the Dow Transportation Index. Also the tax implications of losses from the fed package for companies and specifically the US banking sector is very good news for their recovery."

My comment - Richard Russell is justifiably revered for his experience, market views and philosophical ruminations. Here is a valuable rumination:

"Life is a strange and mysterious adventure. Back in the '50s I spent four years in classical psychoanalysis. It cost me all my money, but it was worth it. The last thing the good doc told me (at least the last thing I remember) was -- "Richard, don't look for the land of milk and honey. It doesn't exist. You must face the fact that life is a struggle."

"He got that right. Because if you think life is a picnic, I'm afraid you're living on the wrong planet. So I've learned this -- you better learn to enjoy the struggle, because if you can't, life for you is going to be one long pain in the rear end."

I had 3.5 years of Jungian analysis in my early to mid-40s. I regard it as one of the best investments in my life to date. It helped me to save and develop a wonderful marriage, improved my other family relationships and gave me behavioural insights that have contributed considerably to my market analysis. That is why I have often said at TCS: "Treat yourself to therapy."

Here is Richard Russell on the US stock market:

"January 31, 2008 -- The cover of the new (Feb. 4) Newsweek magazine blared out in large letters -- "Road to Recession." Really, let's turn to the magazine cover "rule" -- when an item becomes so widely accepted that it makes the cover of a national magazine, the odds are that the item is either not going to happen or it's over.

"Russell Translation -- There ain't goin' to be no stinkin' recession. The magazine (contrary reading) says so, the stock market says so, Richard Russell says so.

(Bloomberg) -- Subprime lenders, homebuilders and banks stand to benefit from a $14.4 billion tax break passed yesterday by a Senate committee as part of an economic stimulus package.

A provision in the bill adopted by the Finance Committee would allow businesses to use operating losses they have in 2007 and 2008 to claim a refund of taxes paid in any of the previous five years. Without the legislation, companies would have to wait years to apply those losses against future profits. Banks, which have posted $145 billion in writedowns and credit losses tied to the falling value of mortgage securities since the subprime crisis began, stand to be among the provision's biggest beneficiaries.

"Russell Comment -- Day by day in every way, things are getting better. Russell, who told you that? The stock market told me that, specifically, the action of the Transportation Average told me that.

"Let's see, the Dow ended December 31, 2007 at 13264.82. I'm writing this Thursday at the close, but it's already certain that the Dow and the market will be down for the month of January. Is that a bad omen? Well, according to ancient Wall Street "wisdom," if the market is down for the month of January it will be down for the entire year. Personally, I don't base my investing on formulas. They've proven wrong too often. For instance, the period from November to April is supposed to be the favorable six months of every year. So far, that period hasn't been very favorable. And years ending in "8" are supposed to be good years. But that clashes with this year's down-January. The odds are that one or the other of these formulas will be proven wrong. I'm betting that the January "formula" will be wrong. I'm betting 2008 will be a fair to good year.

"Oh well, we better just watch the market action as usual, and forget about mechanical formulas. Like the cycles, the formulas work -- until they don't work. It's those exceptions that can kill you."

There are a number of interesting points here, starting with Transports which RR mentions above. Note the dramatic upside weekly key reversal following the low on 22nd January, plus last week's strong upside follow through. This action ensured a failed break beneath the August low and also several other lows that you can see on the chart, as Transports pushed back up into the trading band which began to form in 2006.

RR also mentions banks:

"Where would our economy be without our beloved banks? All during 2007 it looked as though the banks were going to go out of business along with the homebuilders. But no, the P&F chart below shows the Bank Index hitting a low at the 75 box. The Index turned bullish when the first column of Xs rallied to the 87 box. The latest column of Xs is clear breakout above all the bearish red trendlines. The upside "count" is 121. Forget about the failing banks. The P&F chart says the banks are not a worry -- they're a buy."

At Fullermoney, we have long regarded banks as a key leading indicator, so note the dramatic slump, weekly key reversal at the low and strong upside follow through last week. This is a dramatic ending signal, created by short selling, panic selling by longs and short covering following the low on the 22nd. It is a V-bottom ending which I believe will be followed by right-hand extension base formation development - the Type 1 (acceleration), 2 (extreme reaction against the prevailing trend) and 3 (right-hand ranging extension) reversal characteristics - as taught at The Chart Seminar. RR mentioned his p&f chart for banks. Here is one on a 4-point scale to show more back history and you can customise the sale in the Library, if you wish.

I will also show the Dow Jones Utilities Index on this 5-year weekly chart, which as you can see has not broken its August low. In my view it is not much of a bear market if Utilities do not break down. For instance, look at what happened to this Index in the 2000-2002 bear market, shown on this 10-year monthly chart.

You can expect to hear every possible market view so I will summarise mine, once again. A selling climax occurred on 22nd January. That indicated a low of at least near-term significance. The subsequent rally suggests that it was probably at least a medium-term low, defined at Fullermoney as lasting anywhere from several weeks to a couple of years, and occasionally longer.

The template for a medium to longer-term recovery will be a successful test of last month's lows. This means that most indices must hold above their January lows, to confirm that markets have bottomed. It does not necessarily mean that indices will retest those lows - the strongest should remain well above levels seen on 22nd January or thereabouts.

What we require in terms of confirming bullish evidence, is higher reaction lows followed by higher rally highs, defining uptrends and breaking the recent downtrends. If stock market indices cannot do this, and instead fall back through last month's lows, then the bears would be back in charge.

Even if the bullish recovery scenario prevails, which following last month's selling climax I will give the benefit of the doubt unless subsequent events prove otherwise, not all markets will recover at the same speed. Confidence has been damaged in some markets and sectors more than others, and corporate profits will be similarly affected. Even in a generally benign environment, this would lead to extended ranging for some markets.

Having frequently described the USA as the epicentre of global economic risk, I should also point out positive fundamental developments, in addition to the Fed's rate cuts last month. The bipartisan stimulus package should help sentiment. The most important part of the stimulus is not the populist issuing of checks to lower wage earners. Instead, it is the provision in the bill adopted by the Finance Committee, allowing US businesses to offset 2007 and 2008 operating losses against corporate taxes paid in the previous five years. There is a paragraph from Bloomberg on this in RR's copy above.

As always, price charts will reveal the market's leaders and laggards. Meanwhile, an often mentioned contention at this service is that Fullermoney secular themes such as emerging Asia, resources and global infrastructure plays would be among the upside leaders more often than not. There is some evidence of this already, although these are early days following the selling climax.

Industrial mining shares such as Rio Tinto and BHP Billiton are examples. Today, among my personal top-10 investments, I suspect that the Atlantis China Fortune Fund (weekly & daily) offers some of the best recovery scope, following what I suspect will be its first higher low since the November peak. I am not adding money to my pensions-type investment portfolio, as you may recall, and am content to leave my main cash holding on deposit in New Zealand dollars where it currently earns 8.2%. However if I could open a spread-bet long in this Atlantis fund, as I did with Rio a couple of weeks ago, I would do so today.

Importantly, after deliberately deflating its bubbly stock market in a gradual process commencing last October, China appears content with current levels and is allowing new closed-end funds once again (*see Eoin's coverage of this subject, including an important report, below*). Today's big upward dynamic for China's mainland indices - apparently the best single-day percentage move since June 2005 - most likely signals that the correction is over.

Bush Boosts Defense Spending in $3.1 Trillion Budget - Here is the opening from Bloomberg's report by Roger Runningen and Brian Faler:

President George W. Bush sent Congress a $3.1 trillion federal budget for next year that trims Medicare and health care programs, boosts military spending and projects this year's deficit will hit a near-record $410 billion, reflecting the weakened U.S. economy.

The spending blueprint is the biggest ever of his presidency. It would slow the growth rate of spending for entitlement programs such as Medicare by $208 billion over five years. Pentagon spending would rise 7.5 percent to $515 billion, the 11th consecutive year of increases. Programs in the departments of education, interior, transportation, justice and agriculture would be reduced.

The election-year budget is certain to touch off a partisan clash over priorities, spending levels, tax cuts and the deficit. With Democrats controlling both the House and Senate and the political campaign to succeed him fully engaged, Bush's budget stands little chance of being adopted as proposed.

``People will want to get the minimum amount done until the next president,'' said Steve Elmendorf, deputy campaign manager for Senate John Kerry's presidential bid four years ago.

The projected budget shortfall, up from $162 billion last year, reflects a slower economy generating fewer corporate tax receipts, the cost of a $146 billion economic stimulus measure and continued spending to support the wars in Iraq and Afghanistan. The deficit is forecast at $407 billion in 2009. This year's $410 billion deficit would be 2.9 percent of the $13.2 trillion U.S. economy, up from 1.2 percent last year.

My view - Needless to say this budget will not be passed by the Democrat Congress, which will try to limit the US President's programmes for the remainder of this term. However, even if the US economy commences a recovery later this year, as I suspect, and even if a Democrat wins the presidential election and cuts defence spending in 2009, as I also suspect, the next government will find it very difficult to reduce its spending deficit. This is another reason why talk of a US dollar recovery is premature.

Email of the day (2) - On oil, Schlimberger and Halliburton:

"Have attached an interesting article on the peak oil story. I would also recommend listening to the Jan 8th Schlumberger conference call particularly the Q&A with CEO Andrew Gould and his assessment of the market...One of the SLB business lines growing right now is IPM where they offer oil companies complete integrated project management services levering the complete line of technology solutions that SLB offer for drilling and production. As a result of the political situation in Mexico the state doesn't leave any CAPEX for PEMEX to invest in exploration and production and guess who is stepping into that role? Privatization is taboo but working with a resources rich integrated service provider such as SLB or Halliburton is a politically more acceptable alternative and one that is starting to grow. Same thing with the resource restricted state oil company in Ecuador and not to forget Venezuela with some of the largest reserves in the world. PDVSA the Venezuelan state oil company lost 20,000 key technical and management personnel during the strike so they have limited capability to raise production at a time when the Venezuelan coffers are being emptied by the Chavez government on state social projects, not to mention the drop in production levels over the last few years. Interestingly, SLB have set up a Heavy Oil centre of technical excellence in East Venezuela close to the Orinoco heavy oil belt.

"If the Bolivarian revolution (another fools paradise?) is to survive the forthcoming economic storm stoked up by excessive state spending and price controls on private industry Chavez may need to sit down with the likes of SLB in order to get crude production levels back to where they were before he fired all his best engineers/managers and kicked out the International Oil Companies."

My comment - Thanks for an interesting email and article.

It is all but a universal truth that productivity, including oil production, falls following nationalisation.

I do not doubt that Chavez needs Schlumberger but suspect that calling for help from an American company would be a bitter pill for him to swallow. Meanwhile the share peaked with a dramatic weekly key reversal in October and took another big hit last month, before steadying above probable support from the 2006 to early-2007 range. Halliburton remains rangebound but is rallying from the lower side of that pattern. Both remain world-class companies but in the global beauty contest, there is nothing irresistible about their chart patterns.

The article is also interesting and at Fullermoney we pay attention to Matt Simmons but maintain that crude oil is experiencing a medium-term consolidation within its long-term uptrend.

My personal portfolio: Silver long trade partially reopened - I bought a little silver today, paying $16.515, including spread-bet dealing costs, for a March position.

Additional Commentary by Eoin Treacy

JP Morgan China: Insights and Strategy Views from the Bund - Thanks to a subscriber for this blockbuster 158 page report which looks at a number of different sectors in China. Here is a section:

China's December CPI inflation rate eased modestly as expected, to 6.5%oya, from the 11-year high of 6.9%oya reported in November. A higher base effect has started to kick in and food prices, while still climbing, are beginning to show slower increases. Seasonally adjusted, the CPI rose 0.4%m/m, sa, down from 0.7% in November. Through the monthly volatility, the sequential trend has steadily decelerated in recent months: prices rose only 6.2%3m/3m, saar through December.

Headline CPI inflation, measured against a year earlier, has already started to peak. By 2Q08, headline (oya) CPI inflation is likely to slow toward 4-5%. By then, the authorities will be able to push forward planned reforms of the pricing mechanism for gasoline, diesel fuel, and other resource-based products. For 2008, therefore, headline CPI inflation will likely average 4.8%oya, although core CPI inflation will likely move higher from the current 1.0% level.

At the producer level, the recent rally in global energy and commodity prices pushed up December PPI inflation to 5.4%oya. The 1.1%m/m, sa gain was consistent with the uptick in industrial input prices seen in the latest PMI reports.

We expect the economy's growth pace to remain solid in 2008-albeit with some shift in composition toward domestic demand-despite continuing tightening of monetary policy, administrative curbs, and the global slowdown. We expect overall GDP growth to moderate to 10.5%y/y in 2008, from 11.4% in 2007, including modestly slower growth in the current quarter, as sluggishness in global demand continues to weigh on China's exports.

Toward mid-year, the external environment will turn more supportive as the US economy bottoms out. For full-year 2008, export growth is expected to slow to 19%y/y from 27% in 2007-and there is downside risk to this export forecast if global growth turns out worse than we expect. In that case, however, there would be an offsetting upside risk to our FAI forecasts, as the government would boost fiscal spending and infrastructure investment if global demand for Chinese products slowed too much. As for the price outlook, we have revised our full-year 2008 CPI inflation forecast up to 4.8%y/y. We expect core CPI inflation to move higher from the current 1.0%oya, given the expected further liberalization of natural resource and utility prices.

My view - Inflation has been making headlines in China over the last year and has become a political issue which has resulted in the authorities making every effort to get it under control. This has manifested itself in curbs being put on the housing market, bank reserve requirements being raised, a moratorium on new closed-end funds for the stock market, a quickening the pace of appreciation for the yuan and of course a number of interest rate hikes. When inflationary pressures level off, it will allow the authorities to consider easing their tough stance on cooling the economy, which would be a very positive signal for stock markets.

Today's news that two new closed-end funds will be launched after the New Year was a boost to sentiment which has suffered recently. It opens up an important avenue to further investment flows. I know that when we were in Beijing last June, investors were competing, to get a piece of closed-end funds because they were limited in number and demand far exceeded supply. It will be interesting to see how these new funds sell in the coming weeks as a signal of investor interest in the stock market.

Also see this story by Zhang Shidong for Bloomberg which covers the closed-end funds markets. Here is the story in full:

China's stocks rose for the first time in four days, set for the biggest gain in almost two weeks, on expectation the government will take measures to stem recent declines in the nation's two bourses. Shanghai Pudong Development Bank Co. led the advance.

The CSI 300 Index, which tracks yuan-denominated A shares listed on

China's two exchanges, climbed 232.38, or 5.1 percent, to 4,804.33 as of 9:55 a.m. local time. No stock among the index's 300 members fell today, with 284 up and 16 unchanged. The measure has dropped 22 percent from its Oct. 16 peak through Feb. 1.

Pudong Bank, the Chinese partner of Citigroup Inc., jumped 2.77 yuan, or 5.9 percent, to 50. Citic Securities Co., China's biggest publicly traded brokerage, rose 2.70 yuan, or 3.9 percent, to 72.01. Baoshan Iron & Steel Co., China's biggest steelmaker, advanced 0.75 yuan, or 4.8 percent, to 16.42.

China's stock regulator approved two new stock funds, ending a five-month freeze, the Shanghai Securities News reported on Feb. 2. CCB Principal Asset Management Co. and China Southern Fund Management Co. will start closed-end funds, raising as much as 14 billion yuan ($1.95 billion), after the Lunar New Year, the newspaper said.

Email of the day (1) - on the possibility of creating a ratio and overlay:

"Is it possible in the chart library to view inflation adjusted FTSE 100 or 250 from 1930s to present day overlaid with the dividend yield?"

My comment - Thank you for suggesting this interesting combination which we may be able to create at some point but it is not possible for the moment. There are a number of reasons for this, chief amongst them is that Bloomberg's CPI data for the UK only goes back to 1988 and the dividend yield on the FTSE 100 only to 1993. Another stumbling block is that at present we can only plot a two instrument permutation in the Chart Library and your suggestion would require three. I plotted this proxy chart on Bloomberg. If I remember correctly the custom index I created for the inflation-adjusted chart should update with more history tomorrow. If this is the case I will post the chart again. We see that dividend yields have spiked in conjunction with market corrections as one would expect.

Email of the day (2) - on Chart corrections, additions and coffee:

"I think the chart library may have an issue with Dubai, Tapis and Bonny oils as they don't appear to be updating since July 2007.

"Also is there a quoted price for Rock Phosphate that may be included in the chart library please?

"The last few weeks have been a wonderful lesson in applied Behavioural Technical Analysis from you both. Thank you.

"P.S. David mentioned during the week about it being a bit late to buy coffee (Robusta) and Cocoa. What about Arabica? The monthly chart over 20 years looks very interesting to this amateur eye especially if it got over 150. I don't have a position other than that of an avid coffee consumer worried about the cost of his morning fix."

My comment - Thank you for this interesting email and for alerting us to the oil prices which were not updating. This has now been corrected. I have also added a price for Rock Phosphate to the Chart Library.

Rock Phosphate has surged recently in line with other fertilisers. It has been ranging for much of the last 30 years and this upward break is significant. The first downward dynamic is likely to signal that a high of medium-term significance has been reached, however in the meantime the upside can be given the benefit of the doubt.

I agree that Arabica coffee is looking very interesting from a chart perspective and taken long-term it shows some of the best potential around. It is currently testing resistance near 140¢ and a downward dynamic would be needed to question potential for an upward break. Robusta has led on the upside so it may also give a timing signal when this move comes to an end. David's view and mine is that these often volatile commodities are best purchased following reactions within their uptrends

Email of the day (3) - on a water transport index:

"Can you please add the water transport index (from morningstar?), it holds all the USA listed shipping companies."

My comment - I'm afraid that the Morningstar Water Transport index is not on Bloomberg so I cannot add it to the Chart Library. This is a list of 47 US water transport and tanker companies, all of which should be in the Chart Library. I have asked Bloomberg to add the Morningstar index but they are more likely to do it if more than one person asks for it, so if any subscriber, with access to Bloomberg, is interested in seeing this index in the Chart Library, perhaps you will send Bloomberg a Help message asking for it.

Email of the day (4) - on an addition to the Chart Library:

"Thank your for your continued guidance. It is only since subscribing that I feel I have begun to understand the markets.

"A quick request: could the Rydex equal weight S&P500 ETF be added to the chart library please? I think it is a useful breadth tool. For example, the equal weight ETF broke down from its top formation before the S&P index itself."

My comment - Thank you for this inspiring email and we are delighted that you are enjoying the service. The ETF you mention has been added.

Email of the day (5) - on additions to the Chart Library:

"Could you please add JF Pacific Securities Fund and JF Pacific Smaller Companies Fund to the Chart Library?

"Thanks."

My comment - Thank you for these interesting suggestions which I have added to the Chart Library.

Last week's signups for the Free (Abbreviated) Comment of the Day - For the week of January 28th new signups, including subscribers and pre-subscribers, live in the following countries or regions: Australia, Canada, Cayman Islands, Hong Kong, Ireland, Singapore, Sweden, the UK and the USA - 9 in total. In descending order, which topped the list in terms of the last week's new signups? It was the USA, the UK and Australia.

Thousands of people around the world receive Fullermoney's Free (Abbreviated) Comment of the Day, and their numbers steadily increase. Why do so many sign up? It is primarily due to word of mouth or word of press mention, from people who like Fullermoney's global perspective and our Empowerment Through Knowledge theme. Incidentally, on receiving our free daily email, you will not be contacted or solicited with advertisements and other marketing material. No one else will have access to your email address. We respect your privacy.

Tuesday 5th February 2008

State capitalism and free markets - My thanks to a subscriber for this interesting and topical article by MK Venu, published by the Economic Times Hyderabad. Here is the introduction:

THERE is enough evidence to suggest that the years ahead could see a consolidation of state-led capitalism across many emerging markets. Commercial arms of the state in many countries are evolving as savvy players in the global market place. It may seem like a contradiction in terms, but the fact is that the state is learning the ways of the market. This would be anathema to the Anglo-Saxon model of capitalism where the state largely stays out of running businesses. This model believed that the motive of pure profit and not power must guide economic activity. However, a new model is evolving in many of the emerging economies where the motive of profit and power are going hand in hand. China, Russia and significant parts of East Asia and Latin America follow the new mix of profit and power. The Americans are worried about this, but are in some ways helpless as they are also heavily dependant on these emerging economies for cheap goods. The bulk of middle America gets cheap clothing from East and South Asia.

A recent study by a member of Japan External Trade Organisation showed that the developing economies had 69% share in the incremental growth in world output in 2006. The US and EU countries together had only 22% share in the incremental world GDP on a purchase power parity basis. China itself has 29% contribution to incremental global output, ahead of US and EU put together.

It is not hard to imagine that in the near future the bulk of the world output would come from nations which follow a different mix of state and market while competing in the global market place. Some of this is already happening before our eyes.

My view - There is nothing new about state capitalism but the difference this time is the size and number of these sovereign wealth funds, which are growing rapidly. Understandably, countries with large current account surpluses are no longer willing to leave all of their surplus capital in US Treasuries or the government bonds of other debtor countries.

I am not aware of any evidence that SWF managers are savvier than any other large investors. In fact, I suspect they are less so on average, often being less experienced and receiving funds by state decree rather than past performance. I am not even sure that the motive of profit and power is all that different, since few really wealthy investors are shy about using their power in the pursuit of profit.

However as a large thundering herd, SWFs are an increasing presence, which means that they will influence investment fashion trends. Astute investors will monitor their moves.

Email of the day (1) - More on oil production (*see also yesterday's Email of the day (2), partly reproduced in italics*) and more on CEO sentiment readings:

"If the Bolivarian revolution (another fools paradise?) is to survive the forthcoming economic storm stoked up by excessive state spending and price controls on private industry Chavez may need to sit down with the likes of SLB in order to get crude production levels back to where they were before he fired all his best engineers/managers and kicked out the International Oil Companies."

"There have been numerous variations of 'SLB' and turnkey structures that energy companies have used since the early 1980s; 'turnkey' being one aspect that has evolved into what you see at Schlumberger today. The industry evolved this in ironic response to when Britain under 'Old 'Labour' was thinking in the 1970s of nationalising the North Sea oil and gas industry pre Thatcher.

In reality, it allows countries in South America and Africa, after they are finished with their 'experimental nationalism of resources', to allow an entity like Schlumberger/ Baker Hughes /Nabors/Halliburton turnkey services under UN/World Bank/IAB capital syndicated or otherwise.

On what CEOs are doing, that is another chunk of evidence as to what industry is doing. I'm always thankful for pundits wherever they are and economists, as FM has taught us over the years to think for ourselves and just watch the charts. Have a good Tuesday."

My comment - These emails on oil remind us of the Collective's experience and depth of knowledge.

If we do not strive to think for ourselves, including reading between the lines of conventional opinion and always subjecting it to the rigorous test of factual and behavioural chart reading, our views at critical junctures will be more emotional than analytical.

Rod Smyth's The Week - Housing Glimmers: The Beginning of the End - My thanks to Rod Smyth, Bill Ryder and Ken Liu for their informative report published by Wachovia Securities. Here is the introduction:

In 2006 we argued that the housing downturn was still "only at the end of the beginning." We now believe the downturn has reached the beginning of the end. With both mortgage rates and home prices falling at the same time, housing affordability has turned upward - an essential prerequisite for a turnaround in the industry, in our opinion. Last wee we wrote that mortgage holders were being presented with an opportunity to refinance as conforming fixed rate mortgages have followed Treasury yields to four and a half year lows. We believe the Fed's reluctance to cut rates aggressively in the second half of 2007 contributed to the decline in Treasury bond yields as investors raised the odds of recession. Thus, by accident or design, the Fed's actions have led to a remedy for at least one major obstacle facing the economy: the upward payment shock or ARM (adjustable rate mortgage) resets. As mortgage holders refinance into fixed-rate mortgages from ARMs at these attractive levels, their disposable income becomes more stable which should help consumer confidence. As we wrote in our 2008 Outlook, ARM resets threaten to reduce consumption by almost half a percentage point a year. Refinancing helps mitigate this threat. Moreover, while probably too late for the subprime arena, we think mortgage refinancing lowers the risk of default and foreclosure in the rest of the housing market. Indeed, credit risk as measured by Credit Default Swaps - financial derivatives used to trade or hedge credit risk - has fallen in recent weeks (although it still remains at elevated levels).

My view - The US economy may or may not be in recession right now - it is impossible to tell due to the lagging nature of statistical data - although I do not doubt that it has felt like a recession for many people. More importantly, the Fed's more aggressive rate cutting recently is already beginning to cushion downside risk in some sectors.

Subscribers may be interested in the large graph from Ned Davis Research, showing the Housing Affordability Index.

Email of the day (2) - On bonds:

"I agree entirely with yr comments re shorting govt bonds given their current yields compared to the real inflation rates. However, are perhaps Index Linked bonds a more attractive asset class for a longer-term investment portfolio? This appears to be born out by your Standard Life Index Linked Fund chart."

My comment - Good point. However I probably know less about Indexed Linked bonds than you and many other subscribers. For instance, I do not know the extent to which yields have come down recently but suspect they are considerably reduced. Also, the capital gain of the Standard Life Investments Global Index Linked Bond Fund (SLGILIA), while impressive, is in line with price appreciation for Western government bonds recently. This raises the question: will it fall back in line with the next sell-off as recession fears eventually wane?

For the record, here is Bloomberg's paragraph on SLGILIA:

Standard Life Investments Global Index Linked Bond Fund is an open-end investment company incorporated in the United Kingdom. The aim of the Fund is to provide a consistent level of income with capital appreciation being of secondary importance. The Fund invests primarily in sovereign-issued and corporate inflation-linked debt. The Fund may also invest in government bonds.

Yang Liu of Atlantis China and China Fortune funds - She will be appearing on CNBC at 17:30 (HK), 09:30 (Ldn) on Wednesday 6th February to discuss: "How to make money in the year of the Rat."

My comment - The Atlantis China Fortune Fund, also mentioned yesterday, is the second largest position by weighting in my personal long-term investment portfolio.

Email of the day (3) - On BBG's report of tax provisions (*see also email of the day (1) yesterday*):

"After a little investigation, the provision to use operating losses from 2007 and 2008 to claim a refund of taxes paid in any of the previous five years, appears to be a dead duck. Probably for the better as there is also the law of unintended consequences with major interventions, where I believe many unrealized losses may suddenly appear in companies P & L statements for 2008 (lets clear the decks and get tax relief as well). Might not be too good for Equity prices."

My comment - Another good point. Of course the provision, if approved, would be only one of many factors influencing equity prices, but I suspect that investors would quickly realise that it was net bullish for companies. However it would also add to the US government's budget deficit, probably leading to even more printing of dollars.

Email of the day (4) - On insider services, mentioned yesterday:

"I am reasonably alert to insider services for the US, but have no clue about what goes on in the rest of the world. Any thoughts? Also, I believe you have a positive view towards industrial metals for the intermediate term? Thanks for your fine service and many nuanced thoughts............"

My comment - Thanks for your kind words.

On data such as insider buying and selling, other countries are often less forthcoming. However this is one of those times when we should be monitoring it, if possible. I would welcome feedback from investors who are know of accurate records of insider activity in other countries.

I wonder if you or any other US subscribers monitor net odd lot data? The WSJ used to publish the daily figures and perhaps the US edition still does, but it is no longer in the slimmed down European edition. Barron's is another possibility. It used to be a very good indicator for pinpointing market bottoms, something it did consistently during at least the 1960s through 1980s. However these relationships can sometimes change so I would be particularly interested in the odd lot total purchases, minus both long sales and short sales, for January 22nd and a day or two either side.

Additional Commentary by Eoin Treacy

UBS Investment Research Commodity Compass: Price upgrades for Bulks - Thanks to a subscriber for this interesting report by Daniel Brebner which focuses on price increases for bulk commodities. Here is a section on iron-ore:

Iron ore negotiations are continuing between global steel producers and the big three iron ore mining companies. We believe the mining companies are looking for a 70% increase in contract pricing while the steel makers are insisting on a 30% increase. We make the following observations:

1) The premium of the spot iron ore market above the 07 contract price (about 200%) supports the contention that markets remain very tight despite the slowdown in global growth. Positive for miners.

2) Steel prices are poised to rise on a global basis; particularly if input costs such as iron ore, coking coal and scrap increase. Steel makers have been very successful in passing these costs to customers. Positive for miners.

3) The Chinese renminbi has been strengthening, annualising about 20% in January; this should offset some of the cost increases expected. Positive for miners.

4) Domestic production of iron ore within China has been decelerating significantly; if this continues, China's reliance on imported sources of iron ore should increase. Positive for miners.

5) As negotiations continue, China is likely to feel the pressure to settle in order to prevent other parties, such as the Japanese Steel Mills, from settling first. Positive for miners.

My view - CVRD, Rio Tinto and BHP Billiton should continue to benefit enormously from tightness in the iron-ore market as they control the majority of global supply. The reasons given above are credible and we can be certain that the ongoing negotiations will result in a price rise. Just how large that increase is, will be a significant short-term determinant as to whether these companies can reassert their overall uptrends with sustained breaks to new high ground.

HSBC Commodities Global Precious Metals Outlook: Powerless to prevent production declines - Thanks to a subscriber for this 48 page report by James Steel which looks for short-term strength but a dollar rally later in the year. Here is a section:

HSBC's currency forecasts are essentially unchanged from our 27 November 2007 Metals Outlook. The team forecasts a USD/EUR exchange rate averaging 1.45 in Q1 2008 and 1.40 in Q2 2008, which implies that, on average, the EUR will weaken relative to the USD. Interestingly, they forecast the USD/EUR exchange rate will to strengthen further in H2 2008 and H1 2009, averaging 1.35 and 1.30, respectively. This would represent a considerable decline in the EUR from present levels; the last time the EUR traded around 1.30 was mid-February 2007, when gold prices were slightly above USD660/oz. Viewed another way, a USD/EUR rate of 1.30 represents a drop of a little less than 13% from current levels, which is consistent with a gold price of USD790/oz. Although there is admittedly a wide difference between both figures, they are significantly below current gold prices.

Conclusion: Does it depend on the USD?

The analysis of our macroeconomics team implies that the bullion market will be at least reasonably well bid in the near term. Further near-term rallies in gold are entirely possible if the Fed continues to pursue an aggressive rate-cutting policy as a means of solving the credit crisis and averting a possible recession in the US. Any deterioration in the credit outlook by, say, the downgrade of a large bond insurer, would likely elevate investor risk aversion and support gold. US monetary policies are further likely to ignite already heated emerging market economies, potentially keeping commodity prices elevated. These same factors may weaken an already burdened dollar, threatening to send the greenback into a full-scale rout which may threaten the global economy and strain the financial system.

We believe a turning point for gold would come should the G-8 and important emerging market economies form an accord to head off a USD rout. Should the framework for such an accord include the appropriate economic polices designed to strengthen the USD, the USD stands a good chance of rallying later in the year. If the USD manages to recover in line with HSBC's forecasts, gold is likely to come under downward pressure. In previous publications, David Bloom has suggested that the USD will rally this year, based in part on his view that the EUR is substantially overbought and well above its long term fundamental trading range. It is possible that even in the absence of a formal currency agreement the USD might rally, taking gold prices lower.

My view - Gold came under renewed selling pressure today following the key reversal on Friday in what has the appearance of a short-term reaction within the overall uptrend. In the past, when gold has been at pivotal points following an impressive rise, it has posted dramatic downward dynamics which clearly signalled the end of the medium-term move. So far, this is not one of those occasions. In fact the present reaction is above and no larger than that which occurred between early November and yearend. A sustained break below $850 would be needed to question the integrity of the overall uptrend.

As a leveraged trader, who bought at the top, the recent activity forces me to question my timing from an emotional perspective and reminds me that a rule of thumb from the last number of years still applies: don't pay up for commodities. Attempting to remain objective and looking at the bigger picture, I see that the overall trend remains intact

UBS Investment Research: EPS Upgrades: Higher Platinum Price forecast - Thanks to a subscriber for this interesting report which predicts that the recent power outages in South Africa are more than a temporary phenomenon. Here is a section:

Following the deteriorating power situation in South Africa (SA) - which we believe is primarily a structural issue, which could last for many years rather than just months - together with the increased likelihood of production delays as a result of temporary mine shafts closures due to fatalities - we have significantly lowered our estimates of platinum supply from SA by 10% in CY'08 and 8% in
CY'09.

Platinum price forecast raised to US$1,800/oz in 08 and US$2,100 in 09. We are therefore raising our platinum price forecasts significantly - by 18% in CY'08 to US$1,800/oz and by 45% in CY'09 to US$2,100/oz. We are also raising our rhodium price forecasts by 25% in CY'08 to US$7,500/oz and by 33% in CY'09 to US$6,000/oz. Our palladium price forecasts are unchanged.

My view - Platinum has a tendency to lead precious metals in both directions and this was certainly the case from August, with platinum progressively breaking upwards ahead of gold, silver and palladium. The same is true right now, following the stimulus provided by the South African power outages. However, the metal is looking overextended and a downward dynamic, which is clearly larger than those on the upside, would be needed to question momentum. Such a move would also be an indication that the present difficulties in the gold market might be more medium-term in duration.

Email of the day - on phosphate rock:

"Further on phosphates-attached is recent report from USGS. Interesting stats-note NO government stockpile(for such an important ingredient for agriculture) and NO substitute for phosphorous in agriculture.

"MOS(U.S.)obviously has garnered much attention and has moved up quite quickly-wondering whether the Fullermoney collective can add any other names that might still be worth looking into."

My comment - Thank you for this interesting report, which follows up on Email of the Day (2) yesterday. Phosphate rock is an invaluable resource for fertilizer companies and has recently gotten much more expensive following a prolonged base formation. Significantly higher levels are a possibility given the amount of time it has been basing. However this is not a tradable market and exposure is most likely to be gained through shares. If subscribers know of any which fit the bill please let us know.

Today's interesting charts - The Dollar bounced today against a number of currencies, almost all of which can be found in the Chart Library.

USD Dollar per 1 Euro - backing off from the psychological $1.50 level once more. It would need to sustain a move above this level to reaffirm the Euro's uptrend.

Soybeans - testing the January highs and would need to sustain a move above 1350¢ to reaffirm the overall uptrend.

Spain - largest downward dynamic in two-weeks but would need to sustain a move below the lows near 12,000 to reaffirm the medium-term downtrend.

UK (FTSE-100) - encounters resistance near the November lows and would need to break significantly back into the overhead trading range to erode bearish sentiment.

Wednesday 6th February 2008

Why it is so hard to keep the financial sector caged - This is a most considered and informative column by Martin Wolf of the Financial Times. Here is a sample:

The big question, indeed, is whether lessons must be embedded in regulation. Optimistic opponents of regulation argue that the banks have learnt their lesson and will behave more responsibly in future. Pessimistic opponents fear that legislators might create a Sarbanes- Oxley squared. The Act passed by the US Congress in 2002, after Enron and other scandals, was bad enough, they say. The banks might now suffer something worse.

"Dream on" is my reply to the optimists. To the pessimists, I respond: yes, the danger of over-regulation is real, but so is that of doing nothing at all.

Two points shine out about the financial system over the past three decades:

its ability to generate crises, and the mismatch between public risk and private reward.

It is true, on the first point, that none of the financial crises of this period has gravely damaged the world economy, although some have devastated individual economies. But it is probably just a matter of time. What would be happening now if US inflation were out of control or foreign official support for the US dollar were withdrawn? A deep and prolonged US recession would be probable, with devastating economic and political consequences.

It also true, on the second point, that the banking sector is the recipient of massive explicit and implicit public subsidies: it is largely guaranteed against liquidity risk; many of its liabilities seem to be contingent claims on the state; and central banks create an upward- sloping yield curve whenever banks are decapitalised, thereby offering a direct transfer to any institution able to borrow at the low rate and lend at the higher one.

In addition, banking institutions suffer from massive agency problems - between clients and institutions, shareholders and management and management and other staff. All this is also exacerbated by the difficulty of monitoring the quality of transactions until long after the event.

Consider, for example, the process that brought subprime loans to investors in special investment vehicles (SIVs). In between the ultimate borrowers and the risk-takers were loan-originators, designers and packagers of securitised assets, ratings agencies, sales staff, managers of banks and SIVs and managers of pension - and other - funds. Given the number of agents and the wealth of information asymmetries, it is astounding how little went wrong.

Yet big risks have indeed been run. The US itself looks almost like a giant hedge fund. The profits of financial companies jumped from below 5 per cent of total corporate profits, after tax, in 1982 to 41 per cent in 2007, even though their share of corporate value added only rose from 8 to 16 per cent. Banking profit margins have been strong, until recently. Now, at long last, earnings per share and valuations have collapsed.

Yet can anything effective be done to contain the risk-taking this implies? To answer this, we must distinguish "micro-prudential" controls over institutions from "macro-prudential controls" over the entire system.

On the former, the consensus of regulators seems to be that we need tweaks to the existing system. This could include: greater attention to liquidity management, alongside the focus on capital requirements in Basel II; more stress-testing of "value at risk" models; greater transparency throughout the businesses; and greater independence of ratings agencies from issuers.

I would argue, however, that none of this will make a sufficient difference. Regulators must also pay attention to the incentives - particularly the structure of pay - within the businesses. I would argue, in addition, that regulators would have to take a tougher approach than most did in the past cycle.

My view - The challenge, of course, is not to "keep the financial sector caged". Instead, it is one of governance - a subject often discussed in Fullermoney and now very familiar to veteran subscribers. Good governance is a matter of ethics and integrity, commencing at an individual level. Ideally, this is initially instilled in children by their parents, then taught throughout all formal education - not least at graduate schools, and established as a code of conduct by every employer, private or public. One would hope that this was a matter of common sense.

Corruption usually starts at the top within any business or government. It is inevitably imitated, trickling down and creating an amoral and often immoral climate. This is characterised by a "me-first", entitlement mentality, which is highly predatory. In other words, anything goes, so long as it satisfies the narcissistic ego. It is a recipe for disaster.

The potential for damage as a consequence of bad governance at an institutional level is limited only by the size and influence of those entities. In a competitive world, the US financial sector did not implode and contaminate others as a consequence of globalisation or any other external factor. Instead, its wounds are entirely self-inflicted.

What the US financial sector learns from this experience remains to be seen, but its history is not encouraging. Those of us beyond our formative years have seen these banking implosions before, occurring at least once a generation. The people who learn the most from these incidents will be wise, not merely clever. I suspect many will come from the so-called developing world.

Email of the day - On investing in China and Brazil:

"As a relatively recent subscriber (6 months or so), I would like to let you know that I find your service both enlightening and inspiring. Well done to Eoin and yourself and please keep up the good work.

"I note your comments today on the Atlantis fund for China. Also, I recall recently you mentioning Brazil as a candidate for you, were you to make further long-term investments. Do you still hold this view, and if so is there any particular vehicle that you have in mind?"

My comment - Welcome to Fullermoney and thank you for your thoughtful words.

I certainly remain a long-term bull of Brazil and this link will take you to my comments of 10th January, to which you are referring. ETFs for Brazil are listed in the Chart Library.

The Case of the Vanishing Bank Reserves - My thanks to a subscriber for this interesting report by Jonah Ford of Greenrush Capital Management. Here is the opening:

If the chart below [*Ed: see Subscriber's Area*] were a stock you owned in your portfolio, you would probably take a look at it and then flip on CNBC to find out what in the world happened to it. A blue chip style, slow and stable ascent from the 1960's, suddenly dropping from $40 a share to zero. Well, actually below zero. Fortunately for you it isn't a stock in your portfolio, and perhaps unfortunately for us all it does not appear to have any interest in stopping at zero. And it will likely be the biggest story of 2008, when the story breaks.

What the chart actually reflect is the aggregate (total) reserve levels of US banks. As is widely known as and yet seldom understood in detail, the banking system operates on a principle known as fractional lending. What this means in essence is that the banks can loan much more money out than they actually possess at any given moment in time. When you deposit money in the bank, the bank loans that money out, plus a whole lot more.

The Federal Reserve system requires that banks maintain a certain balance of reserves on their books. In other words, they are allowed and encouraged to lend more money than they have, but they have to keep a specified amount of capital on their balance sheets.

This is not entirely unlike the way a margin account works when trading futures. For example you can buy $90,000 worth of gold with about $4,000 margin at the current margin levels set by COMEX. But If you take the $4,000 out of your account, you must to liquidate the gold position accordingly. Banks hold a percentage of their income as reserve levels, and the assets they hold are outstanding (and usually performing or interest-paying) loans.

We've all heard probably more than we'd like to about subprime mortgages. Most of us know at least a few subprime borrowers who have had to tighten their buckle to make inflated payments, and some who have given up and walked away from their homes.

My view - Banking excesses leading to crises are a cyclical problem. Each one is somewhat different and quite terrifying because the numbers are larger, nominally if not in relative terms.

However governments no longer let their banking sectors go bust, as happened in the 1930s. They bail them out, usually via the yield curve, allowing banks to borrow from the Fed at preferential rates and lend at higher rates. Recently, banks have also borrowed from sovereign wealth funds, at punitive rates.

What happens next?

The racing certainty is that we will see the mother of all bank bailouts. This is essential because deflationary risks have soared following the burst housing bubble and banking crisis. The Fed has been behind the curve, as I emphasised for months, but is now catching up. It will do everything in its considerable power to avoid a Japanese style deflation, and it will be helped by various stimulus packages, including fiscal spending. I believe it is way too pessimistic to say that the Fed has lost control, as we hear from some pundits.

Won't all this reflation be inflationary?

Yes, although we do not know precisely where most of the inflation will appear. Currently, we have 'agriflation' caused by soaring food prices but this is a global problem of supply and demand, as I have mentioned before, and has nothing to with Fed policy.

In the USA, it seems most unlikely that we will see another housing bubble anytime soon, and I do not think we will see much wage inflation. Import prices are likely to rise, not least because of the weak US dollar, but the cost of most manufactured goods should only edge higher due to global competition.

'Agriflation' and historically high energy costs during an economic slowdown will lead to some stagflation in the USA and perhaps elsewhere in the developed world. However if a deep deflationary recession is avoided with the help of reflationary efforts and reasonably robust economic growth in developing economies, as I expect, the US stock market should avoid the considerably more serious slump that Jonah Ford expects.

If I am wrong on this last point, and we may not have to wait long for the stock market's verdict, share indices will slump beneath their November lows. Alternatively, if they consolidate the recent short covering rally above those lows, then equities could surprise on the upside this year, despite or perhaps because of the very bearish sentiment currently expressed by so many commentators.

If the bulls prevail, then I would expect emerging market equities to form the next bubble.

Additional Commentary by Eoin Treacy

Wheat Surges to Record on Supply Concerns; Corn, Soybeans Gain - This article by Aya Takada for Bloomberg covers wheat's upward break following the lower Canadian crop report yesterday. Here is a section:

Wheat surged to a record in Chicago, leading other grains and oilseeds higher on shrinking U.S. and Canadian supplies of high-protein varieties used for bread and pasta.

Canada, the largest wheat exporter after the U.S., said yesterday its inventories of the grain plunged by almost a third after adverse weather hurt crops. U.S. spring-wheat inventories will total 88 million bushels on May 31, down 25 percent from a year earlier, according to government forecasts.

The jump in grain prices may increase costs for food producers, including

Kellogg Co. and General Mills Inc., the largest U.S. cereal makers. It also risks stoking inflation and making it more difficult for central bankers around the world to stave off recession by cutting interest rates.

``Wheat prices just continue to explode higher,'' Simon Roberts, head of agricultural commodities at Australia and New Zealand Banking Group Ltd., said today in an interview with Bloomberg Television.

Chicago Board of Trade wheat futures, the global benchmark rose by the exchange-imposed daily limit of 30 cents for a third day. The March-delivery contract was 3 percent higher at $10.33 a bushel in after-hours electronic trading at 1:19 p.m. Tokyo time, beating the previous record of $10.095 set Dec. 17.

``Reduced supplies in Canada prompted wheat buyers to seek alternative supplies in the U.S., leading to a drawdown in U.S. inventories,'' Kenji Kobayashi, an analyst at Kanetsu Asset Management Co. in Tokyo, said by phone.

My view - I added the Minneapolis spring wheat contract mentioned in this article to the Chart Library. Importantly, it has led Chicago wheat on the upside over the past months. Spring wheat broke upwards in late August and continues to set new highs. This move anticipated Chicago wheat's advance by about two weeks. To date, the uptrend has been punctuated by two relatively similar-sized reactions in October/November and from late December until late January. Although it is looking somewhat overextended right now, a downward dynamic would be needed to check momentum, while a larger reaction would be needed to question the integrity of the uptrend.

Chicago Wheat accelerated to its high near 950¢ in September before falling back to 750¢. It then rallied back up to the high and has been consolidating that move for much of the last 6 weeks. Following today's upward break we can give the benefit of the doubt to the upside as long as it sustains the move. As was the case earlier in the year with the European wheat contracts, the Minneapolis spring wheat contract may offer a timing clue as to when this move ends.

World Equity Index Valuations Tables - Here is the monthly list of 96 global indices ranked in descending order by dividend yield and then in ascending order by P/E.

The Netherlands (7.86), Iceland (8.06), Luxembourg (8.4), Norway (9.24), Ireland (9.52), and France (9.98) all have P/Es of less that 10. Belgium (10.2), Spain (10.8) and the UK FTSE-100 (10.94) are all less than 11. This indicates that European stocks are not expensive. Italy (4.91%), Sweden (4.67%), Luxembourg (4.17%) and the UK (4.09%) also all have dividend yields in excess of 4%.

The downtrends for all of these markets have lost momentum over the last month and saw climactic selling in late January. They would need to sustain moves to new lows to reaffirm downward trends. The indices listed above are cheap fundamentally, even after allowing for profits downgrades, but the wider market is ignoring this fact at present. However institutional buyers, who want to build a position, are likely to be nibbling at these levels. As bullish sentiment eventually returns to the fore, these markets have considerable room for expansion.

(Please note: All data quoted above originates in Bloomberg. We realise that some of the data displayed is inaccurate for some indices, particularly where ADRs are included. However, I have endeavoured to remove those indices which were problematic. We continue to publish these tables because the data is generally accurate and going forward we will continue to weed-out the less reliable data sets as subscribers highlight them for us. I have also deleted the FTSE AIM Index from the list because it does not seem to have very reliable figures.)

Mineweb: Nickel market faces shortfall and price spikes - this article from Reuters which appeared in Mineweb covers the remarks of Jessica Cross on the nickel market. Here it is in full:

The price of nickel will find support at $25,000 a tonne and possibly rise to $40,000 a tonne in the next three years due to unexpected delays in production from new mines, a mining analyst said on Monday.

Nickel, a key product in the manufacture of stainless steel, is currently trading at about $27,000 a tonne.

"Looking out three years we are currently anticipating a well-supported price at $25,000 a tonne, with the potential for price spikes to $40,000 a tonne," Jessica Cross, CEO of Virtual Metals, told the Indaba Africa mining conference in Cape Town.

Cross said that strong demand from emerging economic superpower China had bolstered nickel demand.
The Asian giant's thirst for the base metal is not expected to significantly taper off anytime soon.

China's stainless steel production has soared, with the country now accounting for about a quarter of global output. Chinese nickel imports were up 8 percent in 2007 despite the impact of high prices for the metal.

Production start delays in a trio of new nickel projects in New Caledonia and Australia could add to the tightness in the nickel market, said Cross, who suggested that it was headed for a shortfall of 500,000 tonnes by 2012.

My view - Nickel broke upwards from its long base in 2003, accelerated to a high consolidated the gain for the next two years. It broke upwards once more in April 2006 and more than doubled as it progressed to $50,000. The fall from that level was abrupt and the metal found support in August near $25,000. Since then, the support around $25,000 has held and nickel appears to have entered a support building phase prior to eventually reasserting its overall uptrend. It would need to sustain a break below that level to question this outcome.

Email of the day (1) - on exposure to rock phosphate:

"Your comment for the day dated 5/02 asked about phosphate.

"There is an ET F listed in Canada called the Claymore Global Agriculture ETF (COW) which contains companies involved in agriculture and companies manufacturing fertilisers and agricultural chemicals. I have obtained exposure to the phosphate market by this route."

My comment - Thank you for this interesting suggestion which has Mosaic as its largest holding. I have added it to the Chart Library.

Email of the day (2) - more on phosphate companies:

"Thanks for putting into the chart library the Rock Phosphate price. The company that made me think about it is Minemakers here in Australia which has an undeveloped deposit that has become economic to develop with the phosphate price rise. Is 31 December the most recent price available? Because Minemakers have recently been quoting a price near to $200.

"Thank you to my fellow subscriber for the report on Rock Phosphate.

"On a different subject the Lithium prices in the chart library seem to be stuck in July 2007 for some reason.

"Thanks again for the best service around. I am always learning something each day."

My comment - Thank you for this inspiring email. Corresponding with the Collective is also a constant education for me. The most recent price available on Bloomberg is for the 31st December and I think it updates on a monthly basis. Minemakers, which I have added to the Chart Library, may have more up to date information considering they are closer to the coal face so to speak.

Thanks for alerting us to the Lithium price, this has now been corrected.

Email of the day (3) - on phosphate companies:

"The largest phosphate producer in the U.S. is Mosaic Company listed on the NYSE as MOS.

"Office Cherifien Des Phosphates(OCP) of Morocco is a very large North African phosphate producer. But I do not have information on where it is listed.

"The Groupe Chimique Tunisien(GCT) of Tunisia also is a very large North African phosphate producer. No information on where it is listed.

"Yuntianhua Group is the largest phosphate producer in China and it is listed on the Shanghai Stock Exchange A share.

"Hongfu Industry(also known as Guizhou Wengfu) is another very large phosphate producer in China. No information on listing.

"Phosagro and OJSC EuroChem Mineral and Chemical Company are the largest phosphate producer Russia. No information on listing.

"The above should cover about 85% of the world phosphate production."

My comment - Thank you for this informative email which confirms that a large amount of phosphate production is in private hands. Yuntianhua Group is the only one of these companies I could find a listing for.

Email of the day (4) - more on US listed Phosphate companies:

"Here is a link to Phosphate Rock companies in the U.S. I am sorry I have not vetted the site or the list, but readers may find it interesting as a starting point for research.

"Thanks for a great service."

My comment - Thanks for this interesting link which I'm sure will be of interest to other subscribers. The majority of these companies should be in the Chart Library. Phosphate presents an interesting chart pattern, but it remains to be seen if fertilizer companies will succeed in passing on the increased cost of the element to the end customer. Given the fact that grain prices are increasing they may succeed in doing this. Companies such as Mosaic remain in overall uptrends but have become less consistent over the last 6 weeks. Mosaic needs to sustain a move to new high ground to reaffirm its overall uptrend.

Email of the day (5) - on adding funds to the Chart Library:

"Would it be possible to add "New Star Heart of Africa" and the "Fidelity Emerging Europe,Middle East and Africa" funds to the chart library?"

My comment - The Fidelity EEMEA fund is already in the Chart Library but I have also added the New Star Heart of Africa Fund which has an initial fee of 5.25%, management fee of 1.75% and performance fee of 20%. The fund's largest holdings are in Nigeria at 36.25% , followed by Kenya with 9.4%. It is currently consolidating its gains from the November lows and needs to sustain a move above 50.5p to reaffirm the overall uptrend.

Today's interesting charts - The Chart Library has a wide selection of spreads and ratios which may be of interest to subscribers.

South African Rand per 1 US Dollar - The Dollar continues to rally against the Rand and would need to sustain a move below R7.5 to question upside potential.

India - bearing up particularly well following the downward dynamic on Wall Street yesterday. It would need to sustain a move below the recent lows to question potential for further upside.

Sugar - becoming less consistent following an impressive advance from the lows near 260. It needs to sustain a move to new high ground to reaffirm the overall uptrend.

Thursday 7th February 2008

Alex Seagle's The Contrary Investor: Which Way Does This Train Run? - My thanks to Alex Seagle for the latest edition of this highly original and informative letter, published by Fraser Management Associates. Here is a brief introductory sample:

As the political rhetoric ratchets up leading into the November Presidential election, the economy has become an increasingly important issue on the minds of voters. Predictably, outsourcing of jobs from the U.S. is a hot topic. But an underlying trend is building that might surprise many investors: the United States is the new hot spot for global companies looking for lower production and transport costs, and increased supply-chain flexibility. Investments in production facilities and jobs in a variety of industries are actually coming into the U.S., not the other way around.

In mid-January, France's Alstom, a maker of high-speed trains and power turbines, became the latest European company to unveil plans for a facility across the Atlantic. The company wants to build a $200 million plant in Chattanooga, Tenn., to mitigate the impact of the weak dollar on its margins and to get closer to some of its biggest customers. "Long term, a very high euro level is not good news," Alstom Chairman Patrick Kron said. "Let me also add the issue of volatility; we are in a heavy industry and exchange rates that change at the pace they're changing add to the difficulty."

The dollar has lost roughly 20 percent against the euro in the past two years. It's declined about 14 percent against the British pound. Partly as result of that depreciation, Alstom and other companies with global exposure are taking a fresh look at the United States as an attractive location for new facilities.

In recent months, companies ranging from automakers Fiat and Volkswagen to German steel behemoth ThyssenKrupp to South Korean consumer-electronics maker Samsung Electronics have either publicly debated or set in motion plans for U.S. plants. They are worried about the movement of the dollar, so moving to a dollar zone takes a big element of risk out of the equation. The trend reflects a notable shift in strategy.

My view - The USA's economic problems have understandably dominated financial headlines since last August. Consequently we have heard very little about inward investment, detailed by Alex Seagle. Banking crises come and go but the USA remains a great place to do business, and globalisation is a two-way street. These are points for investors to remember at a time when short sellers are scripting some of alarmist headlines.

There is wisdom in this report and I commend it to subscribers. You will also find a second, fascinating feature: The 21st Century Klondike, written by Rafi Chaudhury.

Lastly, readers may also be interested in the January issue of The Contrary Investor, which was temporary overlooked during last month's market drama.

Email of the day (1) - On MLW warrants:

"Thanks to your comments I have booked quite a lot of gains from MLW Warrants this year and currently hold quite a few hoping for more gains. What happens the day after the first exercise option if you don't sell? Do the warrants drop in price by the difference in exercise price? If so, should one sell now and buy back next month regardless of the underlying potential? This extract from the Warrants Alert Newsletter may be of interest to other subscribers:

"Should you exercise your Merrill Lynch World Mining warrants? This is, we suspect, a vexed question for many subscribers. The warrants are exercisable at 478p on 29th February 2008; or at 565p on 27th February 2009. The trust's shares are currently 598p, offering 120p of intrinsic value. The warrants are trading at 112.5p, which means they are at a discount to the 2008 exercise opportunity. If you have the cash, you could exercise now and hold the shares. That's a sensible approach. The alternative is to roll the dice and see what happens over the next twelve months. If the US does go into recession then commodity prices could fall on lower demand, and the warrants could quite easily expire worthless. They could also double in value if the economic news turns out better than feared. The current share price rating for the trust, on a 13.9% discount to net assets, suggests there is some value to be had from holding on and hoping things turn out OK, but the warrants are definitely SPECULATIVE. On the 2009 exercise terms, gearing is 5.3 times for a CFP of 15.08%, which looks no better than fair value. In view of the market conditions we might be inclined to exercise now, or else to treat the warrants are as a pure trading opportunity. They certainly offer plenty of volatility."

My comment - Thanks for your generous comments and well done in seizing your opportunities.

I have not dealt in the warrants, being more accustomed to trading the shares via spread-bets, and of course holding them in my personal long-term investment account. Therefore you and the Warrants Alert Newsletter have far more experience with these instruments, which I regard as additional trading vehicles. The Newsletter's summary sounds sensible to me and the safest forecast is that we will see further volatility.

Email of the day (2) - On the "Mother of All Reflations":

"Following your comments in the audio re the "Mother of All Reflations" how do you feel about the proposition put forward by what one might call the more lunatic fringe of gold-bugs that (simply stated) massive reflation will cause a seismic downward dynamic in the dollar and a consequent massive upwards move in the dollar price of gold (which they view as a proper repository of value),,,,,,,,,,,,"

My comment - More than 40 years in this business have taught me to be wary of extreme forecasts, from myself or anyone else. However, any student of monetary history, particularly over the last century, should know that fiat money, the supply of which is controlled by central banks, loses its purchasing power over time. There are no exceptions and for a good reason. Central bankers, and the administrations that appoint them, are closet inflationists although they will obviously make a considerable effort to manage inflationary expectations among the public.

Therefore the Fed is not the only central bank inflating, as the increase in money supply figures in excess of GDP growth for various countries frequently confirms. However the US economy's "need" for reflation, if the credit supercycle is to be extended rather than allowed to collapse due to its weight of debt, is greater than for most other central banks.

Consequently, risks for the US dollar persist and gold remains in an overall upward trend, against not only the greenback but all paper currencies. For the dollar to experience a "seismic downward dynamic", creditor nations would have to dump it from their reserves. While theoretically possible, this would not be in their economic interests because they rely on exports to the USA.

My personal portfolio: Nikkei futures long increased; wheat purchased and sold - These are delayed reports from yesterday, although I mentioned the wheat purchase in the Audio last night. A Baby Steps Nikkei bid was triggered at 13,450 for the March contract yesterday, increasing my long position. I should have placed it lower.

I also bought Wheat near the limit offer yesterday, paying $10.345 for a March position. On seeing it limit up once again today, I opted for a very conservative strategy to limit risk if it came out of limit and commenced a consolidation. Consequently I was stopped out at $10.45 this afternoon. I may buy back if an orderly consolidation occurs above $10, because the outlook remains bullish.

Prices above include all spread-bet dealing costs.

Additional commentary by Eoin Treacy

Citigroup Industry Focus: Black Gold - Coal That Is* - Thanks to a subscriber for this insightful report by Alan Heap and Alex Tonks which covers the international coal market. This chartbook by the same authors, in conjunction with John Hill, may also be of interest. Here is a section from the former:

Tight coal markets are being squeezed by slower growth in exports and stronger demand from Asia, exacerbated by problems in China, South Africa and Australia. We now expect 2008/09 contract prices to be US$100/t for thermal, US$200/t for coking. Semi-soft prices are likely to disconnect from traditional linkages with thermal coal and a contract price of US$145 is in prospect. PCI prices are expected to reach $170/t.

Thermal Coal The outlook for thermal will be determined by:
Australian port and rail constraints - Port and rail infrastructure constraints are expected to restrict Australian coal exports until at least 2010. Floods in Queensland will further reduce supply near term, although the coking coal market is most affected.

Similar problems in South Africa - The port of Richards Bay is being expanded from 72 to 91Mt. But the rail network will be challenged to deliver the additional coal from mine to port. The recent power crisis has been triggered by short term influences (seasonally strong demand and wet weather disrupting deliveries); but has longer term implications.

Indonesia - Nearly all future growth of Indonesian coal production will be of sub bituminous coals with a calorific vale of around 5800kcls. Many traditional thermal coal importers are capped on the proportion of low calorific value coal they can use, although this is not the case in China or India.

China - China has transformed from a net exporter of coal to a net importer. Whether this situation is sustainable is unclear, but what is clear is that the threat of surging Chinese exports has past. The current energy crisis has been triggered by bad weather but has deeper roots. The government has banned exports until March and longer term measures are expected.

Indian - India, like China, will depend on coal fired electricity generating capacity to power economic growth. New plants will use imported coal from Indonesia.

Europe - At current prices coal is still competitive with gas even at higher C02 prices. Our analysis points to a continued tightness in seaborne thermal markets extending to 2010. Longer term the structural characteristics of the thermal coal market do not support a radical transformation in the industry. Yet medium term barriers to entry will be supportive and the trend in thermal coal demand is considerably higher than many other commodities. As such we have lifted our long term estimates to US$50/t.

My view - Coal prices have gained for some of the same reasons as platinum over the last few weeks. They have benefited from supply disruptions in South Africa and Australia as well as the Chinese snow storms. The Big Sandy Barge price has the longest price history of those listed in the Chart Library and shows that interest returned to the coal market following a generational long bear market in 2000.

Prices remain quite volatile and are currently looking overextended. The first downward dynamic is likely to signal the beginning of the next medium-term correction, which could involve another reaction similar to those we've seen following prior accelerations. However, we can give the upside the benefit of the doubt until we see this type of signal.

What we can deduce from this long-term chart is that coal remains in a secular uptrend and the risks remain to the upside. However, it is likely to continue to be volatile and would need to sustain a break below $40 to question the integrity of the overall uptrend.

Deutsche Bank Talking Point: Clouds hanging over East Africa's largest economy - This article edited by Steffen Dyck for Deutsche Bank covers the investment repercussions of the ongoing violence in Kenya. Here is a section:

A little more than one month ago, Kenya was still considered a shining example of a stable and prospering country. Hopes were high that the elections on December 27, 2007 would be held in a peaceful and undisturbed environment.

The period of stability in Kenya had started in late 2002, when the then government under Daniel arap Moi handed over power to the National Rainbow Coalition (NARC). This also marked the end of almost forty years of one-party rule, which had begun shortly after the country gained independence from the UK on December 12, 1963.

The NARC government under Kenya's third president, Mwai Kibaki, set out to fight corruption which had become rampant in the Moi administration. To this date, progress has been poor, however: according to Transparency International's Corruption Perceptions Index, Kenya still takes 150th place in a global comparison of 180 countries. This puts Kenya on par with Zimbabwe and even behind Angola and Nigeria.

As a result, President Kibaki faced harsh opposition from both within the country and foreign donors. Loan disbursement was temporarily halted in 2005 and 2006 and only in the second half of 2007 did Kenya reach agreement with the International Monetary Fund.

During Kibaki's term of office, the slow economic growth between 1992 and 2002 became a thing of the past. During the five years up to 2007 real GDP rose by an average 5% p.a. Economic expansion was thus markedly lower than in Kenya's neighbour to the south, Tanzania, which saw GDP growth of nearly 7% during the same period.

Despite the existing problems with corruption and other shortcomings - especially in infrastructure - Kenya has enjoyed great popularity with foreign investors since the handover of power from Moi to Kibaki. This is due, above all, to the country's roles as the largest economy in the East African Union and as a trade hub and financial centre for the entire region. Moreover, Kenya plays an important part as a US ally in the fight against terrorism.

Unfortunately, the hopes for peaceful elections have failed to materialise, and claims by the opposition Orange Democratic Movement (ODM) under Raila Odinga that the election outcome had been manipulated have led to ethnic violence. Kenya's population is made up of more than 40 different tribes, with the Kikuyu (President Kibaki's tribe) accounting for the largest portion (22%) of the overall population. Already in the run-up to the December elections, the predominance of the Kikuyu in both politics and the economy had been addressed by the ODM.

While at the start of the year it still looked as though the crisis could be solved quickly, this currently seems increasingly unlikely, despite the fact that President Kibaki and opposition leader Odinga met for talks for the first time on January 24 and that Kofi Annan has come to Kenya to broker negotiations. Large segments of the population want the protests to end, but the violence no longer seems to be linked directly to the elections but rather to feed on ethnic resentment and conflicts that have gone on for generations.

My view - "Governance is everything" has become a mantra at Fullermoney. This is no less the case in developed countries as it is in developing countries, however for historical reasons markets in Africa are at a distinctly higher risk from civil war than other regions. Kenya remains one of the more investor friendly of East African countries and its future stock market performance is tied to the ability of its politicians to restore order quickly.

The stock market accelerated to a high near 6000 in January 2007 and has been consolidating that gain for the last 12 months. Following the contested election result a month ago, the Index has fallen to test the bottom of the range near 4600. An upward dynamic is needed to indicate that demand is returning near these levels.

A number of investors have recently looked to Africa as the next big, very long-term investment destination. This argument carries some weight as many African countries are only now developing capital markets and have huge upside potential. However it will be a long process and will undoubtedly be questioned following political disturbances. The trend towards improving governance in individual countries as well as across Africa needs to continue, if the continent is to fulfil its potential.

Baltic Dry Index Declines for Third Day as Demand Slows in Asia - This article by James Ludden for Bloomberg covers recent activity by the Baltic Dry Index. Here is the story in full:

The Baltic Dry Index, a measure of shipping costs for commodities, fell for a third day as the beginning of the Chinese Lunar Year reduced demand for vessels.

The index, which tracks transport costs on international trade routes, declined 30 points, or 0.5 percent, to 6,002 points today, according to the Baltic Exchange. Supramax carriers, which can haul 50,000 to 59,999 metric tons of goods, were the only class to rise in the benchmark.

Hire rates have fallen 46 percent since reaching a record Nov. 13, reflecting a drop in iron-ore shipments from Australia and Brazil, transport disruptions to coal exports from South Africa and Australia and signs the U.S. is slipping into a recession. The Chinese Lunar Year holiday, which extends until the middle of next week, has also led to a surplus of vessels competing for cargoes in Asia.

Shipping executives including Fotini Karamanlis, chief executive officer of Hellenic Carriers Ltd., expect freight rates to rebound once negotiations over 2008 iron-ore prices are resolved and Brazil and Australia resolve supply disruptions.

The Baltic index may climb to a record in the next six months as Chinese companies recover from snowstorms and resume imports of raw materials, Henriette van Niekerk, a senior analyst at London-based Clarksons Plc, the world's largest shipbroker, said in an interview in Dubai yesterday.

The seaborne iron-ore market totaled 735 million metric tons last year, up from 685 million tons in 2006, according to Magnus Ericsson, chairman of Stockholm-based Raw Materials Group.

Contracts called forward freight agreements, indicating the future price of shipping commodities, advanced.

April-to-June capesize FFAs climbed 5.3 percent to $119,000 a day as of about 2 p.m. in London. Panamax contracts for the same period rose 4.4 percent to $59,250 a day. Capesizes are the biggest vessels within the Baltic index and normally transport coal and iron ore.

My view - The Baltic Dry, Panamax and Capesize Indices have all fallen precipitously from the highs they posted in Q3 2007. This was in part because of fears of an economic slowdown, an expected large increase in the supply of ships sometime in the next year or two as well as orders being cancelled because of disruptions to ore supply in Brazil. However these indices have now all returned to interesting levels and found at least short-term support. Additional ranging here, characterized by higher reaction lows, would indicate support building and raise the chances of an eventual reassertion of their overall uptrends.

Today's interesting charts - we have recently added first and second month continuation charts for the most actively traded commodities, to the Chart Library which may be of interest to subscribers.

Natural Gas - continues to consolidate near the top of the two-year range but needs to sustain an upward break to indicate that a significant supply / demand imbalance has developed.

Arabica Coffee - breaking upwards from the more than three year range and would need to sustain a move back into that pattern to question scope for further upside.

Japan (Nikkei 225) - remains in an overall downtrend and led on the downside. However the Index has lost downward momentum and would need to sustain a move to a new low to reaffirm the medium-term downtrend. Since Japan led on the downside, there is a possibility that it will give a timing clue on the upside.

Email of the day - on an addition to the Chart Library:

"Could you please add ABN AMRO China A Share Fund to Chart Library?

"Thanks"

My comment - Thank you for this interesting suggestion which has been added to the Chart Library. It has a front end load of 5.25%, redemption fee of 0.85% and management fee of 1.5%.

Friday 8th February 2008

Browning Newsletter on climate change: 2008 - The First 6 Months - My thanks to Alex Seagle for this fascinating publication by Evelyn Browning Garriss, published by Fraser Management. Here is the opening:

Back in September, the Browning Newsletter warned that midwinter would be unusually cold. There are times when it is no fun being right. After a frigid December and an early January thaw, North America faced a typical La Niña weather. It was bitterly cold and miserable.

The cold extended from coast to coast. Below freezing weather swept the agricultural lands of California and the Southwest. Wind chills plummeted Butte, Montana's temperatures to a frosty -47?F (-44?C). Temperatures in the Upper Midwest and Northern Plains were about 30?F (16.6?C) below normal. Below zero (less than -18?C) temperatures spread as far south as northern Kansas and Missouri and the Ohio Valley. The freezing cold swept across the South. Even the Gulf Coast was below freezing with both Mobile, Ala., and Gulfport, Miss. hitting 28?F (-2?C).

As cold as it was, the weather brought welcome moisture to many drought-ridden states thanks in part to the Mexican volcanic aerosols. California and the Great Basin have been hammered by a series of Pacific storms that have more than doubled the water content of the Sierra Nevada snowpack. Snow, sleet and rain blanketed the nation with as much as 5 inches of snow in Alabama. The clash of cold northern air and Gulf moisture helped produce two tornadoes along Florida's west coast. Lake-effect snow collapsed roofs in New York and Boston was deluged by seven inches of snow during a rare thundersnow.

Canada basked in relative warmth in early January, following the frigid temperatures of December. However the season's coldest temperatures swept through the western provinces late in the month. Winnipeg survived brutally cold temperatures; almost 10?C (18?F) lower than normal. David Phillips, Environment Canada's senior climatologist, described the climate as, "It will be as cold in Winnipeg as it is at the top of the world."

Eastern Canada also experienced cold but temperatures were not abnormal. What was abnormal was the tornado watch that Environment Canada posted on January 8 for Southern Ontario.

January is ending like a typical La Niña. Freezing storms are rapidly whipping through the Midwest and Northeast. Chicago saw temperatures drop fifty degrees in a matter of hours. Western Canada is cold and a large new storm is threatening British Columbia and the Pacific Northwest. The cold stormy weather is dominant and will continue to dominate in early February.

My comment - There are some interesting analysis on the outlook for agricultural crops in this issue - from the USA to China.

Email of the day (1) - On Russia:

"Could you please cast a glance at the Russian stock market? Two weeks ago, the RTSI index fell through the 200-day moving average. It rebounded several days later only to hit the 200-day MA curve and plunge again. Am I right to understand that this means that the market will have to consolidate for some time before it is able to grow through this ceiling? Is there scope for further downside?"

My comment - Russia's share indices experienced a downdraught last month, in line with many other stock markets, only it has been weaker subsequently. The tradeoff when evaluating Russia's fundamentals is on the one hand, strong GDP growth and world-class resources companies trading at mouth-watering valuations. On the other hand, Vladimir Putin's government has a reputation among investors for skimming off the profits and showing scant respect for the rights of minority shareholders.

Will this change as Putin's nominee, Dmitry Medvedev, is elected president next month? Living in Moscow and being familiar with the political environment, you would know better than I.

Technically, Russia has experienced an extreme reaction against the prevailing trend - the Type-2 ending as taught at The Chart Seminar. This is not dissimilar to what occurred in May-June 2006, checking the medium-term uptrend, only it is occurring from a higher level. Russia's current underperformance is a short-term concern. Having taken out last month's low, a downside failure is now required to indicate that it has bottomed. This would require at least a move above the mid-point of the recent range centred on 1970.

Email of the day (2) - On gold:

"David.. 2 questions re gold…listening to the audio last evening, Eoin foresees that there is a slow down on the downward trend on the market indices and after this bottoming out that there could be some good buying opportunities. As this is likely the case is there a good chance that gold would become less and attractive short term, as you often say that this is a global beauty contest? Secondly given that gold is stretched considerably from its 200 ma, does this concern you re gold, despite being in a long term uptrend? Many thanks for your insightful view."

My comment - These are relevant points. When investors and traders regain confidence in stock markets, that might siphon away some of the interest in gold. Also, extension relative to the MA tells us that this medium-term upside move in gold is maturing and will probably spill over into another medium-term consolidation in coming months. Meanwhile, from a trading perspective, I would prefer not to see the last reaction low on the daily chart taken out. I believe that the longer-term outlook for gold remains bullish.

My personal portfolio: Lumber long opened, and could this be the next big one? - I last mentioned lumber in my "State of the markets", review (Part 4) posted 29th January: "Lumber is intriguing because the price is so low. The first sign of an upward dynamic should spark at least a respectable technical rally." We will soon find out if this is correct.

Last night, having completed my copy and just before I left the office, I noticed that lumber had surged to the upper side of its small range near historic lows, forming the upward dynamic referred to above. I opened an initial stake in this big contract, paying $228.50 for a March position. This afternoon, I increased it, paying $229.30 and $225.80 for two more equal-sized March holdings. People will understandably have reservations about lumber because of the US housing slump. Good point but that problem is reflected by the historically cheap price. Lumber is a global market and a boom in agricultural commodities is underway. These prices include all spread-bet dealing costs.

To address my own question in the headline above - I would not be surprised. Lumber is historically cheap and will certainly recover from these levels. The only question in my mind concerns the length of support building near current levels before a significant rebound occurs. This is unknowable but the overall strength of commodities is in lumber's favour and it is not a crowded trade at present, unlike many other commodities. Assuming it rallies, the next big hurdle is in the form of potential resistance near $240.

I also picked up a bit of corn, and say with some chagrin that this was more emotional than analytical, as I was disappointed to lose my wheat position yesterday due to a too tight stop. I paid $5.195 for a March position and will be fortunate to escape with a profit.

Email of the day (3) - On UK banks (from a pre-subscriber):

"Thank you for a great service. Really look forward to reading your daily comments.

"Given the current uncertainty surrounding the level of impairment that bank's balance sheets have incurred from the subprime fallout, how safe are cash deposits placed with UK banks? And how much protection does the deposit insurance fund provide to depositors should a bank fail?

"Also, how does a small private investor buy UK government t-bills? Is there an ETF or listed instrument which will give one such an exposure? I'm really just looking for a way to keep cash on hand without exposing myself to bank credit risk."

My comment - Thanks for the feedback.

UK deposit insurance is woeful. However the government guaranteed all bank deposits following the Northern Rock debacle last year. The Chart Library lists many interest rate funds.

Email of the day (4) - On Alastair Ross Goobey:

"I don't know whether you carry any obits or not in FM, but I was saddened to read of ARG's death today, having got much enjoyment from thoughtful and erudite articles he wrote in the 1980s and 1990s. Certainly a loss to the investment world, which needs more such characters and people of integrity."

My view - I too was saddened to read of his death the other day. I met him on several occasions at research luncheons during his earlier City days. He had one of the best financial brains known to me. He was also a Renaissance man and a true gentleman. Thank you for attaching this obituary.

Email of the day (5) - On my main cash holding:

"You mentioned holding cash in NZ dollars recently at attractive interest rate. Could you say more about this? Do you have a multi currency account? Do you pay commission on the transfer of funds into the foreign currency? If so, this must offset the interest rate advantage. Finally were you describing cash funds in your trading or investment account - can it be done in both? Thanks in anticipation."

My comment - I did the transaction through a corporate account with a UK bank. I could have selected any of numerous freely traded currencies. The money was in what they call a "Treasury Rollover", which I had set at monthly intervals. I paid a commercial spread in switching from GBP to NZD. For the first month, I got 8.2%. Disappointingly, a fax detailing the next monthly rollover says the rate has dropped to 7.84%, so obviously that varies in line with market rates. It is still a lot better than what I would be getting in sterling, which is also slipping against the NZD.

Email of the day (6) - On EURUSD:

"Hi David/Eoin, thanks for the service which I value highly. I still haven't made it to a chart seminar (Sydney is a long way away) and would like to ask an opinion on EURUSD, as (amongst other things) I trade currencies....

"If you look at a weekly chart, EURUSD has run up from around 1.1800 in late 2005 to just shy of 1.5000. There has been acceleration in Q4 last year, and a "triple top" and failed break of 1.5000. There look to be some classic trend ending signs there.

"Would you be able to give me a "proper" behavioural technical analysis and chart seminar view of this technical action. I am currently flat EURUSD (thankfully), but with the somewhat dovish stance and revised perspective from ECB in yesterday's statement, feel we could be in for a big correction."

My comment - You are welcome and we are delighted that you value the service, which shows that you know how to use it.

Regarding EURUSD, on looking at this weekly chart, ask yourself what are the main consistency characteristic since 2006? Then ask what changed, if anything? Lastly, what do you think would alter the psychology of traders in this market?

Try to do this on your own, before looking at my answers below.

The main consistency characteristics are an unbroken progression of higher lows and higher highs (the former are much more important because there won't be a really big sell-off without breaking the higher lows). There are also similar-sized reactions and a step-sequence ranging uptrend.

In terms of what changed, you can see that the ranging pauses decreased in duration above $1.30, and more importantly the trend accelerated somewhat during its last upside leg. Acceleration is an ending of unspecified duration and the latest range is of slightly longer duration than we have seen for some time, although the downward reactions are not sufficiently large to alarm the bulls.

So supply and demand are temporarily in balance, evidenced by the present range, which is occurring in an accelerated uptrend. Incidentally, everything I have said above is a technical fact, rather than theory. Eoin and I work with technical facts, not theories, because one can conclude anything with the latter.

The last question is the easiest one - a sustained break above $1.50 would reaffirm the uptrend and excite the bulls. Conversely, a sustained break beneath $1.4325 would favour the bears.

Lastly, you might try using commonality - evidence from other cross-rates, which could provide advance warning, one way or the other, not least because neither of these currencies is a powerhouse at the moment. For profitability, try to trade the more in-form currencies against the more out-of-form currencies.

Email of the day (7) - On "more hidden time bombs:

"Absolutely love being a subscriber - no need to say anything more! Questioning though the risks that the credit crisis has more hidden time bombs - I would appreciate your thoughts on the Bloomberg article here."

My comment - Thanks for your inspirational comment.

Time bombs in terms of bad news are generally worst when they catch us by surprise. The ARMs story covered in the article you forwarded is sad and also a disgrace. It is also well known. If you recall crises, real and imagined, during previous decades, the warnings and fears lingered on long after they had been fully discounted. If we have not yet reached that point I suspect we are not that far off it.

Tim Price: Stocks in turmoil as Neasden bank reports shock profit - What better way to end the week than with vintage satire from Tim Price of PFP Wealth Management. Here is the opening:

February 4 (London) - European stock markets were thrown into fresh turmoil today as Société Bancaire de Neasden shocked investors by disclosing that it had inadvertently drifted into profit during its fourth quarter. At a press conference, SBN Chief Executive Officer Boris Nurdbongleur expressed his remorse.

"This is a dark day in the history of Société Bancaire de Neasden, the premier investment banking powerhouse of the Willesden Green and Dollis Hill area. I know our customers, investors, shareholders and taxpayers count on us to lose money, and I feel like I have let them all down."

He admitted that he had tendered his resignation to the bank?s chairman, Mr. Boris Nurdbongleur, but that his offer had been rejected. The bank?s CEO also pledged to launch a full scale investigation into the rogue profit, jointly headed by the bank?s crack Forensic Trade Oversight, Manipulation and Reconciliation Committee, Boris Nurdbongleur, and head of Settlements, Compliance and Executive Compensation, B. Nurdbongleur.

The errant profit is thought to have been triggered when a sandwich delivery man managed to bypass the bank?s state of the art security system, Mavis on reception, and accidentally sat on a keyboard in the bank?s dealing room. Announcement of the profit was delayed pending the purchase of a replacement keyboard, thought to be a Keysonic Wireless Mini, available from Argos Neasden at £34.95. Commentators suggested that this might not be the last occurrence of an incompetent arse in a dealing room this year.

Quote of the week - On buying funds wisely:

"I've found that when the market's going down and you buy funds wisely, at some point in the future you will be happy. You won't get there by reading 'Now is the time to buy'."
Peter Lynch

Additional Commentary by Eoin Treacy

Goldman Sachs JBWere: Commodities Outlook 2008 Zinc: Growing Surplus; Falling Price! - Thanks to a subscriber for this interesting bearish report on the prospects for zinc. Here is a section:

Meanwhile global production growth accelerated to 6.5% (Table 1), driven by a third year of double-digit growth in Chinese mine output, abetted by the commissioning of new mine capacity - both brownfield and greenfield - in Western countries. Yet LME stockpiles continued to edge lower, only bottoming out in October 2007, and belying anecdotal evidence of weaker fundamentals from our industry contacts: (a) that demand was weakening, particularly in North America, (b) that producer stocks of metal had recovered to "normal" levels, and (c) that spot-market treatment charges were rising, indicating a more comfortable supply of raw materials for the smelters.

Worryingly, we believe that last year's implied metal surplus will become much more visible in the first half of 2008. Two of the largest greenfield start-ups of 2007, San Cristobal in Bolivia, and Cerro Lindo in Peru, were ramping up mine production in the back-end of the year but, realistically, the lead-time for this production to flow through to the refined metal market would be in the order of three to four months. This means that the impact of some of last-years' major additions to supply is only now beginning to be felt, a view that we believe to be consistent with the c. 24,000 tonnes (27%) build in LME stockpiles in the first five weeks of 2008. True, inventories remain at very low levels by historical standards (Chart 2), but we are forecasting a 420,000 tonne surplus for 2008 which could raise stocks to more than seven weeks of Western consumption by year-end. We believe that this would imply an annual average price for 2008 well below last year's 147c/lb; indeed, given the revised scale of the surplus in our model, we believe that there is significant downside risk to our current 2008 price forecast of 115c/lb.

For 2009 we envisage a further surplus, in the order of 220,000 tonnes, and we are forecasting an average price of 91c/lb and, again, we suggest that risk to this price forecast has a negative skew. From 2010, however, the market begins to look a little tighter in our view. Quite simply, we struggle to see enough new capacity developments to meet our demand projections in the 2010-2012 period - a situation quite similar to our current view of the copper market. >From 2010, therefore, we expect a significant price recovery, with current forecasts for 2010 and 2011 of 98c/lb and 116c/lb respectively.

My view - Could zinc come back to touch the top of the long-term base near $1000? Yes, is the short answer, but that is a very unlikely scenario. Undeniably the metal has fallen considerably from the Type-3 top as taught at TCS. However the downtrend has lost consistency and zinc has been ranging close to $2200 for the last three months. This is also the longest congestion area within the overall downtrend. To fulfil Goldman's contention that zinc prices are about to move sharply lower, it would need to sustain a move below $2200. Right now, the chart suggests to me that it is more likely to continue to range in this base building phase and is likely to reassert its overall uptrend at some point in the next few years.

Ernst & Young EYeSight on Consolidation: Backpedalling on the cycle - This well argued report by Ernst & Young makes a convincing case for a secular bull market in industrial metals, Here is a section:

Traditionally, the perception of the mining cycle has been that the mining companies respond to high prices by bringing on too much new production, which tips the balance of supply and demand to oversupply, in turn leading to lower prices. At low prices the high-cost mining companies start to lose money and shut down capacity, and this leads to supply shortage and price increases.

This historical behaviour by the industry, however, does not occur in isolation. It is heavily influenced by the overarching economic cycles of periods of growth and contraction.

The charts to the far right show metal prices over more than a century, an in real terms. They highlight a number of periods that have been interpreted as cycles in the mining industry. We believe that there have been specific reasons behind most of these cycles which are unlikely to be repeated in the near future. For example, we believe that the weak prices experienced in the 1990s were in large part a reflection of the collapse of the Soviet Union. This simultaneously triggered the release of 50 years of accumulated stockpiles of minerals alongside a sharp reduction in domestic demand in the Commonwealth of Independent States (CIS). These metal stocks, which had been mined at, quite literally, any cost during the Cold War may have forced down the traded metal prices to artificially low levels until those stocks were eventually depleted - at exactly the time that demand returned.

It should be also recognized that the availability and the use of so many of the metals we take for granted is actually a relatively recent phenomenon, partly driven by technology. 'Relatively recent' here means about a century for metals such as aluminium, and mere decades for a whole host of other metals such as titanium and even uranium. On top of the traditionally recognised economic cycles are the really major developments represented by, for example, the Industrial Revolution, the rise of the US economy, the Cold War, the subsequent collapse of communism in the Soviet Union and now the industrialisation of China.

It is our view that current metals prices are actually a return to sustainable price levels following an extended period of artificially depressed prices, rather than the conventional wisdom that the industry is near the top of a cycle.

Maybe this time it is different…

My view - In one sense things are never different in markets because all great bull markets eventually come to an end. This is often a surprising fact for those closest to the action when a phenomenally powerful bull trend ends. The phrase, "this time it is different" was ridiculed following the Nasdaq bubble because so many investors lost so much money stemming from the belief that earnings didn't matter. Earnings always matter and many of the companies which typified the belief that they don't have gone bust. That should not stop us from appreciating that truly secular bull markets occur because something really is different this time.

The surge in commodity prices over the last 5-years from metals to grains is supported by a strong fundamental theme, which is not about to disappear. Emerging Asia is now the locomotive for global growth and infrastructure development across the region is set to continue for a number of years. In tandem with this move, an unprecedented number of consumers are gaining exposure to the global economy and per capita consumption of all commodities is on the rise.

When investors have spent a generation deriding a sector, it takes time for ingrained beliefs to be dispelled, and as we have seen, doubts can persist for long into the new secular uptrend. However the longer prices remain at elevated levels the more old maxims are challenged. When attitudes change enough to indicate that most investors are overweight in a sector, we know that we are close to the end game. In the case of commodities and particularly industrial metals, we are a long way from that situation.

Today's interesting charts - Just about all commodities are listed in the Chart Library and many of the most commonly traded have both 1st and 2nd continuation charts.

Oil - bouncing from the lower side of the range, having found support near $88 for the third time in two months. It would need to sustain a move below this level to offset scope for some further higher to lateral ranging.

Palladium - continues to rally following the breakout from its two-year consolidation and would need to sustain a move back into that range to question scope for further upside.

Wheat - surging upwards following the breakout from the three-month consolidation and a downward dynamic would be needed to check momentum.