

# Fullermoney *Highlights*

Global Strategy and Investment Trends compiled by Eoin Treacy

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**14<sup>th</sup> February 2008**

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<b>David</b>	<b>Dax</b>	<b>Short 15/01 7707 Mar08</b>	
	<b>Silver</b>	<b>total position stopped out</b>	<b>CL 15/01 \$16.24 Mar08</b>
	<b>Silver</b>	<b>Long 15/01 \$16.19 Mar08</b>	<b>20% rebought</b>
	<b>Gold</b>		<b>CL 16/01 \$882 Feb08</b>
	<b>Gold</b>	<b>33% stopped out</b>	<b>CL 16/01 \$882 Feb08</b>
	<b>Silver</b>	<b>Long 16/01 \$16.145 Mar08</b>	
	<b>Silver</b>	<b>Long 16/01 \$16.105 Mar08</b>	
	<b>Silver</b>	<b>Long 16/01 \$16.09 Mar08</b>	
	<b>Silver</b>	<b>Long 16/01 \$15.965 Mar08</b>	
	<b>Silver</b>	<b>Long 16/01 \$15.83 Mar08</b>	<b>total position repurchased</b>
	<b>Rio Tinto</b>	<b>Long 17/01 £45.218 Mar08</b>	
	<b>Platinum</b>	<b>Long 17/01 \$1569.3 Apr08</b>	
	<b>Dax</b>		<b>CS 17/01 7701 Mar08</b>
	<b>MLW LN</b>	<b>Long 18/01 596.3 Mar08</b>	
	<b>Silver</b>	<b>16.66% reduction</b>	<b>CL 18/01 \$16.35 Mar08</b>
	<b>Gold</b>	<b>Long 18/01 \$885.9 Apr08</b>	<b>25% increase</b>
	<b>Rio Tinto</b>		<b>CL 21/01 £45.113 Mar08</b>
	<b>Platinum</b>	<b>1 unit</b>	<b>CL 21/01 1544.9 Apr08</b>
	<b>Gold</b>		<b>CL 21/01 \$865 Feb08</b>
	<b>Gold</b>		<b>CL 21/01 \$863 Feb08</b>
	<b>Platinum</b>	<b>total position closed</b>	<b>CL 21/01 \$1538.8 Apr08</b>
	<b>Silver</b>		<b>CL 21/01 \$15.62 Mar08</b>
	<b>Silver</b>		<b>CL 21/01 \$15.635 Mar08</b>

Silver		CL 21/01 \$15.63 Mar08
Palladium	total position closed	CL 21/01 \$362.1 Mar08
Silver	total position stopped out	CL 21/01 \$15.615 Mar08
Gold		CL 21/01 \$865 Feb08
Gold		CL 21/01 \$863.2 Feb08
Rio Tinto	Long 22/01 £41.655 Mar08	
Gold		CL 22/01 \$885.9 Apr08
Hang Seng	Long 23/01 22959 Jan08	
Nikkei 225	Long 23/01 12963 Mar08	
Silver	Long 23/01 \$15.855 Mar08	
Silver	Long 23/01 \$15.805 Mar08	
Eurobund	Short 24/01 116.28 Mar08	
Hang Seng	Long 24/01 23957 Mar08	20% increase
Nikkei 225	Long 24/01 13355 Mar08	
Nikkei 225		CL 28/01 13370 Mar08
Nikkei 225	Long 29/01 13300 Mar08	
Gold	Long 29/01 \$930.7 Apr08	
Silver	Long 29/01 \$16.71 Mar08	
Hang Seng	Long 29/01 24329 Feb08	CL 29/01 24273 Jan08
Hang Seng		CL 30/01 24022 Feb08
Hang Seng		CL 30/01 23362 Feb08
Nikkei 225	33% stopped out	CL 30/01 13350 Mar08
US 30yr		
Treasuries	Short 30/01 118.85 Mar08	
Nikkei 225	Long 31/01 13158 Mar08	
Nikkei 225		CL 31/01 13485 Mar08
Hang Seng	Long 31/01 23236 Feb08	
Hang Seng	Long 21/01 23159 Feb08	
Silver		CL 31/01 \$17.01 Mar08
Rio Tinto		CL 01/02 £57.298 Mar08
MLW LN		CL 01/02 633.8p Mar08
Hang Seng		CL 01/02 23350 Mar08
MSCI		
Singapore	Long 01/02 377.7 Feb08	
Silver	Long 04/02 \$16.515 Mar08	
Nikkei 225		CL 07/02 13450 Mar08
Wheat	Long 06/02 \$10.345 Mar08	
Wheat		CL 07/02 \$10.45 Mar08
Lumber	Long 08/02 \$228.50 Mar08	
Lumber	Long 08/02 \$229.30 Mar08	
Lumber	Long 08/02 \$225.80 Mar08	
Corn	Long 08/02 \$519.5 Mar08	
Hang Seng	Long 11/02 23000 Feb08	
Silver	Long 11/02 \$17.355 Mar08	
Silver		CL 12/02 \$17.37 Mar08

	<b>Gold</b>	<b>Long 12/02 \$917.65 Apr08</b>	<b>33% increase</b>
	<b>Silver</b>	<b>Long 13/02 \$17.17 May08</b>	
<b>Eoin</b>	<b>White Sugar</b>		<b>CL 21/01 \$338.5 Mar08</b>
	<b>Gold</b>	<b>Long 28/01 \$928 Apr08</b>	
	<b>Gold</b>	<b>Long 01/02 \$935.45 Apr08</b>	
	<b>Nikkei</b>	<b>Long 01/02 13700 Mar08</b>	
	<b>Hang Seng</b>	<b>Long 01/02 24239 Feb08</b>	

## January 22<sup>nd</sup> Fed Cuts Rate 0.75 Percentage Point in Emergency Move

Here is the opening from today's [report](#) by Bloomberg:

The Federal Reserve cut the benchmark interest rate by three quarters of a percentage point, its first emergency reduction since 2001, after stock markets tumbled from Hong Kong to London amid increasing signs of a U.S. recession.

The central bank cut the target overnight lending rate to 3.5 percent from 4.25 percent, the Federal Open Market Committee said in a statement in Washington. Policy makers weren't scheduled to gather until next week. It's the biggest single reduction since the Fed began using the rate as the principal tool of monetary policy around 1990.

"Broader financial market conditions have continued to deteriorate and credit has tightened further for some businesses and households," the Fed said in a statement in Washington. The FOMC took the action "in view of a weakening of the economic outlook and increasing downside risks to growth."

Policy makers set aside concerns about inflation to lower borrowing costs for the fourth time since September after the unemployment rate rose, retail sales fell and stocks slumped. Chairman Ben S. Bernanke shifted the Fed's stance to a more aggressive approach in remarks this month citing a need for "decisive and timely" action.

And the actual vote:

The FOMC vote was 8-1, with St. Louis Fed President William Poole preferring to wait until the regularly scheduled meeting. Fed Governor Frederic Mishkin was absent and not voting.

Fed officials met by video conference at about 6 p.m. yesterday, spokeswoman Michelle Smith said. Mishkin was traveling and unable to participate, she said. The voting members were the same as in 2007 because the presidents don't rotate in until the first regular meeting, Smith said.

My view - [Good news!](#) However this decision begs the question: [Why didn't they do this at the beginning of the year, or better still, in November?](#)

Sadly, and briefly since this is familiar ground for subscribers, the Fed knew nothing about psychology - pertaining to investors, consumers and corporate managers. It was working by committee, producing statements flattering to camels when leadership was required. It was preoccupied by food and energy price inflation, over which it has no control, while slumping house prices and a financial crisis were sapping the economy and reintroducing deflationary risks. The Fed appeared to believe that waiting for its next scheduled meeting during a crisis was more important than pre-emptive action.

By what logic did St. Louis Fed President William Poole dissent during yesterday's vote, preferring to wait until the next FOMC meeting on the 30th? On second thought, I don't want to know as the answer would undoubtedly be depressing.

More importantly, what will be the effect of this reactionary rather than anticipatory move to cut rates by the Fed today?

It will help to cushion downside risk for the stock market and economy somewhat, although not nearly so much as would have been the case if rates had been lower 'like an elevator' some weeks ago. Unfortunately, risks increased rapidly as the Fed fell further behind the curve. Sentiment deteriorated and US stock market indices completed top formations. Contagion and the Wall Street leash-effect caused most other stock markets to capitulate recently.

Some may feel that this was always predestined and in the charts because of the banking crisis. We will never know for certain but I disagree and there is historic precedent. 'Don't fight the Fed' has proved to be one of the most effective maxims for investors, but the context is crucial.

A Fed that anticipates and is proactive inspires investor, consumer and corporate confidence. A Fed that equivocates and falls behind the curve undermines confidence to the eventual point of panic. The USA's economic problems are real and a serious concern, but there is also a healthy multinational / export sector, profiting from stronger growth outside the States. Equity valuations are quite reasonable, even after allowing for profit downgrades, and they are very competitive relative to long-dated government bonds.

Assuming that the Fed is now determined to catch up with the curve of events - it isn't there yet but has taken a big step today - further rate cuts would help a weak economy, as would the emergency stimulus package. This would lend support to the stock market.

Incidentally, I regard statements that "the Fed is now irrelevant", which we have heard from some quarters recently, as emotional rather than analytical. It should be self-evident that the decisions of those who control the monetary levers will always be important for investors.

Assuming that we see additional rate cuts of at least another 100 basis points in coming months, which I believe are necessary and likely. Wall Street should

avoid the grinding, lengthy bear market that many fear. However it will take time to repair technical damage, not least for the financial sector.

Today's move by the Fed makes it much more likely that other central banks will also lower rates, in regions where there are legitimate growth concerns. This will do no harm to global stock market sentiment. The recent shakeout has created opportunities in Fullermoney themes, for those who agree with them and for whom they are appropriate.

Technically, today's rebounds from the day's lows for stock market indices in Europe and the Americas suggest that we have seen climactic lows of at least near-term significance. Closes beneath these lows, also for Asia where I would expect a rebound tomorrow, would be required to offset current scope for a technical rally.

The rate cut is a big headwind for the US dollar, but bullish for precious metals.

### **January 24<sup>th</sup> State of the markets: stocks, government bonds, currencies & commodities**

Following on from our reviews of markets earlier this week, I think an unemotional summary of where we are right now - from a technical, behavioural and fundamental perspective - might be useful for subscribers. I have done this in a discussion format, including Q&A, with the comments and questions of an imaginary investor in italics.

*What happened in markets so far this week?*

We have seen at least a short-term selling climax in [stock markets](#) and a quite possibly a buying climax in long-dated government [bonds](#).

*But this is a bear market, isn't it?*

It has been for some markets, particularly in the West, where financial and property related sectors have been extremely weak. The Wall Street leash-effect has dragged down all stock markets this month but some of these may be seeing no more than another sharp correction.

*The US economy and banking problems are awful, so what changed?*

Driven by fear, markets had become oversold and the Fed surprised investors with a 0.75% cut in the Federal Funds Rate.

*OK, but most commentators say that won't make any economic difference, and that the Fed and other central banks have little influence in today's financial world.*

How do they know? They make a theoretical point, which may or may not be objective, and it is at odds with decades of historical data. It seems logical to

me that those who control the monetary levers have enormous influence, for good or bad.

*Exactly! Surely the Fed is only stoking the next bubble, isn't it?*

Possibly, or possibly not - that depends on what happens over the next few years, not least in terms of ongoing monetary policy. Meanwhile, it is very unlikely to fuel another US property bubble anytime soon, although it will help to cushion downside risk.

*But surely it can only be inflationary, right?*

Not in the short-term although it may mitigate some deflationary trends in housing and consumer sectors. US inflation, and indeed much of the world's inflation today is mainly in the form of food and energy prices. This is a secular problem of supply and demand and not something that should be tackled by monetary policy. Unlike the 1970s, there is almost no wage inflation in the USA today.

*Returning to the markets, is your view that we have seen a selling climax confirmed by the OEX Volatility Index (VIX)?*

Yes, [VIX](#) peaked at 37 on Tuesday; the same level as in mid-August, and has fallen back to 28. However VIX has soared to higher levels in the [past](#), between 1997 and 2002, as you can see from this monthly chart.

*So, this might only be a selling climax, rather than THE selling climax, right?*

Yes, but not necessarily.

*How will we know, one way or another?*

There is a very practical way to determine this. Following a selling climax, I would give any upside the benefit of the doubt, unless we see a number of stock market indices close beneath the intra-day lows established on Tuesday and Wednesday. Meanwhile, I maintain that we have seen lows of at least near-term significance for the world's stock markets.

*Assuming the Fed's policy is correct, and I am sure you will agree that this is a contentious point, has the Fed done enough?*

Of course the Fed's decision is contentious, as is so much of what it has done in these difficult years for the US economy. Meanwhile, none of us can claim to be entirely objective on this subject but during the recent market meltdown many people came around to the Fullermoney view that the Fed was well behind the curve of events, in addition to its communications problems. I do not think the Fed has done enough and I do think it should cut rates by another 50 basis points on the 30th, as the markets have been anticipating. It would be ironic if Bernanke and Co repeated their October 2007 mistake, by assuming that a rally indicated it had done enough and that the risks were now evenly balanced.

*So you now agree that the US economy is in recession?*

The Fed's earlier prevarication and dithering certainly undermined confidence, increasing the risk of recession and pushing the stock market beneath its August lows.

*If confidence is low, who has done the buying to lift stock markets sharply in recent days?*

This week's firmer tone has been mainly due to short covering, plus a limited amount of bargain hunting.

*Following a technical rally, won't the bears return given the awful forecasts, and what would bring back investment demand?*

The bears will return if the rally is brief and if the short to medium-term downtrends for most stock market indices remain in force. We should expect additional volatility. However, investors' bullish expectations will increase if stock markets rally further in the short term, establish higher reaction lows, and then move above the initial rally highs, as everyone would then see short-term uptrends. Those awful forecasts you mention can also be viewed as a contrary indicator. Also, they may not be unbiased, especially if produced by firms that are heavily short and / or largely in cash and hoping for lower levels.

*Sure, we need to keep our eyes open regarding the objectivity or possible bias of any forecast, but speaking of objectivity, what about all those top formations shown by stock market indices?*

Absolutely - they confirm technical damage, encourage the bears, and remain a short to medium-term concern for any investor who is long and / or in a position to buy. For this reason a VIX reading of 37 this week is obviously not as decisive as 50 would be against the background of an even larger downward acceleration, which we may or may not see. No one knows for certain. However sentiment and oversold readings now point to a stock market rally. It will have to be a good one to neutralise technical damage that has occurred. Meanwhile, review the charts and you will see plenty of upward dynamics, including some upside key day reversals - for instance, the [S&P 500 Index](#) yesterday. Also, banks led yesterday's rally on Wall Street.

*OK, if I nibble as you have already done in Rio, the Hang Seng and Nikkei indices, what would you suggest?*

You might consider value plays, especially in markets where the biggest downside moves have occurred recently, as they could rebound on short covering in addition to bargain hunting. For instance, I scrolled through the Dow 30 last night. Some of those shares have seen big downward accelerations but not all are experiencing the same degree of fundamental problems. There are certainly big shorts in Western banks and property shares, in addition to some good yields. Note the potential weekly key for the [S&P 500 Banks Index](#), and the [FTSE 350 Real Estate Index](#) did not hit a new low this week and it has broken its downtrend.

To be continued.

## **January 25<sup>th</sup> State of the markets: stocks, government bonds, currencies & commodities (Part 2)**

This is a continuation of yesterday's review of markets from a technical, behavioural and fundamental perspective. It is in a discussion format, including Q&A, with the comments and questions based on a composite of what are often consensus views. These appear in italics.

*Returning to fundamentals, haven't markets been discounting fears of a significantly weaker global economy and even the prospect of widespread recession?*

Fear is the operative word. I believe that this month's sell-off has been much more about fear than fundamentals. Basically, investors lost confidence in the Fed, not least in terms of its falling behind the curve of events, as I mentioned before. The 0.75% cut on Tuesday surprised the market, especially those with large short positions.

Interviews from the Davos Summit this week have been revealing. The economists present, who mostly work for banks, are bearish. In contrast, CEOs of multinational companies were mainly bullish. I would pay more attention to the CEOs.

*So you believe in uncoupling?*

No. We actually have more coupling due to globalisation. A key difference this time is that the US is no longer the engine of global GDP growth. Moreover, the world economy is rapidly changing from having been unipolar to multipolar, as I have emphasised on many occasions, with GDP growth led by Asia and the commodity producing regions. Global growth is slowing due to well-documented financial problems in the USA, UK and parts of Continental Europe. However this is far from a disaster because it will only slow high growth rates elsewhere somewhat, reducing problems of overheating and lengthening the economic cycle in the process. If China's GDP moderates from over 11% to 8% or 9%, and if India's eases to 7% or 8%, that will still be very impressive, while reducing the need for monetary tightening in those two countries.

*If these factors reduced global inflation, will you become more optimistic about government bonds?*

No. As mentioned yesterday, we have seen a buying panic in long-dated government bonds in response to the banking related problems, falling stock markets and exaggerated fears for global GDP growth. The US 10-year Treasury yield fell to 3.3% earlier this week, which is less than the risk of inflation. People will almost certainly lose money in these bonds. For income, I would much rather hold higher yielding equities, particularly where there is reasonable dividend cover. A more conservative choice would be cash on deposit in higher yielding Asian and / or resources producing countries.

To be continued.

### **January 26<sup>th</sup> State of the markets: stocks, government bonds, currencies & commodities (Part 3)**

This is a continuation of last week's review of markets from a technical, behavioural and fundamental perspective. It is in a discussion format, including Q&A, with the comments and questions based on a composite of what are often consensus views. These appear in italics.

*I like your suggestions for yield but what about currencies? I notice that some banks are recommending the US dollar as a recovery candidate, not least because it is cheap on a purchasing power basis.*

The competitive pressures of globalisation ensure that no country wants a strong currency - a point often made at Fullermoney in recent years. No country has said that it would like its currency to appreciate. However some countries need a weak currency more than others and I have long said this was true for the USA. Yes, the dollar is cheap relative to other developed country currencies on a purchasing power parity basis. However this is not a hard fundamental if people are unwilling to holiday in the States or to invest there. On entering the USA tourists have been made to feel less welcome since 9/11. Given the economic problems, it is not immediately apparent why investors or businesses should rush to the USA, with the exception of SWFs, which have received very favourable terms when lending money to US banks.

Interest rates are a hard fundamental when considering currency investment and these are declining in the US, creating a further headwind for the greenback. Most countries with large current account surpluses are quietly diversifying away from USD, which remain in oversupply.

I do not doubt that banks would love to see a big rally for the dollar, so that they could short it once again at a higher level, and buy gold following a big setback. They may have to be patient on both accounts.

*OK, so what currencies do you like?*

For several years we have favoured currencies of countries with the best GDP growth rates. These are the Asian region, ex Japan, and exporters of resources.

### **January 29<sup>th</sup> State of the markets: stocks, government bonds, currencies & commodities (Part 4)**

This is a continuation of last week's review of markets from a technical, behavioural and fundamental perspective. It is in a discussion format, including Q&A, with the comments and questions based on a composite of what are often consensus views. These appear in italics and commence with a final question on investment currencies.

*I'm surprised that you would take that level of risk on medium to longer-term cash deposits in foreign currencies.*

Most of us feel comfortable with cash savings on deposit in our country of residence. However with funds in excess of our everyday requirements and held as a medium to longer-term investment, most of us have a wide choice. I think we need to question long established and conventional views on currencies or any other markets from time to time, especially if there is evidence of a significant fundamental change. With this in mind, and in assessing both risks and opportunities in what I have previously referred to as the Wobbly West and the Enterprising East, if the term "risk" is used to describe strong growth in GDP and corporate profits, and a growing current account surplus, then I'll have more of it please.

*OK, let's move on to commodities which have seldom been out of the headlines in recent years. Foods have been the one area where most people seemed to be in agreement during recent months, including Fullermoney. Is it still game on for the rest of the year and beyond?*

Agricultural commodities have certainly been the in-form sector in recent months, outperforming precious metals until the last week and also those most unlikely bedfellows, long-dated government bonds. However we need to be wary of a crowded trade, while taking our timing cue from the price action. Fullermoney maintains that all commodities are in long-term supercycle trends, in line with our Supply Inelasticity Meets Rising Demand theme of the last five years. Nevertheless the sector is always volatile, not least because of the cyclical versus secular debate.

Foods have had a big move, mostly led by the grain and bean complex, as you can see from these monthly semi-log charts of [wheat](#), [soybeans](#), and [palm oil](#) (less historic data available). Here are the arithmetic charts for additional perspective - [wheat](#), [soybeans](#) and [palm oil](#). Price acceleration, as we have certainly seen recently, is an ending characteristic of an unspecified duration, as we say at The Chart Seminar. The size of the acceleration suggests that short-term risks have increased considerably, and it would not be surprising to see a medium-term consolidation of gains. Meanwhile, farmers around the world will hope to profit from this strength by increasing plantings wherever possible. Weather conditions in the main growing regions are less predictable for 2008 but acts of nature usually contribute to price volatility. Where accelerated upward trends have occurred, short trades have a better chance of performing although it is usually prudent to wait for evidence of a downtrend.

On a longer-term basis, I maintain that the paradigm for agricultural commodities really has changed, due to increasing populations and middleclass prosperity in developing countries, leading to greater demand for protein, for which grains and soybeans are a key food source. There is additional demand from bio-fuels. All of this is occurring against a background of low carryover stockpiles from previous crops.

*Point taken, I will use technical stops with any of these overextended trades and if triggered, stay on the sidelines. Are there any cheaper and perhaps less risky agricultural commodities?*

That is a sensible strategy and this monthly chart of [sugar](#) is a reminder of what can happen following dramatic price acceleration. I would not expect the grains and beans to fall as much as sugar from its last peak, but one never knows. Meanwhile, sugar is currently in what I suspect is no more than a [short-term](#) consolidation within its recovery. Robusta coffee's recovery ([monthly](#) & [weekly](#)) is well underway but it has not accelerated recently and remains in a step-sequence ranging upward trend. Similarly, cocoa ([monthly](#) & [weekly](#)) has arguably only just completed its first step above the base formation. It is temporarily overstretched and as a general rule we prefer not to pay up for commodities. Setbacks within clear upward trends usually provide better buying opportunities.

Among agricultural commodities for industrial usage, cotton ([monthly](#) & [weekly](#)) continues to range upwards from its large base and there is a possibility that less of it will be planted this year as farmers seek to maximise profits in crops that have seen explosive upside moves. Lumber ([monthly](#) & [weekly](#)) is intriguing because the price is so low. The first sign of an upward dynamic should spark at least a respectable technical rally.

*I trust you will agree that industrial metals are in a bear market following their burst bubbles and in line with the global economic slowdown.*

I have heard this before over the last several years and there have been significant setbacks for the industrial metals, tin ([monthly](#) & [weekly](#)) excepted. However I think we need to review developments in an historic context and also in line with the same new paradigm that applies to foods above.

Briefly, industrial metals, illustrated here by copper ([monthly](#) & [weekly](#)), underwent a 21-year bear market until 2002, during which production capability deteriorated as miners were in survival mode. This coincided with by far the biggest demand increase, led by China, as the developing world built infrastructure. Additionally, a rapidly growing middleclass in these countries developed Western consumer habits. I maintain that these two factors are much more important over the longer term than a temporary global economic slowdown. The global infrastructure and consumption stories could persist for decades, albeit occasionally punctuated by recessions. Miners have increased production but not at the rate forecast by analysts due to cost increases, plus shortages of equipment and skilled workers. It is still often cheaper for miners to consolidate via mergers and takeovers, rather than develop new greenfield sites.

Meanwhile, copper's chart is an interesting and influential test case in the debate. We see the climactic acceleration to a peak in 2006, followed by a sharp reaction and right-hand extension top development (the Type1,2 & 3 hybrid as taught at TCS). This led to a downward acceleration, persistent rebound and subsequent ranging, all best seen on the weekly chart above. Needless to say, the question of whether this is an extended top formation or

a lengthy medium-term consolidation within a secular bull market, is extremely important for all industrial metals, not to mention the companies that mine them.

I'll continue to back the upside, provided the yearend 2007 reaction low is not taken out. Veteran subscribers may recall a number of lengthy medium-term consolidations, sometimes lasting for approximately two years, for individual metals and also some mining indices and shares. Currently, there are almost certainly more speculative shorts in the metal markets than leveraged longs. [Nickel](#) and [Zinc](#) are currently the most depressed industrial metals but have lost downward momentum in recent months. Downside breakouts from the current trading ranges are required to reaffirm weakness and offset current evidence of base formation development.

*Precious metals are much stronger and gold is heading for \$2300 and rising, just to get back to its 1980 high, adjusted for inflation.*

We remain long-term bulls of precious metals but this has become a crowded trade recently, so disciplined trend-running tactics are advised for leveraged positions. A point to remember when many people are talking about gold being "cheap on an [inflation-adjusted](#) basis", is that it was a genuine bubble in January 1980. Nevertheless it can still move considerably higher over the longer term on wealth creation in a fiat currency world. Meanwhile, watch out for acceleration which would set [gold](#) and [silver](#) up for another medium-term correction. We have seen some acceleration by [platinum](#) recently, in response to the South African power cuts which ought to be a temporary problem. Remember, when trading futures during the long-term uptrends for these instruments, it is better to buy following setbacks and use trailing stops as prices trend higher.

*Why have mining shares lagged so far behind the strength of bullion?*

Two reasons: the big sell-off in global stock markets has damaged sentiment generally, and investors are not convinced that miners will be able to reap the rewards of higher prices for precious metals. My recollection of the last cycle is that the South African miners did not reach their highs until well after gold bullion's peak in January 1980. However I cannot confirm this because our chart of the Philadelphia [Gold & Silver Index](#) only goes back to 1984.

*Lastly, what about crude oil?*

[Crude](#) remains in a secular bull market but you can see some acceleration on the way to \$100, although this is considerably less dramatic than surges for some other commodities shown above. Nevertheless it is likely that a medium-term correction of at least a few months is underway. A sustained break above \$100 will be required to eventually reaffirm the overall upward trend.

## January 15<sup>th</sup> Are the Subprime Losses Big?

My thanks to a subscriber for a very informative table from DB Global Markets Research, listing the USD value of global assets in various categories. It is posted in the Subscriber's Area but DB estimates the sub-prime and synthetic / CDO losses at \$400bn.

<b>Table 1. Are the subprime losses big?</b>	
<b>Total losses due to subprime cash &amp; synthetic/CDO: \$400bn</b>	
	Size (subprime losses in % of size)
Total asset-backed securities market	\$10.7 trn (3.5%)
Total financial assets of US commercial banks	\$10.8 trn (3.5%)
US GDP	\$14.0 trn (2.8%)
Global corporate bond market	\$17.1 trn (2.3%)
Global stock market	\$50.6 trn (0.8%)
Global GDP (in USD)	\$57.3 trn (0.5%)
US household net worth	\$58.6 trn (0.5%)
Total world financial markets	\$149.1 trn (0.2%)

*Source: DB Global Markets Research*

My view - That is serious money to you and me and some people think the total is \$500bn and will increase as the bonfire spreads to credit insurance. It is certainly a shock to the Western financial system, inviting numerous questions, including: Where will markets be in 12 months time?

A considerable portion of the immediate problem is the temporary paralysis of the Western banking system. This is slowly being resolved but recapitalisation takes time. Meanwhile, the losses are real and alarming, representing a shock to other sectors of the US and European economies, otherwise unaffected by the actual sub-prime related fiasco.

Psychological problems for corporations, consumers and investors are considerable because a year ago very few people had even an inkling of what was about to happen. The outlook seems grim, or has certainly been made to look so by an excited and emotional press. Therefore, for perspective, we should refer to the DB table:

The \$400bn of losses forecast is insignificant compared to items in the table, not least DB's calculation of \$149.1trn for total world financial markets.

However, the ongoing and more serious problem that has yet to be checked concerns confidence. The setback in stock market valuations since the sub-prime related problems broke is vastly greater than \$400bn.

Needless to say, governments and their central banks have a big vested interest in stopping the rot. This requires leadership, which has not exactly instilled confidence to date. However governments are crisis oriented and I assume that leadership in monetary, fiscal and psychological terms will improve over the next few months. This does not require a miracle - just common sense.

A year from now, and perhaps well before, I believe calm will have returned to stock markets which will be trading above today's levels, with Fullermoney's secular themes among the leaders. Western banks, at worst, should show clear technical evidence of base formation development. Meanwhile, most stock markets look as if they will move somewhat lower before they trend higher once again.

### **January 30<sup>th</sup> on the difference of opinion between CEOs and bankers at Davos**

Nick Train: "I Forgot More Than You'll Ever Know (About Them/Her)"

My thanks to Tony Smith of Brewin Dolphin Securities for this [report](#), packed with wisdom for investors, by Nick Train of Lindsell Train. The headline quote is by Sir John Templeton on stock markets and Cecil Null on a lost lover. Here is a brief sample:

The truth is that although macro-economics make compelling headlines, we do not invest in macroeconomics. We invest in corporations and, for the most part, we invest in corporations that have weathered macro-economic storms in the past and come out stronger on the other side. Listen to what the companies are saying about themselves, not what the City traders are saying about their share prices and the outlook becomes less threatening, even encouraging!

My view - I made a similar point about Davos the other day, saying the economists (employed by banks) were mostly bearish and the CEOs bullish.

I do not doubt that Stephen Roach and George Soros would be interesting dining company. However if I took their latest prognostications to heart, I would feel suicidal. I do not! Call me an insufferable optimist but I have seen the end of the world unsuccessfully forecast too many times to believe that I can improve on that record.

I commend Nick Train's report to subscribers, for its historical perspective and interesting review of value stocks, which you can assess in the Chart Library.

In conducting their own due diligence, subscribers will have various criteria for assessing shares. When bargain hunting following a stock market sell-off, in addition to value, look for relative performance. Shares that are outperforming

their respective indices, particularly since last week's lows, will either have superior fundamentals, or people will think they are a better story, which is almost as good.

Currently, I can only confirm that we saw a selling climax last week, establishing lows of at least near-term significance for many stock markets. Those lows will have to be successfully tested by indices, and followed by strong additional recoveries to confirm that sustainable floors have been reached.

Conversely, if we see closes beneath last week's intra-day lows by most leading indices, that would reconfirm the overall downward trends and we could expect a further slide.

Either way, there is improved value in the markets today and not least in Fullermoney themes. The main risk is that central banks remain behind the curve of events, further emboldening short sellers and causing more long-side investors to panic in a falling market.

Meanwhile, now is the time to identify bargains, in terms of fundamental value, confirmed by relative performance. In my observation over the last four decades, stocks that bottom out ahead of their indices following a bearish phase, and also show relative strength in the early stages of a recovery, usually outperform for at least the medium term.

### **February 4<sup>th</sup> 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.*)

#### **February 4<sup>th</sup> 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.

## February 6<sup>th</sup> 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.

### **February 7<sup>th</sup> 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.

### **February 8<sup>th</sup> 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.

### **February 12<sup>th</sup> Four recent news items that investors may wish to factor into their analysis of US market prospects**

First, a drama review. We had a repeat of August's shock and awe last month. Practically everyone expects a threepart (an American portmanteau word). George Soros has become the high priest of USA bashers, predicting a road to serfdom. US banks, issuing bearish reports on each other, propelled short selling on the New York Stock Exchange last month to its highest levels [since 1931!](#)

Even Asian investors have been quaking recently.

These are reasons enough for investors to despair of worldly goods and head fatally for the window ledge, except gentle reader, they are contrary indicators.

Let us now consider what some smart people are doing:

Monoline bond insurers meltdown? You have almost certainly heard about it but guess what - Warren Buffett wants to [assume](#) their liabilities. Banks are Devil's spawn, right? Well, that may be an exaggeration and Bill Gross of Pimco said "Citigroup, Bank of America and Wachovia Corp. were appealing", according to this second [item](#) from Bloomberg. Mortgage meltdown? Sure, but this is an election year, so look at Hank Paulson's [latest](#) effort. Lastly, Barton Biggs, who has seen a few market cycles said [yesterday](#) that the market is "at or very close to an important bottom." That remains the Fullermoney view.

OK, back to the practical, technical considerations. Remember the Fullermoney template: If the selling climax on 22nd January marked an important low, as Eoin and I have suspected, stock market indices need to encounter support near or above that day's intraday lows. There is some evidence that they are doing so today. This action needs to be followed by a further rally, sustaining a push above the very recent highs which many indices reached at the beginning of February.

That would establish short-term uptrends, defined by higher lows and higher highs. It would also indicate that the latest round of short selling had been more than offset by new buying from investors. Even in this event considerably more upside progress will be required to repair the technical damage and convince a frightened investment community.

Stock market indices need to break their medium-term downtrends and also push up well into their overhead trading ranges to offset the top formation implications of these patterns. This may sound like a big ask, given all the bearish talk and it would take time. But remember, the last really important technical development was last month's selling climax.

### **January 17<sup>th</sup> on unease regarding Bernanke and Paulson:**

"David, this is a splendid analysis from Lowenstein after 3 interviews with BB. It makes me feel very uneasy about him. You say he is learning on the job. The problem is not the learning but the unlearning which is sooo much harder.

"As Herbert Hoover was such a great engineer, drilled in straight logic, he became a horrible president. Now we have an a nice guy and great academic as Fed Chief steering markets, some of which he did not know to exist a few months ago, let alone understanding them.

"Furthermore, the other guy from GS, Hank Paulson, not as nice, makes me think too. His former company is shorting the hell out of the ABX - he proclaims everything "contained". Next comes this bungled from the beginning "Rescue of Citibank" and now the "Mortgage Farce". When he became Secretary of Treasury, supplanting poor-looking John Snow, one might have assumed he is one in the know, anticipating the future course of financial events. Now this looks to be monopolized by the GS trading book with the Administration being front-runned as always..... Going back in history the parallels to the last months of the Nixon days become apparent.

"I know, the market is a mob, and the mob may get 75 points on Jan 30 and run with it. But later they might reflect why they get this 75 or maybe even 100 points ("down the elevator"). They will have got it because the Administration panicked after Christmas - take a look at Fed Fund Futures since then - this is insider buying if I ever saw one.....

"Sorry for the long mail David, but you and I think confidence is so important. Looking at what is coming down the line in the US credit markets, the Bush - Paulson - Bernanke Team does not make me very confident at this stage."

My comment - Thanks for an interesting and relevant email, addressing concerns that many of us share.

However regarding Hank Paulson, call me naïve but I do not think that his statements and decisions as Treasury Secretary are influenced by Goldman Sachs' trading book.

I have a degree of sympathy for Ben Bernanke, who may feel that he seized the short straw in accepting chairmanship of the Federal Reserve. Nevertheless I have been critical of his leadership, or lack of a reassuringly firm hand. Some of the points that I have made over a number of months were also mentioned in the excellent, balanced New York Times [article](#) that you kindly forwarded. I commend it to all who are interested in what is certainly an important subject. The back history is also highly informative.

I will not review all of my criticisms and concerns about the Fed under Bernanke's chairmanship, as they are in earlier Comments and especially Audios, also referred to in Comment. However I will repeat a couple of what I regard as key points, which were not mentioned in the article.

In addition to remaining behind the curve of events, Bernanke and Co do not really appear to understand market psychology, at least when designing policy as a committee. Consequently investors have lost some confidence in the Fed, as your email and Wall Street's actions have reflected. The unsettling conclusion is that the Fed is dithering and following events, rather than anticipating or at least understanding and reacting quickly to them.

It was this situation that prompted me to previously paraphrase Oscar Wilde's memorable quote from *The Importance of Being Earnest*: To lose one market (housing) Mr Bernanke, may be regarded as a misfortune; to lose both (meaning the stock market as well) looks like carelessness.

Unfortunately, the Fed either forgot or ignored one of the oldest and best adages: "Raise interest rates like an escalator and cut them like an elevator." The logic of this should be obvious to any student of market psychology.

Since the so-called credit crisis emanating from the US became a headline news item, I have occasionally mentioned my own discomfort in making some forecasts on the assumption that the Fed would respond quickly and decisively. It has not and I am convinced that stock markets have suffered additionally and unnecessarily as a consequence.

However the Fed will catch up with events, hopefully in the next several weeks. There will also be a welcome bipartisan fiscal stimulus. Meanwhile, the US remains the epicentre of global risk and most stock markets are being pulled down by the Wall Street leash-effect.

There is currently no technical evidence that the current sell-off is over but some of the action is becoming climactic once again. This is stressful for those who are riding out the storm, even if they are invested in themes far removed from the US financial crisis. It is also an increasingly interesting time for those who are looking for buying opportunities.

**January 18<sup>th</sup> On what does it take for the markets to turn:**

"We have come down a long way and we do see some value; what does it take for the markets to turn? If past history is any clue, the seat of the pants

feel tells me that there are too many hopefuls around still. When everyone gives up, that's the time to buy; but I will have given up as well, won't I?"

My comment - Thanks for making some relevant observations, and with self-deprecatory charm. It shows us that you are able to recognise the difference between your analytical brain and your emotions, which is crucial but not that easy for any of us to do, except after the event.

Regarding your questions, on what does it take for the markets to turn, I partially covered this yesterday - for instance, bank shares need to stop falling. However we should also think about a catalyst for positive change. It could be that Bernanke and a US fiscal stimulus package unexpectedly leap from behind to in front of the curve, in Hollywood fashion, but few of us would predict that from this cast.

Arguably, markets are already somewhat oversold but perhaps not sufficiently to support more than a technical rally. Consequently we could see more climactic action, measured in part by the VIX Index ([monthly](#), [weekly](#) & [daily](#)) pushing above 30. The higher it goes - this is usually in the form of a brief spike - the more climactic and therefore sustainable the stock market's reaction low at that point would be.

As for "when everyone gives up", we have recently seen the strongest of the Asian growth / resources markets wobble, confirming additional capitulation. This is a time to remember that emotionally, we are our own best contrary indicator. It is usually not too good an idea to sell when we start to see blood in the street.

Meanwhile, some forced selling by funds is occurring due to redemptions. There are also leveraged shorts in the markets, promoting their cause with bearish comments. They will be the most aggressive buyers on the turn.

### **January 14<sup>th</sup> on gold**

Desirable tangible assets in finite supply have generally been a good hedge against not only the US dollar but all fiat currencies. However the relative price performance of these assets to each other is seldom constant and changes in line with fashion.

It is no secret that gold has been edging its way back onto the investment stage since 2001, in a move initially regarded with scepticism by most investors, but which has gradually attracted more participants, not least in recent months.

A relevant question is: How long will gold's uptrend last?

No one can know for sure but this 50-year chart of gold in US dollars, [adjusted](#) for CPI inflation, offers some perspective. Gold is experiencing another momentum move within this recovery but it would be premature to speak of a bubble.

Of course gold is not just rising in US dollar terms. Here is a long-term chart of gold in [Swiss Francs](#) and also gold in [Chinese renminbi](#). In fact, gold is appreciating against all fiat currencies, as you will be able to see in the Subscriber's Chart Library. Additionally, gold is currently appreciating against most investment assets, as you can see inversely on this chart of the [Dow divided by gold](#).

However no trend ever moves in a straight line for very long so we need to understand and monitor the current price action.

To see these most clearly, have a look at this weekly [chart](#) showing gold on a log scale. You will see a series of long, ranging consolidations, followed by momentum moves to the upside lasting several months. It is not unusual for trends to develop consistency characteristics for behavioural reasons. Of course they do not always do this so what I say below is only an attempt to guess as to a possible roadmap for the gold price over the next few months.

I suspect we are currently experiencing an approximate replay of the advance evident from September 2005 to May 2006. My guess is that the yearend 2007 consolidation evident in the \$800 region was the equivalent to either the pause just above \$500 in late 2005 and early 2006, or it could more closely resemble the consolidation mostly evident above \$550, before the final surge to the May 2006 peak.

If the former, we will probably see another pause before long, perhaps in the low \$900 region. If the latter, gold will probably accelerate higher without a ranging pause, on its way to another spike peak. Of course we do not know what all the influencing factors will be in the weeks and perhaps months ahead.

Assuming they remain mostly neutral to bullish, gold could form a series of sideways consolidations (steps) within its current medium-term trend. You can see three of these in the earlier advance culminating in May 2006. However speaking as someone who remains long, I would not like to see gold fall back into a lower trading range step. Also, I would not like to see a much larger, churning range, relative to what we last saw at yearend.

Meanwhile, my strategy consists of trailing stops, which I would hopefully tighten in the event of dramatic acceleration. I may do a bit of Baby Steps buy-low-sell-high trading with my futures positions, as I have with silver. When the current momentum move ends, I would expect no worse than another medium-term consolidation within what I maintain is a secular bull mark

### **February 12<sup>th</sup> Merrill Lynch substantially raises gold prices forecast, ups silver too**

This is an interesting [article](#) by Dorothy Kosich for Mineweb. Here is the opening:

Citing broadening investor demand, a weak U.S. dollar, record oil prices and ongoing geopolitical tension, Merrill Lynch Monday substantially raised their

2008-2012 gold forecasts, while also predicting increased silver prices.

Research analysts Michael Jalonen and Jeffrey Schok said they expect gold to average \$925/oz this year and \$1,000/oz in 2009 (up from \$750/oz and \$800/oz respectively). They raised the long-term gold price forecast from \$600/oz to \$650/oz, beginning in 2013. "Due to higher forecasts for the 2008-2012 period, our 10-year average gold price has jumped from \$655 to \$800/oz," they said.

"Notwithstanding the possibility of short-term strength in the US\$, higher gold prices should be supported by positive supply-demand fundamentals including stagnant mine production and robust jewellery demand in emerging markets, in our opinion."

My view - There is an element of catch up in these forecasts but subscribers may be interested in some of the comments on gold mining shares.

At Fullermoney, we remain long-term bulls of precious metals but we are also becoming more cautious regarding medium-term prospects. Throughout their bull move commencing in 2001, precious metals have been prone to medium-term (multi-month) advances, usually led by platinum, which end in acceleration amidst a crescendo of bullish forecasts and price extrapolations.

Peaks are followed by sharp reactions within the long-term upward trends, and then many months of ranging in a new support building process. During this phase investors become despondent regarding gold's prospects and forecasts for all precious metals are downgraded, only to be raised again in the latter stages of the next advance.

I have illustrated these medium-term cycles within the long-term uptrends on many occasions and they are best seen on semi-log scales. Another look could be timely: platinum ([monthly](#) & [weekly](#)), gold ([monthly](#) & [weekly](#)) and silver ([monthly](#) & [weekly](#)).

This sequence of breakout, advance, acceleration, sharp reaction and ranging until the next upside breakout will not always characterise price patterns for the main precious metals. However it has been observed and also become self-feeding for a number of years. It will end when something changes the behaviour pattern of the main participants.

Meanwhile, platinum's acceleration and the overall strong upward bias since last August suggest that we are now at a late stage of this medium-term advance. Tactics, particularly for futures traders, should be particularly disciplined at this stage of the medium-term cycle. It is impossible to know exactly how and when this leg of the uptrend will end but the first clear downward week for platinum could be an early warning.

I do not agree with Merrill Lynch's view concerning "robust jewellery demand in emerging markets", continuing as prices rise. This [article](#) mentioning that Indian housewives have been cashing in recently is a warning. They have a

much closer relationship to gold than most Westerners, and therefore an innate understanding of its price cycles.

Gold mining shares are unlikely to uncouple from bullion's directional moves but they have lagged [recently](#) due to the weak tone of global stock markets. Consequently mining shares could be marginally resistant to the next medium-term setback in bullion, provided equities are firmer generally. My recollection (veteran subscribers may have more accurate memories) is that gold shares did not peak until several years after bullion's bubble high in 1980. However I lack the historic data for gold shares to prove or refute this contention.

### **January 24<sup>th</sup> on industrial metals:**

The last few weeks have seen a large number of mining shares being hit with a wave of selling pressure, seeing a number fall back by a third and some even more than that. This has been for a variety of reasons, but chief among these has been the perception that the global economy will move slow sharply. The corollary is that metal prices will collapse and miners' earnings will plummet. .

To determine if this theory holds water it might be instructive to look at metal prices.

In China, [aluminium](#) prices have been declining since their accelerated peak in 2006 and have returned to the top of the base. While it shows no immediate evidence of rallying, it did fail to break down into the base in November and would need to take out those lows to question recovery potential. On the LME, [aluminium](#) tested the bottom of the two-year range again on Tuesday but is now rallying from that area. This looks like basing activity and would need to sustain a move below \$2400 to question that conclusion.

[Copper](#), traded in Shanghai, remains in a medium-term correction following the spectacular acceleration in early 2006. It recently tested the bottom of its range on an intraday basis but rallied well and has pushed back above the 60,000 yuan level. It would need to sustain a move below the recent lows to question scope for further higher to lateral ranging. On the LME, [copper](#) continues to hold above the December lows in what looks like a failed break below \$7000. It would need to sustain a move below that level to question potential for further upside.

[Zinc](#) remains in an overall downtrend but has been losing momentum since November. It recently retested support near \$2100 and would need to sustain a close below that level to question scope for further base building which should include some higher to lateral ranging.

[Lead](#) fell precipitously, having topped out near \$3900, but that accelerated trend lost momentum near \$2500, where it has steadied for the last six weeks. It would need to sustain a move below that level to reaffirm the overall downtrend.

Nickel was one of the best performers of any commodity in 2006, but gave up much of its gain in 2007, before finding support near \$25,000. It has been ranging above this level for the last five months and would need to sustain a move below it to question potential for additional base building.

Tin remains in an overall uptrend and has so far not succumbed to the selling pressure experienced by the other industrial metals. A sustained move below \$16000 would be needed to signal the onset of a more bearish environment but in meantime the upside can be given the benefit of the doubt.

From these charts we see that most metals have experienced some quite severe selling pressure over the last eighteen months but have steadied in the last few months and were untouched by the recent panicky market activity in other sectors. This indicates to me that we have probably seen the worst of the selling in these markets and that they are in base building phases prior to reasserting their overall uptrends. They would need to sustain breaks below their reaction lows to question this theory.

Both metals and mining equities are priced on future expectations. Miners have been sold recently because of concerns about the global economy and perhaps because they had surged ahead too quickly and were in need of a consolidation. Metals were also in need of a consolidation, although in the cases of zinc and nickel this has been quite severe. We don't get to choose how big a reaction will be and these markets are characteristically volatile. However both have recently found support and throughout this secular bull market, have been best bought following corrections.

### **January 25<sup>th</sup> on South African power outages:**

"My wife and I having just arrived in South Africa on our annual winter migration noticed one very distressing aspect straight away. Rolling power cuts lasting sometimes 4 hours at a time twice daily. I had not realised until now the degree of under investment, since the ANC government took control, in the power industry and the matter will not be rectified anytime soon.

"Already some cities are totally clogged with traffic as all the traffic lights are off during an outage. More importantly it is beginning to affect the production of gold from some of its most important mines. A bull point for the metal if ever I saw one. Platinum group metal production will also suffer.

"A rather macabre joke is doing the rounds at the moment. 'What is the difference between South Africa and The Titanic?  
Answer, The Titanic sank with the lights on.!!!"

My comment - Thank you for this informative email, providing a firsthand perspective of what is occurring. It's been more than five years since I was last in South Africa. It was changing remarkably then and I find it hard to be pessimistic about such a beautiful place but governance is everything from an investment standpoint and the ANC need to move past populism in order to make some long-term development decisions.

This [article](#) by Lawrence Williams for Mineweb covers some of the same topics you mention, as the power outages are damaging production in the mining industry. Here is the article in full:

The power crisis across Southern Africa, and in South Africa itself in particular, has led to the temporary shutdown of all the latter country's major gold operations. Power failures at major mining operations, particularly given the depths of the operations, would be dangerous in that hoisting capacity to bring the miners out of the workings, which would be necessary because of possible ventilation breakdowns, would be severely limited.

South African state electricity provider Eskom has reportedly told the mines it cannot guarantee the continuity of electricity supplies and, as a result AngloGold Ashanti, Gold Fields and Harmony have had to take the decision to shut down their operations until power supplies can be guaranteed.

While South Africa is still the world's largest gold producer, although it is being overtaken by China, any continued disruption of operations would have a significant impact on world gold supplies.

South African gold mine stocks fell on the news, and the disruption to supplies was also a factor in the gold price rising to new highs this morning where it reached just on \$920 at the time of writing.

The power crisis will also have a similar impact on other sectors of the mining industry and platinum supplies will be particularly vulnerable with the country being by far the world's largest producer of platinum group metals. The world's two largest producers., Anglo Platinum and Impala, have also had to shut down their operations and smaller operators will be following suit. World platinum prices have also reached new records as a result.

The crisis is a major blow to the South African economy as well as to the country's miners.

At the moment there is no indication as to how long the closures will continue, but comments from South Africa suggest that the situation may get worse before it gets better. Watch this space!

The JSE [Gold](#) and [Platinum](#) indices have so far failed to move upwards to new highs in line with their respective metals. On occasion these indices have been hampered by a strong Rand but this is not the case here. The companies will continue to benefit from the secular bull markets of precious metals over the long-term but these power cuts could do some damage to their bottom lines in the short term. If this turns into a protracted situation, funding could potentially become an issue for some companies.

In the meantime, this is a bullish outcome for gold and platinum in particular. [Gold](#) broke upwards today and it would have to sustain a move below \$850 to question scope for further upside.

[Platinum](#) is now accelerating. On past occasions when it has moved upwards in this fashion, it has set itself up for a sharp correction, while remaining in an

overall uptrend. This occasion may have a similar outcome but for the moment, a downward dynamic would be needed to check momentum beyond a brief pause.

### January 18<sup>th</sup> Economist Cover: "The End of Cheap Food"

To be fair, our emotions (often mistaken for an analytical reaction) cause us to be our own best contrary indicators. However The Economist does have a reputation for producing some memorable contrary signals with its covers, some of which have been cited in these pages. Have they done it again with this one announcing, "The End of Cheap Food"?



Not quite, at least not yet, as this cover appeared a month ago and food prices have subsequently moved higher. However, this chart of the S&P GSCI Agriculture Official Close [Index](#) shows that prices have accelerated in the last few months. One sees the same in this chart of the unweighted Continuous Commodity [Index](#) (Old CRB), where foods will have made most of the recent running.

What are the implications?

The message, I believe, is that agricultural commodities have become a very crowded trade recently. Practically everyone is bullish and they have been the in-form momentum trade for several months, easily outperforming everything else. Consequently, as a sector, agricultural commodities are becoming susceptible to some mean reversion in terms of the moving averages shown above. However I maintain that the long-term outlook is still bullish, for all the reasons of supply inelasticity and particularly rising demand, previously mentioned.

### **January 30<sup>th</sup> CRH: An international stock market gem from Ireland**

Eoin and I were talking about [CRH](#) today, as it fits my criteria above, in terms of value and recent relative strength. CRH, which is also listed in London and the US, is the world's fourth largest manufacturer of cement. Following a significant fall, it now sells at an historic PER of 11 and an estimated PER of 10, while yielding 2.25%, according to Bloomberg.

As a cement manufacturer operating in 19 countries, CRH is an important player in one of Fullermoney's favourite long-term investment themes - global infrastructure. Technically, CRH has recently outperformed Ireland's [ISEQ Index](#) and clearly shows evidence of base formation development. I expect it to be a leader in the next stock market recovery.

Full disclosure - Neither Eoin nor I own CRH, but it is one of many interesting investment prospects that are becoming available. As veteran subscribers know, with a large and diverse subscriber base, we do not recommend, as it would be a case of recommendations for whom? Instead, we tell you exactly what we think, and why. We also tell you precisely what we do with our own money.

I offer CRH as a template for recovery candidates, indicated not least by recent relative strength, which I think we should all be looking for.

### **January 31<sup>st</sup> Japan: Land of Rising Possibilities or Endless Disappointments?**

My thanks to a subscriber for an interesting [article](#) by Vlad Signorelli, with a slightly shorter title. Here is the opening:

Japan's top political party, the Liberal Democratic party (LDP), may be on a bull hunt. Specifically, a group of LDP policymakers including former Prime Minister Shinzo Abe and ex- Finance Minister Koji Omi are assembling a raft of fiscal policy prescriptions to push the Nikkei back to 18,000 from its current level of 13,400 - almost a 34% increase. Put another way, a faction of Japanese policymakers in the LDP is now intent on restoring investor confidence, which has suffered immensely since peaking during July 2007, when the Nikkei traded at 18,002.

By grounding the discussion of fiscal policy to the Nikkei's performance, the LDP is elevating the market as the ultimate test of policy merit, which is a very helpful way of orienting the policy debate. Indeed, this may be the only way to

get Japanese policymaking out of the thrall of zero-sum thinking -- where every tax cut must be offset by a tax increase or a spending cut --and into a more dynamic setting, where it is understood that faster economic growth and increased production often mean increased tax revenues.

This does not mean that the LDP has suddenly embraced the supply-side doctrine of the Laffer Curve, but latest indications are that some of these policymakers may be picking up the scent and heading down the trail. Among the most interesting proposals being reported by Bloomberg is the recommendation to abolish the taxation of capital gains and dividends. LDP legislators would like such an exemption to be in place temporarily, that is, until the Nikkei reaches 18,000. But they would like to expand existing exemption levels -- Y5million for capital gains and Y1million for dividends -- permanently. Similar to President Bush's 2003 tax cuts, which temporarily reduced taxation on capital gains and dividends and thus helped the U.S. economy out of the post-9/11 economic downturn, the LDP's suggestions could have a similar salubrious effect and breathe new life into the Nikkei, reinvigorate the economy and reverse the LDP's political decline.

My view - Interestingly, two countries are targeting their stock markets at this time - the USA and Japan.

This only occurs during a perceived crisis. The Fed is scrambling to catch up with the curve of events, which had been deteriorating rapidly as every warm body realised, except perhaps on the FOMC until very recently. Rate cuts of 125 basis points in eight days, send a loud message, although not everyone interprets it the same way, naturally.

For instance, some believe that the Fed is panicking, rather than finding its way, albeit belatedly. Others fear it is a sign that the Fed knows something we don't - risible, surely, but it is often mentioned. Has anyone suggested a desperate cry for help? More favourable assessments range from too little too late, to relief that the Fed has been provoked into action. Naturally, traders with the biggest short positions say that neither the rate cuts nor the stimulus package will work.

We have only heard talk from Japan so far, including the publicised proposals mentioned in the article above, and it is certainly not taking place behind closed doors.

I will leave high-minded discussions regarding the morality and long-term economic efficacy of the Fed's actions, or Japan's latest policy discussions, to others. I am more concerned with mundane issues such as the likely effect on stock markets.

Having been provoked into this latest rate-cutting action, the Fed will persist until it has succeeded. Success in the Fed's view can now be defined as restoring a 'feel good' factor by stemming the stock market decline, and ensuring that a recession is either avoided or short-lived.

Given the Fed's slow start, this latter objective would be particularly challenging, except that it will have support from powerful allies. The White House and Congress have already pitched in with a stimulus package. Much more importantly, they will agree on massive fiscal spending programmes.

In other words, if the consumer can't spend or won't spend, and banks won't lend (I've intentionally exaggerated both points to include the consensus view), the government will embark on massive pork barrel schemes, which will be popular with voters.

From an investment perspective, I would not worry too much about the inevitable delay before intention is turned into fiscal spending action. The stock market is a discounting mechanism.

Japan's stock market was a huge disappointment last year and it suffered a draught earlier this month, in line with global equities. Understandably, many investors are discouraged by this poor performance. They may have cause to cheer before long.

The last time Japan's politicians targeted the stock market was in 2Q 2003. Looking back on the bull-run that followed, one might conclude that conditions are less auspicious today. Only because time and a good result inevitably blank out memories of what proved to be unjustified concerns.

In 2Q 2003, serious people feared that we might be nuked by Saddam or even Bin Laden, and that a slide into deflationary depression was distinctly possible. Sentiment is similarly dire today.

I do not wish to sound complacent but the world is full of problems, great and small. Investor sentiment has always been characterised by pendulum swings between manic and depressive. The inexperienced, and those who mistake their emotions for analysis, buy at the manic tops and sell at the depressive lows. We can do better than that.

Japan's stock market is interesting today. However it is a global beauty contest, as Eoin and I are fond of saying. Therefore we need to look at the charts to see what would improve Japan's allure.

The [Nikkei's](#) action was as climactic as any recently. Note the downward acceleration and tail last week, proximity of the probable support commencing near 12,000, and overextension relative to the MA. [Topix](#) is very similar. The [Topix Banks](#) Index peaked earlier (the warning) and had a bigger fall. However it has been losing downside momentum since last August.

Lastly and possibly most importantly, note the 2nd Section Index ([weekly & daily](#)). It also provided an early warning, accelerating to a peak confirmed by a dramatic weekly key reversal, followed by some right-hand top formation extension. The importance of TSE2 is that it also led in 2003, because many of Japan's best valuations were in the Second Section, as is the case today. More recently, TSE2 accelerated lower and note the overextension relative to the MA.

In conclusion, these are important, climactic ending signals. However the recent lows for these indices do need to hold, to indicate that we have reached a sustainable floor, rather than a penultimate low or worse. Personally, I will always give the benefit of the doubt to what is clearly climactic action, provided the lows hold. I should add that these charts cannot support more than technical rallies at present. However a ranging recovery, ideally led by TSE2, would build support as it progressed. Japan has not looked this interesting since 2Q 2003.

### February 13<sup>th</sup> on CDS spreads:

"I was sent this by a friend. What you make of it?"

"Please take a look at the attached. This index is used as an indication of how credit spreads are behaving in Europe. So what the chart is saying is that credit spreads continue to widen in Europe across a range of instruments, the composition of which I am not entirely clear. It's a good indication of risk appetite in the credit markets - the fact that spreads have continued to widen despite the ECB's liquidity injection tells you banks are not borrowing from the central bank to lend, but borrowing because no other banks want to lend.... and they need to borrow to shore up their balance sheets! Is there something messy going on?"

My comment - Thank you for this interesting and useful synopsis. The members of this Index change every 6 months so it is difficult to be certain which constituents have been added and which remain. Resident bond guru, Mark Glowrey, of Investors Intelligence tells me that the Crossover Index is made up of troubled credits which are at risk of crossing over from one rating to a lower one, so it will generally paint a gloomier picture than might otherwise be the case. It is certainly true that financial credits, particularly those which are leveraged remain under pressure and the members of the Crossover index bear this out, with Ineos Finance, Basell ASF, and ONO Finance being the only members trading at a spread of over 1000bps.

Something messy is going on but this is no surprise. The ongoing problems in the credit markets are widely known. What should also be mentioned is that spreads in cash generative businesses such as resources continue to fare much better. Spreads of Libor over government rates continue to contract which suggests that banks are starting to lend to one another again but it will take time for confidence to return.

We have enjoyed a period when the perception of risk, across asset classes, was very low and have entered a period where the perception of risk is being adjusted higher. Charts of the VIX and Swap Spreads show upward breaks from multi-year bases which is indicative of an environment where risk has a higher premium. There is an argument that risk premiums were too low over the last few years and what we are seeing now is more of a normalization of risk perceptions rather than anything more sinister. I have to admit to having some sympathy with this view.

## January 15<sup>th</sup> on access to Middle Eastern and North African markets:

"A question for the Fullermoney brain trust:

"Is anyone aware of an exchange-traded investment vehicle that an individual investor could utilize to get exposure to the Middle East and North African markets? The markets of greatest interest at this juncture are Abu Dhabi, Dubai, Jordan, Saudi Arabia, Egypt, Tunisia, and the like. My broker doesn't trade those countries, so I'm looking for alternatives.

"(Unfortunately, the US-listed ETF "SPDR S&P Emerging Middle East & Africa" is very heavily weighted to South Africa, with just a little bit in Israel and Egypt.) I'd be grateful for any guidance. Thanks!"

My comment - Thank you for this email which I'm sure is also of interest to other subscribers. Most of the funds investing in this area are listed in the Middle East so they may be quite difficult for retail investors to access. A number of funds are listed outside of this region and can be found in the Emerging Europe, Middle East and Africa section of the Chart Library.

The [Saudi Arabia Investment Fund](#) is domiciled in Guernsey, denominated in US Dollars and according to Bloomberg has a management fee of 1.75%. I could not find details of any performance fees or opening charges via the web. It has tracked the performance of the Tadawul index reasonably well since inception. Also see Comment of the Day on [December 11th 2007](#).

The [FIM Sahara Fund](#), listed in Finland, invests in South Africa (38%), UAE (19%), Egypt (10%), Kuwait (6%) and Qatar (5%) and charges a 2% hurdle, 3% management fee and 2% redemption fee. It remains in an overall [uptrend](#) from inception more than a year ago and would need to sustain a move below 13.50 to question the integrity of the move. Also see Comment of the day on [February 21st 2007](#)

The [Mango Capital Fund](#) is listed in the Netherlands and invests in 24 different countries but the top five as of December were Egypt, UAE, Pan Africa, Nigeria and Qatar. This fund invests right across the African continent as well as the Middle East, so it may be outside the remit you were referring to, but I include it because of its performance. It is up [60%](#) since August. It charges a redemption fee of 1.5% after 12 months, 10% before that time a management fee of 2% and a performance fee of 20%.

As with any fund mentioned in Fullermoney, investors should do their own due diligence before investing.

## January 18<sup>th</sup> more on Middle Eastern markets:

Middle Eastern markets have moved to relative outperformance in a clear case of those that are last shall be first and vice versa. Many of these markets soared to incredible heights in 2005 led by Saudi Arabia and lost more than 50% of their value in the ensuing correction. Generally, markets such as Oman and Bahrain which were late to open stock markets participated less in

the accelerated ending and are benefiting now by leading the region upwards. Many western investors who would never have thought of investing in this area are now considering it because of its relative performance. However while this is understandable, the region does not come without its own quite distinctive risks.

The Middle East has only opened stock markets comparatively recently and the region generally is hardly a paragon of either civil or financial governance. It has become a mantra at Fullermoney that governance is everything in markets; the West is no exception here. So I would urge investors to thoroughly undertake their own due diligence before considering such an investment. In the meantime these markets are performing, buoyed by firm oil prices and a willingness by the oligarchy to invest in badly needed infrastructure for burgeoning populations.

The [Saudi Arabian](#), [UAE](#), [Lebanon](#), [Jordan](#) and [Qatar](#) all share a similar pattern where they accelerated to highs in late 2005 and early 2006, fell precipitously and are now in varying stages of recovery below the prior high. They would need to sustain moves back into their base building ranges to question potential for eventual tests of those highs.

[Oman](#) ranged between 2005 and mid-2007 but has been in an impressive uptrend since breaking upwards. This trend has been gathering pace recently. This is a warning signal that it is getting overextended in the short-term and is approaching the roundophobic 10,000 level. However it would need to break the progression of higher lows to indicate more than temporary resistance at that level.

The [Egyptian](#) market has been one of the regional leaders and was one of the first markets to recover its highs following an aggressive sell off in the first half of 2006. It remains in a consistent uptrend although it is approaching the roundophobic 100,000 level which may offer an area of resistance. However it would need to break the progression of higher lows to indicate more than temporary resistance at that level.

The [Kuwaiti](#) market broke upwards from its relatively shallow reaction in April 2007 and consolidated the move for most of the year. It broke upwards once more in early January and would need to sustain a move below 12,000 to question potential for further upside.

## **February 8<sup>th</sup> 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 than 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.)

### **January 16<sup>th</sup> on using the Preset function in the Chart Library:**

"Since the recent (very welcome) upgradation of the charts' options, I have been having some problems; perhaps I am not doing some thing right!

"1. Earlier, the various technical analysis options such as RSI etc. that I would have selected, remained on the charts undisturbed until I changed them. Now, I find that quite often, when I revisit the chart, they have disappeared and I have to again input them. Pressing the 'save' sign also does not help.

"2. Earlier, if I selected say RSI on the daily chart, it would appear automatically on the weekly chart. This does not happen now.

"I shall be grateful if you could point out what I need to do in the new system."

My comment - Thank you for alerting us to your difficulties as I'm sure you are not alone. The reason for the change is that we had to make some decisions about how the Chart Library would function when we introduced the Presets functions to ensure it worked logically.

Your preset functions can be accessed from the drop down menu in the light grey bar at the top of the page. The default settings in this menu are P&F, Candlestick 1-yr daily, Candlestick 5-yr weekly, Candlestick 10-yr monthly and Candlestick 20-yr monthly.

To add you own preset functions to this list. Choose any chart you wish, customise it however you want using the various options in the Charting tool. (The Charting tool is located in the charcoal bar above every chart.)

Before hitting Apply, hit the Save button at the top of the pop-up window, give the preset a name and hit OK. Now hit Apply and refresh the page. You will see that this preset has been added to the dropdown at the top of the page.

For the example you mention, I would suggest setting up one Preset for daily charts with a RSI and another for Weekly charts with an RSI. You'll only have to do this once and you'll always be able to apply them to every chart subsequently.

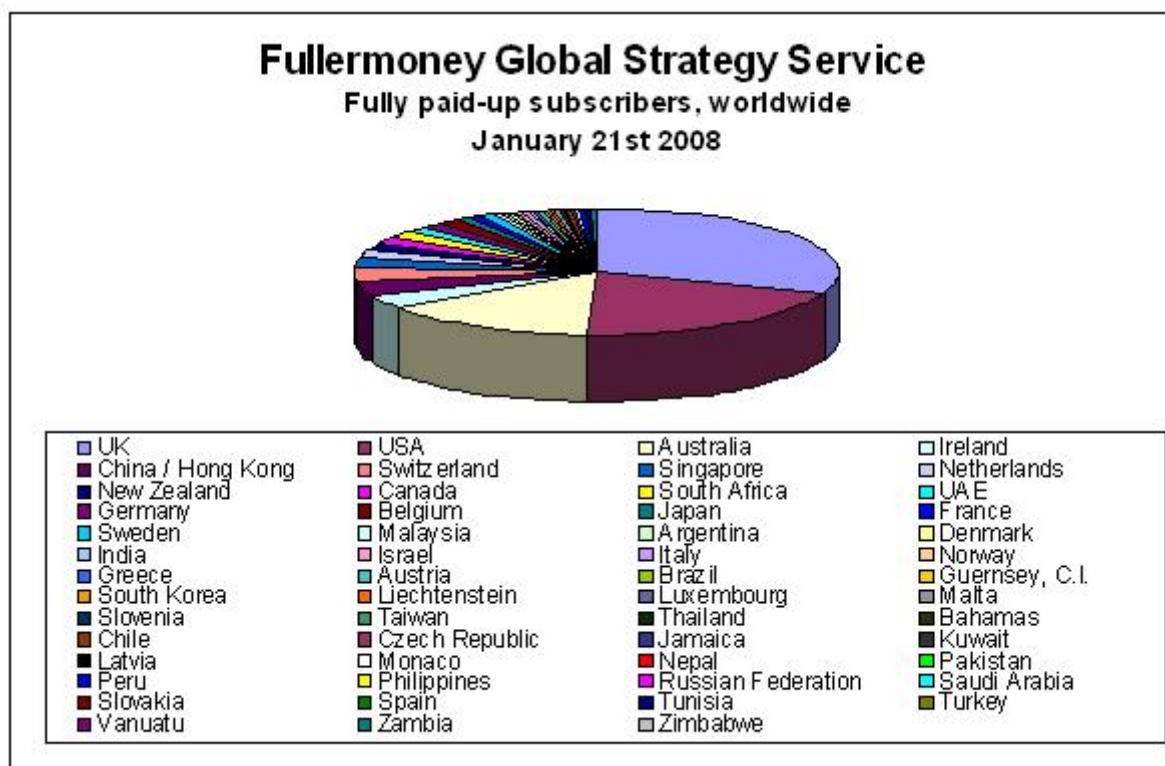
When you select either one of the default presets or one of your own customised presets, it will override whatever you have been looking at previously. This is why the RSI disappeared when you clicked on the weekly option.

### January 21<sup>st</sup> Where do Fullermoney fully paid-up subscribers live?

We last compiled these statistics on June 8th when we had subscribers from a total of 54 different countries, with just over 90% represented by 15 of them. Since then we have grown by 13.29% and the number of countries has increased by two, with subscribers joining us from Latvia, Peru, the Philippines and with one from Gibraltar departing.

Today, those same 15 countries make up 92% of our total subscribers. However there has been some significant re-ordering of the rankings. Ireland which moved from 9th to 6th in June has now advanced to 4th position. Switzerland has dropped to 7th.

In descending order the new ranking: United Kingdom, United States, Australia, Ireland, China/Hong Kong, Switzerland, Singapore, Netherlands, New Zealand, Canada, South Africa, UAE, Belgium, Germany and Japan. Subscribers from anywhere else are also most welcome!



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