

Fullermoney *Highlights*

Global Strategy and Investment Trends compiled by Eoin Treacy

www.fullermoney.com

19th March 2008

David & Eoin's personal portfolio trades	Page 2
February 14 th on market cycles	Page 4
March 18 th Citigroup's Global Equity Strategist Testing the Bull	Page 5
February 14 th S&P Performance After 5% Intraday Rise	Page 7
March 12 th Investors Intelligence Mike Burke and John Gray on Advisors Sentiment	Page 8
February 25 th On the S&P following negative rates	Page 9
March 13 th on coping with tough times	Page 9
February 29 th On the USA and economic decoupling	Page 11
March 10 th on listening to CEOs versus bankers	Page 12
March 11 th Fed to Lend \$200 Billion, Take on Mortgage Securities	Page 15
March 14 th Financial Times Intervene to slow the dollar's decline	Page 16
February 18 th The Debt Delusion	Page 18
February 21 st on credit market conditions	Page 20
February 25 th On credit conditions	Page 21
March 3 rd Marc Faber What's Ahead in 2008	Page 22
March 6 th Credit Swaps Thwart Fed's Ease as Debt Costs Surge	Page 26
March 6 th Filtering the S&P 500 sectors indices	Page 27
February 26 th Nasdaq shares a technical health check	Page 28
March 11 th On Topix PER and valuation contraction	Page 29
March 11 th Filtering the Nikkei 225	Page 31
February 19 th on Australia	Page 32
February 25 th On analysing and trading silver	Page 32

February 27 th Industrial Metals Review	Page 34
February 28 th Metal futures backwardations or contangos	Page 36
February 29 th Uranium Market Outlook on essay on commonality	Page 38
March 7 th on platinum	Page 41
February 28 th The Ethanol Bust	Page 42
March 6 th on food speculation / investment becoming a political problem	Page 43
March 7 th on the performance of grains relative to meats	Page 44
March 17 th Commodity price headlines again today but this time for not maintaining record highs	Page 47
March 14 th Which companies pay reasonably high yields and can cover their dividends?	Page 49
March 17 th on UK listed high yield funds	Page 50
February 15 th Can Chen Zhi save the world?	Page 51
March 18 th China to Take `Forceful' Steps on Inflation, Wen Says	Page 52
February 27 th on the currency peg used by many GCC countries	Page 53
March 6 th World Equity Index Valuations Tables	Page 54
February 29 th Chart Library Filter Live!	Page 54

New Positions in Personal Account Open/Closed			
David	Silver	Long 14/02 \$17.455 May08	
	Hang Seng	Long 15/02 23439 Mar08	
	Lumber	Long 15/02 \$244.48 May08	CL 15/02 \$222 Mar08
	Corn	Long 15/02 \$5.2335 May08	CL 15/02 \$5.10 Mar08
	Silver		CL 15/02 \$17.17 May08
	US 30yr	Short 15/02 117.12 Mar08	50% increase
	H-Shares	Long 19/02 13879 Feb08	
	H-Shares	Long 19/02 13860 Feb08	
	JGB	Short 19/02 137.26 Mar08	
	Natural Gas	Long 19/02 \$8.969 Apr08	
	Eurobund		CS 19/02 116.25 Mar08
	Nikkei 225		CL 20/02 13635 Mar08
	Nikkei 225		CL 20/02 13550 Mar08
	Nikkei 225	Long 20/02 13435 Mar08	

	Nikkei 225 Hang Seng Gold Silver Nikkei 225 Nikkei 225 Gold Gold Gold Corn MSCI Singapore Silver Silver Silver US 30yr H-Shares Dax Natural Gas US 30yr Dax Silver Gold Gold Silver JGB Gold Gold Gold Gold Gold Gold Gold Wheat Wheat	Long 20/02 13455 Mar08 Long 25/02 \$943.35 Apr08 Long 25/02 \$18.18 May08 60% sold Long 27/02 \$19.045 May08 Short 27/02 114.886 Jun08 Long 27/02 13913 Mar08 Short 27/02 6932 Mar08 Long 04/03 \$987.85 Apr08 total position closed Short 10/03 139.506 Jun08 Long 12/03 \$981.15 Apr08 Long 12/03 \$980 Apr08 Long 12/03 \$978.95 Apr08 switched from one account to another for 24hour stop Long 14/03 \$1000.65 Apr08 total position closed Long 25/02 1125.5¢ May08	CL 20/02 23536 Feb08 25% increase CL 25/02 13923 Mar08 CL 25/02 13920 Mar08 CL 26/02 \$935 Apr08 CL 26/02 \$931 Apr08 CL 26/02 \$930 Apr08 CL 26/02 \$5.35 May08 CL 26/02 381.9 Feb08 CL 27/02 \$19.50 May08 CL 27/02 \$19.35 May08 CS 27/02 116.04 Mar08 CL 27/02 13905 Feb08 CL 27/02 \$9.069 Apr08 CS 28/02 116.21 Jun08 CS 28/02 6917 Mar08 CL 03/03 \$20.60 May08 50% increase CL 04/03 \$975 Apr08 CL 04/03 \$20.10 May08 CS 10/03 139.54 Mar08 CL 14/03 \$1000.5 Apr08 CL 17/03 \$1004 Apr08 CL 17/03 \$995 Apr08 CL 26/02 1175¢ May08
Eoin	Hang Seng Gold Zinc Zinc Nikkei Nikkei Hang Seng	Long 27/02 24372 Mar08 Long 28/02 \$2725 3mth Long 12/03 12890 Jun08	CL 27/02 24324 Feb08 CL 27/02 \$957 Apr08 CL 06/03 \$2725 3mth CL 12/03 12980 Mar08 CL 17/03 11865 Jun08 CL 17/03 21285 Mar08

February 14th on market cycles

This is not a new story, but it is an important one with implications extending far beyond Hong Kong. Basically, the US floods the system with liquidity in an effort to offset the risk of recession. This inevitably affects money supply in a number of other countries, contributing to stock market bubbles in high-growth areas.

This was discussed in a superb research [report](#) from Citigroup: The Maturing Bull Market written by Robert Buckland and Orrin Sharp-Pierson, based on a study by their colleague Matt King, posted on 16th October.

The key point is whether we are in Phase 3, which they and we believed at the time:

Phase 3: Short credit, Long equity

The credit bull market is over, spreads start to rise as investor appetite for leverage wanes. The equity market decouples from credit and continues to rise. We think that the market is entering this phase now. This is the mature equity bull market.

Or Phase 4, to which the majority of investors appear to have become converts as of last month, if not before:

Phase 4: Short credit, Short Equity

This is the classic bear market, when equity and credit prices are falling together. It is usually associated with falling profits and worsening balance sheets. Insolvencies plague the credit market, profit warnings plague the equity market. A defensive strategy is most appropriate - cash and government bonds are the best performing asset classes.

The best case scenario, at least from the Fullermoney perspective, is that we are in Phase 3. If so, developed country stock markets hold above their recent lows and range at worst, while Fullermoney themes led by Asian emerging markets, resources and global infrastructure development soar over the next year.

The worst case scenario, again from our perspective, is that we are in Phase 4.

Of course not everything can be compartmentalised so easily, even if one broadly subscribes to these classifications. In other words, the phases could merge or be superseded by something else. For instance, we could have completed a medium-term Phase 4.

No doubt this will sound rather dry, inconclusive and perhaps esoteric to some of you. I am thinking out loud, believing that views must be questioned continuously and tempered by events, not least the performance of markets.

The picture may clear over the next few months. If predominantly in a Phase 3 situation, stock markets range sideways to higher, prior to some upside

accelerations in high-growth areas. Government bond prices weaken. Tentative evidence in favour of this hypothesis was the selling climax for equities on 22nd January and a simultaneous buying climax for long-dated government bond prices. However the stock market lows and government bond price highs must hold.

The Phase 4 hypothesis would regain the upper hand if last month's stock market lows are taken out and government bond prices extend their medium-term uptrends. Advocates of this outcome can point to top formation characteristics for stock markets and the flat performance of many bank shares in recent weeks.

March 18th Citigroup's Global Equity Strategist: Testing the Bull

My thanks to a subscriber for this fascinating [report](#) by Robert Buckland and colleagues at Citigroup, based on a thesis developed by their credit strategist Mark King. I posted an earlier report on this theme, because the general framework resonated with my own impressions, gradually developed and based on the observation of many equity cycles since the mid-1960s. Mark King's basic premise is that there are four phases of a credit cycle:

Phase 1: Long credit, Short equity

This phase immediately follows the bottom of the credit bear market. Spreads fall sharply as companies complete the process of repairing balance sheets, often through deeply discounted share issues (as we saw for Insurance and Telecom companies back in 2002-03). This, along with continued pressure on profits, keeps equities weak.

Phase 2: Long credit, Long equity

The next phase begins as profitability turns and equity prices start to rally. Credit spreads fall even further as corporate cashflow rises strongly. We call this an immature equity bull market. For the present cycle, this phase began in March 2003 and finished in the middle of the 2007.

Phase 3: Short credit, Long equity

The credit bull market is over, balance sheet leverage increases, spreads rise, and investor appetite for credit wanes. Financial market volatility rises. As we progress through Phase 3, the equity market eventually decouples from credit and continues to rise. This is the mature equity bull market.

Phase 4: Short credit, Short equity

This is the classic bear market, when equity and credit prices re-couple and fall together. It is usually associated with falling profits and worsening balance sheets. Concerns about insolvency plague the credit market, while broad profit concerns plague the equity market. A defensive strategy is most appropriate - cash and government bonds are the best performing asset classes.

My view - Most investors will find the four stages above to be logical. The key question: Are we in Phase 3, or did the US financial crisis bounce us straight into Phase 4? Citigroup's Global Equity Strategist addresses this question:

Phase 3 or Phase 4?

So that's the theory. Last year we suggested that we were in Phase 3 - the mature bull. So sell credit, but stick with equities. Now, many worry that we have entered straight in Phase 4, so sell both. Of particular concern are:
Credit markets: the carnage in the credit markets is so bad that equities have little chance of decoupling. Earnings: A US economy teetering on the edge of recession represents a significant threat to global earnings. How can equities go up when earnings are falling?

We address each of these concerns.

Most subscribers will wish to read this report which I certainly found informative. For those who may lack the time, I'll add that despite the financial meltdown, the authors are still inclined to view current action as Phase 3, with lower interest rates being the key to strong additional gains for some markets. Reassuringly, if your portfolio is overweight Fullermoney secular themes, the report favours emerging markets and materials for participating in the forthcoming bubble which they envisage.

Fullermoney's behavioural approach is particularly interested in recent sentiment readings, which clearly indicate that a significant majority of investors are convinced this is a severe bear market. One can understandably be swayed by this tidal wave of fear, but in our more analytical moments we know that sentiment is a contrary indicator. Personally, in attempting to identify a market bottom, I am more influenced by sentiment than any other indicator. Developments since January's selling climax and retest of those lows have been stunning.

These include last week's survey from Investors Intelligence, posted here on Thursday, showing the most bearish reading for Investment Advisor sentiment since the important October 2002 low. The recent data also produced the second lowest reading for at least 10 years. I should have II's latest report tomorrow.

In January, I posted Bloomberg's reports on net insider buying for the first time since 1995, and the highest NYSE short interest since the 1930s! We have not approached a record on VIX but there have been three readings above 35, occurring last August, this January and yesterday.

Inevitably, interest rates remain a crucial factor, and no longer just in the USA where the Fed fell behind the curve last year but has been catching up subsequently. I believe the BoE and ECB are behind the curve and need to cut rates. So do India and China, before my two favourite stock markets for the very long term can become upside leaders once again. These have been very disappointing recently but big shakeouts create additional buying opportunities in markets with good prospects for future economic growth.

Inflation is the main reason behind the delay in lower short-term rates, USA excepted. This will remain a problem, more often than not in my view, due to supply inelasticity and rising demand. However, monetary policy is a crude weapon for dealing with food and energy inflation, as I have said before.

Eventually, somewhat slower economic growth will give dynamic economies such as China and India justification to commence their next cycles of monetary easing. This is probably required before they can reverse recent stock market weakness and resume their secular bull trends.

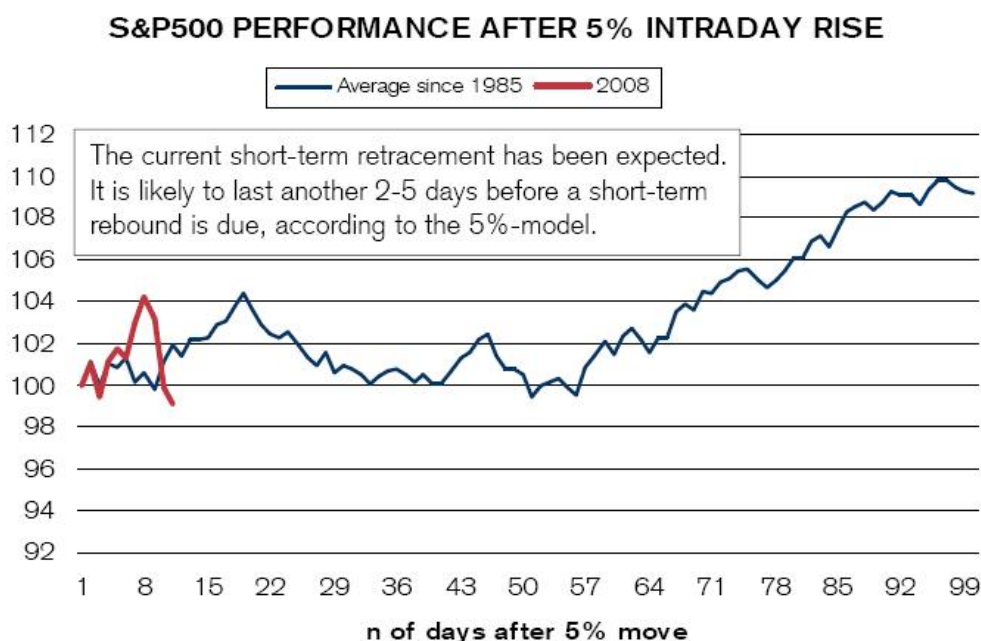
China is an increasingly important influence on other stock markets, particularly regionally, and its leash-effect has been negative this year. The [chart](#) will look frightening to some but the latest decline is becoming overextended. I do not believe that the US economic slowdown, or any other reason is sufficient to drive the Shanghai Composite Index significantly lower. The government has already signalled that there will be fewer floatations to weigh on the market.

The historic [PER](#) for Shanghai's Composite Index, while not cheap at 30, is well below last year's bubbly peak of 50. Hong Kong's Hang Sing [Index](#) is arguably cheap for a strong economy at 13 times historic earnings, and the yield has risen to nearly 3%. I would not be surprised if this week's latest downward break is soon reversed.

See also Eoin's item on China below. I suspect that the article posted may overstate the government's policy response to inflationary pressures.

February 14th S&P Performance After 5% Intraday Rise

My thanks to a subscriber for this fascinating item, which I believe was produced by Credit Suisse.



I have not heard mention of this before, and would like to see the full report in which it appeared, if anyone has it and would not mind forwarding it.

The message, if I read it correctly, is that following a selling climax the S&P 500 bounces and retests its lows, before rising by an average of 10% within a hundred days.

March 12th Investors Intelligence: Mike Burke and John Gray on Advisors Sentiment

My thanks to colleague Jackson Wong for this important [study](#) by Mike Burke and John Gray, published by Stockcube's long established US branch of Investors Intelligence. Here is a brief sample:

The sharp increase in advisor pessimism could be blamed on tumbling index action and the increased belief that the economy is in a recession. All three primary stock averages continue to trade below their declining 200-day moving averages and show penetrations of major support. Last week's acceleration to the downside was enough to cause the latest shifts.

The spread between the bulls and bears is -12.2%, a sharp drop from +5.3% a week ago. This is also the first negative difference since October 2002, shown on the chart as the prior move below the 'O' line. The recent readings remain bullish. There has been and an almost +55% shift in the sentiment spread from the early October 2007 market high. That included a very negative +42.4% difference.

My view - Mike Burke has seen almost as many market cycles as the venerable Richard Russell, who incidentally is quoted in this report on the subject of inflation. John Gray also has decades of stock market experience.

These two colleagues at Investors Intelligence have done as well as anyone I know of in forecasting US stock market action over the last year. Their Sentiment Indicator: Bullish Advisors % Less Bearish Advisors %, is a top example of the behavioural contrary indicators that I like.

The trouble with people in the presence of good indicators is that they want important signals every day. Of course life is not like that, although this week is an exception. There have been only five clearly oversold readings for Mike and John's indicator in the last ten years, but they are the behavioural equivalent of gold dust. The high sentiment readings have been interesting, much more frequent and therefore inevitably less useful.

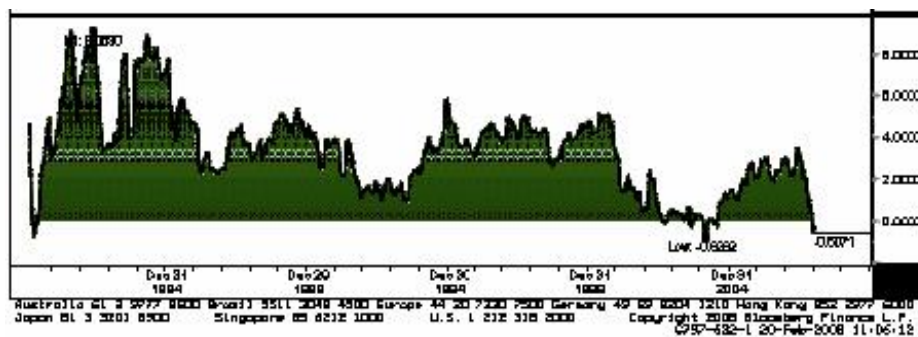
Investors Intelligence has long produced a great indicator for identifying stock market bottoms. Will it work this time? I think so. Many will say: 'It's different this time.' Yes, it is always 'different this time', in terms of the background fundamentals. Could the indicator be giving a false signal, soon to be confirmed by Wall Street moving significantly lower as so many expect. Yes, statistically, either because the credit crunch *really* does spell financial Armageddon, or perhaps a doomsday rock heading straight for earth is spotted by an astronomer tonight. However I would not bet on either of these remote possibilities anytime soon.

"If everyone is thinking the same thing, then no one is thinking."
 (source of quote unknown to me)

February 25th On the S&P following negative rates:

"Given your short position in bonds here I thought you might like the attached. Very quickly from Bloomberg I looked at what the performance of the SPX was following other periods when 2 year treasuries (USGG2YR) minus inflation (GDPCPCEC) became negative. The results aren't accurate to the nth degree but they are interesting. A similar pattern occurred in 1977 but my Bloomberg data doesn't capture the entire period. The table shows SPX performance following the move into negative territory - they were done very quickly though. Here's hoping....."

My comment - Thanks for this useful and informative research, contributed in the spirit of Empowerment Through Knowledge.



Since both the graph and table may be difficult for some of you to read, I'll elaborate briefly. The graph from your fellow subscriber shows the current and two previous instances in 1980 and 2003 when US rates became negative: "2-year Treasuries (USGG2YR) minus inflation (GDPCPCEC)."

Date Real Yield Hit Low	Performance after:			
	3mths	6mths	9mths	12mths
30.05.1980	17%	25%	25%	29%
31.03.2003	15%	17%	31%	31%

Following 30/05/80, the S&P performed as follows: 3mths +17%, 6mths +25%, 9mths +25% and 12mths +29%.

Following 31/03/03, the S&P performed as follows: 3mths +15%, 6mths +17%, 9mths +31% and 12mths +31%.

Sceptics will say: It's much worse this time! They are probably right, at least in terms of the US and UK economies. If we lived in a fundamentally mono-themed world of the credit crunch alone, many of us would have already jumped off a high building. Fortunately, there are other factors. The markets will distil them and deliver the all important verdict for investors.

March 13th on coping with tough times:

"Just following up on your comment about not completely trusting the Australian banks assurances on sub prime - this [article](#) appeared in the weekend Australian newspaper, and I have another question which I hope you could shed some light on. I am only a fairly new subscriber and also a fairly new investor and have loved the recent interaction between yourself (optimistic camp) and the guy who wanted you to join his side (the bearish camp). I was firmly entrenched in the bearish camp but was swayed by the conviction in your writings, the level headedness of your research and the chart based reasons. Suffice to say that I have been torn between the bullish and bearish camps over the past 4 weeks and have only succeeded in tearing myself a new one (i.e. losing money). Could I ask you your advice on how you stick with your investment convictions, especially in the face of wave after wave of bearish news? How did you develop the mental strength to stay with your positions? How much would you say is chart based? I particularly refer to the theme of recent emails saying that you would give the benefit of the doubt whilst the Jan 22 lows hold). Does it purely come down to weighing up all the evidence and then sticking with your gut feeling?"

"Thanks again - I must say for all the emails you get saying how they would pay much more for the service and that you could easily charge much more, I am one of those who loves that you don't!"

My comment - Thanks for your kind words and welcome to Fullermoney, which I hope will help you to develop your investment and trading skills over the long term. Thanks also for the informative article, which I have posted in the Subscriber's Area.

Regarding discussions between bulls and bears in the emails, I want to state emphatically that I respect the views of many people who are currently more bearish than I am, not least some very experienced and knowledgeable subscribers who have excellent track records. In a debate, I would have no trouble in also arguing the bear case. That is what makes this business so fascinating and challenging. No one has all the answers; no one has cornered the market in perspective, and none of us know the future.

Disagreements among reasonably informed and experienced people are often a matter of emphasis. Today, I am particularly interested in sentiment indicators and a number of these have been ringing bells recently, at least for me. They include the first net insider buying in the USA since 1995, the highest short interest since the 1930s (both reported by Bloomberg in late January in articles posted on this site), and the Advisory Sentiment Indicator from Investors Intelligence, which I posted yesterday. There are of course other factors, discussed here and more frequently in the Audio, as that is such an efficient means for Eoin and myself to convey our views.

What about the awfulness of the excesses and credit crunch, some might say. The problems are serious but I believe it is the response that will count most in terms of markets. On the one hand, we have seen waves of deleveraging, which are still in progress. More recently, we have seen increasing injections

of liquidity from central banks, which I assume will continue. The deleveraging is consigning some dubious instruments to the financial sin bin and also creating some outstanding value. Those instruments will perform very well over the medium term, and we intend to identify some of them, in addition to Fullermoney secular themes.

Your other questions are partially answered in my response to Email (3) below. Additionally, "wave after wave of bearish news", as you accurately stated, ensure that quite a few of the problems have been discounted. I expect waves of bearish news, real and imagined, at market bottoms, and a surfeit of good news at tops. I do not accept that we are currently dealing with the financial equivalent of [necrotizing fasciitis](#), although it may seem like it when so many extrapolate their fears (or bearish hopes).

As to "mental strength", to the extent that I may have it, I hope this is based more on common sense than stubbornness. These times are stressful for all of us and I hope to remain analytical rather than lose my perspective in a tide of emotion. It helps if you have a balanced life and maintain a sense of humour when the market is behaving like a drama queen.

February 29th On the USA and economic decoupling:

"I subscribe to a business news [portal](#) where I saw this article today from the Tehran times - it supports your view rather nicely. This actually demonstrates how quickly global economies are decoupling from the U.S. economy. The U.S. has a \$9 trillion National Debt and a net \$3 trillion foreign debt, so obviously any crisis is going to hit indebted countries far harder than nations flush with cash (Russia, China, India, Japan, the "Tigers" and Western Europe). The U.S. is in deep fundamental, historical trouble."

My comment - Thanks for [this](#) which may be a first, since I do not recall posting any other articles from the Tehran Times, although I know Iran has a sophisticated press. I'm sure I have also seen other articles by the banker and economist, Hamid Varzi, in the western press.

It is a credible summary, with which I am in general agreement. In a global economy there can be no total decoupling by the USA's trade partners, but they can move along different trajectories. Too many western commentators do not understand this, maintaining that China etc have little going for them other than supplying the US consumer.

I believe our perspective and analysis improves if we stop thinking of the world in outdated terms of developing and developed. Instead, I prefer to classify nations and their economies as either progressing or regressing.

Countries will progress when governance improves at a root and branch level, or regress when governance deteriorates. They can also progress due to windfalls, such as today's commodity boom. However windfall gains will eventually be squandered if governance is inept. It is a harsh, competitive world, so in a Darwinian sense we either progress or regress. Fortunately it is a process that people can usually influence, collectively at a national level and

also individually at a personal level, particularly if free and protected by progressive Rule of Law.

Stock markets are less able to uncouple from the Wall Street leash-effect, although they may appear to do so in terms of relative performance. However investors move like sheep, in possession of global communications. This is particularly true of institutional investors who are pressured by press, client and peer scrutiny to at least match their benchmark. Many are also momentum driven, not least hedge funds. The focus on monthly performance figures is not always conducive to the best results.

In contrast, private investors, individually unscrutinised by the press, are answerable to themselves and perhaps their immediate families. This gives them greater freedom to 'rush in like fools where angels fear to tread', often doing very well for themselves in the process.

However with progressing economies becoming less coupled to the USA, as the world evolves from unipolar to multipolar, the Wall Street leash-effect is also less dominant than it was in previous decades. When the DOW plunges, investors in other stock markets are still prone to panic, even if the fundamental backgrounds are quite different. However the fundamentally strong markets and sectors will usually bounce back more quickly, as we have seen with Fullermoney's secular themes of Asian progressing markets, resources and global infrastructure development.

March 10th on listening to CEOs versus bankers

Air Liquide chief finds few storm clouds - This is an informative [article](#) by Peter Marsh in today's Financial Times. Here is the opening:

In the past few weeks Benoit Potier has been combining his main job with being an economic detective, searching for the smallest of clues that could indicate a looming recession in the world economy.

So far, his investigations have drawn a blank. "Even though there has been a lot of talk of a recession, I cannot see any signs as yet," says Mr Potier, who is chief executive of Air Liquide, the French supplier of industrial gases that vies with Linde of Germany as the world's biggest producer of these materials.

Mr Potier explains that to avoid charges that he is being complacent, he has been examining all the main facets of Air Liquide's global operations to look for indications that theories about an imminent serious slowdown are correct.

He appears to have a good basis for making broad statements about global demand. Air Liquide sells its products to about 1m customers in a range of industries, from glassmaking to electronics.

He says his products comprise an "infinite" mixture of gases based around about 20 key chemicals including oxygen, nitrogen, argon and hydrogen.

Of Air Liquide's sales last year of €11.8bn (\$18.19bn), of which €10bn came

from gases and the rest from providing engineering equipment, less than a fifth came from France.

Nearly a third of revenues were derived from customers in North and South America, and 18 per cent from Asia.

"A lot of the companies we sell to are telling us they need more of our gases to meet the demand for customers desperate for products," says Mr Potier.

"So long as you have emerging economies - such as India, China, the Middle East and Russia - expanding at 6-10 per cent a year this provides hope that the world economic system as a whole will show some stability."

And a few paragraphs further on:

Mr Potier's optimism adds weight to the comments of other leading industrialists who say they can foresee few storm clouds for the global economy, mainly because of the impact of strong demand from outside the main industrialised nations.

The shorthand for this is that the world is going through a process of "decoupling" in which growth in the emerging economies compensates for any economic difficulties in countries such as the US.

Jürgen Hambrecht, chief executive of BASF of Germany, the world's biggest chemical maker, recently accused financial markets of "panic" over the likely extent of a potential weak phase for the economy, while MAN, the German industrial conglomerate, is predicting record results for this year, driven by rising oil and raw material prices.

My view - Have western financial companies been damaged, severely in a number of instances, by sub-prime slime problems largely of their own creation? There is no doubt about it. Has the west's credit crunch created significant problems for many of its regional borrowers? It certainly has. Are these global problems? Not really or not directly, and they are not even regional problems for hundreds of well managed, cash generative, multinational companies with headquarters in Europe and the USA.

Is Jürgen Hambrecht, Chief executive of BASF of Germany, the world's biggest chemical maker, correct in accusing financial markets of "panic", as reported above? I believe so. Sentiment within the western financial community is exceptionally bearish. This is not necessarily objective, as I have said before. If an investment banker's income is suddenly reduced considerably and future streams of income appear uncertain, the tendency is to assume that everyone else is in the same mess. In psychoanalytic terms, it is called a projection.

I have not seen such a large disconnect between financial consensus opinion and global economic prospects since the Crash of 1987. There are plenty of differences, of course. There always are. However in both instances many

people believed that the USA-triggered financial problems were the worst crisis since The Depression.

In post-Crash 1987, I was more interested in the business community's views on the global economy, since financial types were speaking with the same, uniformly bearish voice. Today, I am more interested in what people such as Benoit Potier and Jürgen Hambrecht have to say about economic prospects, than bankers who may be either traumatised or talking their short book.

By chance, I asked a Swiss-based banker today; of all the financial types he speaks to, what was the ratio of bears to bulls? He thought for a moment and then replied: "They are 95% bearish, at least." Their views can be summarised as ranging from credit problems, including uncertainties, to stock market price charts, which many of us look at every day.

The charts are mostly bearish; you will have either noticed or will not be surprised to hear. The climactic intraday lows seen in January are being challenged by many influential indices, which remain in downward trends. Upward dynamics are required to reaffirm support near current levels. In other words, markets are weak so any upside remains for the bulls to prove.

Until another catalyst squeezes shorts and encourages buyers, bulls will remain tentative and bears will be emboldened by each new low. Significantly, financial indices are leading on the downside once again, despite the declines already seen. Markets tend to overshoot, in both directions.

What should investors do? I prefer to speak for myself and I'm going to ride it out. My personal investment portfolio positions are certainly not immune to contagion selling, particularly during panicky activity as we last saw in January, but most have also shown an ability to bounce back quickly.

While a drawdown can be uncomfortable, I have profited by nibbling in my trading account during climactic selling. The market's main focus is understandably on credit crunch problems but I believe these have limited influence on the long-term outlook for Fullermoney themes. Even if I had had the misfortune to ride a major financial share all the way down (I haven't owned them, yet), I would question the wisdom of selling seven months into a Wall Street decline.

What are other people doing? Eoin discusses the stampede into TIPS (Treasury Inflation-Protected Securities) below, despite the negative yield. I suspect that will end badly for many investors. I would rather invest in Fullermoney themes when shakeouts occur.

In a contrarian play, I also think a bombed out bank such as UBS is interesting. Today, it has an estimated PER of 8.44, although I suspect earnings forecasts are too optimistic. However UBS also has a dividend of 7.58% which is covered 2.67 times according to Bloomberg. Perhaps there will be more shocks in the form of write-downs; perhaps more SWF support is required; I would not rule out a rights issue at some point.

Nevertheless most of this should be reflected by the price ([monthly](#), [weekly](#) & [daily](#)) which is falling for the 10th consecutive month and approaching some important lows. For all its current woes, UBS remains an important Swiss bank with a world-class asset management division. At today's prices, one probably receives the investment banking side for nothing. Charts show that UBS has yet to bottom but the turn is likely to be rapid, when it occurs.

March 11th Fed to Lend \$200 Billion, Take on Mortgage Securities

Here is the opening from today's big news [story](#) by Scott Lanman for Bloomberg:

The Federal Reserve, struggling to contain a crisis of confidence in credit markets, will for the first time lend Treasuries in exchange for debt that includes mortgage-backed securities.

The Fed said in a statement in Washington it plans to make up to \$200 billion available through weekly auctions. Officials told reporters on condition of anonymity that the program may be increased as needed. The Fed coordinated the effort with central banks in Europe and Canada, which plan to inject up to \$45 billion into their banking systems.

U.S. stocks rallied the most in five years on optimism the initiative will help avert a wider credit crunch. Treasuries fell and the premiums investors demand for debt backed by home loans guaranteed by Fannie Mae retreated from close to a 22-year high. Fannie Mae and Freddie Mac, chartered by the government, are the largest sources of money for U.S. home loans.

“This is the most significant step the Fed has taken so far,” said David Resler, chief economist at Nomura Securities International Inc. in New York. “This relieves some of the pressure” in the credit markets, he said.

Today's steps indicate the Fed is increasingly concerned about the investor exodus from mortgage debt, which threatens to deepen the housing contraction and the economic slowdown. Officials said the program is aimed at countering a decline in liquidity in financial markets around the world, and comes after signs of increasing stress in U.S. mortgage securities.

My view - We have known for some time that the Fed and US Treasury were targeting the [stock market](#). Prior to today's announcement, their last big move was to stem the selling climax in January with 125 basis points of rate cuts, in two moves within eight days.

I suspect that Treasury Secretary Hank Paulson was behind the timing of today's [bear trap](#). It was the financial equivalent of a classic rope-a-dope [ploy](#), suckering in the bears, allowing them to control the market for two weeks once resistance from the February highs had rebuffed the last rally, and then springing a surprise announcement just as the range lows were being tested amidst a crescendo of bearish forecasts.

Credit the Fed with having won a round in the stock market while demonstrating that it is not yet the ineffectual spent force, in terms of addressing the credit crunch, as many analysts have claimed. It remains to be seen whether or not bank credit spreads, having widened recently, now narrow just as quickly following what looks to me like the nationalisation of duff loans, although the Fed has not actually purchased the mortgage securities.

The moral and financial efficacy of today's move by the Fed are subjects that I will leave for others. Instead, I will address the outlook for stock markets.

Upside follow through by Wall Street tomorrow would signal further short covering and perhaps some bargain hunting, and increase odds that February's highs will be tested. For evidence of a significant technical improvement, the S&P 500 Index will need to maintain a break above 1400. For this to occur, we need to see a corresponding improvement in the Banks Index (weekly & daily). Today, we have only seen a downside failure but these can be important.

Meanwhile, the last two most significant technical developments are January's selling climax and today's upward dynamics for US indices. Closes beneath both of these lows are now necessary to reaffirm the medium-term downtrends.

Psychologically, today's downside failures for the Banks Index shown above and also the Nasdaq, are actually more telling than a bounce from a low. Most people expect some steadying near a former low. However a clear downside failure, provided it is not just a one-day wonder, shows that a market had every excuse to fall, but did not.

A lengthy convalescence (support building process) may still be necessary for a number of stock markets. Meanwhile, I maintain that the extremely bearish sentiment expressed by so many people recently is a contrary indicator.

There are additional discussions of stock markets below, including Japan.

March 14th Financial Times: Intervene to slow the dollar's decline

Here is today's editorial from the Financial Times:

Selling the dollar is now close to a one-way bet. So great is concern about the health of the US financial system that the dollar traded below Y100 yesterday, and above \$1.56 against the euro. The danger of a dollar rout is rising, and the Federal Reserve, European Central Bank and Japan's Ministry of Finance should co-ordinate intervention to slow the greenback's fall.

Aggressive rate cuts and fears that US taxpayers will have to bail out their banks are undermining the dollar. Both make a surge in US inflation more likely, and since the Fed first cut rates last September the risk has been that foreign investors lose confidence, dump assets and trigger a run on the dollar.

The dollar's decline is accelerating. It fell by 10.4 per cent against the euro in 2007 and appeared to stabilise in December and January, but in the last month it has dropped by a further 6.5 per cent. In trade-weighted terms the dollar has fallen about 3 per cent so far in 2008.

A weaker dollar is an essential tool to stimulate the US economy, but a collapsing dollar benefits nobody. If investors start to dump dollar bonds then the Fed could lose control of long-term interest rates, so rendering monetary policy ineffective. Europe and Japan, meanwhile, would suffer a savage adjustment in their export sectors.

It would be pointless, foolish and wrong to try and fix the dollar at its current level. Markets are the best way to determine exchange rates, and on a trade-weighted basis it is far from clear that the dollar has overshot its fair value. But what intervention might do is slow the decline, by putting fear in the minds of momentum investors who are selling short on margin.

Limited objectives are one pre-requisite for a successful intervention. Another is co-ordination. On past form Japan must be close to unilateral action but a joint move with the ECB and the Fed would be better and more likely to succeed.

A third prerequisite is the cooperation, if not the active aid, of Asian nations that manage their currencies against the dollar. Their central banks could take the other side of an intervention trade in order to diversify their reserves out of dollars and into euros and yen. Instead, they should now allow, and the G7 should press for, faster appreciation of their currencies.

Intervention is never ideal - some of today's problems stem from past manipulations - and there are large risks, most notably that central banks fail and lose credibility. But if the above conditions can be met, some action to stabilise the dollar would be a sensible part of the response to global financial turmoil.

My view - As the US dollar's decline gathers pace, people are beginning to talk about multilateral intervention, an event that I have often said would be required to eventually stem the greenback's decline. However it is likely be more difficult this time. For more on central bank intervention, here is one of my earlier comments from 11th October 2007:

Multilateral intervention would be the most effective means of steadying the USD as I have frequently mentioned before (search under 'multilateral intervention' if interested). I maintain that it will occur at some point, probably preceded by jawboning, assuming that I am also correct in forecasting a weaker dollar. Much depends on the speed of a further decline by the greenback. An accelerating slide would be perceived as a crisis, forcing a response. However there would be less urgency with a ranging decline, which is what we have seen to date. Multilateral intervention would trigger a short-covering rally in the dollar, simultaneously causing a knee-jerk reaction in precious metals and many other commodities. However the dollar's lows

would be retested, judging from previous interventions, and it would be some time before long-term trends were changed.

And on 22nd October 2007:

...even in the event of multilateral intervention, a rare but previously successful activity in the post Bretton Woods era about which I have often commented, other central banks would inevitably find themselves holding even more US dollars. The probable difference this time, and I do expect multilateral intervention in support of the dollar at some point, is that central banks will almost certainly have fewer opportunities of selling the additional greenbacks on at a trading profit, as we have seen following earlier support operations. Moreover, their intervention would invite freeloading by enabling other central banks, uninvolved in the support operation, to sell some of their unwanted US dollars.

What we are witnessing is the long, slow devaluation of the dollar as the world's primary reserve currency - a process likely to last for decades, just as occurred with Great Britain and sterling in the last century.

To date, this has been an orderly process in that the US dollar's downward steps are punctuated by ranging periods, some of which have been lengthy. Quite unintentionally, this process of periodic short-covering by traders, as we are seeing today, has so far staved off a panicky currency crisis. I do not assume that this will always be the case.

A logical tactic of forex traders is to stay with the momentum moves until they slow. Individual central banks have had some temporary success in slowing their currency's appreciation against the US dollar, mainly by jawboning.

However with US interest rates declining, the Fed printing, America's economy the epicentre of global weakness and its creditor governments already holding what they regard as uncomfortably large dollar positions, the greenback is unlikely to stage more than short-covering rallies until the US economy is recovering and the Fed raising interest rates.

Consequently, it is unlikely that multilateral intervention to support the dollar, which would probably have to be repeated, could produce more than some short, sharp rallies. Given the perilous state of the US economy, I believe it will be some time before we see a major rebound by the US Dollar Index ([historic](#), [monthly](#), [weekly](#) & [daily](#)).

February 18th The Debt Delusion

My thanks to a subscriber for this excellent and informative [assessment](#) of the US economy by Thomas Palley for The Australian, reproduced by Project Syndicate. Here is a section:

The differences between the new and old cycle are starkly revealed in attitudes toward the trade deficit. Previously, trade deficits were viewed as a serious problem, being a leakage of demand that undermined employment and output. Since 1980, trade deficits have been dismissed as the outcome of

free-market choices. Moreover, the Federal Reserve has viewed trade deficits as a helpful brake on inflation, while politicians now view them as a way to buy off consumers afflicted by wage stagnation.

The new business cycle also embeds a monetary policy that replaces concern with real wages with a focus on asset prices. Whereas pre-1980 monetary policy tacitly aimed at putting a floor under labor markets to preserve employment and wages, it now tacitly puts a floor under asset prices. This is not a matter of the Fed bailing out investors. Rather, the economy has become so vulnerable to declines in asset prices that the Fed is obliged to intervene to prevent them from inflicting broad damage.

All these features have been present in the current economic expansion. Wages have stagnated despite strong productivity growth, while the trade deficit has set new records. Manufacturing has lost 1.8 million jobs. Prior to 1980, manufacturing employment increased during every expansion and always exceeded the previous peak level. Between 1980 and 2000, manufacturing employment continued to grow in expansions, but each time it failed to recover the previous peak. This time, manufacturing employment has actually fallen during the expansion, something unprecedented in American history.

The essential role of asset inflation has been especially visible as a result of the housing bubble, which also highlights the role of monetary policy. Despite the massive tax cuts of 2001 and the increase in military and security spending, the US experienced a prolonged jobless recovery. That compelled the Fed to keep interest rates at historic lows for an extended period, and rates were raised only gradually because of fears about the recovery's fragility.

Low interest rates eventually jump-started the expansion through a house price bubble that supported a debt-financed consumer-spending binge and triggered a construction boom. Meanwhile, prolonged low interest rates contributed to a "chase for yield" in the financial sector that resulted in disregard of credit risk.

In this way, the Fed contributed to creating the sub-prime crisis. However, in the Fed's defense, low interest rates were needed to maintain the expansion. In effect, the new cycle locks the Fed into an unstable stance whereby it must prevent asset price declines to avert recession, yet must also promote asset bubbles to sustain expansions.

My view - National wealth is not an entitlement; it is the consequence of good governance and enterprise. Paradoxically, when America's economic power appeared to be at its height, it was most vulnerable to hollowing out as a number of developing countries with large populations, led by China and India, adopted capitalism.

Today, the global economy is more dynamic and creative than ever before. It is also vastly more competitive, producing instant winners and losers. Thomas

Palley provides a sobering summary of America's economic dilemma, aspects of which can be viewed as the flipside of Chindia's success.

However, just as success can prove to be ephemeral in a dynamic and therefore competitive global economy, failure can also be transitory, subject to governance. The key is often adaptability.

I do not share Thomas Palley's pessimism expressed in the third paragraph of his article (not shown in the segment above), although solutions may appear elusive at the moment.

'Needs must' is often the mother of invention, as we have seen before and as I believe we will see at an accelerated rate in future. All countries face daunting challenges - concerning energy, water, pollution, food and employment, to mention a few, but inventive capitalism and good governance are the mechanisms for resolving them.

The USA's problems, partially detailed by Thomas Palley, only seem greater because of our shock over America's decline from a higher economic pinnacle. In contrast, China's and India's stunning rates of economic development seem more impressive because up until about 20 years ago their economies remained moribund.

I do not know precisely how the USA will resolve its economic problems. However I suspect it will begin with a reduction in overseas bases and military spending. Simultaneously, I would not be surprised to see a reallocation of government funds, in partnership with industry and also university research efforts, directed towards improving the country's energy situation and overhauling America's aging infrastructure.

It will obviously take time but I would not underestimate the USA's inventive and regenerative capabilities. There will also be inward investments as Alex Seagle [detailed](#) not long ago. Meanwhile, America's multinational companies are doing very well. Consequently, I would not be surprised if we look back at some point in the next decade or two and see 2007-2008 as a nadir for the US economy.

February 21st on credit market conditions:

"What do you think of credit market conditions and its possible impact on equities into early Q2? Many people now say that worst is behind as banks aggressively (especially US) wrote down subprime exposure. Think this is true, but some people do not pay attention to where credit trades in secondary market now. Most of the spread widening occurred this year rather than fall 2007. For example Commercial Mortgage Backed Securities at least doubled this year - CMBS AAA 10 year trades at 340 (+190 YTD), while BBB at 1300 (+500), iTraxx Xover at 577 (+240 YTD), banks everywhere struggle to issue bonds and pretty much corporate credit is trading heavy in any market. I imagine all leveraged loans are dead illiquid and sit on banks books. Which means if conditions do not change we will have further poor mark to market on these positions, which banks, hedge funds, dedicated money, other investors

will have to write down in Q1. Some of them will probably lose more in comparison to what they have written off in subprime... Any thoughts?

"Thank you as ever for your great service."

My comment - Thanks for your kind words and informative insights.

Yes, the credit situation remains a problem, particularly regarding dodgy loans. If you take a long-term view, this is positive because an economy will not establish a platform for long-term prosperity on the basis of reckless lending. It is also why we expect a lengthy convalescence for the firms most affected.

We should assume the obvious - some weak borrowers, including under capitalised companies, overstretched hedge funds or individuals will fail, as may some lenders as we have already seen with Northern Rock, now nationalised by the Bank of England. However most financial institutions have either better business plans, stronger balance sheets and / or successful hedging policies. They are inconvenienced, to put it politely, but not fatally so given central bank liquidity infusions and SWF loans.

Additionally, while the credit difficulties were largely a made-in-America fiasco, albeit either exported to many countries or also copied by them, not least the UK, for many other countries this is merely a temporary problem rather than a crisis. As far as Fullermoney themes are concerned, I think we will look back in two year's time and see that credit-related

February 25th On credit conditions

"Enclosed please find my questions based on a recent Doug Noland article.

"I hope you can address some or all of them. This is an issue of major concern and I welcome your thoughts.

"Thanks for all your wonderful work and your ever more creatively supportive website!"

My comment - Thank you for your thoughtful comments and inspirational enthusiasm for the Fullermoney site.

Thanks also for this [information](#) from Doug Noland and your accompanying questions, certain to be of interest and concern to many readers.

Regarding "minimizing" the credit crunch, we certainly do not intend to do so, but to ask some questions of my own, how do we evaluate it in a practical manner, especially when there is so much uncertainty?

Do we feel "comfortable" about the situation, as you ask? Certainly not, but other than acknowledging a serious problem, who is qualified to conduct a lengthy discourse on this subject, in terms of how it will affect markets? I see

plenty of commentary, lots of extrapolations among forecasters, and often emotion labelled as analysis.

I hasten to add that I do not classify either you or Doug Noland in this latter category. You probably know more about the credit problems than I do and that is certainly true of Doug Noland, who I regard as a superb credit analyst.

However my job is to relate any situation back to the markets. Veteran subscribers know that I have described the US as a high-risk economy since well before the credit crisis became so apparent. That is why I have invested elsewhere, an occasional trade excepted.

A pertinent question which I ask myself daily: has the credit situation either been fully discounted by markets, or at least to a point where other factors are more than compensating for current and undisclosed risk? I will give the latter the benefit of the doubt, as you know, provided the lows of January 22nd continue to hold. Unlike some, Eoin and I will not tell the markets what to do.

In what I regard as an overly US-centric analytical community, I also ask myself if the credit problems, where they exist, will torpedo Fullermoney's secular investment themes of emerging Asia, resources and global infrastructure development? With markets there are no grounds for complacency but I find the evidence in favour of Fullermoney investment themes encouraging.

In specific response to your questions by section: (1) Some corporate balance sheets are undoubtedly overinflated. (2) I suspect many companies are unable to raise new financing, a situation that will favour the strong if it persists. Yes, the US economy has been in serious trouble for some time. Yes, the strength of precious metals indicates a distrust of fiat money. (3) I believe some credit spreads are widening while others are narrowing. (4) Risk is certainly being repriced, including by "technical hedging" and speculative shorting. (5) Fannie Mae and Freddie Mac have long been accidents waiting to happen, which is why they may have to be nationalised. Their results on Thursday will be interesting.

Your questions accent the problems, about which we should be under no illusions. We also have reason to believe that the US government will use every resource available to prevent a further meltdown. I would not underestimate those efforts but markets will continue to provide the verdicts which count for investors.

March 3rd Marc Faber: What's Ahead in 2008

My thanks to a subscriber for this superb [interview](#) of Marc Faber, conducted by Jim Puplava of Financial Sense News Hour. It occurred in January but is no less compelling today in its panoramic sweep and candid assessment of events emanating from the US credit bubble.

It takes two to make a great interview - a highly experienced interviewee who, crucially, is free to speak his mind and an interviewer with an excellent grasp

of the subject. Marc Faber is a familiar name to veteran subscribers and held in high regard at Fullermoney for his global perspective and candour. Jim Puplava is one of the very best interviewers in the business. Here is a sample:

JIM: You bring up an interesting point about liquidity in the world which has a genesis in much of the US trade deficit. As we look around the globe today, Marc - I have a screen on my Bloomberg that has year-over-year money supply growth rates around the globe and what is surprising as I look at this table is to see double digit money supply growth around the globe out of 18 of the top 20 central banks. I think Europe reported last week it's money supply is growing at over 12%, yet Trichet is talking about being tough on inflation. You know, the inflation rates that we're seeing here in the United States, are they not global in nature? Are you finding that, for example, in China where you have the inflation rate going at 6 or 7%, that this is a global phenomenon?

MARC: Yes, I mean that's the point. I mean when recently people were very negative about the US dollar and so forth - and of course, long term you cannot be optimistic about the US dollar - but the US dollar has declined quite substantially, especially against the euro in the last couple of years; and the Europeans are also good money printers. It's not just Mr. Bernanke that is the chief money printer. The others are not much better either. So basically, you have this excess liquidity being created in order to support asset markets and so forth.

But the point about this excess liquidity is that an eternal boom is out of the question. So what the Fed and the other central banks can do is kind of stimulate, through easy monetary policies, credit growth; but the private sector if it becomes, say, risk adverse can withdraw liquidity and a) not lend and people can also refuse to borrow, and so the credit does not accelerate but actually contracts. And that leads to what I call a relative illiquidity (it's not an absolute illiquidity, it's a relative illiquidity) and that then has some negative implications on some asset markets. But to come back to the first question you raise about making predictions, I think the difficulty today is that under normal conditions, say under a gold standard, we would be in a massive deflationary recession at the present time. Now, the central banks are all intent to prevent that and they print money like crazy and throw liquidity at the system by cutting interest rates and taking extraordinary measures. And so the question arises: How did you measure really economic growth and how do you measure your wealth? Say, as I mentioned, if the Dow goes from here to 26,000 - it doubles in value - if at the same time the gold price goes up 5 times, you lost out by being in financial assets. And I think this is what has happened since year 2000. In year 2000, as you know, you could buy with one Dow Jones, 44 ounces of gold. And now you can buy less 15 ounces of gold.

Now, I'm not saying that gold cannot have a meaningful correction, but I think that the central banks have created actually a state which I would almost call a hyperinflation where asset prices go up very substantially and they don't make you really richer. I mean say in 1980, there were six billionaires in the world, and today you have thousands of billionaires in the world, everywhere. And money - the value of money - the purchasing power of money has

depreciated very considerably. And I'm not speaking here of the US, because I was recently in New York and I saw that the price level in New York is actually quite reasonable compared to, say, the price level in Europe and in other countries. But usually when you have a situation like the US that has achieved relatively low price levels through currency devaluations - and the US has pursued a policy to lower the value of the dollar - what usually follows (and not every time - usually what follows) is high and accelerating inflation rates. And the US government of course they will understate inflation, but the pocketbook of the consumer will notice this increase in inflation and what you will then get is essentially prices going up and the standards of living of people going down - in other words, stagflation. [25:08]

JIM: Isn't this one of the signals that gold is giving to the financial markets? When you look through this period of time where we have seen nominal increases in assets and stock markets around the globe, yet if you look at the summer of 2001 when gold was at 255, and here we're looking at gold heading towards \$900 - do you think this is what is being recognized around the globe, that everybody knows that money is dying, it's losing its value so gold is becoming the ultimate currency to hold?

MARC: Basically, my view is this: Normally, the safest investments in a society is cash, deposited in a bank or in Treasury bills. But the Western democracies and governments in general have created over time an environment where actually cash is a disastrous investment because you're losing out to inflation like in the 70s as a result of consumer price increases or in the last couple of years as a result of asset price increases. Now, I'm not suggesting that there cannot be times - three months, six months, one year - when cash does better than, say, stocks or better than real estate. Say, in the last nine months it was better to be in cash than in stocks that depreciated or in real estate that depreciated. But basically, if you print money like the Fed or other central banks do, the value of money - of paper money - goes down and then it's reflected in an increase in the value of assets such as gold that cannot be multiplied at the same rate. I mean someone could say, "oh, the gold price has gone up a lot since 2001." I can turn around and say: "No, the gold price is the same. It's the dollar the dollar that has collapsed against the price of gold." And why did the dollar collapse against the price of gold. You call up Mr. Greenspan and Mr. Bernanke and you ask them about it. Of course, they will never give an answer. Each time Ron Paul asks them a sensible question they just evade the question and they move on to something else because, as I explained, they are a bunch of liars. And actually, if there was a court for honest money, both Mr. Greenspan and Mr. Bernanke should be hanged.

JIM: You know, it was interesting - you mentioned Congressman Ron Paul. The last time Bernanke was on Capitol Hill, he asked him about curing inflation with more inflation, and asked him about what was happening to the dollar. And Mr. Bernanke responded - which I was horrified - and he said, "well, actually if you live in the United States and you pay for things with dollars it really doesn't affect you."

MARC: He's out of his mind. Go to Zimbabwe and ask the citizens there: If you pay in Zimbabwe dollars it affects you that the currency has collapsed? Of course it affects you.

My view - Subscribers will recognise many Fullermoney themes in this interview. In my opinion Marc Faber is unrivalled in terms of his long-term panoramic vision. For timing, I suspect that he and every other investor / trader would agree that it is difficult to be travelling extensively and also remain at the top of one's game.

Here are a few additional thoughts:

The printing of money by central banks will ensure that we avoid outright deflation, short of an ecological disaster of biblical proportions. In countries experiencing strong economic growth, Australia for instance, CBs will try to keep a lid on inflation by increasing short-term interest rates until growth weakens and / or inflation subsides.

In the weak US environment, the Fed is targeting the economy and stock market, ignoring inflation other than mild jawboning, until GDP growth is stronger. Today, Bernanke and Co are more concerned about deflationary pressures from the credit crunch, burst housing bubble and decline in consumer spending.

Most of today's global inflation is from commodity prices, of which the surging cost of food is particularly emotive. However this has not sparked the wage inflation seen in the 1970s, because of competitive pressures due to globalisation, particularly in manufacturing. In countries where tax revenue is falling due to slowing growth the cost of government services is often the next highest inflationary component after commodities.

Regarding stock markets, Marc said:

And so the big bubble is probably in emerging markets; and these markets, obviously if the S&P goes down, will be hit very hard. And I would argue, if someone puts a gun to my head, and says, "Marc, you must buy stocks," as much as I dislike saying this but I would probably rather buy US stocks today, than say some of the emerging markets that are selling at 30 to 50 times earnings.

I'm not sure which markets he is referring to but I do not see bubbles in Fullermoney themes. China's [Shanghai A-Shares](#) Index, which rallied today in contrast to most other stock markets, has seen its PER decline from a high of 63.16 on 17th November to 37.34 currently. However the [Hang Seng](#) Index is on PER of 14.70 with [H-Shares](#) at 18.99 today - far from bubble territory given the strong growth potential. India's [Nifty](#) trades at 21.16 times earnings but here also growth in corporate profits is likely to remain strong. These are not bubbles today although they are candidates to become future bubbles as central bank liquidity chases the best returns.

With the US stock market, I see the domestic and financial shares in deep recession, while many multinational companies are doing quite well, thanks to strong growth elsewhere and the weak USD. If I were to buy US shares, they would certainly be selected from the latter category.

Regarding the [dollar](#), with US short-term interest rates declining, the economy weak and the Fed printing, I see very little upside other than periodic bouts of short covering within the overall downward trend. The next medium-term recovery for the dollar is unlikely to occur much before the US economy is firming and the Fed indicates that short-term rates will rise. However I would begin to turn bullish of the greenback in the event of multilateral intervention.

March 6th Credit Swaps Thwart Fed's Ease as Debt Costs Surge

This [article](#) by Abigail Moses, Hamish Risk and Neil Unmack for Bloomberg covers a number of important issues relating to the credit default swap market. Here is a section:

Credit trading models used by Wall Street have gone haywire, raising company borrowing costs even as Federal Reserve Chairman Ben S. Bernanke cuts interest rates.

General Electric Co. is one of five U.S. companies rated AAA by both Standard & Poor's and Moody's Investors Service, making its ability to repay debt unquestioned. Yet when the Fairfield, Connecticut-based company sold 2.25 billion euros (\$3.35 billion) of five-year bonds last week, its annual interest payment was \$17 million higher than on a sale nine months ago.

Borrowers from investor Warren Buffett's Berkshire Hathaway Inc. to Germany's HeidelbergCement AG face the same predicament. Yields on \$5.12 trillion of corporate bonds tracked by Merrill Lynch & Co. average 2.05 percentage points more than U.S. Treasuries, the most since at least 1997.

The higher costs are an unintended consequence of securities that allow investors to speculate on corporate creditworthiness. So-called correlation models used to value them have become unreliable in the fallout from the U.S. subprime mortgage crisis. Last month some showed the odds of a default by an investment-grade company spreading to others exceeded 100 percent -- a mathematical impossibility, according to UBS AG.

"The credit-default swap market is completely distorting reality," said Henner Boettcher, treasurer of HeidelbergCement in Heidelberg, Germany, the country's biggest cement maker.

"Given what these spreads imply about defaults, we should be in a deep depression, and we are not."

Hedging Losses

The problem started in the second half of last year when subprime mortgage delinquencies started to rise, causing investors to retreat from complex instruments such as synthetic collateralized debt obligations, or packages of credit-default swaps that became hard to value. The swaps are contracts based on bonds and used to speculate on a company's ability to repay debt.

As values of CDOs began to fall, banks that had sold swaps underlying the securities started to buy indexes based on them instead, a method of hedging their losses on portions of the CDOs they owned. The purchases are driving the cost of the contracts higher, raising the perception that company bonds tied to the swaps are suddenly riskier and leading investors to demand higher yields throughout the corporate debt market.

The Markit CDX North America Investment-Grade Index, a gauge of credit-default swaps on 125 companies from Wal-Mart Stores Inc. to Walt Disney Co., more than doubled since the start of the year to a record 171 basis points on March 4. The index, which dropped to a low of 29 in February last year, was at 170.5 basis points at 7:10 a.m. in New York, according to Deutsche Bank AG.

My view - Are we going to see an increase in actual delinquencies over the coming year or two? Another Northern Rock or possibly two may emerge and a number of more funds will go bust, but is GE going to default on its bonds, I really doubt it. If we are not going to get a deep, multi-year depression, then the price of bonds linked to highly rated company debt is very appetising for an institutional investor with the ability to bid below the market.

I believe, what we are seeing today is model myopia. Banks rely on models to price credits and are refusing to stand back and look at the bigger picture. Surely, investors should be listening to the corporate sector, that ultimately pay the coupons, rather than to the market for insurance on these bonds. Companies, for the most part, continue to say that they are quite healthy. The CDS market reflected the complacency of the market before the credit problems and is now pricing in the worst case scenario. As human beings we are less likely to buy insurance when the going is good and much more likely to hedge when we have just gone through a traumatic experience. A quote often mentioned at The Chart Seminar comes to mind:

"Our deeds travel with us from afar and what we have been makes us what we are." George Eliot, Middlemarch.

The appropriate price for many investment grade credits is probably less than it was a year ago, but substantially more than it is today, setting up an interesting position for institutional investors with the ability to bid below the market and succeed in buying high yielding credits at bargain prices because the issuer is temporarily distressed.

I believe it is only a matter of time before banks start to behave with the level-headedness that we would expect from financial institutions. When this occurs, the credit markets could rally substantially.

March 6th Filtering the S&P 500 sectors indices

Today, I put all of the S&P sectors into a folder in my Favourites and proceeded to filter the contents.

The best performing indices in the last three months have been [Trucking](#), [Agricultural Products](#), [Oil & Gas Exploration & Production](#), [Casinos & Gaming](#) and [Fertilizers & Agricultural Chemicals](#). In the last month Oil & Gas Exploration & Production tops the list, [Diversified Metals & Mining](#), [Aluminium](#), [Construction & Engineering](#) and [Steel](#) were the best performers. These results tell us all of these sectors are relative outperformers. It also shows that while agriculturals were some of the leaders over the last three months, industrial metal related companies are coming up strong. From our daily click-through of markets, we came up with the same conclusion relating to the individual commodities. However, this click through tells us that these sectors are also outperforming just about everything else.

When we rank the list by changes between 1 and 3 months, we see that Construction & Engineering is also the second fastest riser on the list, Construction Materials also fare well. Diversified Metals & Mining is also in the top-20 risers over the last 1-3 months. This perhaps indicates that these markets have further to move on the upside. Oil & Gas Exploration & Production is the clear momentum leader and a clear downward dynamic would be needed to check upside potential beyond a brief pause. The Agricultural Products Index is also at an interesting level as it is testing the recent high near 800 and would need to sustain a move below 700 to question potential for an upside break.

February 26th Nasdaq shares: a technical health check

I last reviewed a number of Nasdaq shares on [October 11th](#) and [12th](#) when the Index was breaking upwards against the [S&P 500](#). Since then the Nasdaq 100 has fallen back into its base against the S&P and needs to rally above 1.3 to reaffirm its potential to outperform.

The [Nasdaq](#) has succumbed to similar selling pressures as other global indices, commencing with the fall on November 8th which broke the medium-term uptrend. The break below 2000 in January signalled the onset of another bout of selling, climaxing on the 22nd. In the last three weeks, the downtrend has lost momentum and has posted three higher lows. It would need to sustain a move below 1700 to question scope for some further higher to lateral ranging.

Index heavyweights such as [Google](#), [Apple](#) and [Microsoft](#) together make up more than 20% of the Nasdaq-100. ([Nvidia](#) also shares a similar chart pattern.) These shares along with a small number of other technology shares led on the upside and are underperforming during the correction. None have rallied meaningfully this month and while they look overextended, there are a number of conditions they would have to meet before looking like they were about to reassume their previous bullish mantle.

The first pre-condition, is these shares will have to find support and hold above it. Since they have undergone some quite severe technical damage, it looks unlikely that they will be able to push back up to their highs directly, but will require some base building before a more orderly trend emerges. A period of convalescence, which could be potentially lengthy, is likely to ensue. Ideally, this would produce a progression of incrementally rising lows to indicate that demand is returning at progressively higher levels.

At present, global infrastructure plays such as [Steel Dynamics](#), [Joy Global](#) and [Foster Wheeler](#) as well as Pharmaceutical companies such as [Teva Pharmaceutical](#) and [Sigma Aldrich](#) are leading the Nasdaq. However, considering these sectors are relatively small, they are unlikely to have a major impact on the overall Index. There is no denying that many technology companies are considerably cheaper now than they were three months ago, but they need to perform considerably better than of late to encourage investors back into the market.

Given the general re-pricing of risk globally, there is the distinct possibility that investors will be more attracted to yield rather than growth for the coming months as some of these beaten up shares move into base building phases.

March 11th On Topix PER and valuation contraction:

"David, I note that today the Topix closed at the lowest PE since 1993, and very low price book and price sales ratios (cf. Bloomberg). Japan seems to be the only "cheap" market around relative to its own history. However, this made me think of a theme you used to emphasize, that we are in a bear market, defined as "a generational decline in PEs". I haven't heard that phrase recently on your audios. Do you think that the process of PE compression is finished?

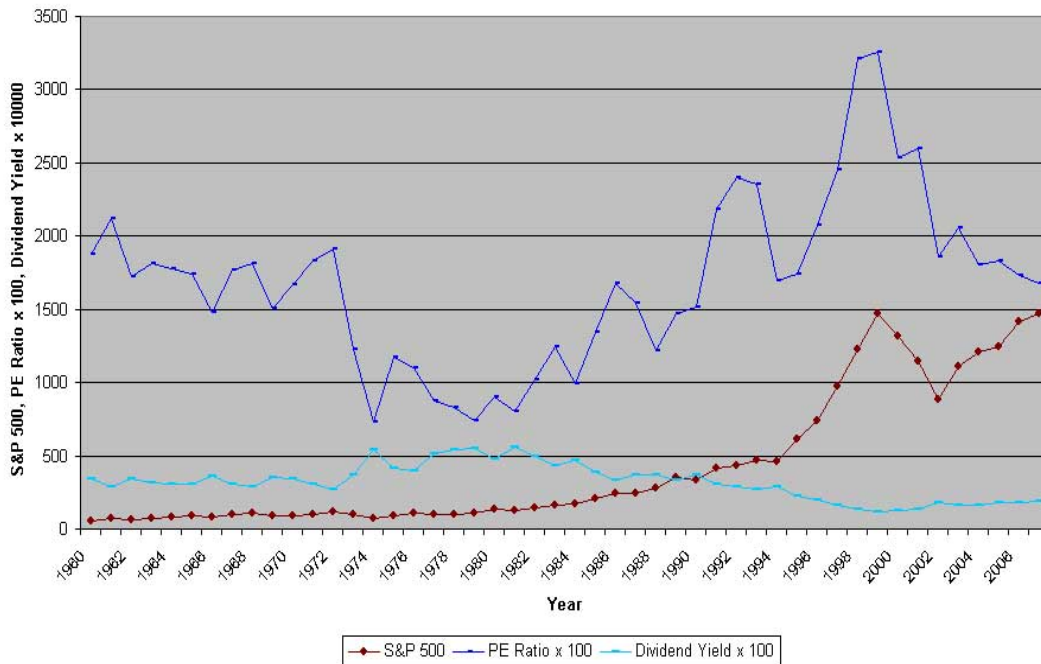
"Thanks for all the good work."

My comment - Thanks for your kind words, and for pointing out an interesting milestone regarding the PER for Topix, although I am surprised by the 1993 date. Is there a possibility that you meant 2003?

Regarding your question, historically, lengthy periods of valuation expansion, often followed by valuation contraction of a similar duration, have been huge influences on stock market returns. For instance, on Wall Street valuations rose for many years at the beginning of the last century and up until the 1929 Crash, stayed low into the mid-1940s, before expanding into the 1960s, followed by a big contraction into 1982, before expanding up into 2000 and subsequently contracting once again.

I recall the 1960s onwards data and you will be able to see much of that history on the chart below from techfarm.blogspot.com, although the yield scale is too condensed and an arithmetic scale for the S&P scrunches early data. If anyone in the Collective has a better picture of this information, including earlier history, I would be happy to post it for our further edification.

S&P 500 Historical PE Ratio and Dividend Yield
1960 to 2007
techfarm.blogspot.com



The graph will show enough for subscribers to understand why I felt that Wall Street could easily experience a generational-long period of valuation contraction following the burst bubble in 2000, with the reaction lows occurring during recessions. However I stopped referring to it because some people would hear my comments regarding a secular bear in valuations and assume that I was referring to all stock markets and also implying that trends for the S&P and DOW would decline. Obviously not because the Fed could, in theory, inflate US stock market indices to vast numerical gains, although they might continue to fall against [gold](#).

I have been unable to source historic PER data for the Nikkei and Topix on Bloomberg, due to data distortions, but I did find interesting yield information dating back to 1993. At 1.66% and 1.78 for the [Nikkei](#) and [Topix](#), respectively, these have certainly improved but are not at globally enticing levels and may remain resistible for the proverbial Mrs Watanabe, unless she feels that the yen carry trade really is dead. My own view is that with minimal short-term rates, the yen carry will be utilized once again when the current phase of deleveraging ceases and animal spirits return to more than just commodity markets. Incidentally, you can monitor yield charts for Japan's Nikkei and Topix in the Library, although there is less back history as they were only *tickerised* (a *Bloombergism*, according to Eoin) a year ago.

In conclusion, Japan has experienced a considerable valuation contraction since its bubble burst in 1990 and historic PERs of approximately 15.50 for Nikkei and Topix are not excessive. However to view this in a global perspective, a number of other stock markets are cheaper today, as you have seen from those monthly tables that Eoin produces. I can also recall single-

figure Japanese PERs during the 1960s and 1970s, although I do not think that either economic conditions or market sentiment justify a return to those levels. I suspect that Japan is near a sustainable low and therefore a long-term recovery situation, but I maintain that charts do not yet indicate that a new uptrend is commencing. Meanwhile, the Nikkei ([monthly](#), [weekly](#) & [daily](#)) and Topix ([monthly](#), [weekly](#) & [daily](#)) indices steadied near their range lows today and I expect a nice bounce tomorrow, following Wall Street's gains.

March 11th Filtering the Nikkei 225

I took a look at the Nikkei 225 this afternoon, using the Chart Library's filtering system. I did this looking at 1 and 3-month performance and looking at those which had moved up the rankings, in terms of relative performance, fastest. I also looked at those which had moved up the rankings fastest between 1 and 12 months. (We would also welcome feedback on how subscribers are best utilising the Filter system.) This to find stocks which were outperforming the Index and to ascertain which are presently leading the market. The [Nikkei](#) broke down from the 6-week trading range this morning but rallied well during the session to close up on the day. Based on the support lent to the markets by the Fed, a rally back upwards to test the top of the range would not be surprising and it would need to sustain a move below today's lows to question the likelihood of this occurring.

Breweries have outperformed throughout this correction. [Asahi](#) Breweries is testing its [20-year highs](#) near ¥2000 and would need to sustain a move below ¥1800 to question potential for an upward break. [Kirin](#) Breweries broke upwards from its [15-year base](#) in 2006 and has been consolidating the move since. It is currently rallying towards the range highs below ¥2000 and needs to sustain a move above that level to reaffirm the overall uptrend. [Sapporo](#) Holdings remains in an overall [uptrend](#) but has lost momentum over the last year. It needs to sustain a move above ¥1000 to reaffirm the uptrend.

Companies described as Import/Export companies have also outperformed since the January lows. Many companies such as Marubeni ([monthly](#), [weekly](#)), Mitsubishi ([monthly](#), [weekly](#)), Sumitomo ([monthly](#), [weekly](#)), Mitsui ([monthly](#), [weekly](#)) and Itochi ([monthly](#), [weekly](#)) fell in line with the overall index into the January lows but have rebounded well and found support above those levels. They would need to sustain moves below that area to question further higher to lateral ranging.

[Japan Steel Works](#) accelerated to its highs near ¥2000 in July last year and has moved into a [consolidation](#) of that gain. Given the relative performance of the overall index in that time, Japan Steel Works is holding up well. A sustained move below the January lows near ¥1350 would be needed to question potential for further higher to lateral ranging.

[Konami](#) is testing the top of the [7-year base](#) near ¥4000 and would need to sustain a move below ¥3500 to question scope for an upward break. [Pioneer](#) Corp hit a [25-year low](#) in January but has rallied in excess of 50% since then and would need to sustain a move below ¥725 to offset scope for some further higher to lateral ranging. [Sanyo Electric](#) has a similar pattern to

Pioneer above, it also hit a [20-year low](#) but has almost doubled since. It would need to sustain a move to new lows to question potential for what could be some extensive base building.

Companies such as Sumitomo Metals & Mining ([monthly](#), [weekly](#)) and Toyo Zinc ([monthly](#), [weekly](#)) fell precipitously into the January lows but have since rallied impressively and appear to be finding support above those levels. They would both need to sustain a move below their January lows to question potential for further higher to lateral ranging.

Amongst sectors, the [Topix Banks](#) Index has fallen considerably in the last year and is approaching levels not seen since 2003. In 2003, Banks were leading the market higher and the resulting rally caused a large number of investors to reassess Japan's investment potential. On this occasion, as Banks continue to decline, they are not offering the same kind of leadership. This may indicate that Japan's recovery may take longer on this occasion, and may require some further support building before it can support a meaningful rally.

February 19th on Australia

[Australia](#) is one of only a handful of developed countries, offering a politically stable environment, with respect for minority shareholder rights as well as excellent reserves in the ground. This is why we continue to consider Australian companies, with world class reserves in the ground, as collectors items from an investment perspective. The [ASX 300 Resources index](#), made up of 78 companies, accelerated to its high near 6500 in November following an impressive rally from the August lows near 4750. The subsequent retracement briefly retested those lows and the Index has again rallied impressively. In the short-term, a move below 5500 would be needed to hinder upside potential, while a sustained move below 4750 would be needed to question the integrity of the overall uptrend.

In line with the bullish environment, healthy state of the Australian economy and rising interest rate environment, government bond [yields](#) are rising and the yield would need to sustain a move below 5.75% to question scope for additional upside. Looking at the [price](#) charts, the 10yr has been in a developing top formation for much of the last decade and is now breaking down. A sustained move back above 94 would be needed to question scope for further weakness.

The [Australian Dollar](#) has been basing against the greenback for much of the last 20 years and broke upwards late last year. It continues to consolidate that gain but would need to sustain a move below [0.85¢](#) to question scope for a test of parity and potentially even further strength in the coming years.

February 25th On analysing and trading silver:

"My sincere thanks and appreciation for all the work you guys do. It is now a habit to start every day with your audio and a coffee... it's now daylight at 6am now in the south of England!"

"A couple of times lately in your daily audio (which is way too short) you've mentioned the silver and gold prices and alluded to formulating an exit strategy prior to the inevitable correction.

"As I watch silver wind up for what may well be its biennial blow off I wonder, ponder and pore over the charts.

"My limited grasp of TA leads me to understand that the "pole" prior to a flag/triangle/pennant should be of the same length/value as the "pole" following the breakout. Looking at the silver chart, this leads me to conclude that the pole from September 2005 to May 2006 should dictate the size of the pole which started around September 2007.

"However, the pole from around April 2003 was at least \$4, yet the pole Sept 05 to May 06 was at least \$7. So how to extrapolate a target for the present pole which started Sept 07?

"Or perhaps I'm in error here, which is more likely. I've trawled through Schwager, Murphy and any other TA source I can find, but I'm at a loss on this one. But as I think about it, the charts never go in predictable steps dictated by poles and pennants anyway ... or do they? They're never so regular. I've tried phi price objectives and all sorts but to no avail.

"I'm up to the proverbials here in silver futures contracts, so you'll appreciate that it's a subject in the front of my mind and close to my heart. When the correction comes I have to assume the magnitude/percentage drop will be comparable to May/June 2006 and I have no desire whatsoever to repeat that one, so this time my exit strategy has to be at least half-baked.

"I'm not trying to pick a top here, but I'd like to at least land in the right airport, as it were. Any comments from yourselves or the Collective would be much appreciated.

"PS Eoin, I trust your good lady is as well as she can be and well on the way to full health."

My comment - Many thanks for your kind words and enthusiasm for the service. And well done for seizing your opportunities in silver!

Regarding Mrs Treacy, Eoin told me this morning that she feels well and is back at home. They are both looking forward to the birth of their second child next month.

Regarding price chart analysis, you will know that at Fullermoney we favour a simple approach, believing that interpretation is an art rather than a science. So we look for trend consistency, to tell us whether or not all is well. In terms of the big picture, we also look for other forms of behavioural repetition and I commend you for recognising a degree of similarity in silver's medium-term cycles ([weekly](#) & [monthly](#)).

You will note that these have lasted approximately 26 months. If that cyclical nature is maintained, and there is no certainty that it will be, we might expect a peak around mid-year. However cycles can quicken as more people recognise and participate in them. Therefore we can assume that quite a few silver traders will be looking for an important peak in the next few months.

It would be prudent, I suggest, to tell ourselves that silver's next peak could occur at any time, including last Friday which is the high to date. However the orderly step sequence of ranging price rises in recent weeks suggests that we could be lucky, in which case silver accelerates once again, prior to the next significant correction.

An important point for me is that the price action is still consistent. This suggests that the trend is still in motion. In other words, it probably has further to run because nothing has occurred to prompt a widespread reassessment among silver traders, including ourselves.

Meanwhile, we certainly do not want to see the current sequence of higher reaction lows taken out. The last one was at \$17. As for the upside, I regard price targets as guesswork - often no more than wish lists - so do not attach much significance to them. However if we ask anyone in silver the theoretical question: where might the next psychological resistance level be, I suggest most would say \$20. Trends often pause near round numbers, as you know, because they are widely anticipated targets which can also cause them to become reassessment points.

Regarding the "poles" that you mention, these semi-log charts ([weekly](#) & [monthly](#)) indicate that the two previous advances were of a similar percentage. If the sequence is repeated, silver would easily reach \$20. However it would be foolish to count on this. You and I can only deal with what the market provides. In a strong uptrend, our focus should be on running the trend, while it is consistent but with trailing stops that will take us out relatively quickly when something goes wrong, as it surely will at some point. Upside acceleration would make our task easier.

Last but not least, keep an eye on platinum ([weekly](#) & [daily](#)) as it so often leads. Currently it shows some loss of momentum but not much selling pressure to date.

February 27th Industrial Metals Review

How many times over the last six years have you heard that the industrial commodity cycle, or "bubble" as it has so often been called, was over? Was it a few times, a dozen perhaps or many? I have certainly been inundated with reports and comments concluding that there was no supercycle; speculation was responsible for the strong gains, and prices had reverted to a bear trend once again, due to either increasing supply, substitution or slower economic growth.

In fairness to these pundits, when industrial metal prices accelerated dramatically, they subsequently fell back sharply. And thus it always was.

Markets that generate considerable interest are often volatile, not least commodities. Market prices are driven by emotional crowds, with sentiment swinging in pendulum fashion between the extremes of manic and depressive.

As for supercycles, the 21-year bear market for most metals until 2001 surely qualified, as it pushed prices for many to all-time (inflation adjusted) lows. And don't the biggest bull markets spring from the ashes of severe bear trends? After all, the 1980s and 1990s pushed the mining industry into survival mode. Consequently key personnel drifted away, plant decayed and there was little exploration or development of known ore bodies.

Uniquely, just as this mining slowdown reached its apex, demand rose to unprecedented levels in only a few years. In the last commodity boom of the 1970s, demand for metals came mainly from the USA, Europe, Japan and a few of Asia's 'little tiger' economies. Today's unprecedented demand for metals is led by China but also comes from burgeoning global infrastructure development. Yes, the USA is experiencing a decline in metals usage but China is a much bigger source of demand for these commodities which remain in scarce supply.

What can we conclude from the charts of futures traded metals and which offer the best prospects? I've reviewed them in alphabetical order:

Aluminium - This has exploded upwards in the last six weeks ([monthly](#), [weekly](#), [daily](#) & [inventories](#)), following a very lengthy trading range which is most likely a medium-term consolidation. Ostensibly, South Africa's power outages and China's harsh winter sparked the move which also indicates a scramble of short covering. Some resistance is likely near the 2006 peak - watch for a downward dynamic and / or loss of momentum to signal the onset of a consolidation. Thereafter, if most of the recent gains are held during this process, the platform of trading evident above \$2400 should support an extension of the long-term uptrend. This will occur sooner rather than later if the inventories, which show some loss of upside momentum, commence a downtrend.

Copper - Here also we have seen a surge of short covering recently ([monthly](#), [weekly](#), [daily](#) & [inventories](#)) and there is also consumer demand evidenced by the downturn in inventories. If gains are now consolidated near or above the 2007 rally highs, we will have further evidence that this whole range is a lengthy medium-term consolidation in its latter stages, prior to a resumption of the long-term uptrend.

Lead - These charts ([monthly](#), [weekly](#), [daily](#) & [inventories](#)) similarly show evidence of both short covering, and user demand as inventories are declining. While former resistance evident above \$3500 is likely to make upside progress more laboured as it is tested, the daily chart shows a consistent staircase uptrend. When this loses momentum, I would assume that lead has commenced a reaction and consolidation of gains, prior to an eventual push to new highs.

Nickel - This is intriguing because it is one of the biggest movers - we have already seen what some of the other metals are doing, and nickel shows evidence of base formation development ([monthly](#), [weekly](#), [daily & inventories](#)). It commenced support building following last August's low but then fell back to extend the pattern. This is an occupational hazard with bases - one never knows how long they will range before sustaining the next upward trend. However what we describe as "Commonality" at TCS helps - rallies by other metals tell us that the sector is in demand once again. The key for nickel will be a decline in inventories and they have lost upside momentum recently. A surge in price should only be a matter of time.

Tin - Here we have a further example of what metal prices can do when inventories turn down ([monthly](#), [weekly](#), [daily & inventories](#)). Interestingly, tin saw only a brief reaction when inventories rose from May to August last year. Perhaps because they were low to begin with and this is probably a reason why tin is the first metal to hit a new high in 2008. Tin has already seen a big move so arguably has less upside potential than the others. Nevertheless the trend is reasonably consistent and higher reaction lows are the key feature. A break in this sequence, best seen on the weekly chart with the last reaction low slightly beneath \$16,000, would be required to negate higher scope. Clear upside acceleration within this trend would also indicate an approaching peak.

Zinc - This is also intriguing because of the big fall from an accelerated peak and small base from which we have seen an upward break today ([monthly](#), [weekly](#), [daily & inventories](#)). Given the considerably firmer tone for industrial metals recently, this pattern appears to have launched a short covering rally towards \$3000. However the risk, as we saw with nickel is that tin then falls back to extend the base. The key factor as to whether zinc has commenced a sustainable uptrend or requires more support building, will be inventories which are still rising but at a slower rate.

Tomorrow, I will take a look at backwardation / contango charts for these metals, aiming to draw some further conclusions in terms of both potential and timing.

See also Eoin's earlier [review](#) on 1st February.

February 28th Metal futures backwardations or contangos

In yesterday's feature on futures-traded industrial metals, I mentioned that I would complete the appraisal with a look at the backwardation / contango charts.

For those new to this terminology, commodities normally trade at a contango, meaning that the spot price for immediate delivery will be lower than prices for forward contracts, reflecting US interest rates (the carry cost) for these mainly \$-denominated commodities.

Conversely, if there is a shortage of supply relative to demand for immediate delivery, the commodity will trade at a backwardation, meaning that the spot price will be higher than the forward contracts.

This matters because the biggest short to medium-term upside moves in commodities will often occur against the background of a persistent backwardation, indicating a scramble for available supplies.

So, in addition to yesterday's assessment of potential, what else can we conclude from the current backwardations or contangos?

I am using weekly graphs for this review but of course subscribers can see more historic data on monthly charts, available in the Library.

Aluminium - The [contango](#) has narrowed in line with the decline in US short-term interest rates but shows no evidence of a supply squeeze similar to what proceeded last year's price spike. Consequently short covering is likely to be an important factor behind recent strength for aluminium [prices](#) while renewed consumer demand and speculative hoarding have yet to cause a shortage.

Copper - While the spread between Comex 1st and 2nd month copper is flat at present, LME copper shows an increasing [backwardation](#). This confirms that short covering has been followed by a surge in consumer demand and possibly also speculative hoarding, which has overwhelmed immediate supplies, making it all the more likely that new highs will be [seen](#) before long.

Lead - As with copper, prices have moved into [backwardation](#) recently. Lead should at least challenge last year's [highs](#) if the backwardation persists and widens.

Nickel - The developing [base](#) formation is inviting but a [backwardation](#) is probably required for nickel to fulfil its big upside potential sooner rather than later.

Tin - The only futures traded industrial metal currently at a new [high](#) for the last few years, tin's strength is surprising since a [contango](#) persists. Consequently recent strength may be due mainly to short covering, following a lengthy pause causing speculators to conclude that a major top was forming. However inventories are low so perhaps someone (China?) is also buying while it can.

Zinc - As with nickel, evidence of a [base](#) formation is inviting. However a [backwardation](#) is required for zinc to overwhelm potential overhead resistance sooner rather than later.

Conclusion - Shorting any of these metals in the current environment would probably be hazardous to your wealth. Upside commonality (all are now strengthening simultaneously) has returned. This clearly favours the bulls, who are spoiled for choice. In other words, I suspect all of these metals will move higher, but some more than others.

In deciding which have the most potential, one has to weigh the various technical / fundamental factors, indicated by chart patterns, inventory data and the backwardation / contango status. Personally, I would give an equal

weighting to the price chart action and inventory trend, and expect the backwardation / contango position eventually to fall in line.

Of course there are also the known unknowns, to quote Donald Rumsfeld in a different context, mainly concerning supply disruptions, although the strength or weakness of the global economy and China in particular will be an important factor. I consider supply scares to be inevitable but have no idea where, when or for which metals. I am reasonably confident regarding the global infrastructure boom, despite a weak US economy. I also expect consumption to increase in progressing rather than regressing economies (developing and developed are outdated classifications for countries).

Working with the known knows, including factors mentioned and illustrated yesterday, aluminium and tin are my least favourites, in that order. I'm rating lead somewhat higher because of its backwardation. I rate copper higher still because of its falling inventories, clear backwardation and broad platform of trading. A sustained break above this level would look very bullish. However, zinc and nickel have catch-up potential because they are barely out of the starting blocks for this current upside move. Inevitably there are reasons for this recent underperformance, to cast doubts on my preference for these two. Nickel is my favourite despite the risk of a delay before it really performs. However as nickel inventories start to trend down, and they have lost upside momentum, the rally should be explosive.

I currently hold ETFS for June copper, nickel and zinc in my trading account, but I bought too soon and have been surprised that this renewed strength for industrial metals has taken so long. I will probably increase at least some of these positions.

My personal investment account is heavily long the miners. These are no longer the steals that they were in late January (I prefer to buy them following shakeouts) but consider their profit potential at today's prices for aluminium, copper, lead and tin, plus the catch-up scope for nickel and zinc. Costs are also rising but certainly not at the recent rate for metal prices. Consequently miners are now in a position to make considerably more money without increasing production.

February 29th Uranium Market Outlook and essay on commonality

My thanks to a subscriber for this impressive [report](#) from UXC. Here is the first half of the conclusion:

The following slide looks at some potential market scenarios for the spot price. The current trend in price indicated by the blue line shows further weakness following a short recovery off its low of \$75. The question is whether the recent recovery was what is known as "dead cat" bounce, where price makes an abortive recovery following a sharp fall, or whether price will eventually recover to even higher levels than it previously attained. We label this second scenario a "rhinoceros market" given the shape of the initial price spike (the horn) and the subsequent more sustained increase (the rhino's head), as shown by the green line. In the former case, price can be seen as being bid

up in a speculative frenzy which was unsustainable, resulting in price now falling back to earth. From here, it could level off or perhaps fall further, as the market is currently under downward pressure. In the latter case, the initial price run-up can be seen as a situation where the market just got ahead of itself, suggesting that price will return to these levels and go higher.

My view - Most analysts understandably assess the price outlook for uranium or any other commodity on the basis of production and consumption estimates over the next year or more. Since they are peering into the unknown, in other words making guesses, it is not surprising that opinions will vary widely.

I respectfully suggest that there is another way to assess the price outlook, which is far less subjective and based on facts rather than estimates, of production and consumption, which are likely to be only part of the story in any event.

I am not about to declare that the answers concerning future price trends are contained in this [chart](#), although it provides a practical grounding. For instance, it did not take a genius to conclude that once uranium's parabolic trend stopped moving higher, the price would fall.

Instead, I am going to talk about Commonality - my term for an analytical approach that I have used for more than 40 years.

Commonality is the study of related instruments, in this instance, markets that are in a similar category to uranium and therefore may be experiencing overlapping price cycles. For instance, if there are twenty other similar or related instruments (there may be more or less), the odds are only 1 in 20 that uranium is actually leading the cycle. Crucially, some may have already commenced their next trending moves. If a number are heading in the same direction, the odds that uranium, which is currently ranging, will follow their lead.

I rate Commonality as a more useful analytical approach than what people are subjectively saying about future supply and demand, which may or may not be right. I also rate Commonality much more highly than the often subjective interpretations of an individual chart pattern, which people may interpret differently, depending on their methodology.

For instance, the Fullermoney approach to chart interpretation, developed through observation and with the help of The Chart Seminar since 1970, is factual / behavioural. Applied to uranium, we can see that it trended gently and consistently upwards; people then chased the price higher in an increasingly speculative and therefore unsustainable acceleration; it fell back sharply and is now in a range, creating additional uncertainty.

Those are technical facts, useful at inflection points indicated by a clear loss of trend consistency, which causes participants to reassess. Widespread reassessment will halt and even reverse the trend. For instance, 'oh dear; not only is it no longer going up, it is weakening. Profit erosion! We better get out.'

Or, 'it has stopped falling; cover shorts and go long. Wait - it's ranging; I'm confused.'

It is time to consider Commonality, commencing with the question: what does uranium have in common with other commodities? Well, it is a metal, and it is also energy.

So, have any other metals and energy commodities shown steady uptrends eventually culminating in acceleration? Yes, actually, they have all done that at one stage or another during this cycle dating back six or seven years.

When the acceleration stopped did they all fall back quickly and sharply? Yes, actually, although a few ranged near their highs before heading lower.

When they stopped falling did they then go into short-term ranging patterns for a few weeks, or lengthy medium-term ranges lasting anywhere from several months to a little more than two years? Most ranged for quite a while, as I recall.

Good! Well recalled and if you were not sure you could easily check it out by looking at the charts - it is usually time well spent. Now for the crunch question: when they stopped ranging sideways, what happened? They ranged higher. All of them ranged higher? Yes.

Did the higher ranging have any other characteristics? Yes, the trends steepened, gradually at first, before accelerating higher once again.

When they stopped accelerating higher, what happened? Some ranged for a while; others fell more quickly but eventually they all fell back quite sharply.

Alright, this next question is particularly important: did they find support above their previous sharp reaction lows? Yes, I believe they did.

Did any of them then repeat the cycle of ranging for quite a few months before heading higher once again, reaching new highs within the overall upward trends? Yes, some several times.

OK, brace yourself - what is uranium going to do? I don't know. Don't give up after all that informative observation and recall - use Commonality. Oh, I get it - uranium will probably range for at least a few months before trending to new all-time highs, and perhaps eventually accelerating to another peak.

I think you are right.

Then let me ask you a question for a change: are you certain? There is no certainty in markets or life, other than death and taxes. However you have identified the cycle, which is still in motion, so the odds are certainly in your favour.

But, but what about Bernanke or the banks? Don't lose your focus, unless you are moving on to analyse another asset class that has little to do with what we were just talking about.

March 7th on platinum

Mineweb.com: More power possible for South Africa mines? - [This article](#) by Tessa Kruger for Mineweb covers the possible easing of power concerns in South Africa. Here is a section:

While the South Africa Chamber of Mines is still awaiting an answer from government and Eskom regarding increased power supply to mines, Minister of Minerals and Energy Buyelwa Sonjica told Bloomberg TV that power supply to mines will be increased to 95% of average consumption.

According to Bloomberg TV, the minister said the "curb" on power supply to mines will be eased as the country's electricity system has stabilised.

This report comes a day before the Chamber of Mines and National Union of Mineworkers (NUM) expect the government and Eskom to respond to their call for increased electricity supply to mines currently running at 90% of average consumption.

Frans Baker, spokesperson for the chamber, said the organisation and labour organisations made a presentation to government earlier this week that showed the socio-economic impact of reduced power supply to the mining industry.

Baker said the parties hoped that government and Eskom's response would mitigate the need to reduce employment in the mining sector. He said several companies across commodities were affected by the reduced power supply.

My view - [Platinum](#) prices have been one of the main beneficiaries of the concerns over power supplies in South Africa and accelerated to impressive highs over \$2300 in the last 6 weeks. However this week saw platinum falling from its highs and posting a weekly key reversal. This week's action marks a high of at least near-term significance and probably the onset of another medium-term correction, provided the long-term trend holds as we suspect.

Since 2004, platinum has experienced two of these corrections. The first was approximately 19-months in duration, the second was approximately 16-months long. The next medium-term correction, if that is what this week's downward dynamic signifies, will probably be shorter than either of the last consolidations but could still range for a year before sustaining another similar upward break.

Since platinum led the move on the upside for precious metals, its topping out may also be a lead indicator for the performance of silver and gold. However, while silver has certainly accelerated over the last few weeks, gold has been much more stable and so could potentially survive any reversionary risk better.

February 28th The Ethanol Bust

My thanks to a subscriber for this interesting and informative [article](#) by Jon Birger for Fortune, also supplied in [PDF](#) in case the magazine's online link is temporary. Here is the opening:

Cargill announces it's scrapping plans for a \$200 million ethanol plant near Topeka, Kan. A judge approves the bankruptcy sale of an unfinished ethanol plant in Canton, Ill.. And that was just Tuesday.

Indeed, plans for as many as 50 new ethanol plants have been shelved in recent months, as Wall Street pulls back from the sector, says Paul Ho, a Credit Suisse investment banker specializing in alternative energy. Financing for new ethanol plants, Ho says, "has been shut down."

How can the ethanol industry be slumping only two months after Congress passed an energy bill most experts consider a biofuels boon? The answer is runaway corn prices.

Spurred by an ethanol plant construction binge, corn prices have gone stratospheric, soaring from below \$2 a bushel in 2006 to over \$5.25 a bushel today. As a result, it's become difficult for ethanol plants to make a healthy profit, even with oil at \$100 a barrel.

My view - Not so long ago the US government was still subsidising farmers, while oil import costs continued to soar. Consequently, for bureaucrats who did not see the commodity supercycle coming, corn based ethanol seemed like a marriage made in heaven, despite its inefficiencies and corrosive qualities.

The risk with alternative fuels and sources of energy is that we do not know what will eventually replace fossil fuels. Nuclear fusion has long seemed like the best solution but no one knows when it will become commercially viable, although we are probably thinking in terms of decades rather than years.

Meanwhile, there are lots of competing technologies that can augment rather than replace fossil fuels, including bio-fuels, solar, wave and wind. The USA's experience with ethanol demonstrates once again that while governments can help by facilitating research, they should let scientists and ultimately the markets determine what works best. It is probably too much to hope that governments will resist lobbyists.

In the light of this latest news on ethanol, reported by Jon Birger, what about the outlook for corn prices plus other grains and beans? By coincidence, I received an informed assessment from the Collective today.

I am grateful to this subscriber for his latest thoughts, contributed in the spirit of Empowerment Through Knowledge. I summarise briefly:

Apparently, US seed dealers are mostly out of stock for soybeans but the demand for corn seed is down 7 to 8 percent from last year. Despite the rise in corn prices, it has been overshadowed by gains for soybeans and wheat.

An unprecedented and dangerous level of speculation is contributing to price rises and also volatility, often to the detriment of the industry.

Of the big three crops, wheat has somewhat less favourable fundamentals, due to increased planting globally and favourable weather to date. Soybean prices have also benefited from scarcity but this could change later in the year for the same reasons.

For 2008, our colleague favours corn but expects volatility to make trading difficult. Consequently, he favours a spread - long Dec '08 and short 'Dec 09.

To me, this makes sense for people who are experienced in such transactions. Corn prices could be squeezed higher later this year, leading to increased planting for 2009. Being a simple soul, I do not engage in spread trades, not least because I could not do it via a spread-bet firm.

Meanwhile, here is the latest [disaster](#) from the gambling den, plus more on [wheat](#) and another item on [soybeans](#), all reported by Bloomberg.

March 6th on food speculation / investment becoming a political problem:

"You mentioned the possibility some soft commodity markets may be affected in the future should producers struggle to hedge production forward. Intervention in Bunker Hunt situations is foreseeable and so is a correction once markets are informed of a true cornered status. The proposed scenario where investment funds would be responsible seems considerably different and intervention by authorities would not just affect one 'player' but a large group of stakeholders. Do you feel that intervention would be unaffected by the difference?"

"The alternative is weak or no intervention, producers in trouble, high prices,...which in case of ...for example corn ...would be troublesome / potentially lucrative.

"Your insight would be greatly appreciated. Thank you for providing a top quality service."

My comment - Thanks for your comments and an important question.

There are several aspects to this as you will appreciate. High prices for foods are good news for farmers, who will endeavour to increase supplies. Meanwhile, skyrocketing prices for staple foods, let alone shortages, are a political and economic time bomb.

There has always been an element of speculation in commodities, which provided additional liquidity and helped the smooth functioning of these

markets, more often than not. However they were never intended to be major investment alternatives to shares and bonds. Nevertheless that is what has happened, resulting in a tsunami of money pouring into commodities, exacerbating price rises that were already occurring as a consequence of rapidly increasing demand.

I fear that this could end badly for the food industry, consumers, the functioning of commodity markets, and for investors. Considering the latter, and we have been big bulls of commodities as you know, the situation is potentially much worse than the Nelson Bunker Hunt saga. He was one eccentric with more money than sense, and soaring silver prices mattered less than the spiralling cost of food.

If prices continue to rise, attracting more money to commodity funds and ETFs as could easily be the case, I think the US government will become involved. Their attitude is unlikely to be: OK, you are prudent investors so the mayhem doesn't matter.

So what should one do?

Tread warily. If / when food prices become a frequent front-page item, the danger signs will be flashing, particularly if commodity market officials and politicians are complaining. Meanwhile, many trends have accelerated. This is an ending signal of unspecified duration and downward dynamics will signal the onset of corrections, as we have so often seen with other markets. If / when investors / speculators in foods take fright, this is likely to spread to other commodities where dramatic price rises have occurred.

Over the longer term, these markets remain in secular bull trends as demand is rising faster than supply, more often than not.

March 7th on the performance of grains relative to meats:

"I'd appreciate your comments on the following [overlay](#) going back as far as the info allows [DJAIGAG](#) versus [DJAIGLI](#) (agriculture vs livestock).

"Maybe the Collective can comment on one interpretation, that this reflects capitulation by livestock farmers as feed prices go thru' the roof.

"The relative value play, if so, is obvious. However, if the agri prices reflect inflation and inflation hedging, then they could have a way to go (I compared DJAIGAG with gold and the former has some catching up to do). I know the charts should tell us via a reversal of the GLI trend, but this looks so compelling I can hardly help myself! So far, my only position is a small combined agri and livestock structured product from Goldman Sachs (ticker GB01) (which has capital protection and 140% of upside). It has been a useful if unspectacular investment. I'm thinking that livestock is one of the few opportunities that offer an un-recognised medium-term inelasticity and an, at least, constant demand once any capitulation is done. Any comments?"

My comment - The [overlay](#) between the Dow Jones Agriculture Index and the Dow Jones Livestock Index show a sharp divergence between the two indices since the middle of last year.

According to the Dow Jones [website](#): the Dow Jones-AIG Agriculture Sub-Index consists of the following seven commodity futures: Coffee, Corn, Cotton, Soybeans, Soybean Oil, Sugar, and Wheat. The Livestock index is [composed](#) of 67% Live Cattle and 33% Lean Hogs.

The value in livestock is, as you say quite, obvious. Since they have so far failed to rise very much above the cost of production, and arguably, are even below that cost. This situation is unsustainable and we are likely to see these prices breaking upwards at some point. Likewise the acceleration in agricultural prices was unsustainable but the secular uptrend in these commodities remains very much in place.

This [report](#) from the UBS Equity Derivatives Marco Sales Desk, kindly forwarded by a subscriber, makes a similar argument. Here is a section:

If the circumstances facing dairy farmers are poor, those affecting pig farmers are even worse. Back in January, Chris Hurt of Purdue University wrote, "Corn and soybean meal futures prices indicate a record high price year. This will mean a record high annual cost for pork producers. Both corn and soybean meal have had higher prices than current levels, but those were spikes that soon moderated.

While live hog prices are expected to average \$46.30 for the year, costs of production are estimated at \$55.60 based on futures prices for corn and soybean meal on January 4, 2008 and adjusted to cash purchase levels. These estimates suggest a loss of about \$9.30 per hundredweight or near \$25 per head on average for the year. This would exceed the previous worst year in modern history which was 1998 with an estimated loss of \$6.78 per live hundredweight. Costs prospects for 2008 at \$55.60 are extraordinary. This can be seen when compared to my estimated costs average for the previous ten years (1998 to 2007) which was \$40.64 per live hundredweight. My previous record annual estimated high costs were \$48.93 in 1996. The largest losses are expected in the first quarter of the year when they could reach \$36 per head and then be around \$20 per head of loss for the rest of the year." (4) The FAPRI model notes that "low 2008 hog prices will lead to large financial losses for hog producers. As a result sow numbers for the second half of 2008 and 2009 will be lower. Given expected input costs, hog prices will need to average \$50/cwt - \$55/cwt in order to provide producers with historical average return levels."

Once again I would just point out the input prices are already well above those used to calculate the scale of the losses being experienced in the industry and that US farmers have shown no indication that they desire to subsidize prices by continuing to over produce at break even or loss-making prices. As the Minnesota Pork Board noted on February 29, "Slaughter this week was up sharply from a year earlier. The estimated Federal Inspection number this week at 2187 thousand head, up 15.7% from a year earlier. Good news from

north of the border. The Canadian Government is offering hog producers in Canada a buyout program in order to reduce the sow herd faster. " (5) The lean hog future curve appears to indicate that the heavy current slaughtering programme, which itself has led to reduced spot prices, will restore the industry to at least break even by the northern hemisphere summer - well ahead of the projections from the OECD and FAPRI. I would accept that there may be element of speculative money flowing into hog contracts and indeed into almost all animal protein futures based upon the simple reasoning that they are some of the very few commodities that are trading below their costs of production, but all this money flow is doing is possibly bring forward the price recovery. It seems impossible to argue that protein prices will continuously trade below the cost of production.

From a technical perspective, the price for lean hogs [lean hogs](#) is still in the broad ranging pattern it has followed for much of the last five years. The momentum approach would be to wait until it breaks upwards from this long range, but given the relatively depressed state of the market today, it represents value and is probably in a buying range around current levels.

[Live cattle](#) remain in a volatile uptrend but recently encountered resistance near \$100. In this market, more than any other, it has been profitable to buy following reactions due to the often intense volatility. Because the action is so whippy, a sustained move below \$80, lasting for a number of months, would be needed to offset scope for further upside potential. Also see Comment of the Day on [February 27th](#).

While the livestock futures have been bypassed by the fervour for other commodities, Agriculturals have accelerated quite spectacularly, attracting many new investors to the asset class and setting new highs for a number of them. However, this week saw downward dynamics on [Cotton](#), [Soybeans](#), [Arabica Coffee](#), [Robusta Coffee](#), [Oats](#), [Rough Rice](#) and [Sugar](#) (Also see David's piece on commodities in yesterday's [Comment of the Day](#)). They had all accelerated to varying degrees and have reacted sharply in the last couple of days. Given the fact that this is not an incident isolated to one commodity, but has affected a whole swathe of the sector, indicates that this is a meaningful high which probably marks the onset of a medium-term correction, within the overall secular uptrend. They would need to sustain moves to new high ground to reaffirm their overall uptrends, but even if this were to happen, medium-term risks have risen considerably for agriculturals generally.

As a trade, we see that the [ratio](#) of agriculture to livestock have been accelerating over the last 6 months but is becoming unsustainable as it goes parabolic. Given the performance of so many agriculturals, it is quite likely to begin retracing some of this gain in the coming weeks.

on the underperformance of lean hogs:

"One agricultural market that has steadfastly ignored the 'scarce resources/global warming' theme is Lean Hogs which is at 20 year lows of 25% of previous peaks (even less in inflation adjusted terms). To my inexpert eye, the long term chart seems to be in a 13 year downward trend. By

contrast, Live Cattle has risen over the last 13 years, at least in line with inflation, and is still within 20% of all time highs.

"Firstly, does any one in the collective know of the macro background that has caused the long term decline in Lean Hog prices (perhaps tariff reductions, farming techniques?)?"

"Secondly, it strikes me that with the sharp rise in feed prices, sooner or later livestock prices will need to rise accordingly. I understand the typical cycle is that initially farmers slaughter more and younger animals in response to a rise in feed prices which cannot be passed on to consumers and that this action depresses the price in the short term but leads to a shortage of animals and higher prices in the medium term. Does any one know the typical length of this cycle?"

"Are we looking at a specialist US market or will it be influenced by global forces of supply and demand as with the grain markets? I have no idea whether there is much international trade in pork and pork products (except that Danish bacon seems to be fairly ubiquitous throughout Europe!)."

And

"Further to my recent submission, the long term chart I was looking at was for the Dow Jones-AIG Lean Hogs Total Return Index. On further analysis, the Lean Hogs 1st Month chart does not show a similar long term downtrend. So I presume that the answer to my first question is to do with the construction of the Total Return index - perhaps the costs involved in rolling from month to month are particularly high for lean hogs. My intention was to buy an ETF tracker for the index but this seems to be a flawed strategy since there seems to be a hidden downward bias in the index itself."

My comment - Thank you for this well-thought through email which contains a number of questions I don't know the answer to. Your second question raises an important issue for anyone considering this trade, however we can probably succeed in identifying the change by keeping an eye on the individual commodity charts as well as the ratios and overlays.

Regarding the international trade in pork, the Chinese are certainly starting to talk about importing pork following last year's blue tongue disease and the recent impact of heavy snows on the herd of young piglets. Inflationary concerns from rising domestic pork prices may also encourage them to act. When they start and to what extent they enter the market will most likely be seen on the charts. If the Fullermoney Brain Trust has any further input, I would be happy to post it.

March 17th Commodity price headlines again today but this time for not maintaining record highs

Agricultural commodities have been the hottest game in town during recent months, closely followed by precious metals. They have been the leaders of

an important secular theme for Fullermoney, long summarised as Supply Inelasticity Meets Rising Demand.

However more recently, we have described agricultural commodities in particular as a very crowded trade. We have also expressed concern over accelerating price trends ([weekly](#) & [daily](#)) - always an ending signal of unspecified duration and severity, but often in proportion to the overall price move, even within long-term trends.

Paul Touradji of Touradji Capital Management expressed it more emphatically in this comment reported by Bloomberg:

'Frenzied Money Flow'

Commodities ``have all gone parabolically higher on frenzied money flow," New York-based Touradji, wrote March 10.

``Unless that money flow continues ad infinitum, in which case prices would go to infinity, then the fundamentals had better be improving as quickly as prices have been, otherwise there is nothing else to keep the markets at these levels."

Here is the article in which he was quoted, followed by several others which may be of interest to some of you:

[Oil Falls More Than \\$6 on Signs U.S. Economy Entered Recession](#)

[Corn, Soybeans, Wheat Fall as Equity Plunge Deters Investors](#)

[Gold Pares Gains to Record as Global Equities, Dollar Tumble](#)

[Cocoa Sinks in N.Y> as Investors Sell Commodities to Raise Cash](#)

There were many more from Bloomberg today but you get the idea. So what is going on?

I do not think that it has much to do with a global slowdown, which is mainly in the west. However I do think deleveraging is a big factor. A number of the better hedge funds with a global brief have done very well in commodities, as have many individual investors who have profited from commodities via shares, funds, ETFs and futures.

To risk a brave contrarian call today, I think many commodities, great secular theme that they undoubtedly are, have run ahead too quickly during the frenzy to buy the one sector with upside momentum. Those that have accelerated the most are increasingly susceptible to medium-term corrections, which I would describe as anything from a few months to two years.

Conversely, bears have had a field day shorting stock market indices and particularly financial shares. Sentiment has reached hysterical extremes, reminiscent of deeply oversold conditions over the decades. If the rational debate today is not about the possibility of financial Armageddon, but instead,

how much blood we need to see in the streets before concluding that the bottoming out process is underway, then we should be thinking more about what to buy among oversold stocks and funds, rather than what to sell.

Lastly, how about this for a contrary indicator:

Goldman's Abby Cohen to Stop Making S&P 500 [Forecasts](#)

For more on the stock market outlook and tactics, see Email of the day (3) below.

March 14th Which companies pay reasonably high yields and can cover their dividends?

This afternoon I searched the Bloomberg database for companies which had gross indicated dividend yields of more than 4% and a dividend cover of more than 2. The countries covered in this [report](#) are the USA, UK, Australia, Switzerland, the Eurozone, Japan, Canada, Indonesia, India, South Korea, New Zealand, South Africa, Thailand, Taiwan and Hong Kong.

In uncertain market environments, investors tend to retreat from assets they perceive as risky and are more attracted by higher yielding assets because of the consolation a sustainable payout provides. Some of the companies on this list may run the risk of going bankrupt or cutting their dividend. The reason we selected two times dividend cover was to weed out the most obvious candidates for a dividend cut, but that does not insulate the list from that risk.

One immediate conclusion is that the USA has a surprisingly small number of companies which fulfil the criteria. Although the interest rate in the USA is lower than some of the other markets, we see that in Europe, where interest rates are 4%, there are a much larger number of companies paying a yield of more than 4%. So few companies matching the search parameters may suggest that the relative risks of investing in the USA compared to other markets are higher.

The only bank on the US list, [Wells Fargo](#), has held up comparatively well when measured against its peers. It has not tested the January lows and would need to sustain a move below \$27 to question scope for some further higher to lateral ranging.

On seeing that the USA had so few companies with a relatively high yield and ability to cover that yield, I did an additional [search](#) of the S&P 500 and Nasdaq 100 for stocks with a Price / Book Value of <1. This resulted in 46 names. Companies towards the bottom of the list such as Countrywide are already speaking with receivers, while Ambac and Bear Stearns run the risk of going bankrupt. A number of other companies also run that risk, but this list also inevitably has a number of companies which offer value around current levels.

These reports are not meant to be a recommendation for anyone, but are intended to highlight companies with some interesting fundamental

characteristics. We would urge subscribers to do their own due diligence before making any investment.

March 17th on UK listed high yield funds:

"Eoin's report on high yielding equities couldn't have come at a better time for me as I am finding it increasingly hard to resist the temptation of such large dividends. For my own purposes I have compiled a list of high yielding UK listed iShares and investment trusts which I thought I'd send to you in case you think anyone else might be interested.

"The list was compiled using data from www.theac.co.uk, www.trustnet.com, and www.ishares.net and I cannot vouch for its accuracy. The funds listed are not intended to be recommendations and not all of them have performed particularly well in the past. I have marked (*) the ones I own.

"I would welcome any information about Morant Wright Japan Income because I can't even find the website.

"iShares:

iShares DJ Asia/Pacific [Select Dividend](#) (yield 5.23%/ TER 0.59%) (Australia 71.65%/ HK 13.9%/NZ 8%/ Japan 3.8%)

iShares DJ [Euro Stoxx](#) Select Dividend (4.0%/0.4%)

iShares FTSE [UK Dividend Plus](#) (5.6%/0.4%)

iShares FTSE EPRA/NAREIT [US Property](#) Yield Fund (7.55%/0.4%)

iShares FTSE EPRA/NAREIT [Global Property](#) Yield Fund (5.15%/0.59%)

iShares FTSE EPRA/NAREIT [Asia Property](#) Yield Fund (3.3%/0.59%)

"Investment Trusts (Fullermoney Themes):

[Aberdeen Asian Income](#)* (yield 4.47%/ TER 1.42%/ discount -6.5%)

[Henderson Far East Income](#)* (4.78%/0.99%/-0.8)

[Schroder Oriental Income](#) (4.56%/na/-6)

[Merrill Lynch Commodities Income](#)* (mining and energy companies)
(3.24%/1.64%/+1.4)

[Middlefield Canadian Income Trust](#)* (diluted exposure to energy and resources) (8.75%/ 0.64% / -8.5)

[Utilico Emerging Markets](#)(3.3% /1.24% / -6.1)

"Other Investment Trusts:

[HSBC Infrastructure](#) (UK infrastructure projects) (yield 5.34%/ TER na /

Discount-1.3) [Babcock and Brown](#) (UK Infrastructure projects) (5.6% /na / -3.3

European Assets (European small cap equities) (7.7% / 1.36%/ -8) [JP Morgan](#)

[European Income](#) (4.44% /1.21%/ -7) [Shires Income](#) (UK equities) (8.26%/ na

/ -2.2) [Glasgow Income Trust](#) (UK equities) (7.55% / 1.1%/ -7.8) [Henderson](#)

[High Income](#) (UK equities) (6.13%/ 1.1%/ -4.9) [British and American](#) (6.67%/

1.08%/ -10.5) [Henderson Global Property](#) (6.93%/ na/ -9.7) [Morant Wright](#)

[Japan Income](#) (7.05%/ na / -15.8%)

"All the best and keep up the excellent work which I enjoy so much."

My comment - Thank you for your enthusiasm for the service and this list of funds which I'm sure will be of interest to many other subscribers. I can confirm that all of the funds listed above can now be found in the Chart Library. Of course, part of the reason yields have risen is because prices have been falling. We should also be aware that there may be some dividend cuts, not least among financial shares.

However, funds such as the Merrill Lynch Commodities Income and HSBC Infrastructure funds remain quite close to their highs and are relative and absolute outperformers. As for the other funds in the list, a number have fallen considerably over the last few months, reflecting the broader market environment. Given the impressive yields and assuming they can maintain them, some of these funds are probably worth watching for signs they are finding support.

You will also be able to track how they are performing relative to a single benchmark and in a single currency using the Chart Library [Filter](#) system. Here is an example.

February 15th Can Chen Zhi save the world?

My thanks to Tim Price for this additional [letter](#). People who respect each other can disagree amicably. It shows that they are independent thinkers. I think this letter is too bearish on China's stock market and probably the west as well. However Tim remains a long-term bull on Asian economies and the resources that Fullermoney favours.

Yes, China's consumer spending, although rising fast, is perhaps only a fifth of that in the USA, so it will not offset America's feared decline in spending. However it does not need to because only America's poor people - half the population or 150m at most - will feel the need to curb consumption. And the employed poor, which are most of them, will continue to spend, albeit at a slower rate. I see this as more of a problem for retailers who will have to slash profit margins to maintain turnover.

As for China having "a billion poor people", Tim was quoting someone else on this point, people underestimate the wealth creation that is occurring. I expect a sharp increase in China's billionaires - India's as well. More importantly, Asia's middle classes are acquiring wealth much more rapidly than their western counterparts.

The "chart of shame" in the letter is indeed colourfully scary, but veteran subscribers have learned to be wary of these overlays. Most dramatic uptrends look similar, as do the retracements. Yes, the chart depicts four bubbles but the other three were much bigger than China's, especially Japan in 1989 and the Nasdaq in 2000.

China's historic [PER](#) has come down significantly, although it is still a lofty 38. However earnings are growing fast, so we should not expect to see western multiples if China's GDP growth continues at a rate of at least 8%. I think

China has done a good job of deflating the bubble without a crash, although this point remains to be proven.

March 18th China to Take 'Forceful' Steps on Inflation, Wen Says

This [article](#) by Li Yanping as well as this [one](#) by Nipa Piboontanasawat for Bloomberg cover today's move to increase bank's reserve requirements. Here is a section from the former:

Consumer prices in China jumped 8.7 percent in February from a year earlier on food costs and supply disruptions caused by the worst snowstorms in half a century. The economy expanded 11.4 percent in 2007, the fastest pace in 13 years.

“China's economy is facing trouble now, because of domestic inflation and the U.S. subprime issue,” said Wu Kan, who manages the equivalent of \$41 million at Dazhong Insurance Co. in Shanghai. “It will be difficult for us to see a growth rate of 10 percent or 11 percent this year.”

The government was maintaining its 4.8 percent inflation target for 2008 “because it helps stabilize consumer expectations,” Wen said. “When prices soar, expectations can be more horrifying than the increases,” Wen said, adding that fighting inflation will remain one of his government's main jobs over its next five-year term.

Chinese policy makers will need to use a package of measures to tackle inflation, Zhou told reporters in Beijing today. He said there was room to tighten all monetary policy tools including interest rates and reserve ratios.

'Requires Skill'

“The timing, scope and choice among different options requires skill,” said Zhou, whose tenure at the central bank was re-confirmed by the National People's Congress yesterday. “It depends on our adjustments and wisdom.”

The People's Bank of China increased interest rates six times in 2007 and lifted the amount of money commercial lenders must set aside on 11 occasions to a record 15 percent.

China will have to raise lending and deposit rates at least once this year, according to a March 12 survey of 12 economists by Bloomberg News. The country's one-year key lending rate is at a nine-year high of 7.47 percent, while the deposit rate is at 4.14 percent, half of the February inflation rate.

The central bank is hoping for “positive real interest rates,” Zhou said today.

The government was “confident” it would be able to combat inflation with the appropriate policies, Wen said. “We still have 150 million tons to 200 million tons of grain reserves, and most industrial goods are still in oversupply.”

My comment - China is performing a fine balancing act between attempting to rein in inflation and supporting rapid economic growth which is necessary to maintain employment. Among global central banks, the Chinese have been most aggressive in controlling the amount of capital banks hold in reserve. This withdraws liquidity from the market in the form of how much banks can lend, but does not encourage consumers to save because deposit rates remain at only 4.14%. This means that Chinese real interest rates are negative. These measures by the government are an attempt to force banks to be careful about which businesses they lend to, rather than the indiscriminate lending to state owned companies of previous years. Raising reserve requirements is seen as a way to slow investment by companies but has little effect on the average consumer.

Raising lending rates impacts the entire economy and are a more pronounced headwind for the stock market. The Shanghai A-Shares ([weekly](#), [daily](#)) accelerated spectacularly last year but encountered resistance above 6000. The subsequent reaction was larger and went on for longer than the previous 'steps' within the uptrend and the break below 5000 signalled the onset of the current medium-term downtrend. This downward move is now becoming overextended and although it could become more over stretched, the end of this portion of the move is approaching. An upward dynamic would be needed to check downward momentum beyond a brief pause and sustained move back above 4750 would question the integrity of the downtrend.

February 27th on the currency peg used by many GCC countries:

"Could you please post a chart of the Dubai Currency ([Dirham](#)) against the USD? I believe the exchange rate is 3.75 but because of the weakness of the dollar I keep hearing that the currency peg will be broken soon and many of the currencies of the GCC will move upwards. Could you kindly comment on this?"

My comment - The weakness of the Dollar puts pressure on economies which are growing strongly because USA's current interest rate policy doesn't provide the ideal fit for a rapidly expanding economy. While the Dollar peg provides stability, it also applies an expansionary monetary policy to countries which might be thinking of tightening as the threat of economic overheating increases. Inflationary problems also become more pressing. However, the fact remains that oil is priced in Dollars and having a Dollar peg is convenient when oil is a state's number one asset.

A weakening Dollar is already pressuring the profit margins of oil producing states, but if their currencies were allowed to appreciate significantly they would be getting much less of their domestic currency per barrel of oil, and other exports would lose competitiveness. I agree that pressure has been mounting on the currencies of the GCC to appreciate, but I have not seen any commentary originating with the leaders of these countries, indicating that they are about to change policy.

As we have seen in Asia, countries can successfully hold down the value of their currencies for long periods of time and grudgingly give up this

competitive advantage for their exporters. I see no reason why the GCC would be any different.

In the meantime, stock markets in the Gulf are some of the best performing in the world. [Egypt](#), [Oman](#), [Bahrain](#) and [Kuwait](#) are all breaking upwards to new high ground, as liquidity continues to flow into the region. While, I would consider these markets to be high risk, considering their historic governance, there is no question that they are also high growth and benefitting from the influx of increasingly large amounts of petrodollars.

March 6th 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.

As has been the case over the last three months at least, European indices have dominated the tables in terms of the lowest P/Es. The New Europe Blue Chip, which is comprised of Eastern European, mostly Austrian companies, is now second on the list with Ireland in third.

Prior to the current correction, these were not at bubble valuations and today 9 European markets have a P/E less than 10, which is cheap when measured against their global peer group. Unless we believe that the credit crunch will have much more marked effect on Europe than on the rest of the world, these markets appear to be under appreciated by the wider market. However, they need to continue to hold above their January lows and will probably not encourage investors return in any numbers, before they can sustain moves significantly above their February highs.

(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.)

February 29th Chart Library Filter Live!

You can access the Filter System screencast tutorial via this [link](#). The tutorial is also accessible from the Filter main page via a link in the top right 'Help on Filtering'

You will also notice the scroll bar at the bottom of the page and a box in the bottom right of the tutorial window, with pages numbered 1-10. By clicking on this box you can skip ahead in the tutorial if you so wish.

Please Note: You can view the charts by clicking on the name of the instrument. Hitting the back button take you back to the filter results.

Sorting by 1-month % returns will always give you the biggest movers. So for example in this search of the [Nikkei](#) sorted by 1-month percentage change in descending order, [Toyo Zinc](#) is the biggest upside mover this month.

In the [UK FTSE-100](#), if you sort this filter, it shows us that [British Airways](#), the fourth worst performer this month, remains in a consistent downtrend.

This filter of the [Commodity Indices, Funds, ITs & ETFs](#) section, redenominating all the funds to US Dollars shows us that [Ecofin Water and Power Opportunities Fund](#) has moved up the rankings fastest between the last 1 and 3 months. In absolute terms, it is being outperformed in absolute terms by the [Merrill Lynch World Mining Trust warrant](#) which has moved up the rankings almost as quickly. [Geiger Counter Ltd.](#), in third place, is rallying from depressed levels.

Interestingly, when one sorts the Commodity Indices Filter above, by Rank Change between 1 & 3 months, in ascending order, it shows funds which were close to the best performers three months ago but have slipped down the relative performance rankings considerably in the last month. The [Central Fund of Canada](#), [Powershares DB agriculture Fund](#) and [Dow Jones-AIG Corn](#) are the top three on this list. While they remain in consistent uptrends, and continue to post impressive gains, they are becoming overextended and are worth watching for any sign of inconsistency, as an indication that this very good uptrend may be ending.

The filter can also be used to vet your favourites for a customised list of instruments in a variety of different base currencies.

Our IT people will be working over the weekend on a print facility which we hope to have with you shortly. Today's release is just the first version of what we hope will be an invaluable tool for searching long lists of instruments. Further down the road we intend to develop more customisable filters which will have more technical options.

(Also see Comment of the Day on [January 22nd](#) for further details)

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