

Fullermoney

Global Strategy and Investment Trends by David Fuller

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

Monday 2nd June 2008

Wall Street Says $-2 + -2 = 4$ as Liabilities Get New Bond Math - [This article by Bradley Keoun for Bloomberg will certainly 'raise a few eyebrows'](#). Here is the opening:

Leave it to Wall Street to profit from its own distress.

Merrill Lynch & Co., Citigroup Inc. and four other U.S. financial companies have used an accounting rule adopted last year to book almost \$12 billion of revenue after a decline in prices of their own bonds. The rule, intended to expand the "mark-to-market" accounting that banks use to record profits or losses on trading assets, allows them to report gains when market prices for their liabilities fall.

The new math, while legal, defies common sense. Merrill, the third-biggest U.S. securities firm, added \$4 billion of revenue during the past three quarters as the market value of its debt fell. That was the result of higher yields demanded by investors spooked by the New York-based company's \$37 billion of writedowns from assets hurt by the collapse of the subprime mortgage market.

"They can post substantial gains as a result of a decline in their own creditworthiness," said James Cataldo, a former director of treasury risk management for the Federal Home Loan Bank of Boston and now an assistant professor of accounting at Suffolk University in Boston. "It's completely legitimate, but it doesn't make sense by any way we currently have of thinking of net income."

The paper profits have helped offset more than \$160 billion of writedowns taken by U.S. financial-services companies during the past year. Now some investors and analysts say the winnings are illusory and may have to be reversed.

"The piper will have to be paid eventually," said Robert Willens, a former Lehman Brothers Holdings Inc. accounting analyst who left the New York-based firm earlier this year to become an independent consultant.

Statement 159

The debate over what is known as Statement 159 adds to the number of accounting techniques called into question as the U.S. debt market unravels. Investors have criticized banks for booking some writedowns in an accounting category called "other comprehensive income" that bypasses their income statements. Accounting rulemakers are now proposing changes to standards that let banks use off-balance-sheet vehicles to juice earnings without tying up precious capital.

Statement 159, formally known as the "Fair Value Option for Financial Assets and Financial Liabilities," was issued in February 2007 by the Financial Accounting Standards Board, or FASB, which sets U.S. accounting rules. It was adopted by most large Wall Street firms in the first quarter of last year and becomes mandatory for all U.S. companies this year, although they have wide latitude in how to apply it, if at all.

Lobbying Effort

The rule was enacted after lobbying by New York-based companies, led by Merrill, Morgan Stanley, Goldman Sachs Group Inc. and Citigroup, which wrote letters to FASB arguing that it wasn't fair to make them mark their assets to market value if they couldn't also mark their liabilities.

"We do not believe it would be appropriate" to let investors consider creditworthiness when valuing bonds if the issuing company couldn't do the same, wrote Matthew Schroeder, managing director of accounting policy at Goldman, the largest U.S. securities firm by market value, in an April 2006 letter.

Companies are allowed to decide for themselves which of their outstanding bonds, loans and other liabilities will get mark-to-market treatment. That's an unprecedented degree of leeway, said Willens, who is also an adjunct professor at Columbia University in New York.

"It's kind of a dumb rule," Willens said. "In the entire panoply of accounting, this is the most flexible and elective and optional rule that we have."

The Fed Objects

Here's how it works, according to Richard Bove, an analyst at New York-based Ladenburg Thalmann & Co. A company decides to designate \$100 million of its subordinated bonds as subject to mark-to-market accounting. The price of the bonds drops to 80 cents on the dollar from 100 cents. So the firm books \$20 million on the "presumed savings that you have on your liabilities," Bove said.

"In the real world you didn't save a dime," he said. "You still owe the \$100 million. It's another one of these accounting rules that basically takes you further and further away from reality."

The Federal Reserve, Federal Deposit Insurance Corp., Office of the Comptroller of the Currency and Office of Thrift Supervision objected to the

rule before its passage, saying in a joint 2006 letter to the FASB that it would ``have the contrary effect" of increasing a bank's net worth at the same time its ``financial condition is deteriorating."

My view - Fullermoney has long maintained that banks are a lead indicator, more often than not. Therefore at a time when confidence in western banks and bankers is at a once-in-a-generation low, the accountancy nonsense detailed above will not help. However a key market-related question for investors is likely to be: To what extent has the bad news, current and anticipated, already been discounted?

For several months we have maintained that while the credit crisis had passed its nadir, the convalescence for banks would be lengthy, not least because their most lucrative business model of the last decade also led to their downfall last year.

While the prospect of banks returning to more prudent forms of banking should be reassuring for the long term, it does not answer investors' present concerns as to how the attractive dividends will be funded. Moreover, minority shareholders have often seen their equity diluted. Consequently they have been voting with their feet recently, as we can see with this weak performance by bank indices in the USA ([monthly](#), [weekly](#) & [daily](#)), UK ([monthly](#), [weekly](#) & [daily](#)) and to a lesser extent, Continental Europe ([monthly](#), [weekly](#) & [daily](#)).

The spectacle of US and UK bank indices testing their January and March lows is certainly not reassuring for equity investors, neither is the recent move beneath the April reaction low by the DJ Euro Bank Index. However on a more positive note, these indices appear somewhat overstretched once again as a consequence of recent and persistent weakness. Nevertheless impressive upward dynamics are required once again to reaffirm support from earlier lows.

The catalyst for such a rebound is not immediately apparent to me, although contrarian thinkers may be encouraged by today's front-page headline for the UK's Evening Standard: "Major Banks in New Crisis". Personally, I regard the current spate of rights issues (secondary offerings) as a good sign in terms of the long term outlook for commercial banks.

(See also Eoin's comments below)

Email of the day (1) - On "Inflation Bites: How I Cut My Teeth":

"I make reference to an article written by FM in the forum area called 'Inflation Bites: How I cut my teeth'

There is an interesting graph showing how the SP500 performed during inflation periods between 1960 and 2005.

"I make further reference to the final three chapters:

It was a steep learning curve, because we had all read and been told in the late 1960s that, 'stocks always went up'. We had to discover the merits of medium-term trading - both long and short, and most of all - commodities.

Investors who backed the supply inelasticity theme in the 1970s and early 1980s, and knew how to trade, made a lot of money. And those of us who allowed ourselves to get carried away from time to time, or ignored the chart signals and trading disciplines in volatile conditions, gave lots of profits back.

I suspect it will be no different in this cycle, which will provide a steep learning curve for the comparative newcomers, defined here as the under 50s. And old dogs will have to pay attention, to avoid repeating mistakes paid for in the 1970s.

Wouldn't life be dull without a challenge?

"I am interested to know your opinion on whether buy and hold is the best strategy for investors over the next 5/10 years who have investments in resources and Asian stock markets?"

"Given the inflationary environment in which we live should we be more focused on medium term trading as you mentioned whatever that may mean? Just trying to avoid the steep learning curve you mention and perhaps put some more focus on trading strategies."

"Thanks for an excellent service and looking forward to the opera season in Verona this year where I will be visiting in the summer."

My comment - Thanks for your thoughtful words, for reminding me of an [article](#) that I wrote nearly four years ago and for asking a very important question. Enjoy the opera season in Verona; I am sure many of us would be interested in your impressions.

I will continue by repeating one of my adages: You and I can only deal with the reality that markets provide. I will also repeat that I do not expect to hear the global economic environment described as 'Goldilocks' (as in - 'not too hot, not too cold, but just right'), anytime soon.

Obviously I do not know how the inflationary environment will play out, although I believe it would be wishful thinking to forecast that it is a short-term development, as some suggest. I think this cycle's inflation will remain most evident in resources, for which there is unprecedentedly intense global competition and some supply inelasticity. However global competition should also restrain wage inflation somewhat.

For equities, monetary policy will obviously be an important factor in determining whether we see valuation compression or expansion, although central bank efforts to suppress inflation would lower PER multiples on average. Among individual companies, pricing power will understandably lead to higher valuations. For this reason I think some investors remain too pessimistic regarding the leading industrial miners.

In answer to your questions, I think buy-and-hold will be profitable for both resources shares and Asian stock markets over the next 5 to 10 years, although it may not be the best strategy. Specifically, I would not pay up for anything and when trend acceleration clearly occurs, it is usually prudent to take some profits.

My personal portfolio: Stops, rollovers and new openings - Like most of us, I wish to have a proper holiday while away with family and friends, so I spent little time thinking about market positions although I did check in briefly on a couple of occasions last week, although not soon enough. Incidentally, we were at the Hay Festival, a favourite destination of ours for a number of years, where we enjoyed many and varied stimulating presentations and discussions, tried to remain philosophical about the typically appalling weather on the Welsh border, which fortunately lightened sufficiently to allow some enjoyable kayaking on the River Wye.

Carelessly, I allowed too much of my recent [silver](#) profits to slip away as the sharp correction in line with weaker oil prices triggered my loose stops at \$17.30 on 28th May, against my July contract purchases at \$16.9930 and \$17.1430 on 16th and 19th May, respectively. On noting this, I repurchased half the silver at \$17.1580 on 29th May, and also doubled my small [gold](#) long, paying \$898.40 for another August position. I suspect that both these metals bottomed in early May but that they are susceptible to lengthy, ranging support building phases as we have seen previously during what is not a period of seasonal strength. Therefore I will be inclined to trade out on short-term strength, if given the opportunity.

I gave back some of my earlier profits in Asian stock market futures, which were on automatic rollover. [Hong Kong HSI](#) longs for May were sold at 24216 on 28th May, against purchases at 26345, 26098 and 25674 on 2nd, 6th, and 15th May, while I simultaneously purchased an equal amount of June HSI at 24182. In similarly mediocre trades, expiring longs in [China H-Shares](#) and the [Singapore Blue Chip](#) Index (FSSTI shown) were sold at 13329 and 385.4, respectively, on 28th May, against purchases at 14320 and 400.4 on 7th and 2nd May, respectively. June longs for the H-Share and Singapore Blue Chip indices were simultaneously opened at 13221 and 386.02.

Perhaps the lesson remains that in this environment one need not pay up. Stock markets are ranging more than they are trending so the best long opportunities occur following sell-offs. I considerably reduced my long exposure to stock market indices in the week before going on holiday, and while I do not share the gloom regarding Asia's prospects expressed by some, I will feel uneasy about the Wall Street leash-effect, until its bank indices improve.

Prices above include spread-bet dealing costs.

Email of the day (2) - On NZD account and resources:

"It would be most appreciated if you would be so kind as to advise me of the contact details for placing a deposit based investment with a New Zealand Bank/organisation which you referred to in one of your excellent daily updates.

"As a point of interest, which I am sure did not escape your notice, Fund Manager par excellence; Anthony Bolton has recently called the top on the Commodities boom and has suggested buying into Banks. A brave call which should prove interesting. The temporary setback in Commodities and Oils has been called by another leading fund manager friend of mine, who is also a subscriber of yours, takes the view that there will be a sharp temporary setback to frighten weak holders. Market forces will then reassert themselves towards the year end when Oils and Commodities resume their up trends.

"I look forward to hearing from you."

My comment - [The NZD deposit was arranged through the corporate banking department of a UK high street bank.](#)

Fullermoney has pointed out medium-term tops in specific commodities but we maintain that the secular bull market has many years to run. I assume that bulls of western banks will be right one day but our view remains that the convalescence will be lengthy. Your friend's forecast sounds plausible to me.

John Ritchie: Japanese Financials Review - [My thanks to esteemed colleague John Ritchie of Stockcube for this timely and incisive review.](#) These graphs are seldom seen and speak volumes.

Fullermoney has been closely monitoring and frequently commenting on the gradual improvement of Japan's stock market in recent months. During my first comprehensive review of all markets since leaving for holiday - always particularly interesting and revealing - Japan was the obvious standout.

I do not think Japan can perform on its own but on current evidence, when the Wall Street leash-effect turns benign once again, Japan should be one of the best performing markets.

Additional Commentary by Eoin Treacy

Pictures du Jour: Banks to indicate direction for stock market - [Thanks to Prieur de Plessis for this interesting report on the relative performance of banks, including a large number of charts. Here is a section:](#)

Global stock markets topped out on the back of the sub-prime/credit debacle in October 2007. Prices subsequently moved lower until reaching climatic bottoms in January/March this year, triggering rallies throughout the world until a few days ago. The big question investors are grappling with at this stage is whether the rise in prices has simply been a bear market rally, or whether we are back in a primary bull market.

I have previously said: "Whereas I am doubtful about the longevity of the rally, I am also not in the Armageddon school. Is the answer perhaps a 'muddle-through' market, characterized by below-average returns? That is my hunch, for what it's worth." (See post entitled "Poll of the Week: Stock Markets - Which Way Jose?" of 25 April 2008.)

In searching for answers, it is appropriate trying to get a grip on the direction of banking stocks as these are usually a good indicator of the market as a whole, especially given the large proportion of financial services of many major stock markets.

The following is a long-term chart of the S&P Banking Index relative to the S&P 500 Index, showing clearly the massive underperformance of banking stocks since the middle of 2002.

My view - The [chart](#) of the S&P 500 Banks relative to the S&P shows the sector accelerating towards the 2000 lows, before losing [momentum](#) from January. It broke down once more in mid-May and needs to sustain a rally above 0.19 to question scope for further downside.

The [S&P 500 Diversified Banks](#) Index remains in an overall downtrend and would need to sustain a move above 0.425 to question scope for some further [downside](#).

The [S&P 500 Regional Banks Index](#) also remains in an overall downtrend against the wider index and would need to sustain a move above .0.07 to offset scope for some further upside.

Bank shares have already fallen considerably and while we have probably past the worst of the surprises relating to the credit crisis, the sector remains deeply troubled. Investors will require time to regain faith in the sector while the banks themselves need time to rehabilitate before being able to generate significant uptrends. A further period of support building, on an absolute return basis, is the most likely outcome for banks.

FT.com: View from the Markets - Thanks to a subscriber for these interesting [video](#) interviews with Jasper Koll CEO of Tantalion on Japan's economic outlook, on Japan equities, banks and reform and on investment opportunities in Japan.

The Japanese stock market broke upwards to a new recovery [high](#) today and the [Topix Banks](#) Index posted its first higher high, on a closing basis, since August 2006. Japanese banks are some of the best performers in their sector globally which is a sentence one will not have read in quite a while.

This is against a market background of other indices backing away from their May highs and international banking indices pressuring their March and January lows.

The Topix [Second Section](#) Index, often viewed at Fullermoney as a lead

indicator, is moving up in line with the other indices. The Yen is also in a mild downtrend against the Dollar which is a boon for companies consolidating their earnings in Yen.

Also of interest in Jasper Koll's commentary was his focus on the [Yen / Brazilian Real](#) cross for the Japanese auto trade. . The [Yen](#) remains in an overall downtrend and would need to sustain a move above 0.0175 to question scope for some further upside.

Japan has been a laggard for more than two-years and its banks were some of the first to turn downwards. Japan is now outperforming and its banks are some of the best performers [globally](#). It remains a question as to whether Japan can sustain a meaningful uptrend on its own but as long as the global market environment remains steady, the upside can be given the benefit of the doubt.

Libor Status Quo to Spur 'Dislocations,' Alternatives - This [article](#) by Liz McCormick and Ben Livesey for Bloomberg covers the release on Friday on the British Bankers Association report on how they are going to deal with fraudulent reports of interbank rates. Here is a section:

The British Bankers' Association's failure to change the way it calculates the London interbank offered rate may cause "dislocations" in money markets and send traders in search of alternative benchmark interest rates.

Following a two-month review of its rate-setting process, the London-based BBA said May 30 it would increase "oversight" of Libor rather than alter how the rate is set. "Details will be published in due course," the association said in an e-mailed statement. Financial products worth about \$150 trillion are indexed to Libor, according to the BBA's Web site.

The BBA has been under fire since the Bank for International Settlements said in March the banks that set Libor understated their borrowing costs to avoid speculation they were in financial straits as losses in credit markets mounted. The decision may further erode confidence in Libor's accuracy and in the 16 banks surveyed daily about their borrowing costs.

"I now expect dislocations in the money-markets to continue," said Kornelius Purps, a fixed-income strategist at UniCredit SpA in Munich. "The BBA has spent the last six weeks investigating this and I would think they will take at least another month."

In the first four months of 2007, the difference between the highest and lowest rates for three-month dollar Libor didn't exceed 2 basis points, or 0.02 percentage point, according to JPMorgan Chase & Co. research. In the same period this year, it was as wide as 17 basis points.

'Inherently Flawed'

The BBA fell short of the type of changes to Libor that investors said could have ranged from removing banks that are found to misrepresent their

borrowing costs to adding an extra survey each day to reflect trading in U.S. hours.

“Libor is an inherently flawed index,” said Willem Buiter, who served on the Bank of England’s Monetary Policy Committee from 1997 to 2000. “Libor is an unresolved problem, especially dollar Libor, as it’s not based on actual trades and actual borrowing costs but on people’s guesses. Either it will die or it will change.”

Angela Knight, the BBA’s chief executive officer, declined to comment on when any changes will be announced or how the group intends to improve oversight. Lesley McLeod, a spokeswoman, also declined to elaborate other than to say the group views the issue “very seriously indeed and will be progressing as soon as possible.”

My view - Is it any wonder that investors hold banks in such low esteem when they even lie about something as important as LIBOR. Libor spreads showing the cost of borrowing decreasing over the last few months are essentially meaningless, because we cannot rely on the data to be a true reflection of what banks are charging each other to borrow.

Perhaps it would make more sense to look at a chart of how AAA rated Composite bonds are spread over the 10-yr yield. This chart shows that spreads continued to widen until early March, which is in tune with the activity in the bond and stock markets. Since the March highs, the spread has had a larger correction, pushed back into the last reaction and is testing the progression of rising lows. At least this spread is a concrete estimation of what actually happened, backed up with real trades. However, it will take a considerable amount of time before investors will believe the figures banks publish and this is likely to lengthen their recovery. An alternative to LIBOR is now a real possibility despite calls that it is too big to displace.

Email of the day (1) - on oil and oil shares:

"Hope you and your family are well.

"The speculative end of my investment portfolio includes some AIM listed Falkland Island oil plays. DES, RKH & BOR are amongst the holdings. These have been held for a few years but something seems to have happen in or around mid Feb this year. I would be grateful for any view you have on the charts.

"There does not appear to be any particular news coming out of the region to cause the charts to move and I wondered if you had any thoughts."

My comment - Thank you, the family are all fine and congratulations on your choices which have performed well since the beginning of the year. I haven't seen anything in particular to explain why oil explorers in the Falklands have suddenly started to garner interest. According to Bloomberg, there are rumours that Desire Petroleum may have a new high profile partner,

Rockhopper Exploration has recently said they have found 5 new fields and Borders & Southern Petroleum may be taking on Shell as a partner. However that does not explain the simultaneous upside move.

Oil broke above \$100 in late-February which may have been a catalyst for greater interest in these shares. If that is the case, then they may be at risk of a correction when oil begins to retrace part of its gain.

Desire Petroleum surged upwards in February and following the initial advance entered a more consistent phase with a progression of rising lows and reactions one above another. A sustained move below 90p would be needed to offset scope for further upside.

Rockhopper Exploration also surged upwards, hit a new high above 110p in April and is now consolidating. A sustained move below 90p would be needed to hinder upside potential.

Borders & Southern Petroleum also surged upwards in February before consolidating its gain for almost two months. It conclusively broke above 80p in early May and recently hit a high near 120p. A sustained move below 100p would indicate the onset of a medium-term correction.

Today's interesting charts - Banks indices are often lead indicators and you can create relative charts to see how they performing relative to their wider indices using the Charting Tool.

Bombay Banks Index - testing the March lows and would need to sustain a move above 8000 to offset scope for some further downside.

Spain - breaking down from the short-term distribution and would need to sustain a move 13,500 to offset scope for some additional weakness.

Thailand - failed break above 850 and pulling back sharply, but is now looking somewhat overextended. However an upward dynamic is needed to check momentum.

Email of the day (2&3) - on additions to the Chart Library:

"Could you please add Bluglass (AX-BLG) to the library - they produce gallium for the construction of solar panels.

And

"I don't know if your chart library covers the Canadian Venture Exchange but if so I would like you to add Exeter Resources (V.XRC) which is on the Casey Research "best buy" list.

"Thanks."

My comment - Both of these shares have been added to the Chart Library. To answer the second question: a large number of Venture Exchange stocks can be found in the Chart Library and we are happy to add any others of interest.

Last 3-week's signups for the Free (Abbreviated) Comment of the Day - For the week of May 11th new signups, including subscribers and pre-subscribers, live in the following countries or regions: Australia, France, India, Japan, Jordan, Netherlands, New Zealand, Singapore, the UK and USA - 10 in total. In descending order, which topped the list in terms of the last week's new signups? It was the USA, the UK and India.

For the week of May 18th new signups, including subscribers and pre-subscribers, live in the following countries or regions: Australia, Finland, Hong Kong, India, Ireland, Malaysia, New Zealand, Singapore, the UK and USA - 10 in total. In descending order, which topped the list in terms of the last week's new signups? It was India, the UK and Australia.

For the week of May 25th new signups, including subscribers and pre-subscribers, live in the following countries or regions: Australia, Canada, India, Ireland, New Zealand, the UK and USA - 7 in total. In descending order, which topped the list in terms of the last week's new signups? It was the UK, the USA and Australia.

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

Tuesday 3rd June 2008

Jim Rogers: First State Investments Conference - Thanks to a thoughtful invitation from John Husselbee of North Investment Partners, I spent much of the day at First State Investments' Conference: *Asia Pacific and Global Emerging Markets Forum - 'Investing in Hot Commodities'*, held at the Institute of Directors. Organised by Charlie Metcalf and Stuart Paul, five of First State's investment management team participated in the presentations which featured the colourful Jim Rogers as guest speaker.

Rogers' long-term views are quite well known and often shared by Fullermoney. He maintains that China's economy will increasingly dominate the 21st century, as we saw with the UK in the 1900s and the USA in the 20th century. He envisages plenty of turbulence during China's rise, just as the USA experienced a depression, numerous recessions, bear markets and several wars in the last century. Each provided an outstanding buying opportunity for long-term investors.

In terms of the shifting balance of power, Rogers' statistical bullet points were informative. Here are a couple:

1. China's citizens save an average of 35% of income versus 2% in the USA.
2. The USA owes \$13 trillion to creditor nations and this figure increases by approximately \$1 trillion every 15 months.

Rogers is a believer in the commodity supercycle, saying that these have previously lasted between 15 to 23 years. He does not expect the current cycle to peak before 2020. Despite all the talk of bubbles forming or bursting, he says that the investment community has barely participated, mentioning only 100 commodity funds in the USA (I was surprised there were that many) versus 70,000 equity funds. Rogers cited a generally inverse ratio between commodities and broad stock market indices. He also maintains that Fed Chairman Ben Bernanke is an avowed inflationist, with the blessings of the Executive branch of government.

By coincidence, today's Conference in London coincided with George Soros' [testimony](#) before the Senate Committee on Commerce, Science and Transportation, which is holding hearings on potential energy price manipulation. Simultaneously, the Commodity Futures Trading Commission is planning to tighten [rules](#) for investors and index funds dealing in commodities. Against this background, I asked Jim Rogers if he was concerned that following surges in agricultural and energy prices, commodity investors / speculators would be branded as pariahs, leading to legislation against their participation in these markets?

I can only summarise his lengthy answer. Basically, he felt that volumes of trading suggested this was unnecessary and that fundamentals of supply and demand were driving commodity prices higher. He agreed that politicians might become involved but that this would have no more than a temporary effect on prices.

My own view is that commodity markets were never meant to be asset classes, a point I note that Soros also made in the article above. Ever since agricultural prices soared earlier this year I have cautioned that commodity investment / speculation would invite a social and therefore also political backlash. I know there are counter arguments but investors in commodity tracker funds will not be regarded as useful stakeholders when the world's poor cannot afford energy and food.

Obviously I do not know precisely how this will play out but despite the commodity supercycle I would be wary about investing in tracker funds which hold foods, as opposed to agricultural shares. Individual trades in commodities are another matter as they arguably help the futures markets to function by increasing liquidity.

Meanwhile, I suspect that adverse publicity and the regulatory spotlights are now causing some energy futures traders to switch from [crude oil](#) to [natural](#)

[gas](#). Precious and industrial metals may also benefit from any move away from foods and crude oil.

I will have more to say about the First State Investments Conference tomorrow.

Email of the day (1) - [On shorting US Treasuries](#):

"Do you think it is appropriate time to short US Treasuries? Also do you know of some ETFs which would go up as the interest rates on treasuries rise? Thanks for all your wisdom and I continue to learn a great deal from you comments."

My comment - [Thanks for your kind words, and I am delighted that you are benefiting from the service.](#)

I maintain that US Treasuries ([long-term](#), [weekly](#) & [daily](#)) and most other long-dated government bonds are in a secular bear market, due to too much supply, low yields and rising inflation. However action remains choppy, not least due to concern over slower GDP growth, so my personal strategy is to sell long-dated Treasury futures short following technical rallies such as we are seeing at the moment.

Email of the day (2) - [On cutting oil subsidies](#):

"As you have been away I was wondering if you were aware of oil subsidies being cut in Asia. Indonesia has cut and prices at the pump have increased by 33%. Malaysia is keeping future subsidies at 2007 levels and the new Taiwan president has said that he will eliminate petroleum price controls."

My comment - [Thanks for the update. I think the gradual removal of most oil subsidies would be in the long-term interests of these countries. Subsidies are politically expedient, may seem humane, but distort markets and siphon capital away from more productive uses.](#)

Email of the day (3) - [On India and today's chart formations](#):

"My self-confidence is being whittled to zero.

"Nothing I see in the charts warrants the slightest credibility in the optimistic consensus having which are in the media or e-mails of various experts. Worse those who are the most quoted with reassuring words are the ones who are the main culprits of the mess.

"Question: have I learned nothing in your seminars, or do your charts show for example the Sensex as well as JII poised for a big bang down?"

"Ditto for many of the stock exchanges. The configurations resemble stage 3

in what you taught in November, or am I totally wrong? I thought that many of your students might appreciate your interpretations at this time on a broader scale. Your visions are very precious but at this point need to be a bit more precise for some of us dimwits, and many points and figures charts in the Swiss market are God awful according to your stage 3 theory...

"I would appreciate your comments."

My comment - I think you are speaking for many investors and would not underrate your perceptions. Many stock market indices formed the rangy, topy, Type-3 top characteristics last year to which you refer. But it is a mixed bag today, in that some markets have drifted lower, others show evidence of support building and a minority have pushed back to or above their former highs.

The panicky environment of January and early March has dissipated but the predominance of rangy patterns contributes to a general feeling of uncertainty, which is an uncomfortable state of mind.

Where financials are weak, I would remain cautious, feeling that upside is limited and slippage, albeit mostly within ranges, quite likely. With India, financials (p&f, weekly & daily) have reversed their outstanding strength which was still evident in early January. This has inevitably contributed to this year's underperformance by the Sensex (p&f, weekly & daily) and JII (p&f, weekly & daily).

I regard the weakness as a mixed blessing - disappointing for those of us who in our dreams might have sold JII at 500, but an opportunity for those who wish to buy following one of the inevitable setbacks. One seldom enjoys profit erosion but I personally can live with this drawdown because I believe that India's long-term potential is undiminished. By coincidence, this informative column by Hugh Young appeared in today's Financial Times. He is one of the investment managers for whom I have the greatest respect.

Meanwhile, those of us who have invested in India for its long-term growth potential will probably have to be patient for a while longer. The combination of commodity inflation, somewhat slower global economic growth and deleveraging remain headwinds for equities. Chindia is temporarily out of fashion. This does not mean that the king and queen of emerging markets lack potential at today's levels; I maintain this is a buying opportunity for the medium to longer term, but the superior performance we have seen before and look forward to once again requires a return of animal spirits among investors.

Additional Commentary by Eoin Treacy

UN Convenes World Leaders to Seek Aid for Food Output - This article by Jennifer M. Freedman for Bloomberg covers today's Forum on agriculture in Rome. Here is a section:

“There are about 10 factors pitting at once against food prices, and this has led to the current crunch,” said Melinda Kimble, who heads the foundation.

While consumers in wealthy nations face higher bills at the supermarket checkout counter, the effect has been more devastating in poor countries, where many people spend more than half of their income on food. The International Committee of the Red Cross says more violence over food prices is possible.

“Governments realize the situation can become explosive,” said Concepcion Calpe, a senior economist with the FAO and secretary of the organization's Intergovernmental Group on Rice.

“Politically it's very difficult to ask people not to eat.” Haitian lawmakers replaced their prime ministers April 12 after riots sparked by food shortages.

With pressure on prices likely to linger, the new aid may do little to lower food costs in the near term, though record harvests for cereal crops such as wheat and rice are forecast this year, experts say.

Costs, Subsidies

Record oil prices will keep fertilizer and shipping costs high, demand for biofuels like ethanol will grow in response to climate change and the system of subsidies that distorts prices and production will not easily be dismantled. The U.S. provided farmers with \$13.4 billion in subsidies in 2006 and the EU paid out about 42 billion euros (\$65 billion).

Food prices will stay “well above their mean levels of the past decade” in the next 10 years, the FAO forecast in a joint report last week with the Organization for Economic Cooperation and Development.

Experts say the higher prices may lead to increased output and downward pressure on prices.

“Arguably in the last 10 to 15 years we had too-low prices because of all the distorting subsidies, and now we are back at a new equilibrium of much higher prices that makes farming attractive,” de Willebois of IFAD said.

Governments will probably be “generous” in pledging money for rural roads, irrigation, agriculture research, drinking water and education in the world's poorest countries, said Marc Cohen of the Washington-based International Food Policy Research Institute.

“I suspect there will be some tangible resources pledged,” he said. “If you look at what's spent on other activities -- let's say the word ‘Iraq’ -- it's not unfeasible levels of spending.”

My view - Food over-production was such a problem in Europe, that the infamous butter mountains and wine lakes were synonymous with bureaucratic incompetence and a Common Agricultural Policy which had outgrown its usefulness. However now that production has decreased and the

price of food has become an international cause celebre, set-aside policies are likely to be revisited. As one would expect, higher demand should result in an eventual corresponding move from the supply side.

While there are a number of contributing factors surrounding the run up in commodity prices, there is a temptation to blame everything on biofuel. The bigger picture is just not that simple. Rising food demand from growing populations who can afford to have a more balanced diet is the key driver behind increased demand for food of all types. This is not something which is about to change anytime soon. In fact as global GDP growth continues to be led by the largest population centres, and millions more enter the middle classes, demand is only going to increase.

Many crops have an annual cycle, which means that when prices rise, a bumper crop the following year is possible as farmers plant more of that commodity. However, this also leads to less of another crop being planted and sows the seeds of the next bull market. When one factors in weather, agricultural commodity prices are volatile. It will take a significant amount of time before global food production taken on aggregate can meet rising demand.

Indian Talent Pays Back Taxpayers, Shuns U.S.: Andy Mukherjee - [This interesting article](#) by Andy Mukherjee for Bloomberg covers the success of India's institutes of technology. Here is a section:

For almost 50 years, the hard-earned money of India's taxpayers has gone down the ``brain drain" as many of the engineers trained at the prestigious Indian Institutes of Technology went overseas and didn't return.

That is now changing.

The supply of top-end technical talent by Indian universities is beginning to create its own domestic demand: The class that graduates from the seven IITs this month will mostly stay home -- or return after short stints abroad -- and pay back the nation's investment, according to a survey by Evalueserve, a New Delhi-based business-research company.

Every third alumnus of the IITs went abroad from 1964 to 2001, mostly to the U.S.; out of the more-recent graduates -- including the Class of 2008 -- 84 percent have chosen to remain in India, the survey says.

The post- and pre-2001 groups have very different attitudes.

``The drop in the number of IITians who believe the U.S. offers a `better standard of living' has been remarkable, from 13 percent to almost zero," says Alok Aggarwal, author of the report and an alumnus of the IIT in New Delhi.

India's example, which has great relevance for policy makers in developing nations, clearly shows that the relationship between education and growth isn't a one-way street: More of the former doesn't always produce more of the latter.

Sometimes the economy has to cross a threshold level of development before the investment in human resources -- especially higher education -- starts producing results.

Demand and Supply

India, which set up its first IIT in 1951, had to wait until 2002 before the promise of rapid economic growth -- and new industries and companies that were born as a result of that expansion -- pushed up demand for top talent to a point where the country could begin to absorb a greater proportion of the domestic supply.

“Education may influence the economy in subtle ways, interacting with other factors,” says the Commission on Growth and Development, a group of business and government leaders led by Nobel Prize-winning economist Michael Spence.

“India turned out world-class engineers and scientists for decades before its economy took off,” the commission said in a report released last month.

Yet, this investment in skills yielded limited economic results, says the commission, “until India discovered a global demand for software services, a demand which has since broadened to include outsourced research-and-development and a wide array of services delivered over the Internet.”

“India, in short, had to solve a demand-and-supply problem, not just a supply problem,” the commission said.

My view - One of the primary advantages India has over more authoritarian countries is its rich supply of people seeking to set up businesses with the ambition to make their enterprise successful on the international stage. If the diaspora of educated, experienced Indians are making their way back to India that can only be of benefit to the country and probably points towards further development and future innovation.

Cocoa Gains on Speculation Disease in Ivory Coast to Cut Supply - [This article](#) by Marianne Stigset for Bloomberg covers the recent more positive trading activity in cocoa. Here is a section:

Cocoa rose for a fifth day in London on speculation disease will limit production in Ivory Coast, the biggest grower, adding to a world deficit. Robusta coffee and white sugar also advanced.

The crop in Daloa, an area that produces a quarter of Ivory Coast's cocoa, has been hurt by capsid bugs as the rising cost of fertilizer and pesticide prompts farmers in the west of the country to curb their use, Reuters said last week. World demand will exceed supply by 41,000 metric tons in the season ending September, the International Cocoa Organization said in March.

The price of the beans climbed on “concerns regarding the quality and abundance of the upcoming main crop in Ivory Coast,” Stephanie Garner, a

cocoa trader at Sucden (U.K.) Ltd. in London, wrote in a report today.

Cocoa for July delivery rose 25 pounds, or 1.7 percent, to 1,497 pounds (\$2,940) a ton by 3:39 p.m. on the Liffe exchange. Prices gained 6.7 percent last week, compared with a 2.5 percent decline in the UBS Bloomberg CMCI Index of 26 raw materials.

The cocoa contract for July delivery rose \$46, or 1.7 percent, to \$2,769 on ICE Futures U.S.

Ivory Coast's National Center of Agronomic Research said May 29 that the cocoa crop was showing no new signs of disease and that it was too early to speculate whether the main crop would be affected. The west African nation's main crop is collected from October to March, while the smaller mid-crop is harvested from April to September.

Cocoa rallied for five weeks through the end of September in London on concern adverse weather and black-pod disease would damage crops in Ivory Coast, Ghana and Nigeria. Ivory Coast and Ghana make up about 70 percent of the world's production.

My view - [Cocoa](#), traded in Sterling on Liffe, broke upwards in January and rallied impressively to a high near £1500 before experiencing a violent reaction against this accelerating trend. However following the 20% drawdown, it recovered steadily and consolidated below the high for the last 6 weeks. It hit a new closing high yesterday and would need to sustain a move below £1400 to offset scope for some further upside.

[Cocoa](#), traded in US Dollars on NYB-ICE, also rallied impressively from the beginning of the year and posted an even larger downward dynamic in March. It remains in a consolidation below the highs, due to the currency difference, and would need to sustain a move below \$2600 to offset scope for some further upside.

Liffe traded cocoa is the only soft commodity I can think of that is making new highs. While the grains have firmed somewhat since March the sector remains in a medium-term correction. Those that perform best are likely to have a fundamental driver.

Today's interesting charts - The Charting tool allows you to save Preset templates so they can be applied to any instrument at a later date with a minimum of hassle.

Ireland - the [downtrend](#) has lost momentum, but a progression of lower highs remains in place. A sustained move above 6500 would be needed to indicate that demand is getting the upper hand.

JGB - upward [dynamic](#), having found support near 134 and would need to sustain a move below that level to offset scope for some further upside.

Natural Gas - breaks [upwards](#) to a new recovery high and would need to sustain a move below \$11.50 to question potential for some further upside.

Email of the day - on solar and additions to the Chart Library:

"I came across a new solar ETF from Claymore, TAN, and was interested in what your views are: with solar energy as an investment theme over the next 5 years? This ETF as a vehicle to get exposure to the sector?"

[Article](#) included below covers the components of TAN and questions posed to Claymore's President.

Also, could you add the following funds to the chart library:

[Gartmore European Selected Opportunities](#)

[BGI European Equity Index](#)

[BGI Japanese Equity](#)

[BGI Pacific Rim Equity Index Fund](#)

[Standard Life Investments select property](#)

[Schroder Global Emerging Markets](#)

[BlackRock UK Dynamic](#)

"Thanks"

My comment - Thank you for these interesting suggestions. I couldn't find the BGI European Equity Index fund's ticker but all of the others have been added to the Chart Library.

[TAN](#) looks like a good vehicle for getting undiluted access to the solar sector. Solar appears to have good long-term prospects as new technologies bring down the relative cost of energy production. However alternative energy shares have not been immune to the recent market turmoil and while they are likely to benefit from further technological advances as well as the continued secular bull market in energy, they are best bought following corrections.

Email of the day - on manganese:

"Prices for all manganese products seem to be increasing. In particular, the price for metallurgical manganese lump ore, which is in acute shortage, continues to set records. You have a chart of 'Manganese Electrolytic Flake 99.7%' in the Library which looks to be distorted. Is it possible to add a chart of manganese lump ore?"

My comment - Thank you for alerting us to the problem with the manganese chart, which has now been corrected. There are no prices for Manganese lump ore listed on Bloomberg so I can't add it to the Library.

[Manganese](#) flake surged upwards in early 2007 before peaking near 4775 in early June. It remains in a consolidation and needs to sustain a move above the highs to reaffirm the overall uptrend.

Email of the day - [on black swans](#):

"Thought you would enjoy [this](#). I had a good laugh."

My comment - [Excellent!](#)

Wednesday 4th June 2008

Fed: "Verbal Intervention" Has Begun - [My thanks to a subscriber for this interesting and savvy report by the forex analysts at Citibank. Here is part of the opening discussion, commencing with one of Bernanke's comments yesterday:](#)

"The challenges that our economy has faced over the past year or so have generated some downward pressures on the foreign exchange value of the dollar, which have contributed to the unwelcome rise in import prices and consumer price inflation. We are attentive to the implications of changes in the value of the dollar for inflation and inflation expectations and will continue to formulate policy to guard against risks to both parts of our dual mandate, including the risk of an erosion in longer-term inflation expectations. Over time, the Federal Reserve's commitment to both price stability and maximum sustainable employment and the underlying strengths of the U.S. economy--including flexible markets and robust innovation and productivity--will be key factors ensuring that the dollar remains a strong and stable currency."

Bernanke's comments surprised the markets. First and foremost they triggered the question as to "why now?" and "why he?". Comments on the USD are usually the domain of the Treasury and the fact that the Fed has chosen to speak on the subject suggests that its stance has been cleared with the Treasury. With regards to the timing of the comments, four possible explanations are on offer:

1. Honesty: Bernanke may have been truthful in that the Fed is concerned about the USD simply because its weakening is raising import prices and could fuel inflation. Some scepticism is probably justified given the relative closed nature of the US economy. But it is also true that the USD sell-off has provided a lift to commodity prices, as it would need to in the absence of changes in other supply and demand factors. Disentangling the two is of course difficult. As a result, the search for 'a hidden agenda' is on.
2. Opportunism: Bernanke may have wanted to capitalize on the recent relative improvement in market sentiment and 'lean into the wind' to sustain the USD. In this interpretation 'benign neglect' would have given way to 'concerned attention'.
3. Policy signal: The Fed wanted to send a (monetary) policy signal and add another chink to the armour of the argument that policy rates will remain on hold for a considerable time. The fact that markets already price in 78bps of rate hikes over the next 12 months suggest that this is an unlikely explanation. After all, any number of formulations could have been chosen to provide a

signal about the policy rate path, without invoking the value of the USD in any way.

4. Conspiracy: The Fed may have wanted to buttress markets ahead of another crisis or negative headline event breaking. Indeed, market speculation about difficulties at Lehman Brothers had already prompted the bank to issue a statement that it had not tapped the Fed's PDCF yesterday and several financial stocks hit a new low (see Technical section). While this alone is eerily reminiscent of the situation prior to the Bear Stearns collapse, combined with the Fed's later admission that it had known of the bank's troubles a week earlier, it raises the possibility that a similar event might be in the offing.

Bottom line:

My view - The US Dollar Index ([historic](#), [weekly](#) & [daily](#)) broke its steep short-term downtrend in mid-March, and I maintain USD weakness was an important topic at the last G7 meeting on 11th April. Subsequently, some short covering, further induced by Bernanke's statements yesterday and today, has helped to steady the US currency.

What is the outlook for the USD, from short to longer term?

How might this affect other markets?

I am in broad agreement with the Citigroup outlook mentioned in the report above. Moreover, I think the USA and its trade partners would like to see at least a quietly steady greenback over the medium term.

The US government has achieved much of its unstated devaluation objectives and further near-term weakness for the USD would most likely be counterproductive, not least in terms of inflationary pressures. America's trade partners can live with the dollar at this level; creditors have no interest in a further devaluation of their USD holdings, and currency appreciation has mitigated inflationary pressures somewhat.

Some commentators look at the USD's long slide and conclude that it should bottom out near current levels, not least because it is "cheap" in terms of purchasing power parity. I have never been impressed by PPP as a currency forecasting tool but even if the USD has commenced a base building phase prior to a significant recovery, as some analysts believe although presumably not at Citigroup, I think the process would be lengthy as we have seen before.

After all, US short-term rates are hardly an incentive to buy the USD and likely to stay low for some time; everyone knows that the Fed will continue printing and the presidential candidates are promising even more big spending, and creditor nations probably feel that they already have too many US dollars.

I maintain that the US Dollar Index will remain in a broadly ranging pattern for a while longer. Beyond that I think the prospect for a significant rally is at least matched by the possibility for another downward slide.

The latter would probably have a whiff of crisis about it and therefore be a headwind for most stock markets. Conversely, a steady dollar should be a benign influence. If the Citigroup view is right, it could pay to acquire precious metals during easing in this seasonally dull period for bullion ([weekly](#) & [daily](#)) and while the USD is temporarily firm.

Also, it looks increasingly likely that crude oil ([weekly](#) & [daily](#)) has peaked for the medium term, with the help of political pressure, switching from oil to gold might not be a bad idea for hedge and pension fund managers who do not fancy being pilloried by politicians during a witch hunt. They can further justify the switch on a buy-low-sell-high basis because yellow gold is trading near its [lows](#) since at least 1985 against 'black gold'.

Email of the day (1) - On agricultural commodity tracker funds:

"In your comment you state:

" I would be wary about investing in tracker funds which hold foods, as opposed to agricultural shares."

"Over the past years I recall you writing on many occasions that you prefer physical commodities to for instance mining shares. Your above comment seems to contradict this. Could you please elaborate - (by the way, I have convinced many of my clients of the physical commodity argument and they hold both shares and CRB or AIG trackers).

My comment - You are absolutely right - the shares are usually more speculative. After all, there are lots of resources shares; many of the minor ones fail, and the others can be adversely affected by all sorts of problems, including rising costs, shortages of essential equipment, accidents, environmental problems, strikes, windfall taxes and other forms of hostile legislation, the ultimate being expropriation.

The exceptions occur when resources shares are exceptionally cheap, or have a particularly fortuitous discovery, or near monopoly control giving them phenomenal pricing power.

The two are not mutually exclusive, of course, and I note that you hold both. My comment that you quote above was based on the possibility of political and regulatory intervention due to the recent surge in food and energy prices. Here is one of today's [articles](#) on this subject.

Incidentally, well done for recognising and also seizing your opportunities; you must have lots of happy clients during what has been an extremely challenging year.

Email of the day (2) - On Peak Oil and the Asian growth story:

"David, I wonder if you could give your current thoughts on Peak Oil and the oil price and whether the price helps us come to the conclusion that Peak oil has been reached. Looking at the yearly figures from the EIA we have world supply growth of 1.4% between 2004 and 2005, 0.9% between 2005 and 2006 and 0.2% between 2006 and 2007. I come to the conclusion that these figures indicate that production is effectively declining (at least by the rate of production increase) and that this is now being recognised particularly in Asia which is the region with the highest energy growth rates.

"Having now again read Dr Samsam Bakhtiaras' report from 2006 his analysis and predictions appear to be accurate and if this is the case then we should reconsider the Asian growth story."

My comment - I have often commented on the subject of Peak Oil and at the risk of sounding pedantic, it depends on what we mean by it. Is the world running out of oil? No, we have used less than half of the globe's known reserves.

Is the world running out of easily recoverable oil? Yes, it is a finite resource and we see the evidence in declining production data from many countries. Moreover there is very legitimate scepticism regarding Saudi Arabia's stated reserves, claimed to be a constant 260 billion barrels a day over the last 20 years, although we have not heard of big new discoveries within the kingdom, and we know the Saudis have pumped 67 billion barrels since 1979. (*These figures were supplied by Jim Rogers at yesterday's presentation.*)

We also know that the global consumption of oil continues to rise. (*See also item below.*)

As for the Asian growth story, we know that rising energy costs are a problem, as they are for every oil-importing country. This has been compounded by increasingly expensive subsidies which are uneconomic and a misuse of capital. The scaling back of these subsidies is causing some concern in the markets. However I regard the move towards market prices for energy as a short-term minus and a long-term plus for economies.

Veteran subscribers are very familiar with both the Asian growth and rising cost of resources stories. In other words, I expect developing Asia's economies to grow at a faster rate than in the developed west, and I also expect that we will all be paying more for our energy in years ahead. Economic growth both contributes to the energy problem and also mitigates it, for those who can afford to pay the higher prices.

Dakota Oil Fields of Saudi-Sized Reserves Make Farmers Drillers - This is a fascinating and informative [article](#) by Anthony Effinger for Bloomberg.

I have also posted it in [PDF](#) format, in case the BBG link is eventually discontinued. Here is the opening:

John Bartelson, who smokes Marlboro Lights through fingers blackened with tractor grease, may look like an average wheat farmer. He isn't. He's one of North Dakota's new oil barons.

Every month, he gets a check for tens of thousands of dollars from a company in Houston called EOG Resources Inc., which drilled two oil wells on his land last year. He says the day his first royalty check arrived was one to remember.

"I smiled to beat hell, and I went to town and had a beer," Bartelson, 65, says.

His new wealth springs from the Bakken formation, a sprawling deposit of high-quality crude beneath the durum wheat fields of North Dakota, Montana and southern Saskatchewan and Manitoba. The Bakken may give the U.S. -- the world's biggest importer of oil -- a new domestic energy source at a time when demand from China and India is ratcheting up the global competition for supplies and propelling average U.S. gasoline prices to almost \$4 a gallon.

And unlike the tar from Canada's oil sands, Bakken crude needs little refining. Swirl some of it in a Mason jar and it leaves a thin, honey-colored film along the sides. It's light -- almost like gasoline -- and sweet, meaning it's low in sulfur.

Best of all, the Bakken could be huge. The U.S. Geological Survey's Leigh Price, a Denver geochemist who died of a heart attack in 2000, estimated that the Bakken might hold a whopping 413 billion barrels. If so, it would dwarf Saudi Arabia's Ghawar, the world's biggest field, which has produced about 55 billion barrels.

Thin Deposit

The challenge is getting the oil out. Bakken crude is locked 2 miles (3.2 kilometers) underground in a layer of dolomite, a dense mineral that doesn't surrender oil the way more-porous limestone does. The dolomite band is narrow, too, averaging just 22 feet (7 meters) in North Dakota.

The USGS said in April that the Bakken holds as much as 4.3 billion barrels that can be recovered using today's engineering techniques. That's a fraction of the oil that Price said should be there, but it's still the largest accumulation of crude in the 48 contiguous U.S. states. North Dakota, where Bakken exploration is most intense now, won't become Saudi Arabia unless technology improves.

"The Bakken is the biggest thing in oil in the lower 48 right now," says Jim Jarrell, president of Ross Smith Energy Group Ltd., a research firm in Calgary. "And among the least understood."

My view - Never underestimate the potential of resources technology to solve the most daunting challenges of extraction. All that is required is the profit incentive and developmental time.

Investment Week: Fund Manager of the Year Awards - [My thanks to a subscriber for this informative item, likely to be of interest to most subscribers. Here is the 2007 list:](#)

Global Group of the Year: Standard Life Investments
Specialist: Evy Hambro, MLIIF World Mining
Emerging Markets: Austin Forey, JPM Emerging Markets
Asset Allocator: Simon Edwards, CF Midas Balanced Growth
Far East: Angus Tulloch and Martin Lau, First State Asia Pacific
Japan: Lesley Kaye, GAM Star Japan Equity
North America: Aled Smith, M&G American
Gilt, Global and Other Bond: Bernt Tallaksen, Mehrdad Noorani and Michael Mabbutt, Thames River High Income
UK Corporate Bonds: Stephen Snowden, Old Mutual Corporate Bond
Europe: Richard Pease, New Star European Growth
UK Smaller Companies: Old Mutual UK Smaller Companies Team
UK: Ashton Bradbury, Old Mutual UK Select Mid Cap
UK Income: Neil Woodford, Invesco Perpetual High Income and Invesco Perpetual Income
Special Award for Outstanding Achievement: Mark Tyndall, Artemis Investment Management
Specialist Group of the Year: Rensburg Fund Management

My comment - [Should anyone think for a moment that these awards might be based on 'Buggin's turn' rather than merit, here is a comment from the forwarding subscriber, who is also one of the panel judges:](#)

"...these awards are essentially a quant and fundamental process. We focus on the last three years with emphasis on risk adjusted returns and bias to the last twelve months as these are annual awards. Many ways to slice the cake but this works and we are prepared to evolve over time."

[Many of these funds are listed in the Chart Library. Others can be added on request.](#)

My personal portfolio: Silver long trade increased - [I increased my comparatively small silver trade by 50% this afternoon, paying \\$16.715 for another July position, including spread-bet dealing costs.](#)

Additional Commentary by Eoin Treacy

[Arisaig Asia Diary May 2008 - Thanks to a subscriber for this interesting report covering reasons to be bullish of China, as well as addressing some of the issues surrounding the Indian market. Here is a section on the former:](#)

"We discussed in last month's Diary the changing face of Chinese companies. And China is changing itself too - from the sweat shop of the world to the world's most important shop window.

In April China's retail sales grew by 22% YoY, their fastest pace since serious data collection began. Central Bank Governor Zhou took the opportunity to announce that China should save less and boost consumption, thereby rebalancing an economy too skewed towards exports and investment. Such a move would herald the most significant global economic event of the coming decades.

There are a number of catalysts for this new policy but all underline the Communist Party's clear desire to secure social stability and, consequently, maintain its grip on power.

Income inequality is the major flashpoint that can no longer be ignored. The impressive economic growth of the past two decades has been led by export industries established on China's coastline, while most of the population is based inland. The richest 1% of Chinese now own 35% of the country's wealth.

Reports of farmers being duped by corrupt bureaucrats, of workers being abused by exploitative factory owners, or of citizens being hospitalized from the effects of pollution have become commonplace. The politicians have finally decided to act.

They are doing so by forcing manufacturers to move up the value-added curve. Low-end manufacturing will have to relocate to cheaper rural areas to survive as export subsidies are being lifted and taxes raised.

Many players will likely go under. However, consolidation will allow better companies to survive and productivity to improve. To support this, the authorities have announced plans to spend a staggering US\$1.2 trillion on infrastructure over the medium term.

In China one must take such claims seriously given the record of delivery and the size of national reserves. Workers' pay and rights will be boosted by new labour laws introduced this year which limit the use of casual labour and promote the principle of a minimum wage, paid overtime and paid holidays.

The government also appears to be serious about pollution, finally recognising the extent of China's environmental disaster in-the-making. Anti-pollution laws are now being enforced.

Finally, Beijing is allowing the RMB to appreciate. In the last three years it has risen by 17% against the US\$. This, of course, has knock-on benefits in that it helps mitigate the impact of inflation and keeps the trade protectionists in the US at bay.

All this is very positive for China Inc. No doubt you will read headlines about factory closures and exporters moving to Vietnam and India. However, these will not be significant from a wider national perspective.

The bigger point is that more factories will relocate inland and income will over time be more evenly distributed. China is thereby executing the blueprint for sustained domestic economic growth: massive infrastructure spending; rising incomes; greater wealth distribution; higher productivity; and more value added activity. This should bode well for our favoured domestic consumption plays.

My view - These are all very bullish factors for the Chinese economy and point toward the growing prosperity of the country and the population generally. Grave social imbalances remain and this will be a major challenge for legislators over the coming decades. The stock market and capital markets generally, are slowly being opened up in a process which will in all likelihood result in future Chinese financial infrastructure resembling that of more developed countries. However the way from here to there will not be linear and a number of significant profit opportunities will present themselves.

The [A-Share market](#) had accelerated to a spectacular high last year before giving up 50% of its value. The magnitude of its retracement sparked concern at government level and the cut in stamp duty was aimed at helping to revive investor sentiment. Since the April low, the market rallied strongly and is now gradually consolidating the gain. The Index probably bottomed at 3138 but it may take time before it can sustain a meaningful rally. The upside can be given the benefit of the doubt as long as it can sustain the move above 3000.

Eoin's personal portfolio: cocoa long opened - given the performance of the soft commodity complex over the last few months, I anticipate the bigger moves on the upside are going to be more as a result of fundamental factors individual to certain instruments, rather than bullishness about the sector generally.

The Ivory Coast [cocoa](#) crop is at risk of disease and cocoa is the only soft commodity currently making new highs. I bought the July [contract](#) of the Liffe traded contract at 1539p this morning including spread-bet dealing costs.

The Telegraph.co.uk: E.ON UK chief: Government 'must come clean on cost of renewables' - Thanks to a subscriber for this interesting [article](#) by Russell Hotten covering the cost of implementing more carbon-efficient power stations. Here is a section:

E.ON believes that building the necessary new generating capacity - from renewables, nuclear and coal and gas - could cost between £50bn and £100bn. All this must be paid for, Mr Golby said.

In a frank warning yesterday, Mr Golby criticised the quality of debate about the country's energy future, saying that it was dominated by single issue

politics. He called on the Government to take a lead in improving understanding of just how serious was the challenge to "avoid the lights going out".

He criticised in particular the notion that moving towards renewables was cheaper. "We must dispel the myth that renewables are cheap. Because we have all been silent on this, people think it won't cost anything.

"I'm not saying that moving to renewables is not the right thing to do. But we need to be honest with our customers. Moving to a low carbon economy is going to cause some economic pain in the short term," Mr Golby said.

As Britain becomes more dependent upon imported gas, and as ageing nuclear generating capacity is taken off-line, consumers will have to pay more for their energy.

The development of renewable power - especially wind - and a new generation of nuclear power stations will eventually ease the problem, but not until well into the next decade.

"If you look at how wholesale [gas] prices have gone, they have accelerated significantly ahead of retail prices. Looking forward into the future, I can't see that the fundamentals are going to change to bring those prices back down," Mr Golby said.

"The reality of the problems facing us is undeniable - an unparalleled transformation of our energy generation infrastructure at a time when prices are high and rising."

My view - Problems such as those being faced by the UK in renewing its energy infrastructure are shared by a host of countries. The drive to develop all types of infrastructure globally is a well recognised theme and is something which will play out over the coming decades. This competition is also forcing up the relative cost of production, making it sensible to begin such projects sooner rather than later.

Quite apart from the environmental concerns surrounding the oil complex, it makes increasing sense to look at producing more energy from renewable sources which are getting progressively cheaper, while over the long term, oil is only getting more expensive. The risk of oil entering a corrective phase has grown considerably, but its long-term potential remains intact. Companies offering exposure to the global infrastructure theme are likely to perform well over coming years.

The weekly Standard: It's Only Going to Get Worse - Thanks to a subscriber for this interesting [article](#) by Lawrence B. Lindsey which looks at the likely length of the housing bust and how it will eventually end. Here is a section from the conclusion:

So, optimists hope that new types of buyers will emerge, with three types

leading the pack: foreigners, inflation-hedgers, and the government itself. Some have said that laxer immigration laws are the way to absorb excess houses under the theory that immigrants need homes. In its popular version this view is actually quite naive. It is harder to imagine an easier immigration situation than the one that existed in the past few years, with its negligible enforcement. But what one might call "volume" immigrants aren't the answer. They are here to make money and save it and crowd themselves into housing, making them poor absorbers of excess homes. Moreover, many of them worked in the home construction, remodeling, and maintenance industries and are now unemployed and leaving the country. Opening the borders further to this type of immigrant is not only politically problematic, but also runs counter to current economic reality.

By contrast, "targeted" immigration might just work the trick. Imagine a hypothetical immigration program that gave a provisional green card to anyone who invested at least \$10 million in residential property and held it five years. To stop them from buying just their own expensive Upper East Side apartments, one might cap the value in each property toward the quota at \$1 million. A mere 100,000 people signing up would not only pump a minimum of \$1 trillion into the housing industry, they would also absorb at least one third of the current excess inventory. Trouble is, such high end immigration is just the type that a Democratic Congress finds most objectionable ideologically.

But foreigners might also be part of the solution thanks to the falling dollar. Not only are house prices likely to be down significantly from their peak, but so is the dollar. The cumulative decline in, say, condominiums in Florida or Las Vegas is at least 50 percent to a European, Japanese, or British buyer. So even without legislation to encourage them, foreigners are likely to provide some of the solution to the housing overhang.

Inflation hedgers are another potential source of demand. They are speculators who are willing to bet that borrowing at low fixed long-term interest rates on real property that will in the long run grow with inflation may be a good investment. True, Federal Reserve governors are correctly expressing their concern about gathering signs of inflation. But it is certainly not out of the question that the political, economic, and banking system pressures might induce the Fed to follow a more inflationary path. The Fed's first job is to preserve the banking system, and a 30 percent national home price decline would certainly prompt it to take action. This would cost money, which the Fed can create, albeit with a risk of further inflation. Now is probably not the moment to place that bet, but if home prices continue to decline at their current rate, late this year or early next year might be.

Finally, there is the government itself. During the last real estate collapse in the early 1990s, the government was forced to acquire a large amount of property as it worked to rescue the financial system. The chances are reasonable that at some point late in 2009 a similar approach might be adopted. The last time around it was called the Resolution Trust Corporation. It was, as one would expect from government, far from surgical in its approach. A lot of investors, bankers, and property holders probably lost more than they deserved to in the process. But it got the job done. It is the ultimate

last resort, using the balance sheet of Uncle Sam to save the housing market. If nothing else works, a new RTC is in the cards, and those who think Barney Frank's bill is a "bailout" will be shocked by its size.

The housing market crash is far from over, and its ramifications will be with us for some time. The combination of excessively easy credit, a rapid run up in prices, and overbuilding set the stage for the current mess. Prices must fall to correct oversupply, and that, in turn, will further adversely affect both consumer confidence and financial solvency. The unique nature of the problem makes a precise ending hard to predict. But it seems likely that some combination of speculative buying, inflation, and purchases by both foreigners and government entities will correct the situation. Now is not the time for ideology, of either the left-wing variety (soak the rich, punish speculators, and conduct a witch hunt through the financial community) or the right-wing variety (stave off government involvement of any form). Pragmatism is a conservative virtue. It is time for everyone to start practicing it.

My view - [When the US housing market bottoms is an unknowable, but what is for certain is the next President will need to be seen to be doing something concrete about the fate of those most affected, if he wants to be re-elected. This means that a Federal bailout for the sector will become increasingly likely the slower it is to recover.](#)

Today's interesting charts - [The Chart Library filter allows you to rank instruments according to performance in a constant currency.](#)

Nasdaq-100 - [rallying](#) and would need to sustain a move below 1950 to offset scope for some further upside.

Oman - [extending this consistent uptrend](#) and, in the absence of acceleration, would need to post a correction larger than 1000 points to mark a significant inconsistency.

South African Rand per 1 US Dollar - [The Dollar](#) is rallying from support near 7.5 and it would need to sustain a move below that level to offset scope for some further upside.

Thursday 5th June 2008

Anatole Kaletsky: Stone Age lesson on taming the oil price - [This is a superb and somewhat controversial article](#), published in The Times recently. Here is the opening:

Just as the credit crunch seems to be ending, the world faces a much more serious economic threat: the explosion of oil prices and the possibility of a return to 1970s-style inflation. Inflation is a more dangerous economic ill than deflation because it is so much harder to cure. Falling prices can be cured easily enough. All governments and central banks have to do is cut interest rates, cut taxes and boost public spending. These are popular steps that readily win political and business support.

The policies required to deal with inflation are, by contrast, always painful and unpopular - raising interest and taxes; cutting government spending and curbing public employees' pay. It is hardly surprising, therefore, that only one country in the world - Japan - has faced a serious deflation problem since the 1930s, while inflation crises have afflicted every market economy in the postwar era and have triggered almost every big recession since 1945. The question, now that the focus of attention is moving beyond the credit crunch, is whether this sad history is likely to repeat itself in the year or two ahead.

The answer depends largely on how governments and central banks worldwide respond to the oil shock. The challenge most discussed in recent weeks is the one facing central banks. If the surge in oil prices causes accelerating pay growth and then a second round of price rises in goods and services not directly exposed to oil, central banks will face stark alternatives: either deliberately to create recessions and mass unemployment by raising interest rates even amid the present property slump, or to accept 1970s-style wage-price spirals, which will have to be cured eventually with even deeper recessions, higher unemployment and greater financial grief.

The other, even bigger, challenge of the oil shock is the one presented to governments. This is the question of what can be done to reverse the rise in oil prices. This question is even more important than the central banks' inflation-deflation dilemma and yet is hardly discussed. Most politicians, economists and financiers simply assume that the trebling of oil prices in the past few years has been a natural phenomenon that must be accepted as an act of God - or at least an inexorable judgment by the markets. However, are there really no policy changes that could restore the more benign conditions in which oil prices of \$40 or \$50 were seen as normal?

The standard answer is "no" - oil at \$100-plus must be accepted as inevitable and natural because growth in global oil production cannot keep up with growing demand, especially from China and the developing world. However, even if this were so - and statistical facts about the "peak-oil" limit to global production capacity are ambiguous, to put it mildly - it begs the question of whether oil consumers could soon take steps that would drastically reduce demand.

Specifically, there are four big steps that governments in oil-consuming regions could take once they recognise the existential economic threat of a \$100 oil price.

My view - It has been wryly said that central banks face a blinking contest in determining whether they should fight inflation, epitomised by soaring food and energy prices, or deflationary pressures signalled by weakening economies.

Of course this is an oversimplification, not least because central banks are the great inflationists. Just consider the inflationary expansion of monetary policy in excess of GDP growth over the last eleven years or more. I maintain that central banks are closet inflationists, in the business of managing inflationary expectations, while ensuring that moderate rate of inflation persists.

When push comes to shove, central bankers will usually blink in favour of inflationary risks rather than recession. Proof of this claim can be seen in the cost of living, which rises much more than it declines in this fiat currency world, especially if we look at our household bills rather than the phoney official statistics.

Inevitably, some central banks feel that they need inflation more than others. It reduces the real cost of debt, albeit at the price of eroding the purchasing power of savings. Ben Bernanke of the Fed, for instance, is more tolerant of inflation due to the USA's indebtedness, than Jean-Claude Trichet of the ECB. For this reason the US dollar's recent rally is standing on stilts rather than a solid foundation.

What of Anatole Kaletsky's "four big steps" for dealing with soaring oil prices?

1. Kaletsky: "...remove energy subsidies."

I agree and also mentioned this yesterday. Asian countries have begun to lower if not remove subsidies. Unfortunately, oil exporters are most unlikely to do this any time soon.

2. Kaletsky: "...reduce the artificial demand for long-term oil-hoarding created by pension funds, insurance companies, endowments and other long-term investors."

I agree and have previously said that most commodities were never intended to be an asset class. This is controversial but I think Kaletsky's points are valid. If one wishes to be in commodities, as I have often been since 1971, trade the near-term futures contracts. This increases liquidity and therefore works with the markets, which were developed mainly to assist producers and consumers of commodities, rather than against them.

3. Kaletsky: "...end America's costly reliance on oil imports. This consensus could lead America towards European-style energy taxes, offset by lower taxes on income and employment."

I never thought I would advocate a tax hike, but I believe this is necessary to avoid a disaster, and it can be offset by tax cuts as Kaletsky recommends.

4. Kaletsky: "...create far greater financial incentives for renewable and nuclear electricity generation."

Once again, I agree. This has long been an urgent matter of common sense. Governments should work in partnership with universities and industry on these projects, while allowing the market to determine which succeed and fail. Needless to say, all of the above will take time and not resolve the immediate problem of high energy prices.

Email of the day - On markets:

"I get a strong sense that the markets are directionless and that there seems to be very little conviction coming from investors, analysts and the economic and financial gurus. Maybe that is because we are not sure about what type of economic environment we are dealing with. The following [article](#) by Paul Krugman argues against the idea that we are looking at a replay of 70s style stagflation.

"Seems Bernanke can't win even if he wins. The other controversy du jour is the expanding coverage of the accusation of speculation by index funds and hedge funds as the reason for the commodity price strength. I should not make light of this, as it would be tragic if a Democratic Congress bought this argument. Don Coxe's most recent audio made a few good points. He obviously believes this to be ridiculous. In the last 5 years, we know that the giant pension funds, from the Harvard and Yale endowment funds (usually first to make changes) to the rest of the massive institutional money, have slowly begun to include commodities in their asset mix. Their reasoning would be as more of a risk diversifier, than as a speculation on commodities. The non-correlating asset optimizing risk-reward theories have steadily been showing commodities to work as an asset class that embellishes return without any extra risk in the passive asset mix. Don Coxe's point is of course, that if this kind of money goes from 0 exposure to 3-5% exposure, it would mean massive amounts going into the commodity futures market through the indexing funds. Of course, Coxe believes it is first and foremost a demand-supply issue. But it is difficult to argue with his point about Pension funds and is Congress about to intervene with the world's largest pension funds buying commodities as a non-correlating asset class.

"I think they might have a problem if they went there."

My comment - [Thanks for a reasoned contribution.](#)

[I certainly concur with your opening sentence. And if this is still the first psychological perception stage of a market recovery as I suspect \(the performance of western banks remain an Achilles' heel for this hypothesis\), then we would expect confidence to remain low during a lengthy support building process.](#)

[Thanks also for the Krugman article. The intensely competitive pressures created by globalisation have certainly helped to cap wages in the USA and Europe. However wage pressure in countries with higher growth rates is often more intense.](#)

[Regarding commodities, I maintain that food and energy were never meant to be long-term asset classes. I know there are counter arguments but investors in commodity tracker funds will not be regarded as useful stakeholders when the world's poor cannot afford energy and food. Of course supply and demand fundamentals made commodities interesting, as Fullermoney as argued for most of this decade, but the tracker funds are now distorting markets which are essential to our supplies of food and energy, without contributing anything to these requirements. This is literally becoming a life and death issue. If the pension and other funds want long-term "non-correlating asset optimizing risk-](#)

reward" diversification, they can buy commodity shares and farmland. They can also buy gold, which has been real money for a lot longer than it has been an industrial commodity.

My personal portfolio: A profit taken in silver; a long in corn opened; gold long increased; TFC repurchased - Deciding to be a bit more active in ranging markets, this afternoon I sold the [silver](#) purchased yesterday. This was a July position bought at \$16.715 on 4th June and sold on the 5th at \$17.135, reducing my overall position by a third. Today's price action in silver is actually quite positive but this remains the most volatile of precious metals. Stop press: I reopened this silver long in late trading because it is at the bottom of a range and today's official closes in a number of markets could be supportive.

I mentioned in Tuesday's Audio that I had heard there were problems with the US corn and soybean crops due to excessive rain and cold weather. Prices rallied yesterday and somewhat belatedly I jumped aboard today, choosing [corn](#) because of its overall relative strength in the sector. I paid 628.25¢ for a July position.

I also bought more [gold](#) this afternoon, as it was lagging for some hopefully temporary reason unbeknown to me. I paid \$875.25 for another August position, increasing my overall trade by a third. Stop press: I increased my long by an additional 33% in late trading, paying \$880.35 for another August position.

Lastly, noting the upside key day reversal in [Taiwan](#) today, I reopened my long in the Taiwan Greater China Fund ([TFC US](#)), paying slightly less than I sold it for last month. I paid \$7.333 for a June position.

Prices above include spread-bet dealing costs.

Today's interesting charts - Charts can signal sudden and important changes in sentiment.

Crude oil (WTI) - Today's upside key day reversal, above important support at \$120, has stemmed the slide for at least the near term and preserved trend consistency in the process. A close beneath this price is now required to confirm a medium-term correction rather than sideways to higher ranging.

USA (Nasdaq 100) - Extending [recovery](#) from March low into overhead trading; would require a close beneath 1980 to question current scope for an additional test of prior resistance.

US Dollar Index - Downside key day [reversal](#) reaffirms resistance near the higher side of current range; a close above 74 is required to indicate higher scope rather than sideways to somewhat lower ranging towards at least 72.

Important update on US corn and soybean crop - My thanks to an informed subscriber for this information which I also mentioned in Tuesday's Audio.

Basically, the US [corn](#) and [soybean](#) crops are in "serious trouble" due to unseasonably cold and wet weather in the key producing states. This has delayed planting and growth, and even drowned some of the corn, necessitating replanting. Consequently much of the crop is two to three weeks late at a critical period. For instance, corn is only 2 to 3 inches high when it should be 4 to 16 inches tall. Young plants in extremely wet fields do not develop deep roots, leaving them vulnerable to drought in the hot summer months. Also late crops are at greater risk of frost damage prior to harvesting.

What could this mean for crop yields? Our knowledgeable source said that of the five slowest planting years since 1990, yields were down an average of 8.4%. The 2008 crop is currently showing the second slowest combination of planting and emergence. A rapid and dramatic improvement in weather conditions is required to prevent a similar lowering of yields. This seems unlikely given the weather [map](#). If you trade grains and soybeans, I recommend that you add the National Weather Service to your 'favourites'.

Additional Commentary by Eoin Treacy

Coal earnings will be constrained by cost increases, as regulations stall new coal plants - [This article](#) by Dorothy Kosich for Mineweb covers the challenges facing the coal industry as costs rise. Here is a section:

As U.S. coal producers benefit from tight global markets for both steam and metallurgical coals, Fitch Ratings cautioned that "high consumable prices and labor costs will constrain earnings growth over the new few months. "

In the report, 'Coal Outlook: Summer Burn, Supply Response', which was released by Fitch Wednesday, Monica Bonar, Director, Fitch Ratings, and analyst Sean Sexton noted that "mining in new or challenging regions can amplify already high maintenance and capital costs."

Constraints to developing new coal mines include high capital costs, the need for sales contracts covering a high portion of new tonnage, and a lengthy permitting process, according to Fitch. While some producers are announcing new projects, the analysts noted that "these have more than two years lead-time and may only replace declining production at existing mines."

While coal producers are benefiting from tight global markets for steam and metallurgical coal, regulatory uncertainty about carbon emissions has stalled plans for construction for many new coal plants, which Bonar and Sexton said, will cap domestic demand in the medium term.

"Stocks are reportedly tight for Northern Appalachian coal, high for Powder River Basin coal, and comfortable for Central Appalachian and Illinois Basin

coals, according to the report. However, the analysts predicted that coal company earnings growth will be constrained by cost increases. "Coal producers are experiencing high prices for consumables such as fuel, explosives and steel in addition to high labor costs. Maintenance and capital costs have been on the rise, which can be amplified when mining in new or difficult areas."

While steam coal inventories are reported to be at comfortable levels, contract prices are up. Fitch expects steam coal realization growth to flatten out over the 12-18 months "absent a new supply growth."

Meanwhile, metallurgical coal prices "have blown through expectations on short supply. World growth in demand for metallurgical coal has not been met by a corresponding increase in Australian coal export infrastructure, particularly port and rail," the report said. Currently, prices are settling at \$305/mt for the year ending March 31, 2009, with supply not expected to significantly ease until 2010.

My view - For decades the trend was to close coal mines because they were uneconomic. To suggest to anyone even a couple of years ago that the industry could undergo a renaissance would have been greeted with derision. However, coal has been rehabilitated although it remains a leading polluter, driven by the expansion of steel and energy capacity in the developing world.

Coal mines faces the same challenges as other mining operations in controlling costs but those producing higher grades have a degree of pricing power they wouldn't have dreamed off only a few years ago. Bottlenecks in transportation remain and are not likely to clear for a number of years.

The best performing sectors in the S&P this year have been trucking and railroads. The Dow Transports Index has also outperformed and is currently testing its highs near 5500. A sustained move below 5150 would be needed to offset potential for an upside break.

The S&P Trucking Index containing only one company, [Ryder System](#), remains in an impressive uptrend from its lows near \$40. A sustained move below \$70 would break the progression of rising lows and would be needed to question potential for further upside

While Trucking is the leader, railroads have performed almost as well. [Burlington Northern Santa Fe](#), [Union Pacific](#), [CSX Corp](#), [Norfolk Southern](#), [Kansas City Southern](#) and [Genesee & Wyo](#) have all surged upwards from the beginning of the year and are clearly leading the market on the upside.

CSX Corp is the only one not still in a consistent pattern. The downward dynamic on Tuesday broke the integrity of the uptrend and makes the share decidedly more high risk.

The others remain in overall uptrends and are probably best bought following corrections with this consistent overall move. They could also be lead indicators for the next major turn down in the overall market when they lose consistency as a group.

Astaire Research: The India Report - Thanks to Deepak Lalwani for his informative [report](#) which this week focuses on the easing of investment restrictions. Here is a section:

In a long overdue move, the Indian Government liberalised rules on bond market investments and Foreign Exchange Commercial Borrowings (FCCBs). The Foreign Institutional Investors (FII) limit was raised to \$5bn from \$3.2bn and for corporate bonds to 3bn from 1.5bn. Also with immediate effect, the limit on how much a company can borrow and repatriate to India for Rupee expenditure was raised from \$20m to \$50m and to \$100m for companies in the infrastructure sector. The changes will apply to both the automatic and approval routes, but the \$500m limit per company per year for automatic approval remains. The Finance Ministry added that the allowable costs of such borrowings would be raised from 150 basis points (b.p.) to 200 b.p. over 6-month LIBOR for debt of 3-5 years maturity and from 250 b.p. to 350 b.p. for debt over 5 years. Also allowable now under the approval route are borrowings of up to \$100m for service sector companies. Thus, for the first time hotels, hospitals and software companies, among others, become eligible.

We believe the Government has been forced to make these moves so as to increase the inflow of foreign currency at a time when FIIs have sold Indian stocks worth nearly \$4bn and the Rupee has depreciated nearly 8% this year. The Government, which was slow to open the debt market, and actually put restrictions on FCCBs last August, is now forced to relax the rules to aid the currency. Although about \$500bn over the next 5 years is needed for infrastructure, which a developed corporate bond market could help provide, the Government has been slow to develop this market.

My view - India still has a long way to go in order to provide the necessary infrastructure to allow a first world economy to develop. Hopefully, the government has come to the realisation that punishing the capital markets is not helping to fulfil their aim of developing the economy. If this type of obfuscation continues the pace of inward investment will slow.

India's Future Rides on 76-Year-Old 'Metro Man' - This interesting [article](#) by Andy Mukherjee for Bloomberg covers one of the more successful infrastructure projects currently underway in India. Here is a section:

Indian politicians never tire of proclaiming that their country's population is among the youngest in the world: Every third person, they note, is aged 30 or less.

What they don't often acknowledge is that one of the biggest heroes in this nation of young people -- the person who is doing more than most to put taxpayers' money to work for the benefit of citizens -- is a railway engineer who turns 76 next week.

Elattuvalapil Sreedharan, popularly known as India's "Metro Man," is the managing director of Delhi Metro Rail Corp., which operates the newly built

world-class subway that's transforming the economy of India's capital, New Delhi. It's also improving the city's air quality, altering its social life and even influencing norms of individual behavior.

Funded by government equity and debt and a soft loan from the Japan Bank for International Cooperation, a \$2.3 billion, 65-kilometer (40-mile) section of the project was completed in 2005, three years ahead of schedule.

Not just that: The stations are clean and spacious; littering is almost non-existent; people wait their turn at the metal detectors; the trains are comfortably air-conditioned even during peak office hours; the waiting time is short; and trains are punctual 99.9 percent of the time.

Delhi Metro has been such a hit that real-estate values have already risen along the planned routes for the second phase of the project in which an additional 121 kilometers of tracks are being laid at a cost of \$4.3 billion.

My view - It has been identified ad nauseam that India is badly in need of infrastructure to ease the way to more sustained growth. The New Delhi Metro is a good example of what can be done when infrastructure projects are given high priority and let us hope that is this the beginning rather than a single example.

Eoin's personal portfolio: Nikkei long opened and corn long opened - Seeing the strength of Wall Street and positive action generally in Japan, I opened a long in the June [Nikkei](#) contract paying 14,520.

I also opened a long in the July corn contract paying 638.25¢. [Corn](#) has been the leader in of the grains and broke upwards today to make a new high. I am willing to give the upside the benefit of the doubt.

China's forex reserves hit 1.76 trillion dollars: report - Thanks to a subscriber for this interesting [article](#) posted on yahoo but written by AFP. Here it is in full:

China's foreign exchange reserves rose to 1.76 trillion dollars at the end of April, state media reported Monday, reaching a level higher than the rest of Northeast Asia's combined.

China's reserves, by far the largest in the world, expanded by another 74.5 billion dollars during April, the China Business News reported, equivalent to about 100 million dollars every hour.

At 1.76 trillion dollars, China's reserves are now larger than those of Japan, Taiwan, South Korea and Hong Kong combined. The growth in reserves came amid rising official concern about a fresh surge in hot money -- or speculative inflows -- spurred by a strengthening yuan and a widening spread between falling US interest rates and rising Chinese rates.

The increase in reserves was roughly three times larger than the trade surplus

and the value of incoming foreign direct investment -- the two traditional sources of reserve growth.

This led analysts to conclude that perhaps as much as 50 billion dollars entered the economy in the form of hot money.

"This (figure) seems to suggest the inflow of hot money is speeding up," the newspaper quoted Logan Wright, an analyst with Stone and McCarthy Research Associates, as saying.

My view - The [Yuan](#) remains in an overall uptrend against the Dollar following the end of its peg back in 2005. The pace of its ascent may not be to every one's liking but there is no denying the direction the yuan is moving in. This is a point not lost on investors, capable of investing yuan denominated assets.. The strengthening currency remains a valid reason for considering investing in China and when perceptions coalesce around the view that the equity market has bottomed, funds flows could increase even further.

Today's interesting charts - Just about every liquid and many not so illiquid commodities can be found in the Chart Library.

Russia - [reacting](#) in a consolidation following recent strong gains and would need to sustain a move above 2500 to reassert the overall uptrend.

Euro per 1 US Dollar - The Euro finds [support](#) at the lower side of the range and rallies well. It would need to sustain a move below today's lows to offset scope for some further upside.

Oats - [breaking upwards](#) from the short-term range and testing the March highs. A sustained move below 400¢ would be needed to offset scope for further upside.

Email of the day (1) - on additions to the Chart Library and finding securities:

"Thanks for prompt reply regarding the Inverse US Treasury ETFs-PST and TBT; just wonder if you could add to the chart library ETFs that track respectively the same indices however with longer trading history-[IEF](#) and [TLT](#) for the 7-10 Yr and 20+ Yr US Treasury Index, on top of PST and TBT.

"Would also like to have the following HK/China ETFs and close-end funds added to the library:

[TDF](#)-Templeton Dragon Fund

[GCH](#)-Greater China Fund

[CAF](#)-MS China

[FXI](#)- iShares A25 Tracker

[CHN](#)-M Currie China Fund

[820](#).HK-HSBC Dragon Fund

[2827](#).HK-CSI 300 China Tracker

[2823](#).HK-A 50 Tracker

"Thanks!"

My comment - Thank you for these suggestions. All but three of the funds listed above were already in the Chart Library and they have now been added.

Email of the day (2) - on additions to the Chart Library and finding securities:

"Maybe it is because I am lazy or perhaps because I want to be more efficient with my time but please could you add the following UK listed property companies to the Chart Library. I review them everyday and this is sector which may come to life in the medium term. They are:

F&C Commercial Property ([FCPT.L](#))
ING UK REIT ([IRET.L](#))
Invista Foundation ([IFD.L](#))
Invista European Real Estate ([IERE.L](#))
MedicX ([MXF.L](#))
Terra Catalyst ([TCF.L](#))
TR Property ([TRY.L](#))
TR Property Sigma ([TRYx.L](#))
UK Commercial Property ([UKCMq.L](#))
ING Global Real Estate ([IGRE.L](#))
iShares FTSE EPRA Asia ([IASP.L](#))
iShares FTSE EPRA UK ([IUKP.L](#))
iShares FTSE EPRA Europe ([IPRP](#))

"My apologies if they are already on site but I haven't been able to find them. I would find this helpful and I hope fellow subscribers will too. Many thanks one the great "one shop stop" service."

My comment - At present the Chart Library has two different searches but we are currently working on combining them to make finding any of the more than 17,000 securities easier. All but one of these funds was already in the International Equity section of the Chart Library. I have added the Terra Catalyst fund.

To Search the International Equity Section, select it from the main Chart Library dropdown menu. Alternatively, when you hit the search button you will see a 'Search the International Library' tab.

Friday 6th June 2008

Alex Seagle's The Contrary Investor: Electrifying Developments - I always enjoy this [letter](#), written by Alex Seagle of Fraser Management Associates. The current issue features in reverse order, renewable energy, railroads and a technology aspect of infrastructure development. Alex Seagle also mentions me in this issue but don't hold that against him. Here is the opening:

The Contrary Investor has ruminated frequently on the investment opportunities associated with the need for infrastructure repair and

replacement. Our focus has been on the aging water and wastewater infrastructure in the U.S., but the theme stretches across many of the systems we take for granted will work to serve our basic needs. For example, the bridge collapse in Minnesota last year was a grim reminder of the state of our roads and bridges, and the need to replace a startling number. Taken in the aggregate, infrastructure issues will require trillions of dollars in the very near future.

Another area for study is the nation's electrical power grid. The electric industry has been talking for decades about bringing the nation's antiquated, inefficient, glitch-prone energy grid into the Computer Age. Now, with energy demand rising twice as fast as supply, it's finally happening, thanks to a rare alignment of interests - government, business, consumer, and environmental.

Government and industry studies estimate that a modern digital energy grid could trim the country's power usage by 10 percent, reduce greenhouse gas emissions by 25 percent, and eliminate the need for \$80 billion in new power plants. It is another example of the "it's not a question of whether such a grid can be built, but when."

The basic idea is to replace a passive, analog electricity delivery system with one that is two-way and aware of what is happening to it at any moment. In other words, a smart grid. It will be a very large market opportunity. According to the Edison Electric Institute, utilities over the next 20 years will spend hundreds of billions of dollars on infrastructure improvements, including computers, sensors, and networking systems. This is a huge new market for IT and networking companies, and there is no shortage of firms big and small scrambling for a piece of the business,

My view - Global infrastructure development has been one of Fullermoney's secular themes for a number of years, although more often than not we have thought of it mainly in terms of demand for industrial resources and heavy equipment. However technology also has a major role to play in global infrastructure development, as it increasingly does in so many other industries. This helps explain why the sectors' relative strength is likely to be more than cyclical.

I will be speaking at Fraser Management Associates' Contrary Opinion Forum at Basin Harbor, Vermont, from October 8th to 10th, and look forward to seeing subscribers at this event.

Email of the day (1) - [On agricultural prices and relief:](#)

"With regards to agricultural prices, the medias all talk about speculation but never about the source, i.e. inflation and printing money. You might have noticed that the number of bills in circulation which have been remarkably stable at about \$815 billion over the last few months have suddenly jumped to \$823 billion. Put a velocity factor of 20 on that, and you have got one whopping injection...

"Off to Cairo with my wife Maya who has been invited to give a concert there, so we're trading stock market anxiety for stage fright, which I suppose is some kind of relief."

My comment - [Good point and enjoy the relief.](#)

Niels Jensen's The Absolute Return Letter: The Untold Story - [My thanks to a subscriber for this excellent research covering many oil-related topics discussed on this site recently. Here is the opening:](#)

"If you look at the facts, they show that the price of oil is about supply and demand"

Henry Paulson, U.S. Treasury Secretary

In the rather mundane world of investments, rarely has one individual caused as many ripples as Michael Masters¹ did when, only a couple of weeks ago, he chose to share his thoughts on commodity prices with the distinguished members of the U.S. Senate Committee on Homeland Security and Governmental Affairs. If ever a cat was put amongst pigeons...

Masters merely suggested that speculative demand is behind much of the recent rise in commodity prices and that U.S. lawmakers must curb speculators' access to commodities if they want to get commodity price inflation under control. The debate is reasonably straightforward. Are commodity prices driven by economic fundamentals (i.e. a function of supply and demand) or are speculative investors (primarily pension funds, index funds and hedge funds) to "blame" for the stratospheric rise of commodity prices in recent months?

I actually touched on this subject in last month's letter and do not intend to repeat myself. However, it appears to me that a number of hard facts have been swept aside, as the move in oil prices has become rather one-sided in recent months. Even if you believe in the concept of Peak Oil², it is important to recognise the fact that oil prices, like all commodity prices, are sensitive to economic up- and downturns. In the following I intend to take a hard look at those arguments underpinning the bull story on oil prices.

The notion of Peak Oil has led many to believe that global oil production is actually in decline. When I did my research in preparation for this letter, I was astonished to learn how many so-called 'experts' seem to confuse Peak Oil with global production decline. In reality, global production has risen every year since 2002 and it continues to grow. Peak Oil is a local phenomenon (at least until now), with large oil producing countries such as the United States, Venezuela, the United Kingdom, Norway and Indonesia all in terminal decline.

My view - [I think subscribers will find Niels Jensen's analysis of oil supply and demand clear and informative. Also, we know that today's prices can only encourage technology-enhanced efforts to increase production of both conventional and non-conventional reserves. Today's prices for crude oil will also boost the alternative energy industries.](#)

Jensen's comments on long-term investments in commodity tracker funds is also interesting, not least the last paragraph of his report.

Email of the day (2) - On previous growth built on cheap oil:

"David, whilst I fully respect your wealth of knowledge I must point out that you are ignoring the high oil price and its effect on world growth particularly Asia. With Peak Oil potentially either here or not that far away as evidenced by sluggish production growth is it not time to reconstruct portfolios around Peak oil. Growth over the last decades has been built on cheap oil and growing production. I believe in your supply inelasticity theme in respect of oil but that is at odds with your portfolio which is heavily geared to growth and as oil provides something like 95% of transport fuel, growth is at risk. By the way, the article you posted today from Hugh Young for all his ability makes no reference to the price of oil and that in itself tells me something."

My comment - You make some good points and I think this is a question of judgement rather than knowledge. Higher energy prices have always been part of Fullermoney's Supply Inelasticity Meets Rising Demand theme. If you want to emphasise energy more heavily, I personally would think more about the alternative / renewables sectors. I intend to comment further on this shortly. They are being developed by democracies and cannot be nationalised by totalitarian regimes.

For the record, my personal long-term portfolio is about equally weighted between resources and growth, which are interrelated to a certain extent, although I suspect the growth story will outlast the energy story over the very long term. And if not, perhaps due to some ecological disaster, energy will be a less promising investment without GDP growth.

My personal portfolio: Nikkei long increased; profits taken in silver; partial profit taken in gold; loss taken in HSI - I maintain that Japan currently has the most interesting technical patterns among non-resources, developed country markets. Therefore I increased my [Nikkei](#) trade early this morning, shortly after Japan's opening. I would have done better to hold off as I paid 14630 for another June position, doubling my exposure.

In today's nervous, choppy market environment I'm looking for opportunities but trying not to take too many risks. The best way to do this, I believe, is to buy low and sell high. Having seen my precious metals positions move in and out of profit, and having some gold that is still underwater following a too optimistic purchase last month, I decided to use today's strength following today's US employment report to take some profits. First, I sold two-thirds of my remaining [silver](#) longs at \$17.358 for the July contract, against my purchase at \$17.158 on 29th May (reported on 2nd June as I was on holiday at the time). And in what proved to be too cautious, I placed a tight stop on my remaining silver long as I had paid up for it at \$17.19 last night. My stop was triggered this afternoon at \$17.22, also in the July contract. Using today's

strength I also reduced my [gold](#) longs by 25% today, selling an August position at \$891.65 against my purchase at \$880.35 yesterday.

Needless to say, this is leveraged trading. The overall patterns for gold and silver remain attractive and I maintain these monetary metals are in secular bull markets. Investors in the bullion funds hold what I regard as some of the safest long-term assets. Gold shares are much more volatile but should have another run at some point, at which time I may take some profits.

This evening, noting forecasts of further rain in the US grain and bean regions, I increased my [corn](#) long by 50%, after raising the in-the-money stop on my initial position. This may be justified fundamentally but it is risky as there is talk of the CFTC becoming involved in an attempt to cool these markets. Consequently I am using a tight stop. I paid 660.50¢ for a July position this evening. I also note that while I mentioned yesterday's corn purchase, I forgot to add the price. For the record, I paid 628.25¢ for July corn and have also added this information to yesterday's copy.

With the oil price up \$11 later today, I decided to offset my Nikkei purchase by closing my [Hang Seng Index](#) longs. I sold my June positions at 23763 against my purchase at 24182 on 2nd June.

Prices above include spread-bet dealing costs.

Chris Roberts on the Hang Seng Index - Chris is one of the most experienced technicians. Here is his [latest](#) forecast.

Today's interesting charts - To develop your working knowledge of the Subscriber's Chart Library, use the "Filter" and "Help" buttons shown at the top-right section of the Library.

Gold - [Rebounding](#) from lower side of \$850 to \$950 range in what looks like a medium-term consolidation within the long-term uptrend ([weekly](#) & [monthly](#)). A close beneath the former level would be required to question current scope for sideways to higher trading.

Platinum - Firm within [range](#) after encountering support near \$2000; would require a close beneath \$1950 to offset current scope for sideways to higher trading within the long-term upward trend ([monthly](#) & [weekly](#)).

Crude oil - Surged [higher](#) following yesterday's upside key day reversal. The medium-term [trend](#) is steepening once again and at a rate that is unlikely to be sustainable beyond the short term. However a close beneath \$120 remains necessary to check this trend beyond a temporary consolidation.

Germany (DAX) - Resumed [decline](#) following failure to maintain break above 7000; now requires a close above this level to offset scope for some further retracement of gains since the March low.

USA (S&P 500) - More than [reversed](#) yesterday's upward dynamic; requires close above 1410 to offset scope for some additional retracement of gains since the March low.

Quote of the week - [On progress](#):

"Progress might have been all right once, but it has gone on too long."
Ogden Nash

Additional Commentary by Eoin Treacy

Dollar Falls to One-Week Low Versus Euro as Jobless Rate Rises - [Thanks to a subscriber for this interesting article](#) by Ye Xie and Bo Nielsen for Bloomberg covering the weakening of the Dollar over the last two days. Here is a section:

The dollar fell to a one-week low against the euro after a government report showed the U.S. unemployment rate increased the most in more than two decades, adding to evidence the economy may not be rebounding.

The decline pushed the currency to its biggest two-day drop since March on speculation the Federal Reserve may refrain from raising borrowing costs this year. The dollar fell yesterday as European Central Bank President Jean-Claude Trichet said a July increase in the main refinancing rate, now twice the U.S. benchmark, is "possible." Crude oil surged for a second day

"It's another blow to the dollar after Trichet's hawkish comments yesterday," said David Powell, currency strategist in New York at Bank of America Corp. "The labor market is deteriorating. The interest-rate differential is moving in favour of the euro and against the dollar. We're going to retest \$1.60 in the next few days."

The dollar decreased 0.9 percent to \$1.5728 per euro at 12:08 p.m. in New York, from \$1.5593 yesterday, when it dropped 1 percent. It touched \$1.5750, the weakest level since May 28, compared with the all-time low of \$1.6019 reached April 22. The dollar dropped 0.6 percent to 105.34 yen, from 105.94. The euro increased 0.3 percent to 165.70 yen, from 165.20.

The U.S. currency has fallen 0.9 percent against the euro this week, while gaining 0.1 percent versus the yen. The euro was headed for a weekly increase of 1.1 percent versus the yen.

My view - [The Dollar](#) has been in a downtrend for the last two-years and its decline picked up pace in February as it fell through 75. Having found support above 70 in late March, it moved into a range which has persisted for the last few months. In terms of duration and amplitude, this is a similar sized reaction to that seen between November and February. The downward [dynamics](#) of the last two-days cap the advance in the short-term and the Index would need

to sustain a move above 75 to question the integrity of the overall downtrend.

Given the similarities with the last distribution a further break on the downside can not be ruled out. Looking at back history, the Dollar generally tops and bottoms in a war between supply and demand which can take years to resolve. This suggests that the tops and bottoms form big rangy, volatile patterns and this case may be no different. Since the Fed is beginning to voice concern relating to a weak Dollar, we may be in the region of an important low, but there isn't a great deal of evidence to support that view on the chart just yet.

Mineweb.com: Canadian potash miner hits new records on CEO outlook and output increases - Thanks to a subscriber for forwarding this interesting article by Roberta Rampton which contains a number of quotes from Bill Doyle, Potash Corp's CEO. Here it is in full:

Shares of Potash Corp hit a record high on Thursday as its chief executive gave a rosy outlook for the world's largest fertilizer company to a Merrill Lynch conference.

Record grain prices have spurred demand and prices for fertilizer, sending the Toronto-listed shares of Potash up more than 175 percent in the past year, reaching a record C\$221.75 on Thursday.

Bill Doyle said the company is prepared to mine 50 percent more potash fertilizer annually in coming years, at prices that are poised to rise further still.

"Yet many investors seem more concerned about what's in the rear-view mirror and whether they missed the ride, with the result that our forward multiples ... are the lowest I can remember," Doyle said.

"We encourage our shareholders to keep their eyes on the road ahead because our earnings potential is far greater than where we've ever been before," he said.

Potash shares were up 4 percent or C\$8.40 at C\$220.90 in Toronto late on Thursday.

Doyle said surging world demand for food will mean farmers need to continue to produce record crops, and said he does not believe crop prices will turn lower any time soon.

Potash producers have not been able to produce as much fertilizer as customers want to buy for almost a year, and Doyle said he expected the shortage would last into 2009.

"We're very excited because we know for sure between now and June of 2013, there's no new greenfield mine coming on anywhere in the world," Doyle said.

There has been a flurry of interest in exploration in potash belts in Russia and Canada, but Doyle cautioned it takes five to seven years and at least \$2.8 billion to build a new potash mine, plus infrastructure costs.

"Anyone looking at greenfield (projects) must justify their project on pricing in years eight and beyond, and that's a very big bet to make," he said.

Agrium Inc , another key producer in Canada's potash belt in the western province of Saskatchewan, is examining whether to build a new mine.

Last month, BHP Billiton Ltd bought out a Canadian junior potash mining partner.

BHP has said it will decide whether to move forward on potash plans in 2010, Doyle said, meaning the mining major would produce potash in 2017, at the earliest.

"We'll wait and see what happens there, but it's not immediate. There's no quick fix here," Doyle said.

My view - Potash is a true example of a Supply Inelasticity Meets Rising Demand theme. State controlled enterprises occupy much of the potash market leaving a small number of publically traded companies that offer exposure. The nature of how potash deposits are spread around the world also makes it difficult to increase the number of companies mining the commodity.

[Potash Corp of Saskatchewan](#) is one of the largest publicly traded companies in the sector and accelerated to the high near C\$200 in April before consolidating for a month and broke upwards again yesterday. A sustained move below the most recent lows would be needed to question the integrity of the overall move.

All commodities have firmed somewhat over the last couple of days, led my oil. The [CRB](#) Index, which is heavily weighted to oil broke upwards to new high ground today and would need to sustain a move below 415 to question upside scope. The [Continuous Commodity Index](#) (Old CRB) is more evenly weighted and was slower to recover following the March reaction. It continues to push back towards the highs and a sustained move below 540 would be needed to question upside potential.

Deutsche Bank Talking Point: Long overdue investment grade rating affirms Brazil's increasing economic and financial maturity - [This article](#) by Markus Jaeger for Deutsche Bank covers a number of important Brazilian economic fundamentals. Here is a section:

Brazil used to be what sovereign debt analysts call a serial defaulter. Like many other Latin American countries, Brazil frequently defaulted on its external debt obligations during the 19th and 20th century. In 2002 during the run-up to the presidential elections, Brazil again narrowly avoided yet another

default. Since then a disciplined, stability-oriented economic policy combined with a bit of good luck (read: rising commodity prices) has transformed the country from a serial defaulter into a net external creditor and, following the S&P and Fitch upgrades, into an investment grade credit.

The improvement of Brazil's external position has been nothing but impressive. Brazil, like the other BRIC countries, is a net external creditor. Increasing external assets and declining external liabilities turned the public sector and the economy as a whole into net external creditors in 2006 and 2008, respectively. In combination with the retirement of virtually all the government's domestic foreign-exchange-linked debt, this has reduced the economy's vulnerability to sudden stops and eliminated the fear of floating. Strong external fundamentals, a floating exchange rate and an inflation-targeting regime have rendered the economy very resilient to even severe future shocks.

Manageable economic and financial weaknesses persist. This year Brazil will be running its first current account deficit since 2002. But even under pessimistic projections, the current account deficits will likely be fully (or largely) financed through net equity inflows in 2008-09. A widening current account deficit should not be of concern. Inflation has been increasing and is set to overshoot the target for 2008, forcing the central bank to hike rates. Importantly, the central bank, the government and society today accept the need to maintain price stability. The decline in inflation has greatly benefited the poor and has helped President Lula secure a second term in office. It is difficult to see how Brazil's commitment to low inflation could be seriously undermined. Public sector debt remains high. Net public sector and even more so gross public sector debt remain high. While we project a decline in debt over the next few years, current primary spending dynamics are not compatible with long-term debt sustainability. But for now, sustainability is not a concern. Brazil's growth potential is relatively limited. One of the main causes has been insufficient investment. Brazilian gross domestic investment amounted to less than half (!) the level of China and India during 2005-07, so it is no surprise that Brazil grew less than half as fast as China and India over the past decade. But although growth is relatively low (it is actually high by the standards of the 1990s), this won't undermine the outlook for financial stability.

My view - [Brazil](#) has been blessed with abundant natural resources and is benefiting from the commodity bull market and should continue to do so for the foreseeable future. The challenge is to turn the commodity bonanza into a modern diversified economy rather than squander the proceeds as has been the norm for countries in this situation. Signs that Brazil is rising to the challenge are good and the stock market has been one of the best performers internationally over the last 5 years.

A consistent progression of rising major reaction lows is evident over this timeframe. Each consolidation is above the last on a closing basis. The last consolidation was longer than any seen since late 2006. The upside can probably be given the benefit of the doubt, in the medium-term, provided the Index does not sustain a move below 55,000.

In the short-term, the Index has been one of the best relative performers over the last few months but has pulled back recently.. It needs to sustain a move to new high ground to offset potential for some lower to lateral ranging in this region.

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.

Europe continues to dominate the list when sorted, in ascending order, by P.E. [Switzerland](#) is the exception, it is towards the lower side of that list. This is in part due to the fact that companies such as [Clariant](#) and [Syngenta](#) are priced for growth and on average have contributed more to higher P/E than valuations in the banking sector.

When sorted in descending order by dividend yield, two REIT indices are towards the top of the list. The [Bloomberg REIT Index](#) and [TSE REIT Index](#) are both yielding more than most other indices. The Bloomberg REIT Index, composed of US listed REITS has a yield of 5.34% versus 2.23% for the S&P500 and is performing in line with that index.

(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.)

Email of the day - on P&C Global Gold & Natural Resources Fund:

"At your earliest convenience, please review the following:
[P&C Global Gold & Natural Resources Fund \(CY\)](#)

"When I try to retrieve charts related to this fund, I receive the following: ID not found: 50638."

My comment - Thank you for alerting us to this omission. On further investigation the fund is no longer quoted by Bloomberg and was deleted from our database as part of a routine sweep of inactive securities. However, as you know, the fund is still active. Roughly the same time as your email, the fund contacted us and sent all of the back history as well as the most recent prices. These have now been uploaded to the Chart Library.

Eoin's personal portfolio: HSI long stopped out at a loss - [The stop on my](#)

Hang Seng long was hit this afternoon at 23945 against my purchase on March 29th at 24,447 including spread-bet dealing costs.

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