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

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

Monday 16th June 2008

Anatole Kaletsky: Oil is too important to leave to market forces - This is another interesting and controversial article by The Times columnist, on a topical subject. Here is the opening:

Towards the end of last year, as financial panic about the global credit crunch reached its climax, I wrote that a taxpayer-backed "plan B" would soon be needed to the save the world banking system. If financial markets failed to clear up the sub-prime mortgage mess by the end of the first quarter, the consequences would be so horrific that governments would have no choice but to step in.

This government-backed plan B was implemented in late February and early March with the rescue of Bear Stearns and the nationalisation of Northern Rock. As a result, the credit crunch is no longer a big threat to the world financial system, even though it's painful impact on the British and European economies has only just started.

As the banking crisis has eased, however, a far greater danger has emerged to global prosperity: the price of oil. It looks increasingly as if this is another challenge that cannot simply be left to market forces. So is it time for a government-led plan B to curb the price of oil? I believe it is - and there are growing indications that world political leaders are starting to think along these lines.

The present oil boom looks reminiscent of the housing bubble, the dot-com bubble, the Japanese share bubble and all the financial bubbles before that. It started with a genuine and important structural shift in the world economy - the growth of China and the decline in non-Opec oil production - but financial markets have magnified this beyond all reasonable bounds.

But another more important aspect of the oil boom is now attracting political attention: An oil price above $100 a barrel is an enormous danger to the world economy. It threatens to reignite global inflation, wreck development plans in China and other emerging countries and magnifies geopolitical risks by redistributing some 7 per cent of global GDP, roughly $4 trillion per annum, from the stable societies of America, Europe and developing Asia to potentially hostile regimes. These regimes then leak this money to Wahhabi fundamentalist madrassas, communist insurgencies in South America and mafia activities from former Soviet states.

As politicians and voters start to grasp this, pressure is mounting for something to be done. As a result, a series of energy-related summits has recently been announced, starting with an emergency meeting of oil producers and consumers in Saudi Arabia and culminating in the G8 leaders' summit in Japan in July. What, then, might a Plan B to reduce oil prices consist of? And could it possibly work?

My view - Anatole Kaletsky has made another useful contribution to the debate.

(*See also my detailed comments on this subject posted on 5th June*.)

Email of the day (1) - On the big industrial miners:

"An article in Bloomberg calls attention to the grab for minerals on the bourses of the world. Are you tempted to handicap that race? Do Freeport McMoRan, Lonmin, Alcoa, or Teck-Cominco appeal as takeover plays? Are you still pining for Xstrata, especially now that Vale failed to purchase them?

"With several analysts (Marc Faber, James Montier, etc) coming out with bearish commentary on base metals companies, are you again looking for a place to leverage up again, or holding on for the eventual recovery?"

My comment - Thanks for your timely questions and the interesting article. Taking your second paragraph first, we should welcome bearish commentary from notable analysts because it helps to prevent a serious bubble from developing in this sector.

Regarding your invitation to handicap the takeover race, I'll point out that you and a number of other subscribers are better informed on this subject than Eoin and I. One cannot do everything and we are top-down strategists, who rely on price charts for timing but others for the takeover stories.

We remain long-term bulls of the miners for all the reasons previously mentioned, not least pricing power, and in the interests of full disclosure, I should remind subscribers that I am overweight in this sector. Tactically, we prefer to buy the leading miners following periodic and inevitable shakeouts. Our main concern for the sector would be a global recession, possible although not probable in this environment, as that would certainly curtail demand for at least a couple of years. However a recession would most likely punctuate the resources supercycle - by slowing, delaying and perhaps lengthening it, rather than causing a lasting derailment.

I expect further mergers and SWF participation within the sector, but hope leading miners remain prudent in their deals. Although this remains a tricky overall market environment for investors, I believe many of the miners are more interesting today following some corrections. For those of us who have neither specialist skills and information in the sector, nor the time to acquire it, a diversified fund such as BlackRock World Mining Trust (BRWM LN), and also listed elsewhere) is a sensible way to participate.

My personal portfolio: Corn and oats stopped out - Given the surging price and prospect for some more favourable weather, I raised my trailing stops for corn longs this morning. As the first one was triggered, I sold a third of my position at 740¢ for the July contract, against my purchase at 660.50¢ on 6th June. My oats stop was the next to be hit. Accordingly, my July position was sold at 417¢ versus my purchase at 413.25¢ on 11th January. Lastly my main corn stop was triggered for the remaining two-thirds of my position. This was sold at 730¢ against my purchase at 628.25¢ on 5th June. Corn is due for a consolidation but I doubt that the crop damage story is over, although it may be on hold for a while, pending the possible effects of hot weather next month and in early August.

These prices include all spread-bet dealing costs.

Email of the day (2) - On bank safety:

"I revisit the basic question of bank safety. I may be posted to Switzerland soon, and may have to open an account with a Swiss bank. This bothers me as Swiss banks have been in the news lately for their write-downs.

"Your line has been that banks will recover in due course, and that there is little risk of bank failures. However, should the worst come to the worst, I would prefer to have accounts in the safest possible banks, safe in the sense that, in extremis, the govt would step in to save the bank. Would you have views on which banks might be safest:

-among the big two:
--CS and UBS
-a couple of Cantonal Banks
-private banks

"Another solution might be to go for an Asian bank - you say they are in relatively good shape - with a Swiss branch: a Taiwanese or Singapore bank? A list of what you consider to be the safest Continental European banks would be appreciated."

My comment - Congratulations - I have yet to meet anyone who did not enjoy their posting in Switzerland.

I do not believe I ever said that "there is little risk of bank failures". To clarify this point, I have often said that western banking sectors have tended to implode at least once a generation. During my 43 years in this business to date, I have seen this happen at least three times. I offer these two paragraphs from 9th November as a brief summary of my views:

Banks have always committed excesses, occasionally to the point of bankruptcy. However they are ruthlessly efficient when in survival mode. Bank overheads are being slashed and the sector will be much leaner during the recovery. Also, in a worst case scenario, which this probably isn't, governments no longer let their banking sectors go bust, although they occasionally allow a small to medium-term financial institution to fail, just to remind the industry that there are consequences.

Instead of allowing a Darwinian mass extinction within their financial sector, central banks now recapitalise them through the yield curve, at the taxpayers' expense. I do not complain about this; it is probably in the best interests of us all. Viable economies require stable banking sectors.

At Fullermoney, we are certainly not banking sector experts. However if UBS was unable to protect its depositors and allowed to go bust by Switzerland, there is probably no financial security, not even the illusionary safety of protecting one's gold bars from a machine gun turret.

In other words, for all its problems, UBS is unlikely to be more risky than leading banks in your current country of residence. But don't take my word for it, when you can let the market tell you by the relative price action, bearing in mind that banks have been favourite shorting candidates for hedge funds and the banks own prop desks.

Is this the best industrialised stock market for today's economic climate? - Oh no, I can sense some of you thinking - he is going to mention Japan. Yes, and you may recall the adage: The best investment opportunities occur when those who know it best, love it least, because they have been disappointed most.

Sure, one could easily argue that Japan is a politically ossified old people's home, destined to disappoint investors in perpetuity. This claim is not short of circumstantial evidence.

If the bears are right, Japan's stock market will soon break downwards once again. After all, on weekly charts the Nikkei and Topix bounced in March from where one might expect, looking at the earlier data, but have now rallied back to their overhanging top formations and the declining 200-day MAs.

Interestingly, however, Japan is the only developed country stock market that I am aware of where the reaction lows for major indices since March are still rising, albeit only just. Consequently the Nikkei and Topix have shown relative strength since mid-May, as we can see from these daily charts.

I have said before that Japan cannot hold out on its own, but if Wall Street and other markets are now steadying in response to an oversold condition (see also "Stock markets approaching moment of truth", posted last Thursday) then Japan is a likely upside leader. Obviously the higher reaction lows need to hold, otherwise Japan falls back into its trading range of the previous three months, as have many other indices.

Why might it maintain this relative performance? I can think of two good reasons, also mentioned in last Thursday's Audio:

1. Japan, I believe, is the most efficient user of oil, although Germany is probably a close second.

2. Japan certainly has the lowest inflation rate of any country, but it is likely to rise.

These two factors could be significant at a time when everyone is understandably concerned about high oil prices and global inflationary problems. However Japan has the world's highest savings rates, partly due to the long deflation, but the prospect of higher inflation should encourage consumer demand. Also, we often hear about Japan's demographic problems but at least that means fewer poor to feed. Japan also has the lowest interest rates and a soft currency.

For full disclosure, my largest trading longs at present are in Nikkei futures, although I am using a tight stop. I also have a fund investment in Japan, in a discontinued pension plan that I intend to transfer to my main SIPPs account.

Email of the day (3) - On Japan (from Japan):

"You have recently made some very astute observations regarding the likely reasons for the relatively good performance of Japanese stock markets. This article discusses one of them, inflation.

"I can honestly say that this is the first time in over 10 years that I have witnessed real price rises in Japan, although prices of most goods and services have yet to increase."

My comment - Thanks for your insights and an informative article. When I visited Japan in 1987, 1988 and 1989, Japanese consumers were among the biggest spenders on the planet. We know what followed, and now the pendulum has begun to move in the direction of increased spending once again.

Email of the day (4) - On my reference to stochastics:

"I noticed on Thursday's commentary you referred to, for the first time as far as I can see to the stochastic indicator.

"I have never seen you refer to such an indicator in the time I have been a subscriber or while I was reviewing articles from the archive. Come to think on it, I have never seen you refer to a book on technical analysis either, even though there are many on the subject.

"By your not referring subscribers to certain books would indicate to me you don't find much faith in many on the subject. Do you view stochastics as good indicators for determining oversold conditions normally? Is this something you apply to all markets when looking for an over sold condition?

"On a different point, I notice you don't indicate how you decide on the exact point of entry for your trades, such as; a crossover of two moving averages etc... Do you use a specific type of indicator for entry points or just support and resistance 'eyed' from the chart directly?

"By the way: Looking forward to the chart seminar in November and having 40 years of knowledge distilled down into 2 days. Soon your knowledge will be my knowledge.

"The feeling on enlightenment awaits."

My comment - Using the Fullermoney Archives Search just now, I found 13 entries under "stochastics" over the last three years, and 4 under "stochastic". There is also a stochastic feature in the customisable Chart Library, as you know.

Veteran subscribers, particularly those who remember the Commodities chart book that we produced from the early 1970s until online graphics had completely taken over, contained 'Overbought / Oversold' indicators. In the accompanying notes I described an oversold reading in an uptrend as a potential entry point; an over bought reading as a caution, and vice versa in an overall downtrend. These indicators preceded stochastics, but were very similar, also being momentum indicators.

Momentum in its various forms, not least acceleration, has always been very important to me, as it was for Eoin when he made presentations on technical analysis at Bloomberg, before joining Fullermoney. However I do not need to have a squiggly line on the bottom of my charts, particularly as it scrunches down price data, to remind me that a move may have run temporarily ahead of its sustainable trend potential.

There are some good points in any book on charting but it took me several years in the 1970s to unlearn the more mechanised, pattern identification aspects of TA which I had read about in the 1960s. I found these variously simplistic, or over-elaborate, often arbitrary or theoretical, so you will not be surprised to hear that I do not have a mechanical system for point of entry on trades. However entry and exit points are certainly discussed at TCS.

The Chart Seminar evolved from the work of Bill Jiler, Edwards & Magee, and Alexander Whelan, into what I have called Behavioural Technical Analysis for over 30 years. This is a study of crowd psychology, monitored with chart facts rather than theories. Our two-day workshop will continue to develop, now with Eoin's guidance.

I am delighted to hear that you will be attending TCS in November, which I hope you find both liberating and empowering. I look forward to meeting you and other delegates at the reception following the second day. Anyone else potentially interested in TCS may wish to see the Delegate Testimonials from Eoin's seminar last month.

Additional Commentary by Eoin Treacy

Mining & Steel blockbuster - Thanks to a subscriber who thoughtfully forwarded this heavyweight UBS 228-page report by the Global Mining Team and Global Steel Team, containing just about everything one could wish to know about the mining and steel industries. I have only read a portion of it but will set aside time to read it in full. Here is a section:

Cost structures also have a major impact on prices and supply. In times of stable supply and demand it is the marginal cost of production that ultimately determines long-term prices. Costs in recent years have been seriously affected by (1) rising structural costs of energy, freight and materials, and (2) local infrastructure costs. The relative production costs are also affected by exchange rates of the major commodity producers (Brazil, Australia, Canada and South Africa plotted below) as measured against the US dollar; in most cases there has been substantial appreciation against the US dollar with the exception of the South African currency.

Oil, freight and steel prices have been significantly upwardly volatile since 2003, and we believe are underpinning systemic cost rises that are expected to be felt in commodity production costs in the coming years. These higher costs will likely be felt both in much higher capital costs and higher operating costs. The higher capital costs and the interrelationship with underlying prices, such as steel and oil, are illustrated in Chart 32 below. The experience of the 1970s, when systemic costs of oil and steel rose, suggests that the process costs, such as construction, rise over time in response to these rising input costs. We expect the steel price of 2007-08, driven by an explosion in raw materials costs, will lift the overall capex cost index (CE Index), but is likely to have more leverage on materials-intensive subcomponents, such as structural support, as shown below.

We expect 25-30% inflation in structural supports in 2008, while the overall index is expected to advance 15-18%. These inflation factors have been worked into the individual cost estimates below.

The cost structures of specific metals, bulks and steel are illustrated below. These charts highlight the differentiating costs in producing these materials; in aluminium, alumina and anodes make up over 50% of the total cash costs. Electrical power composes nearly 30% of the cash costs in aluminium on average.

Given the widespread nature of regional power costs in some regions such as China, power comprises nearly 40% of total aluminium cash costs. The copper cost structure shown above highlights the processing components of costs from mining, milling and treatment and refining costs in refining copper from concentrates. The chart also illustrates that gold, silver, molybdenum, cobalt and other metals provide additional revenue or credits. To calculate net cash operating costs these credits are deducted from the cash, leading to a condition that some mines have negative net cash costs for copper. Credit deductions are also a factor in other metals' processing, such as nickel, zinc and lead.

The cash cost structure of thermal coal since 2002 shows a broad rise in most cost components; there has been an effective doubling in nominal terms since 2002 because of higher labour, fuel and exchange rate appreciation in key producing countries.

My view - Great bull markets become self-feeding. This is as much the case with the commodity secular bull as it was with the technology bull before it, albeit underpinned by a far more profitable business plan. The advent of China to the resources markets has been the main demand driver for this bull and it is now being supplemented by rising demand across a whole range of developed and developing markets. Supply has risen over the last eight-years, although there is still a preference to 'buy rather than build', which does not help to increase global production. However, input prices have also risen considerably and these have raised the marginal cost of production.

This marginal cost of production is the main fundamental bears cite to argue that prices will return to a historical mean. However, if prices stay at elevated levels for long enough, then the average will rise and force a re-evaluation of long-term expectations. Mining and steel are now enormously cash generative enterprises and they represent one of the few industries with a large degree of pricing power. The downside is that costs are rising for everything from tyres to labour and the sectors supplying these necessary inputs suffer from some of the same Supply Inelasticities that are helping to drive the bull market in mining and steel products.

It will take a significant amount of time before the bottlenecks in the commodities sector are worked out, making the probability of a long-term bull market more compelling.

CIMB Asean View - Thanks to a subscriber for this interesting report by Hoon Chew covering a number of markets but with a focus on the impact of commodities. Here is a section:

Lopsided impact of commodities Delving a little deeper into the performances of companies in the last three years in terms of P/E multiple expansions, we find again that it is the Indonesian equity market that is indeed driven upwards mainly by commodities. Out of the top 20 stocks that have re-rated the most in Indonesia, nine of them are commodity plays. In Singapore and Thailand, out of the top 20 stocks that have re-rated the most in the past 3 years, three are from the commodities sector. Malaysia is less impressive and seems to have had less of a re-rating from commodities - only one out of top 20 stocks that have re-rated the most is from the commodities sector (Asiatic).

What is interesting to note is at the same time, one would have expected to see transportation stocks and utilities (both of which are notoriously sensitive to fuel costs when it comes to earnings) to be found in the stocks that have de-rated the most. This was not the case. Hence it seems that investors have generally been more receptive to re-rate commodity stocks upwards, but less inclined to aggressively de-rate stocks that get hurt the most from commodity price rises. This was presumably a function of the buoyant equities markets at the time. With a more pessimistic outlook now for equities, the P/E derating for commodity stocks would likely be more than any P/E re-rating for gainers should commodity prices turn.

My view - Indonesia remains in an overall uptrend but the most recent reaction has been larger and lasted longer than any since the onset of the bull market in 2003. The Index peaked in January following a Type-2 top formation, as taught at The Chart Seminar, and posted a large weekly key reversal in the process. It found support in April near 2200 but needs to hold above that level for the trend to remain consistent. A sustained move above 2500 is needed to indicate that the bulls are regaining the upper hand.

Bumi Resources, the share with the largest weighting in the JCI and a coal producer, has recently broken upwards to new high ground and is currently consolidating the gain. A sustained move below 700 would be needed to question upward potential.

Eoin's personal portfolio: corn and soybeans stopped out at profits - corn is clearly accelerating and I tightened my stop this morning. It was hit soon after the open this afternoon at 740¢ against my purchase at 715.5¢ on June 12th. I also raised my soybeans stop as the bean had rallied to test its March highs. It was hit this afternoon at 1565¢ against my purchase on June 12th at 1538¢. I continue to hold my other commodity long in Liffe Cocoa.

Email of the day - on water:

"Hope you are both well and thanks for the seminar, still, amongst other things, trying to document and sort out a structure based on my learnings and notes and I am sure I will get there soon.

"Anyway, something hit my radar today and its not the first time but this time I felt I would share it hoping you may share an opinion with the collective.

"In terms of London tradable instruments, iShares S&P Global Water and Lyxor ETF World Water (not in the chart library as far as I can see) have popped up on my radar for 12 week highs. It seems at present Water is not being talked about much although it is having some coverage. I wonder, has the sector been "least loved" in the past, is this a potential Stage 1? Seems to me that the fundamentals seem to stack up more so than any commodity, based on the fact they will all continue to need more water. Like the Black gold madness of recent times, what potential do you see for water to be the new "clear gold"?

"P.s. Luton airport believes your Fullermoney umbrella to be an offensive weapon - Can't believe it, don't believe it!"

My comment - My apologies for getting to your email a couple of weeks late and thank you for these interesting suggestions which can both now be found in the Chart Library. And sorry to hear about the umbrella, I had thought we were past that sort of nonsense by now.

Water was an overhyped investment theme a couple of years ago and many funds have been consolidating for the last 18 months. There is currently a wide divergence between those that are heavily weighted by water utilities and those that focus on water technology. However, there are a couple which are heavily weighted to the latter and are now starting to break upwards:

Powershares Global Water Resources ETF is testing it highs near 23 and would need to sustain a move below 22 to offset scope for an upward break. The Palisades Water Index, which it purports to track, has already broken upwards and would need to sustain a move back below 2000 to question upward potential.

The First Trust ISE Water Index Fund has also recently broken upwards and would need to sustain a move below 23 to question upward potential.

Hedgeweek.com: Imarex launches BDI Index Futures contract - Thanks to a subscriber for this interesting article covering the introduction of a new futures market covering shipping rates. Here is a section:

By trading the BDI Index Futures contract, stock portfolio managers can protect the value of the shipping equities portfolio from upside and downside price risk of the broader dry bulk market.

A shareholder in several listed dry bulk shipping companies can sell the contract short, profiting from a falling BDI, to protect the value of his portfolio against a fall in freight rates that would drag down the value of his shares.

'The BDI itself is a retrospective index published once a day and reflecting market movements in the previous 24 hours,' Michelet says. 'It is not a gauge of what might happen next - basically, you cannot trade the BDI itself. We have launched the BDI Index Futures to do to the BDI what S&P 500 futures do to the S&P 500 - make it tradable.'

The contract fills a void left by the Biffex, a London-based freight futures contracts with settlement based on the Baltic Freight Index which closed down in 2001, before the current shipping boom.

'The renewed interest in a similar product to the Biffex which is suitable to all manner of different shipping investors has grown from a whisper a few years ago to a roar in 2008,'

Michelet says. 'We believe that the time is fully ripe for the reintroduction of a simple, electronically traded futures contract for dry bulk shipping.'

My view - This is a useful new addition to the suite of instruments allowing investors to take a view on the commodity sector and is to be welcomed. The contracts have only been in existence for a couple of days, so I will wait a few weeks before adding them to the Chart Library.

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

"Could you please add First State Global Listed Infrastructure Fund to the Chart Library? Many thanks."

My comment - Thank you for this suggestion, which has now been added.

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

"The following TSE index is missing from the chart library:

"TOPIX Iron & Steel.

"Can you add it?

"Also will you be adding the TOPIX-17 Series indexes?"

My comment - Thank you for pointing out this omission, which has now been added. I had not heard of the TPX17 but I will add these sectors tomorrow.

Last week's signups for the Free (Abbreviated) Comment of the Day - For the week of June 8th new signups, including subscribers and pre-subscribers, live in the following countries or regions: Canada, Czech Republic, Iceland, Ireland, Japan, Netherland, Nigeria, Singapore, Switzerland, the UK and USA - 11 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 Ireland.

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 17th June 2008

Fidelity's Anthony Bolton speaks out - My thanks to a subscriber for this informative article by Anthony Bolton, justifiably a household name in the UK for his exceptional performance at Fidelity over many years. I also know that he is a charming Renaissance man, particularly fond of music, which he also composes. Anthony Bolton's article is published by Hargreaves Lansdown and here is the introduction:

My views have received quite a bit of press coverage recently and unfortunately, as is often the case, what I said and what has appeared in the newspapers is not quite the same thing. Therefore I am pleased to have this opportunity to express my views more fully, explaining where I think the risks and opportunities lie over the next year or so. These are my personal views and not Fidelity's. Please also bear in mind that giving market views is not a science: commentators who are right more than 60% of the time are very rare.

First, let's put my views in context. I have only had a strong view on the future direction of UK market a few times in my four-decade investment career; right now, I don't have a particularly strong view. Second, my views are as much a reflection of sentiment and behavioural factors as they are economic trends. Others are far more qualified than I to make economic forecasts.

From a sentiment perspective, the March low in most Western markets was a good low. Corporate events such as the rescue of Bear Stearns often mark low points in markets. The strong negative sentiment prevalent at that time was enough to make me bullish at least for the short term. Even today sentiment remains quite negative, which is a helpful contrary indicator. For example, hedge fund net exposure to markets remains at a level that is still very low from an historical perspective. In addition, insider buying in the UK - directors' purchase of their own stock - is strong relative to historical levels adjusted for tax based sales.

My view - For timing, you can see that Anthony Bolton is a behaviourist, at least in his earlier comments.

As a leading member of the investment community, he is no cheerleader, so we can be somewhat reassured by his calm assessment of the overall outlook and also his interest in the banks. However Bolton is also quite cautious; not only does he not expect a quick recovery in the market, he also thinks we will see new lows for at least the US (I assume he means the S&P 500 and FTSE 100).

This is certainly a risk, evident by the deterioration in technical patterns for so many indices since mid-May, not to mention the inflationary concerns. However I am surprised to see that Bolton is optimistic about the next few months, but looks for the actual low "to come late this year or early next."

Anything is possible, of course, but if we are to see new lows, I would have thought they were more likely to occur sooner rather than later, in line with the seasonal pattern of weaker performance which can extend into October. Thereafter, stock market performance has usually been robust at yearend and in the first quarter of the next year.

(*See also last Thursday's feature on stock markets*.)

Email of the day - On short selling abuses:

"I am an attorney that has been following the developments surrounding counterfeit shares and "naked" short selling; which is short selling that takes place without actually borrowing shares and/or not intending to deliver borrowed shares. I believe you will be hearing a lot more about the abuses of short selling, especially "naked" short selling, in the near future.

"As exemplified by the lawsuits filed by Taser and Overstock, these abuses are becoming more widely recognized. Unfortunately, I am afraid that the abuses are so pervasive, that they are impacting the integrity of the markets, especially for smaller companies trading in the USA and Canada.

"I applaud any regulation in this area, since regulation is severely lacking regarding short selling abuses."

My view - Thanks for an interesting email on a controversial topic.

I maintain that there is nothing wrong with the concept of short selling *per se*, but I agree that it has been abused, not least because of the feckless policies of some regulators including the SEC. "Covered" shorts, meaning that the short seller was also long the stock, are a valid means of hedging a portion of one's portfolio.

When I took the NYSE exams in 1968, one could not have an uncovered short without borrowing the stock. There was also the Uptick Rule introduced in 1938, as a consequence of the Crash of 1929, to prevent pyramid selling which causes panics. Unfortunately, large traders, including prop desks, persuaded the SEC to water down or actually remove its sensible regulations on short selling.

I gather there were few protests from the exchanges themselves, which sided with their more active customers, in the interests of greater turnover revenue. Unfortunately, this made the stock exchange more of a casino than it was previously. I disagreed with the SEC's removal of the Uptick Rule just over a year ago, and also posted their flimsy explanation. I was pleased to see that Michael Lewitt of Hegemony Capital Management agreed in his superb seminal paper: "What's wrong with Wall Street and how to fix it", posted on Fullermoney in April.

Meanwhile the short-selling abuses have continued, and not just in the USA. For instance, prop desks sell a sector such as banks or building companies short. The colleagues in the same firms will advise their big clients to do the same. Then the firm will produce a sell recommendation which is of course flashed to the press. This is an amoral industry.

Apologists say *caveat emptor* and argue that it is no more than the process of robust capitalism creating efficient markets. They add that it is no worse than momentum buying. This is risible. Their cowboy activities intentionally create panics, and can seriously damage firms by jeopardising rights issues and credit ratings.

I believe we have seen record levels of short selling in the USA and UK this year. I doubt that this is mostly hedging and suspect it is exacerbating an already difficult economic situation by sowing exaggerated fears of doom and gloom.

Following the credit derivatives debacle, people understandably wonder what the investment banks will turn to for their next business model. We will find out but I suspect it will include more long-short prop trading. Fair enough, but I would like to see closer monitoring by regulators and a reintroduction of the Uptick Rule in the USA, and its adoption by regulators elsewhere.

Richard Russell on inflation - This is a gem:

Russell comment -- Without the discipline of gold, no monetary authority or political master has the courage or the backing to maintain a constant value of money.

When asked about gold, Alan Greenspan (then Fed chief) answered that the Fed "acts" just as if gold is still the discipline behind the dollar. Nonsense, this is the great lie, and Greenspan knows it. When confronted with a contracting economy or rising unemployment, central banks always fight such conditions by lowering rates and expanding the money supply or at least making money "easier." Thus, the purchasing power of the dollar sinks ever-lower, if erratically.

Of course, the current prices of a car or a bushel of corn or wheat can provide guidelines on whether inflation is heating up or not at the moment. But gold has one particular quality. It's a store of value. Try storing a bushel of wheat over the years or sitting for years with a TV set or a Prius car. No, only gold serves as both a unit of exchange and as an eternal store of value.

And this is one main reason why central banks hate gold. I've often noted that there is one thing that every central bank will avoid like the plague -- that is to compare the purchasing power of their fiat currency over a period of years. The Fed may talk about current inflation -- but as for a history of the purchasing power of the dollar, they'll avoid that at all costs.

The price of one ounce of gold was 20.67 dollars when I was a boy. The price of an ounce of gold is now around 880. The one-ounce gold coin that was around in 1930 is just as good and as beautiful and as untarnished today as it was back in 1930. Not so a bushel of wheat or a 1930 Ford car.

My comment - The author of Dow Theory Letters is at his anecdotic best in this item.

My personal portfolio: CAD/USD long trade reopened - Although the USD is ranging generally, I suspect it is slightly overbought and unlikely to break decisively up out of the majority of its cross-rate patterns, as many suggest.

Consequently I bought CAD/USD today, by purchasing the CAD's September future, for which I paid US$0.9798.

Please note - Unavoidably, I have been away from the office for most of the day so my contribution to this copy is less than usual.

Additional Commentary by Eoin Treacy

Mineweb.com: Potash to extend bull market - Thanks to a subscriber for this interesting article by Barry Sergeant covering the continued bull market in potash and related companies. The article contains a comprehensive list of potash companies which may be of interest to subscribers. Here is a section:

o The next five years will be the greatest growth period in PotashCorp's history.

o Primary driver of higher grain prices is food demand and not biofuels. Only 5% of total grain production goes into biofuels and the remainder is for food demand. People understand the supply side of food but have difficulty with the demand side.

o Commodity index funds have also been blamed for higher grain prices but this explanation doesn't make sense because there's been no physical hoarding or ownership of grain by such funds.

o Crop yield growth has declined by half since the 1970s. One contributor has been a reduction in government-funded agricultural research.

o Capacity to improve food production and meet growing demand exists but there are no overnight solutions.

o Only 19% of food production costs are on farm costs (i.e., fertilizer, seed, etc.) and 81% are off farm costs (i.e., transportation, packaging, marketing, etc.)

o Potash prices have not peaked. PotashCorp is not seeing demand destruction at current fertilizer price levels. There is a significant payback from applying fertilizers. Corn offers the lowest return but it's still a $3 return for every dollar spent on fertilizer (6 for 1 for wheat in India and 7 for 1 for palm oil in Indonesia and Malaysia). Expect potash demand from Brazil, China and India to double over the next 15 to 20 years.

o Significant barriers to entry still exist to bring new greenfield potash mines into service. While there are no restrictions to joining Canpotex for producers with proven capacity, the actual cost of a conventional mine project could increase from $2.5 billion to $4-$5 billion when infrastructure is factored into the equation.

My view - Potash remains in a vertical trajectory as viewed on this p&f chart. This is very similar to the path uranium followed in 2007. In uranium's case, the chart was easy to analyse, because it was so remarkably consistent. The first down tick was a major inconsistency and preceded the onset of a medium-term correction. Uranium shares, which had soared, also turned down when the price of the commodity began to retraced part of its gain.

Potash and uranium are very different commodities but they are both illiquid markets, where access is almost exclusively through equities. The first down tick on the potash price could also signal a correction in potash related equities.

Potash Corp remains in a consistent, although accelerating uptrend. A sustained move below C$185 would be needed to offset scope for further upside.

Mosaic remains in a consistent step-sequence uptrend; where each reaction is one above another. A break of the rising lows would be needed to question upside potential.

Uralkali continues to accelerate at a rate which is unsustainable beyond the short term. The first clear downward dynamic, which is not immediately offset, will be a clear indication that the share is entering a medium-term consolidation of its gains.

Agrium is also accelerating and a clear downward dynamic would be needed to question potential for some further upside.

K+S continues to accelerate in a fashion which is unsustainable beyond the short term. The first clear downward dynamic which is clearly larger than any previous reaction and is not immediately offset will be a signal that the share is about to enter a medium-term consolidation.

Israel Chemicals remains in a consistent, although steep uptrend, and would need to sustain a move below 6500 to question potential for some further upside.

Most of these shares are clearly accelerating as investors continue to gravitate towards the agricultural sector. However, as with the uranium sector before it, the potash price is worth keeping an eye on for signals that it may be topping out because it could be a lead indicator. For those who are long of this sector, the use of trailing stops is advisable.

The Times: Two sliding sectors do not a recession make - Thanks to a subscriber for this interesting and well argued piece by Anatole Kaletsky where he takes an overtly sanguine attitude towards the prospects for the US economy. Here is a section:

To be sure, housing and finance, two important parts of the economy, are in serious trouble. Yet housing now accounts for only 3.5 per cent of GDP, down from a peak of 6.5 per cent two years ago, so most of the pain has already been felt there (in contrast to the situation in Britain and Europe). The financial sector is bigger, employing 5.9 per cent of American workers, but only a small proportion of these are employed in cyclically sensitive jobs related to mortgages or wholesale finance. These two sectors between them employ far fewer people than the manufacturing and tradeable service industries that are benefiting from the cheap dollar. And thus far the troubles in US banking and construction have been almost exactly offset by gains in America's booming international trade.

There is a world of difference between a dislocation confined to only one or two parts of the economy, such as housing and finance, and a generalised economic decline. Remember the official definition of recession devised by the NBER: "A recession is a significant decline in activity spread across the economy, lasting more than a few months, visible in industrial production, employment, real income and wholesale-retail trade. A recession influences the economy broadly and is not confined to one sector."

The difference between a general recession and a sectoral slowdown is not just a semantic quibble. For businesses and workers, a slowdown is a period of weak growth, modest job losses and disappointing profits; a recession is marked by mass unemployment and widespread bankruptcies. For the financial markets, the two have totally opposite implications. In a recession, share prices collapse and the only safe assets are government bonds; in a slowdown, there are big shifts in relative performance between stock market sectors, but equities generally do well (as they did in the late 1990s and late 1980s) while safety-first bond investors suffer enormous losses, as they did in 1994-95 and 1986-87.

What, then, is the evidence of America moving into recession? Looking at the statistics used by the NBER, there is little or none - at least so far. GDP has continued to grow, albeit slowly, in the past two quarters and almost certainly will accelerate in the current quarter because of booming exports; industrial production has been positive, as have real income and whole-retail trade. Employment has fallen slightly, but by nowhere near as much as in the mildest of past recessions. Reliable high-frequency indicators, such as the monthly purchasing managers' surveys, point to continuation of modest growth.
Most importantly, consumer spending has remained robust.

My view - I am in general agreement with this article and the two-speed US economy has been a recurring theme in Comment of the Day and the Subscriber's Audio since at least April 18th.

Part of the reason for the remarkable bearishness evident among investors is because the financial sector is where the trouble started and remains focused. Many commentators are either experiencing the worst affects of the credit crisis themselves or are talking their short book. This cacophony of apocalyptic sentiment overshadows some of the positives which are helping to make sure the broader US economy does not enter recession.

Multinational firms whose international operations shield their bottom lines from the slowdown in the US domestic economy are doing extremely well in this environment. The weaker Dollar has also been a bonus for any company consolidating foreign earnings in the greenback. Technology companies which led on the upside before the current correction remain outperformers as do best-value consumer related companies such as Wal-Mart.

It is one thing to assume that the US economy will avoid recession and quite another to assume the stock market will recover quickly. However, even with that proviso 66 of the 147 S&P sector are in positive territory year-to-date while the Index is down 7.39%.

The Index found support near 1250 in January and March and rallied to test the lower side of the overhead top formation by mid-May. It has since retraced part of that move but would need to sustain a move below 1250 to question potential for some further moderately higher to lateral ranging in the coming months.

John Mauldin's Outside the Box: The Road to Revulsion - This article by James Montier contains an interesting timeline of comments surrounding the 1929 crash, which originally appeared in Marc Faber's Gloom, Doom & Boom letter. Montier contrasts today's housing bust with that of Japan. The article appears in accordance with Fullermoney's long standing policy of also posting views with which we do may agree, in the interests of objectivity. Here is a section:

The comments made every time the market rallies are characterised by the ever-present optimism that we have discussed many times. I suspect that is exactly what we are witnessing currently.

The first wave of concerns created by the bursting the housing/credit bubble (and make no mistake they are two sides of the same coin) is subsiding. The optimists believe (or at least hope) that the worst is now over. Indeed the probability of a recession in 2008 has dropped to 39% on the Intrade contract!

However, from our perspective such sanguinity is likely to be misplaced. The slowdown in the US is barely starting. The charts below show that both the demand and supply for credit are evaporating. This effective shutdown of both sides of the market should be a serious concern for monetary policy makers, as it is one of the hallmarks of a liquidity trap situation.

Note in particular how widespread the lack of demand for credit is, as well as the supply! This isn't just about the housing market. Obviously demand for mortgages (both commercial and residential) is lacking, but so is the demand for consumer credit, and corporate credit. This doesn't bode well for the outlook.

The underlying asset development is likely to have much further to run as well. The chart below shows the developments in US house prices and Japanese land prices during their bubble and burst. The point of this chart isn't to say that US prices will follow Japanese prices, but rather to illustrate the long drawn out nature of the healing that has to occur. Indeed, one client recently asked me if this was worse than the S&L crisis. To my mind it is much worse, as securitisation was part of the solution to the S&L problems, whereas it has been part of the problem in the build-up in this bubble.

My view - We have a lot to learn as individuals about how the crowd reacts when a major investment mania bursts, so the 1929 timeline contained in this article is very educative. However, just because the 1929 crash led to a depression does not mean the current US economy is gong to enter one. Call me naïve but I believe central bankers have learnt something in the last 80 years.

The probability of a long convalescence for financials and real estate related shares remains high, but that does not mean the rest of the economy has to be in deep recession. As argued in my commentary on the Kaletsky piece above, a number of other sectors are outperforming. The global economy, which is a far greater consideration now than it was 80 years ago, is also still relatively healthy.

Eoin's personal portfolio: cocoa long stopped out at a profit - My long in July Liffe Cocoa, purchased on June 4th at 1539p was stopped out this morning at 1615p including spread-bet dealing costs. The commodity has been up on consecutive days and I felt the risk of larger reaction within the overall trend may be in the offing, so I raised my stop.

Today's interesting charts - The Chart Library contains sector indices for a wide range of international markets which may be of interest to subscribers.

UK (FTSE 350 Banks) - rallying from support near 6500 and would need to sustain a move below that level to question potential for some further upside.

Ireland - remains in an overall downtrend which has lost significant downward momentum. However the Index needs to break the progression of lower highs to indicate that the bulls are regaining the upper hand.

India (Nifty) - finds support at the January and March lows and would need to sustain a move below 4400 to question scope for some further upside.

Live Cattle - breaks upwards to new high ground and would need to sustain a move below $97 to question further upside potential.

Cotton - rallied impressively over the last couple of weeks but is looking temporarily overextended. However a sustained move below 75¢ would be needed to question medium-term potential for some further upside.

White Sugar - rallying impressively from support near $320 and would need to sustain a move below $340 to question scope for some further upside.

Email of the day - on how to take a contrarian view on the US real estate market and the Dollar:

"Could your subscribers recommend any interesting fund or public company for a foreign investor prepared to take a contrarian view on the US real estate market and the American currency?

"I would greatly appreciate their suggestions and comments.

"By the way, I've noticed that the Chart Library covers a relatively small number of RE related funds. Or is it just my limited experience in searching through it?

"Many thanks for your great work!"

My comment - Thank you for this interesting question which I'm sure subscribers will be able to answer better than I can. The list of Real Estate related instruments currently available in the Chart Library is a result of additions made following suggestions by subscribers.

Wednesday 18th June 2008

RBS stock market alert: Fund managers react - The RBS report, which I have not seen in full, has generated controversy today, as you will see from the response in this article from The Telegraph. Here is the opening:

Fund managers have reacted strongly to the forecast by the Royal Bank of Scotland of stock market crash and warn investors not to act in haste and panic.

The Royal Bank of Scotland has advised clients to brace for a full-fledged crash in global stock and credit markets over the next three months as inflation paralyses the major central banks.

"If you strip out anything stocks related to oil, energy and mining in the FTSE you will see that the market is already down by 30 per cent over the past year. We are in a bear market which has been masked by the performance of those sectors."

Buxton points out that many UK shares closely connected to the slowing economy are down between 50 and 80 per cent over the year already and it is too late for investors who have yet to protect their portfolios. They will merely crystallise losses, he says.

My view - In the financial game, if you want to attract attention, publish an extreme forecast. It will generate the publicity sought, but often at the expense of accuracy and credibility.

Any forecast is in with a chance but I am more in agreement with the respondents quoted in the article.

Email of the day (1) - On where to invest:

"As a retired person preparing to invest capital, I seek your wise counsel, as there appear to be considerable headwinds faced by anyone starting to invest now. Whilst I prefer to remain optimistic about the future, I hope I am now wise enough (made enough mistakes) not to ignore warning signs. I note that the RBS Capital strategy team (18th June) 'expects one of the worst stock market crashes in 100 years with inflation anticipated to paralyse the markets and precipitate a crash'. A buy signal, braver souls may say; but obfuscation of financial data is creating many conflicting signals for investors. Your readers may in interested in the independent report published by John Williams entitled www.shadowstats.com which seeks to distinguish between the fact and fiction surrounding financial data. For example the official US data on unemployment is for a level of 5% whereas John Williams (JW) indicates a true level of 13%. In the case of official GDP this is 2.5% whereas JW indicates a level of minus circa 2.5%, and finally of most concern is Consumer inflation - Official 4%- JW estimates 12%+. Whilst we are not the US we are certainly the effect of their economic and political activity.

"Most of your readers are probably aware that both the Bank of England and The US Federal Reserve owned privately owned organisations (source The Creature from Jekyll Island - G Edward Griffin) whose sole purpose appears to be the endless printing of money and the management of our expectations thereon. 'Google'- 'The Grandfather Report' reveals a prodigious database detailing the extent of the potential for massive inflationary pressures faced by the United States that are the result of a fiat monetary system, which is now a world wide phenomenon.

"The lifeblood of the stock market must, to a large extent depend upon the ready supply of free capital and the current parlous state of banks both here and in the US are not supportive in this regard.

"Whilst I notice that you, David favour the stock markets of China and India where money supply figures are 17 and 21% respectively, does not this create the condition of high risk and potential volatility only suited to a longer term investor? It appears in line with the Fullermoney investment themes, investors may be forced to accept that for future protection against inflation or lack of trust in a fiat money system, the only route would appear to be to accept the more volatile option of investing in commodity based entities. Whilst it is accepted that you do not provide individual advice, my question to you David is what action could a more risk adverse investor take having regard to the above?

"Your service is most appreciated and the benefit of the 'collective' is a great credit to the thought provoking excellence which your service engenders.

"In the event that you consider this email too long please feel free to edit any part thereof should you consider it worthy of reproduction (if at all) in any form on your site."

My comment - Thank you so much for your kind words and informed, articulate assessment of the investment scene, certain to be of interest to many subscribers. I also thank you for editing it so meticulously, which means that I save time in reproducing your email.

Regarding the RBS Capital report, I think (hope) it exaggerates the risks, but I agree with your point that "obfuscation of financial data is creating many conflicting signals for investors." Also, the inflation problem is certainly a concern, although not a surprise to Fullermoney subscribers since the seeds for it, in terms of inflationary monetary policy, had been sown since 1997, as often mentioned.

I agree that there are many economic difficulties which are not supportive of stock markets. I regard today's inflationary problems, which are global, as more serious than the banking crisis which is mainly confined to the west. There is a risk that central banks, having fanned the flames of inflation with excessive monetary growth relative to GDP, will now overreact in their efforts to douse this fire.

I have often mentioned that most of the inflation was coming from resources prices and government services in many countries, not least the UK. Unfortunately but inevitably, soaring prices for food and energy are highly emotive. I maintain that the prices consumers pay for these staples will stay high, more often than not, despite sharp fluctuations in underlying commodity prices.

However, given the annualised data, if commodity prices levelled out for a year, their contribution to inflation data would be zero. Thereafter if jawboning and the economic slowdown mostly contain wages, central banks will declare at least a partial victory against inflation, albeit at the less publicised price of a lower standard of living for many people. The claim of lower inflation would probably not hold up under close scrutiny but at least central banks would be able to switch their emphasis to stimulating economic growth for a while.

Regarding investments, you mentioned China and India, which given the declines from their 2007-2008 peaks, happen to be the worst performers in my personal portfolio at present. They will always be volatile but I maintain they are the king and queen of emerging markets, best purchased following setbacks.

From the perspective of a risk-adverse investor, I would avoid any complicated financial schemes, including the structured products that some firms are promoting at the moment. On considering their fees, I think they are better priced for the vendor than the customer. Also, one needs to read the small print beneath guarantees, which I suspect are not as watertight as one would hope.

Again from a risk-averse perspective and for someone concerned about inflation and who did not wish to trade, I would have some of my money in a gold bullion fund. My second purchase would be an equity income fund or two, now that most stock markets have seen significant corrections. This area requires both experience and forensic accounting skills, and managers such as Neil Woodford of Invesco Perpetual have certainly demonstrated that they can add value in excess of their fees. Wanting some growth, but recalling the risk-adverse mandate, I would consider Asian region funds overseen by Hugh Young of Aberdeen, and Angus Tulloch of First State Investments. Since these invest mostly in emerging Asia, I would also consider a Japan fund. Lastly, I would be interested in some smaller positions spread among various resources funds, giving sector coverage, including renewable energy.

I would accumulate gradually and on weakness, while markets remain in a difficult patch. Looking well ahead, when the equity income funds next distinguish themselves by their capital appreciation, I would lighten positions in favour of the other sectors mentioned above. I would always hold some cash...just in case.

Email of the day (2) - On Anthony Bolton:

"David...In your "My View" response to Anthony Bolton's article you didn't comment on his views about commodity shares (he's a seller).

"Let me be specific...would you hold your core positions in Resource Shares if you expected a 30 %+ retracement?"

My comment - I will always take Anthony Bolton's views more seriously than those of pundits for whom a bubble is anything which they have not participated in, that has also performed.

As a veteran subscriber you will recall a number of 'commodity bubble' articles since at least 2004. Bolton is not saying that; if fact, he states that he does believe we are in a commodity supercycle. Also, he did not specify which commodity shares he was selling but I assume that he has reduced his weighting in the sector.

Fair enough, we have a global economic slowdown. Meanwhile, not all resources shares are equal. The most risky ones are where parabolic accelerations are occurring (*see Eoin's superb item on potash yesterday, including comparisons and suggested tactics*).

I did mention last month that the likes of Rio and BHP had run temporarily ahead of themselves, although these were certainly not bubble-type moves, either technically or fundamentally, in my view. In answer to your specific question: yes, I have held either in anticipation of a sharp corrections or when surprised by them, because I regard that as normal. I have also used such reactions as buying opportunities, and may do so again.

I am also prepared to ride out a dull period, which I suspect is what Anthony Bolton anticipates, as that is also normal. I too believe in the commodity supercycle and that the best is yet to come for miners. A dull period for the sector would probably not be that unwelcome for Rio and BHP, as it would give them the opportunity to make some timely takeovers.

If I appear more sanguine than some other investors, it is because I prefer to take a Warren Buffett approach with my SIPPs and ISA accounts, which are of course unleveraged. I am much more active in my trading account, which I use as an ATM. I also hold a substantial cash reserve in high-yielding currencies, which is my 'just in case' money.

My personal portfolio: Losses on industrial metal rollovers and also TFC; T-Bond short increased - I mentioned above that I use my trading account as an ATM. I should have added, most of the time. Sometimes the markets use me as an ATM, although only temporarily and only in comparatively small amounts in recent years, I am relieved to say.

The reason is improved money control discipline. This means different things to different traders, such as not averaging down and often a tight stop. I sometimes average down, if the pattern has not been compromised, because I start small relative to my capital and build positions incrementally. There are also times when I will not average down, but may hold onto a small position considerably longer than most other traders, giving it time to develop. This has worked in my favour more often than not, although certainly not with the metals mentioned below.

Additionally, I often introduce a breakeven stop relatively quickly, assuming that the position is moving in my favour. This reduces the risk of loss, albeit often at the price of profit potential. I usually find this an acceptable tradeoff, especially as it introduces an element of quality control, shaking me out of choppier positions while keeping me in those that trend strongly. Lastly and most importantly, I only build big positions behind trailing stops in trending markets, with one rare exception. This is the Baby Steps strategy which I may use more aggressively if there is solid technical and especially fundamental evidence that a market is cheap and in a Type-3 ranging base formation.

The tactics described above are appropriate for me, but to each his own. Successful traders develop their own systems to suit their temperaments and skills, although all know the importance of money control.

I previously mentioned that I had decided to roll forward my three losing metal positions in copper, nickel and zinc. The copper was particularly badly timed although I made a second and better purchase near its reaction lows. However this only made a small profit, having been stopped out during a reaction. Why did I roll the positions forward when in the global beauty contest other commodities are stronger? I think people are too bearish of industrial metals. However I also know that they will not perform until a sufficient number of other people agree with me. For that reason these remain among the smallest positions in my trading accounts.

Here are the details for yesterday's sales and rollover purchases: my June copper ETFS was sold at 4389.5 against my purchase at 4668.34 on 11th October. My nickel ETFS was sold at 3003.451 against my purchase at 4128.52 on 10th October. Lastly and worst of all, my zinc ETFS was sold at 834.0705 versus my purchase at 1446.16, also on 10th October. I simultaneously purchased September ETFS at the following prices: copper 4434.7325, nickel 3036.4116 and zinc 843.2238.

Today I introduced a breakeven stop for copper because it is near the higher side of its large range and benefited from industrial action in Peru.

My June Taiwan Greater China Fund (TFC US) expired at 675.63 last night, against my purchase at 733.3 on 5th June, and I simultaneously purchased a September position at 683.04.

Lastly, I increased my September T-Bond short by 50% today, selling at 112.84.

Prices above include all spread-bet dealing costs.

Additional Commentary by Eoin Treacy

China Has `Limited' Scope to Halt Stock-Market Plunge - This article by Darren Boey and Chen Shiyin for Bloomberg covers today's rally in Shanghai A-Shares and the potential for the market over the medium term. Here is a section:

The increase in the reserve requirement ``delivered a clear message that the Chinese government's focus remains on reigning in inflation,'' Ulrich wrote.

Shares of refiners and power producers may receive a boost should inflation slow and enable China to relax controls on fuel and energy prices to offset higher raw material costs, Ulrich said.

China Petroleum & Chemical Corp., the nation's largest refiner, and Huaneng Power International Inc., a unit of China's largest power producer by capacity, have both plunged 47 percent this year.

China's government has introduced a series of measures since the start of the year to halt the stock-market slump, including resuming approval for new mutual funds and suspending a tax on mutual fund income, Ulrich said.

The government cut the tax on equity trading on April 23 to 0.1 percent from 0.3 percent to halt the slump, two days after the Shanghai Composite Index, which tracks the larger of the two mainland markets, sank to more than 50 percent below its October record.

The move prompted a 9.3 percent surge on April 24 in the Shanghai Composite, before it fell 3 percent in the next two days.

There are ``diminishing returns to supportive measures and a danger that investors will become overly-focused on the direction of government interventions rather than investment fundamentals,'' Ulrich said in the report.

My view - Back in 2005 when the Chinese government decided to intervene in the stock market, they announced that they would defend a level and had created a fund to buy stocks. We commented on it then, as it certainly sparked our interest. In the last few months, we have seen a number of measures introduced to support markets, with intermittent effect so far. However, these measures are cumulative and have succeeded in slowing the pace of the decline. The potential remains for the government to intervene directly, and buy shares, if other measures do not succeed in their objectives.

So far, they have attained a relatively orderly unwinding of the 2007 acceleration. Today's upward dynamic, in the form of a key day reversal, from near 3000 signals that demand is returning at least in the short-term. To give a more convincing signal some follow-through on today's action is needed.

Over the medium-term, the Index needs to sustain a move above 4000 to break the progression of lower highs and indicate that the bulls have regained the upper hand. Given the speed and size of the decline, the convalescence is likely to take time; with most likely outcome being a period of support building during which investor confidence can recover.

The Maple Leaf Memo: Canada Booming while US Struggles - This article by Roger Conrad and David Dittman highlights the impressive performance of the Canadian stock market in the current environment. Here is a section:

The first two days of the current trading week, however, highlight an emerging disparity between North America's major equity markets. Canada's economy will never "decouple" from the US, but the S&P/Toronto Stock Exchange Composite Index has certainly diverged from the S&P 500.

The two broad market indicators have been moving in opposite directions in 2008, corresponding to the increasingly influential role oil is playing on investor sentiment. The S&P/TSX Composite is up nearly 9 percent year-to-date, while the S&P 500 has shed nearly 8 percent.

Late in Tuesday trading, the S&P/TSX Composite had posted a gain of 123.68 points (0.83 percent), while the S&P 500 was off 5.41 points (0.41 percent).

Earnings expectations drive the stock market, and according to a recent report from CIBC World Markets, resource stocks will push average earnings growth for Toronto Stock Exchange-listed firms to the 30 percent range during the second half of 2008. The weaker US economy--and the weight of its financial sector--will limit TSX growth to 10 percent in the second quarter, but energy and materials stocks will make an enormous difference going forward.

My view - Canada is blessed with incredible natural resources, a relatively small ,extremely well-educated population, close proximity to its largest market, a stable political environment, one of the highest standards of living in the world, a well diversified economy which although heavily weighted to the resources sector right now, also has significant clout across a number of other sectors.

Canada is not only outperforming its nearest neighbour but the majority of other global stock markets and certainly those in the developed world. The TSX plotted a very consistent orderly uptrend from the 2002 lows up to the July 2007 highs. The reaction from near 14,600 was larger than any seen though out the length of the uptrend and from a higher level. This marked the onset of a medium-term correction which bottomed in January. The retest of the January low found support significantly above 12000, broke the progression of lower highs in April and broke upwards to new highs in May this year. It has been consolidating that gain for the last month.

In terms of commonality, Canada is the best performing market of those dominated by the resources sector which have broken to new highs this year. The pattern at present remains consistent and we can give the upside the benefit of the doubt as long as it can sustain the move above 14600.

Email of the day (1) - on impact of rising fertiliser costs on farmers:

"I read the comments regarding Potash today and wanted to share a few thoughts with you. First of all, my father was a tomato farmer. Growing up on the farm I often heard him say... "Son, the farmer always gets screwed". And what he was referring to was the fact that farmers always took the risk while suppliers and brokers took the profits. Here I've watched potash prices triple over this past six months and can only say, it's happening again. Sure there is a crop shortage, but doesn't that mean less crops to fertilize? Less fertilizer needed??

"And one more thing, everyone talks about the need for lots of fertilzer to enhance the crops, but there is a funny thing about fertilizer.. Too little and you have a little less crop, but too much and you have no crop! Too much fertilizer and the whole crops dies. So I've watched with interest as the analysts have doubled and tripled earnings estimates, while the company Potash is screwing farmers with outsized price increases. But is there really lots more potash being sold? I think not.

So I watch and wait, because this is going to be fun when the bubble bursts, unless it doesn't…"

My comment - Thank you for this email which raises a number of interesting points. Farmers are facing some of the same challenges as producers of raw materials in dealing with rising input prices. The higher costs for power, fertilizer, labour, transport, machinery etc. are raising the marginal cost of production. While this is a problem for farmers, it also puts a floor under prices for their products. Given the secular nature of this move, it is unlikely we will see corn, for example, fall back below $3 anytime in the foreseeable future. If this is the case, farmers should be able to sell their produce at significantly higher prices in the coming years, than they would have received over the last decades.

This article from Mineweb.com dated April 17th covers the higher prices, China is being forced to pay for potash based fertilizers. Here is a section:

Chinese fertilizer importers agreed on Wednesday to pay more than triple what they did a year ago to get hold of tight supplies of potash, sending the shares of global fertilizer makers to record levels.

China, the world's biggest import market for the nutrient, which is used to boost crop yields, will pay $650 to $670 a tonne for product delivered to its ports, analysts estimated.

"With the intense pressure on global food production and continued growth in potash demand, this is the reality for our industry for the foreseeable future," Bill Doyle, chief executive of Canada's Potash Corp (POT.TO), the world's top producer, said in a statement.
Potash producers have found it hard to keep up with demand as farmers around the world, flush with returns from record grain prices, rush to produce more grain to feed people, livestock and the burgeoning biofuel sector.

The 2008 contract prices were higher than expected, and volumes were far below last year's levels, said Mikhail Stiskin, an analyst at Moscow-based brokerage Troika Dialog.

"China will be kept on a short leash by producers that are keen not to allow for a possible restocking," Stiskin said.

Global competition for potash and the drive to increase global yields have supported prices over the last few months. However, the CEOs of potash firms appear to becoming increasingly bullish. I understand the fundamental story behind the potash bull market, but I am also wary of increasingly bullish forecasts following an impressive acceleration.

Email of the day (2) - on potash and uranium similarities:

"Many thanks for your comparison of the vertical trajectories of potash today and uranium last year. Please flag that first downward tick on potash for us -- whenever that happens. I followed your lead on uranium and hope to do the same with potash. Needless to say, I'm ever grateful for your ongoing guidance."

My comment - History doesn't repeat itself but it does rhyme. In pointing out the similarities between the current price of potash and the 2007 performance of uranium, we can make an educated guess about what will happen when the price of the commodity starts to turn down, but there are no guarantees.

Monitoring the price charts will prove to be the best strategy for timing the end of this phenomenal medium-term move within the overall secular bull. Let's make this a collaborative effort. The potash price can be monitored in the Chart Library, and we can all watch it for that first downtick, that way, we are much less likely to miss it.

Email of the day (3) - from a new subscriber:

"Greetings to you from one of the probably more unusual of subscriber's destinations, from the North of Tanzania, East Africa.

"Let me explain this and answer your questions as briefly as I can.

"I am by education and profession a Lutheran pastor from Bavaria in Germany. (In this respect it was encouraging for me to read that you had studied philosophy, which is a related field and not something like economics ...) Since eight years, and for two more years to come, I am lecturing at a university in East Africa.

"I discovered Fullermoney 3 or 4 years ago and have read the abbreviated commentaries ever since, together with a huge amount from the archives. Although it took me until last week to subscribe (and I also booked The Chart Seminar in November 08 earlier this year), I want to state that I feel an extraordinary thankfulness for the education, which the Fullermoney website has given me over the past couple of years. I started investing for the first time in 2003, and my education and general knowledge had thus far not prepared me for this field of life; it was Fullermoney from where I benefitted most, and in a most decisive way. Having been an ignorant in finance before, I consider Fullermoney to be one of the most important discoveries of my life. It gave me what I needed on a turning point in my development, and this is remaining a work in progress.

"One aspect in all this is that I have become also interested in, as you once wrote about yourself, the intellectual challenge, which the markets provide.

"My investment time horizon is long only, I'm not a trader, but am interested in building up a pension account. For this I have a horizon of about 20 years or more. My hope is to identify generational trends (if there are new ones), and to avoid the severe global recessions. This is very much in line with what David seems to be intending. What I also hope to find, with your help, over the coming years, is the one or the other medium-term trend from which I might benefit for medium-term purposes. But this is secondary.

"My investment vehicles are, thanks to my special situation, and at least for two more years to come, limited to what my home bank in Germany is offering: a number of investment funds/trusts (fortunately partly the same as mentioned in Fullermoney). I also own an amount of physical gold as inflation hedge for the long term. In the future I expect to extend this investment universe, but for the moment this doesn't make much sense. (The power and internet cuts and shortages in Tanzania alone make short-term activity impossible, for example.)

"The markets of my greatest interest are in line with the big Fullermoney themes Asia, Resources, Inflation hedging. (I had identified these already before I discovered Fullermoney, but understood at that time less than 5 percent about them and about investing, compared to now.)"

My comment - Thank you for this informative email and welcome to the Service. I'm looking forward to meeting you at the November Chart Seminar. Living in Tanzania sounds like an adventure. Cousins of mine taught at the university in Dar es Salaam about 15-years ago and loved it.

When I was at university, I used to get strange looks when I told people I was studying philosophy. The looks only got stranger when I said I wanted to work in finance. However, I believe it has left me in good stead. The main thing I learned was to dissect arguments and that is a useful skill for a career analyst.

We all have a natural predilection to either analysis or trading / investing but few people are born with both. Personally, I find analysis much easier than trading. I often have a good sense of where a market is going, although nobody is infallible in that regard, but have to work hard trying to make money from the move. Discipline and a degree of introspection are key, when attempting to control one's emotions and manage a position. My most profitable trades usually coincide with when I successfully keep my ego in check. The opposite is also true.

The Fullermoney Collective is made up of a wide and varied group of fascinating people who have diverse life experiences. It is by sharing our collective knowledge and perspectives that we all progress in our financial education.

Email of the day (3) - on ways of taking a position on the US real estate market:

"Suggestion for possible contrarian RE play as requested yesterday:

"MacroMarkets has sought permission to launch "Up" and "Down" Macros (ETFs) tied to the S&P/Case-Shiller Composite 10 Home Price Index. These funds, when approved will provide a means to speculate upon the direction of home prices. This may appeal to foreign investors as they can speculate on US housing via the ETFs without having to own a home.

"Given that shorting without owning stock is such a contemporaneous topic I wonder if anyone would 'loan' their house to an investment bank for a short sale to benefit someone else. It would be a bit like "Hello I'm from the government and I'm here to help you....". Sorry I couldn't help being facetious.

"MacroShares Major Metro Housing Up (UMM)

"MacroShares Major Metro Housing Down (DMM)"

My comment - Thanks for this interesting email which I'm sure will be of interest to other subscribers. I will add UMM and DMM to the Chart Library if they are approved.

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.

Aluminium - rallies well and breaks the progression of lower highs from the peak near $3200. A sustained move below $3000 would be needed to question potential for at least a test of the highs

Cocoa - breaks upwards to a new highs but is looking overextended in the short term. However a downward dynamic would be needed to check momentum beyond a brief pause.

Japanese Yen per 1 Euro - The Euro is testing its highs and would need to sustain a move below 165 to question potential for an upward break.

Email of the day (4) - on a problem with the data for BRWM:

"May I ask you to have a look at BRWM in the chart library? I've had to re-enter it to my favourites, but now there is a time gap."

My comment - Thanks for pointing out this data error. I have reloaded the prices and it should be fine from here on out.

Email of the day (5) - on a name change:

"Australian nickel producer Sally Malay(SMY) has changed its name to Panoramic Resources(PAN) a few days ago.

"Can you please incorporate the change in your Chart Library?

"Many thanks."

My comment - This has now been completed.

Thursday 19th June 2008

Contrary indicator? - Stagflation fears drive investors away from equities - My thanks to colleague John Ritchie for this article from the front page of today's Financial Times, written by Rachel Morarjee:

Stagflation fears drive investors away from equities

Investors are more pessimistic about equity markets than at any time in the past decade, according to a poll of global fund managers.

The new level of bearishness comes after a lurch downwards in global shares, with the S&P 500 dropping 7 per cent from its May high, while the FTSE 100 has fallen almost 10 per cent in the same period.

Sentiment towards equities is even more negative than during the period between 2000 and 2003 when the sell-off in global stocks was much sharper.

Investors have cut their exposure to both equities and bonds and are moving into cash as fears of stagflation mount, the Merrill Lynch survey of 204 asset allocators and fund managers found.

A net 27 per cent of investors surveyed were underweight in equities relative to other asset classes, while a net 42 per cent were overweight cash, up from a net 31 per cent in May. The net figure is the balance between those respondents who favour an asset class and those who do not.

The outlook for global growth and profit expectations is deteriorating as investors brace themselves for higher inflation and subsequent higher interest rates, the survey noted. A net 81 per cent of respondents believe that consensus earnings estimates for the next 12 months are too high.

"Investors don't know where to go. They are favouring oil and commodities plays in equity markets, which shows that inflation is playing havoc with the rest of the economy," said Karen Olney, chief European equities strategist at Merrill Lynch.

Europe has borne the brunt of investors' shift away from equities, with the eurozone moving from investors' most favoured region to least favoured over the past 12 months. A net 22 per cent of investors are underweight in eurozone equities, citing the strength of the euro as a concern.

But the bearish stance towards the eurozone is dwarfed by the negative view of the UK. A net 38 per cent of respondents are underweight UK equities, the most negative stance in a decade.

The popularity gap between the booming oil industry and the embattled banking sector has reached unprecedented levels among European investors. A net 62 per cent of respondents are overweight oil and gas, while a net 62 per cent are underweight in banks.

My view - With yesterday's front page headline also reading: "Learn to live with inflation, says King" [*Ed: meaning BoE Governor Mervyn King*], and numerous pundits vying for bearish bragging rights, no wonder investors feel as if they are standing on the window ledge of an upper floor in a tall building.

But perhaps we should step back into the room, gentle reader.

It may seem counterintuitive but if we have learned two important things over our investment years, they are:

1. Cease buying and commence selling when the crowd is euphoric.

2. Buy or at least hold onto your long positions when the news is all gloom and doom.

But, David, what if it really is different this time?

It might be, but that is seldom a good bet. Meanwhile, stock markets appear at least temporarily oversold and crude oil has not extended its uptrend. Today's pessimism is not a dramatic, climactic signal such as we last saw in January and March, but it is an indication that people are becoming too pessimistic once again. The latest US Advisors Sentiment indicator from Investors Intelligence makes interesting reading, so I will post it tomorrow.

Email of the day (1) - On the Iowa flooding:

"I was sent these pictures this morning from a fund manager who runs an agriculture fund. Pictures show some of the devastation you have commented upon. You may want to share this with fellow subscribers. On another note, he told me today of one US investment bank being a seller in the market of agriculture related products on moral grounds. Looks like someone has been having a word!"

My comment - Many thanks, for the informative, albeit sobering, pictures. Unfortunately we also know that this story has been repeated beyond Iowa.

I am a great admirer of farmers, who have a demanding job and require an indomitable spirit. We could not live without them, but by the nature of their occupation they are the ultimate speculators.

Farmers plant, not knowing if the seed will germinate. If the crop emerges, the farmer does not know if it will survive the hazards of weather, disease and insects. Even if the crop thrives, the farmer's eventual harvest may be jeopardised by weather. The farmer has many upfront costs but even if successful in his harvest, he faces an uncertain market in terms of the price he will receive for his crop.

In contrast, I can secure my food, without breaking sweat, by visiting the local shop or supermarket. I can also benefit financially from the crop cycle by trading the better commodity trends via futures or other instruments. It hardly seems fair.

What about the price trend for corn futures?

It has lost upward momentum following an overstretched rally, leaving it susceptible to a pause and reaction. My guess is that we have not seen the final high, but we may have a pause in the appalling news. The point about a crisis is that when it is no longer seen to be worsening, it is at least temporarily discounted. Weather in the USA's Midwest has now improved and the floods will subside. The next period of risk will most likely occur if very hot, dry weather arrives next month. Meanwhile, a sustained break above the psychological 800¢ level is required to offset current scope for sideways to somewhat lower ranging.

Commodity investment flows: Headlights through the fog - My thanks to a subscriber for this interesting and topical report from Barclays Capital, which is a robust reply to claims that investment in tracker funds have lifted commodity prices. Here is the opening:

There has been unprecedented interest in commodity investments over the last couple of years. Investor funds have flowed into the commodities at the fastest-ever rate as the sector has moved to the top of the list of investor's favoured alternative investment exposures. At the same time, fundamentals have undergone significant structural shifts, leading to a tightening right across the sector. Growth in the consumption of raw materials in developing economies (primarily China with an additional impact from India, Latin America and the Middle East) has created relentless demand for commodities across all sectors. In many cases, consumption increases have already been dramatic. At the same time, commodity producers, with no incentive to improve production capabilities during two decades of weak commodity prices, are ill-equipped to meet increased demand expectations. Supply is further hampered by reserve depletion, shortages of key inputs plus political obstacles. As a result, the price of many commodities has surged to all-time highs this year. The commodities price boom has stoked the debate about whether speculative inflows have had an instrumental part to play. Many commentators pin the push higher in commodity prices on a "tidal wave" of assets pouring into commodity-linked indices and products. Indeed, given the nature of recent press coverage, the casual observer might be forgiven for thinking that commodity prices are all being swept higher on an irresistible tide of speculative buying that is pushing prices ever farther away from fundamental values. There are widespread claims of the billions of dollars of investment money that are flowing into commodities and the distortions this buying is creating in prices. A rational investor faced with the media chorus of "bubble, bubble, bubble" might decide that commodities are just not worth the risk. However, we think that would be a mistake. Commodity markets continue to behave in all sorts of different ways, with the most important differentiator between markets and sectors being the trends in supply and demand.

Much of the comment on commodity investment is ill-founded and confusing. It is therefore the aim of this report to assess the new institutional and retail investment activity in commodities, provide some reliable measures of investor flows and add some context to the current debate surrounding their impact.

Market participants

Participants in commodity markets can be classified into two groups: the first includes those such as producers, consumers or merchants with physical risks to hedge. The second comprises investors without physical risks, hedge funds, pension funds or any other type of investor that seeks to gain a return from commodity exposure by adding unhedged market risk to their portfolios.

Within the investor category, the institutions primarily consist of pension funds and insurance companies who invest through commodity indices. They account for the bulk of new fund inflows into commodity markets. Despite much talk of the large number of pension funds entering commodities markets the trend is only in its infancy, as many pension funds still consider commodities to be a peripheral diversifying investment to their portfolio.

Retail investment in commodity markets (including private investors and high net worth individuals) has been one of the fastest-growing categories, with in excess of $50bn assets under management via the easy-to-access Exchange Traded Product (ETP) category.

What's it actually worth? - Our estimates and methodology

Until recently, tracking investor interest in commodities was limited to the tracking of non-commercial futures positions in US futures markets, as reported by the US CFTC. However, the phenomenal growth of institutional and retail investment in commodities means that these new sectors have now become too important to ignore. The task of tracking these sectors is not easy because the data is partial and comes from a very wide range of different sources.

We use reported data, from various issuer websites and databases, on commodity ETPs, US commodity index-linked mutual funds plus issuance of medium-term notes (MTNs), and then estimate commodity index AUM attributable to institutional investors from industry sources to assess the trends in investment flows into commodities. Using this methodology, we arrive at a final number of $225bn at the end of Q1 08, where about $139bn is attributed to indices (which include $17bn tracking index-linked mutual funds and $122bn in index AUMs attributable to pension funds), $46bn to ETPs and $40bn to MTNs.

My view - I have long been an admirer of Barclays Capital, as I appreciate the variety of tracker instruments that they have created for investors, not least among commodities. Investors who have recognised the commodity supercycle, and invested or speculated in the various instruments available, including resources shares, trackers, funds and futures, have generally outperformed those who have shouted 'bubble' at the mention of commodities in recent years.

I agree with Barclays that fundamentals of supply and demand have been by far the main drivers behind appreciating commodity prices. These moves are depicted here by the CRB Index, nominal and inflation-adjusted, and the CRB's original version known as the Continuous Commodity Index or Old CRB, three of many such indices in the Fullermoney Library.

However I do not agree with Barclays that tracker funds investing in futures have had little or no influence on price trends for commodities. They base their assertion on two points:

1. The rollover - this means that expiring contracts are sold and the fund simultaneously purchases 2nd or 3rd month futures.

Yes, but these are long-only trackers catering to a significant new source of demand, which has grown rapidly.

2. Small percentages - Barclays says: "…our estimate of the value of index positions in the NYMEX oil futures market at the end of Q1 is $43bn which is equivalent to around 2.9% of the notional value of monthly turnover, 12% of the value of open interest and only 2% of the value of annual physical oil supply."

Assuming Barclays' estimates are a fair approximation, $43bn and certainly higher recently, represents a considerable amount of new demand for oil. Also, 2.9% of notional value of monthly turnover may not sound like much, but it is unleveraged demand whereas all the other futures activity from hedgers, industrial consumers and speculators is highly leveraged. Lastly, $43bn may be only 2% of annual physical oil supply, but most supply is not traded on the futures markets.

Also, while oil is the biggest commodity market by far, my guess is that the percentages for tracker participation in agricultural commodities are currently higher.

Consequently, I view commodity futures trackers as the growing elephant in the room, contributing to upward pressure on prices for what are often essential resources, prone to shortages in today's environment which is often characterised by fundamentals of inelastic supply and rising demand.

However I do not assume that this will always be the case. When supply eventually catches up with demand for a lengthy period, or in the case of crude oil, supply combined with substitution lowers demand, investors will reduce their exposure to commodity tracker funds, exerting downward pressure on prices in the process.

For this reason, I think CFTC officials or their equivalents at other futures exchanges, not to mention politicians, should be wary of hasty legislation to deter commodity investment or speculation. Arguably, they would have welcomed investor support when prices were depressed for lengthy periods, and may have cause to do so again at some stage. Moreover, legislation by, or more likely imposed on the CFTC, would probably drive much of today's investment demand to rival exchanges.

Email of the day (2) - On copper:

"I noticed in today's commentary you refer to copper as benefiting from recent events in Peru but that it is now at the top of its range. However, I see copper as just recently giving a buy signal and a few days ago I acted, averaging in around the 365 area. I've been watching copper for quite some time now and thought I had jumped on at a good point. What am I missing here?

"Many thanks for all the sterling work you guys put in."

My comment - Thanks for your appreciation.

I don't think you are missing anything, although you did slightly misquote me.

What I actually said was:

Today I introduced a breakeven stop for copper because it is near the higher side of its large range and benefited from industrial action in Peru.

Here is the weekly chart.

My personal portfolio: A partial profit taken on gold longs; sugar profit taken as tight stop is triggered; a portion of CADUSD mistakenly sold and repurchased, and increased - Remember when gold used to track Wall Street? …Until it did the opposite commencing last year. These linkages, including moving conversely with the USD, come and go. They may or may not be justified, but are at least a function of fashion, and become self-fulfilling for a while. However gold in the eyes of investors is variously real money, a barbarous relic, a commodity, jewellery and an industrial metal. More recently gold has been tracking oil, although this too will eventually pass, probably with the yellow metal outperforming black gold.

Meanwhile, gold is in a trading range, where I maintain it is worth accumulating on reactions, and if one trades futures, taking some profits on rallies, at least until the overall upward trend eventually resumes. Having seen gold trade lower this morning, when crude oil was also down, but rally following the petroleum contracts rebound, I decided to take a partial profit on seeing oil weaken once again. Accordingly, I sold some August gold at $906.60 this afternoon, against my purchase at $898.40 on 29th May, reported here on 2nd June as I had been away at the time.

With sugar on a stalk (or should I say cane?), I raised my tight stop once again this morning. It was triggered this afternoon, causing my August long to be sold at $378 versus my purchase at $350.5 on 11th June.

I placed a breakeven stop on my CAD/USD long and then meant to increase the position. However being more familiar with the USDCAD quote, and no doubt experiencing a senior moment, I sold when I meant to buy. Consequently half of my position was sold at $0.9843 against my purchase at $0.9798, annoying as there is a 10-point spread. Feeling very foolish, I reinstated the position a few minutes later, buying at $0.9847 after a slight pullback. This evening, I increased my overall position by 25%, buying at $0.9840.

Prices above include spread-bet dealing costs.

Additional Commentary by Eoin Treacy

PWC Review of global trends in the mining industry -2008: Mine* As good as it gets? - This report by the Mining team at PWC covers a number of interesting issues relating to the global mining industry. Here is a section on the attitudes of CEOs to their businesses:

The answer behind the change in attitude by the large miners with respect to their peers rests with one word: "value". The CEOs believe that the market has still not properly grasped the China story (and of course the fast developing countries include India) and the future increase in demand that will occur over the next decade. They also have learned, often the hard way, that bringing on new capacity is difficult and costly. Thus the supply / demand gap will continue and potentially grow. This should lead to high commodity prices over time.

There is a general view among the CEOs that analysts have been too conservative in their valuations of miners due to the usage of commodity prices that do not fully take into account future potential. This has lead to significant premiums being put on the table when a transaction occurs, as we saw when Rio Tinto acquired Alcan, and this is by no means an isolated example.

The CEOs are suggesting that mining companies are being undervalued and, therefore, there are good long term bargains to be had by undertaking transactions. This becomes obvious when viewing the commodity prices needed to support the prices being paid for individual assets, as they are often considerably higher than analyst's forecast. It is notable that even when this premium is paid for one company it is not then picked up in the valuations of similar companies, leaving them vulnerable to a deal to unlock the value.

The advent of the credit contagion has led to a bout of stock price reductions in the industry and, therefore, while investors were starting to more properly value the miners, this has since disappeared. Again we find ourselves with miners valued at a level that does not offer the blue sky that all those involved in the industry talk about regularly. It is certainly a positive outlook that is offered by the CEOs and one that is different to what is heard from other sectors at the moment.

Indeed the credit contagion has a silver (or maybe golden) lining for the big miners. Many of the projects that were on the development table of juniors will now be much harder for them to finance. Consequently, forecasters' supply expectations may not be met, driven by project delays from a lack of finance or labour, maintenance and other issues (such as weather, water and power), negatively impacting production. While analysts include uninterrupted supply expectations in their forecasts, this remains an unrealistic assumption, particularly in an industry that has been flat out delivering the maximum product possible over recent years. This is contrasted with demand assumptions that do not take a circa 10% GDP per annum growth in China into account.

My view - Buying assets rather than developing them has been a compelling argument for a number of years and remains attractive because of the rising costs and time lag in getting new greenfield projects off the ground. As a direct result of this trend, the resources sector took over from the financial sector as the biggest driver of M&A activity this year.

This story by Ambereen Choudhury and Brett Foley for Bloomberg covers details of that move. Here is a section:

Metals are the new green on Wall Street, as mining has displaced financial services to become the biggest source of mergers and acquisitions.

The value of announced mining takeovers more than tripled to $199 billion in the first five months of 2008 from a year ago, even as the global pace of M&A dropped 37 percent, data compiled by Bloomberg show. Financial-services companies, the largest driver of merger fees for the past two years, disclosed $173.5 billion of transactions in the first five months. It's the first time mining mergers have topped the M&A table since Bloomberg began compiling the data in 1998.

``We have moved into the age of commodities,'' said Carl Hughes, a London-based partner at Deloitte & Touche LLP, who oversees the firm's energy and resources practice. ``You clearly have a large number of mining companies just generating cash and profit like there is no tomorrow.''

A $100 billion deal is ``imminently possible,'' said Shaun Treacy, who runs Lehman Brothers Holdings Inc.'s global metals and mining group from London. That would be in addition to BHP Billiton Ltd.'s $147 billion unsolicited bid this year for Rio Tinto Group in the world's largest mining transaction.

``The race is on for valuable, high quality, scarce resources,'' said Treacy, 41. ``Rumors are circulating about various transactions, as there continues to be significant appetite.'

Mining executives could cynically be accused of talking their own books, in projecting a long-term secular bull for their industry. However, they have had to compete with developing country companies backed by their governments, as well as SWFs, in attempting to secure access to promising reserves. So they are in every sense of the phrase, at the coal face.

We also have to take into account the long-term plans of city planners in the major population centres of the world. They have massive young populations, which will need housing and jobs in the coming decades. When one also factors in the exodus from the country to cities in many of these countries, the long-term demand for resources could be unprecedented in human history.

Is it any wonder that mining companies are scrambling to take one another over, as they compete to gain access to reserves in politically stable parts of the world. This is a trend we can anticipate continuing for the life of this secular move, because, making the decision to develop a site which may not be operational for 7 or 8 years is a gamble, even in the demand environment evident today.

We can also anticipate that the cost of bringing new greenfield sites on-line is only going to get more expensive; making the case for taking over an existing operation all the more compelling. When respectable, cautious companies are throwing caution to the wind and investing heavily in exploration and development, we will most likely be in the third stage of this bull market, but that does not appear to be coming anytime soon.

Mineweb.com: Canadian oil sands expansion decision put back as original economics now marginal - This article from Reuters Jeffrey Jones, covers the increasing costs of bringing new projects on line. Here it is in full:

Petro-Canada (PCA.TO) is rethinking the design for an expansion of its MacKay River, Alberta, oil sands project due to surging costs for the steam-driven development, an executive said on Monday.

Petro-Canada, the country's No. 4 oil producer and refiner, had aimed to spend about C$1.2 billion ($1.2 billion) on the project, slated to start up in late 2011.

"It would have been maybe 20 percent higher than that" based on the work done on the previous design, vice-president Andrew Stephens told reporters after speaking to an investment conference.

"Since we've done that, we've seen real cost pressures, not only in terms of capital equipment but also in terms of operating costs as natural gas gets higher," he said.

In addition, Alberta's decision to increase royalty rates starting in 2009 contributed to making the economics of the project "marginal," he said.

Petro-Canada has pushed its go-ahead decision for the 40,000 barrel a day expansion to the first quarter of 2009 from the last quarter of this year.

The company is now considering integrating parts of the expansion with the much larger Fort Hills oil sands mining project, in which Petro-Canada has a 60 percent interest, Stephens said.

"There are some elements of equipment that we might be able to eliminate, and we might be able to produce some product that can be blended with the Fort Hills," he said.

He said Petro-Canada will not have a new cost estimate until it finishes the "rescoping" of the design.

The first phase of MacKay is expected to produce 25,000 barrels a day this year. It is an "in situ" oil sands project, in which the company injects steam into the ground to loosen up the tar-like bitumen, allowing it to be pumped to the surface in wells.

Petro-Canada shares rose 6 Canadian cents to C$58.69 on the Toronto Stock Exchange on Monday. ($1=$1.02 Canadian)

My view - Miners are not the only companies in the resources sector experiencing cost pressures. The Canadian Oil Sands are one of the few truly massive reserves of bitumen in the world, but a dearth of cheap, readily available energy, needed to sustain these operations, is restricting growth of the industry.

Natural Gas prices remain in an overall uptrend which has been rivetingly consistent from the lows near $7. While it would need to break the progression of higher lows to break this uptrend, today's key reversal suggests it may have hit a near-term peak. Follow through tomorrow would provide a stronger signal while a sustained move above today's highs would be needed to question this hypothesis.

New operations seem to be in a Catch-22 type situation. They need a cheap source of energy to exploit the resource, but the whole reason the operation is viable in the first place is because energy prices are high. This makes profitable operations, already in place and producing oil all the more valuable.

Email of the day - on potash:

"Reading the e-mail yesterday from the tomato farmer's son I am amazed that he believes farmers actually take any risk these days. Between the latest twice-vetoed pork-laden farm bill in the US and the sky-rocketing price of arable land anywhere, not to mention the EU's agricultural subsidies for decades, we are a long way from the days when Willie Nelson, Mellencamp and other rock stars used to do "farm aid " concerts.

"POT nurtured and developed its resources for decades while its stock price went sideways and now that it has pricing power should it just give it away? Saskatchewan has oodles of potash 3,000 ft underground and a mining-friendly environment so there is nothing stopping BHP or others greenlighting new projects. Furthermore, in contrast to commodities like steel or coal, a corn farmer who spends $1 on potash sees a return of $3 the same year on increased yields and a palm oil farmer in Asia a return of more than $6. You don't have to have an MBA to see the value in that type of return. POT (and I'm sure MOS also) will tell you that ALL their global customers are on allocation so the price increases have only just started. I believe only about 2% of a loaf of bread is the fertilizer cost so I don't think we can lay the blame on POT for global inflation.

"Finally, I don't much care what the charts say, the good Lord only saw fit to put decent amounts of potash in Canada, Russia and Belarus and until a mining company (other than POT) has the guts to step up and greenlight a new project the world needs to get used to increasingly more expensive potash. It is the only known source of Potassium on the planet because I don't think bananas are a cost efficient substitute for millions of acres and I don't think it is the western world's prerogative to tell Chinese and Indian consumers that they can't eat animal protein.

"Some stocks actually do go up 17 fold - take a look at the chart of ATI for example from 2003 -2007 (titanium - who knew??) so don't bet against POT just yet. This is not a bubble, this is good old-fashioned supply and demand and in 7 or 8 years when new resources are brought into production prices will surely go down. Until then there is money to be made,"

My comment - Thank you for this informative email and congratulations on what must be a profitable investment. I am in full agreement with your bullish stance on potash and also believe it has a long way to go before it reaches the peak of this long-term move.

However, I would like to reiterate that I also believe at least some investors will head for the exit, when the potash price starts to turn downwards. In this respect, it could be similar to what happened to uranium in the medium term.

This does not tell us what the subsequent correction will look like. How the potash price performs following its next medium-term peak, will have at least some impact on how the equities perform. If potash finds support relatively quickly and pushes up to new highs, investors might quickly find their way back to the equities. However, if the potash price has a more significant correction, then the equities may go through a more protracted medium-term consolidation.

At present, all we know is that the price of potash is accelerating and that is an ending characteristic of unspecified duration. It is currently lending a substantial boost to the share prices of related companies. There is no indication yet that it is over, but we will know what to look for when it is.

Eoin's personal portfolio: Hang Seng long stopped out at a small loss - I was stopped out of my long in the Hang Seng last night at 22,950 against my speculative purchase at 23,153 on June 12th. I had been attempting to buy low but the Index was unable to rally and against the background of weaker indices globally. I tightened my stop, as a result, which was quickly triggered. I may get the opportunity to buy lower.

My recent grain and cocoa trades have offset and left me in net profit, when measured against my misadventure in the Hang Seng over the last months.

Friday 20th June 2008

Minor metal prices soar on demand for more fuel-efficient jet engines - This is an informative item from Javier Blas for the Financial Times. Here is the opening:

The airline industry's fight for survival in the face of soaring oil prices has triggered a massive jump in the price of a number of obscure and scarce metals that are used to improve the fuel economy of jet engines.

Traders said demand for minor metals such as rhenium, chromium, cobalt and titanium was booming as Rolls-Royce, General Electric and Pratt & Whitney bought them for new super-alloys that helped cut aircraft fuel consumption.

The jump in the price of rhenium - an extremely rare metal that was the last naturally occurring chemical element to be discovered - is the most striking example of the new environment.

The rhenium price yesterday surged to a record of $11,250 a kilogramme, more than double last year's level and up from about $1,000 in early 2006, traders said.

My view - The simplistic view on commodities is that we are witnessing a speculative bubble which will soon be punctured by slower GDP growth in China and elsewhere.

There is speculation in commodities, as we see periodically in all markets. However the main fundamental drivers of the supercycle, which Fullermoney has discussed at length over the last seven years, are global infrastructure demand and frequently scarcity.

Shortages are due to a number of factors including costs, finite supply, weather, accidents and politics. There is a lesser known but rapidly growing source of demand for what have traditionally been known as minor metals. However many of these could be more accurately described as high-tech metals, used by the aerospace, electronic and medical industries.

Demand for some of these, mentioned in the FT article above, has proved remarkably resistant to the economic slowdown to date, as you can see from these weekly price charts: rhenium, chromium, cobalt and titanium.

What are the investment implications?

I certainly will not be selling my mining shares and funds, although I expect price action to remain volatile.

At a time when investor sentiment has deteriorated once again, and stock markets are battered by an apparent perfect storm - credit problems, deleveraging, slower GDP growth, corporate profit downgrades and inflationary pressures - all of which give rise to rumours of ever greater problems, it would be easy to overlook the most broadly based global growth story in history.

While some western countries skirt close to recession, most of the world is doing quite well, except for the inflationary problems. I do not minimise these, having long forecast an inflationary cycle, led by resources. However I have also said that it would be erratic rather than linear. I suspect that inflation will peak in most countries over the next few months. Interestingly, this has already occurred in China, although the partial removal of energy subsidies will lift it again temporarily (*see also the report from Yang Liu of Atlantis, below*).

Email of the day (1) - On a theory / strategy for housing:

"I know that UK real estate shares would not currently feature well in the International Beauty Contest. I have recently emigrated from South Africa to the UK (at R14 to the £) and have a sum of money allocated towards buying a house. I have naturally been waiting in anticipation of the falling house prices and at some point will need to make a decision. My theory is that listed property shares/trusts lead house prices both when falling as well as when rising. eg British Land, Land Sec, and Liberty International rose by 267%, 201% and 188% respectively from 28/12/2001 to 29/12/2006, and since that date have now dropped by 56%, 41% and 38% respectively. I do not have housing stats for those periods but believe that both the rise and fall of house prices were less and somewhat behind the property shares. Would it therefore make sense to invest my "Housing Allocation" into a spread of property shares when they show signs of bottoming and then hopefully benefit by their rise ahead of the housing market.?? I see this as a form of hedge as I will at least be invested in the same asset class, but could benefit a lot by the shares leading the house prices up.

"I would greatly appreciate any view you may have on this strategy."

My comment - What I appreciate about this email is that you have done your own research, and shared it with the Collective. You are, of course, comparing the shares of commercial property companies with house prices in an unspecified area. However they are not unrelated and the stock market is a lead indicator, as you know.

You have worked out the potential benefits, so if you will forgive me for responding to your question with a question of my own: have you also considered the possible downside? For instance, you might jump the gun. I thought British Land and Land Securities had commenced bottoming out at yearend 2007, but they subsequently broke downwards once again.

This would not necessarily invalidate your hypothesis and its potential, although it would probably lengthen the lead time, but you have to weigh your anticipated gain against possible psychological pressure if things are not working to plan. You need to ask yourself how you and any dependents would react if it did not work out as you expect. For instance, could it jeopardise your quality of life, or do you feel that you can handle the risks, both emotionally and physically? Once you have analysed this with the same diligence as your financial research above, you may have your answer.

Email of the day (2) - On the Hang Seng:

"Hello. I hope everything is ok beyond the Atlantic. I would like to know your opinion about the Hang Seng. It has been erratic and it reached the downside target that Chris Roberts suggested days ago. Is it ok to assume that it is a play linked to the US with more Beta? Am I very simplistic if I think that, if US stocks recover, the HS will go upwards?

"Once again, thank you David for your support."

My comment - Thanks, and I think you are correct. The Wall Street leash-effect is in charge once again.

Yang Liu on China - I think many subscribers will be interested in this report by Yang Liu of Atlantis. Here is the opening:

China's equity market was recovering well until the interruption caused by the rare earthquake in Sichuan in the middle of the month. Investors' confidence towards China has been impacted again by such a shocking natural disaster which led to profit taking and shrinking turnover in May 2008.

What else can be more important than such a major earthquake to keep investors alert in China? The answer is inflation. May CPI eased to 7.7% from 8.5% in April, as expected, on both food and non-food prices. Data suggests that food price inflation moved lower in May, consistent with the moderating trend seen in the latest Ministry of Commerce and Ministry of Agriculture figures, as well as May PPI readings. The slowing rate of food price inflation, 11.0% yoy in May, down from 11.9% in April, suggests that the effects of the snowstorm are receding and the impact of the earthquake has, so far, been limited.

Despite the earthquake on 12th May, moderating inflationary pressure and the shortened May holiday, retail sales growth stayed robust, showing strong consumer demand. The 21.6% growth in May was just shy of the 22% in April. Accounting for the 7.7% rate of inflation, May real retail sales grew 13.2% yoy, the fastest pace of growth since January this year.

Going forward, China's economic policy will aim to keep inflation at a satisfactory level in the second half. External uncertainty and reconstruction after the snowstorm and earthquake should see robust FAI demand over the coming 6 to 12 months. Also, given the moderating inflationary pressures, there is unlikely to be further credit tightening in the second half. May data continued to show the momentum of growth and inflation. The gain in money supply growth in May prompted the PBoC's decision to hike the RRR by 100bps in early June. This should be seen as a passive monetary move promoted by hot money inflows because excess liquidity remains a threat to China's high inflation.

We can understand why China should maintain a rapid investment-driven economic growth profile in the second half of 2008 as a result of the reconstruction and rebuilding stage after two natural disasters within 4 months. We believe the PBoC still prefers to utilise quantitative tools (RRR hike) over the short term because it has been cautious in using price tools (interest rate hike) for the choice of monetary policy over the past six months.

My view - The Sichuan earthquake was an appalling human tragedy but reconstruction will help to sustain China's growth in the post-Olympic period. I agree with Yang Liu's view that China is in an enviable fiscal position. I wish that I had developed the wisdom to sell this fund last October. I will have to settle for enjoying the recovery and what I believe will eventually be a move to much higher levels.

My personal portfolio: A coffee long opened; gold purchased; Nikkei stop triggered; CAD/USD partially stopped out - My Nikkei stop was triggered this morning, resulting in a sale at 14100 for the September position, versus my rollover purchases at 14029 on 11th June. I remain bullish of Japan but it cannot perform on its own in what remains a difficult period for stock markets.

I bought Arabica coffee this afternoon, paying $142.65 for a September position. In a click through charts with Eoin, we noticed that it was firm within a ranging pattern (weekly & daily). A search on Bloomberg produced this item of seasonal interest, although frost in Brazil is a rare occurrence.

Noting that oil had firmed but gold had eased, I bought back the yellow metal that I had sold yesterday, at a slightly better price, paying $901.85 for another August position.

CAD/USD reversed an earlier decline today, triggering a tight stop on 40% of my position. This was sold at $0.9800 against my purchase at $0.9798 on 17th June.

Positions above include spread-bet dealing costs.

Investors Intelligence: Advisors Sentiment - If ever a picture was worth a thousand words, this is it. Don't miss this report, produced by veterans Mike Burke and John Gray.

My view - Mike Burke and John Gray's comments are interesting but this graph speaks for itself. There has never been a reading at current or lower levels that was not soon followed by a sharp rebound, including during the last bear market. This indicates to me that we are within a week or two of a bear squeeze, providing at least a tradable rally in which I aim to participate.

Quote of the week - On looking back:

"The farther backward you can look, the farther forward you are likely to see." Winston Churchill

Additional Commentary by Eoin Treacy

China's Cocoa Demand Rises on Living Standards, Researcher Says - This article by William Bi for Bloomberg covers the changing dietary habits of emerging nations. Here it is in full:

China's chocolate consumption is increasing 10 to 15 percent a year as living standards rise, buoying demand for cocoa, a consumer market research firm said.

``Chinese consumers are demanding higher and higher quality products,'' which generally contain more cocoa, Song Songyun, vice general manager of Beijing-based Sinomonitor International, said in an interview yesterday, citing the firm's annual study on China's consumer market and media.

Tightening supplies from Africa and growing demand for chocolate in countries like China and India, where disposable incomes are rising, have helped cocoa climb this week to its highest since at least 1989 in London.

In the first four months of this year, China's imports of cocoa beans rose 13 percent to 15,543 metric tons, while imports of cocoa powder gained 22 percent to 6,342 tons, according to data provided by Beijing Orient Agribusiness Consultant Ltd.

Most Chinese chocolate products sold, worth about 20 billion yuan ($2.9 billion) a year, are in the medium to lower range of the market, containing less cocoa, Song said, adding that China's current per capita chocolate consumption ranked very low.

``This is a big potential market. Chocolate is becoming important in gift items in China, like for Valentine's Day, Spring Festival and lucky candy for newly weds,'' Song said.

Cocoa, heading for its best annual performance since 2001, has gained 59 percent this year on speculation crops in Ivory Coast, the world's biggest grower, are threatened by disease. The UBS Bloomberg Constant Maturity Commodity Index of 26 raw materials has climbed 28 percent.

Cocoa for July delivery settled little changed yesterday at 1,663 pounds ($3,278) a ton on the Liffe exchange in London. It rose as high as 1,688 pounds yesterday.

My view - Changing dietary habits across the developing world are impacting food prices right across the agricultural sector. When people move from a subsistence lifestyle, to one where they can afford more nutritious foods, they quickly become used to their new circumstances. Civil unrest can result when populations are forced back beneath what is now considered a floor in terms of food variety and quality. The recent Mexican tortilla riots are one such example.

China and India have successfully raised hundreds of millions of people out of abject poverty and into the middle classes. It is only to be expected that their per capita consumption of 'luxury' food items such as cocoa and coffee increase along with the increase in disposable income which is the hallmark of a developing middle class.

Cocoa is currently one of the better performing commodities. This is at least in part due to increasing demand from the emerging world on the demand side and disease affecting the Ivory Coast crop on the supply side. Interestingly, the high cost of fertilisers and pesticides is a contributing factor to the low quality of the current crop.

Cocoa accelerated to at least a 20-year high near 3000p in March, before experiencing an aggressive reaction. However, it found support quickly and rallied impressively back to the high over the last three months. It broke upwards again last week and a downward dynamic would be needed to question momentum beyond a brief pause.

Coffee is also worthy of mention. Arabica broke upwards from the 3-year consolidation in early February and accelerated to a high near $170. It reacted, in common with much of the agricultural complex in March, but found support just below the breakout point and retains the progression of rising major reaction lows from April 2007. A sustained move below $125 would be needed to question potential for an further upside.

Robusta did not consolidate in the same way as Arabica between 2005 and early 2008. It was in a gradual uptrend for much of this time before accelerating in the last quarter of 2007 and early 2008. (The gap in the continuation chart from November illustrates the contango at that time.) Following the reaction from the high, Robusta found support near $2100 and would need to sustain a move below that level to offset scope for some further upside.

Email of the day (1) - on an addition to the Chart Library:

"I was wondering if you could possibly place the CNX Banks Index in your lovely Chart Library? My apologies if I have missed it and it already exists in there. Thank you"

My comment - Thank you for alerting us to the existence of this index. I have also added the CNX Defty Index which is a capitalization weighted Index of the Top-50 companies in India.

The CNX Banks Index broke down three weeks ago, in common with the Bombay Banks Index. Both indices have led the wider market from the peak in January and are worth monitoring for signs they may be finding support.

They both need to sustain moves above this week's highs to question scope for some further downside.

The CNX Defty Index broke down at the same time as the banks but has underperformed to a greater extend. It needs to rally back above the March lows to question scope for some further downside.

Email of the day (2) - questions about how to read relative charts:

"1. Can you explain oil to gold spread and overlay chart and what this is telling me? Same with Dow / Gold overlay. This might seem dumb but also how to do you read these charts & more importantly what's the current chart saying. Eoin mentioned lately on one of his audios this was important.

"2. Within the filter system in the chart library, if I compare a stock relative to say the S&P 500 what is this telling me. I am not 100% on how to interpret the result.

"3. Same with the chart of 'NYSE short interest as a total % of shares', same question how do you read this chart OR as an example what is the current chart indicating. Are there other open short interest charts one should watch?

"You don't have to publish these questions, but if you could let me know the answers so I could become more informed that would be great.

"Looking forward to attending the chart seminar in Nov '08"

My comment - Thank you for these questions which I'm sure will also be of interest to other subscribers. I'm looking forward to seeing you at the Chart Seminar. The ratios you mention, among others, often come up for discussion at The Chart Seminar. I'm looking forward to seeing you there. Taking your questions in order:

1. The Gold / Oil ratio is simply the price of gold divided by oil. The scale is currently close to 7. This means it takes 7 units of oil to buy one until of gold. A year ago it was closer to 12, so gold is getting cheaper when measured in terms of oil.

The ratio fell aggressively from near 10 in February to the current level, as oil outperformed but it is now looking somewhat overextended. The current level is also close to an historic area of support and the ratio would need to sustain a move to new lows to reaffirm oil's outperformance.

The overlay chart simply shows us that both oil and gold are on the same general trajectory, within their secular bull trends.

The Dow / Gold ratio is the value of the Dow Jones Industrial Average divided by the price of Gold. This is used as a proxy for the secular moves between outperformance of equities relative to equities. It is possible to view this chart back to 1957 in the Chart Library and here it is going back to 1920. The chart illustrates that the Dow has outperformed commodities in three secular bull moves in the last 90-years. These climaxed in 1929, 1965 and 1999. The current reading shows us that that the Dow has retraced more than half its bull market relative to gold but has significant room to underperform further.

Since oil and the other commodities are all on a similar track to gold, they also have significant potential for appreciate further relative to the Dow. You can create your own relative charts for commodities against the Dow using the Charting function in the Chart Library.

2. Using the Filter system, if you filter the members of the S&P500 relative to the S&P500 Index, the performance figures will show you how much each individual stock is outperforming or underperforming the Index.

For example Jabil Circuit Inc. is up 27.8% in the last month, as of yesterday's close. When looked at relative to the S&P500, it is up 34.5%. This is because the Index fell in the last month while the share advanced.

Please see the Filter Help Pages for instructions on how to use the Filter system.

3. The chart of the NYSE short Interest as a % of Total Shares Outstanding has just moved above 4%, an all time high. I can think of two reasons to explain the uptrend of the last two years. The first is that the number of shares outstanding may have shrunk because of share buybacks and de-listings. If the number of shorts was static to rising, this would result in an increase of the percentage of shorts.

The other reason is that there are simply more market participants managing a long / short or wholly short book. We can conclude from this chart that if the number of shorts is increasing, then capital is accumulating to fuel the next big upward move. This is because at least some of these shorts will be forced to cover their positions when the market rallies.

I'm not aware of any other indices where it is possible to monitor the percentage of short interest so easily. If subscribers can suggest any, and they are available on Bloomberg, I would be happy to add them to the Chart Library.

Topix-17 sectors - I added this new arrangement of 17 Japanese sectors to the Chart Library today. Filtering the selection; we see that only the TPX-17 Foods Index is making new lows. The Index has been ranging for the last 5-months and posted a new low this week. A sustained move above 180 would be needed to offset potential for some further downside.

The TPX-17 Machinery Index is the best performer over the last 3-month. It is currently pressuring the progression of rising lows over the last two-months, but is one to watch as a recovery candidate, when the current market uncertainty resolves itself.

The TPX-17 Autos & Transport Equipment Index is the only one to have posted a positive result in the last month. It encountered resistance near 180 and needs to sustain a move above that level to confirm that the bulls have regained the upper hand

Today's interesting charts - The Chart Library has two Search Engines. One searches the more than 16,000 equities, funds and ETFs in the International Equity Library and the other searches through the rest of the Chart Library for indices, commodities, currencies, bond prices and yields, ratios, spreads and overlays.

Corn - losing momentum beneath the round 800¢, following an accelerated move from 600c in the last 3 weeks. It needs to sustain a move to new high ground to offset potential for some further consolidation of recent gains.

Thailand - posts an upside key day reversal having found support near the January lows. Follow through next week would confirm a more positive signal and it would need to sustain a move below today's lows to question scope for some further upside.

New Zealand - breaking down from the short 6-month distribution. A sustained move above 3400 is needed to offset scope for some further downside.