

Fullermoney

Global Strategy and Investment Trends by David Fuller

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

Monday 23rd June 2008

Stuck in the Middle - [My thanks to Tim Price of PFP Wealth Management for some welcome knockabout humour at a time of gratuitous gloom from most commentators. Here is the opening:](#)

"Well I don't know why I came here tonight
I got a feeling that something ain't right
I'm so scared in case I fall off my chair
And I'm wondering how I'll get down those stairs
Clowns to the left of me, jokers to the right
Here I am.."

- "Stuck in the Middle with You? by Stealer's Wheel; also the soundtrack to the notorious ear-removal sequence in Quentin Tarantino's 'Reservoir Dogs'.

There has never been any shortage of clowns and jokers in the investment markets, but it sometimes takes a bear market to flush a few out. In contradiction to the widespread fear that hedge funds would precipitate the Next Big Crash, we now know that it was actually the banks that laid its (wobbly) foundations. Now, with sentiment fragile and fund managers widely sheltering in cash, the journalists are having a go at pushing at the pedestal. "RBS issues global stock and credit crash alert," warned Ambrose Evans-Pritchard of the Telegraph, inviting "one of the worst bear markets over the last century". The RBS research note in question was more subtly entitled "Crude-flation Concerns Spike"; while crude-flation is undoubtedly an uglier word even than stagflation, it is not clear who Spike is, nor why he should be concerned. It is certainly difficult to know quite how worked up (if at all) to get about the RBS note in question. Some of us evidently felt that the markets had already "crashed" in the conventional sense of the word, given the falls in credit markets and stocks - particularly banking stocks like, say, those of RBS (-60%) - since the summer of 2007. "The very nasty period is soon to be upon us - be prepared," warned RBS on 11th June (2008). The market environment is nasty already, and has been for quite some time, as anybody with any form of investments will surely testify. Perhaps future research will report the sad passing of Queen Victoria or the sinking of the SS Titanic. But it is always nice to hear that the banks who brought us the credit crunch in the first place are bang up with events. Just after they've had their latest emergency rights issue.

There is, of course, a long and inglorious history of commentators calling for a Crash.

My view - When the contemplation of suicide seems only slightly less abhorrent than investing, the market is usually oversold. Towards the end of Tim Price's letter he reminds us of two appropriate quotes for such occasions from legendary investors - Sir John Templeton and Warren Buffett. Don't miss these quotes.

Regarding the RBS forecast, veteran subscribers will recall that just as increasingly bold extrapolations by forecasters in what has already been a significant uptrend are often a contrary indicator, the same applies in reverse.

(See also the Investors Intelligence Advisors Sentiment report posted on Friday 20th June and the Merrill Lynch survey discussed on Thursday 20th June.)

Here is a second [report](#) by Tim Price, discussing recent financial books by George Soros and Charles R Morris.

"Views, Trends and Recommendations" - My thanks to a subscriber for this interesting [report](#) by Adrian Schonauer of Banque Bénédict Hentsch. Here is a brief sample:

We are well aware that earnings estimates can be revised down anytime, and that effective earnings may be below estimates. Still, we find it interesting to compare current figures with the 5 year average (source Bloomberg). It shows that all sectors are clearly below the average. Thus, if earnings are confirmed and P/E's make it back to the 5 year average, there is roughly a 50% upside potential for stocks.

We find it particularly interesting that the two cheapest sectors are the financial sector (which dropped the most in a year) and basic materials, such as metals & mining (which rose the most in a year - see chart on next slide).

My comment - This is an interesting and perhaps timely observation. The bearish riposte, I suspect, will be that the 5-year average PERs were too high; deleveraging is occurring; growth is slowing; profits will fall, and valuations can go to single figures.

Perhaps, but this bearish view is an extrapolation, to which one could reply: How do they know?

My own view is that for long-term investors, the risk of being too bearish today probably outweighs the risk of being too bullish. However what I do not yet see is the bullish catalyst to lift stock markets up out of this self-feeding decline, beyond a bounce.

I suspect many subscribers will be interested in the graph on slide 8 of Adrian Schonauer's report, comparing the performance of Materials with that of

Financials. This is topical following comments in some quarters that one should be selling Materials and buying Financials.

The two are not mutually exclusive, of course. I will be holding my mining shares and funds, but I cannot quite bring myself to buy banks just yet. However I do not doubt that the survivors will stage a significant recovery over the longer term.

My personal portfolio: Gold long trade increased - Hoping that [gold's](#) decline today was an overreaction, I bought a little more, paying \$883.45 for the August position. This price includes spread-bet dealing costs.

The Weekly View: Dow Testing March Lows - Sentiment Not Yet at Bearish Extremes - My thanks to the RiverFront Investment Group for this timely [report](#) by Rod Smyth. Here is a brief sample:

We have three main investment rules: "Don't fight the Fed, don't fight the trend and beware the crowd at extremes." Having been supportive of stocks since last August, the Fed is now neutral, hamstrung by the weakness of the dollar and the rise in inflation expectations. Sentiment is becoming bearish (a plus from a contrarian perspective), but has not reached the bearish extremes that would give us strong conviction that the month-long decline is over (see The Weekly Chart). The primary trend remains the market's biggest negative as it is clearly declining. We see considerable technical support for the S&P 500 between Friday's close of 1318 and around 1270, the March and January lows. On balance, we expect these levels to hold in the coming weeks followed by a rally that will, once again, test the primary downtrend.

My view - The January and March lows for the [S&P 500 Index](#) occurred against the background of what was clearly climactic selling activity, characterised by heavy volume and volatile activity. We are not seeing that this time, at least not to date, as the market is drifting lower.

What are the implications?

The market is generating its own technical signals and they have been negative since mid-May, led by [bank indices](#) which have moved steadily lower. I imagine many investors are wondering if they will see further action from the Fed, which was proactive in January and March.

However Bernanke has less ammunition this time, at least in terms of interest rates. He may be hoping for a downward improvement in the price of [crude oil](#) but this has yet to materialise. Stock market sentiment is mostly bearish and this is a contrary indicator, as pointed out previously, but buyers are cautious and short-sellers will be emboldened if they conclude that the Fed is indeed "hamstrung", as Rod Smyth suggests.

We can expect some drama fairly soon but markets may have to go somewhat lower before we get a bounce of consequence.

Additional Commentary by Eoin Treacy

Deutsche Bank Uranium Sector: Using IEA's 2050 IEA calls for 1000 new reactor builds by 2050 - [Thanks to a subscriber for this enlightening report by Paul Young, Joel Crane and Brendan Fitzpatrick which focuses on Australian uranium companies. Here is a section:](#)

Energy mix targets we estimate that uranium demand could increase by 215% under the ACT Scenario, and by 290% under the BLUE scenario, to 243kt and 300kt of U₃O₈ per annum respectively (see Figures 3 and 4). Even if either scenario is achieved, which is heavily reliant on international legislation and government willingness to adopt and embrace change, we believe that world is on the verge of a uranium renaissance. In our opinion, the financial markets continue to underestimate the potential for a rapid increase in uranium demand going forward. Saying that, we do acknowledge that the increase in demand may be slow, and we forecast just a 2% demand increase between 2008 and 2010, but a 17% increase between 2010 and 2015.

In our opinion, the biggest impediment to achieving the IEA's ACT and BLUE targets is not global legislation change but the potential inability of uranium supply to respond to a likely spike in demand from 2015 onwards. To put it into context, the world's largest uranium development project is the well documented expansion of the Olympic Dam mine, located in South Australia, with a total uranium resource (measured, indicated, inferred) of ~2,240kt of uranium. We believe that the proposed expansion of Olympic Dam involving a large open cut mine and expanded processing facilities could deliver an additional 15ktpa of uranium from 2016 onwards. However, the world would need to find and develop an additional ten Olympic Dam sized mines by 2050 to supply sufficient uranium to the world's nuclear reactors under the ACT scenario and an additional 15 Olympic Dam sized mines under the BLUE scenario. Severe under investment in the uranium sector has resulted in few if any significant new uranium discoveries since 1980. Therefore we believe that supply could struggle to respond to the potential increase in uranium demand between 2010 and 2050.

We note that uranium is significantly underperforming other energy commodities in 2008 (shown in Figure 6). In our opinion, the current spot price of US\$59/lb may not be high enough to encourage new uranium supply, from both greenfields and brownfields projects, particularly from projects in high cost construction countries such as Canada, Australia and the US.

Over the past week Ux Consulting has reported that two utilities are seeking uranium in the spot market (one for 100,000 pounds and the other for 300,000 pounds), and that they may have found suppliers only willing to offer at or above the \$60 level. We believe that continual supply issues and the likelihood of increased demand from utilities should drive the spot price higher in 3Q 2008.

My view - The speculative excesses that fuelled the massive run up in uranium-related companies ended when the commodity price had its first downtick, following a spectacular advance which climaxed in 2007. We have long said that uranium is the best of the long-term energy plays; however it remains in a predictable medium-term correction which has yet to bottom conclusively. A large number of speculative stocks were IPOed on the back of the initial run-up, and those that had much less uranium than they claimed have disappeared during this correction. Stocks with no earnings remain considerably higher risk than those with a steady income, in this, or any other sector.

Since mid-2007 [uranium](#) has more than halved and remains in a medium-term downtrend which is losing momentum. An upward dynamic would indicate that at least a short-term floor has been reached; while a sustained move above \$95 is needed to break the progression of lower highs and suggest that the bulls are regaining the upper hand.

All of the companies mentioned in this report can be found in the Chart Library. While most uranium related equities are unlikely to outperform other commodity related stocks, before the uranium price shows signs that it is recovering, a number have weathered the current drawdown better than others.

[Energy Resources of Australia](#) (ERA) more than doubled between late 2006 and early 2007 before giving up almost the entire advance. However, it bounced sharply from AU\$15 and rallied impressively to AU\$25, before moving into a consolidation of the gain. It has plotted a progression of rising lows within the range and would need to sustain a move below AU\$20 to question scope for an upside break.

[Extract Resources](#) peaked considerably earlier than the rest of the sector. It also gave up much of its gain by the time it bottomed on August 17th and has rallied impressively to retest its highs. It has been consolidating the gain for much of the year and would need to sustain a move below AU\$1 to question potential for an upside break.

[Mantra Resources](#) has been in a consistent uptrend from its IPO although its advance has picked up pace in the last few weeks. However, a downward dynamic would be needed to check momentum beyond a brief pause.

[Alliance Resources](#) also gave up almost its entire advance before finding support near AU\$0.50 in April. The share has since rallied impressively to AU\$1.50 and is currently consolidating. It would need to sustain a move below AU\$1.15 to question scope for an upside break.

[A-Cap Resources](#) found support near AU\$0.20 in March and rallied impressively in May. A sustained move to new lows would be needed to question recovery potential.

A number of other companies such as [Paladin Resources](#), [Uranex](#), [Bannerman](#) and [Marathon Resources](#) have all recently found support in the

region of their lows and appear to be in support building phases. They would need to sustain moves to new lows to offset scope for some further higher to lateral ranging.

Two Canadian companies not mentioned in the report, but leaders in the sector, are [Cameco Corp](#) and [Denison Mines](#). Cameco broke upwards to a new high a year ago, but was unable to sustain the move and fell back into the range. It broke down from the range in January, but was unable to sustain that break either and has since rallied back into the consolidation. It would need to break the progression of higher lows, from near C\$31, to question potential for some further higher to lateral ranging.

Denison Mines, in common with a number of other uranium miners, found support earlier this year and has entered a support building phase. It would need to sustain a move below C\$6 to question this hypothesis.

Eoin's personal portfolio: Arabica coffee position opened and US Treasury short opened - I opened a long this morning in September [Arabica](#) coffee paying \$147 including spread-bet dealing costs. It broke upwards emphatically on Friday and maintained the gain today. I am willing to give the upside the benefit of the doubt as long as it sustains the gain.

I also opened a short in the September [US 30yr Treasuries](#) this afternoon selling at 113.35 on the decimalised contract. All prices quoted include spread-bet dealing costs.

Deutsche Bank Commodities Weekly - Thanks to a subscriber for this [report](#) which contains items on a number of issues, but here is a section by Adam Sieminski on natural gas:

LNG in short supply after 2010

The outlook for the global LNG market is tight in our view. The US market's size, liquidity, diversity of supply and storage capacity make it the "sink" for LNG cargoes, but, a shortage of global natural gas has left the sink without a sufficient tap of supply. The US "call on LNG" exceeds available supply. Long term we believe the situation will deteriorate further. The expected 2007 FID of nearly 90Mta of LNG capacity saw only 10Mta receive project sanction i.e., a near-term supply growth breather in 2009 will give way to shortages post-2010.

While supply struggles, demand strength continues to surprise, led by earthquakes in Japan, droughts in Spain, and the emergence of new demand centers in Kuwait, Singapore, Chile and Argentina - the southern hemisphere now competes for US summer imports. Short supply has polarized returns, driving shipping & regas often below cost of capital, yet upstream returns to > 50% IRR.

Strong international demand plus a security of supply and environmental premium in Asia and Europe has left international prices set by the marginal

price of demand, pushing long-term contracts to straight line oil parity, with implied pricing of USD17/mmBtu at USD100/bbl oil. Global tightness will leave the US exposed to price spikes (likely weather induced) up to global market levels. We believe the key point will be that rival gas markets for example in Asia and South America will be prepared to pay more for LNG supply than US buyers.

Figure 2 shows how demand exceeds supply, which is an unlikely scenario and one that will, in our view, be resolved by higher prices.

Working gas in storage increased to 1,943bcf 13-June according to EIA's Weekly Natural Gas Storage Report, Figure 3. According to the EIA, the implied net injection of 57bcf into working gas was 37% below the 5-year average net injection of 90bcf for the same report week. Nymex natural gas for July delivery is currently trading near USD12.85mmBtu, at a 10.3x ratio to WTI crude oil.

My view - Natural gas has been trading in a range relative to oil for much of the last 15 years. It was close to the upper side of that long consolidation towards the beginning of the year and is slowly backing away from those levels as it continues to outperform oil. A sustained move above 12 would be needed to question the integrity of this trend.

Natural Gas remains in an overall uptrend from the lows near \$7. The key day reversal posted Thursday was unaccompanied by any follow through and the progression of rising lows remains intact. It needs to break this sequence to offset scope for some further upside.

Mineweb.com: Social unrest in Peru focuses around mining sector wealth - [This interesting article by Terry Wade for Reuters covers the ongoing unrest surrounding the nation's mining sector. Here it is in full:](#)

Blockades and strikes this week exposed deep rifts in Peruvian society and more protests are likely unless the government finds a way to spread the wealth from an economic surge to workers and the poor.

With global prices rising for the natural resources that Peru exports, social conflicts are becoming more frequent and are putting President Alan Garcia in a bind.

Garcia wants foreign mining and oil companies to invest billions in Peru to help cut the poverty rate of 40 percent, but many people complain they have yet to reap the benefits from an economic boom now in its seventh year.

"Protests and conflicts about how to redistribute wealth are inevitable because expectations are high and there is lots of poverty," said Santiago Pedraglio, a political analyst. "The government must figure out how to avoid more conflicts."

Before lifting a blockade on Thursday, 20,000 residents of Moquegua

occupied roads, took 60 police hostage, and severed access to a smelter and mine of Southern Copper (SPC.LM) (PCU.N), Peru's largest copper producer, to demand that their province receive a bigger share of taxes paid by the company.

Workers at two important copper mines in Peru also held strikes this week, pushing up global prices until they were persuaded to return to their jobs.

Garcia, whose approval rating hovers at 35 percent, is under pressure to reduce poverty quickly or risk losing support for his free-market policies at a time when left-wing parties are eyeing Peru's next presidential election in 2011.

The latest round of protests only ended after Garcia's chief of staff promised to boost economic aid to poor provinces and beef up anti-poverty programs.

LOOMING CONFLICTS

Still, more strife looms. Peru's ombudsman's office says there are 116 unresolved conflicts over natural resources nationwide.

Poor indigenous communities in the mountains are demanding a bigger slice of huge profits generated by foreign mining companies, while tribes in the Amazon rain forest are worrying that oil drilling will contaminate their lands.

Incidents of strikes, roadblocks or protests in the past six months doubled to 65, over the number in the previous half year, at a time when Peru's economy is growing faster than ever. It expanded 9 percent in 2007 and 13.25 percent in April from the same month a year earlier.

More discord is a sign that record metals prices have raised public expectations and intensified the frustration felt by those who think Peru's swift growth has passed them by.

In at least one case, resistance to mining on environmental grounds forced a foreign company, Manhattan Minerals, to scrap plans for a mine in a town in northern Peru. Currently, a nearby town is trying to stop Chinese miner Zijin (2899.HK) from building a \$1.4 billion copper mine.

Unions are also intensifying their demands for better pay and benefits. Peru's largest federation of mining unions has called a walkout for June 30, and the country's leading confederation of workers plans a general strike for July 9.

Nonoy Lanatta, director of the nongovernmental organization Grufides, says the central government has failed to fairly share mining tax revenue with the provinces, especially poor ones that desperately need help.

Many poor towns where new mines or oil and gas wells are being built lack water, electricity, schools and hospitals.

"The state is totally absent in many provinces, and it only arrives once people start protesting," Lanatta said. "Mines are always beneficial for mining

companies, but mines don't always end up benefiting communities and towns."

My view - Resources booms for countries such as Canada, Australia and Norway have, in the past, resulted in governments ploughing much of the profits back into the country; raising standards of education and public services in the process. However in countries where a history of stable, good governance and democracy is lacking and often where huge inequalities exist between ethnic minorities and the ruling elite, the trickle down has been largely absent.

Many South American countries are relatively new to peaceful, orderly changes of government. New regimes are under enormous pressure to make the lives of their electorate better. Attracting inward investment brings much needed foreign capital into the country, but making sure that observable improvements are also being made to people's lives is difficult when government is weak in the regions remote from the capital; where resources are often situated.

With this background, we can expect continued interruptions to supply from countries such as Peru and Bolivia as well as a number of others around the world. This uncertainty is a support to prices for the metals and other commodities affected, as is currently the case with copper.

Copper is consolidating below the recent highs and would need to sustain a move below 350¢ to question scope for an upward break.

Today's interesting charts - Bond prices, yields, spreads and interest rates for a wide range of countries can be found in the Chart Library.

Euro Stoxx 50 Banks - breaking down from the medium-term range and needs to sustain a rally back above 300 to offset scope for some further downside.

India Nifty Index - breaks down from the medium-term range, following the Banks Index. It needs to sustain a move back above 4500 to question scope for some further downside.

US Treasuries - remains in a medium-term downtrend and would need to sustain a move above 115 to break the progression of lower highs.

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

"Could you be so kind to add Greatwall Motor HK: 2333 to the chart library also Epure International Ltd (EPUR) had a stock split a few month ago, could you reflect that (3 for 1) split in the Chart Library?"

My comment - Thank you for alerting us to this split which has now been corrected in the Chart Library. I have also added Greatwall Motors.

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

"Would you add the following to the chart library please?

"db x-trackers S&P Global Infrastructure ETF (Bloomberg Ticker [XSGI LN](#)).

"As always thanks for a great service."

My comment - Thank you for this suggestion which was already in the International Library but has now been added to the Global Indices and Funds section of the Chart Library.

Email of the day (3) - on an addition to the Chart Library:

"Thank you for your continued service and commentary.

"Could you please add [JSM Indochina Fund](#) at just under US\$1 a share to the chart library, this is a Vietnam closed-end fund.

"Many thanks"

My comment - Thank you for this suggestion, which has now been added to the Chart Library.

Last week's signups for the Free (Abbreviated) Comment of the Day - For the week of June 15th new signups, including subscribers and pre-subscribers, live in the following countries or regions: Australia, Brazil, Canada, France, Hong Kong, Iceland, India, Ireland, Italy, Japan, Netherlands, New Zealand, Sweden, Switzerland, Turkey, the UK and USA - 17 in total. In descending order, which topped the list in terms of the last week's new signups? It was the USA, the UK and Australia.

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

Tuesday 24th June 2008

Bernanke Plays 'Dangerous Game' Weighing Talk, Action - [Here is the opening of this topical item](#) from Bloomberg:

Federal Reserve Chairman Ben S. Bernanke, by voicing concern about inflation and the slumping dollar, has fanned investor expectations for an

interest-rate increase as soon as August. He may regret it.

Raising rates may exacerbate the economic slowdown and roil banks whose losses sent their stocks down the most in a decade this month. Forgoing a rate boost next quarter risks damaging the Fed's credibility and deepening its divisions. Already this year, three officials have dissented on rate decisions.

While Bernanke's warning that the Fed will "strongly resist" a jump in inflation expectations led traders to bet on a rate increase, economists are more skeptical. All 101 in a Bloomberg News survey said the Federal Open Market Committee will keep the benchmark rate unchanged tomorrow and most analysts this month predicted officials will stand pat until 2009.

"That's the dangerous game," said Scott Anderson, senior economist in Minneapolis at Wells Fargo & Co., the fourth-largest U.S. bank by market value. "Instead of putting the shot across the bow on inflation," Bernanke might have "held off a few more months to let the credit crisis heal a little bit more."

The Fed chief shifted stance after soaring costs of energy and imported goods threatened to stoke consumer price expectations. Gasoline climbed 37 percent in the past year, according to AAA. Import prices excluding petroleum rose the most since 1988 in the 12 months to May, government figures show.

Bernanke's Message

Bernanke said at a Boston Fed conference June 9 the risk of a "substantial downturn" in the economy had diminished and accelerating inflation "would be destabilizing for growth." The previous week, he said the falling dollar caused an "unwelcome" increase in domestic prices and the Fed was "attentive" to the problem.

There are widespread expectations among traders for a rate rise in the next three months: There are 36 percent odds of a boost in August and 93 percent in September, according to futures contracts on the Chicago Board of Trade. Economists in a monthly Bloomberg survey through June 11 projected the Fed will keep the rate at 2 percent this year, according to the median estimate.

The FOMC begins gathering today in Washington and will issue its statement tomorrow around 2:15 p.m.

My view - I maintain that Bernanke turned a bit hawkish with his statements in May because he could, following a 2-month stock market rally. Shades of November 2007.

The Fed Chairman and his colleagues find themselves in a high-stakes game of poker. Given a strong hand, in terms of the US economy, I am sure that they would choose to raise rates to underpin the dollar and combat inflation. Unfortunately, Bernanke and Co have a decidedly weak hand, although not entirely by chance, as they have contributed to inflationary pressures by

allowing money supply to expand rapidly for many years, as you can see from this long-term [chart](#) of M2.

However if we examine the M2 data on this shorter-term [chart](#), we can see a pause in *The Rake's Progress* commencing in the second half of March. With the Dow approaching its January and March lows, we should ask whether or not Bernanke is bluffing?

Probably, provided he is not being influenced by his critics. I would be very surprised if he raised rates anytime soon, despite being considerably more concerned about inflation today than at the January or March stock market lows. Nevertheless most of that inflation is from energy and food prices - global developments which cannot really be controlled by the Fed's monetary policy. However if I am wrong and the Fed does raise rates, I think the stock market would certainly fall further, quite probably contributing to additional economic weakness.

In attempting to navigate between the Scylla of inflation and the Charybdis of a weak economy, I do not think this is the time for Bernanke to turn hawkish in deed as well as word.

Prieur du Plessis: Sun Rising Over Japanese Stocks - My thanks to Prieur du Plessis for his [latest](#) in the Investment Postcards from Cape Town series. He quotes me in this issue but don't hold that against him. Here is the opening paragraph:

Scanning the globe for investment destinations can be a daunting task. When it comes to stock markets, however, relative strength analysis serves a useful purpose of highlighting under- or outperforming markets (or individual stocks) at a glance. Having perused a bunch of these charts, the Japanese situation stands out as being of particular interest.

My view - The technical data is certainly interesting, as Prieur points out. However international investors may wish to consider an additional timing question:

Can the Japanese stock market maintain its recent performance?

My answer is both yes and no, which requires an explanation.

I think Japan will maintain its relative performance, for the reasons mentioned by Prieur. However, at a time when global stock market sentiment remains fragile, I do not think that Japan's stock market indices can rally on their own.

While the Wall Street leash-effect remains negative, I would not expect any meaningful gains from Japan. However from a medium to longer-term perspective, I would regard a pullback as a buying opportunity.

Uranium to Fetch \$90 as Indian Reactors Drive Demand - My thanks to a subscriber for this informative [item](#) from Bloomberg. Here is the opening:

The uranium industry's worst year is about to collide with a nuclear construction program in India and China that rivals the ones undertaken during the oil crisis of the 1970s.

The result is likely to be a 58 percent rebound in uranium to \$90 a pound from \$57 now, according to Goldman Sachs JBVere Pty and Rio Tinto Group, the third-biggest mining company. Uranium plunged 57 percent in the past year as an earthquake damaged a Japanese nuclear plant that's the world's largest and faults shut down reactors in the U.K. and Germany.

Plans for India and China to end electricity shortages will ripple from northwest Canada to the Australian outback and the flatlands of Kazakhstan, the primary sources of uranium. India will start up three reactors this year, with another six due in 2009, in India, China, Russia, Canada and Japan. Uranium demand worldwide will rise as fast as oil this year, or 0.8 percent, Deutsche Bank AG forecasts.

“The first wave of growth is going to come from the emerging economies,” said John Wong, fund manager with CQS UK LLP in London, which has \$10 billion under management including \$150 million of uranium investments. “People are starting to look at coal, at gas, at oil and seeing the energy prices go up, they wonder about uranium.”

My view - Uranium was overhyped and the bubble burst just over a year [ago](#). The accidents mentioned above help to explain why prices have more than halved and remain weak today.

So will it recover? If so, when? What are the best ways to participate?

Among resources, uranium has probably been the biggest disappoint for investors over the last year. However the uranium power plants are being built so the companies involved are the most immediate financial beneficiaries. Two shares that we like are the French company Areva ([CEI FP](#)) and Japan's Toshiba Plant Systems ([1983 JP](#)) which owns Westinghouse. These two companies are the industry leaders and both show considerable strength relative to their national indices.

I agree with Goldman Sachs' view on the uranium price, although market timers may wish to wait for the first upturn in this market. The two uranium holding companies in the Library are Canada's Uranium Participation Corp ([U CN](#)) and the UK-listed Nufcor Uranium Ltd ([NU/ LN](#)).

Uranium mining shares are more speculative and may require patience. However the pure producers will probably do best when uranium is fashionable once again.

(See also Eoin's feature on uranium posted yesterday, including an informative report and a technical review of the shares.)

Email of the day - On inflation in Zimbabwe (my deletions to protect anonymity):

"I am a friend of #####, a struggling Zimbabwean coffee farmer and long time subscriber to FM whom you have met several times over the years. I thought you might be interested in a PS he added to an email sent on Sunday....

P.S. Went to the supermarket yesterday and filled a trolley. The bill came to \$1.2 trillion, for which I had to write 3 cheques as we are only allowed to write cheques up to \$500bn!!

"I was in Zimbabwe last May. Whilst there I bought a Chinese take-away for 3 people. It cost me a million bucks. About £8 at the time. When ##### was in the UK two weeks ago, he gave me a \$50,000,000 bill, valued at the time at £0.10!

"Written on the face of that bill is the following. "Fifty Million Dollars on or before 30th June 2008 for the Reserve Bank of Zimbabwe. Issue date 2nd April 2008. BEARER CHEQUE.

"I seem to remember that Molosavic started his terrible deeds when inflation hit 56,000% in the month before he started war. Do the historical charts on inflation / currency devaluation give any hint to the future direction and longevity of a rogue regime?"

My comment - I have no special insights on this subject but the situation in Zimbabwe remains tragic and is also worsening, with the Mugabe regime propped up by his cronies, including the generals. Hyperinflation is the most destabilising of accelerating trends and therefore unsustainable by definition. Unfortunately, colonial history, apathy and politics have prevented intervention by the United Nations, so far.

My personal portfolio: A gold trading profit taken; coffee long increased - While I remain a long-term bull of gold, with the price ranging at present I aim to do some buy-low-sell-high trading. Accordingly, this afternoon I sold an August position at \$894.45, against my purchase at \$883.45 yesterday. This reduced my gold futures longs by a third.

With a slightly better than breakeven stop protecting my coffee longs following last week's upside breakout, I increased my holding by 50% today, paying \$150.20 for another September position.

These prices include spread-bet dealing costs.

Please note - [I will be away from the office on Wednesday.](#)

Additional Commentary by Eoin Treacy

Martin Spring's On Target: Oil to Go to \$250...or Down to \$50? - [Thanks to Martin Spring for his ever informative letter which on this occasion focuses on energy. Here is a section on Coal Seam Gas:](#)

Coal deposits contain varying quantities of almost-pure methane, which is the main constituent of natural gas.

That "fire-damp" has always been a deadly threat to coal miners, causing explosions. But where it can be recovered, coal seam gas (CSG) - also called coal-bed methane (CBM) -- is a valuable substitute for natural gas. It already accounts for a tenth of gas supply in the US, and in Australia's coal-rich Queensland state, a quarter.

Boreholes can be drilled down to tap gas found in:
Coal deposits so gassy that they have been too dangerous to mine;
Deposits that have not been worked for other geological reasons;
Worked-out and abandoned coal mines.

Currently the focus of greatest excitement over methane is Australia, beneath which lies almost one-tenth of the world's coal reserves.

A bidding war drawing international oil/gas giants is under way for ownership of that nation's resources of coal seam gas (CSG).

They are particularly attractive. They are vast in scope. They're located in a country with stable government and business environment. And they offer proximity to Asia's high-growth energy markets, which already take two-thirds of global shipments of liquefied natural gas (LNG).

The world's first plants for liquefying coal seam gas are now under construction on the Queensland coast. They will draw gas by pipeline 400-odd kms from inland coalfields, converting it into some 11 million tons of gas a year for shipment to Asian buyers.

To put that figure into perspective, it's more than half as much liquefied natural gas as Australia already exports, and equivalent to 5 per cent of current global shipments of LNG.

Motivated by rising prices and paucity of cheap onshore natural gas reserves, Australia has moved aggressively into exploitation of the gas in its coalfields.

Production of CSG has expanded ten-fold over the past seven years. Australia, claims EnergyQuest CEO Graeme Bethune, has moved from being "a rank beginner to a world leader" in CSG recovery technology.

My view - Extracting gas from coal beds has been a topic of interest for those concerned with alternative supplies of energy for some time, but it was unviable until recently because of high costs. Rising demand and a willingness to invest in long-term projects are changing the industry. Demand for natural gas globally is projected to continue to grow aggressively in the coming decade, which is helping to change attitudes as to what types of reserves can be accessed.

Companies in this sector have already experienced a re-rating in the eyes of investors and many have accelerated in the last few months. They now appear to be consolidating gains and are probably best bought following reactions.

Origin Energy is currently the subject of a hostile bid by BG Group and broke upwards to a hit a new high today. It would need to sustain a move below AU\$14.57 to question scope for some further upside.

Santos almost doubled in the last three months and was looking somewhat overextended when it encountered resistance near AU\$22. It needs to sustain a move to new high ground to reaffirm the overall uptrend and offset scope for a further consolidation of recent gains.

Queensland Gas is more volatile than either of the companies profiled above. It doubled from the March lows before posting a downward dynamic at the beginning of June, it has since found support near AU\$5, but needs to sustain a move to new high ground to offset scope for some further consolidation of recent gains.

Arrow Energy also doubled and would need to sustain a move below AU\$5 and back into the year-long range to question scope for some additional upside.

Metagasco broke upwards in early June but was unable to sustain the move. Given the size of the failed break, a retest of the lows near AU\$0.8 seems likely. A sustained move above AU\$1.20 would be needed to question this thesis.

Sapex broke to new high ground in May and accelerated to a high near AU\$0.70, where it is currently consolidating. It needs to sustain a move to new high ground to offset scope for some further consolidation of recent gains.

Molopo Australia accelerated in a spectacular fashion in early 2007 before topping out near AU\$1.75. The ensuing downtrend retraced most of the advance before bottoming early this year. It broke the progression of lower highs in March and quickly rallied back towards the highs. The share broke upwards earlier this month and the upside can be given the benefit of the doubt as long as it can sustain the move.

All of these shares have sustained impressive moves which have coincided with the advance of oil and natural gas. They may be at risk of a more lengthy consolidation in the event that the energy complex enters a medium-term

correction. However, this could be viewed as buying opportunity for a number of energy related companies when it eventually occurs.

Email of the day - on LNG supply:

"This is one area through a lot of political posturing needs to be placed in balance. The new provinces off NW Europe have great promise to counter Russia supply (Irish NWCS had Calgary company who did work for some clients pick my brain on this as we know from Rockall west there is great promise) .

"Blaming the Democrats doesn't get needed LNG projects going. I feel the industry has sold the concept very poorly to the public. Seems Middle East and SWFs 'rule' as the US has to start thinking about the Colorado Shale and deep water Miss. Canyon off Gulf and bringing Eastern Canadian LNG deposits under a 'continental energy framework.'

"Alberta economy slowing on energy side but spoke to friend on infrastructure construction and it is still very buoyant- can't get qualified people to work in province.

"In time, a NAFTA/EU bloc imho if energy projects don't play catch up, could be a possibility in the next 30 years, to balance economic growth just in energy (was suggested to and with cynical sneers in Houston 2002 although few even T Boone Pickens said Friday, here in Calgary on a Q&A this 'it may be time to re think this area-maybe a strong North Atlantic energy bloc is the way to go') in BRIC and the LNG/NG kings as you know are the Russians. By pooling syndicated capital, great economic growth will occur if everyone can get their heads out of the politics.

"Ironic this, just thought I'd pass it on, and got enough staring for posing the question that day."

My comment - Thanks for this update on the LNG market. Given the costs of putting LNG installations in place and the dominant position Russia occupies, some joined-up-thinking is needed in how best to meet the needs of Europe and North America. I do not think that the idea of a North Atlantic energy arrangement is unreasonable, but a great deal of negotiation would need to take place to make it happen. Perhaps a full blown energy crisis would spur politicians to take such an idea seriously but it is unlikely in my view in the absence of such an event.

Deutsche Bank Asia Economics Special: India's Inflation Problem - Thanks to a subscriber for this short [report](#) by Sanjeev Sanyal dated June 20th covering India's inflationary problem. Here it is in full:

RBI likely to respond aggressively to inflation spike
The rate of wholesale price inflation jumped to 11.1% yoy in the first week of June. Most observers (including us) had been expecting the inflation rate to

jump to around 10% on the back of a hike in administered fuel price hikes. Therefore, the actual reading would have come as a surprise for both financial markets and policy-makers. Energy prices are rising but other categories are also seeing spiraling prices. Non-food primary articles registered inflation of 16.3% while that for manufactured goods has jumped from 4% at the end of 2007 to 9% in early June.

As we have been arguing in recent months, India has an inherent inflation problem that is being fed by domestic factors. First, the government has opted for aggressive fiscal expansion ahead of national elections including debt-forgiveness for farmers, rural employment generation schemes and generous pay increases for the public sector. Second, we feel that the country is now suffering from increasingly severe supply-side constraints. In our view, the supply-side constraint is partly the result of five years of very rapid economic expansion and partly of a palpable slowdown in the government's reform efforts.

The larger-than-expected jump in inflation will add to the concerns of an already worried Reserve Bank. We now expect an additional 50-75bps worth of hikes over the next six weeks. These may be accompanied or followed by increases in the cash reserve requirement. Furthermore, the Reserve Bank would resolutely defend the exchange rate from depreciating further. It has a large pile of foreign exchange reserves and, we feel, would look on this as a good time to use it.

My view - In any democracy, the incumbent party will always manipulate policy in an election year in an attempt to curry favour with the electorate. India is no different. However, the central bank has stated clearly that it wants to keep inflation under control. This was illustrated on June 10th with the 25 basis point hike and today with [50 basis points](#). The tightening of lending standards and rising interest rates are headwinds for the stock market. Here is a section from a story by Cherian Thomas and Anil Varma for Bloomberg on today's announcement:

India's central bank raised interest rates for the second time this month and asked lenders to set aside more money as reserves to cool inflation running at a 13-year high.

The repurchase rate was lifted to 8.5 percent from 8 percent and the cash reserve ratio to 8.75 percent from 8.25 percent, the Reserve Bank of India said in a statement issued in Mumbai today. The move comes after the central bank increased its repurchase rate by a quarter percentage point to 8 percent on June 11.

Governor Yaga Venugopal Reddy is under pressure from the finance ministry to tighten monetary policy to rein in inflation, currently at 11.05 percent. That will further hurt consumer and investment demand and threatens to derail India's record 8.8 percent economic growth since 2003, the fastest after China among the world's major economies.

“A tight monetary stance will have to continue for another year to slow inflation to the desired level,” said Rajiv Kumar, a former policy adviser in the finance ministry between 1992 and 1995 who is now the director of the Indian Council for Research on International Economic Relations. “Growth could come down to as low as 6.5 percent by 2010.” He spoke before the central bank’s rate announcement.

With general elections scheduled to be held in less than a year, Prime Minister Manmohan Singh wants to control prices in a country where more than half the population of 1.1 billion live on less than \$2 a day.

‘First Line’

Finance Secretary D. Subbarao said on June 21 that monetary policy is the “first line of defense” as the government tries to rein in prices before elections by May.

“High prices will most definitely result in aggressive monetary tightening, even at the cost of lower growth, making things all the more unenviable for the government,” said Rohini Malkani, a Mumbai-based economist at Citigroup Inc. “With inflation likely to remain at elevated levels for the rest of the year, political parties have started positioning themselves for the next elections.”

India’s inflation rate has almost tripled this year, eroding the popularity of Singh’s ruling Congress party, which lost ground in nine of 11 state elections since January 2007.

India “will continue to take determined and calibrated measures as and when warranted,” Reddy told reporters in the western city of Pune on June 23. Bonds gained after Reddy’s comments on optimism the central bank will rein in prices.

The [Rupee](#) has is also being used as a tool to control inflation. The authorities started to allow the Rupee to appreciate in [2002](#), following more than two decades when it was a congenitally weak currency. It now appears to have entered a new secular bull market. The Dollar found support against the Rupee in Q1 and rallied impressively during May, but encountered resistance near R43. It would need to sustain a move above that level to question scope for a renewal of Rupee strength.

With inflation to the fore and with politicians apparently willing to sacrifice some growth, the Sensex is much more closely approximating the performance of Western stock markets, most affected by the credit crisis. The [Sensex](#) broke below the March [lows](#) last week and needs to push back above 15,000, promptly, to offset scope for some further downside. The [Bombay Banks](#) Index has been a leader throughout the current malaise and is worth keeping an eye on for signs of recovery.

Mineweb.com: Indium prices expected to explode due to LCD demand - [This article](#) by Pratima Desai for Reuters covers the potential increase in an other

minor metal. Here is section:

Most people could list a host of reasons why prices of computers, televisions and mobile phones are rising, but few would be able to pinpoint indium.

Having languished below \$500 a kg for the first four months of the year, indium prices jumped more than 60 percent to \$700 a kg at the start of June.

Prices have since slipped to about \$650 a kg, but are expected to head higher and the chances of the silvery-white metal revisiting records above \$1,000, possibly before the end of the year, are now much higher. Behind the rise are accelerating demand from the electronics industry for liquid crystal display and flat screens, stagnant supplies, the threat of strategic stockpiling in China and investment demand.

"There just isn't enough material to feed what is really quite a voracious LCD machine, which needs ever larger amounts of indium," said Douglas Hunter, a director at UK-based minor metals trading firm Wogen Resources.

"The flat panel industry is increasing production at 25 to 35 percent per annum."

A thin uniform film of indium-tin oxide on glass creates a unique optically transparent electrical conductor for LCDs.

To illustrate demand growth for LCDs, particularly in Asia ahead of the Beijing Olympics, is Korea's Samsung Electronics which is planning to invest 2.74 trillion won in a new LCD line with Japan's Sony.

My view - The minor, or high tech, metals are some of the best examples of the Supply Inelasticity Meets Rising Demand theme. [Indium](#) bottomed out in 2002 and exploded upwards between 2003 and early 2005, before losing momentum. Over the course of the next two years it gave up more than 50% of its value before finding support once more near 500 in February. It has yet to break the progression of lower highs but would need to sustain a move below 500 to question potential for at least some further higher to lateral ranging. .

Today's interesting charts - The Chart Library has in excess of 17,000 instruments which may be of interest to subscribers.

Japanese Yen per 1 Euro - breaks [upwards](#) to a new 11-month highs and would need to sustain a move below ¥167 to offset scope for some further upside.

Brazil - finds at least short-term [support](#) near the prior highs and the reaction is looking somewhat overextended. However it needs to break the progression of lower highs to indicate that the bulls are regaining the upper hand.

S&P 500 Banks - looking slightly steadier following overstretched decline, but needs to put together more than one day on the upside and needs to break the short-term downtrend to offset scope for further weakness.

Wednesday 25th June 2008

Commentary by Eoin Treacy

Warren Buffett Says Sell to Me, Not 'Porn Shop,' as Growth Dips - [This article](#) by Richard Teitelbaum for Bloomberg covers an interesting dichotomy between companies with cash for acquisitions and those still reliant on access to cheap capital. Here is a section:

Warren Buffett is in Toronto, fielding questions from a crowd of 300 executives. One asks what makes people want to sell their companies to him.

The Berkshire Hathaway Inc. chief executive officer replies that he tells a prospective seller to think of the company as a work of art.

"You can sell it to Berkshire, and we'll put it in the Metropolitan Museum; it'll have a wing all by itself; it'll be there forever," he says at the February meeting. "Or you can sell it to some porn shop operator, and he'll take the painting and he'll make the boobs a little bigger and he'll stick it up in the window, and some other guy will come along in a raincoat, and he'll buy it."

Buffett, 77, can afford to throw a little mud on his competitors in the private equity industry. Wall Street's acquisition machine has seized up, while Buffett, in the valedictory chapter of a career stretching back more than 60 years, is on a buying spree.

He has \$35.6 billion in cash to spend, and he's looking for companies that he can buy at a reasonable price, that have experienced managers he trusts, products with strong market positions or other competitive advantages.

Buffett's biggest catch so far in 2008 was Marmon Holdings Inc., a conglomerate owned by Chicago's Pritzker family. On March 18, Berkshire announced it had bought 60 percent of Marmon from the Pritzkers for \$4.5 billion. Buffett is buying the rest in increments during the next five to six years.

My view - Only a few years ago Warren Buffett commented that he couldn't see much value because private equity firms had bid up the prices of potential targets. He has a lot less competition today, as a result of the credit crisis, and prices have fallen considerably.

Mergers and acquisitions are being driven today by companies with plenty of cash on their balance sheets. This is true of Berkshire Hathaway, but also of the mining sector which continues to lead the world in terms of M&A activity this year. Considering the competition for world class assets in politically stable parts of the world and the relative scarcity of such companies, this trend is likely to continue.

Email of the day (1) - [on the S&P 500 and what to do next](#):

"I follow up with a preceding email where I expected a failure on the MA200 for the SP500 (the history is rhyming).

"But the concern here is, of course, what's next. Do we have to sell, to short, or to wait and buy the upturn?

"You are keeping a relatively positive stance and, if I understand correctly, are advising not to be "bearish" now.

"Given my admiration towards Fullermoney I can afford to be a little provocative here, and would like to share the following thoughts:

"Is the market oversold? For the short term, I do not know what "oversold" or "overbought" really are. They may only be psychological views, unless some divergence between the prices on one side, and volume or breadth on the other, can be noticed. I don't see any so far.

"Longer term, we have currently a downtrend on the weekly charts and, of the 9 indicators I follow, 6 are bad, 2 are steady after having trended down, only one is still OK (short term rates).

"Next, we have the sentiment indicators, which are saying clearly that we are not at a top. But regarding a bottom they sometimes lead the market by a fair amount of time, and currently, the figure from Investors' Intelligence is not as bad as it was last March. It is at the January level, before a painful plunge.

"The last time I wrote, the Gallup poll on the general mood of the economy was showing 19% "satisfied" -all time low- and I took it as a positive sign.

"Now it is 14%. Even better? I don't know.

"We can see that today, every single professional investor try to be a contrarian. In addition this professional crowd is always right during a period a time, since it creates the trend. But while the crowd is working, if we really want to see a bottom, we have the option to take all its opinions as contrarian signs. What I am writing right now can be seen as a contrarian indication if you are in a bullish mood. Each new statement about the risks the market is facing can be seen as a positive sign...or a negative one, depending on your mood, or on your book.

"So the reading of a sentiment indicator, or of the headlines, per se, may not be enough and should be completed by some very clear indication that the bearish trend is over. I do not see this, but I may be wrong.

"Finally we have the March bottom. We can think that as long as this bottom holds, we have to give the upside the benefits of the doubt. But this bottom is still far away and a lot of money can be lost or made before we know if we go under the bottom or if it holds. Like at the poker table, we have to pay to

check. But I wonder if there is really a difference between this and a plain buy-and-hold strategy. If we think that it is too late to sell now, what will we do when the March bottom is busted? Hold, in the name of value investing?

"To sum up, I have the impression that everything, TECHNICALS INCLUDED, is telling to be bearish, the only reason not to listen being that it is too clear.

"Maybe who is following the obvious is the true contrarian today...

"I am pretty much a student of the markets and my purpose here is more to understand better and have your ideas than to challenge your views."

My comment - Thank you for this thoughtful and informative email. You are correct that the Investors Intelligence indicator is not at as low a reading now as it was in March, but it is getting into severe oversold territory. By oversold or overbought we mean that it is reflecting an extreme of sentiment which is unlikely to be sustained beyond the short-term. Presently, bears have no reason to change their minds about the direction of the S&P. It could break to new lows and sentiment could get even more bearish. However, the temptation is to get increasingly bearish in line with sentiment and that is usually a mistake.

We have forecast for a number of months that the convalescence of the S&P 500 will be lengthy and so far this has been borne out. The failure to break back into the overhead trading range in mid-May was a further indication that the recovery will take time. (Also see Comment of the Day on [May 7th](#)).

One of our main concerns is the weakness of the banking sector. The [S&P 500 Banks](#) Index led on the [downside](#) and remains in an overall downtrend, with a progression of lower highs. The Index has been falling on almost consecutive days since May and the last two days are the first two consecutive days on the upside in that timeframe. Today's weak close will not instill confidence and it needs to rally above 200 to break the short-term downtrend. The general health of the banking sector is a bellwether for the wider market. If the Banks at least stop going down, a headwind to sentiment will have been removed.

The [S&P 500](#), having failed to break upwards in [May](#), is now testing the January and March lows. The [Dow Jones](#) is currently testing its lows and the [Nasdaq 100](#) remains substantially above its lows.

To take your questions in order: Is it time to sell? Speaking for myself, I believe it is too late to sell now, Sentiment is deteriorating and we are in region of prior lows, so there is the potential for at least a short-term rally. For our view to be correct, the market needs to hold at or above the January / March lows and remain in the overall ranging pattern. Any downside break needs to be retraced quickly; otherwise another downleg is a possibility. If we are wrong and the current consensus view, that the period from the January lows to now, was a distribution within a developing downtrend, is correct, then you would be justified thinking about selling part of your position and more into

a future rally. For that view to be correct, the market needs to sustain a move below the January / March lows.

Is it time to short? Again, I think that this not the right time to short, as the S&P 500 and Dow are both in regions of prior support. I believe that those who are already short will have lowered stops in advance of the test of these lows.

Is it time to wait? I believe it is. Stock markets are volatile and I have no qualms about saying it is difficult to make money in the current environment. A war is going on between supply and demand and at present the bears have temporarily got the upper hand. On the charts, I believe arguments are more evenly weighted.

Is it time to buy? Trading opportunities will exist when the market bounces, whenever that occurs. We have seen over the last five-months that at the upper side of the range sentiment is more sanguine and at the lower side it is extremely bearish. As long as the current ranging activity continues, we can expect these sorts of mood swings. The Nasdaq has outperformed the other main US indices and is probably the best recovery candidate if the Dow and S&P bounce.

The bigger question is whether one wants to be in the S&P or Dow at all right now. The best case scenario for the coming months is the potential for a rally towards the upper side of the range. Given this prognosis they are lagging in the global beauty contest. A number of resources markets are outperforming in the current environment and should continue to do well and even better when sentiment improves. A number of Asian markets are also potentially stronger recovery candidates.

China Life Buys Funds, Signaling Market's Bottom, Journal Says - Thanks to a subscriber for this short article by Josephine Lau for Bloomberg detailing some renewed interest in the Chinese stock market. Here it is in full:

China Life Insurance Co. has been snapping up "large quantities" of open-end stock funds, a move that signals the end of China's equity market slump, the China Securities Journal reported, citing unidentified people.

Chinese insurers have been following China Life's lead in buying index-linked funds, boosting optimism that Shanghai's key Composite Index may rebound at about 2,800 points, the state-owned newspaper said, citing analysts without naming them.

The move by China Life, the country's largest insurer, is significant because of its bellwether size and its influence in the industry, especially its tendency to undertake large-scale purchases, the newspaper said.

Sales of China's stock funds may be bolstered, reversing an equity market slump that had limited the new funds this year to 1 billion yuan (\$145.6 million) each, the newspaper said.

My view - Signals have been increasing that the Chinese market is entering a bottoming out phase, prior to being able to sustain the next meaningful rally. The lowering of stamp duty rates triggered the important rally from 3000 in April. Allowing new open-ended funds and slowing the issuance of new shares are measures also aimed at supporting the market. If domestic institutional investors are again returning to the market, this can also be taken as a positive.

The [Shanghai Composite](#) topped out near 6000 late last year and began to find [support](#) in the last few months having declined more than 50%. This percentage decline coincided with the government measures to support the market. The downtrend is losing momentum, but needs to push back above 3000 to break back into the last range and above 3750 to break the progression of lower highs, to indicate that the bulls are regaining the upper hand.

Email of the day (2) - on corn and wheat:

"My weather maps are showing another big rain event coming for some of the wettest areas over the next few days. It looks like E. Iowa could get over 4 ins. My contacts say that corn and beans are in far worse shape than most people think. Many reports of corn 6 to 10 ins. tall, not waist high as it should be, and beans 1 to 2 ins. tall or "barely visible". The satellite imagery for vegetative health shows that E. Neb. , S.Dak. , N.Dak. , Mn. , Ia. , Il. , and parts of Ind., and the N.Delta are in extreme stress. Ironically I have only seen this stress as a result of severe drought, not floods. The crops are so late , that if frost occurs at a normal date this year, it could cause substantial losses to an already severely damaged crop.

"Earlier this year I predicted that God would punish us for turning food into fuel. Normally He makes a mockery of my predictions, but it looks like this time We are on the same page.

"Best regards,"

My comment - Thank you for this informative update on the corn and soybean crops in the US Mid-West. [Corn](#) jumped by more than a third between June 1st and 16th, and finally encountered resistance near 800¢ when the rains stopped. It has since moved into a relatively orderly consolidation of those gains. As a result of the spectacular advance earlier in the month, the [weekly](#) chart is looking overextended. However, since the grain has been able to sustain most of its advance and has not been limit down on any day following its high at 791¢; it could still advance further if more bad weather affects the crop. A move below 700¢ would indicate that sentiment was turning more optimistic on the health of the crop.

[Soybeans](#) also rallied earlier this [month](#) but not to the same extent and encountered resistance near the March highs close to 1600¢. It is currently consolidating below that level and would need to sustain a move below 1400¢ to question potential for an upside break.

Email of the day (3) - [on coal contracts](#):

"Could you explain the difference between coal NX1 and QZ2 as shown in the chart library and would you agree that the strength of coal is having as much of an influence on inflation as oil ?"

My comment - The [NX](#) contract is listed on the European Energy Exchange while the [QZ](#) contract is listed on NYME.

I would not agree that coal is having as inflationary an effect as the high price oil. No one uses coal in their cars and it is a thinly traded futures market, nor does it feature in the official calculations of inflation used by governments, to the best of my knowledge.

Coal remains an important source of energy for power stations globally and coking coal is in high demand from the steel industry. Coal represents another iteration of the Supply Inelasticity Meets Rising Demand theme and probably contributes to inflation in the higher cost of power but not to anything near the same extent as oil.

Please Note- [David is away today but will return tomorrow.](#)

Thursday 26th June 2008

More Rain Soaks Missouri, Adding to Midwest Flooding - [This article from Bloomberg](#) is relevant to yesterday's informative email on this subject. Here is the opening:

New rains in Missouri have delayed the expected crest of the Mississippi River until June 29 and pushed it a foot higher than originally forecast.

Up to 8 inches (20 centimeters) of rain fell in central Missouri overnight and drained into the Missouri River, which meets the Mississippi just above St. Louis. The new influx means the Mississippi will now crest at about 38.7 feet in four days, rather than today, and will be 8.7 feet above flood stage, said Nicole Dalrymple, spokeswoman for the Army Corps of Engineers in St. Louis.

"It does look like the forecast has been altered a bit," Dalrymple said by telephone. "The rain has extended the crest arrival."

In addition, northeastern Missouri received 2 to 5 inches of rain overnight, and that went directly into the Mississippi, National Weather Service meteorologist Ben Miller said by telephone from St. Louis.

A flood "bulge" has moved down the Mississippi from Wisconsin and Iowa into Illinois and Missouri over the last two weeks, bursting more than a dozen levees and flooding more than 3.4 million acres, most of it cropland, in an area about five times the size of Rhode Island. At least 24 people have died as a result of the flooding and bad weather.

Missouri has entered a "dangerous" period because many of the earthen, agricultural levees that hold the river back have been soaking in high water for more than a week, said Alan Dooley, spokesman for the U.S. Army Corps of Engineers in St. Louis.

My view - The latest rains are adding to an already serious situation, with implications for global food prices.

In the years of bumper crops, it was not an exaggeration to say that the USA played an important role in feeding the world. The unfortunate probability this year is that US [corn](#) and [soybean](#) yields will be significantly reduced. Even if drier weather occurs shortly, as one would normally expect, crops with shallow roots due to today's excessive moisture will be at risk if the very hot and dry weather normally experienced from mid-July to early August returns this year. Autumn frost may be an even greater threat to crops planted later than usual due to excessive rain in May and June.

Email of the day - On a report and colourfully named "signal":

"I have been a subscriber for some time now, fully enjoy your service and the commentary. Very insightful. Any chance that you might have a copy of the RBS report mentioned 18th June 2008?"

"I also wanted to ask about your opinion on the Hindenburg Omen that seems to have occurred last week (according to some newsletter services that I subscribe to). Thanks and keep up the good work!"

My comment - Thanks for the feedback.

I did not see the RBS report, although we got the gist from press comment and on the 18th I did post an [article](#) from the Telegraph which discussed it.

I have no opinion on the "Hindenburg Omen", other than it is a great title, worthy of Hollywood. At the moment, I think stock markets have more obvious problems to worry about, not least the spike in energy and food prices.

Investors Intelligence's Advisors Sentiment - This [indicator](#) provides a unique insight.

My view - What does it tell us?

Oversold readings of this magnitude have always coincided with market bottoms of at least near-term significance. Could it be different this time? That is always a possibility, because the fundamental background is never the same, but it is probably not a good bet.

Given Wall Street's continued weakness, it would take a rally tomorrow and early next week to prevent an even more extreme reading when this important sentiment indicator is next updated.

Meanwhile, of the many headwinds buffeting stock markets, [crude oil](#) is probably the most important. A sustained break above \$140 would reaffirm the uptrend for crude and certainly be bearish for most global stock market indices. A close beneath \$120 remains necessary to confirm a peak of medium-term significance.

Additional Commentary by Eoin Treacy

Which country indices are leading the world over the last three months? - We have long exhorted subscribers to view the investment world as an international beauty contest where they can pose as the judges. In the current environment, with many developed market indices, at best ranging and at worst breaking below their January / March lows, it might be useful to know which indices are leading global stock markets.

To find this list, I went to the Chart Library and put all of the country indices in the world into a section in my Favourites. I then went to the Filter function and imported that section. (Please see the Filter Help Pages for instructions on how to do this). This gave me list of every country index in the world. I then sorted it by 3-month performance.

This initial [list](#) is in local currencies which is useful for those of us with access to spread-betting accounts because there is no currency risk involved. As an example of the difference currency can make, Zimbabwe came top of the list, because of the country's rampant inflation and imploding economy.

African and Middle Eastern markets currently feature highly on this list because they are relatively uncorrelated with Wall Street. For example, Ghana (2), Lebanon, (3), Qatar (4), Jordan (6), Tunisia (9), Oman (11) and Kuwait (13). However, these are also relatively shallow pools of liquidity and are easily influenced by a small number of large funds active in them. While the growth story for many of these markets is a strong one, they are also at risk of extremely sharp corrections, when investors seek to withdraw funds. Anticipating a high is necessary in such markets, because liquidity can disappear when they begin to sell off aggressively.

Of more significance is the continued strength of a number of resources markets in local currencies with Norway (5), Russia (7), Chile (10), Canada (15) and Brazil (16). These are larger liquidity pools and are leading the advance for markets easily accessible by international investors. Given the secular nature of the commodity advance, these markets should also do well over the long-term.

Here is the same list, but with the [US Dollar](#) as a common base currency. On this list we see that Zimbabwe is at the bottom, where one would expect it in the current environment. With a uniform base currency, investors in funds denominated in that currency have a better idea of where the best returns have been found over the last few months. (As an aside, this function can also be used to evaluate the relative performance of various funds denominated in different currencies.)

On this list we see that Middle Eastern and African markets continue to figure highly but resources dependent markets have moved up the ranking significantly. Norway is now 4th while Brazil is 6th and Russia remaining at 7th. These markets are outperforming in absolute and relative terms and across a range of currencies.

On the first list Japan is ranked 14th in performance over the last three-months, but when adjusted for the Yen's weakness it slips to 37th. This primarily indicates that the weakness of the Yen is an important factor for the Japanese stock market but also illustrates that those interested in taking a medium to long-term position would be well advised to consider some sort of currency hedge.

Also of interest is the performance of the Nasdaq, which is clearly the best performing of the major US indices. Over the last three-months, it is ranked 15th of 85 markets, in US Dollar terms. While its actual performance lags that of the leaders globally, in relative terms, the Nasdaq has been a safe haven for US Dollar investors. Once sentiment improves, the outlook remains positive for it continue to outperform both the Dow (55) and the S&P 500 (41).

(Please Note - It is also possible to use 10 other major international currencies as bases for analysis using the Filter system.)

Tomorrow, I will look at how the best performing stock markets measure up against, commodities and bonds.

Eoin's personal portfolio: Treasury stopped out at a loss. Corn and soybean longs opened - My speculative short in [US Treasuries](#) was stopped out this afternoon at 114.35 against my sale on Tuesday at 113.35 for the September contract.

I also opened longs in [corn](#) and [soybeans](#). These were at 753.5¢ and 1529.25¢ for September and November contracts respectively. All prices quoted include spread-bet dealing costs.

Mineweb.com: The kings of iron ore get record prices - This [article](#) by Barry Sergeant covers the pricing power of iron-ore miners and contains a comprehensive list companies involved in this area. Here is a section:

Rio Tinto's record settlement for benchmark iron ore annual contract prices, announced this week, is akin to oil prices instantaneously moving up to \$270

a barrel, or gold bullion jumping in a jiffy to around \$1 800 an ounce. Unlike oil, gold, and other well known commodities, most iron ore trades under contracts, where major counterparties negotiate annual changes, if any, in prices.

Vast amounts of iron ore go mainly by rail to inland markets; much of that tonnage, in turn, is subject to long term prices that may be State influenced. The more visible and decidedly free seaborne market is dominated by Vale, Rio Tinto, and BHP Billiton, three names which also rank as the three most valuable mining stocks in the world. While each stock is classified as diversified, bulk commodities comprise the majority of each stock's current value: iron ore, coal, base metals (dominated by copper and aluminium), and other bulk commodities and metals.

BHP Billiton also operates an oil and gas division, bulk commodities which currently trade at infamous levels. But where oil and gas prices have been on the move for years and recently peaked (for now), base metal prices first peaked as early as 2006. Iron ore and coal prices have been laggards, in a sense, during the commodities upcycle, in place since early 2002. In the past 12 months, where oil and gas prices have risen between 80% and 105%, benchmark Appalachian coal prices have risen by 157%, underpinning a substantial and ongoing revaluation of listed coal stocks across the world, possibly with the exception of overheated Chinese equity markets where corrections continue across all sectors.

Iron ore prices started to move during 2004, after more than two decades of trading in a churning band between USD 0.22 and USD 0.40 per metric ton unit (mtu). The individual pricing of iron ore products differentiates chiefly between lump and fines, with lump trading at a premium to fines. Iron ore prices roared upwards in 2005, but the 2008 settlements are unprecedented both as to value and also percentage escalation. In its announcements this week, Rio Tinto said its 2008 fines prices had been raised by 79.9% year-on-year to USD 1.4466/mtu, while its lump was up 96.5% to USD 2.069/mtu.

My view - Pricing power is something other sectors would kill for. When one contrasts the ability of miners such as Rio Tinto and BHP Billiton to raise prices compared with a company such as Vodafone, I know where I would rather be invested.

Volatility in the price for a number of the major mining stocks has accompanied moves to significant highs in the last year. [Rio Tinto](#) accelerated upwards following the BHP Billiton bid, only to give up almost the entire advance in January, before surging to new all time highs near 7000p. It has since given up some of the advance and is currently pushing back into its previous range. It needs to sustain a move above 6000p to give a clear indication that the bulls are regaining the upper hand.

[BHP Billiton](#) has a similar pattern to Rio Tinto above and needs to push back above 2000p to indicate renewed bullish dominance.

[CVRD](#) has a more evident progression of rising lows than either of those profiled above. The failed break above BR65 has resulted in the share pulling back to the first area of potential support near BR55. A sustained move below BR50 would be needed to indicate that a lengthier correction is unfolding.

Worries about a global recession are having an impact on sentiment regarding these shares. However, the pricing power available to them is tremendous and sooner or later this will be appreciated by investors once more. As in the past, these shares have been best bought following reactions and this case is unlikely to be any different.

Coffee Climbs to Three-Month High on Lower Exports From Brazil - [This article by Shruti Date Singh for Bloomberg covers some of the reasons behind the recent surge in coffee prices. Here it is in full:](#)

Coffee rose to the highest price since March after shipments slowed from Brazil, the world's biggest producer, where the harvest trailed last year's pace.

Exports of arabica beans in June through yesterday fell 19 percent from a month earlier, data from Brazil's Coffee Exporters Council show. Growers have harvested 5 percent to 8 percent of the crop, compared with as much as 18 percent a year earlier, Brazil's Guaxupe Region Coffee Cooperative, the world's largest coffee cooperative, said yesterday.

"The lack of selling is helping a lot" to support prices, said Marcio Bernardo, a broker with Newedge USA LLC in New York. Coffee futures for September delivery climbed 2 cents, or 1.3 percent, to \$1.5035 a pound on ICE Futures U.S., the former New York Board of Trade. Earlier, the price reached \$1.515, the highest for a most-active contract since March 14.

Most-active futures have increased 35 percent in the past year, including a 1.3 percent gain yesterday.

This year, Brazil will harvest 51.1 million bags of beans, up from 37.6 million last year, because trees are in the higher-production period of a biennial crop cycle, the U.S. Department of Agriculture has forecast. A bag of beans weighs 60 kilograms (132 pounds).

The potential for cold air coming into Brazil's coffee- growing region also continues to support futures, Bernardo said.

Weather 'Premium'

"Even though there is no risk of frost, because it's cold weather, the market has a premium," Bernardo said.

The threat of a frost or freeze affecting Brazil's coffee trees runs from June 1 into the first week in August, with the highest risk from June 21 through July, according to Joel Burgio, a Meteorlogix LLC forecaster in Woburn, Massachusetts.

While temperatures may be slightly below normal in the next few days, the forecast doesn't call for damaging cold, Meteorlogix said today.

Arabica beans, the main variety traded in New York, are grown mostly in Latin America and used by specialty coffee companies including Starbucks Corp. Robusta beans are used in instant coffee and are grown chiefly in Asia, Brazil and Africa.

My view - [Arabica coffee](#) accelerated to \$170 in March and experienced a severe downdraft in common with a number of other commodities at that time. It has since found support near \$130 and continues to have a sustained progression of rising major reaction lows over the last four years. The break above \$140 signalled that the bulls have regained the upper hand and Arabica would need to sustain a move below \$145 to question scope for some further upside.

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.

Dow Jones - breaks [below](#) the January and March lows and needs to sustain a move back above 12,000 to offset scope for some further downside.

Gold - [rallying](#) from the lower side of the three-month range and would need to sustain a move below \$875 to question scope for at least a test of \$950.

Oats - breaking [upwards](#), having consolidated well in the region of the prior high. A sustained move below 425¢ would be needed to question scope for further upside.

Friday 27th June 2008

Caroline Baum: Fed Should Run Policy, Outsource Communications - [This is an interesting article](#) by the Bloomberg columnist. Here is a good section on differences in the USA today, compared to the 1970s:

Then there's the issue of inflation expectations, which are more of a concern to policy makers than consumers.

Lower Living Standard

“In previous cycles, consumer expectations about their financial well-being did not collapse when inflation went up,” said Neal Soss, chief economist at Credit Suisse. This time around, according to the Reuters/University of Michigan Survey of Consumers, rising inflation expectations are being met with “a collapse in expectations about their own financial futures, suggesting consumers don't expect to be compensated for higher prices with higher wages,” Soss said.

Consumers' inflation expectations one year out rose to a 27- year high of 5.2

percent in May, according to the survey. Even so, "the majority of all households expected a declining inflation-adjusted income during the year ahead," the survey said.

The Fed's fears of a wage-price spiral in the U.S. seem to be a relic of another era. While inflation is always and everywhere a monetary phenomenon, in the words of the late Nobel laureate Milton Friedman, the structure of the economy and transmission mechanism of inflation have changed, Soss said.

Transmission Mechanism

"There are two important differences between the inflation process in the 1970s and now," he said. "First, the price shocks in the '70s were generalized because they were reflected in wages. Nobody gets a raise today to compensate for the higher cost of gasoline."

Union membership is small today -- 12 percent of the workforce last year -- compared with almost 30 percent in 1970. Cost-of-living adjustments aren't automatic.

"Second, the inflation of the 1970s was supported by inventory accumulation," Soss said. "We're not seeing signs of that now, most likely because credit isn't available."

Consumers can expect higher inflation all they want, but inflation expectations can't become inflation reality without some transmission mechanism.

Credit is harder to get, and consumers are increasingly falling behind on credit card payments in addition to their interest on mortgages and auto loans.

It doesn't sound like an environment where consumers are willing or able to borrow to buy real assets to guard against the falling dollar and higher inflation.

My view - I think this is a very good summary. I expect much of the USA's inflation to remain in the form of higher prices for energy and food. The Fed cannot do much about this because it is a global problem.

US consumers are also encountering disinflationary pressures from falling house prices. This too will stay the Fed's inflation-fighting hand, keeping the US dollar softer than many currently expect. Consequently households will also have to pay more for many imported consumer goods, as exporters pass on their higher manufacturing costs.

These are reasons for a slower economic recovery than the USA has experienced in previous cycles. They suggest continued weakness for the domestic economy, with growth coming from America's exporters and multinational companies.

What about the rest of the world?

The immediate threat is an inflation shock to growth, particularly if energy and food prices continue to spike higher. This risk is hard to quantify because it would occur mainly due to production problems, current and unknown, rather than increased consumption since demand is likely to slow during a global economic slowdown. Energy exporters are least susceptible to this risk.

Among the BRICs, [Russia](#) and [Brazil](#) have the better current prospects. There are more medium-term risks for [China](#) and [India](#), but a significant proportion of these have already been priced into their stock markets. Additionally, I maintain that these two countries should have the better long-term potential, subject to governance.

[Canada](#), with its abundant resources and small population, is in a strong position. Japan's market should be interesting when there is some respite in the bearish [Wall Street](#) leash-effect. [Japan](#) has few resources but its strength is a small population of 127 million, which is well educated and has high savings rates. The country has leading edge technology, is energy efficient and unlike most other nations, would welcome some consumer-led inflation.

Iowa Farmer Sees 'Years' of Damage to Corn Crops From Flooding - This is a concern, indicating that significantly lower prices may not be achieved quickly by another growing season and more normal weather patterns. Here is a section from [Bloomberg's article](#):

The flooding wiped out more than \$8 billion of this year's crops, according to the America Farm Bureau Federation. For at least the next decade, farmland along the Mississippi River and its tributaries may require more fertilizer to make the soil rich enough to maintain yields, said Jerry Hatfield of the U.S. Department of Agriculture. That will push up costs. The price of fertilizer rose 69 percent in the past year.

“It takes 100 years to build an inch of topsoil,” said Hatfield, director of the USDA's National Soil Tilth Laboratory, a land-management study center in Ames, Iowa. Tilth refers to soil's suitability for farming. “The floods washed it away in minutes.”

Jim Andrew, who farms outside Jefferson, Iowa, 50 miles (80 kilometers) northwest of Des Moines, said he's not sure corn production will bounce back quickly. Some farmers may choose lower yields over the rising cost of fertilizer, which may further deplete corn supplies and drive up prices, he said.

“If I'm using 100 pounds of nitrogen on an acre and I need 150 to improve my yields, I may not be gaining enough to justify the expense,” said Andrew, whose Scottish ancestors purchased the first tracts of his land for \$1.25 an acre in 1855. His farm may recover more quickly, he said, because he uses no-till practices that encourage healthier soil by relying on earthworms rather than machinery to churn land.

Hardened Soil

Farmers may find that fertilizer is less effective because the earth has been compacted by water, making it more difficult for nutrients to reach plant roots, Hatfield said.

“That soil just won't do as well for awhile because of the stress the water put on it,” he said. Even well-cared-for land may take four to five years to recover, he said.

My view - To reach the USDA's current crop forecast for [corn](#) in 2008, it will take optimum weather conditions from here on, including less moisture over the next three weeks, warm but not too hot weather during late July and early August, and no early frost. The probability is that estimates will be lowered as the ear progresses.

Email of the day - [On central bank assassinating bull markets:](#)

"The current SP500 pattern seems similar so far to that seen in 2002-2003 where there was a triple bottom, with the last made on lower volatility; the Eurostoxx made a lower final low. Then, as now, sentiment is very bleak. However, now the fear is inflation, versus deflation in 2002. Bonds are in a downtrend currently. And some central banks are raising rates. I know you have talked about bull markets being assassinated by central banks raising rates. I agree that we are due for a bounce from around current or slightly lower levels. For a sustainable run we would need to see crude oil peaking. But how do your past concerns on central bank assassinations affect your views of where global markets are headed? Thank you again for your invaluable guidance."

My comment - Thank you for your kind words, accurate recall and important question. I have previously said that bull markets do not die of old age, adding that they are usually assassinated by central banks, due to concern over rising inflation.

The 2002 background was very different from today, as you point out. Fearing deflation back then, many central banks were cutting interest rates. More recently, many central banks raising rates. Consequently this is a more risky environment because the deflationary fears in 2002 proved to be exaggerated, although few believed it at the time.

This raises the question, could central banks be overreacting by raising rates today? Possibly, in my view, because if the [oil price](#) rises much further there will almost certainly be an economic shock, as we last saw in the 1970s. In fact we may have already crossed that threshold and the problem is compounded by soaring food prices. Moreover, [bank](#) shares, which I regard as a leading indicator, remain very weak in a number of markets, not least where property prices are also falling.

Consequently, while this resembles a perfect storm for stock markets, a considerable amount of bad news has already been discounted. At some point, probably within a few months if not weeks, there will most likely be

some respite in the bearish outlook and / or investors will begin to look beyond the trough of this economic cycle and its inflation problems.

Central banks which have raised interest rates the most, will be in the best position to lower them. Meanwhile, I would be wary of excessive pessimism at a time when the level of short sales in many markets is high and investors already hold considerable reserves of cash. I also caution against unwarranted optimism while chart patterns remain weak.

My personal portfolio: Palladium stop triggered; a gold profit taken; a loss on Singapore rollover - I really should not trade [palladium](#), due to the very wide spreads quoted, which can be up to 5 points each way for a commodity currently trading at \$470, compared to 1 point spread for gold which is over \$900. I assume the difference is mainly due to turnover. Anyway, my breakeven stop was triggered at \$461 on 25th June (I was away that day, thus the late report) against my purchase at \$459.3 on 21st May.

In [gold](#), I continue to lighten futures longs on rallies because the pattern is currently ranging within the long-term uptrend, in line with seasonal factors and its previous trading history for this cycle. Accordingly, I sold half of my remaining August position at \$912.65 late yesterday, against my purchase at \$901.85 on 20th June. Today, I sold the remaining August position at \$928.70, against my exuberant purchase at \$927.80 on 22nd May. I am hoping that in these choppy markets I will have a chance to repurchase gold on a setback within the current range. My risk is that gold moves higher because commodities remain the in-form sector.

My small long in the Singapore Blue Chip Index ([FSSTI](#) nearest equivalent for pattern) expired at 366.6 this morning, against my ill-timed purchase at 386.02 on 2nd June. Questionably and somewhat masochistically given market conditions, I allowed this to be rolled forward, paying 366.32 for a July position.

Lastly, and highly speculatively, I reopened a long in [corn](#) this afternoon, paying 767.50¢

Prices above include spread-bit dealing costs.

Crude oil: Chart of the week - A new all-time [high](#), although most of today's gains were not maintained. Nevertheless, a close beneath \$130 is now required to seriously question the consistency of this medium-term uptrend, and \$120 to confirm that a significant correction was underway.

Quote of the week - On rainbows:

"There can be no rainbow without a cloud and a storm.
JH Vincent

Additional Commentary by Eoin Treacy

How are the world's best performing stock markets doing relative to commodities and bonds? - Yesterday we looked at which country indices were performing best in local currency and US Dollar terms. Today, I thought to look at how the best performers in yesterday's search are doing relative to other instruments when considered in a constant currency.

To do this I took all of the best performing stock market indices from yesterday and put them in a new section of my Favourites along with most of the commodities and a large number of bonds from the Chart Library. The resulting list was then sorted by 3-month returns. (Please see the Filter Help pages for instructions on how to do this.)
<http://www.fullermoney.com/filterhelp/fmfilter.html>

Commodities dominate the [list](#), with Coal, Potash, Corn, Natural Gas and Oats in the top-5 positions. While a couple of African and Middle Eastern stock markets feature in the top-10, Norway is at 13th, Russia is at 20th and Brazil is at 22nd of 78 instruments. The clear signal is that commodities are far and away the best performing asset class over the last three months.

When we sort the list by those moving up the rankings fastest between 1 and 3-months or between 1 and 6-months, commodities continue to dominate the list. This indicates that not only have they been outperforming, they continue to lead.

Of particular note is the performance of [wheat](#) which lost more than 40% of its value between mid-March and late May. It was losing momentum for the last month of its decline and the upward dynamic, which pushed the grain back above 800¢, was an indication that investor interest was returning. It would now need to sustain a move below 850¢ to question scope for further upside.

From this analysis, we see that commodities are outperforming country indices. Factoring in yesterday's results, the country markets doing best are those most heavily weighted to commodities. Whenever this leadership starts to break down, we will have a signal that equity markets generally are moving to a position of relative outperformance once more.

In terms of the choosing where to be invested, the most profitable strategy has been to be long of commodities and commodity related investments, this will not always be the case but there is currently no sign that it is about to change.

VIX 26% Below 2008 High Points to More Declines for U.S. Stocks - Thanks to a subscriber for this [story](#) by Elizabeth Stanton and Jeff Kearns for Bloomberg covering the VIX Index. Here is a section:

The most-watched gauge of price swings in U.S. equities indicates stocks have further to fall after the Dow Jones Industrial Average declined to the lowest level since September 2006.

The Chicago Board Options Exchange Volatility Index, or VIX, rose 13 percent to 23.93 yesterday, leaving it 26 percent below its 2008 high. The Dow is poised for its worst June since the Great Depression after record oil prices and credit-market writedowns sent it to its biggest drop in three weeks.

“It could get worse,” said Richard Weiss, who helps oversee \$60 billion as chief investment officer for City National Bank in Beverly Hills, California. “When I walk down the street and everyone who knows me says ‘Oh my God, how are you guys doing?’ that’s when it’s time to start scooping up everything with both hands. We’re not quite there yet.”

The volatility index, which traders sometimes use to forecast price changes in the Standard & Poor’s 500 Index, closed above 30 for the first time this year on Jan. 22 after stocks retreated to a 16-month low. It reached a five-year high of 32.24 on March 17 when the S&P 500 traded at its lowest level of 2008, the day after the Federal Reserve led a bailout of Bear Stearns Cos.

The VIX is derived from the cost of options used to protect against declines in the S&P 500 and usually increases when stocks slip. Its climb above 30 in January and March marked bottoms for the benchmark index for American equities and preceded rallies of 3.3 percent and 7 percent in the following months.

My comment - [Over the last year, brief surges to a reading of over 35 on the VIX Index](#) have been reliable indications that we are close to important market bottoms,. This was the case in August, January and March. We are currently at a reading near 24.

On previous occasions when the Index has hit highs above 35, it was on an intraday basis. On all three occasions in the last year, it surged from below 30 to its high and was back below that level within three days. We also see that all three of these moves originated from levels between 25 and 30. The message here is that the surges above 30 can occur quickly and have ended quickly. Each of these highs on the VIX has been followed by a sharp [rally](#) in equity markets which is probably something to watch for on this occasion if the [VIX](#) continues to appreciate.

Email of the day - [on placing stops](#):

"I just had what could have been a rather unsavoury experience in my spread betting account that I thought would be useful for 'the Collective' to know about and watch out for.

"I normally put in a price far from the current price as a target to try and take advantage of market spikes. However this worked against me when my spread bet was rolled over because my target price did not take into account

the increase in the price for the new September contract. Surprisingly, the firm rolled me over at a higher price (446) and immediately sold my position as my target (444) was lower than the price I was rolled over at! Fortunately, I noticed this, argued with the firm who agreed to reopen my position at the price I was taken out at. As you can tell, I still have a lot to learn about setting stops and targets and I would very much appreciate your guidance and opinion about this!"

My comment - First of all, I don't think you've done anything wrong. The spread-betting firm should adjust where your stop is in line with the change in the position. This is only fair, considering the reason you had an automatic roll over was to avoid unwarranted maintenance of the position in the first place.

Placing stops is not an exact science and there is no right or wrong answer on where they should be placed. One of the best reports I've come across on stops was written by Jan Bylov for Nordea. He was kind enough to forward it to us and it appeared in Comment of the Day on [November 22nd](#).

Placing a stop is a money control tactic which may or may not be suitable to a position. This is a decision each of us makes for ourselves. When a decision is made to place a stop, there are generally two types: we can make it a technical stop or a financial stop. Technical stops are calculated in line with the consistency of the trend, while a financial stop is placed with a concern for one's bank balance being tantamount.

Speaking for myself, I tend to use financial stops either when I have a large a position and am unwilling to allow for the potential loss of placing a technical stop or I am protecting profits. Financial stops are based more on one's pocket and size of position than on where the market might potentially find support in a reversionary move. Choosing which instrument to buy or sell is a function of analysis, but choosing how much to buy or sell is more about money and ego control.

We buy because we believe the instrument will rise and want to maximise our profit potential. However when our expectations of how far the instrument will move diverge from how much money it is prudent to allocate to the trade then we could be in trouble.

Let's take an example. [Oil](#) remains in a consistent uptrend and has just broken upwards to a new high. Considering the bullish forecasts for the energy complex, I'm sure that some investors will have bought this breakout. However, this is a risky environment considering how high it is and how mature this bull move is. Many of these speculators will have placed stops.

A financial stop could be anywhere below the current price, but it is unlikely to be very far away from where the commodity is trading right now. It might be at the top of the range near \$139, in the middle of the range at \$135, underneath the last range near \$130 or anywhere in between. Depending on how close the stop is placed to the current prices, one's expectations of how much oil could appreciate would have to be potentially considerable to justify the risk / reward ratio of the trade..

On a technical basis, the most consistent thing about oil's advance is the progression of higher lows and it would need to take those out to question upside potential. Following today's clear upward break, a technical stop below \$130 would be the only rational area to place it at the present time. If oil were to advance considerably above \$140, one could consider raising it but probably not before.

Our prospective trader would argue that this is too far away from the present price and he would incur a significant loss if he had his stop that far away. However, if one decides to even have the position, given the reversionary risk which would still be consistent drawdown within the overall trend, then positions need to be sized according to where the technical stop is best placed. One needs to size one's positions more in line with our potential loss than how much we want to make from a trade.

As mentioned above, there is no sure fire way of placing stops and it is a largely a function of one's own risk management considerations. However, in my own experience, my most profitable trades have resulted from being reasonable with my position size and realistic about how far away a potential stop needs to be to keep me in a consistent trend.

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.

Euro Stoxx 50 - remains in a short-term consistent downtrend as it breaks below the March lows. An upward dynamic and/or a close back above 3475 would be needed to check momentum beyond a brief pause.

Gold - testing the upper side of the three-month range and needs to sustain a move above \$950 to confirm that the bulls have regained the upper hand

Cocoa - remains in a very consistent move having broken upwards from the two-month consolidation. A downward dynamic would be needed to check momentum beyond a brief pause.

Email of the day - on finding companies in the International Equity Library:

"Could you, please, add Uranium Energy Corp (UEC) New York, to the Chart Library?"

"Thank you very much"

My comment - This share is already in the International Equity section of the Chart Library. If you select the International Library from the Dropdown menu and search for UEC, it will pop up.

Email of the day - [on Case / Shiller indices for US house prices:](#)

"The S&P Case/Shiller index data hasn't been updated since 2007, could that be fixed? (Composite [10/20](#))"

My comment - [All three of these indices have now been updated with the most recent data available on Bloomberg. However because the composite chart is now in negative territory, the Chart Library is unable to chart it. This is an enhancement I will speak to our IT people about implementing.](#)

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