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

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

Monday 11th August 2008

Morgan Stanley: Dollar Gain Signals Pain; Rally Prompts Exit - The USD's best rally since 2004 has not converted everyone to a bullish hypothesis, as we can see from this article posted on Bloomberg. Here is the opening:

Just because the dollar posted its biggest gain against the euro in almost eight years doesn't mean the U.S. currency won't continue to be plagued by the nation's slowing economy, widening budget and trade deficits and negative inflation-adjusted interest rates.

The 4 percent surge against the single European currency this month was enough to prompt Bank of America Corp. to tell its customers to exit trades betting on more gains. Morgan Stanley still forecasts the greenback will approach a record low by October as the U.S. housing slump and credit-market losses keep the Federal Reserve from raising interest rates this year.

Barclays Plc in London and New York-based Merrill Lynch & Co. said trading patterns suggest the dollar's 5.1 percent gain in the past three weeks measured by an index of six major trading partners can't be sustained.

That's mostly because there's no indication the U.S. will return to the late 1990s annualized gross domestic product growth of 4.23 percent with inflation running at no more than 3.3 percent. Since September, 2000, the dollar has declined more than 44 percent as inflation accelerated to an annual 5 percent today, growth slowed to 1.9 percent and U.S. interest rates provide no cushion for holding U.S. assets.

``I would not chase the dollar's strength versus the euro as the pair has moved beyond interest-rate support,'' said Sophia Drossos, a strategist in New York at Morgan Stanley, who also recommended closing out bets on the dollar versus the currencies of Malaysia and Singapore. ``The dollar is not out of the woods. It will take the market a while to come around to our point of view.''

Unsustainable Recovery

The dollar strengthened to $1.5005 to the euro last week from $1.5564 on Aug. 1, the biggest weekly increase on a percentage basis since January 2005. It surged 2.08 percent on Aug. 8, touching $1.4998, the most since

Sept. 6, 2000, and the second largest rally since the euro was introduced in 1999.

My view - Contrarian thinkers, on reading this article, will find sufficient disagreement to support either a bullish or bearish view of the USD. Fundamentally, I find it difficult to believe that the US currency has broken its secular downtrend, but the recent, strong rebound has certainly put at least a medium-term floor under the greenback.

Fullermoney posted a technical review of all major asset classes on Friday, including a blueprint on how to assess the USD from here, in terms of either its eventual confirmation or negation of the recent upward break. (*See also my full answer to Email of the day (4) below*.)

Email of the day (1) - On China's demand for resources:

"The address above takes you to the presentation given by Mr Howard Balloch at last week's Diggers & Dealers Conference in Kalgoorlie. To my mind it is one of the most clearly presented arguments for the continuation of strong growth in the Chinese economy and demand for resources. Mr Balloch was, I believe, Canada's ambassador to China before establishing his own consultancy/advisory business in Beijing."

My comment - Many thanks for this extremely interesting presentation which contains many informative graphics. Here is a bullet point on China's Consumer Spending:

Private consumption as a % of GDP is only 36%, compared to 70% in America, entailing that as China's middle class grows, consumption on basic metal-intensive goods such as new homes, automobiles, electronics, and appliances will increase drastically. China will have as many consumers as the EU and USA combined by 2020.

Howard Robert Balloch was indeed Canada's Ambassador to the PRC from April 1996 until July 2001, when he founded The Balloch Group, which has offices in Beijing, Shanghai, Hong Kong, Wuhan, Hangzhou and New York. He is also Vice Chairman of the Canada China Business Council, so we can assume that he knows vastly more about China than most western observers.

Given some of the very bullish forecasts in his presentation, I wondered what he considered to be the main risks to his forecasts. He cited seven factors, some of which are wildcards: banking, environmental problems, export collapse, inflationary pressures, pandemic, socio-political instability and Taiwan.

Balloch did not elaborate on banking but while Chinese banks were generally regarded as a weak area a decade ago, the biggest ones such as Industrial & Commercial Bank of China (601398 CH) and Bank of China Ltd (601988 CH) were cleaned up prior to their privatisation in 2005. The charts remain weak, in line with China's Shanghai Composite Index, but my distinct impression is that Chinese banks are in enviable financial positions relative to their western counterparts.

Environmental problems are a big concern for China but there is also money to be made in the cleanup, which the PRC has begun to address. Under export collapse, Balloch estimates that "a 10% reduction (US recession of 1%) would reduce Chinese GDP growth by 1.5-1.7%." My own view is more cautious because there are good reasons why the US economy may not bounce back quickly. Also, I assume that China's exports to Europe and perhaps some other regions will also drop sharply.

Inflationary pressures have been a very big problem over the last year but China was quick to address them structurally, where possible in terms of food, and the recent break in crude oil's medium-term uptrend is very encouraging news. However I think it would be prudent to assume that oil prices will move higher at some point, as global GDP growth improves over the medium term, not least with the help of crude's current correction.

Of Balloch's last three potential problems - pandemic, socio-political instability and Taiwan - I classify these as diminishing risk wildcards. One cannot rule out pandemics but China dealt effectively with SARS and bird flu, which were not unique to the country. The risk of socio-political instability is not limited to authoritarian regimes and economic progress is usually the best antidote. China's leaders have proved to be among the most economically adept, and have been increasingly tough on corruption. Lastly, a genuine thaw is underway in relations with Taiwan, which have improved considerably over the last six months.

My own wildcard risk for China is the stock market's current underperformance - presently the worst in Asia and a drag on the region. China will need to address this, as it last did in 2005, since the latest downward break is a concern. I think it is another buying opportunity for investors who are willing to take the long view, but I will feel happier when we next see clear evidence of a base formation and establishment of a new uptrend. However, China's main share indices will be well off their lows at that point.

Don't miss Howard Balloch's enthusiastic concluding message on page 34 of the presentation above.

Email of the day (2) - On constructive criticism regarding trading:

"In the spirit of constructive criticism, I offer the following:

"1. You and Eoin have made some great calls on crude oil. There have been some spectacular, tradable moves both up and down. I have yet to see either of you ever enter a trade in crude oil.

"2. You were calling for a medium-term correction for China at the Chart Seminar that I attended last November. Yet you did nothing to hedge any of your long-term holdings in a move that lost 50 percent of its value.

"3. You have a decidedly bullish bias for equities. In the past 2 years, where there have been trending, tradable downside moves, you are constantly looking for "oversold" indicators for pick a bottom. I understand you want to look to buy in markets related to so-called "Fullermoney themes", but you constantly refer to the US stocks as a "secular bear market" yet you have yet to trade a position related to this secular theme.

"4. You have had a good call on the Type 1 acceleration tops in the grains and beans, yet have not traded any of the move down -- corn dropping from 8.00 to 5.00 makes as much money as corn rising the same distance.

"5. Recently, you have been slow to recognize the same "oversold" indicators in the US dollar that you constantly look for in equities. When the dollar has its largest rally in over 3 years, you have missed a good trade, especially since the charts that you "rely" on to "show the way" were screaming upside breakout over the past few weeks.

"6. I totally agree with your thesis regarding gold as a long-term secular bull investment. Yet when your seasonals are bearish, and the charts show a breakdown, you need to have the flexibility to trade from the short side when there is a $100+ move in a month's time.

"7. I understand not trading much last year around the time you had your surgery, or around vacations that you and Eoin take, but it seems that you are trading much less recently than in the past. You gain more respect when you are risking capital on your ideas.

"Thanks for listening. On balance, you have a great service. I understand the difficulty of producing what you do on a daily basis. I do not intend any offence with these comments, only hoping that they might make your service even better."

My comment - Thank you for your comments and I appreciate the spirit in which they are offered. The man who is afraid of constructive criticism, closes one of the main doors to personal development.

I agree with most of what you say, although the dollar did not look like a "screaming buy" to me in the first half of July when it was sagging, however we did comment on its firming pattern subsequently. I did open hedge shorts in stock market futures on several occasions, although I never held them long enough, often because of stops that proved to be too tight. For the record, I seldom trade what I regard as countertrend moves in Fullermoney secular themes such as gold, preferring to increase or reduce positions within long-term trends, as opportunities or risks are perceived. Also, not being happy with my trading recently, as sometimes happens, I have done less of it. I also regard my pa trading as secondary to producing Fullermoney's research.

If I could live last year over again, what I *really* should have done was sell most equities in my investment portfolio when the S&P 500 had its upside failure last October, as US bank shares were breaking downwards once again. However if I had, I would have bought most of it back by now.

For the record, Eoin and I declare all of our personal trading and investing to subscribers as a matter of integrity. Hopefully, it also keeps our analytical feet on the ground more often than not. However in producing this service our first priority is to monitor and then interpret the markets in preparing our daily analysis, charts and reports, produced for a global subscriber base.

Lastly, I appreciate your thoughts on what might make the Fullermoney service "even better". My own view is that this will most often be achieved through the collective process of empowerment which helps each of us to improve our own individual investment and trading decisions.

Email of the day (3) - On renewing and TCS in Australia:

"Dear David, just renewed my subscription. What a year. I have learnt so much from your informative commentary. Thank you. I Hope that Eoin will bring The Chart Seminar to Australia. Book me in!"

My comment - Thanks for your continued interest and enthusiasm. It has been one of those sufficiently frightening years where it helps to be either a young optimist, or an old stager with a good memory who can recall that it usually isn't this scary.

I am sure Eoin will take TCS to Australia at some stage, although that may be a few years away.

Email of the day (4) - On oil and the US dollar:

"Thank you for all your enlightening commentary, I am much enjoying being a subscriber (for just over a year now). With regard to your comments on oil undergoing a correction to perhaps as low as $100 do you not see this as being a major factor in the US$ recent strength and therefore the likelihood that we will see further US$ appreciation in the near term as there is another 16% or so potential downside in the price of oil (to the $100 level)?"

My comment - Thank you for your kind words and a very interesting hypothesis / question.

Yes, to the extent that oil has been the main driver of sentiment during its spike upwards and even faster descent, evidenced by the fact that the dollar has risen just about every day as oil has fallen since mid-July. In other words, oil and the USD are currently inverse images of each other with oil calling the shots.

The next question, however, concerns the durability of this inverse association. The market's verdict is that people have been bidding the USD higher recently, and commentators will attach explanations. However if the dollar happened to be declining, we could just as easily argue that the world needs fewer of them to pay for less expensive commodities. Remember, the USD rose when oil was rallying in 2005, and it was coming down during crude's earlier correction between July 2006 and January 2007, as you can see from this weekly overlay chart.

Over the longer term, I would say that when oil is not rising so fast that it erodes demand, as we saw recently, its fundamental background is one of generally rising demand, together with an increasing cost of production due to a scarcity of conventional oil. In contrast, I doubt that the demand for USD is rising, beyond the recent reversal of a momentum play. Moreover, there is very unlikely to be a shortage of USD, due to the USA's preference for printing its currency well in excess of GDP growth, and the cost of producing dollars is low.

In conclusion, I suspect Morgan Stanley's view on the USD above could be right, although it is now for the dollar bears to prove.

Please note - Eoin is away but returns tomorrow.

Tuesday 12th August 2008

Mike Lenhoff: Revisiting the case for high yielding investments - debt as well as equity - My thanks to Tony Smith of Brewin Dolphin for his colleague's latest Market Strategy letter, which makes some good points. Here is the opening:

This chart shows the year-on-year growth rate for US GDP over the past 40 years along with the contribution from net exports in goods and services. The message is not that each cyclical downturn has been associated with a rise in the contribution from net exports but that, whatever its contribution, net exports have never prevented the US economy from sliding into a recession. The contribution from net exports today is greater than at any time in the past four decades but will this make a difference? Probably not!

US GDP grew by 1.8 percent year-on-year in the second quarter of 2008. Yet 1.5 percent of this growth came from net exports. Less than a third of a percent came from domestic demand. The domestic economy has lost pretty well all momentum. So imports have been curbed but US exports have been holding up well, thanks to a competitive exchange rate and the strength, at least until now, of the developing economies. The contribution from net exports is just about all that is holding up US growth, but this is now likely to give.

Interest rates are rising rapidly throughout the developing economies. The Reserve Bank of India raised interest rates by 50 basis points last month. This came on top of the three-quarter point increase announced in June. The

Central Bank of Brazil raised its target rate by 75 basis points in July and further increases are expected before year-end. The Bank of Russia also announced a quarter point rise in its key refinancing rate last month, the fourth such increase this year.

Of the BRICs, China has been the odd one out. The People's Bank of China had been raising interest rates up until the end of last year but has stood pat this year. However, it has been raising the reserve requirement ratio. The authorities have also let the Renminbi continue to appreciate. The subsidies on oil consumption have been reduced. The result now is that growth is slowing - and inflation is decelerating.

Interest rates are going up elsewhere, not just in the BRICs. They are going up in the Middle East (Egypt's central bank just raised interest rates), in Asia (the Bank of Korea just raised interest rates) and in Latin America (interest rates just went up in Peru and are expected to go up in Colombia this week). The risk then is that, in aiming to take the heat out their economies, the developing world slows down considerably.

For the US economy, the bottom line is that the contribution from net exports is likely to fade. Given that US domestic demand has turned negative already on a quarter by quarter basis, a recession starting later this year seems inevitable.

That spells further downward revisions to earnings growth pretty well everywhere.

My view - Don't miss the graph, referred to above, at the beginning of Mike Lenhoff's report. What he says is correct, so I will make a different, longer-term point.

The long-term health of the US economy, in my view, depends in no small measure on its ability to generate more exports. This will take time; it will not be easy, and it will require a soft currency relative to those of faster growing economies.

Email of the day (1) - On a testing period and a great quote:

"Once again, congratulations on your continued excellent service, especially during such a testing period.

"To that end, I read with interest the e-mail you received today offering "constructive" advice.

"In response, I thought you might like to see a favourite quote of mine which comes from Larry Hite, one of the founders of the multi-billion dollar fund management company, Mint Inv Mgt, "It's amazing how rich you can get by not being perfect." "

My comment - Thanks for your kind words and a wonderful quote. I met Larry Hite in the 1970s, before he became famous. Although quiet, he was obviously very bright, modest and had his ego well under control.

Deepak Lalwani's The India Report - My thanks to the author for this informative report published by Astaire Research. Here is a section:

The Government, according to Junior Finance Minister P.K. Bansal, is expected to have enough support to push through legislation on some politically acceptable reforms in the Monsoon session of Parliament from August 11. These may include: (A) Insurance: To raise foreign equity from 26% to 49%, a move stalled earlier by the Communists. (B) Banking: To remove the existing 10% voting cap and allow foreign banks to have voting rights equal to their ownership in private sector banks. Also to reduce state ownership in public sector banks. (C) Pension reforms: Long-pending reform to allow 26% foreign equity in pension fund companies. Could be raised to 49% if (A) above goes through. (D) Privatisation of state run companies: 3-4 companies could be partly privatised, but time is short especially since market conditions are not favourable. Some state run companies maybe listed to bring benefits of greater visibility and more accountability in changing public sector mindset of current managements.

The retail sector is seen as being too politically difficult to introduce foreign ownership for multi-brand firms. Hopes for a 10% ($10bn) privatisation of state-run telecoms giant BSNL have been revived following the Government's recent confidence vote win in July when the Communists were replaced by the pro-business regional ally, the Samajwadi Party. The Government had said in January it wanted to list BSNL but this was shelved following stiff opposition from the Communists and trade unions. Union leaders still oppose the privatisation. The company is estimated to be valued at $100bn and the 10% listing would make it the country's largest IPO. Current market conditions do not favour such a large issue but the Government hopes investor sentiment may improve in future months. The money raised would help the Government's finances considerably at a time when international credit agencies are considering downgrading the country's credit rating due to stretched public finances.

My view - The Government's confidence vote win in July is the main reason why India has been Asia's best performing stock market since the middle of last month. The coalition government's replacement of the Communist minority with the Samajwadi Party can only help India's lumbering and complex democracy to move forward, behind the leadership of private industry.

Email of the day (2) - On intervention theory behind USD strength:

"David, the strength of the surge in USD from its mid July low on the Index of just over 71 to just over 76 today has been surprising. There has been some commentary on central bank intervention here:

"As a fairly recent FX trader I have not directly experienced an intervention, so not sure what to make of the recent price action or the intervention theory. Do you have a view on the whether the surprising strength has been caused by intervention or some combination of other factors?"

My comment - Thanks for an interesting point and also this link. Given the simultaneous occurrence of the USD's rally and crude oil's fall, I had wondered aloud in Audios, as you may recall, regarding the possibility of some informal agreement to support the US currency in exchange for more oil. However I was not aware of any other information or rumours on this subject.

The evidence cited is interesting and I would not rule it out. However stealth intervention to support the USD would be a departure from the high-profile multilateral interventions that we have seen in the past. I have written about this on occasion and you could search the Archive under [multilateral intervention], if interested. (*Note: exact spelling and sequence of words is required for Archive searches, and one or two words will usually produce the best results*.)

If James Turk is right, then it increases the likelihood that the US Dollar Index's lows will hold for a lengthy period, if only because having embarked on this course of action, central banks would almost certainly defend the low if necessary. However, if Turk's view were to become widely accepted, it would also embolden forex traders to attempt a retest of that low, as we have seen before. Currently, the DXY's rally (weekly & daily) looks at least temporarily overstretched and susceptible to a consolidation.

All We Are Sayin' Is Give Free Market a Chance - My thanks to a subscriber for this interesting Econtrarian report by Paul Kasriel of Northern Trust. Here is a brief section:

The lack of a free market in credit-risk assessment also played a role in today's economic and financial market turmoil. According to a Business Week April 8, 2002 article, "In 1936, the Comptroller of the Currency decreed that banks could hold only investment-grade securities. Ever since, regulators have been delegating risk assessment to the rating agencies. A rising tide of regulatory requirements has forced banks, insurers, mutual funds, and other financial institutions to pay attention to bond ratings. The upshot: Companies, municipalities, and governments that want to tap the U.S. capital markets need credit ratings." So, fiduciary institutions are required by law to invest only in instruments stamped "investment-grade" by ratings agencies. This does not mean that fiduciary institutions cannot do their own credit analysis, but why incur the extra cost when the regulators implicitly are endorsing the credit analysis being done by the credit rating agencies.

Is there a free market in regulator "approved" credit rating agencies? The Business Week article continues, "To prevent unscrupulous outfits from selling triple-A ratings to the highest bidders, the Securities & Exchange Commission in 1975 designated the ratings of Moody's, S&P, and Fitch as the only ones that may be used to satisfy creditworthiness regulations. The SEC later anointed four more as Nationally Recognized Statistical Ratings Organizations. Mergers have left just the original three." So, no, there is not a free market in approved credit rating agencies.

Prior to the 1970s, credit rating agencies were compensated by the investor in securities, not the issuer, as is the case now. There is an obvious conflict of interest when the issuer compensates the rating agency. Of course, investors are not precluded from doing its own credit analysis or paying another firm for its analysis. I suspect that a free-market response to the erroneous credit analysis performed by the Big Three rating agencies will lead to more independent credit analysis on the part of investors going forward. But prior to the recent episode, regulation did not encourage such independent analysis. Had the regulatory-anointed Big Three not slapped "investment-grade" on so much dubious product in this past credit cycle, there would have been less demand for the product. With less demand, there would have been less product originated and fewer credit problems to deal with today.

My view - I enjoyed Paul Kasriel's view but will add that without governance, free markets would soon descend into anarchy. Many of the problems that he and others have described in such detail are due to bad governance, which also contributes to the undermining of ethical standards.

Email of the day (3) - On trading and emotional capital:

"Congratulations on a most informative site. In over twenty years of professional financial market trading and risk management I have never come across a market commentary that so superbly combines macroeconomic theory, market behavioural psychology and technical analysis. I only wish I had come across Fullermoney sooner.

"In relation to yesterday's e-mail referring to trades you may or may not have made I would like to point out that in my opinion it is not necessary or indeed maybe practical for anyone to trade every move in every market. Nor is it necessary to trade long or short at every signal in the markets that one does trade. It really depends on the overall trading method applied which will in turn directly relate to one's Bank of emotional capital.

"For example, if one's trading method is governed by secular themes (which your's would seem to be) then it may be that the method does not allow for trades in the opposite direction to that theme. If the theme is to be long oil then one can BUY oil or Exit Long oil but not short it. To act contrary to one's method will take a serious toll on one's emotional capital. To short oil, if one thought it was in a secular bull market and one's method was to trade according to that theme, and to subsequently watch the market rally against one would be for me a far more significant drain on emotional capital than to have a profitable trade were the market to fall. The point is that it is not so much the prediction that is important but the subsequent discipline to act in accordance to one's trading method that is important.

"Emotional capital is every bit as important as financial capital and every time one trades a little emotional capital, reserves from positive past trading experiences are put at risk.

"As for trading every market, well unless on has a highly systemised approach or method then in my experience it is impractical and possibly reckless to trade (not invest) across more than six to eight different market sectors. That does not mean that one is not watching other markets (leaders, etcetera) to assist in positioning; again it depends on one's method. And again, how many markets one is actively trading will have a direct impact upon one's emotional capital reserves. The more positions the greater the strain.

"Perhaps you should have delta hedged some of your retirement fund equity positions. However, as I understand from following the site, many of these positions are investment plays that were only to be unwound in the event of the end of the secular theme or extreme overvaluation."

My comment - Many thanks for your thoughtful comments and especially for sharing your perspective on Emotional Capital (*my capitalisations for emphasis*).

This is an extremely important subject for both traders and investors. In my opinion, your thoughts on Emotional Capital are profoundly wise. Those of us who both read and absorb your message will surely benefit from it.

Please note - My market analysis for today is in the Audio.

Additional Commentary by Eoin Treacy

Email of the day (1) - on bond yields and spreads:

"Would it be possible to add to your charts information for bond yields of various maturities of Ireland, Spain and Italy?

"An article in last Saturday's Frankfurter Allgemeine Zeitung (FAZ) showed that 10 year bond yields for German government securities were 4.37% while those for Ireland were 4.81%. That's surely an extraordinarily large gap given a common currency and appreciably lower government debt levels in Ireland (relative to national income). A growing gap between these yields may be a proxy for growing investor uncertainty that European Monetary Union (EMU) will hold together."

My comment - Thank you for this interesting question. I have added 10-yr yield charts for Germany (4.273%), Austria (4.48%), Belgium (4.574%), Netherlands ((4.393%), France (4.388%), Spain (4.559%), Portugal (4.695%), Ireland (4.577%), Finland (4.383%), Greece (4.866%) and Italy (4.761%). The Eurozone 10-yr yield is 4.27%.which equates to the German rate.

Euro skeptics have long pointed to this disparity as a reason why the Euro has no long-term future. I would suggest it indicates that at least some countries will eventually be ejected or withdraw from the Euro because they do not and cannot meet the conditions for entry. The difference in yields is a way for investors to differentiate between the risk of lending to a country such as Germany relative to one such as Greece.

I agree that monitoring the spreads between weak economies and German Bunds would be a fair indicator of how much risk investors are attaching to these countries' fiscal policies.

Email of the day (2) - on overlays between the US yield curve and the S&P500:

"Thanks for adding the US Yield Curve, requested by another subscriber. Would it be possible to make an overlay chart and compare the yield curve (on one axis) with US GDP Growth (on the other axis)? I believe the Yield Curve could be a very good lead indicator for economic activity by 12-18 months.

"By the way, in the comparison between the Yield Curve and the S&P 500, could you please plot the equity market in logarithmic scale - it will make it a bit easier to look at some of the earlier signals on this 20 year chart.

"And many, many thanks for the Beijing tips, they have been immediately forwarded to one of my friends who works for the IOC and has to spend months out there."

My comment - Thank you for these interesting questions and I'm delighted to hear you liked the Beijing travel advice. Your friend might also be interested in the email posted directly below.

I'm afraid we cannot yet create a chart with more than permutation. I created this chart of the yield curve spread chart overlaid with US GDP growth year-on-year using Bloomberg. Here is the same chart rebased to a common denominator.

You are at least partly correct in your assumption that the yield curve is a lead indicator for economic activity. These charts show us that the yield curve has bottomed on three occasions since 1980 before GDP growth. The lead has always been more than a year but not more than two years. Peaks in the yield curve have not coincided with peaks in GDP growth.

Since the yield curve has rallied impressively since the beginning of the year and certainly appears to have bottomed, we can probably expect US GDP growth to pick up some time next year.

Regarding your second question, it is possible to change the overlay of the yield curve compared to the S&P 500 to a log scale chart. Simply click on the log scale tab in the Charting menu. However, while log scales successfully illustrate historical data in the lower S&P 500 chart, it scrunches up the percentage data in the upper yield curve chart.

Email of the day (3) - on how to see the best that Beijing has to offer:

"Having been travelling in China for 5 weeks last year, there were many highlights to mention but talking about Beijing I have to bring Mr. Storm the concierge from the Holliday Inn to the attention of the Fullermoney subscribers. Mr. Storm seems to work for himself, next to his concierge job. We had a fantastic inside tour seeing local areas without any other tourist in sight; I can not recommend Mr. Storm strong enough. In my opinion you have not seen the real Beijing, without the help from him.

"I looked him up again and this was the first what came up when I Google him.

"I can only strongly recommend him, the price he charged last year was embarrassing small money for the service he provided."

My comment - Thank you for this suggestion which I'm sure will be of interest to those travelling to Beijing.

Neither I nor anyone associated with Fullermoney has anything to gain from this review.

Email of the day (4) - on South African shares:

"Thank you for the wonderful service. After attending the chart seminar twice I feel well equipped to cope with the present market turmoil.

"At the moment I am watching my local market closely. Banks have broken out and it remains to be seen if this rally will continue and broaden in to other sectors.

"Towards this end I would appreciate it if you could add the following JSE Top 40 Equities that I am unable to find in the chart library (share code in parenthesis)...

"Aveng (AEG), Exxaro (EXX), Liberty International (LBT), Lonmin (LON), Mondi Ltd (MND), Murray & Roberts (MUR), Netcare (NTC), Pretoria Portland Cement (PPC).

"Lonmin and Liberty are dual listings with a listing in the UK. However, it is the SA listing that I would like to track.

"Thank you again for your sober guidance in these trying / interesting times."

My comment - Thank you for an interesting email and we are delighted to hear that The Chart Seminar was a worthwhile investment of your time. Thanks also for pointing out these omissions which have now all been added to the International Equity section of the Chart Library,

Today's interesting charts - Did you know that the Chart Library has hundreds of different currency crosses?

Taiwan - found support above the July lows and is now testing the recent highs. A sustained move below 7000 would be needed to question potential for at least some further upside.

Tin - continues to extend the downtrend having broken below $20,000 last week. A sustained move above that level is now needed to question scope for some further downside.

US Dollar per 1 Australian Dollar - The Aussie Dollar continues to weaken but is looking somewhat overstretched. However, an upward dynamic would be needed to check momentum beyond a brief pause.

Email of the day (5) - on finding equities in the Chart Library:

"I have just taken out a one month trial subscription. How do I see the charts for individual shares as well as those that I can see for national indexes?

"For example, how can I see the chart for Barclays Bank, for Dexia or for a Japanese bank?"

My comment - Welcome to the service. The more than 15,000 equities in the International Equity section can all be accessed via this menu.

The International Equity section can be found second from the top in the main Chart Library dropdown menu. It can also be accessed through the green link to the right of the search field in the Chart Library search engine.

Email of the day (6) - on adding currency crosses to the Chart Library:

"Could you add the following 3 charts to the Library:
- BRL USD (Think I subsequently found this one)
- BRL GBP
- Renminbi (CNY) GBP"

My comment - All of these rates can now be found in the Chart Library, quoted both ways around. To find any of them simply put the ISO currency code, as you illustrated above, into the search facility.

Email of the day (7) - on additions to the Chart Library

"Would it be possible to add the DJ US Regional banks index DJSRBK, and DJ US Financial Sector index DJUSFN to the chart library.

"Thanks"

My comment - Thank you for these interesting suggestions which have now been added to the Chart Library.

Last week's signups for the Free (Abbreviated) Comment of the Day - For the week of August 3rd new signups, including subscribers and pre-subscribers, live in the following countries or regions: Australia, Canada, Hong Kong, Singapore, the UAE, the UK and the USA - 7 in total. In descending order, which topped the list in terms of the last week's new signups? It was the UK, USA and Hong Kong.

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.

Wednesday 13th August 2008

The Case For and Against the Dollar - My thanks to Axel Merk of Merk Mutual Funds for his interesting and informative article on the US Dollar. It is posted in the Subscriber's Area but here is a section:

Given a sharp drop in euro holdings in the U.S. Treasury's Exchange Stabilization Fund, it seems that the U.S. Treasury may have intervened in the currency markets, possibly out of fear that a more significant run on the dollar could have resulted while Congress was pondering about its GSE bailout. While taking out insurance against such a scenario may be understandable, we would argue that the recent surge in volatility may well be the side effect of such intervention. Without having proof, we would not be surprised if other countries, notably Asian governments, also interfered in the markets, although with very different motivations.

Asian countries have been suffering from a slowdown in the U.S. However, because of surging commodity prices and inflation, they have been reluctant to keep their currencies weak to spur exports. With commodity prices off from their highs, Asian governments may be blinded into thinking that inflation is less of a problem; that would allow them to weaken their currencies yet again. Taking advantage of historically low trading volume during August seems to be a tempting opportunity.

The positive of the surge in volatility is that it teaches hedge funds a lesson - too many of them pile into the same trades. In recent months, we believe these funds may have shorted financials to buy commodities and sell the dollar. The global deleveraging must continue; for that to happen, hedge funds must have their access to credit be tightened as well. We hear that brokers close out positions of speculators if margin calls are not met promptly; such a development causes more severe pain in the short-term, but may be necessary.

In the meantime, a lot of technical damage has been done to precious metals prices and hard currencies versus the U.S. dollar. Just as everyone was piling into the same trade, now it seems the speculators all either wanted to exit or received margin calls and had to exit their trades. Pundits were eager to call a major shift in the market, declare the end of inflation, the rebirth of goldilocks.

It is on this perceived drop in inflationary pressures that has contributed to the dollar's recent rally. As European growth may be coming to a halt under a strong euro and high commodity prices, the idea is that the European central bank will focus more on growth, thus possibly lowering rates; that the Fed may be able to raise rates; and that Asia may be able to keep their currencies weak. Indeed, these are good arguments for a dollar rally.

We are concerned that pundits and policymakers alike may be pining their arguments more on hope than reality. The potential for interest rate hikes in the U.S. with drops in Europe may be the most compelling one to support the dollar, but will it happen anytime soon? In Europe, we expect the European Central Bank to take their time before they are convinced that the commodity boom is indeed over. The reason to be skeptical is that, of all things, the Fed may see falling commodity prices as a warning sign of a downward spiral in economic activity. Given the large number of homeowners that owe more on their homes than they are worth, the Federal Reserve may actually want inflation: a recent survey shows that one third of those who bought a home in the past five years now owe more on their home than it is worth. The Fed would never say it wants inflation, but what is needed is a relative adjustment of the cost of home ownership versus other goods and services. This can happen through a decrease in the value of homes - something most undesirable due to the negative implications on consumer spending -, or through an increase in the cost of other goods and services relative to housing. It's the latter that the Fed may be banking on. In our assessment, the Federal Reserve will try to push growth until inflation can no longer be ignored. For the Fed, this threshold is likely to be the TIPS spread over Treasuries; that's the premium paid for inflation-protected securities (TIPS) over bonds. Note that these TIPS reflect core inflation as measured by the government.

By then, real wages may not have picked up and if the Fed indeed decides to tighten monetary policy then to try to bring inflation under control, it may cause a rather severe recession. To wait until inflation is apparent even in the TIPS market may be waiting for too long as it may be extremely painful to get inflation back under control. However, the Fed may think it does not have another choice as the consumer and financial sectors are too fragile to tighten monetary policy.

Will inflation bring the dollar lower? It is possible that we will enter an inflationary growth period, but that may not be enough to cause a sustainable rally. In our assessment, the risk of a lower dollar is alive and well. We don't have a crystal ball, either, but investors agreeing that this risk is real may want to consider diversifying to take that risk into account.

My view - This is the second item of evidence indicating that there was unannounced intervention in support of the dollar last month (*see also yesterday's Email of the day (2)*). I maintain that this was a quid pro quo deal for more WTI-type light crude oil.

However rather than involving Asian countries, I also maintain that any intervention deal would more likely have been arranged with the Saudis during the recent Bush-Cheney visits. All that this would have required is sufficient buying commencing in mid-July to squeeze USD shorts and creating a momentum move on the upside. I would not be surprised to see further information on this quiet intervention from forensic accountants / economists in coming months.

Meanwhile, I agree with Axel Merk's view that, unofficially, many within the Fed, including Ben Bernanke, feel that under current circumstances the US economy actually needs inflation. Austrian school economists rightly point out that no country ever inflated its way to prosperity. Few would disagree but US monetary officials have long been closet inflationists, Paul Volker excepted, and their immediate concern is to pull the economy out of a downward spiral. It's not unlike the prayer: Please make me virtuous, but not yet.

Email of the day - On gold, plus an article posted in the Subscriber's Area:

"I was surprised to hear at the end of last night's audio that you thought gold would be at same level as now in a year's time."

My comment - Many thanks for the article: "Stage two of the gold bull market is just beginning", by Ambrose Evans-Pritchard of The Telegraph (link may require registration so I have also provided a PDF). He covers many of the arguments advocated by perennial gold bugs over a number of years. Fullermoney is sympathetic to some of these views and over the last eight years I have advocated that gold was gradually being remonetised in the eyes of investors.

However, we have also commented at length on gold's lengthy medium-term corrections, evident since its recovery commenced following the 1999 low. Despite some obvious psychological support near $800, it is premature to conclude that this correction has ended, especially given some of the technical damage mentioned in the article above.

It is obviously important for investors to identify secular themes, where they exist, as they often provide the best opportunities. However, no one knows when a secular theme will end, or perhaps even more importantly for traders and most investors, the number and extent of corrections that will occur within that very long-term trend.

I can testify to the cost of not protecting positions when clear technical warnings such as dramatic trend accelerations occur, although fortunately seldom in precious metals in recent years. Also, it has become increasingly clear over the last year that the investment environment, characterised by the west's credit crisis, global inflation, slower economic growth and massive deleveraging, is very different from what we enjoyed between 2Q 2003 and early 2007. This has increased risks, including greater volatility, and introduced much more uncertainty.

With gold, we students of commodity cycles have been fortunate for a number of years because the secular trend was so apparent following gold's emergence from the 21-year bear market against a background of enormous monetary expansion. Better still, the upward trend has been relatively consistent, more often than not.

Best of all, we had a reliable lead indicator in platinum, which telegraphed gold's major moves in advance, often by several weeks. As veteran subscribers will recall and can see again on this overlay chart, platinum's lead was particularly useful in signalling the move to new highs in September 2007; it was also the first to peak following the acceleration into February 2008; it also broke downwards in July, well ahead of gold.

I do not assume that platinum will always lead but there is little doubt from this weekly chart that its prior uptrend has suffered considerable damage in the last five weeks. And while the decline is becoming quite overstretched and is approaching potential support from underlying trading ranges, this is unlikely to support more than a technical rally at present. It will take time for platinum to establish a new floor.

Meanwhile, the charts of gold above clearly show evidence of trend deterioration, in terms of price and a significant breach of the 200-day moving average. So does silver with its larger fall and similar break of the MA, before finding some support near $14.

I do think precious metals commenced a technical rally yesterday, in line with other commodities that have been hit hard by deleveraging, crude oil's plunge and the US dollar's rally which also looks overstretched. In the current economic environment I do not have a strong view as to the gold price a year from now. That would be guesswork at this time but I see no reason why the secular bull market should not reassert itself within the next few years, as part of the commodity supercycle. Meanwhile, I prefer to be guided by the chart action. Remember, gold does best when it is rallying against all fiat currencies (*you can monitor those charts in the Library's Relative Charts section*).

A bell ringing day in the markets, signalling technical rallies - Actually, for many of these instruments it started earlier in the week but the first of the dynamics occurred today. A number of overstretched trends have been checked, consequently closes beneath the recent lows would be required to question current scope for some additional recovery over the short term: gold, silver, platinum (less convincing action today but very overstretched), nickel, copper, soybeans, corn & wheat (all three were limit up today), NZD (upside key day reversal) and AUD (big tail).

Also, although crude oil's move is modest by comparison, it would not be surprising to see the steep downtrend give way to more two-way ranging before long, although I still think there is a good chance that we will see $100 or lower before the next sustainable rally occurs. Natural gas is very overextended and should see a technical rally before long.

Lastly, the SEC's ban on the naked short selling of banks expired today and this has resulted in some evidence of selling, as you can see from these charts of the FTSE 350 Banks, DJ Euro Banks and S&P 500 Banks. If these indices retest their lows, let alone extend the overall downtrends, this would weigh on global stock markets. Conversely, if they hold most of the gains from last month's lows and break above the recent highs, this would help the broader indices to extend their rallies.

Prices of North American instruments were downloaded before today's closes.

My personal portfolio: JII long trade closed - I opened this leveraged trade in JII because it was so oversold last month. Selling the long today was a cautious decision, based on a concern that softness in other Asian stock markets might weigh on India's recent better performance. I sold my December JII long at 334.62p this afternoon, against my purchase at 298.42p on 18th July. These prices include all spread-bet dealing costs.

Please note: I have absolutely no intention of selling the JII in my personal long-term investment account, in any other environment other than the next bid upside acceleration, whenever that occurs.

Additional Commentary by Eoin Treacy

New Chart Library enhancements: High and Low Filter and New Note facility - It is now possible to filter the Chart Library for instruments which have made new 6-month, 12-month or All-Time highs or lows in the last 5 days.

To do this, simply enter the Chart Library via the menu on the left hand side of Comment of the Day. Click on the filter tab in the toolbar in the upper right of the Chart Library screen. You will notice a new aquamarine bar with a drop down menu at the top of the page. Select High / Low Filter.

The High / Low filter has a wide number of applications but here is a bullish example but those interested in shorting weak shares can also filter out the downward breaks:

Select the International Equity Library from the dropdown menu. Select the US from the 'Region' dropdown menu and click the S&P500. Hit close. Next select '12-month' from the next dropdown menu. Then select 'High' from the third dropdown and hit 'Run'.

This should give you 34 instruments, based on yesterday's close and sorted in alphabetical order. Taking a quick look at the list, we can immediately see that the Consumer, Pharmaceutical and Biotech sectors are well represented. When you click on the name of any of the companies, a new chart window opens up. Quickly clicking through this list; some interesting chart patterns immediately present themselves.

Here are some examples: Johnson & Johnson accelerated to a high near $70 in early 2005 before entering a lengthy consolidation. A progression of higher lows has been evident within the range over the last three-years and the share broke upwards last week. A sustained move below $70 would now be needed to offset scope for some further upside.

Lockheed Martin plotted a consistent uptrend from 2004 to late 2007 before losing consistency and moving into a consolidation of gains. It broke upwards this week and the upside can be given the benefit of the doubt provided it can sustain the break.

McCormick & Co Inc peaked in late 2004 and moved into a lengthy consolidation of gains. It had been ranging towards the upper side of this congestion area for much of the last year and broke upwards last week. A sustained move below $40 would now be needed to question scope for further upside.

McDonalds Corp peaked in December above $60 and fell sharply before finding support near $50. It has since moved back towards its high, consolidated the move and broke upwards last week. A sustained move below $60 would now be needed to question scope for some further upside.

Qualcomm bottomed in 2002 near $12 before rallying to near $40 over the next two years. It has been consolidating since 2005, maintaining an incremental progression of higher lows in the process. The share broke upwards to a new recovery high last week and would need to sustain a move below $50 to question potential for some further upside.

Thermo Fisher Scientific remained in a consistent uptrend before encountering resistance near $60 in October. Following a brief pullback to near $47 it pushed back up to test the highs and broke upwards last week. A sustained move back below $59 would now be needed to check scope for further upside.

Wal-Mart surged upwards from its more than 2-year base in March and reached a medium-term peak near $57. It has been consolidating in this area since. Wal-Mart broke upwards to a new high 5-days ago, but was unable to sustain the move and fell back into the range. A sustained move above $60 is needed to reaffirm the overall uptrend.

The methodology for selecting instruments to filter is exactly the same as that for the Performance Filter. I will be updating the Help pages in the next few days but in the meantime here is a link to the Filtering Help pages.

Chart Notes - It is now possible to add a note to any of your charts. You will find the 'Note' tab on the right hand side of the black toolbar above the chart. Here is a link to the Help Pages.

Email of the day (1) - on a correlation between Dollar strength and a sell-off in commodities:

"If one buys a commodity such as oil which is priced in dollars, the investor sells his dollars in exchange for the oil. Conversely if an investor sells his oil he receives dollars.

"The CFTC have argued that index funds effectively hoard commodities, driving up their prices. My guess is that there is some truth in this. Their review, I am certain has rattled some index fund investors who have taken the decision to sell their holdings ahead of any possible rule change which might have nasty consequences, particularly for the larger investors.

"So, if there is a wave of commodity index fund sellers who are exchanging there commodity index investment for dollars, should we not be surprised to see dollar strength as these investors have now switched to 'hoarding' dollars? If so, should we not take a closer look at index fund trading volumes as a guide to when the current dollar rally might lose momentum?"

My comment - Thank you for this interesting question. It is often observed that when Wall Street sells-off, the Dollar firms. The logic behind this correlation is relatively simple because investors selling shares are in effect buying Dollars. The sell-off in commodities, particularly oil, has also corresponded with a rally in the Dollar, so there is a temptation to assume that commodity position liquidation is the cause. Volume for funds such as the iShares GSCI Commodity Indexed Trust has been abnormally high over the last month, but I am reluctant to believe that this continues to be the cause of the Dollar's strength.

While commodity markets are much larger today than they were only a few years ago, they are still dwarfed by the size of the equity and bond markets. Massive percentage liquidations of the commodity positions is unlikely to have the same effect as a broad based equity sell-off and this has been a larger Dollar rally that we have seen since 2005. Liquidation of large commodity positions may have helped to spark the Dollar's rally, but following the break above 74, the move probably owes more to short covering and momentum buying than investors in other asset classes raising cash.

When commodity index fund holders have completed their sales, it will remove part of Dollar's support but by that time, other factors are likely to be more important to the direction of the currency.

Today's interesting charts - Did you know that the Chart Library filter system can scan thousands of instruments in seconds to find interesting investment opportunities?

Soybeans - rallies, having found support near 1200¢ and would need to sustain a move below that level to question potential for some additional upside.

Topix 2nd Section - continues to extend the 10-week downtrend and needs to sustain a move above 2800 to offset scope for some further downside.

Gold - bounces well from the psychological $800 level and would need to sustain a move below that area to question scope for some further short-term upside.

Email of the day (1 & 2) - on additions to the Chart Library:

"Is it possible to include the following two funds in the chart Library? Ta

"1) Aberdeen Asset Management Charity Select Global ex UK Equity Fund Inc 1) Aberdeen Asset Management Charity Select UK Equity Fund Inc."

And

"Would you mind adding the Hussman Total Return Fund (HSTRX in the US) to the Chart Library? Thank you."

My comment - Thank you for these interesting suggestions which have now all be added to the Chart Library.

Thursday 14th August 2008

Stephen Roach: Pitfalls in a Post-Bubble World - My thanks to the subscriber who also sent Email of the day (1) below for this report published by Morgan Stanley. Stephen Roach is always lucid and he is one of the more experienced economists writing today. Here is a brief section:

In short, Washington has responded to this financial crisis with a politically-driven, reactive approach. Policy initiatives have been framed more by the circumstances of the moment than by a strategic assessment of what it truly takes to put the US economy back on a more sustainable path. By perpetuating excess consumption, low saving, unrealistic goals of home ownership, and moral hazards in financial markets, this patchwork approach has the biggest flaw of all - it does little to change bad behavior. Far from heeding the tough lessons of an economy in crisis, Washington is doing little to break the daisy chain of excesses that got America into this mess in the first place.

If this crisis is anything, it is a wake-up call. For all too long, the United States broke many of the most important rules of conduct for a leading economy. It failed to save. It levered asset bubbles in both equities and homes to sustain unparalleled excesses in current consumption. It went deeply into debt to sustain that course of action and borrowed heavily from the rest of the world to close the funding gap. The authorities were complicit in this binge - especially a central bank that condoned unbridled risk taking and excessive monetary accommodation.

The longer the United States sustained the unsustainable, the more it believed in the perpetuity of its charmed existence. The real message of this crisis is that this game is now over. But steeped in denial and feeling the heat of voters in a politically charged presidential election year, Washington politicians insist that the game can go on. More than anything, America now needs "tough love" - a new course that owns up to years of excess and the remedies those excesses now require. It is the broad outlines of what that new approach might entail - more saving, as well as more investment in both people and infrastructure. An energy policy might be nice as well - as would be more prudent stewardship of the financial system. This program won't win any popularity contests. But in the end, it is America's only hope for a sustainable post-bubble prosperity.

My view - Governance is everything and a country's worst problems are usually self-inflicted. In taking a long-term view, investors should ask themselves which countries are consistently demonstrating superior economic governance. Their economies and stock markets are likely be among the best performers over time.

Email of the day (1) - On phases of market cycles:

"Attached is a very good discussion of the road ahead from long time bearish commentator Stephen Roach.

"On a related question, I wonder if there is any update to the superb 4 phase Equity/ Credit Cycle" series from Citigroup?

"Would you agree the market is saying we are moving into "Phase 4", where one is best short Equity & Credit. An environment where the Fuller money "Phase 3" mature bull market themes (Emerging markets & Resources) join the rest of the stock market in underperformance.

"Indeed, if one were to overlay Stephen Roach's 3 stage approach detailed on page 4 pf the attached presentation, then surely this adds weight to a "phase 4" type environment for equities?"

My comment - Thanks for the report, which I have used as my lead item above.

I have not seen a recent update on the Citigroup Four Phase Equity / Credit Cycle reports, but trust someone will forward the next one when it is published. However, as I recall the last report was still looking for an upward spike in emerging markets - a seductive theory for those of us who were overweight the sector.

It might have been a reasonable assumption at the time, but was speared by a massive spike in both energy and food prices, as we now know. Those events exposed the limitations of all roadmaps and mechanistic cycle theories, which are inevitably based on historic observations. If history repeats, or more likely rhymes at best, then the roadmap may offer some perspective. However events can so easily upend the entire premise.

So allowing for the events above, what conclusions can we draw regarding the present market cycle, particularly about how it will play out in future?

The only honest answer is to say - very little that you can be certain of today, except to repeat the obvious - this too will pass. In other words, there is so much uncertainty, from investors to policy makers, that anyone sensible has far more questions than answers.

All we can do is look at what has happened: there has been a considerable shock to the global financial and economic system, resulting in a considerable markdown for equity prices and some other assets.

The 'perfect storm' - consisting of credit contraction, deleveraging, slower GDP growth, higher inflation and interest rates - which I have often referred to in Audios, has not completely passed but it is almost certainly moderating rather than intensifying.

Key tangible evidence to this effect is provided by sharp declines in most commodity prices, and crucially for crude oil. Therefore it is extremely unlikely that a bounce in some commodities, which commenced this week and I illustrated yesterday, will ignite a renewed wave of surging consumer demand and speculative buying anytime soon.

We have low levels of consumer and corporate confidence, suggesting a lengthy convalescence, as I have mentioned before. It is no exaggeration to say that investors are shell-shocked, evidenced by previous waves of climactic selling and often record low sentiment readings.

The good news is that these degrees of pessimism are contrary indicators, evident near the bottom of previous cycles. We also know that levels of cash in money market funds, in the USA at least, are at record highs (*see Martin Pring's report for graphic: Record Cash Levels on Sidelines*).

In conclusion, what investors need most today is patience, in case the convalescence period is longer than what we might wish for. You and I can only deal with the reality that markets provide. We should expect far more pessimism and despair in reports and media coverage, which is typical of market troughs. We should keep this last point in mind, monitor the price charts, expect plenty of ranging, and watch for an eventual shift in central bank policy to targeting GDP growth rather than inflation.

Email of the day (2) - On emerging (progressing) market presentation:

"Watching a webcast today by Tom Elliott, a global strategist with JP Morgan Asset Management here in London, he showed this great chart. Basically he shows charts of GDP growth and market indices for six Emerging Markets (aka Progressive Markets). Whilst he is not overweight short term as P/Es need to fall further, long term he is a bull based upon Commodities; Transport/ Infrastructure spend paid by cash rather than debt and the growth of the consumer. As always keeping my emails short and to the point."

My comment - Many thanks, and quite a few other subscribers will agree with the long-term premise.

Email of the day (3) - On the copper chart:

"I'm not much of a chart guy as my infrequent previous comments have indicated but looking at the 5 year copper chart from the library I can stick my ruler along the bottom of the trend line and get a perfectly straight line along the lows from roughly may 2005, feb 2007, dec 2007 and now mid-aug 2008.

"At all of these rising lows copper bounced significantly - any significance to this ?"

My comment - Charts show you exactly what the market is doing, both historically and also today. I am not aware of anything else that conveys a similarly important, factual message in terms of supply and demand.

You have identified a linear uptrend, which others may also be watching, so it has some psychological significance. However, we have pointed out copper's failed breaks above the 400 level and its recent breach of 350. Therefore a sustained push back above that level is required to reaffirm the linear uptrend and also a downside failure.

Please note - I will be away on Friday the 15th.

Additional Commentary by Eoin Treacy

Chart Library High / Low Filter Example looking at new 12-month new lows in the last 5-days for the S&P 500 - As with yesterday's example, here are the instructions how to create this filter:

Simply enter the Chart Library via the menu on the left hand side of Comment of the Day. Click on the filter tab in the toolbar in the upper right of the Chart Library screen. You will notice a new aquamarine bar with a drop down menu at the top of the page. Select High / Low Filter.

Select the International Equity Library from the dropdown menu. Select the US from the 'Region' dropdown menu and click the S&P500. Hit close. Next select '12-month' from the next dropdown menu. Then select 'Low' from the third dropdown and hit 'Run'.
Based on yesterday's close this filter should produce 20 results. This is an interesting statistic in and of itself because yesterday's filter of new highs produced 39 results. Here are some of the more interesting examples:

Edison International accelerated to a peak near $60 in May 2007 and over the course of the next 7-months ranged laterally above $50 which had marked the previous peak. It broke below that level January and although it rallied quickly back above $50, was unable to sustain the move. It broke down again three weeks ago and would need to sustain a move back above $48 to question scope for some further downside.

Federated Investors plotted a gradual uptrend over the last 8-years where it consistently failed to sustain upside breaks. This was also the case this year when it posted a new high near $45, but subsequently fell quickly back to $30. While this has been an area of psychological support in the past, the current move breaks the progression of rising lows. A sustained move above $36 is now needed to check potential for further downside.

General Growth Properties has already fallen considerably from its high near $67 and rallied well having found support in March along with the majority of other shares. However, it broke to new lows five-weeks ago and the downtrend is gathering pace. An upward dynamics is needed to check momentum beyond a brief pause.

Prologis maintained a consistent uptrend before peaking in early 2007. The subsequent volatile ranging phase has the characteristics of a Type-3 top, as taught at The Chart Seminar. The share has fallen abruptly over the last few months and needs to sustain a move above $50 to question potential for some further downside.

Williams Cos. plotted a remarkably consistent uptrend from its lows in 2003, through to its recent high near $40. The failed break to new high ground in July and subsequent pullback was the first time the share had failed to sustain an upward break. Last week's decline broke the progression of higher lows. This suggests the onset of at least a potentially lengthy medium-term correction and it needs to sustain a move back above $32 to question scope for some further downside.

Forbes.com: Valero Looks Finer With Fatter Crack Spread - This article by Samuel Ro for Forbes.com covers an energy sector which has languished due to oil's strength but may benefit from its weakness. Here is a section:

Companies in the energy sector have not benefited equally from the bull market in oil and gas.

High oil prices have helped integrated energy companies like ExxonMobil and services companies like Schlumberger book record profits. Refiners, however, have seen their profits plummet.

This disparity is often explained by the crack spread, the difference in price between a barrel of refined product and a barrel of crude oil. In recent months, crude oil and gasoline prices reached record levels, but crude oil price jumps have generally kept ahead of gasoline prices. In other words, the crack spread has narrowed. Because refiners buy crude oil and sell refined products like gasoline, shrinking crack spreads bring deteriorating profit margins.

The recent pullback in crude prices could spark a rebound for refiner stocks such as Tesoro and Sunoco. The quantitative model employed by the Forbes Growth Investor newsletter, however, has singled out one refiner that may outperform its peers.

Valero Energy operates 16 oil refineries across North America with a combined throughput capacity of over 3 million barrels per day (BPD). It sells refined products such as gasoline, heating oil, diesel fuel and jet fuel through 5,800 wholesale and retail outlets under the Valero, Diamond Shamrock, Shamrock, Ultramar and Beacon banners.

The company's refining segment was responsible for 91% of 2007 net sales and 97% of operating income. Over half of its refining throughput capacity is in the Gulf Coast region (Texas and Aruba). The rest is in the Northeast (Quebec, Delaware and New Jersey), the mid-continental states (Tennessee, Texas and Oklahoma) and the West Coast (California).

My view - Crack spreads (2:1:1, 3:2:1, 5:3:2) broke down from a relatively well defined trading range in February before finding support near -240 in June. They have since rallied well from this area and would need to sustain a move to new lows to question recovery potential. -160 marked the lower side of the previous 18-month range and a sustained move above that area would be needed to indicate that the market has returned to a more normal cycle. (Also see Comment of the Day on May 9th)
http://www.fullermoney.com/x/default.html?id=1350&schtxt=crack

Refining companies have fared particularly badly as the declining crack spread ate into profits even as the price of oil made new highs. Their profitability may improve if the crack spread can sustain the present rally. Related equities fell in line with the crack spread but have been slower to rally, presumably because of fears about demand destruction due to high gasoline prices. However, these may become less or an issue if oil continues in a medium-term correction as we expect.

Valero Energy topped out near $80 in July last year and remains in a consistent downtrend. The fall from $50 to $30 was an accelerated move and the share is looking overstretched. However, no upward dynamics have been posted and trading activity over the last few weeks has been steady at best. It needs to break upwards from this short-term range to realise short-term recovery potential. A sustained close below $30 would reassert the medium-term downtrend.

Sunoco peaked in early 2006 and moved into a consistent downtrend from July 2007. The progression of lower highs, which were the hallmark of the downtrend, has been broken by the recent rally. And it would need to sustain a move below $32 to question scope for some further upside.

Tesoro peaked in 2007 and entered a consistent downtrend from October. The downtrend remains intact but is losing momentum. However the share needs to sustain a rally above $20 to break the progression of lower highs.

Looking at these three refiners, we see that Sunoco is responding best to lower oil prices and an improvement in the crack spread. It is likely to continue to lead the group as long as the technical background continues to improve.

Mineweb.com: How the mighty are varied - This article by Barry Sergeant covers the varied interests of the world's largest mining companies. Here is a section:

The world's biggest diversified resources stock, BHP Billiton, seems to have it all: oil and gas, aluminium, copper, nickel, iron ore, manganese, metallurgical coal and energy coal, with additional exposures to uranium, gold, zinc, molybdenum, lead and silver. In its latest financial year, BHP Billiton's biggest money spinners were base metals (especially copper), followed by oil and gas, iron ore, and metallurgical coal.

Rio Tinto majors in iron ore, aluminium, copper, diamonds, coal, uranium, gold, and industrial minerals, and recently overhauled Vale as the world's No 2 miner, measured by value. Vale has long ranked as the world's leading seaborne iron ore producer, but is widely diversified, and in recent years has made considerable efforts to build a dominant position in nickel.

Vale's second-quarter 2008 revenue increased to USD 6.7bn from USD 3.8bn in the comparable 2007 quarter, but nickel revenue plunged to USD 1.9bn from USD 3.2bn. It seems that the group's nickel exposure has been the key reason for its derating relative to its peers.
Anglo American, characterised by heavy exposures to platinum (via its near-80% interest in Anglo Platinum), and copper, and, to some extent, ferrous minerals, stands out as the least price-penalized top 20 miner. Shenhua, the China-listed coal producer, stands at the opposite end of the scale, with a stock price that has lost nearly three-quarters of its value. The stock has suffered the added malady of a massive bubble bursting across Chinese stock markets.

PotashCorp, in position number 6, leads the heavily rerated potash mining group; like a number of its peers, it also mines phosphates, and produces nitrogen from natural gas. Mosaic and Uralkali also rate as Tier I potash producers, but have been fairly heavily sold down in recent months.

Xstrata, heavily exposed to earnings from copper and coal, has been sold down on falling earnings from its zinc, nickel and lead operations. Norilsk, most heavily exposed to nickel earnings, has been sold down in patterns similar to those seen for Vale. India's NMDC has performed relatively well, in line with its focused iron ore output.

My view - The world's largest miners, particularly those controlling top-class assets in politically stable parts of the world continue to provide excellent exposure to our long-term Supply Inelasticity Meets Rising Demand theme. However as with all such secular trends, they will go through medium-term periods of consolidation and relative underperformance when compared to other sectors.

The FTSE 350 Mining Index has posted impressive gains over the last 4-years and accelerated to a high near 30,000 in May. This was a spectacular outperformance of the wider market and marked an important medium-term peak for the sector. From its high, the Index has fallen sharply back towards 20,000 in a move which has caused investors to question the integrity of the overall theme.

However, while the stock market is in a period of consolidation, the secular theme remains intact. Infrastructure development across the global continues to be prioritised; particularly in the emerging markets. Supply of key commodities continues to experience severe bottlenecks.

The impressive upward acceleration from March to May surprised and delighted many investors but the subsequent retracement has been traumatic. In the last few days, the Index found support above 20,000, which has been an area where demand has returned in the past. A sustained move below 20,000 would be needed to offset scope for some further upside and suggest support building will take place at somewhat lower levels.

The market environment remains uncertain and anxiety levels remain at elevated levels so, given the size of the drawdown, it remains questionable as to how quickly the Index can rally back towards its highs. With that said, this is probably a bad time to sell, given the proximity of historical support and the overextension in the market. Longer-term investors may be tempted to nibble at these levels as valuations are becoming more attractive, but doing more than that at this stage could be considered relatively risky.

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

"Could you please add ASX Code: PXS (Pharmaxis) to your Australian chart library?

"Thank you."

My comment - This can already by found in the International Equity Library.

Friday 15th August 2008

Commentary by Eoin Treacy

Gold, Silver Slump, Leading Commodities Drop on Dollar, Growth - This article by Feiwen Rong and Dave McCombs for Bloomberg covers today's fall in the precious metals market. Here it is in full:

Gold plunged below $800 an ounce, silver dropped as much as 12 percent and oil, corn and copper slumped as the dollar's rebound reduced the appeal of commodities after a six-year boom.

Palm oil tumbled as much as 9 percent, and rubber and wheat fell as the dollar headed for its longest winning streak in more than two years and on concern a spreading global economic slowdown will reduce demand for raw materials.

Commodities, measured by the Standard & Poor's GSCI index, have tumbled 21 percent from their record July 3, descending into a bear market. Oil traded near its lowest for more than three months, gold for eight months and silver for almost a year. Copper and corn reached six-month lows this week.

``Prices have made a peak,'' said investor Marc Faber, 62, who publishes the Gloom, Boom & Doom Report. ``Whether that is a final peak or an intermediate peak followed by higher prices, we don't know yet. It could go lower,'' he said by phone today from Chiang Mai, Thailand.

Gold fell to $782.27 an ounce, its lowest since Dec. 3, at 9:52 a.m. London time today. Silver's 12 percent drop was the most since June 2006 and the metal traded at $12.905 an ounce, down 9 percent.

``It's a big shakeout in gold and silver for people who have been long but don't really believe in the commodities,'' said Mario Innecco, a trader at MF Global Ltd. in London. ``If you do it speculatively, with leverage, I don't recommend buying it now.''

Hedge Funds
Gold has dropped 24 percent from its record $1,032.70 an ounce on March 17 and silver has slumped 40 percent from its $21.3550 peak the same day.

``I expect commodity prices to remain subdued until mid- 2009,'' said Arjuna Mahendran, head of investment strategy at HSBC Private Bank in Singapore. ``The major issue in commodities is the proliferation of ETFs and hedge funds. As they unwind positions, this leads to the price overshooting.''

The dollar has climbed 5.3 percent against the euro this month and reached a 5 1/2-month high today, heading for its fifth weekly gain. U.S. consumer prices rose at the fastest pace in 17 years in July, reducing the ability of the Fed to lower interest rates should the economic slowdown deepen.

Gold's rally has been ``dollar-driven probably because we are supposedly seeing more writedowns in the European banks,'' Charles Dowsett, head of structuring and trading of precious metals at ABN Amro Holding NV, said by phone from Sydney. ``We could see gold go all the way down to $750 an ounce.''

Possible Rebound
Gold may rebound from a slump and rally through 2010 as fabrication demand rises and on expectation the dollar will resume its decline against the euro, Citigroup Inc. said, forecasting the metal to average $950 next year and $1,000 in 2010.

``Longer term, we would not be surprised to see gold double,'' the bank's analysts John Hill and Graham Wark wrote in a report. ``We would be aggressive buyers at current levels expecting gold to work higher through 2009/10.''

Crude oil for September delivery dropped as much as $2.26, or 2 percent, to $112.75 a barrel on the New York Mercantile Exchange, and traded at $113.10 at 9:58 a.m. London time. Copper fell 2.4 percent to $7,207 a ton on the London Metal Exchange, corn declined 2.8 percent to $5.61 a bushel, and palm oil tumbled as much as 8.7 percent to 2,392 ringgit ($714) a ton.

My view - Precious metals extended their medium-term downtrends today with breaks below the lows posted this week. As the above article illustrates bearish sentiment is multiplying as the metals fall but is this to be taken as a contrary indicator at this stage?

Platinum continues to lead the other precious metals and has been as consistent on the downside as it was throughout its impressive advance from $1600 to more than $2200. The trend is now looking overextended and today's action is potentially climactic. An upward dynamic is needed to confirm this hypothesis.

Deleveraging in the commodity sector is sharply affecting the ability of precious metals to rally significantly, but what we are now seeing is an overshoot in some of these markets. Platinum has fallen 39% from its highs while palladium has fallen 50%. These are extraordinarily sharp corrections and have done some significant technical damage to their uptrends. It now appears that while there is potential for a relief rally, subsequent support building is necessary before either platinum or palladium will be able to generate rallies powerful enough to exceed this year's highs.

Silver broke down from the 5-month range late last week and has fallen to a low of near $12. A fall of 42% from the high. Silver has been prone to sudden reactions such as that seen today, which have often been climactic signals. As with platinum an upward dynamic would help to confirm at least a short-term low.

Although gold has fallen 25% from its high, it is in better technical shape, so far, than the other precious metals. This week saw the metal break down from the 5-month range and drop to a low near $775. The metal was unable to sustain today's lows and rallied well by mid-afternoon. It would now need to sustain a move to new reaction lows to question scope for some further short-term upside.

The fate of the Dollar is a not insignificant factor in the direction of precious metals and its recent rally has been a headwind. The Euro has been in a staircase uptrend against the Dollar since early 2005. The current reaction has done technical damage to the overall uptrend and the rate is currently testing the MDL stop near $1.44. An upward dynamic is needed to check momentum beyond a brief pause. As measured by the Dollar Index, this is the biggest Dollar rally since 2004 and while it is looking somewhat overstretched, a sustained move below 76 would be needed to question scope for further upside.

Oil is by far the most important commodity and its decline has also be a headwind for precious metals. It entered a medium-term correction as it broke down from the Type-2 top as taught at The Chart Seminar and has yet to find a bottom as it continues to move towards the psychological $100 level and potentially lower. A sustained move to new high ground would be needed to offset scope for further downside.

For investors in precious metals this has been a harrowing time where portfolios have taken a beating. There are a range of arguments against this sector advancing, including a strong dollar, deleveraging in the commodity complex, demand destruction due to high prices and a negative platinum lead. However, we must not forget that acceleration is an ending signal and they cannot keep falling at this rate so there is cause for some optimism.

Platinum's upside acceleration was a warning that we were on the cusp of a medium-term correction. However, the faster downward acceleration this week also indicates that we are swiftly approaching the lows for this reaction. At Fullermoney, we continue to believe that precious metals are in a long-term secular uptrend, but given the technical deterioration, investors will have to be patient before these metals can justify significantly higher levels. However, for investors unwilling to wait out the correction, this is probably a bad time to sell considering how overextended the market is right now. Patient, more risk tolerant investors may consider nibbling around current levels or more prudently wait for a clear upward dynamic which will signal that at least a short-term floor has been reached.

Eoin's personal portfolio: silver and gold longs opened - I know I am taking risks by attempting to anticipate the market but I am willing to take that risk by staying well within my allowable capital for these trades. If I am wrong in thinking that we are in close proximity to a low, then platinum will deteriorate further and today's lows will be taken out in sharp order.

For the record, I opened small initial long positions in October Gold at $792.05 and December Silver at $13.225. All prices include spread-bet dealing costs.

Stop Press - My too-close silver stop was hit as the metal fell through $13. I continue to hold by gold long.

UBS Cuts Estimates for Citigroup, JPMorgan and Morgan Stanley - This short article by Ambereen Choudhury covers the continued tendency of banks to issue negative ratings on each other. Here it is in full:

UBS AG cut its price estimates for securities firms including Citigroup Inc., JPMorgan Chase & Co. and Morgan Stanley on expectations that a tough market environment will hurt third-quarter results.

``We continue to be neutral on both the brokers and universal banks as we think balance sheet concerns and lackluster earnings will continue to weigh on the stocks,'' said UBS New York-based analyst Glenn Schorr in a note to clients today.

My view - Banks have made money by shorting each others stock over the last year and continue to issue negative recommendations on each other. Banks led the way on the downside and remain a significant bellwether for the wider market.

The ban on 'naked shorting' expired a few days ago and banks fell back to the bottom of their tight short-term range. However, we have yet to see any of the major banks making new lows. For the most part they have sustained their impressive rallied from mid-July. As long as this is the case we can continue to give the nascent stock market rallies the benefit of the doubt.

Email of the day (1) - on SPDRs:

"Please excuse my ignorance

"But please could you explain what are S&P depositary receipts (symbol SPY) is there any a connection with S&P?"

My comment - The S&P Depositary Receipts are more commonly knows as SPDRs and are the Standard & Poors stable of ETFs. SPY is the S&P500 tracker.

Email of the day (2) - on an addition to the Chart Library and an enhancement request:

"Please can you add Kansas hard red winter wheat to the Chart Library?

"The improvements being made to the library are much appreciated. I would really like it if it is possible to add a function that allows one to draw trendlines on charts. If this is not a major change to incorporate, please can you consider it?

"Many thanks and kind regards"

My comment - Thank you for these interesting suggestions. I have added Hard Red Winter Wheat to the Chart Library.

The ability to draw lines on charts is one of our priorities but will probably not be implemented until after we have completed some additional filter studies.

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

"Pease can you add Li-Ning (HK:2331) to the chart library.

"Thank you."

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

Email of the day (4) - on p&f books:

"Could you please recommend me a paper or a book where I can read about the P&F technique?

"Many thanks for your help."

My comment - I don't know of a point & figure book I would recommend because I learned most of what I know about point and figure from the Bloomberg help pages, some hand written notes a friend loaned me and The Chart Seminar. If subscribers feel confident about recommending a book please let me know. Here is a link to the Introductory pack from The Chart Seminar.

Please Note - David will be back in the office on Monday.