

Gold & Dow Jones Finally Invert: The Golden 'It Had To Be'



January 6, 2008

JAPAN

Nikkei:

I declared yearend to be a fulcrum point that would catch everyone off guard, because managers wish for markets to respond to their book-closings, vacation plans, or whatever other arbitrary factors for which the markets have no concern whatsoever. Indeed, yearend 2007 will have created extremes that can best be described as pauses that were caused due to seasonality. And with the New Year upon us, I warned, the true trends would now take hold.

They have.

Consistent with a 100% perfect 19-year track record of identifying every secular and cyclical turning point in the Nikkei, I used last May – June to repeatedly warn of a smash to the 14,000 – 15,000 area by yearend, from 18,000. This, I argued, would be followed by the next cyclical leg of the secular bull market, the low of which I had identified in March – April 2003 under 8,000.

However, I argued and do still maintain, the Yen's new bull market and the Dow's new secular bear market would be a drag on the multi-nationals that dominate the Nikkei. The same factors, I argued and do still maintain, would be a major positive for Japanese domestic stocks.

The Yen's renewed secular bull market got going 5 months ago and, in 2004, 5 months had passed since the Yen's peak, before the domestic stocks had started down. Everything fits.

The long since forecast mirror image of the 1990's is underway: The Nikkei and Dow will go up and down together, quarter-over-quarter, but the Nikkei will be making higher highs and higher lows, while the Dow will be putting in lower highs and lower lows.





Domestic Stocks:

Headlines are appearing here and there in the esoteric circles that my research occasionally sources, that managers are seeking emerging stocks and value equities in 2008. I won't comment on emerging country stocks, except to say that at least folks are showing that they are looking elsewhere than where the money has been made recently.

The only thing that has masked the building strength in our chosen Japanese themes has been the Nikkei, which has served as a general deterrent from Japanese equities, the domestic themed and value components of which have been declining on low volume, unlike the big caps (Nikkei, Topix). And, again, Westerners are loathe to do anything original like, say, lead and front-run others before yearend. Leadership requires too much imagination. That, or no one likes to feel lonely.

Last month's report and general theme focused on...*"esoteric investment product for windfall gains in 2008 for hedge funds and sophisticated individuals,..."* : Regarding the latter, I advised paying attention to the portion in the Shanghai section entitled, *"The opportunity."* This month, I draw you attention to Shanghai's sub-

section entitled, **"The special situation."** The Shanghai section follows immediately below.

Conclusion & strategy:

100% long the Yen (see Yen section below), investors hold Japanese domestic demand oriented value stocks.

SHANGHAI

Consistent with what should be a powerful year for the Chinese economy, the Shanghai is acting in a manner that is consistent with prior analyses in these recent reports. Namely, I felt that the market could actually double top or even make a slight new high. This could indeed occur when the Dow completes a wave-2 countertrend rally, after completing this ongoing smash.

For those thinking of Chinese indices that are tradable and/or optionable, however, think again.

The two available indices that can be traded exclude certain stocks due to Chinese trading restrictions. The upshot is that these two US-listed indices look like, and have patterns more akin to, the Dow than to the Shanghai, which, ultimately, itself follows the Dow. The simple reason is that inflation and protectionism will put in the final high, at that moment when folks least expect it (1st quarter, I suspect). Much as has been the case with the Dow!

The special situation:

The key to profiting from a major international out-performance play stems from knowing:

- What region will be strong
- What offers the best value within that region, relative to the volatility of that index, which in turn determines the long-term premiums that one must pay for that index
- That engineering which further maximizes leverage AND diminishes risk

Taken together, these three points spell enormous risk-adjusted long-term profit potential.

The last bullet point reflects why little opportunity has been lost, for now, in acquiring what I have engineered, with regard to the special opportunity that the December 2, 2007 report discussed.

For now, it simply seems as if everything is continuing according to the same inter and intra-market relationships. To the trained eye, however, this is not the case. The first quarter will bear this out, as indices start off in new and different inter and intra-market trends (note the Dow and gold today). To truly benefit from that, again, I have structured that which insulates against this recent kind of forecasted turbulence, but the greater feat will have been to profit mightily by way of this same structuring/strategy. For now, as things get going, its first benefit will have been the insulation against pain. Soon it will have been a matter of extreme profit leverage, even as others suffer sorely. And, with that,....

NEW YORK

Last month's report concluded, "2008 is going to be a whopper!" A headline after this year's first session read: "Dow off to its steepest start-of-a-year point drop ever."

I warned that Christmas was bad and that Thanksgiving sales tipped off the smart money. I joked about how the easily manipulated business news shows ran stories of how Christmas would be saved by Europeans traveling to the US to save money on a cheap dollar (since airfare is free for those European shoppers).

Many times I have warned that a collapse in consumer spending leads to a Dow collapse within a month. And this is not theory. This is chartable and empirically knowable, therefore. Well, forebodings about the retailers have been among the headlines shaking the markets. When the Christmas sales numbers come out in a few months, the smart money will have dumped their shares onto the guys who watch the backward looking news shows.

Remember, business shows don't seek to help investors with tomorrow. They are there to sell and what sells is to play up to what people are already believing (hence, the concept of contrarianism). Ron Insana is gone (from prominent sight, that is), and is anyone out there worth watching now (just a fan's thought, there)?

Technical:

The following chart on page 6 clearly and unmistakably shows 5 completed waves from the 2005 2nd-quarter low. It is as unmistakable as the 5-wave subdivisions within wave 3 (the sub-divisions are bracketed). The pursuant 1-year daily chart reflects the week's decline, which is not included in the weekly chart above it (weekly charts are updated weekly).



The chart immediately above shows a deadly shoulder-head-shoulder formation that, after running into moving average resistance, rolled back down, after having been artificially held up for yearend (window dressing and all that, which is why I recommend that industry pros take their vacations some other time and not miss the opportunities that their silly colleagues create for them).

From last month's report:

"The moving average (weekly chart) shows support to be in the Dow 11,200 area, while the 1-year daily chart that follows it illustrates 200-day moving average resistance achieved. Still, it can be surpassed with a move to 13,600, but it would change nothing, in the context of the discussion above."

This analysis could not have been more accurate. Therefore, we can get to 12,000 imminently, but the multiple starts and stops (downtrend sub-divisions) means that the likelihood of a decline toward 11,000 as I've contemplated before (see previous paragraph) has become that much more likely.

"Hitting 2700 is dangerous enough. Will they actually cut $\frac{3}{4}$ of a point?"



You are encouraged to revisit last month's report to review the forecasts made therein. The only chart reprinted as-is is that of the

NASDAQ which is found immediately above at the bottom of page 7. It is preceded by a facetious comment from last month that indicated that no fed news could come that would save the market, since it wasn't even in the cards anyway. By the way, the NASDAQ was down almost 100 Friday, and is a long way from 2700 now...and a long way from where it's going to be.

VIX:

I have commented and maintain that this new bull market in volatility is defined by the 200-day moving average and this is most obvious by the chart immediately below.

By connecting the lows and by then connecting the peaks of the second and fourth quarters, an obvious and menacing triangle becomes evident. The significant upshot is that volatility will spike toward its highs in the mid-30's, which would coincide with the coming stock market debacle.



Conclusion and strategy:

The conclusion from last month's report remains ideal:

"The Dow in 2008 has an appointment with 8800, and even the first quarter may well get the job done. I've learned this over the last 25 years: When the Street realizes that something is going to happen, they just make it happen and don't wait for others to sell ahead of them. Remember, the Fed has already forecast a weaker 2008. HEAR THE BELL!!! It's ringing so loud, it's drowning out the fat lady."

Related equity comments appear in the gold section below.

PRECIOUS METALS & DOLLAR (YEN):

Technical (gold):

From last month's report:

"Beware the yearend opportunities, as extremes are achieved in equity, currency, and metals markets, as fund managers are guided by business considerations, as opposed to purely market factors and considerations."



Gold made new all-time highs this past week and, in doing so, finally showed the *bull world* a scary sight. At last, the

Dow and gold went in opposite directions. Do you know what this means? It means that it isn't a matter anymore of the Americans counterfeiting the world to death. Funny money increases nominal prices no more. It means, my friends, that bad news is bad news. We are exiting bizzaro-land.

Anyway, I've been perfect on gold since exactly 6 years. Of all the bulls last year, my year beginning forecast probably came in among the very closest to where we ended up. As for \$1000 in 2008, stick around. All that has happened has occurred without the equity market bear yet in gear, nor with its attendant panic. So, the best is yet to be.

Technical (silver):

Again, reprinted:

"Readers were advised to go 200% long on a spike toward \$11.00, which was perfectly achieved.

"I stated clearly that *this move alone in one's holdings would create the year's desired portfolio returns, all else notwithstanding*. Frankly, for 6 years, it has been as easy as taking candy from a cavity-ridden Western central banker."



Notwithstanding the superb and easy returns that readers have enjoyed by following the precious metals strategies in these pages, such as the commentary above, which provided investors with a 100% return on capital(!) - and precisely to protect some of that profit - one should note the lower high in silver and scale back to 100% long, since the move to \$20.00 does not feel to be underway, intuitively speaking.

Remember, the strategy above doubled capital on a mere move into the 15's, which was such an obviously un-risky investment – if only one knew how to time getting in. And, in the precious metals, that's what you pay me for.

Starvation:

Not to be a downer, but, in the past, I have extolled the virtues of the work of one Dr. Raymond Wheeler, whose work I came upon ages ago thanks to Robert Prechter.

Dr.Wheeler has been in heaven for many years now and has been calling the market correctly for just as long. He foresaw everything, which occurred, as regards the shifts of power from East to West, emerging markets, bear markets, you name it. How? Climatology. And climatology precedes psychology (technical analysis), since climate determines psychology (see bullet points below).

[For you curious purists: Before and dominant to climatology is astronomy, since the stars have the lead effect there (note that the most successful trader of all-time was W.D. Gann). Fundamentalism is at the bottom of analytic forecasting, since it lags the most. Okay, enough education.]

Basically, there are 4 categories.

- Warm and wet (most bullish)
- Warm and dry
- Cold and wet
- Cold and dry (most bearish)

The latter speaks of inflation that is due to shortages, rather than excess demand as a result of growth. Countless millions starve, not 'just' 60,000 children a day, maybe some number that CNN would have to cover just because the planet's democracies start to....maybe. War. Well, you get the picture. Inflation due to intense human misery and unspeakably godless greed. You, know, that for which you can count on bible thumpers. (And this is why I shouldn't write at 4:00 a.m.)

YEN:



From the December report:

“The lag between the currency and domestic non-multi-national equity turning points was the same in 2004 as it is now, as will be evident very soon, with 2008 upon us.”

The crucial importance of the Yen is not only as regards Japanese non-multi-national large-cap equities, but as regards US stocks and real estate, as well. The Japanese finance minister very recently said that Japanese investment is solely about parking reserves, while Japanese individuals are starting to stampede back home as they customarily do when the currency going gets rough. It's ALWAYS the same.

In any event, the Chinese he pointed out, however, have to reinvest in US assets with their economic surpluses (though that policy is about to nosedive, based on what the Chinese have been warning). Anyway, the Japanese, he explained, are invested in US Dollars as a portfolio mater, not as a matter of reinvested surpluses.

Anyway, after pulling back to 115, the New Year has quickly reverted the Yen back to 108. This is the most profitable major fiat currency now, as I've been writing for some time. While I was early, we held the Swiss Franc (after having also held the Euro), and which I still hold. So, I have provided the very best risk-adjusted currency asset allocation since 6 years, this month. Today, it remains so with:

Asset Allocation:

- 45% gold
- 5% silver
- 25% Yen
- 25% Swiss Franc

From the September report: **“This is a wonderful time to own the Yen, gold...and silver!”** I have a feeling that I will be reprinting this for some time to come.

Good fortune to all,

Sid Klein

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