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MANAGERS!
IT IS VERY LATE

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SUMMARY:
The news is disastrous. Let's simply let it go at that.

At the lows, I simply explained that all the bad news will be ignored and that if one wishes to remain enthralled and distracted one could guess what the background news will be when the peak comes. I offered some ideas on that, but the news is something that everyone touts, so I therefore continue to offer what others do not, rather than offering what is available anywhere else.

I was big on discussing and forecasting fundamentals when I was 6 – 18 months ahead of the curve in making such analyses, principally in Japan where such foresight and analysis were utterly out of the main.

Okay then, the fundamentals is now just descriptions of excuses, and I can't be too much bothered. So, now, let us make money.

This summer, there remains a final major phase of rally to this intervening countertrend phase which I have likened to 1931 in prior reports. As such, I draw your critical attention to secular shifts in inter-market directionality, as well as ***historic*** shifts in directionality, as per the Kondratieff cycle. This is crucial for hedge and other managers of all stripes.

The forecasted rallies of "several thousand points" in our equity markets of interest have long since been confirmed and rewarded, again underscoring the accuracy with which I have remained attuned to where we are in the otherwise hazardous Kondratieff cycle. The purpose is to protect wealth with such knowledge, while turning hazard into opportunity.

For 2009, I forecasted China to be the strongest market of the year, followed by Japan. However, while this letter underscores SKGS' significant forecasts and strategies, I must underscore in this summary the basic points that apply to all markets:

We continue to focus our hedging strategies – and global asset allocation strategies, by extension – on acquiring (warrant) premium that is deemed to be undervalued, since similar directionality between markets causes a mispriced warrant, if correlated markets later shift directionality as expected.

This is critical now because there are lows or acceleration points at higher lows for different inter-market structures (long term premium on cross trades), precisely because there may be a final phase of rally for certain markets, while others merely advance in a bigger trend (i.e. - precious metals) and are therefore temporarily sharing a directionality that masks the fact that such shared trends are actually in flux, to the more trained eye (Kondratieff is a tricky business, it may seem).

Identifying turns in markets is not the same as identifying the turns in the relationships between them. Of course, and as I always point out, this is all-important for global asset allocation, as well.

The matter becomes still more subtle and critical when the changes in relationships and directionality are undergoing multi-decade shifts; and such is the stuff of windfall profits.

So, during this phase of preparing for a final rally within this post-collapse countertrend rally phase, I again seek what I found in 2008 (when there was doubt at that time, as to whether a final rally in global equity markets would ensue or not):

Given the crosscurrents contemplated in this rally, I believe we again have situations in long dated outperformance premiums, where the underlying index will increase, regardless the initial direction of markets, before increasing in earnest once the global bear market resumes.

JAPAN

When Japan scoured the bottom, these pages identified that bottom as a re-test that was occurring on a typical lag to China, which had already made its low in the 4th quarter (see Shanghai below).

I further pointed out that a failure to make a new low with the Dow was merely confirming my view that these 3 markets would enjoy the order of strength that we have in fact seen: China, Japan, and, lastly, New York.

So, as far as "a multi-thousand rally" that would imminently begin, the Nikkei has rallied about 43%, en route to my target of 11,000 – 12,000. As we see from the 2-year chart, the Nikkei broke out over 9,000, which has become support.

It was always discussed that cross-charts bottom about 3 months ahead of the individual markets. It was further evident that the very long term low against the Dow was .9. Also evident, as expressed here, was the fact that the Nikkei was anything but a preferred Japanese index. Therefore:

Firstly, **Japan-related strategies** were best entered when the Nikkei tested .9 (the Dow's value), during the 4th quarter. Secondly, that the benchmark has rallied from .9 to 1.1, an increase of about **22%.**

Please scroll to next page for 2-year daily Nikkei chart.

CHINA

In the 4th quarter, I made clear that what had been my favourite short for 2008 was now my favourite long for 2009. I added that all worthwhile outperformance plays should ideally be established during the 4th quarter, since the primary consideration was what I believed to be Shanghai's superior position against "everyone" in 2009, and that its low would therefore bring the best global outperformance plays.

This was and is being born out, as this index is up about **75%** from its low (twice the performance of the Dow), at which point I was repeatedly and graphically highlighting the outrageous potential that existed in this market.

NEW YORK

The Dow has resisted at that level at which the Nikkei has since created support (9,000). Simply, the Dow will have been the laggard that will probably not attain to the earliest expectations that I had had for it, in the way of target rebound levels. However, it will surely confirm my earliest prognoses for inter-market relative strength, among our three benchmark global equity indices.

The global daily stochastic readings support the notion of a pause, but that is neither here nor there. What matters is that it is very late in the game for making adjustments....and re-positioning is a must at this time, just as positioning oneself during the 4th quarter was the only way to maximize 2009's returns. The cautioning to money managers here is clear.

Global indices and sectors are approaching critical resistance levels that merit action, even though those levels will be broken. Simply, global rotation will begin in earnest soon and the best investments are those that will trend higher with the markets, while trending still higher even as markets revert to the bear camp, whether such appreciation results from changing relative performance (i.e. - shift in co-directionality), or even absolute performance (shift in *historic* co-directionality).

VIX

The uptrend in New York has been accompanied by the familiar inverse relationship to the VIX. I had felt that it was worth noting that this relationship could end and thereby catch managers with their pants down, though this gradual rally has not at all supported such a break in relationship between equity price activity and corresponding volatility.

As the volatility index approaches this strategist's targets, one wonderful opportunity is worth mentioning, particularly since those benefits will be short-lived.

Simply, falling volatilities become another factor in improving premium prices (for purchasers), including the long-dated variety. Further, it becomes an easier market environment in which to transact; and such are the carefully planned-for times when one must act decisively with discipline, as per existent strategies and targets.

There is a relationship that managers do not follow daily as a matter of course, between the VIX, premiums, and the best timing for cross-trades. Best timing and prices are matters for the disciplined. Simply following a market or markets does not indicate the best timing, pricing or leverage for the underlying warrant.

PRECIOUS METALS

The activity in the precious metals is extremely bullish, particularly from a very long term perspective. The 2-year daily gold chart on page 2 reflects the bullish trend since $700, as well as the resistance at $1,000.

What is not apparent here is that the <u>very</u> (not shown) long term view illustrates a rising wedge, with the flat resistance line at $1,000. The big picture is indeed very bullish, especially for silver, and all-critical for hedge funds and inter-market premium players.

A breakout toward $2,000 and $3,000 should commence with a bang. In any event, at first, gold and silver will decline with the equity markets when they finally reverse, but who knows from what levels?

This is (again) a key time for planning, in attempting to secure tomorrow's wealth and its enhancement.

YEN, DOLLAR

There need not be any confusion derived from any Dollar rally that could continue here, if Dollar assets feel like rallying during this global countertrend period. Said rally will not have been anything worth shifting asset allocations over...and we will not have done so.

Having remained consistently in-tune with where we are in the Kondratieff Long Wave Cycle, I am pleased with what may be globally unsurpassed success in asset allocation in risk adjusted terms, since 2002. Currency allocation, whether paper or precious metal, has been rarely touched over the past 7½ years.

This is a balance sheet story, not one of the of the income statement. This is the all-critical K-Wave conclusion. So, all that matters is who has how much – not how much they can earn (i.e. – import/export, etc.); forget fundamentals as you were taught them.

CONCLUSION

The picture painted by this letter makes obvious where asset allocators and hedge players alike should have had their money as of the 4th quarter, while clearly indicating that one must reposition at this time, if one wishes to plant the seeds of maximal success for the period which follows this intervening countertrend rally phase.

That we may begin a B-wave in equity markets would be no accident, while the precious metals are lined up in that corresponding manner that creates additional and most special opportunities, indeed.

So, here it may be a well-placed segue to express that, to-date, as is all too often the case, those seeking to be more conservative have also enjoyed the greater leverage.

And considering what the leverage seekers did to the world as we knew it, this is justice, no? Anyway, this remains our sacred formula.

First, there was the customary 50% collapse (New York). Then, I further called its bottom and forecast the global rally (*a la 1931),* which is presently underway.

As history is being made, how many major and easily playable cycles are left?

Sid Klein