

Trend in Force, but a Global Pullback in Offing?



May 3, 2009

SUMMARY

The February 23 interim report was entitled, "**HAPPY DAYS - 1931 AWAITS: HEDGE MANAGERS: AWAKE!**" The reference of course was to the huge rally that followed the crash of 1929. Last month's title followed with, "[What to Do With Perfection?](#) Enjoy it: 1931 Comes Twice Per Century Only."

April 2, 2009:

"Again, whatever happens, the cross-relationships (hedge plays) have long since bottomed and, in this environment, such investments are all that I recommend. With the best risk adjusted profile, why take on any unnecessary risk, especially since there is ample leverage provided, *without* the otherwise assumed risk?!"

March 1, 2009:

"The only reason why investors have lost money instead of making a ton of it without stress and greed is that they have been unable to adopt a simple prescription:

"Precious metals, Yen, Swiss Franc (equals 4 currencies) – YES. Long term Treasuries (as of 2009) and Western equities – NO. Japan – YES. Shanghai in 2008 – NO. Shanghai in 2009 – YES.

“Straight long investments (except the 4 currencies) – NO. Hedge investments – YES!”

The prescription remains accurate and continues to be vindicated. Now, the game is all about guessing the news story that will have been discounted, by a market that is even ignoring the “P”- word: pandemic. (Please see NEW YORK, below.)

As I wrote in a recent issue, while the extreme in bearish sentiment had been seen in New York, as measured by the customary 50% collapse from the peak, the game would be on, in guessing what would be the good news to come.

Curiously, I ventured further that once sentiment again shifts, a few birds dying in Japan would be enough to set off the next decline. Such is the message of technical analysis, which is the measure of the investing public’s psychology. In any event, the “P”-word is being ignored, and that is further evidenced by the lows having been seen.

JAPAN





The weekly 10-year Nikkei chart at the bottom of page 2 illustrates an overhead resistance level but, perhaps more importantly, the coincident weekly (3-year) stochastic is overbought.

Meanwhile, the 2-year daily chart immediately above reflects an index that is coming into its 200-day moving average. This is a good stopping point, given too that its moving average is approaching an overbought condition, as one can see. This could result in a higher right shoulder in the Nikkei. We'll soon see.

Strategy

February 8, 2009:

["Japanese stocks will continue to outperform most anything, except perhaps China. In 2009, they are both relative superstars."](#) No change.

SHANGHAI

March 1, 2009:

["There is no question that SKGS has again identified the extremes and lows in the global inter-market relationships. 2008 was easy was for hedge fund and other managers who followed SKGS, and 2009 has shaped up in like fashion."](#)

February 8, 2009:

"Furthermore, the following chart reflects a nice uptrend and a healthy basing pattern that is well ahead of any global market. My 2008 dog of the year is my 2009 darling of the year. A pullback will create the final 2009 entry opportunity.

March 1, 2009:

"Will the last month of the quarter provide us what we seek?"

The following 2-year daily chart illustrates a market that has been in a steady uptrend since the early part of the 4th-quarter. Along with a supportive 200-day moving average, the technical picture reflects a different ongoing story in China, now that much ridiculous excess has been relieved in 2008.

The pursuant 10-year weekly chart on page 5, including its 3-year moving average shows us why this index has a lot of potential rocket fuel to sustain it. Of course, its negatively divergent and overbought stochastic would line this index up to be part of a global correction, in which New York, quite predictably, found itself to be the laggard. It is also kissing its 3-year moving average.





Conclusion:

This is the best market in the world, as witnessed by its steady uptrend and its having been the first to bottom. Having relieved itself of speculative excess, the superior fundamentals can hold sway, as they should.

Of course, all that will change when the 3rd phase of the depression begins. The third phase, as students of the Kondratieff wave know, is marked by war. The upshot is that an event will be orchestrated that will excuse the US government from paying the Chinese people their hard-earned savings.

Then, all Shanghai bets will be off, obviously. We're far from there, for now.

NEW YORK

February 8, 2008:

"...with a dragged out bottoming phase, where there is no real additional damage to the downside, but, rather, an accumulating frustration in the marketplace that coincides with fund managers' 1st-quarter-ending disappointments."

March 1, 2009:

"Yep, this is what's happening and the convoluted logic and proof that I present to you is that everyone is beating up on New York. That the hedge plays are all doing great is a lead indicator to the reversal after yet another 1st-quarter low (like last year), in this index that has fallen the magical 50%."

Yes, indeed, the sideways activity ended, while bearish sentiment was building. Doing so without any net negative progress set the market up for a reversal in psychology and newly discovered good feelings, when the market broke out this week. Of course, the dog was just playing some catch-up to the stronger markets in China and (even) Japan.

As the Dow broke out this week, the news *du jour* was a working-off of inventory in the last quarter, coupled with less bad economic results than what had been feared. So, what is the bullish news that the market will work to discount over these coming months?

The axiom is, "Never fight the Fed." To clarify, never fight the powers that be. These days, "the powers" want the people to spend, since it is zero-interest money that is being printed up, at the expense of the rest of the world. Bernanke (Mr. Fed) said as much.

When the powers that be want something, the TV shows come out in full support, since the mind-numbing medium of television is the shortest route to the mass's minds and hearts. Even Comedy Central has not been immune as a disseminator of this now holy message. Stewart, Colbert and, yes, even the Canadian born boys of South Park have all done their part, albeit not necessarily with much conscious awareness in doing so.

Conclusion:

March 1, 2009:

"A low this month, 10,400 thereafter (1931 parallel)...and, then, hell."

The Elliott Wave numbering on the 10-year weekly Dow chart, which follows on page 7, clearly illustrates the completion of wave-A of this bear market.

The 2-year daily chart that also follows on the next page clearly shows a dangerous triple divergence in the daily stochastic, while the Dow also approaches its 200-day moving average.

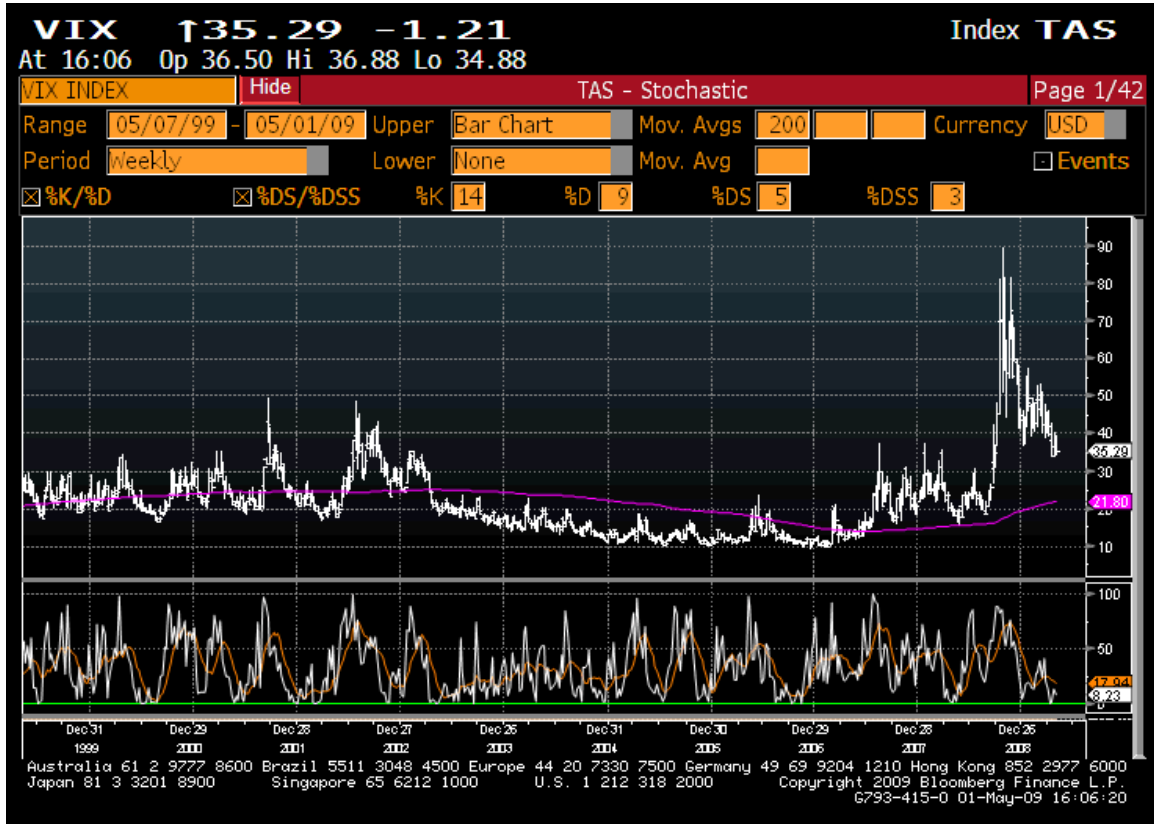
Evidence is mounting that a global sell-off may be in the offing. And, yes, it is indeed possible that such a decline would be wave-5 of A. So much the better, but I doubt it and, no matter what, the cross-relationships have seen their lows.



VIX

The VIX is coming into support, which further supports the notion that a decline may be imminent. As for trading this index, I follow the VIX principally as a market barometer.

The sole trade that we did was shorting it at the highs and covering after a 50% decline (100% profit); this will stand for now...though I suspect that we'll be back for more, later.



Both the 10-year weekly chart above as well as the 2-year daily chart below, suggest that the index is approaching support. Again, this would typically relate to a decline in the market.



PRECIOUS METALS

"The precious metals have been outperforming everything, since quite some time," as I wrote last month.

However, if gold were to drop, say, \$30 - \$40 during a global paper asset sell-off, then, under-invested accounts could use the opportunity to buy.

Food for thought: Especially when examining the moving averages of the 10-year weekly and 2-year daily charts that follow on the next page, one may contemplate the possibility of a wave-C being underway, with the recent re-visitation of \$1,000 marking wave-B.

What is the significance in practical terms? Particularly by holding over \$700, gold would then be set for a wave-3 eruption toward \$2,500+, after this next low.



March 1, 2009:

"We were 200% long (silver) and then cut that position in half after a 40% run-up. Now we're long forever, or until otherwise notified, whichever comes first."



Likewise, following the same logic as the gold argument above, silver would accord investors a pullback to a level above \$10.

My, my; what a sweet level that will be remembered as having been, during the desperate years ahead. Please heed this SKGS cautioning.

Please scroll down to page 12 for the 2-year daily silver chart.



YEN & DOLLAR INDEX

April 2, 2009:

"Apart from the Swiss Franc, the Yen is the only fiat currency that SKGS readers hold. I had referred to it as the best currency for capital gains, several months before it finally took off, and at levels that have since made the wait very worthwhile."

March 1, 2009:

"This very sharp short term Dollar/Yen rally is coming to an end."

Looking at the 2-year daily and 10-year weekly Dollar/Yen charts below, respectively, the March 1 commentary merits repetition, as the Yen rally again appears ready to resume.



See page 15 for Dollar Index comment.



The 10-year weekly chart at the top of page 14 reflects a serious negative divergence, while the daily chart that follows it illustrates a clear A-B-C countertrend pattern.

NB: Given present market conditions, I will bolster coverage with additional interim reports, each week in May, and leading up to the next report.

This time, the movements won't be sideways. The media will again have things to report on, both new and old. But that's nothing new, right?

Sid Klein

LEGAL NOTICE: This market letter is the work product and intellectual property of Mr. Sidney Klein. It arises out of his training and profession as an international expert on financial equities. It is a private correspondence from Mr. Klein to his subscribers. Any person who copies or otherwise disseminates this letter becomes subject to international criminal and/or civil prosecution under the Universal Copyright Convention and the Berne Convention for the Protection of Literary and Artistic Works. Nearly all countries in the world have signed both of these Conventions and have pledged to enforce them through their own legal systems. In addition, Interpol may be called upon to assist in the international enforcement of these Conventions through its processes of arrest and extradition. If you are the *recipient* of a copy of this market letter, whether through the internet or by facsimile, you should immediately report to Mr. Klein the name of the person or entity who sent it to you. Send your email to sidklein@sidklein.com.

DISCLAIMER: This market letter is intended to assist in the dissemination of information to private subscribers. The information contained herein represents Mr. Klein's best efforts in good faith to advance knowledge to his clientele, but there can be no implied guarantee as to its accuracy or completeness. The information is given as of the date appearing on this market letter, and Mr. Klein assumes no obligation to update the information or advise on further developments relating to the information provided herein. No solicitation to buy or sell securities is intended, and none should be inferred. Investments are inherently risky, but investment risk itself is a function of individual preferences. Thus any opinions, recommendations, or judgments expressed in this market letter are of necessity abstract and general. They must be modified, accepted, or rejected by individual subscriber/investors whose risk averseness cannot be known to Mr. Klein.