

IT'S ROLL-OVER-UGLY!



September 7, 2008

JAPAN

Monthly and interim reports this year have expressed that this market has but a final minor move down to complete its multi-year correction. I am referring to all Japanese indices, though non-big-cap indices should lead behind the Yen's blocking.

As regards the Nikkei charts below, the next monthly letter will label the move so as to make it clear. Simultaneously, I will label the Dow, so as to make clear the coming decoupling of these markets, which have been enjoying the same directionality...to the naked eye.

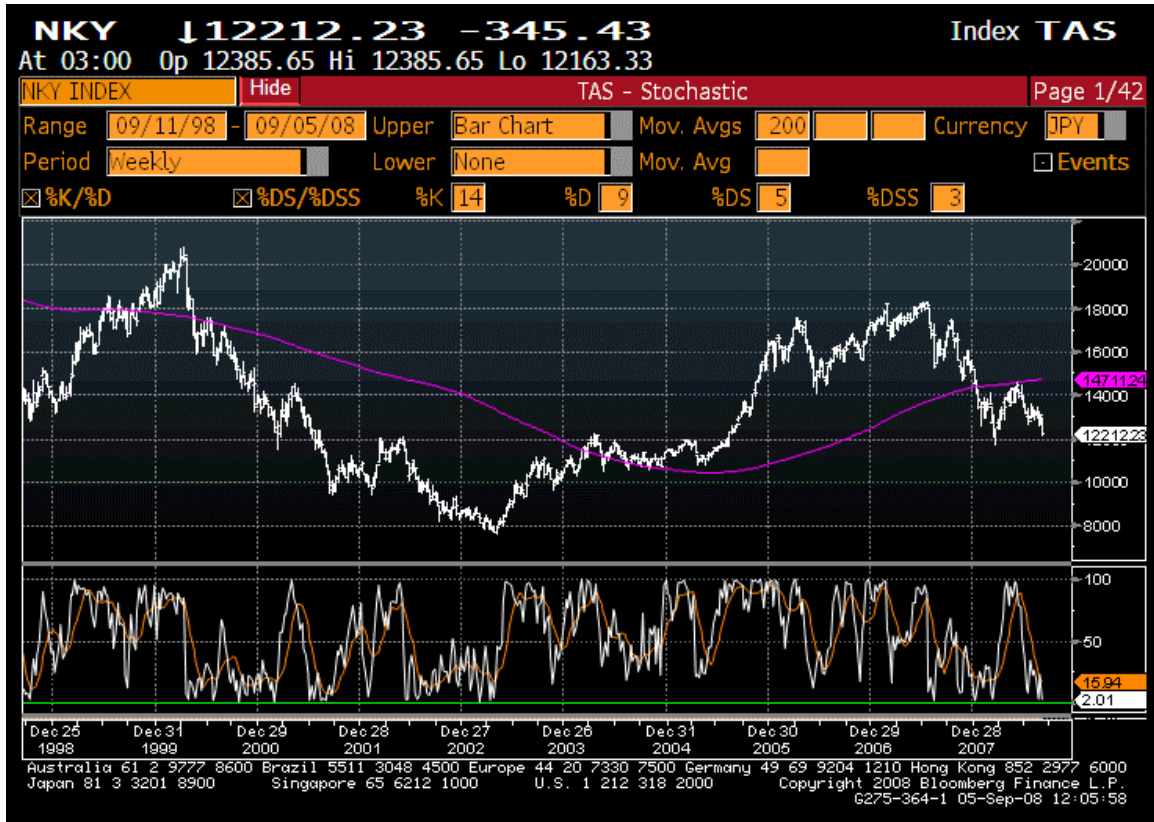
This will be yet another year where calendar yearend will have marked the ideal buying opportunity in Japan. This common (annual?) occurrence is brought on largely by selling by Westerners, headed by the Americans and English.

This is why and how I was able to identify the extremes at yearend last year, particularly with respect to the Japan/China trade (please see http://www.sidklein.com/past_reports.html). Stocks and indices tend to pause on the way up or make the low at yearend, or slightly into the New Year.

ALL DAILY CHARTS IN THIS REPORT ARE 2 YEARS.



ALL WEEKLY CHARTS IN THIS REPORT ARE 10 YEARS.



As things are unfolding right now, the daily stochastic (charts on page 2) will have created a triple-divergence, which, I believe, is the most powerfully bullish signal. The weekly stochastic will have diverged, as well.

Strategy:

Japanese indices, and baskets of stocks that may serve as indices, will have bottomed by yearend, but their roles as out-performers versus other world markets, both within and without Asia, will have been key to hedge funds sooner, rather than later. Read on.

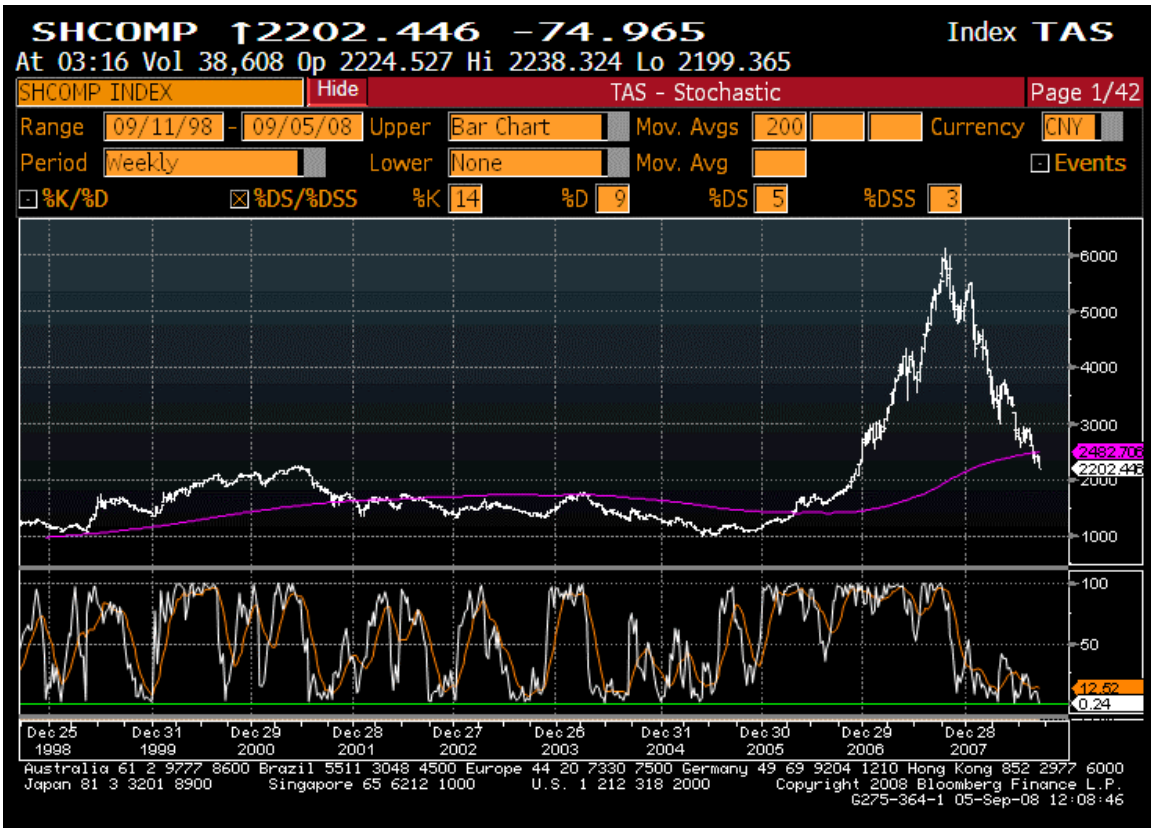
SHANGHAI

Clearly and quite predictably, China was the short trade of the year. The key was finding a relatively cheap way of doing it.

Among my arguments was the fact that the Shanghai index below doubled since Greenspan turned bearish, which I had likened to Templeton turning bearish on Japan at 26,000 (en route to 39,000).

Anyway, the bears are so dead that they may not even reincarnate. But I believe they will. This implies a monster rally into 2009, and starting not far from here, in terms of points.

The 2-year daily and 10-year weekly charts appear on page 4.



NEW YORK

From the July market report:

“Whether we get a summer break in the market burnout or not, including a last-gasp-of-breath rally or not, the Dow is heading to under 9,000....and fast.”

The false level of the Dow is brought on by the printed-paper that was created and continues to be created by its government. As a most knowledgeable reader said to me (close paraphrase), **“As long as the world is dumb enough to give us their goods for paper, we’ll keep right on doing it. Why shouldn’t we? We’ve got the world’s most powerful army to maintain our position as the world’s reserve currency.”**

As a Canadian and member of a true democracy, I would have been offended but for the fact that my friend and reader was merely making an academic and intellectual observation. Anyway, the point is that the Dow has out-performed because, (a) the paper flows into equity indices, among other things, and, (b) the Dow is supported by foreign currency-denominated earnings. “The Army” has created a win-win.





Still, is the Boeing strike a sign of the times? Wage demands occur at economic cycle peaks, and therefore right when least affordable. Go tell a union that they should have thought this through somewhat earlier.

Anyway, the headwinds of ugliness will drive the Dow much lower quickly when it occurs, as indicated above, whether the Dow is the single best way to short the US, or not. Regardless the best strategic approaches for profiting from collapse, or the best indices to comprise them, the ugliness of the Dow's pattern reflects its incapacity to get out of bed.

After 2008's multiple efforts to resurrect the US' leading and strongest index, it is rolling over and ugly. The bulls will abandon the market for years to come before this is all over, with a simple sentiment, "Roll over, ugly; *I can't look at you no mo.*"

VIX

The daily VIX chart follows on page 7. It is followed by the weekly graph on page 8. As forecast, the daily chart's up-trend channel did indeed hold.

Meanwhile, the weekly VIX chart held above the neckline support, as well as ever-arcane 200-week moving average.

Again from the July report:

“The VIX, as is evident on both charts on the next page have fallen into major neckline support levels, while the second chart, the 10-year VIX, also came into very long term moving average support.

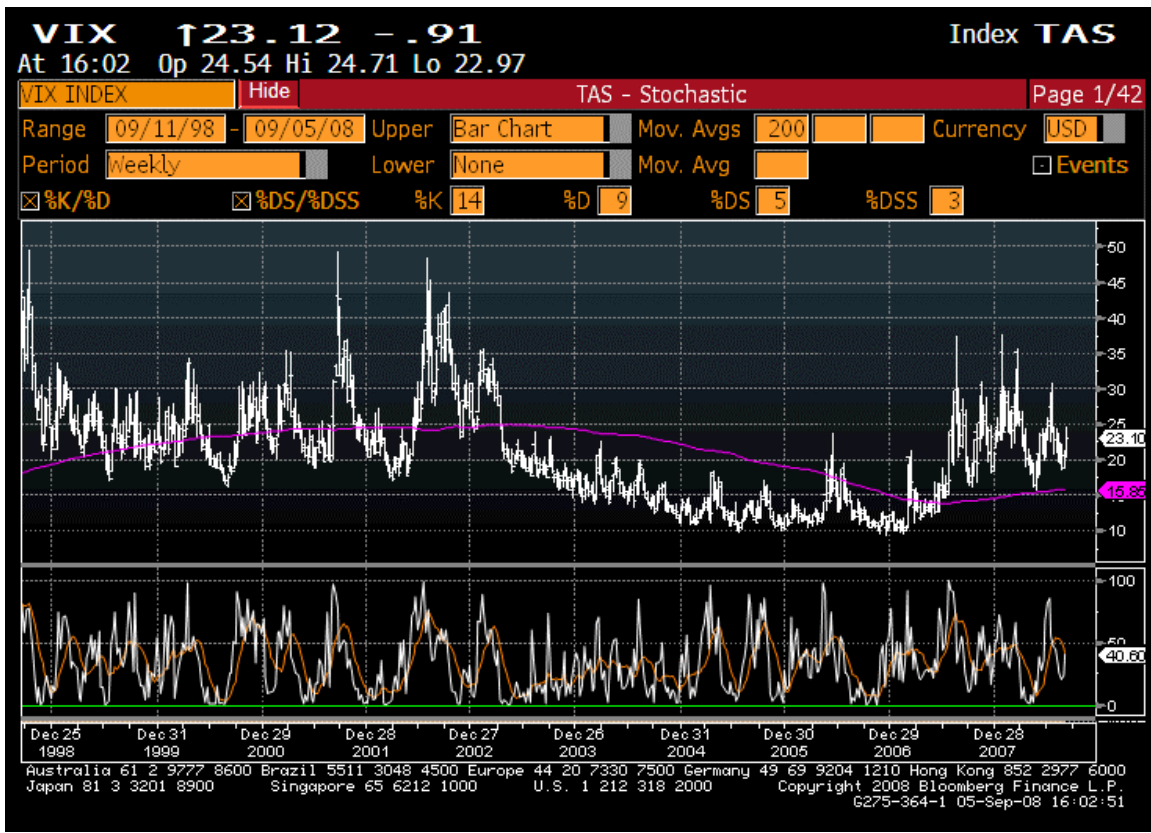
“The first chart on the next page is the 2-year daily. The upshot of both charts together is that an intermediate-term correction has completed in the VIX with a lot of upside before this is over.

“Whether it stutters first or not, the key point is that there is a lot of room to rise...and that the equity market runs in the opposite direction of this indicator.”

Strategy:

Buy points in this indicator should be used to fine-tune the purchase of time premium, for the selected derivative strategies, based further on the investor’s global criteria, with respect to the underlying index of choice.





OIL

200-Week moving average and Elliott support lie closer to \$80; these correlate well to the comments on gold that follow on page 10.

While the daily chart on page 9 suggests a bounce is possible, and perhaps even likely, as the up-trend channel has not been breached (just about at the trend-line), the pursuant weekly graph (also page 9) shows why \$70 - \$80 is more likely support.

The indicators (daily and weekly stochastic) are oversold (though without positive divergences), so logic dictates waiting for a rally before shorting.

The assumption made in these pages is that there is no exigency to maintain a position or point of view of any kind, so, short, but only if there a juicy rally. Trends are down, but I have no desire to get in the way of a possible bear trap in waiting.



GOLD

If gold rallies 5% or so, it'll be a tradable opportunity for those who would like to exit ahead of a third corrective leg down (corrections are 3-legged).

Just under \$1,000, I felt that there would be a final rally that would precede an intermediate term smash that could take gold down to \$700. I missed acknowledging – as I always had in the past – that one's attention should primarily be on the greater risk and that one should be positioned accordingly.

The movements of April and May were identified well, but I feel a need to nail any rally from here, precisely so as to benefit from any smash to the final bottom in the \$650 - \$700 area.

I have also cautioned in earlier letters this year that the cross-charts, which express key indices and currencies in gold, would be most indicative in identifying the next major low in the metal. I expressed this months ago, when I observed that there was too much that was overpriced, when expressed in gold.

The good news in all this is that wonderful long-term opportunities are going to open up early in the coming quarter, both in gold, as well in the cross opportunities. This will figure into the tailor-made warrants that are intrinsically long/short positions.

Like oil, the daily chart on page 11 illustrates that the up-trend has not been broken, while the weekly graph on the same page reflects the reasons for the deep concern I expressed early in the second quarter about the potential depth of any correction and/or how dragged out in time it could be.

Strategy:

Those who are long-term holders of gold, such that 50% of all liquid wealth was held in that currency since it crossed \$500, have since reduced their position to 50% (25% of liquid holdings).

Positions of such size should not be swayed by intermediate moves for strategic purposes, to the point of holding less than 50%. However, those whose positions in gold are not as "staunch", so to speak, may reduce their holdings to zero (0) from 50%, on a 5% rally from here.



DOLLAR

The daily Japanese Yen chart on this page shows us 2 things. Firstly, the currency reversed from a level that was 3 Yen beyond what I had initially forecast.

Secondly, it shows us that the bloodletting in Japanese Yen denominated securities should be over, as far as the effect of the currency is concerned.

Thirdly, the reversal came from neckline resistance. Fourth, it came after the Yen retraced 50% of the preceding decline from 124 to 95. Fifth, and finally, the past week's jump of about 5 Yen does not reflect in the weekly chart on page 13.

The weekly chart shows the correct price level at the top, but, being a weekly chart, there is no downward movement that can be seen. That will only be evident next week but, more importantly, the 10-year weekly graph on the next page has also formed a right shoulder and has rallied into neckline resistance.

For good measure, it has come into the 200-week moving average.





The 2-year daily US Dollar Index chart on page 14 reflects the strong short covering-inspired countertrend move in the Dollar.

However, the 10-year weekly chart on page 15 shows the bounce to be anything but strong, but rather lame, in fact.

There, we see a miserable drubbing from 120 to 70, since the bear market began at the beginning of 2002. That chart on page 15 exposes this pop to 80 as merely being consistent with prior rallies this decade.



The following chart, it may be further noted, not only came into resistance, but also was repelled by the 200-week moving average.

If anyone wished to argue that the Dollar's trend broke over resistance, please note that that only has some minor truth to it because the drubbing has been that steep!

Simply, the fundamentals are in place, backed by a political will to print money, to resolve anything from mortgage debt to credit card debt, off the backs of the peoples of the world.



On page 16, I have published the 2-year daily chart of the South Korean Won. On page 17, the 10-year weekly Won chart appears.

I do so this month for 2 special reasons. Firstly, the Korean market may figure nicely into some ideas for Asian long/short trades later on, as may China again. But Korea is a special situation in its own right, and the currency is a good place to begin the study.

This month, we start the project slowly by focusing on the currency. I may say now that there is a definite observation to be made regarding the relationships between the Asian currencies and the trends of their respective stock markets. This is very much so with the Won.

In any event, compelling research has indicated that the Korean market and currency are desperately dependent on the Fannie and Freddie bailouts that are unfolding, due to Korea's insanely overweight positions in their securities; I wish to do more of my own work on this.

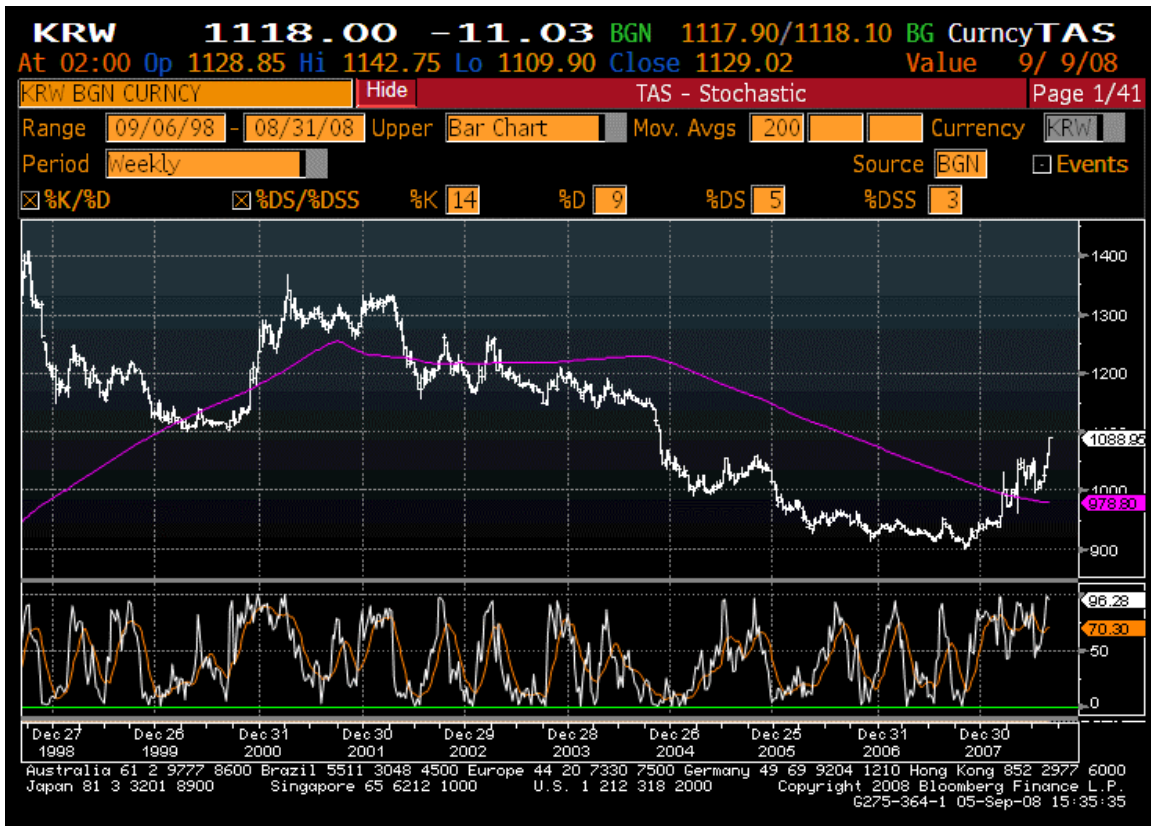
This much I can say for now: Firstly, the daily AND weekly moving averages converge just over 1000, leaving room for a down and dirty trade right now, by going long the Won.

Secondly, of the 6 key equity indices that I've begun to follow more closely, this coming rally in the currency may provide the bounce in my desired index for going short.

Without getting into it this month, we may be approaching a special Japan/Korea trade. It has been on my mind as a play for a while, and the circumstances now seem to be unfolding.



Please scroll down to page 17 for the 10-year weekly chart of the Won.



Sid Klein

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