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The Obvious, The Unobvious, The Ugly

September 7, 2009

SUMMARY

Hedge fund managers were cautioned in SKGS of the aging process of this year of countertrend and that, one by one, 2010's premier opportunities would fall by the wayside during this year's 2nd-half, as was the case last year.

And this is what has been well underway this summer, in multiple asset classes. Asia has offered the most glaring chances.

So, in the equity markets, turns in globally strategic outperformance investments are obvious. This is equally true in the precious metals and other markets and asset classes around the globe. Certainly, then, this holds true of inter-asset class plays.

Due to the comments below on the precious metals, regarding the metals and the sundry inter-asset class plays related to them, patience will now be required.

Whether such patience pays off or not will be seen. Above all, asset allocators and hedge fund managers have always been best advised to be ready for the opportunities when they would present themselves. But momentum players therefore often lack the vision and courage required to be Johnny-on-the-spot.

In this issue, only our look at the Shanghai gives any indication as to the above, since it is a market of common focus for SKGS, particularly since SKGS' performance at its peak, as well as at its ensuing low (2007 and 2008, respectively) profoundly resembles my 1990s' achievements with respect to the Nikkei. I had wondered whether the Shanghai would be my "new Nikkei" and, for the time being, it appears that the answer is yes.

However, the Shanghai aside, multiple Asian and other world markets have peaked or are imminently doing so. The outperformance plays (cross-charts) are somewhat more obvious, since "imminent" is as good as a done deal. Remember, cross-charts tend to bottom about 3 months early since they reflect which markets are leaders on the way up or down, as the case may be.

What is less obvious is the timing of the sell points of the still advancing markets and, worst of all, how to treat markets where ideal entry points have clearly been missed. Waiting could mean missing the boat altogether, while not doing so could mean straying from proven and more comfortable methodology.

The various lows in cross-charts suggest imminent peaks around the world. Cross-charts are no longer covered in these pages, ever since I had decided to stop doing investment bankers' work for them.

JAPAN

In the days leading up to the very recent Japanese election, I was again interviewed by Nikkei Quick News [see "Sid in the Press" folder (in Japanese only)].

My sundry comments concluded with utter profundity: "It doesn't matter."

More seriously, I again explained that we are at that point in the Kondratieff cycle where financial collapse is followed by the yet-to-commence-IN-ERNEST economic debacle.

This will occur in 2010, and the third event in this phase of the K-Wave sequence will follow some time afterward. Regrettably, that event, as SKGS readers know is global war, amid famine and the dry planetary climate that will have helped usher it in.

After bombarding the young journalist with these comments, I further explained that one could NOT look to the "new era of innovation"* to bail out the world (she had enquired about the advent of the electric car and other technologies coming our way).

* The New Era of Innovation actually commences at the end of the 50 - 70-year K-Wave sequence, and about which she had questioned me.

I explained that the phase known as the "new era of innovation" in fact is a CAUSE of further financial collapse, since it represents a competition for capital, precisely at a time when the financial world must heal its excesses.

Of course, this is ironic and counter-intuitive, but it happened before...and will again...and again. (Consider that the television was invented by Zenith in 1929, as an example; I have forgotten whether it was in fact the colour television.)

In any event, you read of the Nikkei`s low here in SKGS at 7000, as I also believed that the sequence of market turns would be (and remain) China, Japan and the US, respectively. As well, at 7000 I forecast 11,000 for the Nikkei and, as you can see below, this target has all but been achieved, as well.

10-year monthly and 2-year daily Nikkei charts follow on the next page.

Allow me to first remind here that the Nikkei is the SKGS Japanese equity market benchmark, while underscoring the point that the large-caps are not at all the way to invest in Japan. There are sundry fundamental, technical and politically-driven reasons for this.

Please scroll down to page 4.


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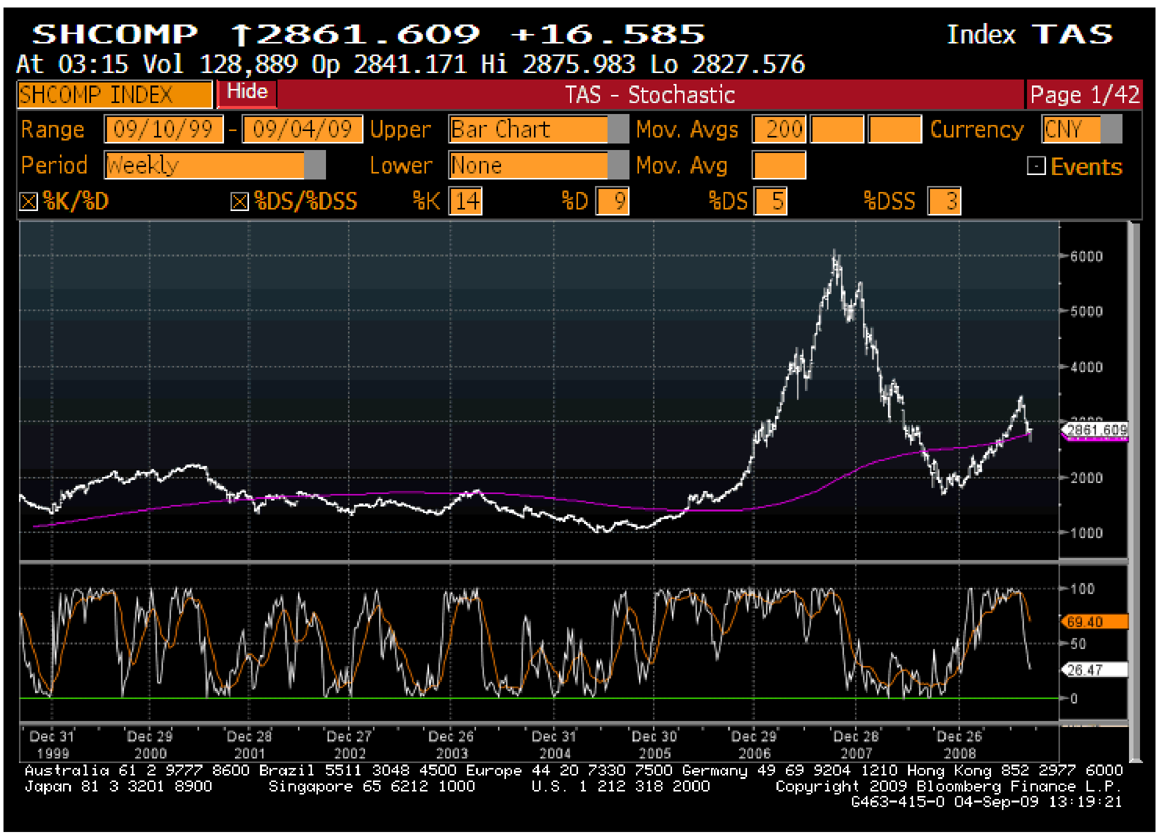
SHANGHAI** (see end of this letter)
This market has been leading on the way down as well as up. However, for those lamenting having been unprepared to take advantage of the easiest of equity outperformance (long/short) plays out there, this very recently smashed market might well recover these most recent losses all the way (while it may be a wild consideration.

At the lows, I wrote that "anything under 2000" was a buy and that one could look for the 3000 - 4000 area as a target on the way up.

10-year monthly and 2-year daily charts follow. Since pictures can stand in for hundreds of words, I'll allow these charts to express the vindication of prior forecasts, as the Shanghai predictably doubled from bottom-to-top.



NEW YORK

As forecast, wave-c of C is underway, which means, "be alert!"

This is not the sole truth, however. The recent August 26 interim report used long and intermediate charts of Consumer Confidence and GDP to show that the markets could hold up to yearend, on the strength of an improving economy through the 1st-quarter of next year.

Previous letters (at the very bottom and at beginning of this year) have warned of the temporary effects one could expect of the US' money printing scheme, which effectively has the world paying its debts, supported by the benefit the US enjoys of the Dollar being the international currency, while also having the world's largest military forces to back it up.

The question is whether the lead time of the stock market to the economic peak will be virtually nil, as has largely been the case this decade, or will there be a lead time, after all? There was such a lead time at the lows early this year, but perhaps this time the market will again lead the economy's peak (like the good old days), for two reasons:

Firstly, we have had the initial shock of the FINANCIAL collapse. Secondly, the market is very over-valued. Therefore, ANY (and I am not going through all of them here, please realize) financial events that trigger nervosa could do it.

You know, like someone yodeling amid mountains pregnant with the desire to shut him up.

Again, monthly 10-year and daily 2-year Dow charts follow; they tell my story above rather well.

Please scroll down to page 8.

VIX

The weekly 10-year chart immediately below (page 9) clearly shows a beautiful retracement to neckline support. The daily 2-year VIX chart reflects the predictable and to-be-expected overshoot down.

Along with the weekly moving average (10-year chart) again supporting he VIX I have always commented on how the VIX stops where the weekly stochastic supports it), it is profoundly unlikely that the long triangular downtrend (see monthly chart) will be defied.

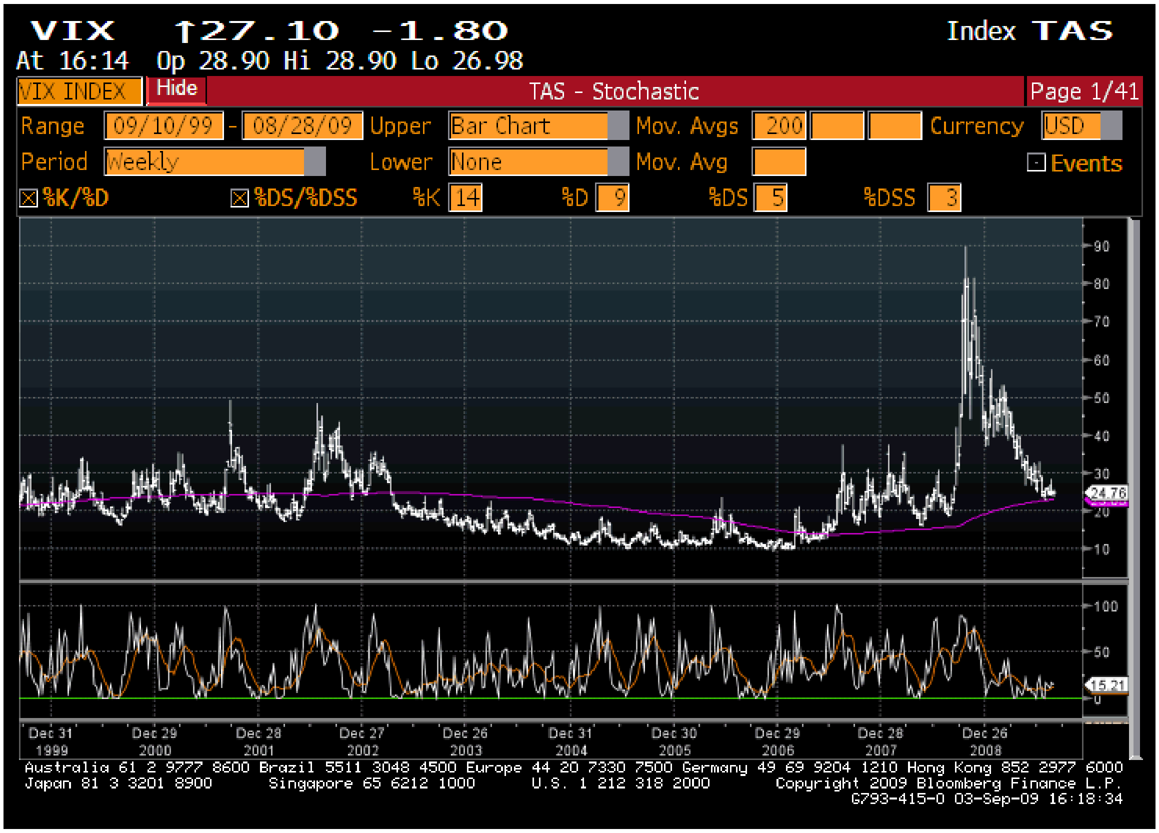
This supports SKGS's initial notion that the market would stop in this time frame. At the same time, I cautioned that only through outperformance plays would one be able to neutralize such shorter term uncertainties.

A triangle is busted out of with a vengeance and this countertrend indicator therefore suggests a US market on the ropes.

Last year I warned that since cross-charts bottom about three months ahead of the individual markets, and since market extremes were three months away from their extremes at most, it was foolhardy to delay investment plans. It was great error to ignore that analysis. So it was and remains ignorant to focus on whether there will be any lag between the market extremes and the economic ones. The VIX is just another nail in the coffin.

So, will there be any lead time, this go around? Anyone dumb enough to bet on that?

No one who pays to read me, I'm sure.



Please scroll down to page 10.

PRECIOUS METALS

Monthly 10-year and daily 2-year charts of (1) gold, (2) the Philly Gold and Silver Index (XAU) and (3) silver follow, respectively. They illustrate the following:

Gold has been the most powerful, due mostly to global, including sovereign accumulation, which has skewed the obvious. Namely, that silver's spike from $20 to under $9.00 represented the true Elliot Wave (technical) interpretation of the correction of this decade's advance, which is similarly illustrated by the XAU.

Note how the XAU has emulated silver, which therefore made the XAU's fantastic rally this year very obvious. Simply, the XAU has emulated silver, rather than gold.

SKGS took a 200% position on silver at the lows. It is not only silver that has erupted (the position was reduced to 100% long, after a strong run-up). The XAU has quickly regained almost all of its corrective losses. Hedge fund players and asset allocators not on the ball have truly missed glaring opportunities.

Understanding the correct wave count has continually meant <u>everything</u>. Just as knowing where we are in the K-Wave sequence has meant everything. Having both right has provided SKGS' unparalleled results.

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XAU INDEX
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CURRENCY

The 10 and 2-year charts of the Yen and USD immediately below reflect a simple fact: The Yen has been the best of the major quality fiat currencies, as the Dollar maintains its secular downtrend. The latter's losses since the Yen`s low around 123 do not perfectly reflect the Yen's gains, as the latter's gains have even out-paced the Dollar's losses.

Please scroll down to page 15.


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ASSET ALLOCATION

Same old same old, regarding liquid assets (and why wouldn't everything be liquid, hmmm?):

50% gold: (Forget 40% gold + 10% silver as an alternative; more on that in the future.**)

25% Yen, the paper I hailed at its low as the best fiat currency in the world for capital gains.

25% Swiss Franc.

** - I have often warned that the powerhouse to trust is India, not China. Simply, the latter has millennia of capitalist history, while being non-violent and superior on the level of humaneness. The key, I always cautioned, is a society with democracy and legal system that provides the infrastructure for settling contracts.

A prosperous week to all,

Sid Klein