Sid Klein Global Strategy
1001 BOUL. DE MAISONNEUVE O., BUREAU 950, MONTREAL, CANADA H3A 3C8
TEL: (514) 939-2221 FAX: (309) 417-0942
e-mail: sidklein@sidklein.com
www.sidklein.com

PEAK MARKET ARROGANCE: OUTDOING THE BULLS

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SUMMARY

This month, SKGS has already been published twice, including the interim report of the 16th; what a difference a week makes, hence a further update. From last week's SKGS conclusion:

"The fun has begun. Believe it….before sweating that 2010 will bring with it old nightmares. Stay the course."

The preceding warning is most "curious", given a note I received from a reader over the past week. He was cautioning me that playing the short side could prove difficult, given that the Fed may have different designs.

That's what investors of all stripes were saying during the last few thousand Dow points, before the cold sweats of global nightmares took hold in 2008.

As I have written so often, the greatest enemy an investor has is himself. Fund managers are loathe to be "too" contrarian, for fear of appearing or feeling out in the cold. Amazingly, acting well in advance to obtain the best leverage and safety is rarely the focus.

The fear of being even a little early overrides what should in fact be the key and major concern, namely, **being even a little late!**

Still, I do try my best to help avoid that, and this past week illustrates why.

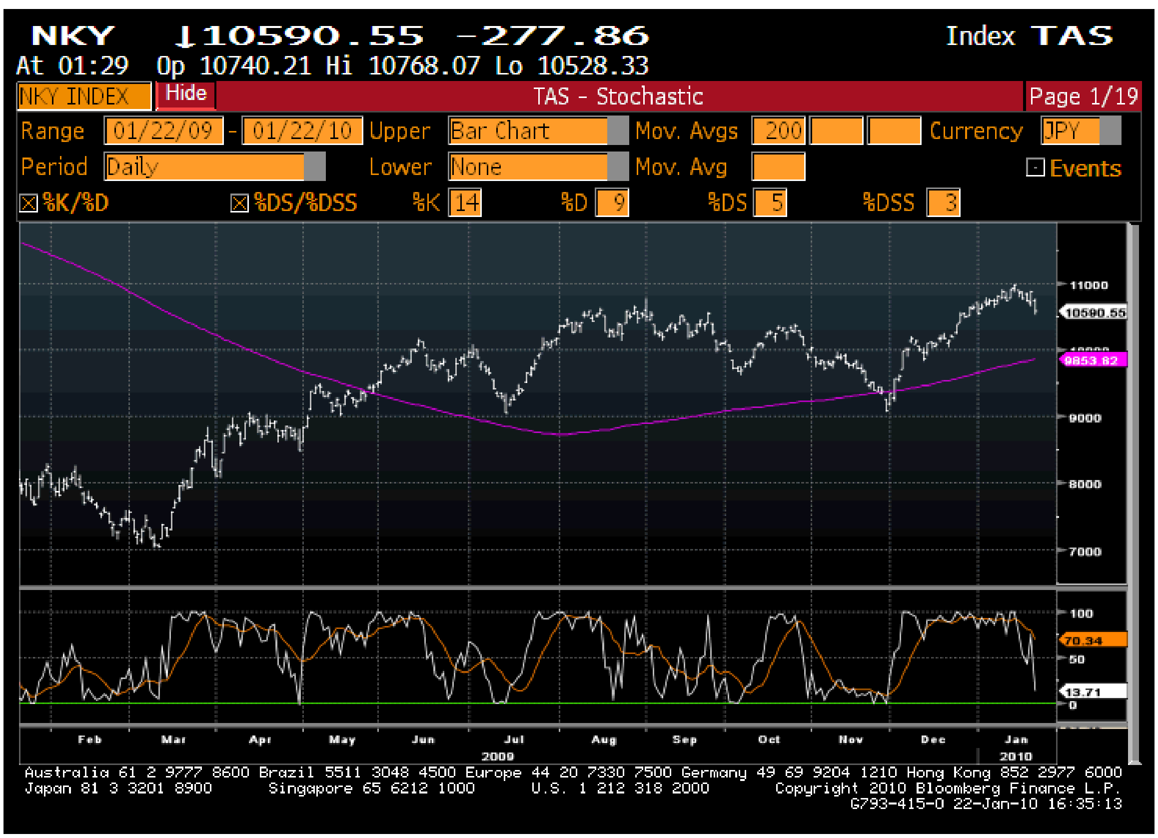
The **VIX** chart (p. 7, 8) suggests a spike in global time premiums (implied volatilities), off of levels that could go no lower. The "patient" missed the best sailing boat. You see, among other things, the VIX low, as discussed in the past, also coincides with the lows in a variety of long/short plays in the credit space.

All charts in this report are daily 1-year graphs.

JAPAN

The Nikkei's rally has satisfied any Elliott Wave (EW) interpretation for a completed countertrend rally. It has also **perfectly** satisfied the **11,000** target for this countertrend rally, which I published one year ago, at the perfect low at 7000.

Right on the nose, actually. Secular bear markets made easy, eh?



The safest play is, as already reported, the Topix Small index, and not the Nikkei (above) which will follow global indices lower, at least until it gets back to 7000.

As last week's interim report illustrated, the Nikkei was turning down from a level that was near its 200-day moving average (MA), when the index is viewed in USD, as opposed to Yen, as the index is ordinarily quoted.

The chart of the Topix Small follows immediately below.

Please see this month's reports for a look at the countercyclical nature of this deeply oversold index (including longer term charts/indicators), including its rather impervious nature to external (foreign) selling pressures.

It is not only large funds that may avail themselves of investments which benefit from long/short strategies, including currency diversification; listed markets offer sundry products which can be combined to provide the sought after strategies.

As I've often pointed out, those who achieve the greatest leverage are often those who seek the greatest safety. And during this cataclysmic secular bear market, this is as it should be!

In the context of the latter sentence, please review the last 5 paragraphs of the page linked here (the site is due for its annual update shortly): http://www.sidklein.com/Japanese_equity_markets_expert.html

CHINA

If any Asian market would make a final stab at the highs, it would be the Shanghai index, which chart follows immediately below.

The index could bounce off of its 200-day MA and challenge a 6-month old triangle's downtrend line, which would absolutely complete all that my EW interpretation could demand of this "wave-5 of c" (EW count not shown).

There are two strategic conclusions to draw from the comments and charts above:

This market must be shorted, but that the correct way of doing so, as reported last week, is via the Kospi, as the Shanghai's premiums are comparatively huge, particularly due to the Kospi's extensive and belaboured topping process.

China, however, also carries risk (time) premiums that are the result of the "trauma" caused by the shocking collapse last year, which I had targeted to near perfection. Similarly, its ensuing low and this high were almost as perfectly forecast and identified in these pages.

KOSPI

Both the Kospi and Kospi 200 (chart below) have satisfied any Elliott requirement, though that never means that a minor move is impossible. In fact, one is free to pray for it, if one is a fund manager who understands the need to be a "little early", to not pay spiked time premiums.

Investors do not grasp that **indices** (or stocks, etc.), cannot be timed in the way that **time premiums** or **options** need to be. And there is no way of explaining something that requires an abstract-minded talent, to correlate different securities, particularly when one of the securities has a forward-looking aspect which is tied to discounting what the underlying security is going to do.

Recently, there was a substantial jump in call option premiums on as Asian index, whereby the premium was 50% higher than where it had been about 10 days earlier, when the underlying index had actually been higher than the level at which the option premium had assumed the price which was now 50% higher. Specialized investments require specialized knowledge.

If the opportunity presents itself, after having planned and prepared for it, pounce! If there no longer are any second chances, well, make the best of it, somehow, according to the prevailing circumstances.

NEW YORK

As the following chart is not from Bloomberg this week, but, rather, BigCharts, the 200-day MA does not appear. Last week, I drew readers' attention to the fact that the MA was being kissed…and that it would be the kiss of death.

I have viewed this top as one of the easiest peaks ever to identify, and that is saying something, as many tops have practically jumped out and bitten the noses of those investors not shivering in fear, and therefore too close to the chart to see the plain and obvious.

I have recently discussed with readers that the Dow could see 9500 very quickly, hence the publishing of this interim report. While the oft-discussed steep uptrend meant a sharp decline could commence at any time, a secondary uptrend channel (channels not shown this month) points to support around 9600.

I have written that there are other indices which were underscoring just how truly precarious this market peak is, and how it was every bit as obvious.

To illustrate, this time, the next page provides a 5-year look at the NASDAQ. I will not even bother with an analysis. If all the bearish arguments aren't self-evident, one shouldn't be reading these reports anymore in the first place.

Okay, alright……(1) right shoulder, (2) neckline, (3) maximum allowable retracement levels.

When it is easy, don't argue. 5-year returns are easily achieved by taking the candy from the baby when the hand is extended.

Heavens! The long/short plays have never been more numerous or easier…and one was given a year to prepare for it, ever since I identified the global bottom. So, why do grown men fear babies?

Yeah, I'm having a good time now.

Anyway, does one need a $10 calculator to appreciate the endless possibilities, whether or not for the more risk-averse hedge players? Separately, however, one has to know which indices to best match, and the strategies best suited to benefit from this secular bear, even after having brought the right indices together.

That's extra.

VIX

Again, from last Saturday's report:

"Strategy

"Revert to a 100% long position at Monday's open, with a close-only stop below 15.75."

Monday's open was **16.93** and the VIX has already approached **30!**

After the massive gains on the short side from 85 to 40, and the more recent 3 – 4 point loss on the long side, we are again quickly on the side of major gains in this index, which SKGS used to and still usually follows only as an indicator, rather than as a tradable security.

You see, playing a bear market is easy, if one's psychology is not intimidated into not being a bit early sometimes.

Note paragraph 3 on page-2. (The December spike down is an error on BigCharts.)

PRECIOUS METALS (gold, XAU, gold/silver, Golden Star)

The January 10, 2010 letter, referring to SKGS's previously-stated target of $1,080 **("Short term, based on the above, support is now around $1,080")**, noted that, before rallying off of the December low, **"Gold pulled back to $1,079.50, intra-day."**

As evidenced by the gold chart on page 8, gold has again corrected to the $1,080 level, by testing **$1,081.95,** intra-day. In doing so, gold may have completed an "a-b-c flat" correction, in EW terms.

The XAU chart (p. 9) shows that its own correction may be complete, which would suggest that any further gold decline could be discounted, or that it may already be all over.
It is fascinating how many "contrarians" have come out of the woodwork to call intermediate or long term peaks in gold. They range from those who cannot accept having missed this decade's move(s)……to has-beens.

There is a basic fundamental question: How arrogant does one have to be to assume that the Americans have any say in what happens to the metal's price?

The international fiat currency has been and is being printed out of sight, so there is no question of a purely deflationary price decline in asset prices. Yes, this bit of price control (gold) is in the hands of those to whom "power and wealth have been shifting for years" (as I have often reported)….the East. Specifically, where gold is concerned, the Chinese. Deal with it we must.

Anyway, the position of gold's MA suggests the possibility of net sideways activity for some weeks, as a greater likelihood than further price decline, when also considering such factors as the prices of the related equities.

As far as the above-mentioned equities are concerned, the XAU chart immediately below has come into support at 160, and the 200-day MA, while the price pattern would be completing an a-b-c correction.

This, anyway, is the interpretation contemplated last week, as we looked at investment in the GDX. (Please see last week's study of the relationships between, gold, the XAU and the GDX.)

GOLD/SILVER ratio chart appears on page 11.

As part of a special analysis for an institutional reader, the above chart was published, citing this month's low as the completion of an "A-B-C, Wave-2" correction, which would precede a Wave-3 advance this year, to markedly higher levels.

I have referred to this trade, and options on same, as a sophisticated means by which to add to one's gold holdings, as long term charts and studies of this relationship suggest much higher levels over the years immediately ahead.

Curiously, the spike up this past week, which we see immediately above, occurred while the metals were declining.

Long/short trades offer so many strategic possibilities, including just as many improved risk/reward scenarios.

Page 12 illustrates a chart of Golden Star, a previously discussed stock which has under-performed gold in more recent years. Still, it has been a good trader and, recently, I have advised interested parties to await the $2.50 USD area before getting back in.

After its yearend blow-off, the latter level would satisfy a few technical targets and, certainly, $2.25 would also make sense. No matter what, any investor should be a long-term player and, with that view, the reward could be explosive. That has not ever changed,

PUBLICATION NOTE: As I have often done in the past, during significant turning points, SKGS is published more frequently.

Therefore, as a result of interim reports such as this one, the regularly scheduled letter could be delayed or suspended, in lieu of more regular coverage. There would be a notification of same, if additional interim reports are indeed foreseen.

Sid Klein