

JAPAN ASIA INVESTMENTS

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SPECIAL REPORT

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Dear Investors,

These past 3 years have proven to be the most difficult and disheartening for investors since the 1972-74 bear market. **As the “conclusion” section below illustrates, this needn’t be the case.** Investors have lost faith that anything can make money, while regulators and compliance departments exist these days mostly to impede business, as the avoidance of lawsuits seems to them to be as good as actually making money. Such is the ever-predictable attitude of those bankers who were equally rapacious when times were good.

Were they actually “good”, though?

GREED:

To illustrate popular culture’s present view of the investment banking community (once known as “brokerage firms”, remember?), Saturday Night Live performed a most damning skit of the financial community that reflects the public’s widespread distrust that has been engendered. The performance is being emailed throughout the continent.

It’s easy to blame others, though.

Several Sid Klein’s Daily Fax (SKDF) reports in 1999 warned that the secular bull market in New York was coming to an end and that the coming phase in the Kondratieff cycle (sequence, in fact) would bring economic and stock market upheaval, that would simultaneously spell opportunity for those prepared for it. After all, one man’s loss is another’s gain. It is a matter of being schooled as to which investments prosper in the environment in question. To that end, countless reports discussing Japan, the US, the Dollar (currencies) and gold have been offered, both by SKDF and, over the past 16 months, by SKWC.

I found, however, that investors gravitate to what they know rather than expand what they know. If brokers (or whatever their called these days) remain ignorant, is that another’s excuse to not broaden horizons, only to blame the brokers for not having enlightened them? Leaders attract leaders. Sheep attract masters.

On January 13, 2000, SKDF pinpointed the all-time high of the US' secular bull market within 1 day (see "selected past comments" within the "previous comments folder" at www.sidklein.com):

"January 13, 2000: Happy Millennium. Now let us begin. The forecast Y2K short squeeze is over and the bear market in New York is free to begin. Japan will pull back with it on a lag as Westerners do the margin call thing. Its bull market vs. New York will accelerate, however, and many cheap Japanese equities in certain groups will actually rise (rotation) as the Nikkei is dragged down by the tech sector. For appropriate accounts, we are buying calendar put spreads (March/February) in New York...."

Valuation in the US didn't make sense and the low risk bet for investors was Japanese Domestic Demand Oriented Value Stocks (DDOVS): Hard-to-find risk and a ton of upside price potential. Speculators could have bought the aforementioned put spreads, for example.

There are appropriate ways to invest and appropriate ways to speculate. The key is to select consciously and not own the wrong asset class according to one's intention. Regrettably, investors remained invested in highly speculative securities and speculators were wiped out. Please note the following 3 comments, also available online in the "selected past comments" section within the "previous comments" folder:

"January 24, 2000: While in Asia, the Dow dropped sharply to 11,000 and I commented that the Dow should either rally to a slightly lower high or to a new high to convince players that the smash was false before collapsing to the 9,500 – 10,000 range in this first quarter. As I reminded members of the media last week, it is important to probe key intermediate cycle peaks as one may actually end up successfully shorting the peak of the long term cycle. We may have achieved precisely that 10 years to the month after having shorted, what was at that time, the greatest bull market ever to the week in Japan (Jan./90)...."

"February 25, 2000: ...Intermediate term forecasts called for a breakout and acceleration to the upside of the Nikkei versus the Dow Jones along with a break in the latter index THIS QUARTER to the 9,500 – 10,000 zone.

Nailed.

We bought puts on the day of the peak (Jan. 14) and today we exited. Nailed?"

"April 14, 2000: ...It certainly is not good for hot stocks that, sure enough, have been deflated by margin calls needing to be met. This latter phenomenon has also hit Japan. We now see why I have consistently cautioned to shun the Softbanks of the World and stick to "domestic demand, undervalued, under-owned, non-new-economy Japan". Especially with March 31st year-end out of the way, we are seeing the results...."

As the preceding 3 comments from 2000 indicate, SKDF provided extraordinary gains with pinpoint accuracy to speculators. More importantly, the speculator **knew** that he was speculating and he knew as well how much he could potentially lose. At the same time, investors and speculators everywhere knew neither that they were speculating nor just how much they were *gambling*. That's what "speculation" is called when one doesn't know what one is doing or, as Robert Prechter has written, what speculation becomes when it offers no **economic** value. Nortel owners in this country are aware of no economic benefit as having been accrued to our marketplace. Softbank fell about 95% too.

FACTS:

In any event, as the commentary above indicates, technology stocks everywhere, including Japan, did indeed go on to **Crash!** That dragged the Nikkei down (it inherited 30 tech stocks at the top), as **DDOVS** bottomed at the same time that everything else peaked and SKDF did correctly target New York's secular peak, just as it had 10 years (to the month) earlier in Japan. As for Japan's late '99 top, it followed the 50% rally in the Nikkei that SKDF had forecast in October 1998 (see "Sid in the press" folder re: Barron's and the Globe & Mail). In essence, the only safe haven of which I am aware right since January 2000 has been DDOVS.

JAPAN & DDOVS:

The "previous comments" folder is inundated with commentaries discussing the extreme merits and preferred timing for DDOVS. This report, then, will refer more to other themes and offer only one of many Japan commentaries written Feb.16, 2002:

"Westerners are selling Japanese shares to meet margin calls at home. This will worsen as the forecasted Dow spiral to 4,000-6,000 accelerates. Of course, there will be a point at which freshly discovered genius will dawn to the inspiration of Japanese share purchase. Then, the market's acceleration will force investors' hands, particularly those responsible for fund allocation (what could be more timely than the boardroom tribunals of institutions?)."

"With screaming opportunities in stocks, (strategically selected) bonds and the Yen, foreigners will also realize that these securities actually represent a safe haven! With the under-pinning of cheap valuation, domestic demand-oriented value stocks (DDOV's) in particular will be equated by smart money with capital preservation, as well as wealth creation."

NEW YORK:

What is sad is that the Dow rallied back to 11,500 in May 2001, coming within 200 points of the Jan. 14, 2000 summit. Through 2000, more reports than can be quickly counted reported that the yearlong topping process was very much akin to that of the 1973-74 period. The ensuing crash from May 2001 confirmed that analysis.

“Investors” were being given yet another chance, though the New Economy investors (public) were already trapped (NASDAQ). The Dow has thus far collapsed from 11,700 – 7200, while the more important (cap-weighted 500 share) S&P has crashed 50%. Who believed these SKDF forecasts in 2000?

Regarding the latter, the NASDAQ crashed from 5000 – 1100, dragging countless “name” stocks down 90% or more. SKDF stood out in warning that the New Economy stocks were the modern day “Nifty Fifty” (1973 – 74) and that retail investors would be demolished since that is where most of the money went. The “real bear market”, therefore, SKDF wrote, was the NASDAQ.

Most recently, SKWC forecast the Dow rally would not exceed 9000 (having exited at 8500). Then, after a near double top around 8700, SKWC warned that a pullback should ensue to 7800 before any cyclical bull market could have a chance. This has already been achieved.

GOLD:

On Jan. 21, 2002, SKWC wrote:

“Gold: All indicators are positive and a \$40 run at any time may be seen as likely. Many individual companies have turned-up chart patterns and seem ready for break-outs! One such possibility may be Durban Roodepoort Deep ADR (Drooy)...”

Therefore, though gold had bottomed at \$250 per ounce at the beginning of 2000, testing \$260 in 2001, SKWC only turned bullish at \$285 in January 2002. Since that time, SKWC has maintained that gold and gold stocks are in a secular bull market. Identifying **every** intermediate term move since turning bullish, our present position is that the maximum downside is now \$345, raised from \$333. The metal has already spiked back toward 350\$. One of many gold and Dollar warnings appeared on Mar. 3, 2002:

“GOLD: The U.S. Dollar will have proven to be overvalued and, in search of a liquid currency that is worth its weight, capital flows to gold could have a far more dramatic effect on its price than what market watchers imagine. If the Philly Gold and Silver Index (new up-trend in place) and levered gold stocks are any indication, this will indeed be the case. Apart from Japanese Domestic Demand-Oriented Value stocks (DDOV's), this continues to be the only group in which I believe. Let others roll the dice.”

Further supporting gold and the Dollar, the Mar. 23, 2002 letter commented:

“GOLD: Friday's strong advance in gold further supports the case that higher lows are being built in the metal, against which (gold) stocks are trending higher and higher. Apart from DDOVS, this remains the only theme in which I believe. It is reiterated here that a portfolio of gold companies that are leveraged to the price of the metal makes a great deal of sense, in the context of one's financial situation.

“The supporting background for gold includes a U.S. Dollar that is overvalued versus the Yen and the Euro.”

The Mar. 30, 2002 missive continued:

“GOLD: If I may be repetitious, the metal is in a new and powerful bull-market that will soar beyond all present expectations. As so often written here, follow the gold stocks (the Philly Index) for true direction and maintain a portfolio of quality, highly leveraged (to the price of gold) junior gold stocks for profit.”

The oft-reiterated view is maintained that a break over \$350 (which has now occurred), prepares the market for a move to \$500 (before advancing still further), with little resistance between here and there. From bottom to top, since turning bullish, gold has rallied from \$285 - 390.

SKWC has written more than once of gold's eruption to \$500. From the April 13, 2002 market letter:

“GOLD: This thing is going to fly over \$500 at one point...and it won't stop there. There is no change in the views held from the outset. Maintain a portfolio of junior gold stocks that are leveraged to the price of gold. We wrote of one stock and it doubled toute suite. Focusing on that sort of thing would make one lose sight of the big picture for which one is invested and in which one imagines oneself painted holding a bouquet of gold flowers.”

Regarding gold stocks, the position of favouring equities leveraged to the price of gold is maintained. Speculators and investors using the Philly Gold and Silver Index (XAU) may use 67 as a buy point, with SKWC viewing 60 as the worst-case scenario. That index has seen a rally from 59 to 89 since SKWC turned bullish, based on when SKWC turned “permanently positive” on the underlying metal (the low in 2000 was 45) and the potential remains enormous.

DOLLAR:

SKWC took its secular stand in the foreign currencies (Yen, Swiss Franc and Euro) at about the same time as gold. On Feb. 16, 2002, SKWC wrote:

“Several corporate bonds with relatively short maturities offer competitive or superior yields to ours (Canada). A decade ago, I advised purchasing Swiss and German bonds that were paying more than ours. My argument: they're solvent, we're not (did or does that matter for parochial and pedestrian brokerage firms?). Well, gains for holders of Swiss Franc and other currencies have been superb. Of course, it was obvious, right? Later, some economist will knowingly inform us that the balance of payment figures should have made the Yen's new bull market obvious.”

From bottom to top, since turning bullish on these currencies for wealth preservation and the maintenance of real return (!), the Yen has rallied from 77 – 87½. The Swissy has run from 59 - 74, while the Euro has advanced from 86 – 109.

SUMMARY:

In the final analysis, SKWC believes that one ought to only be positioned with the secular trend. For this reason, though a cyclical bull market is now forecast for the US, the author of these commentaries enjoys no confidence about that forecast or conviction about betting on it.

As a result, the only market in which one may find investment merit is Tokyo, focusing on DDOVS that reflect a theme that has not suffered any losses since 2000, while everything else but gold has been fraught with danger...and who needs that?

Gold and gold stocks round out the portfolio, while our favourite currencies are those in which our desired investments are denominated.

PERFORMANCE:

The purpose of this report's exercise is not about bragging; it is about illustrating that, as in past deep recessions or depressions, capital preservation and wealth creation opportunities are as great as ever, as long as one does not insist that life adapt to one's preferences and predilections. One must adapt to the market. That's reality. Accept it or get out.

We conclude this report, then, with a summary of investment performance, based on the numbers above. For gold stocks, we'll use the XAU performance as a reasonable average, though it in no way reflects the several forecasts that advised getting in and out of the market at key levels, with that portion of one's position which was deemed tradable. As well, the XAU price level used is that one at which SKWC turned bullish on gold and no accounting is made for the 3 approximate 100% gains recorded on individual stocks. Similarly, SKWC has enjoyed uncanny success in targeting every peak and trough in the US since SKWC has taken over from SKDF. These figures do not account for these entries and exits. Finally, something similar may be said of the currencies.

CONCLUSION:

All figures here reflect top-to-bottom or bottom-to-top performances, as the case may be. **No exits and re-entries are included, much as that would add to performance. Dates used are those above, when SKDF or SKWC made the market call in question** (as follow-up to this report, feel free to visit "previous comments", including "selected past comments" within that folder, as well as "Sid in the press", online at www.sidklein.com).

- the Dow fell **38½%**
- the S&P collapsed **50%**
- the NASDAQ was destroyed **78%**, taking many high-fliers down worse than that

- *by contrast DDOVS, that offered and offer the best risk-adjusted profile, bottomed when the US peaked and portfolio issues are up about **30%** (not shown), with much of the gains coming over the past 4½ months (currency excluded)*
- the Yen rallied **13½%**
- the Swiss Franc has performed **25½%**
- the Euro has erupted **27%**
- gold shot up **37%**
- the Philly Gold & Silver Index (XAU) advanced **50%**

THE BOTTOM LINE:

The Dow's recent intermediate term objective of 7800 has already been crossed. As well, a key warning is maintained here: Yes, a cyclical 15-month bull market in the US is possible but the operative word is "possible". If it happens, then the condition for an even greater eruption in DDOVS exists. For US "investors", the key consideration is the prevalence of an ongoing SECULAR BEAR market that was preceded by a secular bull market that observed no historical rules on the way up. Therefore, a drubbing that knows no rules on the way down is also possible.

SKWC will not give a major buy signal until the target (offered 3 years ago when the very thought was deemed unthinkable) of Dow 4000 is achieved. Finally, even if there were a cyclical rally, one would have to be a helluva stock picker. In Japan, however, where a SECULAR BULL market has begun, stock picking, particularly among DDOVS, is both risk averse and leveraged.

As this report is being concluded, DDOVS are powering ahead and even the Nikkei's spread and ratio versus the Dow is opening up noticeably.

The purpose of this report has been to illustrate that the fault lies not in the stars but, rather, in ourselves. It's all out there for our taking.

At the end of the day, capital preservation and profit result from proper analysis, not comfort. If being right comes with being comfortable and being comfortable comes from running with the majority, Nationalists and Fundamentalists would be right.

People who are right don't try to kill each other, rather,...they are comfortable.

Wishing you the comfort of profitable contrarianism,

Sid Klein

THE COMMENTS ABOVE ARE BASED ON DATA BELIEVED TO BE ACCURATE BUT NEITHER ACCURACY NOR COMPLETENESS CAN BE ASSURED. NO RECOMMENDATION TO PURCHASE OR SELL SECURITIES SHOULD BE INFERRED AND READERS ARE STRONGLY ADVISED TO CHECK WITH FINANCIAL COUNSEL AS TO THE APPROPRIATENESS OF ANY TRANSACTION FOR THEIR ACCOUNT. BARRING THE AUTHOR'S EXPRESSED PERMISSION, READERS ARE PROHIBITED FROM COPYING OR SHARING THIS LETTER BY EMAIL, FAX OR ANY OTHER MEANS.