

Precious Metals: Up, Up & Away Dow: Last Gasps, but Collapse Imminent? Yen & Japanese Domestic Stocks: A New Cycle of multi-Year Growth: 2007-09



The precious metals/Dollar section that is published on Gold-Eagle on a delayed basis is replaced on this special occasion by the original transmission in full.

November 5, 2006

JAPAN:

Fundamental:

The Japanese economy is set to slow less than other Asian countries, as a result of the coming US slowdown. The exceptions are China and India, whose markets are even more insular.

Meanwhile, Japan is actively and expediently pursuing economic partnerships and trade agreements with China, India and Australia, as reported in the past. Now, negotiations are closer to fruition. Japanese capital and political planning is taking the most strategic route. Emulating the impeccability of Japanese social and economic planning, government and business is focusing on the areas of greatest growth, while becoming less active in the West. To benefit from all this, Japan will have played the role of Asia's financier. No matter how many times

I've written it, it cannot be stressed enough that many appear to underestimate the powerful potential that Japanese capital can and will have in expanding in these markets.

SKC has been years ahead of such events, including what is unfolding now. Today, landmark financial history is being written.

Remember, as I've opined before, an additional factor may be that Asia is ready to replace the bitterness resulting from prior conflicts with Japan with a concern about a perceived growing Chinese monster. Still, it comes down to the basic analysis that I've written so often: Japan is Asia's financier, as the US was the West's financier after the Depression.

Japan has ended its deflation. The banks have resolved their problems and are lending, racking up profits. The government is awash in Japanese savings that will continue to be used to expand its Asian presence. And now, Japan benefits from what has been forecasted in these pages for six years:

Yes, the Yen will have become the world's third bloc currency, and a major cycle low has been seen this year, as so often reported. Foreign governments, I wrote, will increasingly use the Yen to store savings (see Yen below).

Higher profits and profit forecasts are going to be drivers behind higher stock prices and sustained growth in multiples, until an acceleration and blow-off in about 18 - 24 months.

DDOVS:

The New York and London Stock Exchanges seek partnerships or business exchanges with the Tokyo Stock Exchange. The world's third largest stock market will again be the second largest, and smart money knows it.

Know this: Liquidity will only expand, for the economic and investment reasons cited above, as well as the fact that equity investment is gearing up to benefit over the longer-term from greater Western participation and underwritings. What this means as well is that small and mid-cap stocks will be enormous winners over the coming five to ten years, as liquidity and the expansion of market caps allows pension funds and other Western institutions to own these stocks.

On a more than anecdotal note, online brokerage firms that focused marketing efforts on seniors enjoyed accelerated profit growth. As reported in the past, the vast majority of investment capital is in the hands of people over the age of 50. Their growing demand for stocks is a further sign of unfolding and potential demand for domestic stocks, as Japan holds trillions of dollars worth of Yen in AAA savings that are held by people who need to use but a small amount of their savings for living.

As these are older investors, they will steer toward more conservatively valued companies. This is yet another driver for DDOVS. Remember, as of a year ago, with the Nikkei doubled, the domestic investor was still not participating. They have begun a new cycle of equity investment that is in its very early stages. The investment world will again see what can happen to prices when the Japanese turn the liquidity loose.

Though the Yen did indeed bottom it did not liftoff this year. This weighed on domestic stocks considerably. I mistakenly felt that they would bottom in the first quarter, when the Yen did in fact make its low. I continue to believe that this equity theme is bottoming in its third three-year cycle this decade. Valuations and chart patterns, whether long, intermediate or short term, all point to bottoms in this seasonal period of lows during November and December.

I initially planned to recommend and review a number of Japanese stocks selections in the November and December issues. They will be covered at once next month, instead. Given the timing, as per the comment in the previous paragraph, one might wish to prepare to pull the trigger next month on stocks covered in that December report.

Nikkei/Dow ratio:



The Nikkei/Dow ratio chart (not shown) has corrected into a buy zone that allows for a cycle rally to commence in that relationship (ratio), at any time. To correlate this in plainer language, in looking at the individual indices' charts (see Nikkei chart above), the Nikkei can fall back to test the 14,000 zone as the Dow suffers an initial and more serious correction, as part of the resumption of its secular bear market.

In other words, asset allocators and the investment world will see more of a new secular bull market in the ratio, which means a Nikkei that makes higher highs and higher lows, while the Dow makes lower highs and lower lows. While redundant, the view often expressed in these pages has been and remains that **we have long since begun to see the mirror image of the nineties**, when the Nikkei and Dow went in opposite directions.

Strategy:

On a long-term basis, and for the reasons discussed in the DDOVS section above, the DDOVS theme optimizes how to benefit from the previous paragraph, by focusing on the best Japanese theme. One that is supported by the secular trend and valuations that, together, provide long term preservation and growth potential that is tailor-made for this phase of the Kondratieff [Long (economic) Wave] cycle. Be best positioned for the passing of the torch from West to .East.

Can there be any question that Asia, with Japan as the conduit is the way to invest in the region? Japan (and Asia) is less affected by a US economic than others, while domestic stocks are virtually unaffected at all. The expanding business and investment with the rest of Asia will only expand the Asian business playing field.

Value stocks will have become growth stocks as they are the best poised to expand, invest and participate in Asia. Plain and simple. For all the obvious economic reasons, the play on the price earnings multiples, as well as the fact that they are coming off a major cycle low, means that returns for many stocks over the coming two years will be triple-digit, as the secular up-trend advances, now that the correction of the initial cycle move up from the 2000 – 2001 lows winds down.

NEW YORK:

The collapse in the housing and real estate market may take 1.5 – 2 points off GDP next year. I have already written that the previous rate hike would be the last and the realization that this may be the case began a drive out of plentiful cash held by the public.

Those who felt that the market would be driven to new highs, as next year would get the brunt of the bear market, have been proved correct. However, in

anticipation of window dressing for yearend that would be triggered by such investments' effects, has the Dow already topped, ready to ambush those who can't imagine a collapse now?

What I do conclude is that short-term indicators suggest that a new high is likely, in much the same way that there was a final Dow rally in the first half of January 2000, after taking a year-beginning hit that had followed Y2K's failure to end all life as we know it. That rally squeezed those I thought would be last shorts ("oh, even Y2K's non-disaster can't bring down this market") and the first part of this week may, along with these US elections, manifest a similar phenomena.

Last month, I analyzed that the Dow would have to be down this month, if it were to not negate the sell signal given by the very "heavy" and therefore extremely significant monthly stochastic. That was incorrect and, so, that major sell signal remains in effect.

Never has bullish opinion been so bullish for so long, but (and so) the net of all indicators suggests that the market is peaking now, but not prepared to collapse before Christmas. For us, the point is moot. Our allotment for puts for this 12-month period was invested at 11,200. Any new put purchases (in puts that are three months longer-dated), therefore, creates the opportunity to sell the puts bought at 11,200 after a 1000-point decline, while holding the newly acquired options. The first puts will probably be in a profit situation just due to a volatility spike. Though, volatility since then has collapsed back toward lows. The good news is this means that even 10-month puts will very likely double on a Dow down to even 11,200, just a thousand off the peak. With the Dow and VIX at these levels, never have I seen Dow or S&P index puts that had more leverage, or been so sensitive to any down-move in the market, than right now.

A background of higher precious metals and oil prices is not at all inconsistent with a Dow apogee that now appears evident....

OIL:

Oct 4: "In any event, oil tanked the morning after the most recent report was transmitted. The strategy remains the same unless oil touches \$57, or closes the week below \$58 (please see chart below)."

Indeed, see the chart below, for the froth is gone and we're good to go.

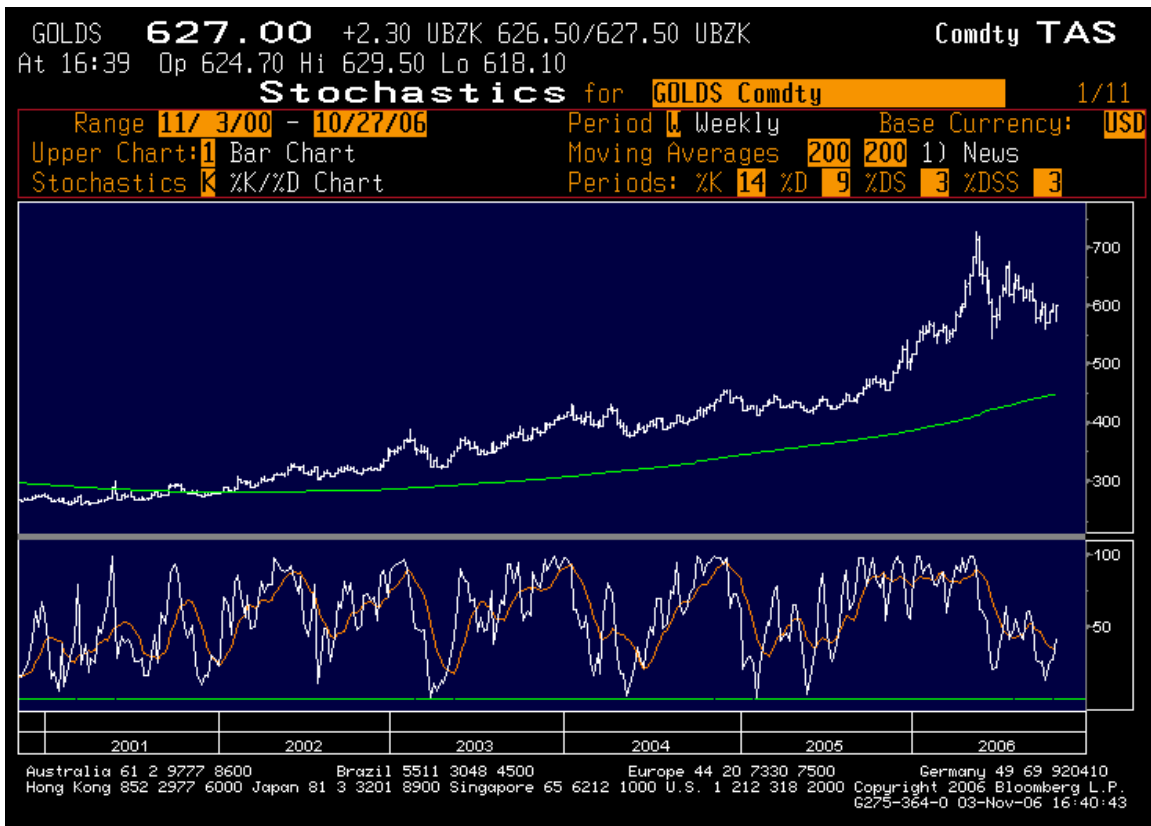


Strategy:

The strategy remains unchanged. The day after the recommendation to go long, oil fell into the \$60 - \$61 zone. Market-if-touched (at \$57) orders came close (within cents), causing cardiac unhappiness for traders. However, one could also conclude that the stop strategy was perfectly placed. In any event, I reiterate that oil could make a new high, or not, but that either way the next move is up, and it should be a nice trade. In any event, let the stop strategy be your guide. As a special situation, SKC had precisely targeted oil at its previous and significant intermediate term low. This play will not be as explosive, simply because I will take a more reserved strategic approach, as the pattern is farther down the road, the US economy is slowing, and the Republicans could always lose pig...I mean big. If they don't, oil would further benefit.

PRECIOUS METALS & DOLLAR:

Perfect again. The correction was indeed A-B-C, as so often described and forecast. This is what has played out and while the very early-year forecast of \$850 per ounce for **this year** is unlikely, **\$750 isn't**. Either way, the forecast stands, that a larger "Wave 3 of 3" will be underway next year, en route to \$2000. Ask yourself (again): "How much do I feel like making?"



October 4, 2006: “For trading positions, I turned bullish almost immediately after gold hit \$550 and turned bearish almost right at the countertrend peak “just under \$700”, as forecast. Thereafter, I turned bullish again at \$605 (on August 31st), choosing not to wait to see if the metal would indeed revisit \$550.

“Well, “more fully re-test” has occurred and it must be taken advantage of. At \$280, many didn’t believe. Then several occasions existed between that level and \$400. Then 500. And for all the opportunities, we did see \$700, and we will again, and \$800, and \$1000, and so on. I avoid discussing my long-term numbers because I find that that only distracts investors from what’s being projected for this cycle or the intermediate term.

“Bottom line: 100% long gold. That’s always the case in the “bond” portfolio, but this is true for trading accounts now, as well.”

Retracing our steps:

After commenting that a low had just been seen on **June 20, 2006** with gold then at \$575.30 and silver at \$10.26, the **June 28** letter then reiterated: “**Gold and silver have bottomed and any new lows would be minor. Here too rallies**

could be sharp, violent, and short lived. Many markets are in periods of corrections within corrections.”

From the **July 12, 2006** report: “When gold’s low was identified, I forecast a massive A-B-C rally, implying that gold would rally all the way to back to approximate highs, before collapsing back to recent lows around \$550. For the very near term, for those who didn’t enter earlier, this week’s breakouts may be tradable, as our stocks are worthwhile for the longer term, in any event.”

Then, on **July 18**, “As for gold, it has come through with SKC’s huge rally within a correction. Simply, I looked for a rally off of the bottom toward \$700, before re-testing the lows.”

Silver strategy:

“How much do I feel like making?”

This question is most appropriate with respect to **silver**. As discussed with investors and readers this fall, how hard is it to watch silver go to \$20 on 50% margin (a move that is already underway)?

People trade with very little margin (i.e. futures), but I’m not thinking as a speculator. I’m thinking as someone who wants to capitalize on a portfolio’s capacity to use a comfortable vehicle and strategy. In the early stages of secular bull markets, several such opportunities may present themselves.

Unless silver, far from maintaining its secular bull market, were to actually reverse and actually make multi-year lows and thereby confirm a secular bear market within which all this has been countertrend (the definition of absurd), there is an enormous low risk opportunity, by using as much as but/and only 50%.

Supply shortage, unexplainable short interest and long-term momentum that cannot be broken: all describe how young this great secular bull market is. At its low, silver fell to under \$10.00. Consider an investment of \$50,000 that buys \$100,000 worth of silver at, say, \$12.50. What is the profit at \$20.00? The metal is going much higher than that but that’s a bare minimum target for 2007. The best things in life are simple. Keep the basic calculations that way.

There are times when one is wise to invest a small amount of money in an inherently leveraged instrument (i.e. options), there are times when it is wise to use a conservative vehicle and strategy, and invest in a leveraged fashion (i.e. silver strategy). There are still other times when it is appropriate to use a leveraged item with open risk and profit (futures), using a stop (i.e. oil strategy).

Which contemplated strategy to use depends on the market view held with regards to the investment in question. This is further considered within the context of the asset allocation decision taken toward that investment class or market.

Just as gold has bottomed and can now rally to new highs – and **perhaps quickly** – the same can now be said of silver. Again, do the math.



Japan will benefit for years from an ever-expanding international acceptance of the **Yen** as a **reserve currency**. For six years, I have forecasted that the Yen will have become the world's third bloc currency. Gaining international status helps that along, to say the least.

Russia has over \$260 billion in reserves that are held in Dollars, Euros and Pounds. Russia's central bank has already begun purchases of Yen that is intended for its foreign-exchange reserves. The new cyclical bull market in the Yen began. The liftoff is a matter of course and the time is near. Very near. But the very long term is nothing short of crucial (for provincial-minded Western investors, for instance).

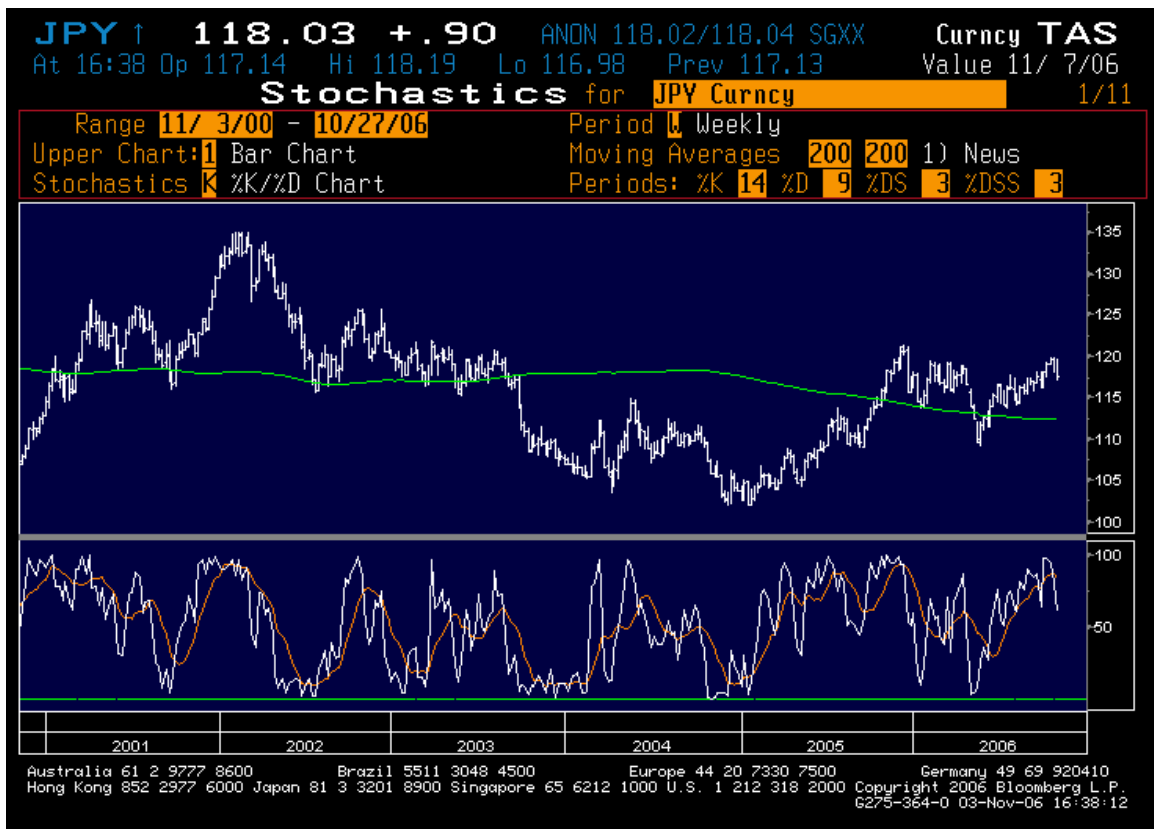
A rate hike is unlikely before yearend in Japan and this rate game has been what has held back the impending Yen breakout. Next year will be a dilly for the Yen and ideal confirmation would be a 2-3 Yen reversal that is presumably related to a central bank decision of some form of change of policy, or other.

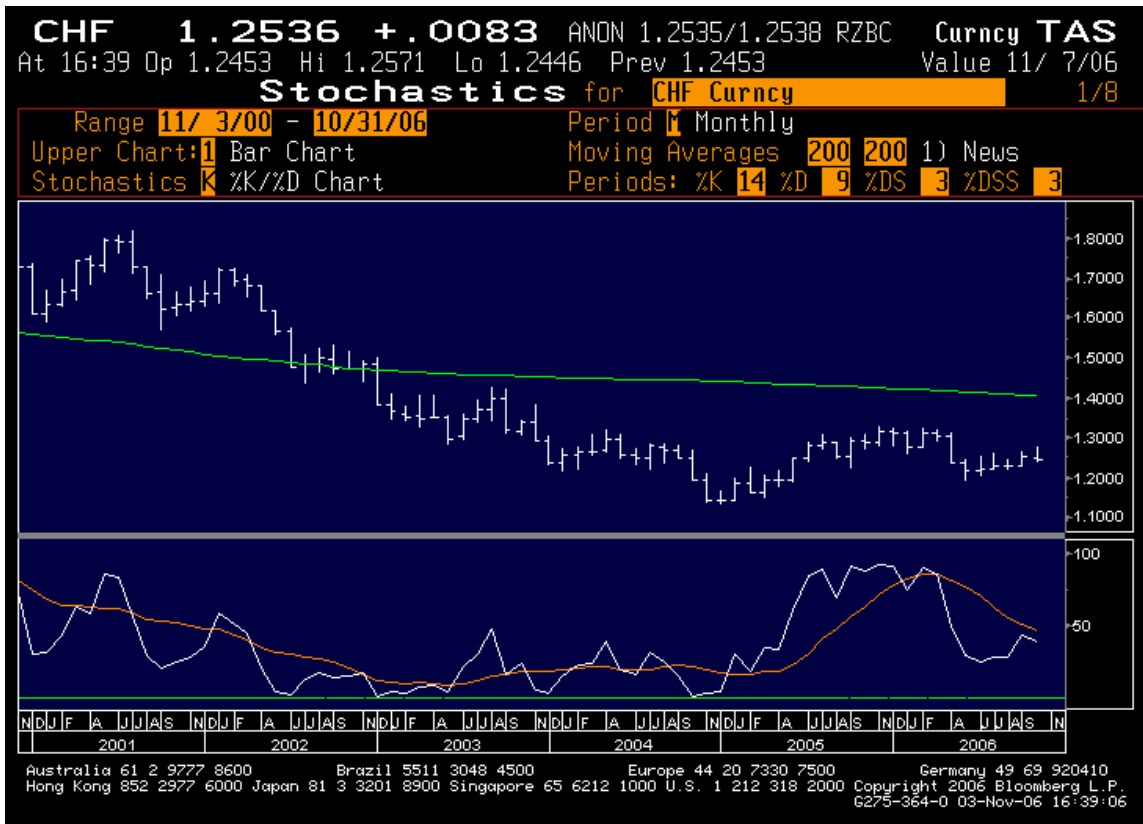
Comparing the Yen (below) to the Swiss Franc (follows Yen chart), we see this superior and most resilient safe haven, this partial fiat gold proxy, the Swiss

Franc. Hence, what I believe to be the ideal asset allocation, which remains unchanged.

Asset allocation:

Reviewing the recent years and regarding three losing put positions in three years, I can only point to asset allocation as salvation. Puts represent a minor percentage of anyone’s wealth. By itself, trading gold and silver ETFs or equivalents has “paid the bills” for years - and with unsurpassed timing. Gold represents 50% of investors’ entire wealth (or gold and silver 40% and 10%, respectively). This is rounded out by 25% Swiss Franc and 25% Yen. (Continued after Dollar/Yen and Dollar/Franc charts.)





If all other markets have been rewarding this decade, including the Dow, which has been difficult post-2004, no regrets. If this year is as bad as it gets, for instance, and the great years are blockbuster, well, okay.

NB: One chart above is weekly while the other is monthly, to show that stochastic readings support the Dollar-bear resumption scenario.

Sid Klein

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