The Sid Klein Comment

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Confirmations

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Gold: $580.50
Silver: $10.22
Yen: 85.93

This month's third interim report comes as the regularly scheduled letter is to be published. After the Canada Day – US Independence Day celebrations, we'll look more closely at the fundamentals of each of our four sectors. For now, let's summarize.

JAPAN:

Construction and real estate are racking up Japan's highest profit growth rates, while consumer prices are now having an inflationary effect.

SKC has led all in directing attention to the fact that consumer prices would soon prove inflationary, as pent-up demand finally draws on savings due to Big Bang's sundry and obvious successes.

The Nikkei has a strong floor at 14,000 and investors may be expected to front-run that level. Therefore, any new short term low would not be by much. In the first quarter, my stance had been that taxes and higher rates would be the focus of attention as an excuse to deflate excess foreign hedge fund buying and fund buying. Everyone owned the same stuff. But I also felt that the subsequent correction would create major buying opportunities, in this cycle turning point year for markets.

Government officials have remarked that the recent correction is due to a need to remove excess leverage from the system and that such re-balancing is nearly complete. In the downdraft, domestic stocks have been dragged down or staying down on extremely light volume. It's possible that after the testing of recent lows (higher or lower), the Nikkei's ensuing rally could be short-lived before testing lows. (This jibes with view on New York.)

Japan's central bank decided to not raise rates, but what it actually had said that was important was that the draining of funds should not be taken as an immediate signal regarding the raising of rates. Is Japan now where the US was in 2004, with the Fed funds at 1%? Yes, but there's no need to say so. The desired effect was achieved without aggravating the US' need to not pressure rates further. But the only thing that is going to matter from now on will be whether the BoJ raises rates. Relative rates competition will continue to create gold buying opportunities, in an ongoing bull market in that precious metal.

Japanese domestic stocks are generally still of three categories: Firstly, there are those that simply have corrected during the same time period as the Nikkei and are at lows on light volume. There are off-cycle stocks that have just made higher lows, higher within nice up-trend channels as well. Then, there are late economy cycle plays. These are at their perfect lows after a strong rally and basing period. Stocks fitting that description include those that are affected by the real estate market's lows, after 14 years or so. While all these factors have come together for the seasonally weak June quarter-end period, the Yen is completing its pullback. These different factors will reverse, to the profit of Japanese portfolios.

This is the period of major acceleration for the Japanese economy in the 2006-2008 period. While the Dow is crushed, the Japanese stock markets will be making higher highs. First, we had the breakout in the Nikkei/Dow ratio (chart). And now, we'll see the inversion of the 90's: Lower lows in New York, higher highs in Japan (higher and higher gold and silver prices, too).

NEW YORK:

The minimum bearish expectation is 10,600, while the 10,200 – 10600 lies below. I think there's only a 25% chance that the Dow will crash through right now. Any upside would hasten the larger smash. Either way, moves will be large and they will be negative before the year is out. For now, a new low to complete a sequence of market decline for the short term would be consistent with bottoming formations in Japan and gold. Remember:

The top is in and this rally is corrective.

PRECIOUS METALS & DOLLAR:

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.

Sid Klein