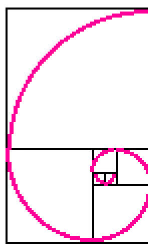


Sand Spring Advisors LLC

Slouching Towards Trouble

by,

Barclay T. Leib

February 21, 2010

In November 2008, the *New Yorker* magazine published an article entitled *"In For It"* about an election night party where one anonymously-named hedge fund manager (in all truth, yours truly) made some predictions. The story that reporter Nick Paumgarten penned went, in part, as follows:

> For the Republicans in the suite, resignation had taken root weeks, if not months, earlier, and had grown into a kind of worldly indifference, grounded in the half-sincere belief that our new President, be it Obama or McCain, would be no match for the havoc in the financial markets and the spiraling economic mess. It is a widely held view among the investor classes that no one in Washington has any clue how the world really works.
>
> The host predicted that President Obama would have a miserable term and face a challenge from within his own party in 2012…
>
> Another guest, a trader and market strategist who had voted for Ralph Nader, agreed about 2012, but according to a different logic. He expounded on a belief he held regarding the cycles of history and the markets. It was based, he said, on the formula for the circumference of a circle—the idea that 2p*r* might apply to the financial cycle—and, in combination with various Fibonacci fractal techniques, it had made him a lot of money. You could slice up history into what he called pi cycles, each lasting exactly three thousand one hundred and forty-one days, or 8.6 years. You could subdivide these, by the hours on a clock, say, or the signs of the zodiac, and detect mini-cycles of 8.6 months. He rattled off a series of inflectionary dates and occurrences: the Nikkei high, in late 1989; the ruble collapse, in mid-1998; the historically tight credit spreads in early 2007. By God, he was onto something.
>
> According to pi-cycle theory, after a failed attempt at a rally between now and next spring, the market will not hit bottom until June, 2011, so Obama may be doomed to muddle through a deepening recession and the unpopularity that comes with it, and whoever succeeds him in 2012, should he lose, will then have the chance to ride the recovery—to be, in the public's untrained eye, the transformative F.D.R. or Ronald Reagan that people dearly want Obama to be now.

Since taking office eight weeks after this article appeared, President Obama has – charitably – run a muddled and confused Presidential agenda. He somehow wants our economy to de-leverage while still facilitating lending to marginal housing and business borrowers. The U.S. government must get its fiscal house more in order while at the

same time providing additional tax credit relief for child care, elderly care and to small businesses hiring additional workers. Our banks are vilified for not lending enough while at the same time told that they need to have higher capital adequacy ratios and fewer business areas within which to generate income. Their windfall profits from the early 2009 stabilization are deemed so egregious as to merit special taxation policies. America needs to address entitlement reform if it is ever to reduce its huge deficit (which ran at 9% of GDP across 2009), and yet Obama feels it critical to expand Federal involvement with and spending on healthcare.

Someone out there wants to *have his cake and eat it too*. Unfortunately, the effective "economic corner" towards which governmental policies for the past thirty years have now led us is more suggestive that there is simply *no cake left to eat*.

When I see Obama today I see a man acting as if he is still on the campaign trail. Instead of sitting behind a desk and getting down to the hard work or actually doing something – hammering out nitty gritty details and the like -- he feels compelled to get on a plane to go to some part of the country to give a cheerleading inspirational speech.

Carefully read the passage below from yet another hedge fund manager, and see if these words don't aptly describe the current position of our well-intentioned, but naïve and somewhat frustrated, 44th President:

> "Obama aspires to be a transformational leader capable of overcoming opposition and mobilizing mass support through his eloquence and attractive personality, emphasizing the positive and self-evident virtue of his aspirations. At the same time, [under the Obama approach,] by assembling the best and the brightest, the attendant programs will be implemented in efficient, nuanced ways through guiding and inspiring, but not directing the Administration's legislative allies. *This mix hasn't worked*. Peaceful or not, transformational change tends to be a ham-fisted business of first principles, not nuance. Uncontrolled legislative allies often have their own divergent agendas.
>
> [For better or for worse,] the public holds elected officials accountable for events on their watch, regardless of whether the officials argue the problems in question long antedated the current officeholders. Add to this fatigue, overload as the agenda of immediate issues stretches resources thin, and shoves to the side longer-term issues on which the President wishes to lavish attention, and the inevitable inadvertent linkages and trade-offs among problems, and the stage is set for a term largely extemporizing from "crisis" to "crisis," amidst rhapsodizing about the Administration's bold intents *and what might have been but for crisis/events/opposition."*

Ok already, I am not an Obama basher. In my heart, I like him as a person and admire his effort and vision to try to create a new and better America. The problem is: complexity rules, and America's former excess is just too great to be easily remedied.

Within various speeches, Obama typically begins his depiction of America's financial malaise as having started with a bunch of "greedy bankers." What he misses – and just blindly does not see -- is that it really started with the excesses of government.

The problems of America's current economic state today arguably started all the way back with a Johnson Administration – an administration that did not know how to pay for both the Vietnam War and the "Great Society" together, but spent the money anyway. It continued into the August 1971 decision by Richard Nixon to move America off the gold standard – effectively buying some time where excessive spending could continue without immediate negative consequences. Until of course the oil price went nuts in 1973-1974 and then again in 1979-1980.

Paul Volcker then had to be relied upon for a small dose of "tough love" with his shock therapy of ultra-high interest rates in 1981-1982. But then even Volcker acquiesced in August 1982 and effectively joined the party brigade led by Ronald Regan who cut taxes to keep the party going, but also thereby made the federal debt build-up even bigger.

Then we hit the 1986-1989 policies of Treasury Secretary James Baker. Faced with a burgeoning twin budget and international trade deficit, Baker could (and likely should) have elected another bout of Volcker tough love by encouraging an economic recession with higher U.S. interest rates. But what able-bodied American politician (particularly one who went to Princeton's Woodrow Wilson School – my alma mater) can actually bring himself to create a recession on purpose? Instead, Baker tried to get tricky, and encouraged Japan to lower its interest rates in an effort to stimulate foreign demand for U.S. goods.

When Japan then grudgingly implemented Mr. Baker's advice, all that happened instead – very much as an unforeseen consequence -- was the creation of an equity and property market bubble in Japan that attracted global capital. Japan soon grew to control 25% of global savings. This 1989 bubble of course eventually ended in a 1990-1991 Japanese Crash that effectively remains ongoing today.

At this point in the mid-1990s, capital went sloshing out of Japan in search for a safer home back in the U.S. and Europe. Bill Clinton and his Treasury Secretary Robert Rubin just happened to be in the right place at the right time as this transpired. There was no piper to be paid at that time.

If they had really wanted to, there was a moment circa 1996-1997 when the Clinton administration could have slowed down the building economic chaos. This was when the issue of financial regulation of derivatives was being discussed, and CFTC commissioner Brooksley Born argued that the CFTC should be granted control over the over-the-counter derivatives market. Rubin, Clinton, and current Obama advisor Larry Summers all argued: "no." Let freedom reign and the good times roll.

Then alas -- particularly post 9-11 -- George W. Bush started aggressively spending government money again while the economy sputtered, and all the hidden warts of America's 1965-2000 excessive spending and debt build-up started to manifest themselves in problematic ways yet again. With Greenspan (and subsequently Bernanke) at the helm of the Fed keeping interest rates artificially too low for years on end, the path of least resistance was for the U.S. dollar to tumble. At least initially, this dollar weakness was actually supportive of American corporate profitability, and partially masked underlying substantive economic problems. The faux illusion of prosperity was created. Across the greater portion of two decades, stocks went up as the

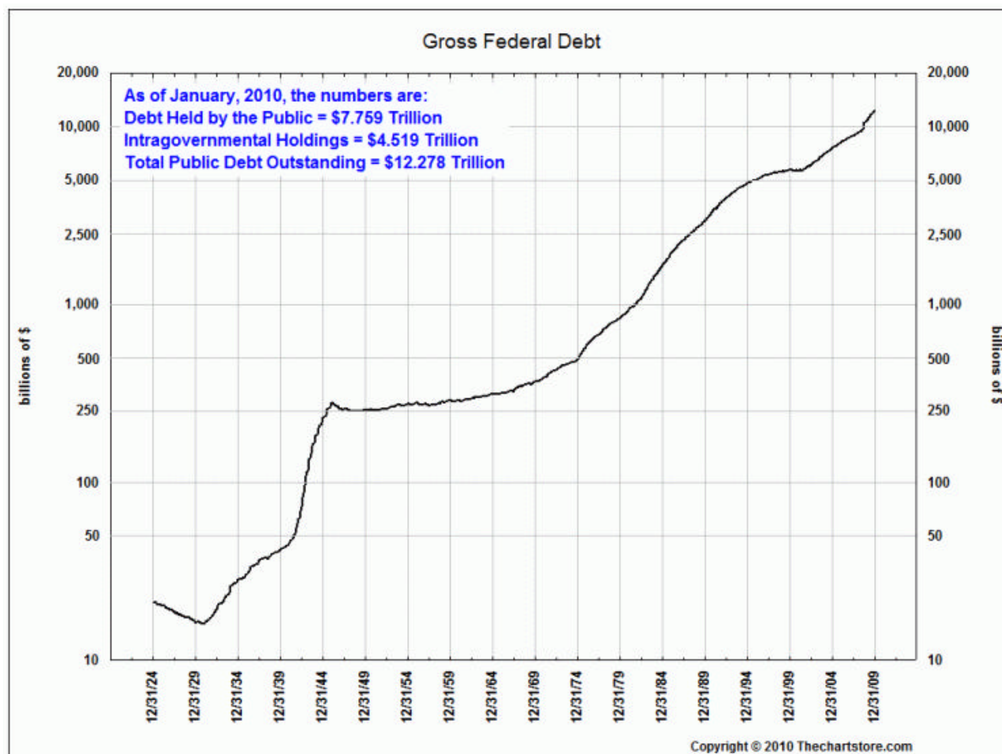
dollar went down. Americans weren't really richer in true global terms, but they felt richer in domestic terms.

But when the Fed did start tapping on the interest rate breaks just lightly in early 2000, all hell breaks lose. Stocks tumbled. Americans then started to scream. Another shot of morphine emanated from Greenspan starting in 2002, but by 2007, the economic patient was crying again about house prices that have plunged below loan-to-equity financing thresholds.

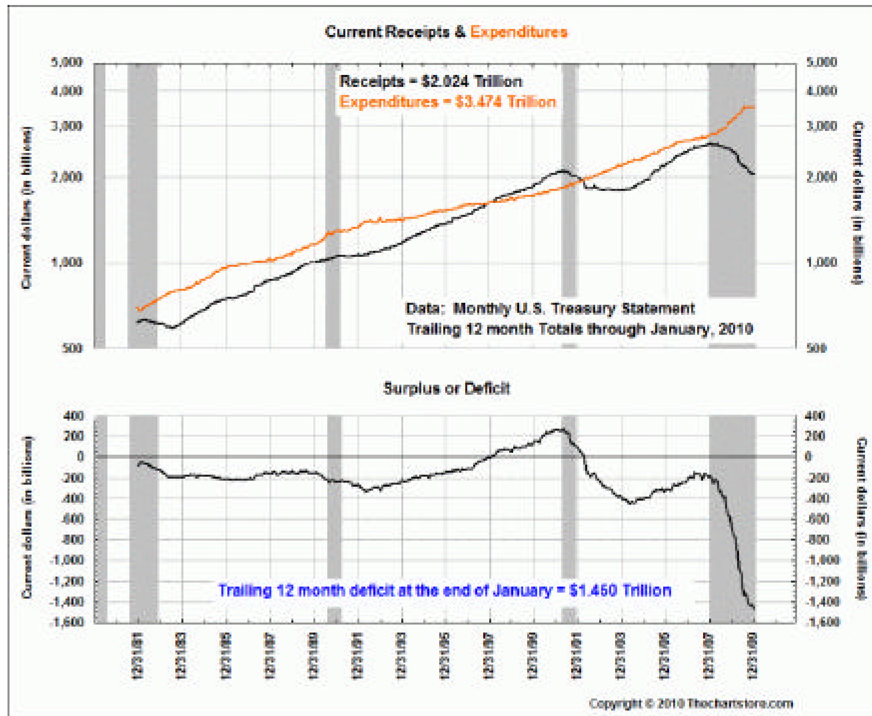
Somewhere along the way, *governmental policies were the true root behind all of this* – not the evil bankers of Wall Street. The bankers simply played the board game under the rules that were set for them. The basic status of the economy was already far askew long before the bankers start bending any of these rules.

Yet this is the core fact that Obama completely and myopically misses, and because he misses it, he is highly unlikely to be able to find the correct solution to current imbalances. The correct solution does not involve "dancing around the edges." Instead, it likely involves more serious core surgery on the entire system. The current tax code should likely be scrapped and simplified. Savings should be encouraged; not dis-incentivized. Interest rates need to end up at a more normalized higher level, not at ultra-low artificially maintained levels. America's entire psyche and equity market likely need to take it on the chin in a period of real retrenchment and pain.

Sadly, America's political system does not currently embrace pain in a noble fashion. Instead, it strives to avoid it. It will take a crisis – a war perhaps – to reshuffle the economic imbalances that have developed. When I say this, I imagine perhaps America and China somehow at odds – thereby giving the U.S. and excuse to renege (or otherwise walk away) from the $755 billion of Federal debt owed to them. Even still, this would only put a minor dent in the $12.4 trillion of total Treasury debt outstanding.

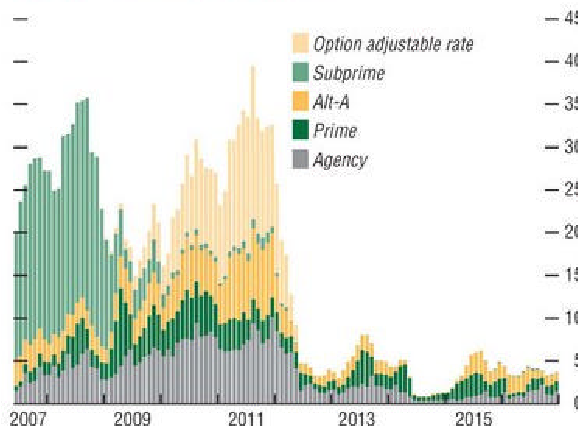


The real immediate problem finds itself in the divergence between the yellow line of federal expenditures and the black line of federal receipts depicted below. This is simply a time bomb waiting to derail America.



Meanwhile back in the boom years of 2003-2006, over $600 billion of emerging market corporate and sovereign debt got refinanced – with much of the corporate debt carrying "covenant-light" terms. Much of this debt will be due for rollover during the next two years. Who exactly is going to step up to roll this debt, and on what terms? Current problems with Greece are just a front-end taste of these global refinancing problems to come.

And how exactly are we going to navigate past all the option adjustable and Alt-A mortgage rate resets due over the next 18 months?



No, on a cumulative basis, this will all be too much for Mr. Obama's well-intentioned efforts to change America. *He is unfortunately the wrong man at the wrong time.*

Interestingly, note that the peak in mortgage resets depicted in the chart above roughly hits in mid-2011 – exactly when our pi cycle low is due. This should be a dour and depressing time in America, but when we make it past this hurdle, whoever is elected President in 2012 will look like a hero – whether he (or she) be a Republican, Independent, or another Democrat.

In the meantime, we expect something akin to a 1939-type year for 2010. We say this looking back at the analog rhythm that exists between the 1929 peak and the 1999 peak 70-years later. Stocks topped in 1929, and seventy years later they effectively did so again in 1999. 1930-1932 was a nasty first taste of the Great Depression. 2000-2002 was a similar nasty first taste of what was then called the demise of the dot.com bubble, but may someday be called the beginning of the "Great Malaise." Between 1933-1937 business revived again, and similarly between 2003-2007, there was a Fed-induced economic rebound. But starting in August 1937 and similarly between February and October 2007, many markets started to break again. In the latter instance, serious cracks in the sub-prime lending market were followed by various quant hedge fund problems in August 2007, followed by the equity market meltdown of late 2007 through to early 2009. The last three quarters of 2009 represented a rebound period -- just as did most of 1938. Are we now due for a 1939-1942 type of environment as current economic angst slowly leads to more global geo-political angst?

For those who don't quite remember what 1939 looked like, it was a "start-stop" affair with protracted weakness from late spring to mid-year, followed by a late year rally – to close roughly unchanged. New lows then followed into 1940-42 before the arrival of WWII eventually ended the Great Depression.

Will this mean 2013 brings a major global conflict akin to 1942?

As we wrote back in 2001 in our article the *The Cycle of War*, war tends to be on an eleven year cycle somewhat tied to sunspot maxima. Our last sunspot maxima came across 2000-2003, more or less centered around the 9-11 World Trade Center attack. Conversely and not surprisingly, the buoyant market ebullience of late 2009 actually transpired across a year of very low sunspot activity -- a slightly late sunspot minimum period. So 2012-2013 would be a logical window for another maxima period together with an acute period of global conflict and tension.

Grab your hat and hold on. While the next sunspot maxima is currently predicted by NOAA to be less ferocious than the 2000-2003 maxima period, might it even be possible that the protracted financial tension of 2007-2009 wasn't really the "Big Kahouna," but simply the warm up?

Such is the view of Robert Prechter of Elliott Wave fame who would suggest that we are about to embark on a 3 of a III wave down within an overall nasty C-wave. Per Prechter, it is the C-wave portion of economic downturns where the impulse for revolution and secessionism tends to manifest itself in society.

Source: Elliott Wave Intl

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The recent rise of "Tea Party" participants will likely gain more main stream support between now and 2013. If Obama has swung us towards the left with Big Government as our supposed savior, the unfortunate pendulum of human emotion placed under economic stress may next easily swing us violently to the right where there will be calls to do away with our present form of Government altogether. At the extreme, one might even think: Weimer Republic slipping its way toward Hitler fascism.

How ironic it is that in a recent straw poll of prominent conservatives, Congressman Ron Paul – previously viewed by many as a fringe nut case – was voted as the most favorite Republican candidate for 2012.

Ron Paul Wins CPAC Straw Poll

By tmartin on February 20, 2010

Ron Paul wins this year's straw poll at the Conservative Political Action Conference (CPAC), overtaking Mitt Romney and Sarah Palin as conservatives' favorite for the 2012 presidential nomination.

Ron Paul	**31%**
Mitt Romney	**22%**
Sarah Palin	**7%**
Tim Pawlenty	**6%**
Mike Pence	**5%**
Newt Gingrich	**4%**
Mike Huckabee	**4%**
Mitch Daniels	**2%**
Rick Santorum	**2%**
John Thune	**2%**
Haley Barbour	**1%**

Yet fundamentally the answer to understanding the real pressures of 2011-2013 continues to reside in China where a huge experiment in faux capitalism currently transpires under the auspices of a communist government.

Just read the recent Bloomberg articles below, and compare what is happening in China today to what happened in Japan in 1988-1989. In both instances capital accumulated within a bubble environment created by governmental policies that were not sustainable over the long term. In the current instance, and in reaction to the 2008 slowdown in Western demand, the Chinese put their monetary "pedal to the metal" last year by huge quantitative easing (absolutely dwarfing America's own quantitative money printing) and aggressively extending credit for various building and construction projects across the country. This has kept the Chinese people employed in the short-term, and the general appearance of prosperity. But whether anybody really needs all of these buildings and construction projects is another question. While global savings has headed to China, the level of bad loans in the Chinese banking system – suspect even before the problems of 2008 – has likely burgeoned to truly monumental levels. Consider the following item that I read in early February:

Feb. 5 (Bloomberg) -- Non-performing loans in China have risen into the "trillions of renminbi" because of poor lending practices, an insolvency lawyer said.

"We work really closely with SASAC, the state-owned enterprise regulator in China, and there are literally trillions and trillions of renminbi of, frankly, defaulting loans already in China that no one is doing anything about," Neil McDonald, a Hong Kong-based business restructuring and insolvency partner with Lovells LLP, said at an Asia-Pacific Loan Market Association conference yesterday. "At some point there's going to be a reckoning for that."

China's government is tightening controls, including banks' reserve ratios, to prevent record lending from fueling inflation. The Shanghai office of the China Banking Regulatory Commission warned yesterday that a 10 percent fall in property values would treble the number of delinquent loans in the city. Liu Mingkang, chairman of the CBRC, said Jan. 4 that loans were channeled into stock and property speculation last year, which China has been taking measures to stop. CBRC's press officer is not immediately available for comment today.

Chinese banks issued a record 9.6 trillion yuan ($1.4 trillion) of new loans last year as part of a 4 trillion yuan stimulus package aimed at bolstering growth through the global financial crisis.

"At some point in China, maybe it will be two, three or five years, but at some point there will be in the property markets and in the markets generally, there will be rationalization of very poor lending practices," McDonald said during the panel discussion on restructuring and refinancing at the Global Loan Market Summit in Hong Kong.

A few days later on Bloomberg, an even more detailed description of the China situation appeared:

Feb. 12 (Bloomberg) -- Jack Rodman, who has made a career of selling soured property loans from Los Angeles to Tokyo, sees a crash looming in China. He keeps a slide show on his computer of empty office buildings in Beijing, his home since 2002. The tally: 55, with another dozen candidates.

"I took these pictures to try to impress upon these people the massive amount of oversupply," said Rodman, 63, president of Global Distressed Solutions LLC, which advises private equity and hedge funds on Chinese property and banking. Rodman figures about half of the city's commercial space is vacant, more than was leased in Germany's five biggest office markets in 2009.

Beijing's office vacancy rate of 22.4 percent in the third quarter of last year was the ninth-highest of 103 markets tracked by CB Richard Ellis Group Inc., a real estate broker. Those figures don't include many buildings about to open, such as the city's tallest, the 6.6-billion yuan ($966 million) 74-story China World Tower 3.

Empty buildings are sprouting across China as companies with access to some of the $1.4 trillion in new loans last year build skyscrapers. Former Morgan Stanley chief Asia economist Andy Xie and hedge fund manager James Chanos say the country's property market is in a bubble.

"There's a monumental property bubble and fixed-asset investment bubble that China has underway right now," Chanos

said in a Jan. 25 Bloomberg Television interview. "And deflating that gently will be difficult at best."

Third Costliest

Investor concerns have spread beyond real estate. Among 15 major Asian markets, the benchmark Shanghai Composite Index is valued third-highest relative to estimates for this year's earnings, after Japan and India, even after falling 8 percent this year.

A glut of factories in China is "wreaking far-reaching damage on the global economy," stoking trade tensions and raising the risk of bad loans, the European Union Chamber of Commerce in China said in November.

More than 60 percent of investors surveyed by Bloomberg on Jan. 19 said they viewed China as a bubble, and three in 10 said it posed the greatest downside risk. The quarterly poll interviewed a random sample of 873 Bloomberg subscribers and had a margin of error of 3.3 percentage points.

Digesting the debt from a popped property bubble may slash bank lending and drag growth lower for years in an economy that Nomura Holdings Inc., Japan's biggest brokerage, says will provide more than a third of world growth in 2010.

Japanese Comparison

The risks are so great that a decade of little or no growth, as Japan experienced in the 1990s, can't be dismissed, said Patrick Chovanec, an associate professor in the School of Economics and Management at Beijing's Tsinghua University, ranked China's top university by the Times newspaper in London.

The Nikkei 225 Stock Average surged sixfold and commercial property prices in metropolitan Tokyo rose fourfold before the bubble burst in 1990. The Nikkei trades at about a quarter of its December 1989 peak.

"You have state-owned enterprises using borrowed funds from the stimulus bidding up the price of land -- not even desirable plots of land -- in Beijing to astronomical rates," Chovanec said. "At the same time you have 30 percent-plus vacancy rates and slumping rents in commercial property so it's just a case of when you recognize the losses -- or don't."

China's lending surged to 1.39 trillion yuan in January, more than in the previous three months combined. Property prices in 70 cities climbed 9.5 percent from a year earlier, the most in 21 months.

Reasonable Control

Policy makers are starting to rein in the loans that helped fuel the property boom. Banks should "strictly" follow real estate lending policies, the China Banking Regulatory Commission said on its Web site on Jan. 27. It called for banks to "reasonably control" lending growth.

The People's Bank of China today ordered banks to set aside more deposits as reserves for the second time in a month to help cool expansion in lending. The requirement will increase 50 basis points effective Feb. 25, the central bank said on its Web site. The current level is 16 percent for big banks and 14 percent for smaller ones.

"The liquidity bubble last year went to the property market," said Taizo Ishida, San Francisco-based lead manager for the $212-million Matthews Asia Pacific Fund, in a phone

interview. "I was in Shanghai and Shenzhen three weeks ago and the prices were just eye-popping, just really amazing. Generally I'm not buying Chinese stocks."

'Dubai Times 1,000'

Chanos, founder of New York-based Kynikos Associates Ltd., predicted that China could be "Dubai times 100 or 1,000." Real estate prices there have fallen almost 50 percent from their 2008 peak as the emirate struggles under at least $80 billion of debt. The economy may shrink 0.4 percent this year, Shuaa Capital, the biggest U.A.E. investment bank, says.

The commercial property space under construction in China at the end of November was the equivalent of 6,800 Burj Khalifas -- the 160-story Dubai skyscraper that's the world's tallest.

It's difficult to determine how exposed Chinese banks are to real estate debt because loans booked to some state-owned companies as industrial lending may have been used to invest in property, say Xie and Charlene Chu, who analyzes Chinese banks for London-based Fitch Ratings Ltd. in Beijing.

A drop in the property market may be accompanied by a surge in nonperforming loans. The Shanghai office of the banking regulatory commission said on Feb. 4 that a 10 percent fall in property values would triple the ratio of delinquent mortgages there.

Bank Shares

Hong Kong-listed Industrial & Commercial Bank of China Ltd., the world's largest bank by market capitalization, has dropped 13 percent this year. China Construction Bank Corp., the second-largest, has fallen 11 percent. Both are based in Beijing. Hong Kong's benchmark Hang Seng Index has declined 7.3 percent over the same period.

Fund manager Joseph Zeng says he has a contrarian view on China's banks, on the grounds that rising interest rates this year will benefit their net interest margins.

"For us, non-performing loans are not expected to be a big issue until 2013, the peak of the current economic cycle," said Zeng, head of Greenwoods Asset Management Ltd.'s Hong Kong office, in a phone interview. He declined to say what he is buying. Greenwoods has more than $500 million under management.

China has firepower to deal with a crisis. The nation has the world's largest foreign exchange reserves, at $2.4 trillion, and government debt of only about 20 percent of GDP last year, according to the International Monetary Fund. That compares with 85 percent in India and the U.S. and 219 percent in Japan.

Own-Use Excluded

CB Richard Ellis doesn't count empty office buildings bought by banks and insurance companies when calculating vacancy rates, since some of the space is for the owners' use. The Los Angeles-based company said in a report that vacancy rates are starting to fall and rents to rise for the best office buildings as China's fast economic growth buoys demand.

Gross domestic product expanded 10.7 percent in the fourth quarter from a year before, a two-year-high, after the government introduced a $586-billion stimulus package.

"In many cases when you look at these buildings and say, that's never going to be fully occupied, somehow 12 to 18 months later the building is full," said Chris Brooke, CB Richard

Ellis's Beijing-based president and chief executive officer for Asia.

Overcapacity may be looming in manufacturing as well. China's investments in new factories and properties surged 67 percent last year to 15.2 trillion yuan, more than Russia's gross domestic product. Excess steel capacity may have reached about 132 million tons in 2009, more than the 87.5 million tons from Japan, the world's second-biggest producer. The Beijing-based EU Chamber of Commerce report said a "looming deluge" of extra cement capacity is being built.

Balance Sheet Deterioration

While neither Xie nor Chu see nonperforming loan ratios reaching the level of a decade ago, when they made up 40 percent of total lending, they say banks will see deterioration in their balance sheets.

"A lot of people will lose a lot of money, but the banks will probably not go down like in the 1990s," Xie said in a phone interview. "Of course there will be a lot of bad debts. There will be a lot of mortgages gone bad I think."

Rodman displays the slide show to private equity and hedge fund clients brought in by banks such as Goldman Sachs Group Inc. at his office in eastern Beijing.

"China is the only place in the world that despite having more empty buildings than the rest of the world has yet to reflect those valuations on their balance sheet," Rodman said.

Empty Buildings

Gazing south from the building that houses the Beijing headquarters of Goldman Sachs, UBS AG and JPMorgan Chase & Co., one of the first structures in the field of vision is a 17-story office tower at No. 9 Financial Street. Empty.

Farther along are the two 18-story towers of the Bank of Communications Co. complex. Dirt is gathering at the doors and the lobby is now a bicycle parking lot. A spokeswoman for the Shanghai-based lender didn't return phone calls and e-mails.

The supply of office buildings will continue to grow. Jones Lang LaSalle Inc., a Chicago-based real-estate company, estimates that about 1.2 million square meters (12.9 million square feet) of office space in Beijing will come on line this year, adding to the total stock of 9.2 million square meters.

The city government is driving growth regardless of the market. Financial Street Holding Co., whose biggest shareholder is the local municipal district, plans to build 1 million square meters of additional office space starting this year, and is talking to potential clients such as JPMorgan, said Lydia Wang, the company's head of investor relations.

Doubling the CBD

Across town, the district government is seeking to double the size of the city's Central Business District, which already has the highest vacancy rate ever recorded in Beijing. It was 35 percent at the end of 2009, according to Jones Lang LaSalle.

For its part, Beijing-based Financial Street Holdings has "100 percent" of its properties, which include the Ritz Carlton hotel and a shopping mall, rented out, Wang said. The empty buildings along Finance Street don't belong to the company, which is 26.6 percent owned by the district government.

Zhong Rongming, deputy general manager of the Beijing-

based China World Trade Center Co., which built China World Tower 3, said the company is "optimistic about 2010 prospects" given China's accelerating economic growth. He said the new tower will include tenants such as Mitsui & Co. and the Asian Development Bank.

One new addition to Finance Street may give real estate boosters cause for concern. No. 8 Finance Street will be the headquarters for China Huarong Asset Management Corp.

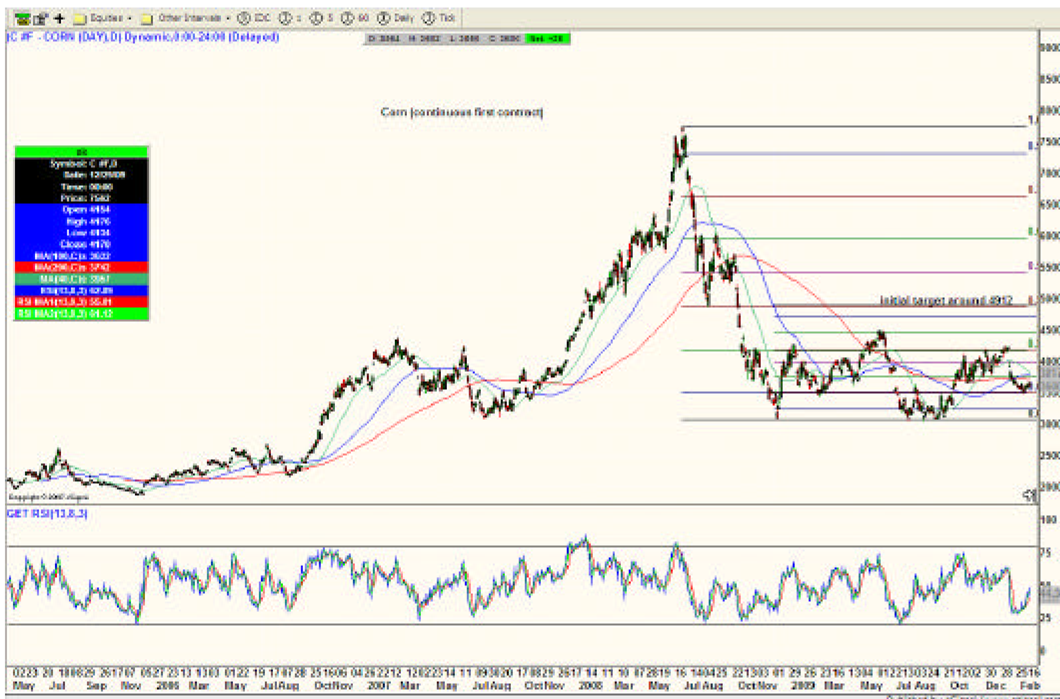
The company's mission: selling bad debt from banks.

Because of these loose lending practices in China and further quantitative easing policies in the West, there has been a rush in the latter part of 2009 to own gold, copper, and other precious and base metals as a store of value. But the precious and base metal markets are arguably now quite "crowded trades." They may work in the end, but not without a few "trap door" heart-palpitating moments along the way as hedge funds dart in and out, and weak-handed investors get flushed out.

At present, the chart below of copper should scare the hell out of anyone still "drinking the Kool-Aid" and staying long of it. In our humble opinion, shorting copper may end up as the single best trade of 2010 – particularly if one were to hedge it by being long a basket of agricultural commodities that as of yet have hardly moved off their lows.

With an ever burgeoning global population -- which also faces increasingly scarce water resources and increasingly erratic weather patterns -- I feel that agricultural markets represent a better potential haven against inflation than chasing precious and base metals markets.

Markets such as corn are certainly starting off far less pricey.



If space permitted, we could go through a long list of individual company chart patterns that appear like good potential shorts to our eye. Most of these revolve around some element of consumer spending and include DAL, DDS, GWW, LULU, LTM, MAT, MLM, PII, POOL, PSS, SKX, TGT, UPS, WFC, and WMS.

Conversely, we are able to find a few companies in the food /water /nuclear/ agricultural area where we can espouse more bullish technical views. These include, in part: CCJ, CDZI, DANOY, LNN, NEOG, OME, SFD, and the ETF WOOD. Even in a bear market, we feel that these stocks have some chance to advance.

In terms of timing, May 18, 2010 is 4.3-months removed from our last minor January 7, 2010 pi cycle high. This would be an idealized time to see perhaps a low in copper and/or equities, with a retest of this low then following later in the summer (with a peak of negativity on or around Arch Crawford's August 1st astro period of acute tension).

If such a "double low" were to transpire, and the 1939 pattern were to hold, one might then expect a sharp rally into the mini pi cycle high date on September 26, 2010. From there, the markets would be expected to go down again into mid-June 2011. I must warn however that pi cycle highs are far more precise than anticipated lows, so it is best to simply anticipate a generally sloppy spring/summer, rather than focus on any specific date for a low.

More will follow on specific equity chart patterns in subsequent letters and web postings once the current February bounce period has clearly come to an end. We currently anticipate such "an end" in the coming days, but need to actually see this turn before we completely rule out other potential paths. Astro folks will of course note that March 1st represents an important "Bradley Turn" date, and it will be interesting to watch the price action around that period.

Some double vibration fractal bands remain up in the 1200-1230 S&P region, and while we do not believe that these index levels will be reached, it is of course possible that the current bubble builds for longer than we currently anticipate. If we were to immediately decline into the Bradley date on March 1st, and then hold on the S&P around 1086, this might be oddly a more bullish pattern set-up in the short-term.

As one last note, 15 out of the past 16 Mondays (or the first day of the week if Monday was a holiday) have been up days. To publish this on Sunday, February 21st in front of yet another potential Monday jam-fest, is thus a tad dangerous. Maybe the resumption of trading in China on Feb 22nd after their New Year celebration will bring something different this Monday – particularly as they absorb their recent 50 bp reserve requirement increase. If so, we will take a down day on Monday as an encouraging sign that the recent rally has truly started to lose its sea-legs. Stay tuned.

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