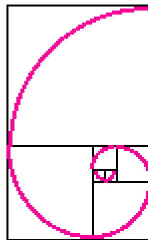

Sand Spring Advisors LLC

A View into 2008

by,

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"Will there be a 2008 recession in the U.S. or not?" – such is the question that we hear being posed all the time these days.

If you believe in "no recession," then most in this camp would in a "knee-jerk" fashion buy stocks, sell bonds, and stay long commodities. If you believe that a recession will arrive, then the obvious response would be to sell stocks, buy bonds, and get out of commodities.

Our view of 2008 is that a recession will slowly start, but that it will take longer to arrive than one might expect. Everything these days seems to take longer to arrive and really matter than one would expect. In the meantime, there should still be enough supply-side tightness in the oil market (let that read not enough demand destruction) that oil continues to move higher, and increased stagflation results. The higher oil goes, the more pressure there will be on bonds. 4.1% hardly seems like the right price for U.S. government debt. Remaining long oil and increasing shorts on U.S. Treasury bonds could be the best combination of positions across 2008, with equities and the U.S. dollar kind of ending up stuck in the middle.

The key pi cycle dates of 2008-2009 are:

July 31-Aug 1, 2008 – a date we now view as a probable equity market low;
April 19-20, 2009 – a probable equity market bounce high

After April 2009 bounce high, the next major pi cycle low is due on or about June 13, 2011. The period between April 2009 and June 2011 should be the really nasty period equivalent to the recessionary period of 2001-2002. In front of this, 2008 into early 2009 should be more of a "hang period" with some false starts of sudden volatility, but perhaps an overall muted period of cooling off.

As a matter of background, 2008 in the Chinese calendar is the Year of the Rat – a water sign that tends to cool off the overly ebullient typical fire of the markets. There at times may be a quiet calm, but also a very poor "sloshy" foundation underneath this calm. It will feel like a trap door could open at any time, but often it will not.

As recently pointed out by many financial astrologers, including Manfred Zimmel at www.Anamita.at, astrologically, from 1995-2007, Pluto (the planet controlling death and new beginnings) was in Sagittarius – a sign of happiness, expansion, optimism, growth, and

abundance, with particular importance to the world of the media. It was over this period that the Internet became so important and real estate markets turned red hot. But from late January 2008 through to 2024, Pluto will be in Capricorn – a more cautious, defensive, stubborn, and pessimistic sign that may bring increased contraction and scarcity, with increased restrictions and price fixing by the government.

2007-2009 also marks a period where Saturn (leadership) is in Virgo (restraint, discipline, caution, organization, conservatism). The last 1978-1980 period of Saturn in Virgo saw the rise to power of Ronald Reagan and Margaret Thatcher as reformers of government, but it also marked a period where inflation initially ran out of control (as gold ran up to $850 and the world faced the Iranian oil crisis across 1978-1980). I think we can already taste a bit of the same type of environment across 2008-2009.

And then of course we have the Olympics in Beijing in August, and the U.S. elections in early November. The former is likely to bring feelings of a new global community (new highs in the FXI ETF up at Fibonacci target 230-235?). The latter U.S. election period is likely to bring fear of change and transition to new operating norms – but with some stultification in the markets in front of the elections until the exact path of the new leadership is more fully defined.

At present, there is of course a wide open field of candidates for the U.S. Presidency. Our view on the elections in a nutshell is: pity the poor candidate who actually wins. That person – whoever it is -- will step into a "left punch" of economic meltdown across 2009-2011 and likely be blamed for it. Please don't call us irrationally pessimistic or overly fatalistic. We simply believe that the underlying established pi cycle rhythms are more powerful than the new policies of any individual. And how ironic it would be to move from one unpopular Republican President to an even less popular Democratic President.

So with the above few paragraphs providing an overview of our expectations, let us delve into some specific chart patterns.

For awhile now, many readers know that we have been following the 1942-1947 chart pattern as a possible analog for the years 2002 through 2007-2008. Missing from this analog at present (to make it really work) would be one last swift early-2008 equity market decline lower to around the 1305-1350 region of the S&P. We would not be surprised to see this happen with a quick "wush" across January 2008. But what initially could seem like Armageddon would likely then dissolve in a range-trading type of an affair, with an upward bias subsequently developing – particularly beyond July 31, 2008.

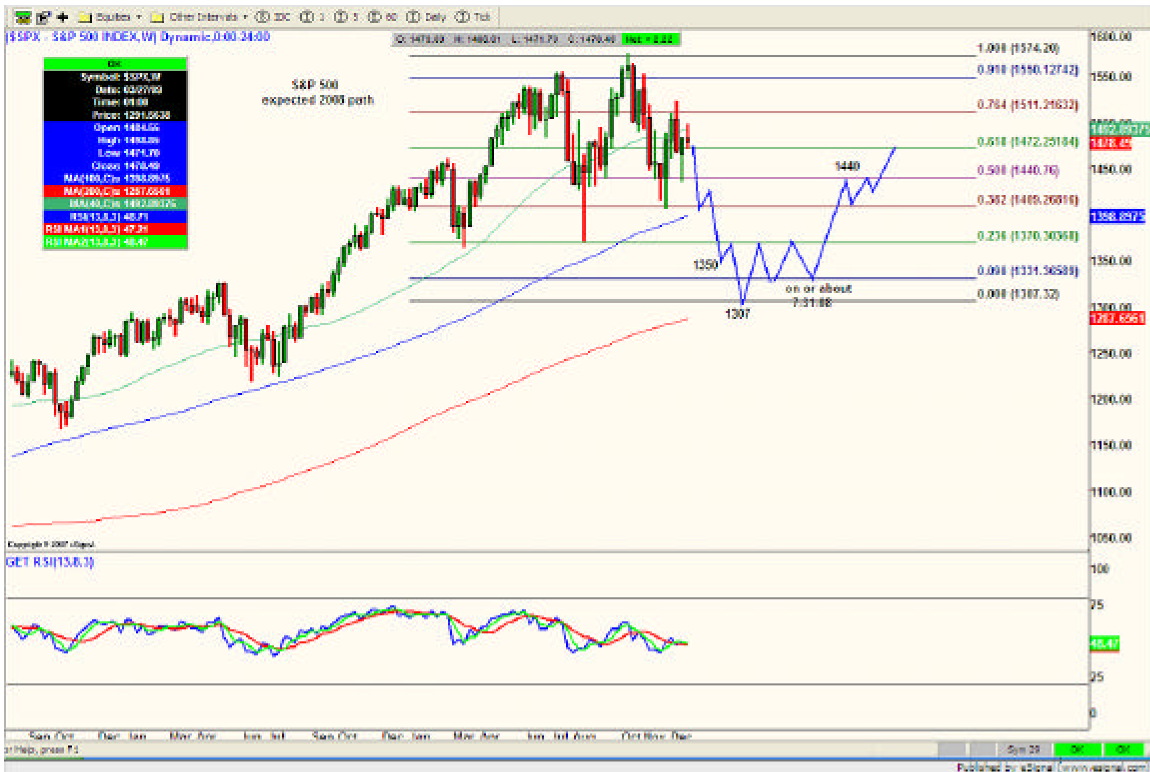
Peter Eliades, writing back in 1978, pointed out the following decennial pattern in years ending in "8":

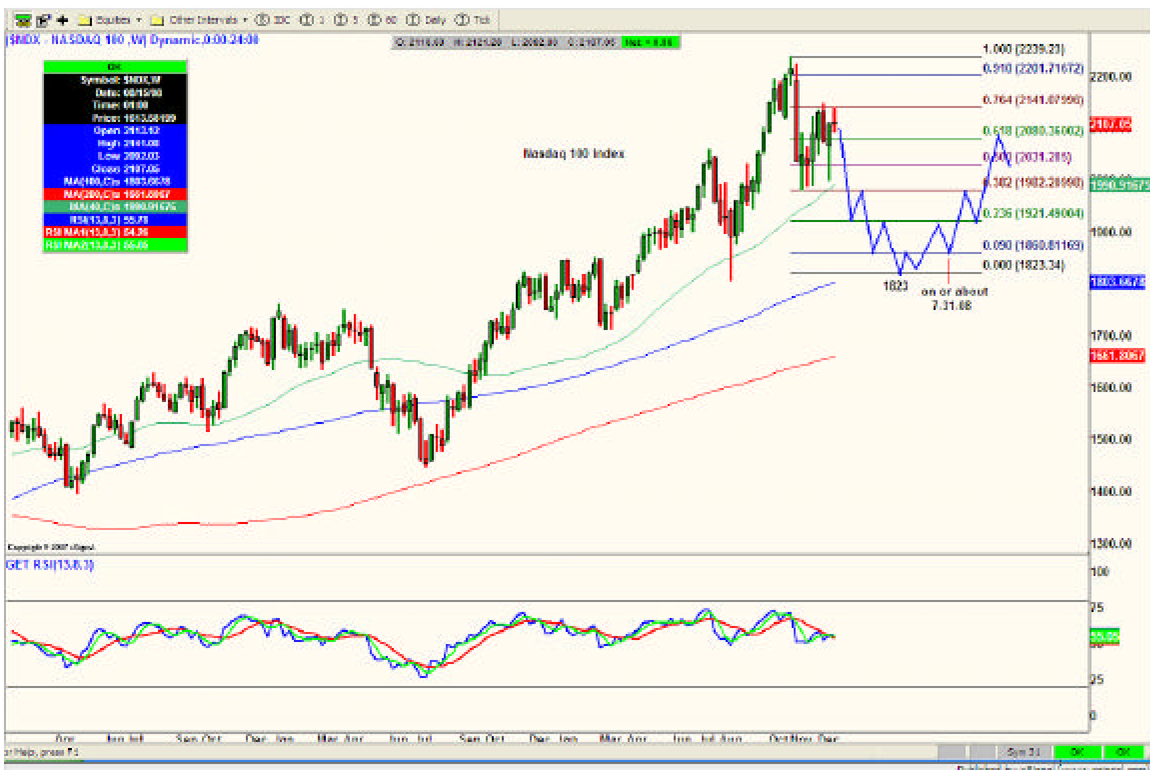
> "There has been a consistent decennial pattern throughout this century occurring in years ending in eight. The record is astounding. These are the figures for the past 80 years. In each of these years bottoms were reached in the first quarter of the year and were followed by dynamic rallies before the end of the year. The rallies in many cases continued after the completion of the year ending in eight, but we are tabulating the results in percentage moves from the bottom to the ensuing top that occurred within that year alone: 1968 (22%), 1958 (33%), 1948 (18%), 1938 (39%), 1928 (58%), 1918 (23%), 1908 (67%), 1898 (49%). This pattern continues back to 1878 ..."

Writing further in 2007, Eliades goes on to state:

> "We were aware of this decennial pattern and decided to search for a longer pattern which included these 10 year periods. We noted that every 30 years a market rally began whose beginning marked a low spot not to be returned to for at least 11 years. It always began within three months of the first month of the 8 year."

While we do not expect the 2008 lows to herald a new bull market that will last 11 years, we do expect that from lower levels, a tradable rally will exist. But first we need to attain the lower 1305-1350 region on the S&P. Maybe the 2008 year will end up looking about as follows in terms of the S&P 500 and Nasdaq 100 price charts:





In terms of tradable "inverse ETFs", we see the following targets for QID (double inverse of Nasdaq), SKF (double inverse of financials), and SDS (double inverse of S&P 500):

Meanwhile, we see the Crude chart as follows for 2008:

And longer-term, this is where we see 30-year bond yields headed:

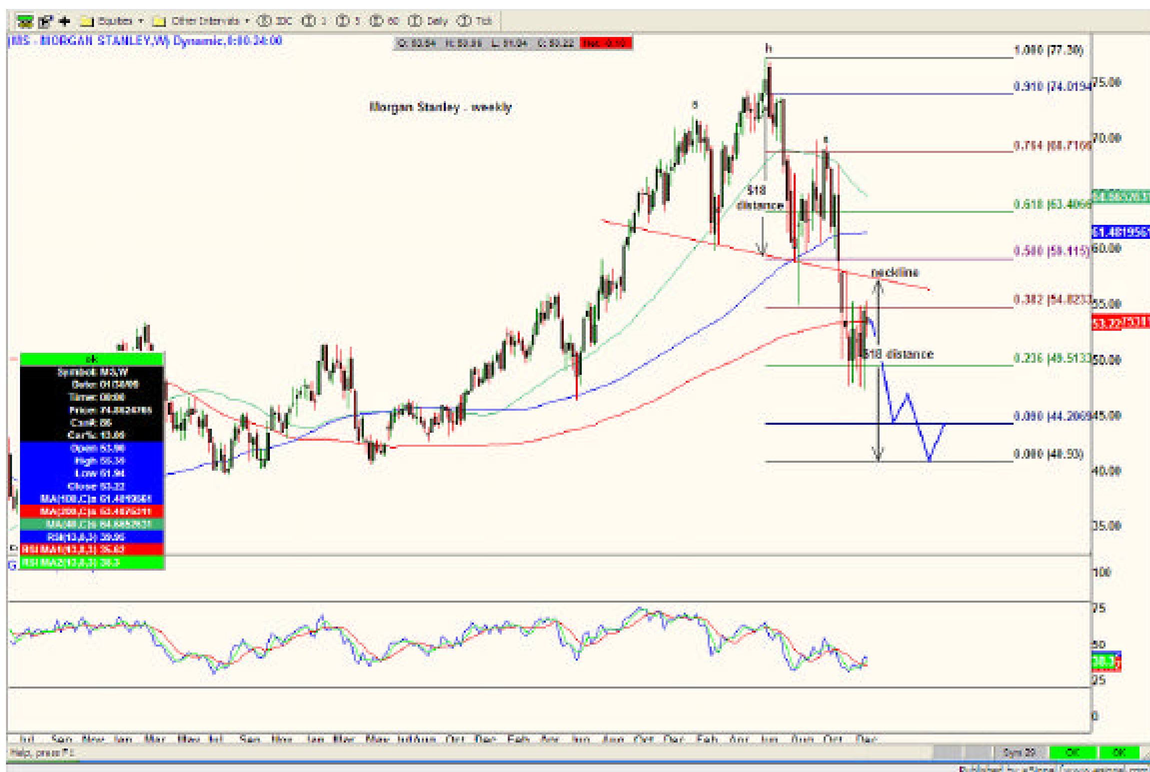
Our view of long-bonds slowly losing their appeal and rising in yield is arguably the most controversial and currently elusive of our views. But fundamentally we see the following structural imbalances across the world:

- U.S. rates have been kept artificially too low for too long (courtesy of Greenspan/Bernanke and overly accommodative foreign buyers of our debt).

- Because U.S. rates have been kept artificially low for too long, and the U.S. runs a consistent twin spending deficit, a weakening dollar has been the effective “shock absorber” under constant downside pressure – but to the point now where the lack of purchasing power of the dollar abroad has been stretched to silly levels. At this point, dollar weakness will have a hard time stretching further, so some of the global imbalances will need to be felt in other ways and impact other markets – namely a back-up in U.S. Treasury yields to more attractive levels (courtesy basically of a bond buyers strike).

- As rates normalize to a more appropriate higher level, the dollar may actually rally, but higher rates and a higher dollar will not be good for U.S. corporate profitability. Stocks will be under pressure. 2008-2011 in general will be somewhat dour years for U.S. equity investing. It will be a period where the “Piper will finally be paid” for two decades of past excesses. At the end of this period, America’s psyche as a nation may be broken, and its past geopolitical dominance shifted somewhat to the Chinese.

Within such an environment, and while we previously cautioned readers to "rotationally" start thinking more about potential tech shorts than financial shorts, we still believe that financial stocks will remain under pressure. $21 is a specific downside Fibonacci target that we have for Citibank, and equivalent targets for Morgan Stanley and Lehman Brothers come in somewhere near $40 and $38 respectively.



Indeed, think of the above picture of LEH in terms of yet another analog – 1994 bonds (see below). The current upward sloping wedge formation on LEH can be seen as a 4th wave, with a 5th wave of real fear and loathing still to follow.

Or consider the Fannie Mae weekly “coil” on its highs back in 2000 as a possible analog formation for what may start to transpire with Goldman Sachs on a daily basis in 2008. Will it be a step-and-stumble lower for GS from here? We think so.

As always, our views are simply our own personal opinions, and are not meant as direct investment advice. Consult your own Registered Investment Advisor before committing capital to any positions mentioned here.

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