Global Report –June 2010

UK

Europe

US

Japan

Emerging Markets

Bonds

Commodities

Currencies

June 2010

World Investment Strategy

IRC INVESTMENT RESEARCH OF CAMBRIDGE

Introduction

Investment Research of Cambridge was established in 1945 to specialise in technically-based research of the financial and commodity markets. The company has built up an international reputation for its expertise in predicting the trend in global markets and individual stocks.

Contents

World Investment Strategy	2
The World at a glance	4
United Kingdom	7
Europe ex UK	8
United States	10
Canada	11
South Africa	12
Japan	13
India	14
Pacific ex Japan	15
Emerging markets	17
Bonds	19
Commodities	21
Currencies	23
Road maps	25

■ Source of data for charts: Investment Research of Cambridge, Q-Data, Alpha Terminal, Thomson Reuters

World Investment Strategy

"It is always darkest just before the dawn". Just as we give up hope there will appear the first cautious flecks of light, then slowly the outlook will brighten. This improvement is welcome but should not be greeted too enthusiastically.

Markets are now in a downtrend and this will in fact last until October. However the setback will not go in a straight line, but rather in moves of two steps down and one step up. There will therefore be rallies.

There should, in fact, be one really strong and sustainable rally lasting between four and six weeks. During this period being short will be painful, but going long is also not recommended.

In an average year the market rises until late May, when we sell and go away. There is a mid-summer rally that starts in July and goes into August. Then the wobbles start and September is reliably the worst month. The actual low comes in October, but this month usually ends with the start of a strong rebound.

This average pattern can get slightly bent out of shape and this year it became obvious that the rise was not going to last until late May. In practice, the 19th of April marked the peak of what was an exhausted move. As the fall started earlier than usual, the mid-summer rally will also probably begin a bit early.

The prediction is that the climactic fall in almost all world markets will go further, taking them to oversold levels. Between the 10th and 20th of June will probably be the start of the mid-summer rally. Use that window of opportunity to close short trades.

Except for really short term traders, we do not advise going long. The absolute top priority for long term investors is to preserve capital. Ignore the rally and make sure you are ready to buy again in October.

There will be many who take the rally phase as evidence that the old bull move is alive and well and is now resuming. They are likely to be wrong and will learn an expensive lesson.

The notion that the global economy is in great shape and in the midst of a self sustainable V-shaped rally is a delusion. We are more likely to see a flying saucer.

The global economy is deep in debt, to the point where servicing the interest takes it ever further down. Tax rates are going to rise dramatically even though the actual amount of tax raised will have the flight path of a brick over a cliff edge.

The only way out of this mess is to be prudent, frugal, thrifty and shrewd. Work hard, save hard, cut out any wasteful expenditure, and, above all else, do not do anything stupid.

No market will be immune from this setback. Even our favourite areas such as India, Brazil, and gold will fall back. We have already thought it prudent to reduce exposure. We fully intend to go back to being overweight of these markets again, but not for at least three months and possibly longer. Until then you have got to have money in the bank.

The markets in secular uptrend will probably bottom first. There is already a trend in the flow of funds from the west to the orient. This story is going to run and run.

The ones that are safest to buy on the fall have strong demographics and reasonable valuations. It is quite possible that the fall during the next few months will take the Chinese market back down to levels where it will merit going back on this list.

We also think that the resource-based markets will follow a similar pattern, but not yet. The chart of the commodity index clearly shows a top in place and a further fall is needed. We must have patience.

The good news is that we do not expect the entire world to have a depression. The growth in the emerging markets will prevent that. However the mature giants of the western world will have a double dip in 2011. Count on it.

Summary: world market overview

Our caution of the past two months has paid off. The rally that had started in March 2009 has officially ended. It is broken.

Remember the story of Humpty Dumpty who sat on a wall? Once he was broken, all the King's horses and all the King's men could never put Humpty back together again.

Bear markets are, however, cunning brutes, they are likely to conjure the idea that he can be mended. He is only bruised but not dead. What will signal this is a rally.

Our road map predicts that there will be a mid-summer rally. In practice it is likely to come early. It is in fact imminent. It is likely to retrace a Fibonnacci move of 38.2% of the recent falls - and it might even go a bit further.

The strongest markets are only just below their 200-day moving averages. The rally will inevitably put them back above those levels. They will, therefore, still fulfil the definition of a bull market. This will tempt in many investors. Strange women from Rosy Scenario to Goldilocks will appear in the chorus line. Politicians will especially enjoy the show.

Unfortunately it is a tragedy, you will not like the ending. It is a rubbish play. Do not even go and watch it, or leave early. Get to the front of the taxi line. Go home and stay there. It is going to get rough on the streets outside.

We do not mind watching these events on the News at Ten if it is in Greece or Spain, but unfortunately it is much closer to home.

There is nowhere to run to. When people need money they will sell anything and everything. Assets that have in the past been non-correlated, will move in perfect harmony.

This is likely to be a case of less is more. Do not worry that you are getting no return on your money; at least you are preserving your capital. And eventually you will be able to buy more with it.

Even the best markets will fall back to some extent. The summer rally is a chance to sell.

We have already sold out of Brazil and India despite our long term optimism. We have even sold our gold holding. We fully intend to buy back these assets but not for a while.

Our best guess is that the summer rally will end in late July. August will be rocky and September worse. The buying low is likely to be in October.

There is one thing you need to know, and that is we are not always right. But just now it does seem wise to be prudent. Survival is the name of the game.

The silly season is upon us. Do not think about investing, instead concentrate on Wimbledon, Henley, Ascot, Cowes and holidays.

The World at a glance

Major markets

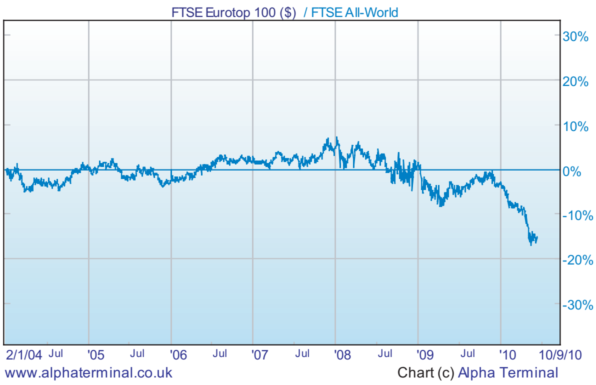
US relative to world: currency adjusted

The US is in better shape than the other mature markets of the western world. That means although it is sick, it is not dying. It is in a relative uptrend to the global index. On our ranking table it is in the strong category, but even so it has broken the uptrend that had been in place since March 2009. The correction tends to have a fall-rally-rest-of-fall shape to it. The mid-summer rally is due soon. We are running early this year. Aim to be out by late July, from then on things get tough again.

UK relative to world: currency adjusted

The UK is relatively good within the context of Europe. Only Germany is above it in the ranking table. But how good is that when they are both in the weak group? Being stronger than Greece is not that hard to do. The UK market is in a relative downtrend to the global index but not a steep one. At least now the Conservative-Liberal coalition is doing the right things to get us out of debt. It will work, but slowly. As David Cameron has warned, it will involve pain.

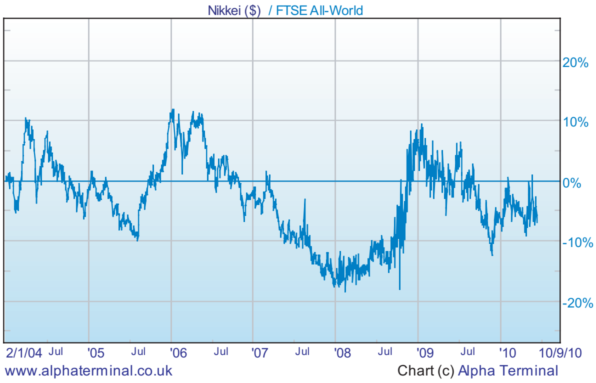
Europe relative to world: currency adjusted



This is horrible. The actual and relative trends are steeply negative. The entire lowest category of the ranking table is composed of European markets. Only Denmark, Switzerland, and Germany are above this level. There is at present no sign of a reversal of this state of affairs. Avoid.

The world at a glance

Japan relative to world: currency adjusted

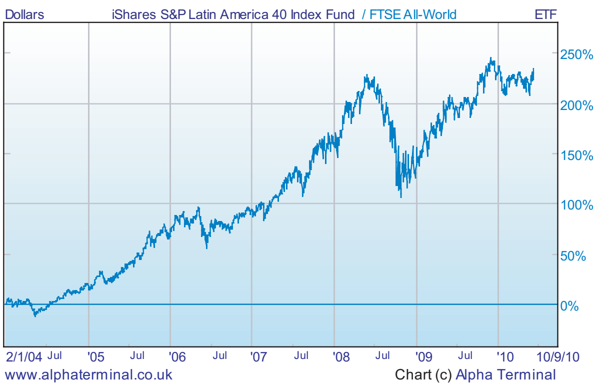


- This market had been showing some relative strength for a while. It even looked like a possible bottom. But forget about it now as it is breaking back down again. As a result of its recent strength, Japan is still in the strong part of the ranking table, but it is slipping down the league. This is redeemable, but the only way it will happen is if the yen weakens. Investors would then win on the swings but lose on the roundabouts.

Pacific ex Japan relative to world: currency adjusted

- This is still the best except that the major market here – China – is weak. On balance, we think it is worth reducing exposure and taking some risk off the table. If we get a mid- summer rally, as seems probable, then sell more into the rise. The worst part of the overall correction phase will come from August onwards. When the time comes to move back into equities again, this region is likely to see heavy buying. Flows of funds support the idea that economic power is shifting from the west to the orient.

Latin America relative to world: currency adjusted



- This is the second best area and, indeed, looks similar to the Pacific region. In nominal terms these markets will be falling but around strong long term secular uptrends. However, they are also high beta which means that in any given month they can drop more than the markets in secular downtrend. The net result will be a volatile plateau at high levels. Eventually they should break out upwards again.

Global stock markets ranked by quintiles in dollars

Country	Quintile	Above 25D Moving Average	Above 200D Moving Average	Upward Sloping 25D SMA?	Percentage Change (US $) % 1 MONTH	AVG	3 MONTH	AVG	12 MONTH	AVG
Philippines	++	×	✓	×	1.1		4.7		30.3	
Chile	++	×	✓	×	0.2		-4.6		22.7	
Colombia	++	✓	✓	×	5.6		0.1		36.3	
Thailand	++	×	✓	×	-2.1		4.9		31.8	
Indonesia	++	×	✓	×	-0.3		6.5		42.2	
Malaysia	++	×	✓	×	-5.2		-0.1		25.5	
Canada	++	×	×	×	-2.4		-6.8		14.3	
India	++	×	×	×	-3.4	-0.8	-4.4	0.0	11.2	26.8
Singapore	+	×	×	×	-3.9		-2.7		17.6	
Venezuela	+	✓	×	✓	2.4		11.1		-26.1	
Argentina	+	×	×	×	-0.4		-7.3		26.3	
Mexico	+	×	×	×	-1.8		-7.3		26.5	
Turkey	+	×	×	×	0.9		-0.9		49.6	
Hong Kong	+	×	×	×	-3.0		-7.3		3.0	
United States	+	×	×	×	-5.4		-7.8		11.7	
Japan	+	×	×	×	-8.7	-2.5	-5.5	-3.4	6.9	14.4
Peru	0	×	×	×	-9.0		-6.8		-0.2	
Russian Federat	0	×	×	×	-2.1		-11.1		16.6	
South Africa	0	×	×	×	-2.5		-10.7		16.1	
Taiwan	0	×	×	×	-7.5		-8.1		6.3	
Denmark	0	×	×	×	-0.9		-9.2		11.0	
South Korea	0	×	×	×	-7.0		-7.5		18.2	
Brazil	0	×	×	×	-3.7		-15.5		20.1	
Israel	0	×	×	×	-6.9	-5.0	-14.6	-10.4	26.4	14.3
Germany	-	×	×	×	-2.6		-11.9		-1.0	
Switzerland	-	×	×	×	-2.9		-14.9		8.7	
United Kingdom	-	×	×	×	-2.3		-13.1		3.4	
Sweden	-	×	×	×	-0.9		-13.8		22.0	
Egypt	-	×	×	×	-7.6		-10.1		-0.4	
China	-	×	×	×	-6.0		-17.0		15.7	
Australia	-	×	×	×	-10.9		-18.2		11.6	
Netherlands	-	×	×	×	-4.1	-4.7	-17.8	-14.6	1.3	7.7
Belgium	--	×	×	×	-1.0		-19.0		-0.8	
Czech Republic	--	×	×	×	-9.1		-16.9		3.4	
Poland	--	×	×	×	-5.4		-19.0		18.6	
France	--	×	×	×	-5.1		-23.5		-12.9	
Hungary	--	×	×	×	-7.7		-21.6		16.8	
Austria	--	×	×	×	-8.8		-20.2		-11.3	
Italy	--	×	×	×	-6.8		-26.7		-21.3	
Spain	--	×	×	×	-8.3	-6.5	-30.4	-22.2	-21.6	-3.6

Ranking and data in US Dollars

United Kingdom

It is worse than we thought

The Conservatives and Liberals are going to give this coalition their very best shot. All controversial issues will be pushed to the back burner. The top priority is to cut expenditure and start the long process of getting out of debt. It will be painful.

Now in office and having access to the real data they find that things are worse than they had expected. Of course they would say that wouldn't they? They may as well blame the outgoing Labour party for as much as possible.

The trouble is, this is not the usual political knockabout. There honestly will need to be brutal cuts. People will not enjoy this, but they know it is coming and they did vote for it. It may well turn out that only a coalition could get these measures through. The unpopularity can be shared.

For the FTSE index the top was on 16th April at 5833. Then there was a fall of 13%. After a rally the next fall was 9.8%. Theory says there has to be one more leg down before the mid-summer rally starts, and it will be between 10% and 13%. This gives downside targets of between 4500 and 4700.

This leg seems to have already started and on present form the target zone will be achieved by the middle of the month.

The mid-summer rally will then go back up again to probably no more than 5300. It may do this slowly over a period of four to six weeks. Bear market rallies often fool people by being more complex than expected. Even so, we expect another fall again to the real lows in October.

The Prime Minister is going to give a long speech to prepare the ground and the next budget will reveal the details. The market will discount these. Then the rally can begin. We would use this as a selling opportunity.

We see nothing wrong with sitting on cash for a while, even though it gives no return. We will learn to see this as a good result.

FTSE 100 index

FTSE 100 index relative to world

Europe ex UK

It is an ill wind

Most strong winds are good for somebody, even if the benefit is not obvious at first glance.

German exports are fiercely competitive at any time, even when the currency is strong and they seem expensive. Give them an extremely weak currency and they have an unfair advantage.

This is all very well but the fact remains there are no European markets above neutral in our ranking table.

Germany is the best performer, followed by Switzerland. This shows that investors are bolting back to safe havens as far as they can. It is still a risk-off trade.

Working up from the bottom of the table it goes Spain, Italy, Austria, Hungary and France. No surprises here.

The really big move has been in the euro. It always seemed likely that it would drop below $1.20. There is significant support between $1.16 and $1.17 and it would be surprising if it broke below this area in the short term without a fight. At these levels the Germans are on a batsman's wicket and will hit big scores.

We may well get a snap-back rally to $1.34. It would be painful to be short during this move. There is a good chance that this technical bounce could occur very soon.

The stock markets themselves will also have a rally but the ones at the bottom of the table are not good buys.

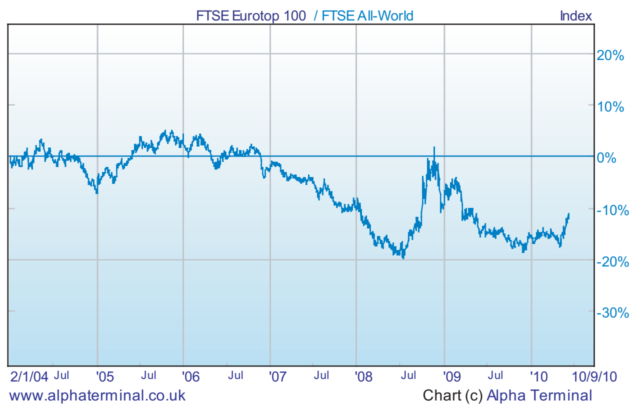
The rally is most likely to be driven by traders closing short sales.

The bottom line is that, even with a rally in both the currency and the markets, the problems remain. Not only have they not been cured they have hardly been addressed.

On balance we can see a rally coming but regard it as a selling opportunity. Preservation of capital is still the top priority.

European equities

European equities relative to world



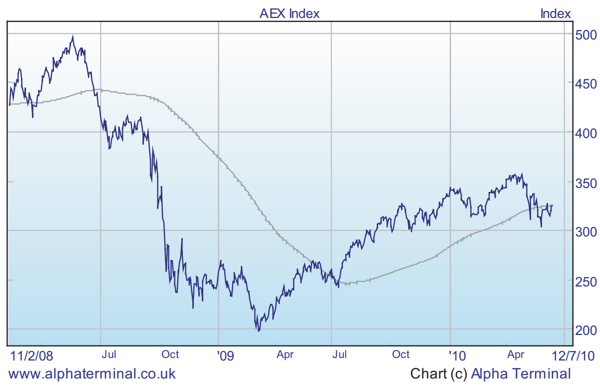
Europe ex UK

France

Germany

Switzerland

Netherlands



Scandinavia

Spain

United States

Rally round the flag

When the S&P index topped out on 23rd April it plunged 12%. Then it rallied and the second fall was 11%. Wave theory expects one more drop, giving a target of about 1000. We should then be ready for the real summer rally. This might get back up to 1150.

These days volatility is so high that the normal 38.2% bounce can be exceeded. Many of the normal rules of thumb are being stretched.

The entire pattern is running early this year. The rally phase is expected to end by late July or very early August. Then the big drop comes to October.

At the end of July there will be many people saying that the bull move is resuming, we have just had a wobble but everything is back on track now. Their arguments will seem convincing. We think they are likely to be proved wrong.

It may well take courage to sell at the top of the rise. We are not even going to buy for the bounce. We think an important top is in place. The tactic of buying bear rallies goes against our strategy of preserving wealth. Capturing the rally is hard to do, too hard for us to try.

The dollar trade-weighted index has been strong recently. It has however almost completed the rise to important overhead resistance. We think it will top out between 91 and 93. Then it will be a sell.

With the risk that we could lose on both the stocks and the currency, we do not wish to try and be too clever. It is certainly true that the US market is showing relative strength. It just scrapes into the strong category. Only Canada is above it, but that means that its safe haven status is almost fully discounted.

Valuation arguments are not compelling, and the debt mountain is still there. This is a weak year in the Presidential cycle and the market is likely to make a buyable low, later and much lower than present levels. We must be patient and cautious. Patriots can rally round the flag but we prefer to stand aside.

S&P 500

Dow Jones Industrial Average

Canada

Waiting for Godo

We like this market from a long term point of view. It is in a secular uptrend and we think we will profit both by owning the currency and the stock market. But as the Irishman said, "if you want to make that journey you shouldn't start from here."

No market is immune to what is going on in the wider world. When they fall, they will all go down together. This one will hold up relatively well, but it will still give a lower and later entry point. In an absolute returns world it is still not a buy.

The TSX Index topped out on 27th April at 12,320. It has had two setbacks of 7%. Roughly a half of that which other western markets have endured. Given that there should be a third leg down, that still leaves 11,000 as the strong support level.

The mid-summer rally could easily take this index back above its still rising 200-day moving average. Consequently, the market would, technically, remain in bull phase. It would be one of the few markets that does so.

On our ranking table it is in the strongest category. It is the best of the resource-based markets. South Africa has fallen back to neutral and the Australians have shot themselves in the foot (they may have to get a new prime minister).

In the long term, we are very bullish about the demand for food and therefore fertilizer. The Canadians are, for example, by far the biggest players in the potash market

We also believe that the use of natural gas as an energy source will rise. It is such a cheap, clean form of fuel that this is inevitable. Canada is very rich in gas.

As a result of the problems in the Gulf of Mexico, there will be a go-slow on tar sands development, but in the end even this should pay off well.

On the currency front we believe that, once the rally in the US dollar is complete and Helicopter Ben's printing press starts running again, owning the Canadian dollar will be a winning trade. It will go to a substantial premium against the US dollar and maintain the differential.

We do not want to be out of this market for long but, again, patience is required with October probably the best buying window.

Canada

Canada relative to world

South Africa

It's not quite time

The 2010 South Africa World cup slogan is Ke Nako which means "it's time". We really like this market, but do not feel it is quite the right time to buy into it. It is having a well earned and indeed overdue correction, or consolidation phase. There will come a more appropriate moment to invest in it for the long term.

The patterns are in fact similar to those of Canada but not quite as strong. The JSE Index is now in the middle of the table, but still comfortably above Australia.

The Reuters Commodity index has rolled over into a downtrend. It is likely to fall back at least 38.2% of the previous rise. We are sure it will become a strong buy again but, whilst the correction is under way, all the constituents including gold will fall as well.

When global investors need money they will sell whatever they can to raise it and that includes strong markets like South Africa. Even allowing for a mid-summer rally, by October all markets will be lower than they are now. This will probably be by a larger margin than many currently expect.

The JSE topped out at 29,565 on 15th April and dropped initially by 10%. After a rally the next fall was the same size. Strong support came in at 26,000.

Although the theory indicates there is one more fall to come, we doubt the index will go below 25,000, and may just retest 26,000.

The mid-summer rally could then cause a bounce to around 28,000. It is, however, unlikely to make a new high.

The August to October fall might well test 24,000 and at this point (and time) we would be interested in re-investing in this market.

JSE All-Share

JSE All-Share relative to world

Japan

It is going down

This market is showing some relative strength in that it has now risen from the weak part of the ranking table to the lowest part of the strong category. In actual price terms it is still going down.

Not only is there no clear buying signal yet, it is still in downtrend. There is support indicated at 9,000 for the Nikkei Index, but it is doubtful whether this will hold.

A much better support line is at 8,650, which is a 61.8% retracement of the rise from the March 2009 lows.

It may well be in the great scheme of things that some sort of massive base pattern is forming, and has been doing so since 2009, but all we can say is that at the moment the chart looks no more convincing that it did in 2003.

The 2003 lows may have to be revisited again to confirm the bottom to the secular downtrend. In round numbers we are waiting for 7000.

Even the currency is confusing. The old days of the carry trade are over, we have to wait for new parameters to become established.

We view the yen as neutral in the range Y90 to Y94. We would be required to follow any break outside these levels. The slopes of the moving average are moving in such a way that suggests a yen sell signal will be given but it has not happened yet.

If the yen breaks through Y94, a period of profound yen weakness is likely to ensue. This would help the export stocks but, if we bought these, we would need to cover the currency exposure.

At present, it is still premature to buy into this market. There are likely to be buy signals triggered in many other markets before one is given in Japan.

Nikkei 225

TOPIX

India

Partial inoculation

There is a virulent flu virus going around and most people are coming down with a nasty bout of it. Some have a good immune systems while others have been inoculated with a wonder-drug. These will dampen the symptoms but you still feel terrible for a while. A similar effect will be seen in global equity markets.

Even India, our favourite long term investment market, will fall back a bit between now and October. We do not need to be fully exposed while this occurs.

If we thought we could call it exactly, we would sell out completely and buy back on the lows. In practice, we know we will probably not be that clever. It is difficult to finesse bear markets.

We have, therefore, halved the position. We aim to re-establish an overweight position in October. If we are wrong, and the market just goes straight up from here, we will buy back at the higher level and will regard the loss as rather like of paying an insurance premium. It is well worth it for the peace of mind.

The Sensex index has fallen back from 18,000 and has been as low as 16,000. There is considerable support at this level - it has held every time it has been tested since August last year.

Although the index has subsequently rallied, it is still below its 200-day moving average and could fall back to around 14,500 later in the year. This would be a 38.2% Fibonacci retracement of the rise from March 2009. Such a setback would still keep the index in a secular uptrend.

If a base develops around 14,500 we would expect to go overweight again.

It is still the case that India is not linked to the west by trade to anything like the extent that China is. The language, the demographics and the country's ability to feed itself are all factors that make it a preferred market.

Latest flow of funds figures strongly support the idea that long term money is moving from the west to the east. In spite of all the marketing hype surrounding China, we still think that, ultimately, it will be India that will outperform out of the two and will also be less risky.

India

India relative to world

Pacific ex Japan

Rollercoaster ride

When you are suffering from a dose of flu, going for a ride on a rollercoaster is not a good idea. We should stop our children doing this for their own good, even if they do not see it that way at the time.

High beta markets can be brutal in both directions and the ride so rough that few have the nerve to stay on for the long term. We cannot see the point of experiencing a white knuckle ride and have always believed in "Selling to the sleep point."

The big market of the region is China. The Shanghai Composite index has fallen 22% since mid-April.

On our ranking table it has dropped into the weak category.

The all-time high was in 2007 and the fall from there is 60%. This does not square with the marketing hype. The truth is that the market got out of step with its own economic development around the time of the Olympics. A massive correction was needed to get back into step. The chart reveals that if the Shanghai index gets back to between 2,100 and 2,200 then this might have been accomplished

If we see these levels in October time, we would expect this market to pick up again in step with India and Brazil.

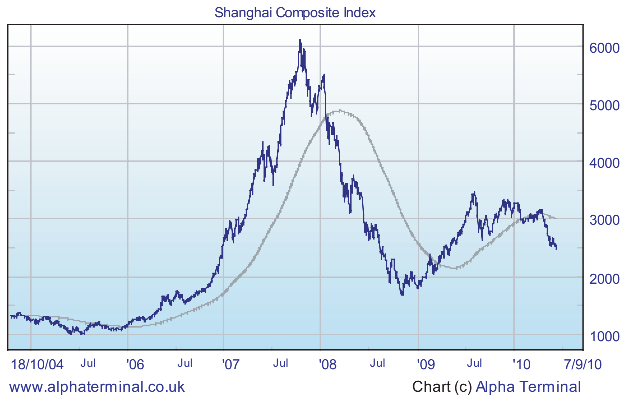
Australia has broken down and is now in the weak part of our ranking table. Notably, it is the weakest resource-based market. This is largely the fault of the Prime Minister. He may well lose his job soon.

We do not really trust the situation in Korea nor for that matter in Thailand or Taiwan. But reading geopolitical risks is a different skill set. What the charts are saying is stand back from these markets at the moment.

The time will come to buy but in the meantime we do not want to handle the volatility – it could make us rather queasy.

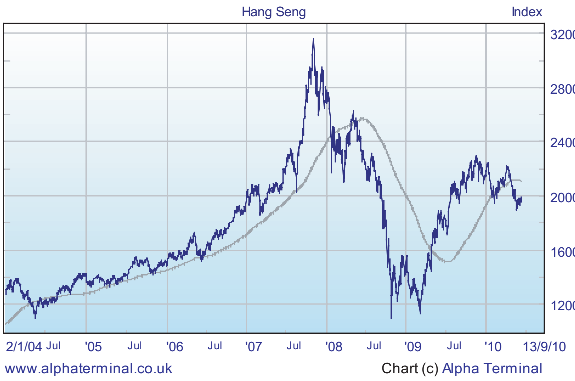
Australia

China



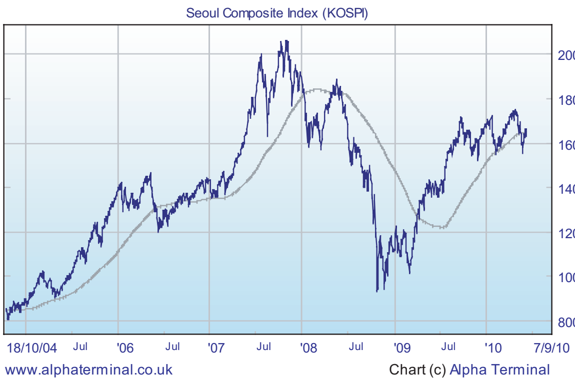
Pacific ex Japan

Hong Kong



India

South Korea



Malaysia

Taiwan

Thailand

Emerging markets

Same difference

By now the story is familiar. Nobody escapes a dose of the bug. Even the good guys go down.

Along with India, Brazil had been our largest holding, but we have now sold out. The IBOV index dropped 20% from the April high and is now well below the 200-day moving average.

It is still in secular uptrend, but it is also high beta. The buying low in October could be another 20% from current levels.

Mexico is similar to Brazil. We like it long term, but it can have more of a setback in the short term. The potential for the pullback is sufficiently large to warrant being out of these markets for now.

Using the normal Fibonacci retracement rules, the next setback could be of the order of 20%.

Turkey is also in the strong part of our ranking table but we have to repeat that no market will be immune to a global sell-off. Although a mid-summer rally is due soon, it is not likely to pass the 'so what' test.

It is true that the Turkish Index is holding above its 200-day moving average, which is itself still rising. There is also plenty of support just below the long term average which has held since December whenever it has been tested.

Many of these markets are in secular uptrend and we do not expect these to be broken. But the cyclical correction can be large because the rally from March 2009 was so exceptionally huge. These swings are all in proportion to each other.

Brazil

Russia

Emerging markets

Emerging markets index

Mexico

Chile

Turkey

Eastern Europe index

Poland

Bonds

Oliver Twist

Oliver Twist had the brass nerve to ask for more. There comes a point when enough is enough and any more would be greedy. If you are an Oliver and hold your plate out now, you are literally asking for it.

The vital resistance levels that had to hold were a yield of 4.84% on the 30 year treasury bond and 4% for the 10 year bond. A break of those levels would - and still will - signal a new era of inflation. This will be more than nasty, it will be positively scary.

When investors went into panic mode they moved into bonds and the yield consequently dropped away very sharply from these danger levels. We had been anticipating such a move and last month set targets of 3.5% and 3% respectively. In both cases these levels were slightly overshot but markets are now steady.

Be careful about asking for more. Much lower yields would signal a depression. In the other direction, a rise above the recent highs would signal inflation.

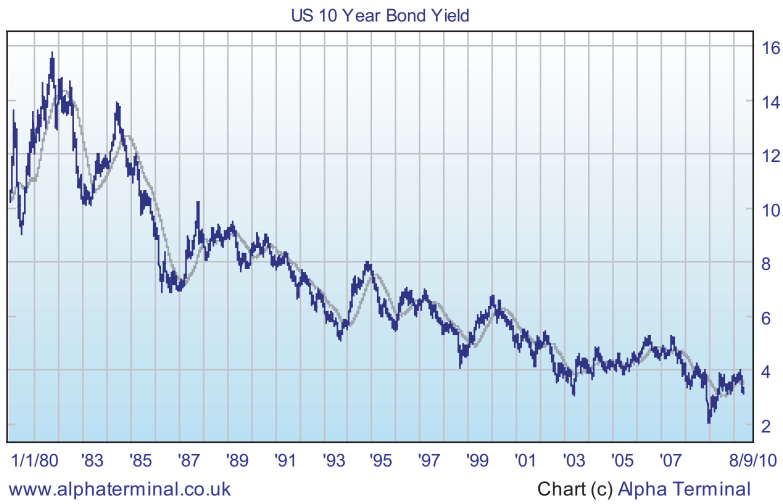
We are likely to be hearing the word stagflation a lot more in future.

Economies are going to have a double dip. It is not due whilst the last stimulus is still being frittered away in the normal hopelessly inefficient way that all government spending always unfolds. It will come after that. Our work has never deviated from the view that it is unavoidable but will not come until 2011.

Most governments will try to keep rates as low as possible for as long as possible whilst they grapple with the dire situation in the economy at large and property in particular. They are doomed to fail, but will not give up without a fight.

Rates are range bound for the time being within the ranges spelled out. But, as we have been seeing recently, not even countries are safe. The idea that US treasuries are the safest sovereign debt haven will only last until helicopter Ben starts printing money again. After that we will not want to own bonds, we will only want to be holding gold.

US Treasury bond 10 year yield



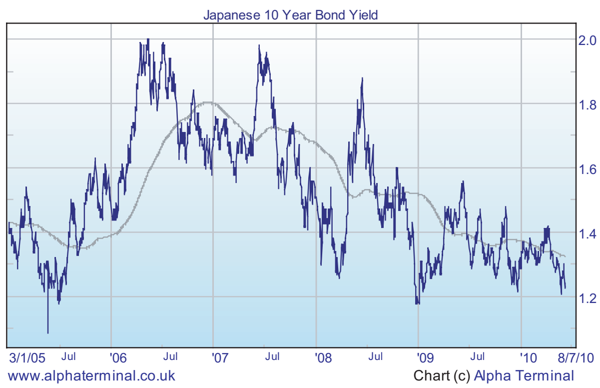
Bonds

US benchmark bond 30 year yield

UK benchmark bond 10 year yield

German benchmark bond 10 year yield

Japan benchmark bond 10 year yield



Commodities

Sell them all

Last month we told you to “Pick and Choose” the right commodities. This time we have a clearer view. Stop mucking about. When in doubt get out.

All commodities have made a top except gold. They are going down into a major correction phase. This does not invalidate the idea that they are in secular uptrend, but the cyclical correction is going to be nasty.

The only exception is gold. This has not been behaving as a commodity but as money. If it was just down to jewellery demand the price would be $800. The rest of the demand is hedging the risk of the default of fiat money. This is driving the long term uptrend.

We have just sold our gold at a new all time high. When we bought it not many people considered it a good investment. Just recently a lot of Johnny-come- lately types have been telling us to buy. Even Mr Bernanke was talking about gold. A clear short term sell signal.

Our road map for gold suggests that it will go much higher, probably to $2,000 next year. If they print enough dollars, it could go even higher.

But, first we have to take some deflationary pain.

The technical wave count for gold indicates a decent correction is imminent. This could last several months. It will take place while equities have their mid-summer rally. Only when equities tank again will gold suddenly look attractive again. This could occur in the August to October period.

The trader in me has taken a profit. We aim to get fully exposed again later. All the other commodities must fall back much further and then go through the process of making a base. That will all take time. Whilst China is cooling down this is not likely to occur.

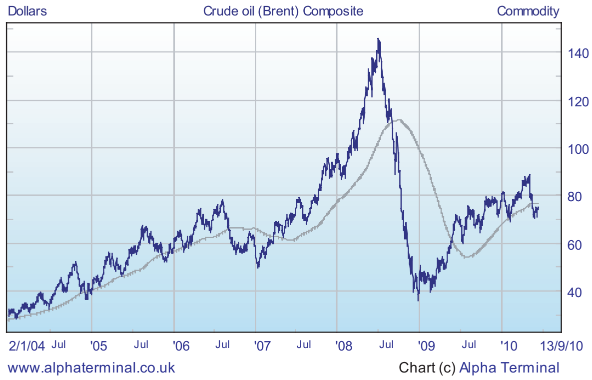
Commodity price index

Gold

Commodities

Platinum

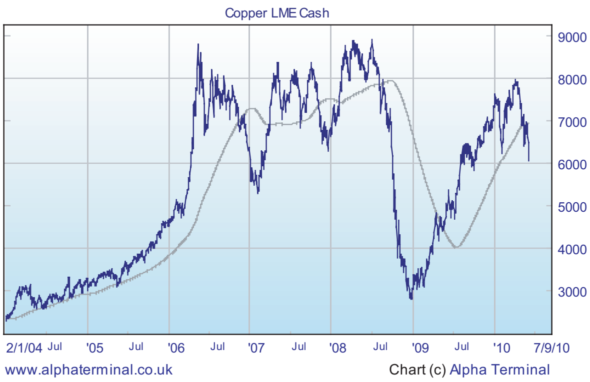
Oil



Silver

Palladium

Copper



Aluminium

Currencies

Nearly but not quite

A trend is a trend until it stops. The best part of the currency trends of the past six months are nearly at the stopping point but not quite yet.

It is all driven off the DXY or dollar trade-weighted chart. Last year this fell continuously to a low of 74 in November. As soon as it turned, three levels were indicated for the bounce. They were 82.5, 86, and 90. It has been up to 88.7. The best is done but we are not quite at the turning point.

In practice, the top could just be 93. There is a bit more dollar strength before the Fed undermines its value again.

In terms of the euro, this has meant euro weakness all the way down from $1.50 to under $1.20. There is strong support between $1.16 and $1.17. Again, it is nearly there. Being short euro under $1.20 is risky. There could be snap-back to $1.34 as quick as grease lightning.

Of course, if the euro region does not take a lot of nasty medicine then some of its sickest patients are going to die. Fortunately, the doctors are pretty good and can keep them alive for a little while longer. But the long term prognosis is very unclear.

We think the yen looks vulnerable. Actually it looks like a good short. No unequivocally clear signals have been given yet but it is shaping up to go down.

We also do not like the Australian dollar. It was way too pumped up until May and it has now clearly broken down. Any rally is doomed to fail as there is long term resistance below the 200-day moving average at 89. There is also medium-term resistance at 85.

Sterling is stronger than the euro but weaker than the dollar. The Prime Minister has an agenda to get the country out of debt, which will in time help sterling. There is a probable base building near $1.40. We have no reason to forecast levels below $1.35 at present. A break below that level has not happened since 1985.

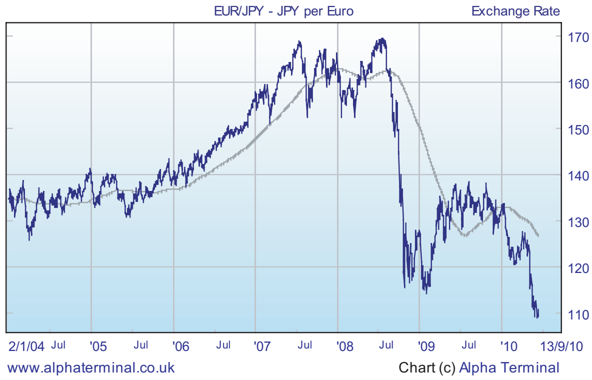
US dollar: trade weighted

US dollar/euro

Currencies

US dollar/Japanese yen

Euro/Japanese yen

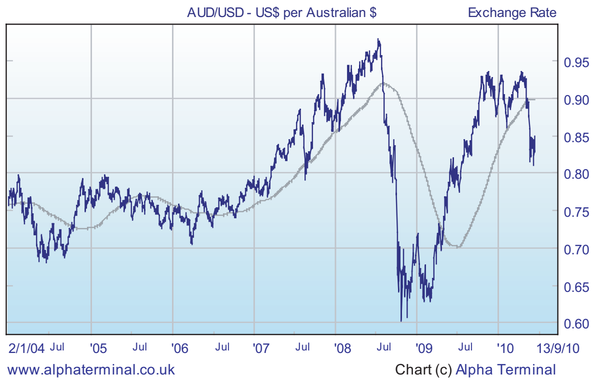


Sterling/US dollar

Sterling/euro

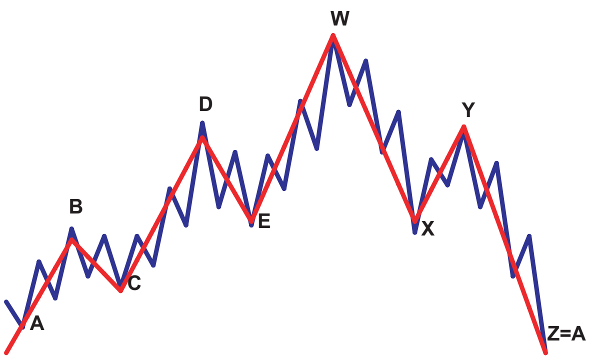
US dollar/Canadian dollar

Australian dollar/US dollar



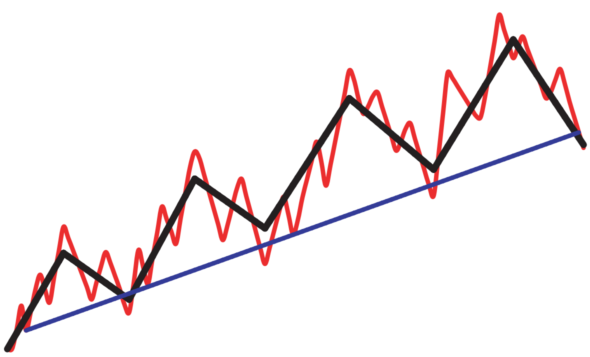
Road maps

Standard road map



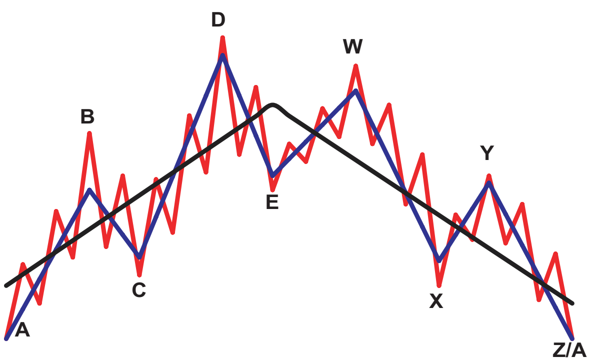
- These road maps are the basic shape of a so called Elliott Wave. We deliberately letter our maps differently from Elliott aficionados. The normal time scale for a complete cycle is four years driven by the Kitchin wave. The bull phase has three surges getting progressively more powerful. The bear phase is a fall, followed by a rally, followed by the rest of the fall. Big waves are composed of smaller waves of exactly the same basic shape. In practice, the waves we wish to trade can be traced out as the Index moves away from and back towards the 200-day moving average. If it is below that average, then it is a bear market.

Standard road map skewed by secular uptrend



- The standard model can be distorted positively by a strong secular uptrend. The small waves tend to take the same amount of time, but there is always an upwards bias. Even in the bear part of the cycle, a new high might be made and the next drop back is the end of the correction. The rule on this road map is always buy the dips as long as it is clear that the underlying secular trend is still valid.

Standard road map skewed by secular downtrend



- The basic map can also be distorted negatively. This, in practice, makes the bull part of the cycle very short and stunted. It also has the effect of lengthening the down part of the cycle. The rule here is always to sell the rallies. The secular trends that perform these distortions last for multiples of the four year cycle. Trends of 16 to 20 years are quite normal. On rare occasions they can be longer.

Source: Robin Griffiths based on Schumpeter

Investment Research of Cambridge, PO Box 37389. London N1 0WE Tel: 0207 278 4605