PIVOTAL EVENTS

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Signs Of The Times:

"***SunGard Easily Sells $3 Billion of Junk Bond to Fund an LBO***"
WSJ, July 28

"***Careerists With Dollar Signs in Their Eyes Head to Bay Street***"
FP (Toronto), July 30

"***A New Way to Profit From Commodities***"

"***Studies show the cheapest way to invest in commodities is in index funds.***"

"***RBC launches commodity linked notes***" **FP, August 2**

Stock Market: The window within which the first drop of an expected "choppy" summer was likely to close last Friday. The Dow did "***kiss***" the upper band within the time frame, but the correction was deferred.

However, the S&P has been trending towards a Fibonacci .618 retracement of the post-2000 plunge. This works out to 1254 and so far the high has been yesterday's 1245.9.

The hot action in stocks and industrial commodities now seems eligible for a brief correction.

Following this, the ChartWorks study of two weeks ago introduced the possibility of a peak similar, for example, to the end of the bull market in January, 1973. The highlight would be a brief up-thrust to new highs for the move and then the failure. Mid-September would be an ideal target for the high. It would be mathematically appropriate if the S&P made it to the 1254 level.

Overview: Some would think that the real driver is the discovery that the economy is in the perfection of the "Goldilocks" mode, which was last "discovered" in late 1999 – early 2000. At the time, we thought it was a rationalization to stay long the biggest stock speculation in history. Now it is to stay long the next bubble.

On the one, the focus was tech stocks; on this one, it is industrial commodities and residential real estate. In January, 2004, Stephen Roach, at Morgan Stanley, wisely observed, "***The image of the Fed as a 'serial bubble blower' is not that far fetched after all.***".

Our own view on this has been that the Fed has been blowing bubbles since they opened the doors in 1914 and, at some point, the world will wake up to the realization that great speculations will always occur and that it is best that central banks don't add their own speculative theories and practices to events that occur naturally and so regularly.

Last week, we used the term "Geriatric Bull Market" and would add that when the party is in full swing and the Rolling Stones "*Satisfaction*" is on full blast, even the oldest in the crowd can kick up their heels. We'll take this metaphor a little further by noting that the speculation is now becoming the equivalent of dancing non-stop to Bill Hailey's *Rock Around The Clock*, Presley's *Jailhouse Rock*, the Shandell's *Mony Mony*, Orbison's *Pretty Woman*, Bob Seger's *Old Time Rock and Roll*, and Long John Baldry's *King Of Rock And Roll*. [1]

On this sequence, the market for stocks, commodities, and homes is about at the equivalent of *Pretty Woman*, and the line "*No one can look as good as you. Mercy . . .*" seems descriptive.

By this model, the excitement is high and there are only two numbers left. These could use up all the available speculative energy by mid-September.

As the saying goes, dance close to the exits – the air is usually cooler and fresher.

Technicals: For the past few weeks, we have been noting that the window for the first "chop" of the summer would close at the end of July. That model was based on the repetitive swings following a year of 52 weeks of bullish sentiment readings. Typically, this pattern held for the first 7 months and this is now over, but the correction seems "close enough".

The July 26 edition of ChartWorks introduced an overview model and this would require about 7 weeks of speculative zoom. One example given was the conclusion of the bull market in January, 1973. The zoom would include homes, industrial commodities, and the stock market. The latter two could reach upside exhaustion by mid-September.

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[1] Some 20 years ago, this writer was part of a group that had a big log house at Whistler Mountain. The strongly built refractory table could sit 22 for dinner and many of the parties were bigger than that. One of the house rules was that when Baldry's *King Of Rock And Roll* was played, everyone had to dance – but not on the floor. That meant the fireplace, furniture, kitchen counter and, of course, that huge table. Sadly, Baldry passed away on July 21.

Warnings signs would include the advent of the next phase of credit spread widening and the reversal of the treasury curve to steepening. Providing some anticipation of this is that the UK curve, from the 10-year to the 3-month, has been in a steepening trend since June 8.

Further confirmation of pending exhaustion would be provided by gold outperforming silver.

INTEREST RATES

Last week we concluded that if the party continued after the close of the July 31 window, the long bond would be sluggish. The bond future slipped from 115^10 to 114^21 on Tuesday. Wednesday's Treasury announcement popped prices by half a point, but support is possible at 114.

A brief correction in the hot games could stabilize the bond future. We are also concerned about the ChartWorks outlook for dollar weakness continuing into September.

The Dollar Index reached our target of 90-92 (91.5), from which a correction well into September has been targeted.

It has been possible that this could initiate or be associated with mounting concerns about liquidity.

The Canadian Dollar is a little off its best, which was 83.15 on July 12. The interim low was 80.87 on July 27, from which it has recovered to 82.23.

This seems to be testing the high and increasing financial concerns after mid-September could initiate the next downtrend.

COMMENTS FOR METAL AND ENERGY PRODUCERS

Energy Prices: Clearly, there are enormous forces at play. Perhaps it has the makings of another "Perfect Storm".

Most have used the phrase to describe when something goes wrong – almost as if it was an accidental twist of fate that brings a great speculation down.

In the marketplace, and as we have described it, the Perfect Storm includes both the upside and the inevitable downside of a monumental speculation. In the oil game, there is little doubt that this is the upside of a Perfect Storm which, ironically, has been amplified by the unusually early arrival of the hurricane season.

This, along with the "Peak Oil" story, is building a very big Perfect Storm. We like to refer to Stanley Jevon's 1865 publication that the world was going to run out of coal. He was a British economist and the book, which was published in 1865, was titled "***The Coal Question: An Inquiry Concerning the Progress of the Nation, and the Probable Exhaustion of our Coal-Mines***". Using today's terms, his book could be called "Peak Coal". He also indicated that it was almost a religious experience to fully grasp the concept. In it he states "***This is a question of almost religious importance which needs the separate study and determination of every intelligent person***.".

The mid-1860s saw the culmination of a 20-year bull market in commodities, which blowout set up the great financial bubble that climaxed in September, 1873. A 20-year bear market for most commodities and tangible assets followed.

This makes us alert to the culmination of this mania in commodities. In this regard, some of the leading energy stocks are becoming irresistible and our objective is to anticipate the major swings. Last week's advice may be a little early, but two things should be kept in mind.

The overall stock market could top in September along with most industrial commodities.

The oil play is becoming very mature and vulnerable.

Driven exuberance has eliminated the typical seasonal decline into late June – early July as well as the rare example of weakness into late July. However, there is the usual seasonal strength into early October to consider.

It is uncertain how much exuberance this can contribute to a market that has become parabolic, but it does provide some indication of when the next intermediate decline for the stock-side of the play will occur.

Typically, natural gas sets a key high in June and that was 7.69 on June 17. The setback was to 6.98 on July 1 when the switch was put back into the party mode. Along with the stock market and crude oil, natgas has been partying – in this case, up to today's 8.68.

Golds: Yesterday, Placer reported a loss on the second quarter due to their hedge book and increasing costs relative to gold.

This succinctly explains why we focus on the real price of gold, which decreases during a boom (increases mining costs) and increases during the consequent contraction (reduces mining costs relative to gold's price).

Obviously, this ancient relation has been overriding the goldbugs' focus on the "***dollar down – gold up***" equation. An outstanding example occurred through the 1929 financial bubble. Gold's price was fixed at 20.67 per ounce until the end of 1932.

With the boom, Homestake's earnings declined and during the consequent contraction earnings and the stock more than doubled by late 1932. This was before the street had an idea of Roosevelt's flaky financial experiments. In the face of no change in the dollar price of gold, the gold mining industry profited immensely – ***as the real price went up***.

Because the calculation of the CPI is so suspect and only reported once a month, we have been using gold's price relative to commodities as a guide.

Our gold/commodities index set a cyclical high of 255 in May, 2003. The high for gold shares was set at the end of 2003. The most evident bear was in the real price and in exploration stocks. (Check out the www.GoldColony.com index.) The focus on the dollar price sustained the senior golds until March of this year when, with the failure, the seniors joined the bear market.

As we have been discussing it, the key aspect of the bear has been a cyclical decline against the cyclical boom in the orthodox world of finance. However, the golds have been basing since May and anticipating the next business and stock market contraction.

From a low of 185 in May, our gold/commodities index recovered to 202 at the end of June. The test was to 188 on July 13, from which it has made it to yesterday's 198. Going through 202 would set the uptrend. This week, the HUI has popped through significant overhead resistance and the exploration index, which has recovered from 99 to 112.5, needs to break through 115 to set its uptrend.

In the world of physical gold, investment demand has been increasing and it will surge on the next phase of credit spread widening and with the reversal in the treasury curve from flattening to steepening.

	FRI	MON	TUES	WED	THUR NOON
JULY	**29**	**1**	**2**	**3**	**4**
High-Yield Spread	306	303	301	304	—
Treasury Curve	108	105	107	105	106
Base Metal Prices	1005	988	1012	1000	1004
Dollar Index	89.4	88.9	88.8	88	87.9
Gold	429.5	431.4	431.4	436.2	437.9
S&P	1234	1235	1244	1245	1237

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SIGNS OF THE TIMES

THE GERIATRIC BULL MARKET

"I'm not looking for a steady income and security.
I just want to make a big, fat killing and check out."