

PIVOTAL EVENTS
FRIDAY, OCTOBER 11, 2002
BOB HOYE

Big Picture: The decision to increase equities from 35% to 42% has prompted some inquiry. While we have called or anticipated all of the intermediate rallies, we did not increase the recommended weightings for pension funds because the valuations were extraordinary, bullish opinion was adamant, and the bear market was nowhere near the minimum duration of 3 years.

Of course, it is quite likely that the market will go to outstanding valuations [outstanding valuations are 1 times book and a 6% dividend yield, which are found at the end of bear markets.] but, until that is accomplished, valuations will continue to be of little guidance on intermediate rallies or declines.

While we still have high valuations, prices are lower than at any rally point in the past 2 ½ years and, of most importance, the bulls are becoming dismayed. The latter is shown in the S&P registering capitulation on the ChartWorks proprietary model. The weekly reading is kicking in as it has on 13 such periods of heavy liquidation over the past 100 years.

Our view in 2000 was that there would be a number of capitulations until the post-2000 bear was over. This is Number 4.

Also worth noting is that, once the capitulation registers, it could last for up to 6 weeks or more before the low is accomplished. We are now at the condition reached in October and again in December, 1931. Thus our view for a tradable rally out of the eventual hole.

Outlook For 2003: The point to be made is that, while the stock market has been as bad as it was from 1929 to late 1931, the economy is not in the same category. The unprecedented continuation of the median home boom is the only reason and, like any bubble since Asia blew out in 1997, every speculation has reached saturation and has collapsed. This is inevitable and will fit the Austrian School's theory that the boom and bust are proportionate.

Our work has been empirical rather than theoretical and concludes that all of the requirements to conclude a post-bubble contraction seem unlikely to be accomplished within the shorter three-year duration. Without the intensity of 1929 to 1932, the contraction will likely be prolonged, as followed the 1873 bubble. The combination of 3 different approaches suggests that a very worthwhile rally could run from when the low is accomplished (perhaps in November) until around May.

Thus our advice to increase the equity weighting from 35% to 42%. Why the 7 points? - 7 is lucky.

There are about 50 sub-groups and not all will bottom at the same time.

Confidence: In early January, 2000 we noted that short dated treasury rates typically soared for some 18 months as a stock mania blows out. This began the regular reminder that March would be the "18th month". On January 28, 2000, the Boom Indicators had reversed from the most positive reading of +12 to +6 and we advised reducing equity exposure from 60% to 40%. The reading has now improved from -12 to -11.

At important lows, as in late 1998, it took from October, 1998 until February, 1999 to become convincingly positive. It's slow, but some solid improvement by, say, around March would suggest the end of the bear.

In the meantime, let's consider it as a good potential rebound within a more leisurely contraction, such as followed the new financial era that ended in 1873.

Sector Comment: Preliminary work suggests that the utilities could lag and golds could rally with the orthodox market.

INTEREST RATES

Credit Spreads: Last year, the model expected credit spreads to widen until around November. The 9/11 atrocity accelerated this and the crisis drove the junk spread to 825 bp over treasuries on October 2. After November, spreads were expected to narrow with the other "good stuff" until around March.

This was prolonged as spread action, seemingly compelled by a shortage of junk, drove the spread to 535 bp in May. Fortunately, a remarkable increase in "Fallen Angels" eased the shortage and this week the spread reached 923 bp.

Our July 19 edition discussed the fact that widening would accelerate in September to dislocating conditions by December and noted that "*this would involuntarily turn investors into sub-prime lenders*".

This seems to be working out.

Yield Curve: Shorter-dated treasuries were expected to increase with the "good stuff" until around March and then resume the long decline with the opposite stuff. For example, the 90-day bill rate rose to 1.84% in March and has declined to 1.55% this week. Our eventual target has been around 1%.

This natural decline is feeding into the long end for some 6 weeks longer than we thought possible, but steepening due to long rates rising could be starting.

The Long Bond: The long bond has become speculative. The refi game is an unstable loop that is connecting a soaring median home market to soaring bond prices. Just because everyone is watching the phenomenon and calling for its end doesn't mean that it won't end.

Part of the play has been to buy SUVs and this seems to be faltering. With the discounts and zero financing costs, the depreciation on a new car is larger than ever and is forcing prices down in the second-hand market. The average car now is a sound driver for at least 10 years so the rage to have a new one will rapidly be seen as uneconomical.

Perhaps 4 years of record light vehicle sales will be done in by the 3-year bear market. If so, the house mania will follow and, as odd as it seems, this will be tied to the end of the mania in longer maturities.

Confirming this is the ChartWorks note, as of today, that the 10-year yield has given a weekly capitulation "buy" reading. This means a significant increase in longer term interest rates.

Spreads Again: Since May, Merrill's junk index has increased in yield from 1096 bp to 1395 bp this week. In the same interval, the yield for a medium grade corp has gone from 788 bp to 701 bp on September 17. Considering the appropriate carnage in the junk market, this seemed inappropriate. However, since then the yield has increased to 742 thus ending the divergence as the spread has widened from 226 bp to 270 bp this week. This spread narrowed to 197 bp in March.

Real Long Interest Rates: Clearly, real rates have been rising for junk but have been declining, since May, for better credits. While this is part of the remarkable speculation in bonds, it should be recognized as favourable and that section of the Boom Indicators turns one notch positive. This improves the reading from -12 to -11. The worst reading possible is -14 and the worst reading reached was the recent -12.

COMMENTS FOR METAL PRODUCERS

Gold: Gold's price relative to commodities sold off from 263 on May 29 to 228 on August 21, from which it based until September 12. Under the appropriate conditions of the liquidity contraction resuming, the index has improved to 241.

Gold Shares: Beyond the treasury curve and gold's relative price share action, at times gold shares anticipate gold rallies.

Our basic model expected the first speculative high in the long bull market to be set around May (✓). After a relief rally, golds were expected to weaken again as the general stock market suffered heavy liquidation beginning in early September.

This was reviewed in our September 20 view that *"the stock market plunge could take gold shares with it"*. The plunge is on and, using Newmont as the proxy, the ChartWorks suggests that it is within a week of a "buy" condition. For those who are underweighted, we would start aggressive buying now.

Gold/Silver Ratio: Money market spreads have finally joined the distress being suffered by the junk bonds since late July. Needless to say, this is serious and was confirmed by a rather quick increase in the gold/silver ratio to 74. This may ease over the next week and last week's edition discussed the action in brief terms that are worth repeating:

Our June 7 edition noted that silver was at an important top, from which a long bear market in nominal terms, and relative to gold, would follow. Silver's high was 510.1 on July 15 as the gold/silver ratio set a low at 62.5. The piece concluded with "Rising through 70 would anticipate the next phase of credit distress. Our long term target remains around 110."

This ratio is not only the oldest price series in history, it also has the characteristics of a credit spread. In rising to 70.9 in early September, it anticipated developing distress. On September 26, it broke 71 and, now at 71.8, bank and financial stocks are very weak.

Energy Prices: Our view in June was that both crude oil and natural gas prices would recover until early October. From a low of 24.12 on June 10, crude recovered 28% to 30.8 on October 1.

Natural gas sold off to 2.66 on August 6 and, making up for lost time, zoomed 55% to 4.14 on October 2.

Both have declined a little, but it's enough to break the rising trendline. As we have outlined, U.S. "Gunboat diplomacy" in Iraq will likely start in early January. This would force a brief speculative rally in a much longer downtrend. The money markets are now showing a concerning loss of liquidity that, with the collapse in the junk market, does not auger well for global business conditions into next year (credit distress is global).

October 2002	MON 7th	TUE 8th	WED 9th	THU 10th	Noon FRI 11th
Swap Spread	68	67	69	68	66
Junk Spread	878	895	919	923	-
Treasury Curve	311	310	312	315	321
Base Metal Prices	471	472	471	472	475
Gold	321.9	318.2	319.6	316.5	316.6
S&P	786	799	777	804	820

PIVOTAL EVENTS

FRIDAY, OCTOBER 4, 2002

BOB HOYE

Market Lore: Speculative action is fungible. Whether in stocks, bonds, or commodities, excess has similar and measurable characteristics as does its consequent unwinding of suddenly and chronically unsupportable positions.

Any veteran of the formerly notorious Vancouver Stock Exchange would note that no matter how preposterous the story is, as long as the trend is up it will be ardently believed and will enjoy spreading circulation. Then when the trend breaks, sobriety and chagrin prevail until the play is utterly abandoned.

Of course, within the lengthy liquidation process there are brief short squeezes and what has occurred with collapsing Vancouver schemes has occurred in New York a few times lately - a very dynamic rebound that lasts for a day and a half. The week enjoyed another such day and a half winning streak.

The Record: Last month was widely reported as the worst September since 1937. In looking at the monthly chart, all of the biggest bars have been to the downside. Since 1900, these have also occurred in September 2001, November 2000, April 2000, August 1998, October 1987, May 1940, and September 1931.

The latter is the most pertinent as it was a September of Year 2 after the climax of a new financial era. Ours dropped 12% while the 1931 example clocked a 31% plunge. However, the

cumulative declines are similar with the Nasdaq down 77% at the end of 3 Qtr. Year 2 and the Dow (speculative index then) down 75% to the equivalent 3 Qtr. Year 2.

Hey, we are just the messengers - not editorial writers or investment bankers. Our product is research, not paper.

The Model: For 2 Qtr. 2002, the high was expected for March and that it would be the high for the year would be confirmed by the ChartWorks registering important "overboughts" (4) with a sharp plunge in April (4).

New lows for the bear were expected in June, but were not accomplished until July 23. Then, after some recovery until late August-early September, the decline would resume and set the low for the trend and for the year by December.

Outlook 2003: Due to the unprecedented continuation of the boom in the median home and big cars, the economy is not as bad as the action in stocks and credit spreads. On October 2, the WSJ observed: *"Tumbling share prices may have hammered portfolios. But, instead of limiting the damage by saving more, many Americans have retreated into an orgy of spending."* However, veterans of the markets, rather than contrived economic theories, know that the compulsive action inevitably reaches saturation.

The editor's alert to this failure has been unrequited since April. But the reversal in the treasury curve to steepening and in Fannie's changing fortune suggests that the speculative anomaly could pop.

Every cyclical or secular bear market in history has been eventually accompanied by the equivalent in business activity and we do remain alert to this.

In spite of this, the rally out of this hole until around May could merit an increase on equity weighting.

Asset Allocation: When our boom indicators reversed in February, 2000, the advice was to reduce equity exposure from 60% to 40%. Then, when the models worked out so well on the rally to May, 2001, the advice was to reduce to 35%, which would be the minimum. The Indicators remain unchanged at the very concerning -11 and, should the car and house boom fail, it would drop another notch.

Nevertheless, some technical and historical work has been calling for an important, and possibly cyclical, low for around November-December and it seems appropriate to increase weightings from 35% to 42% equities.

One Model: The ChartWorks "post-euphoria" patterns following the extravagances of Dow 1929, Gold 1980, and Nikkei 1989 have provided outstanding guidance on the main trend as well as on the intervening trades. We have also called the model "Road Maps" and these have led us to a significant low for the late October to early January window, from which, on each example, a cyclical bull market ensued.

Historical: This approach has been based upon all of the five new financial eras since the first big one ended in 1720. The first thing to understand is that the bear markets have been a

consequence of the speculation and not due to policy error by central bankers. The post-bubble contractions strongly suggest systemic inadequacy rather than policy error.

Now that cause and effect have been cleared up, the next importance is that, using the two most recent examples as they occurred in the U.S. (1873 and 1929), the bears lasted 5 and 3 years respectively.

The rule seems to be that all of the unsupportable speculative positions will eventually be liquidated. Following 1929, it was intense, but being on a sound money basis may have fostered the rapid clearing of that hangover.

However, since 1934 the U.S. has suffered a "flexible" currency (as it was originally touted) and, while it didn't change the duration of our new era, it seems to be moderating the rate of post-bubble liquidation. In May, we noted that the period from mid-year to December could be as broadly severe as in the post-1929 contraction or, more generally, moderate as in the post-1873 example when the U.S. also suffered a fiat currency. (In this regime, the government insists the note is a dollar, but the market determines what it will buy in tangible assets or, until recently, in financial assets.)

As events rolled, the stock and spread markets have been very bad, but the economy has been supported by the "buying orgy" in homes and cars. On the observation that the economy has to get as bad as the stock market before the contraction can conclude, this one is not over. The upshot is that the stock market is due for a rally that will likely have little to do with the near-term condition of the economy.

This is the first increase in the equity weighting since the Indicators turned positive in early 1999, but this one is not based upon any improvement in the Indicators. An increase from 35% to 42% equities could be completed by early January - it's time, at last, to "buy the dips".

COMMODITIES

As we have been outlining, there has been some strength in commodities that may not be signaling a robust global economy. Since the low of 878 in March, our grain index soared 45% to 1272 on September 11. It has been the worst drought in a generation. However, a tested high is in and the extent of the downtrend will depend upon the 3-year drought ending.

Because of the consumer "buying orgy", the 350 target by December for our base metal index has been deferred. Crude oil prices have recovered from 24.12 in June to 30.8 on Tuesday. Our target has been a seasonal high for early October and this is being met. Once the top is in, our view has been that the decline would be mainly due to seasonal forces joined by declining global business activity. Of course, the U.S. raid to assist political reform in Iraq would briefly pop energy prices.

The rise in the Baltic Freight Index has been extraordinary and there have been a number of explanations, with this week's shutdown of West Coast ports adding to the list. An old fashioned short squeeze still seems to be the best explanation.

However, the steepening yield curve and widening credit spreads are doing a number on the banks and financials. Although this ominous condition may ease in the next month, it doesn't augur well for international trade.

INTEREST RATES

Credit Spreads: After March, widening was expected to resume and reach dislocating conditions in December. However, pressures became overdone last week with some stability evident in junk, emerging debt, and the bellwether 10-year swap rate. This, along with a stabilizing stock market, could prevail for 4 or 5 weeks, making for a choppy but flat October. This could be disquieting to those who are adamantly bullish or bearish.

Yield Curve: As part of the credit stringency likely to resume after early September, the curve has been expected to steepen. This has been the case and the pundits' tout about steepening being good for bank stocks is not working. It shouldn't be, as severe steepening is integral to a post-bubble deflation. From the August 22 high of 963, the BKX has dropped 34% to 640, which is threatening the July low of 636.

Short rates were expected to rise until around March (✓) and then begin a lengthy decline to eventually around 1.00% for the 90-day bill.

The Bond Future: The September 20 ChartWorks showed some similar patterns that, once an "upthrust" was accomplished, a tradable price drop would follow. On that week, falling below 112 ½ would be the trigger and, as the September 26 memo noted, the failure would be at 113¹⁹.

Naturally, part of the rally has been due to slowing business activity since mid-year as well as to recent stock market weakness. However, as we have been noting since July, is the highly unstable refi convexity trade (in engineering terms - positive feedback mechanism). Lower rates (on schedule) prompt refinancing of mortgages. This is for financial advantage and funds have been employed to upgrade the house, buy a second one, a bigger car, or even cover margin calls.

On the refi, mortgage holders are paid down, who then position in treasuries, which adds to declining yields, which stimulates more refi, etc. This has now become compulsive action and, where the advantage was substantial, as from a 6 ½% to a 5% yield, it is now being done for a \$40 reduction in monthly payments.

As with any positive feedback system, it goes parabolic until it fails catastrophically. This is not to say that the long end of the treasury curve can get trashed, but it does mean the refi speculation will collapse. Mortgage default rates have been soaring.

COMMENTS FOR METAL PRODUCERS

Base Metal Prices: Obviously - no instability in this sector, which is in a long-term decline in price and eventually a flattening of the growth rate of the consumption curve to zero (0).

The weak point for the year could be set late in November with the next slide in the stock market likely to begin in early October and end around Christmas. The usual seasonal recovery to March-May could be constrained by the collapse of the median home and big car "buying orgy".

Gold: The last low for gold's nominal price was 306.6 on August 22, which was also the last high for the stock market. The stock market is not the only item marked down in gold terms. Relative to commodities, our index troughed at 228 from August 21 to September 12, from which it has recovered to 250.

This reversal has been tested and it is likely that the correction expected after May has been accomplished. This has been accompanied by appropriate steepening of the treasury curve and widening spreads.

So far, the relative price has gained 9.6% while the nominal price is up 4.7%. This was the case as from October, 2000 to January, 2002 as both the relative price and gold shares outperformed gold's nominal price. Then, on a knee-jerk basis, the goldbugs became impetuous just in time to set the forecast highs in May, 2002.

After September, gold's real price has been likely to start the next move, which should be substantial and lengthy. However, liquidity problems in the broad stock market could depress gold shares. Strong buying on such weakness is recommended.

Gold/Silver Ratio: Our June 7 edition noted that silver was at an important top, from which a long bear market in nominal terms, and relative gold, would follow. Silver's high was 510.1 on July 15 as the gold/silver ratio set a low at 62.5. The piece concluded with *"Rising through 70 would anticipate the next phase of credit distress. Our long term target remains around 110."*

This ratio is not only the oldest price series in history, it also has the characteristics of a credit spread. In rising to 70.9 in early September, it anticipated developing distress. On September 26, it broke 71 and, now at 70.8, bank and financial stocks are very weak.

SEPT-OCT 2002	MON 30th	TUE 1st	WED 2nd	THU 3rd	Noon FRI 4th
Swap Spread	66	63	62	64	63
Junk Spread	853	845	853	857	-
Treasury Curve	311	319	314	316	316
Base Metal Prices	467	469	483	475	476
Gold	323.9	320.9	321.5	321.1	321.1
S&P	815	848	828	819	806

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FRIDAY, SEPTEMBER 20, 2002
BOB HOYE

Fed Chairman: *"We were confronted with forces that none of us had personally experienced. Aside from the then recent experience of Japan, only history books and musty archives give us clues to the appropriate stances for policy."* - Alan Greenspan, Jackson Hole, Aug. 30, 2002

Obviously, Mr. G. is not a subscriber to Institutional Advisors nor does he seem to recall his own criticisms of excessive accommodation by the Fed during the 1920s' new financial era. Published in the *Activist* in 1966, it showed the clear reasoning typical of libertarian economics.

For some years, we have thought that Greenspan's libertarian side was running a crafty strategy. As Fed Chairman, he would play the Keynesian accommodation role as best as was possible. Then, when the inevitable post-bubble contraction was seen to be undeniable, critical review would then be able to conclude that the recurring phenomenon is due to systemic rather than policy failure.

Unfortunately, the gist of his Jackson Hole address reveals confusion and inadequacy rather than Machiavellian confidence. For those who haven't read it, Jim Grant's essay of September 13, 2002 is worth reading, as is the following excerpt.

"Although the Federal Reserve System employs 485 Ph.D. economists, only one is a living symbol of the dynamic U.S. economy. And now this one man says that he didn't know about the stock-market bubble, couldn't have known and, even if he had known, wouldn't have been able to make a move against it. It isn't a great advertisement for a monetary dictatorship."

Nothing daunted, we would add that the dollar's 90% depreciation over 50 years is a constant record of folly, of which the inevitable result is sensational bouts of asset inflation. Ironically, the collapse of the old era of tangible asset inflation is celebrated as brilliant policy while the collapse of its equally destabilizing inflation in financial assets is described as a deplorable series of policy mistakes.

Stock Market: Some critical calls:

July 19, 2002: *"Stockholders, generally speaking, are replicating their behaviour typically found at exhaustion lows that precede tradable rallies ... the dollar index has registered a Double Capitulation on the weekly reading and it can rally with the similar readings registered on the stock market."* [Low July 23]

August 23, 2002: *"Both price targets and technical dynamics sufficient to reverse the stock market have now been achieved. That this occurred close to the expected time window increases the confidence that the scheduled plunge to around December will also be accomplished. The next target would be the July lows and, by December, declines in the senior indexes could amount to 25% to 30%."* [High August 22]

Wrap: Technical deterioration since late August is now accompanied by widening credit spreads, steepening yield curve, as well as renewed weakening in base metal prices.

These moves have been likely to begin in late September and are foreshadowing another phase of heavy liquidation.

Sector Comment: The slide has been expected to encompass most sectors and could become severe enough to bring down some of the golds.

Big Picture: The detailed study of the culmination of every new era since 1700 has been invaluable in identifying the top in January - March, 2000. Also invaluable has been the ChartWorks' study of the consequences of the "Great Speculative Euphorias" of the past 100 years. These, of course, were the Dow in 1929, Gold in 1980, and the Nikkei in 1989. The latest update is attached and, using the Nasdaq as the proxy, an important low has been possible in the late October to early January window.

In conditions that have perplexed fundamental research, this form of technical analysis has provided reliable guidance and some readers will focus on the term "cyclical" low and "no offside day within the next two years". This should be placed in perspective. [The August 20 ChartWorks noted Nasdaq overhead resistance at 1416. The high close was 1423 on August 23]

The ChartWorks is using a monthly count from the March, 2000 high and the pattern has been close to those on the "Post-Euphoria" examples. However, our "Post-Bubble" model, which includes action in spreads and the curve, has used the count in years - 2002 being a typical *Year 2* after a bubble (other than the housing boom).

This model was based upon the observation that a number of significant events in 1929 replicated the previous bubble-year of 1873. Then 1930 was similar to 1874, etc.

This worked for 2001, which was *Year 1* and so far has been working for 2002, which is *Year 2*. The post-1873 contraction was less intense and more protracted than the post-1929 example and lasted for 5 years, which compares to the bottom in July of 1932, which was *Year 3*. With the unprecedented continuation of the housing boom, the contraction has yet to become severe.

The net of this is that, while the housing frenzy is vulnerable (mortgage default rates at 20-year highs), the business side of the contraction has not been severe enough to contemplate the end of a post-bubble bear market nor is it likely to become severe enough for completion by, say, January. In which case, the stock market recovery as developed by the ChartWorks could be rewarding but within the confines of an 1875 style prolonged financial and economic contraction - time, rather than orthodox theory, will tell.

INTEREST RATES

We have steepening in the treasury curve and widening of credit spreads. The significance is that it is coming in on schedule and, confirming that, the next phase of the liquidity crisis has begun. This has been expected to become acute by around December.

Without getting into the definition, Merrill Lynch's distress ratio is threatening to break to new highs. From 62% with the 1990 recession, it declined to around 3% in early 1998. As part of the crises since LTCM in September, 1998, the ratio increased to 32.8% in December, 2000. With a

couple of swings, it declined (improved) to 16.8% in May. As part of the "bad stuff" likely to resume after mid-year, it has increased 30.6% on September 16.

Breaking above 32% seems inevitable and would confirm our expectations of dislocating conditions by December.

Our advice since 2000 has been that investors should minimize exposure to risk. As we have phrased it, when looking at an offering, repeat the mantra "On an if, as, and when redeemed basis."

The Long Bond and The Curve: Our advice to traders during June was impaired as the stock rally was delayed until July 23. However, the advice to investors has been worthwhile. Shorter rates were expected to decline after March (✓), but steepening wasn't scheduled until September when it would signal the resumption of another liquidity crisis.

Our August 9 view was that investors should use the rally to reduce exposure to the very long maturities. The problems in the lesser credits in the fall could pull prices down at the long end. However, by the 16th, that the refi action was becoming impulsive was noted and on August 23 we concluded that the stock market was about to roll over, which would "release another bond rally".

Technically, the price advance has been methodical and the proprietary "overbought" model has not been registering. However, the ChartWorks has researched a pattern that seems appropriate. Once this immediate move loses momentum, a 5-point break would follow.

COMMENTS FOR METAL PRODUCERS

Base Metal Prices: Industrial commodity prices have been expected to plunge with the stock market in September (crude has been expected to rise into October). Adding complexity is that the dollar has been likely to weaken as well. This could curb the slide in base metal prices. However, hard deflation has followed every bubble and, whether measured in euros, sterling, gold, or eventually dollars, most tangible asset prices will plunge.

Our May, 2000 study expected a multi-year bear market for base metal prices. This is *Year 2*.

Gold: Gold's real price is poised for the next, and quite likely, substantial move up. With the correction expected after May, our gold/commodity index declined 13% from 263 (May 29) to 228 which prevailed from August 21 to September 12. It has since recovered to 235. This has been accompanied by steepening of the treasury yield curve and widening credit spreads, indicating the financial conditions typical of the post-bubble increase in investment demand.

In previous examples, as the usual instruments of credit contract, it leaves a liquidity vacuum that must be filled. In all cases, gold's real price increased, which improved operating margins, production to satisfy this increased, and gold shares outperformed the general stock market. This method expected the cyclical low for gold and gold shares to be set in November, 2000 (actually October) and then begin a multi-year bull market. The first speculative high was likely to be set in May, 2002 (✓) against a plunge in the stock market.

While noting that this has worked out, it is essential to stress that when our research was completed we expected that this would be difficult, if not impossible, to do using any form of analysis of supply and demand or of the nominal price.

Put yourself in the summer of 2000 and, using orthodox methods, attempt to forecast the cyclical low and then the first speculative high some 18 months later. It can't even be done by back-testing. The irony is that anyone could have reviewed the behaviour of gold's real price through all previous financial bubbles and derived our model any time before 2000.

As laid down in 2000, the model expected that increasing financial distress in September, 2002 would prompt another significant leg up for gold's real price.

Gold Shares: The post-September stock market slump could take gold shares with it. Aggressive buying on dull or weak conditions is recommended.

SEPTEMBER 2002	MON 16th	TUE 17th	WED 18th	THU 29th	Noon FRI 20th
Swap Spread	55	54	55	56	57
Junk Spread	792	791	795	808	-
Treasury Curve	306	306	308	307	311
Base Metal Prices	489	478	478	478	475
Gold	317.1	317	320.6	322.6	323.3
S&P	891	873	869	843	844

ChartWorks

September 20, 2002

NASDAQ - Thirty Months and Counting

The NASDAQ is now thirty months past its all-time high print of 5132 on March 10, 2000. Using previous bubbles as measurements we can anticipate an important cyclical low within the coming four months.

We looked for complacency around the 22nd to 24th month (January to March 2002) following the top and then a severe decline this spring. The next event was to be a rally back to the top of the 34-week 5% trading band. This became a direct hit at 1426 on August 22nd, twenty-nine months after the top. This rally pattern occurred in the 27th to 29th months following the tops of the Nikkei, Gold and '29 Dow. It was also concurrent with a daily-overbought reading in our proprietary CWSum Index and produced an RSI reading in the high 50's (also present in the Nikkei, Gold and '29 Dow).

Where to now? From the overbought test of the trading band the declines to the ultimate **cyclic (not secular) lows** have been 10, 14 and 20 weeks later. This provides a **time window of October 31st to January 9th**. These declines were 24% (Nikkei), 21% (Gold) and 54% ('29 Dow). **All three declined at a rate of 1.7% to 2.7% per week**. Given these rates, the NASDAQ could be **1126** by October 31st.

From an investment and money management perspective, the most important fact is to accept that the downtrend 'is in motion until it ends'. In order to clear unsupportable positions, the market will get as overextended as it needs to.

Back in the 1980's we recognized a recurring pattern that could be used to identify the end of major bear markets shortly after the low was in place. The key was not to pick the bottom, but find a low risk entry point shortly after the low was in place. . . and do this without premature entries. Only a reversal through an upside resistance will prove that the trend has turned positive. The most recent occurrence of this pattern was in gold at \$258.30 in September of 1999.

Using this same technique when viewing the final months of decline in the post bubbles ('92 Nikkei, '82 Gold, '32 Dow), we find:

- No false buy signals.
- Long within two weeks of the bottom.
- Immediate upside action first two weeks after purchase.
- Gains of 24% (Nikkei), 64% (Gold) and 67% (Dow '32) within the next two months.
- From point of entry, no offside day within the next two years.

If prices breakdown from here we will start publishing the reversal criteria.

Use of Daily US10YR02 C=11.5000 ~0.20

Bonds - Nearest Contract 2001 to 2002

A close below 112 1/2 would indicate that a larger correction into the 105 - 107 range is likely.



Inverse US10YR02 K=10.218 0.010000

Bond Price Inverted to Reflect Yield 1979 to 1981





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