



Annual Issue Price £150

city@bpr.co.uk

EUROPES BUSH BAITING IS MISGUIDED, AS HE APPEARS TO BE THE ONLY LEADER ADDRESSING HIS OWN COUNTRIES PROBLEMS!

INTEREST RATES & BONDS

Rates to be cut further despite inflation fears
Fear of inflation makes yields rise
The JGB is not ready to short yet

GLOBAL STOCK MARKETS

Don't fight the FED is still the mantra but the Dow & Ftse will be weighed down by overhead trading range.
Watch the CAC and the DAX for clear downtrend breaks.
TMT's are now providing a "once in a lifetime" opportunity.

CURRENCIES

Dollar ready to resume its rally against the Yen.
Pound looks set to weaken vs \$ & €.
Sterling crisis for Blair Govt?

COMMODITIES

Oil to stay above \$26.
Tin & Nickel fall despite backwardation.
Gold explodes out of range as volatility increases.
Soybeans rally.
Cotton hits historic lows.

The recent visit of President Bush to Europe produced all the usual socialist grandstanding and cant by EU leaders. They patronisingly lambasted him for abandoning the Kyoto climate control agreement despite the fact that no EU member has ratified it or hit the emission cuts agreed. This hypocrisy is heightened by the fact that Bush could never of ratified the agreement in the first place. The reason for this is the resounding 99 to nil against by Congress when Clinton presented the agreement in 98. Bush is no fool and was not prepared to waste time and credibility in trying to push through a lame duck agreement which stood a snowballs in hells' chance of being passed.

This common sense stance has angered our EU commissars no end as political correctness has not been served. Bush has however committed an even more heinous crime, he has decided to provide more energy capacity thus putting his countries interests first. What a strange thing for a leader to do when he has rolling power cuts in the worlds 6th largest economy (California)!

Is it any wonder European leaders hate him when he provides such a terrible example to the world's electorate?

Bush has realised that the biggest threat to US growth and thus world growth is a global energy shortage and consequent high cost.

The US energy report states that energy shortages will "undermine our economy, our standard of living and our national security". This is unlikely to be a short-term problem as the report estimates that US energy consumption will increase by 32% over the next 20 years. This is below the global trend of

55% according to OECD figures. To offset this shortfall the Bush proposes easing regulations that block construction of electric, gas, coal and nuclear power plants because conservation alone cannot match demand with supply without undermining the economy. The Californians know full well that this is no scare story.

A dearth of new or modernised refineries is a major cause of the oil shortage (witness backwardation on gasoline contracts and heating oil). Nuclear power has been out of favour since the late 70's and the 3 mile island meltdown. Nevertheless technology has not stood still and maybe nuclear energy may well make a global comeback, as it is clean as long as contamination is avoided.

In the US about 20% of power is generated by nuclear stations compared with 75% in France. This percentage is set to shrink to 12% as old power stations get switched off due to no new permits being granted since 1976. Clearly this will change and although no one supports possible global warning all Governments have to address their own priorities first. This is especially relevant as if the US did have an economic meltdown due to power shortages Europe would suffer terrible economic consequences.

In Europe, I suspect Belgium, Germany, Holland, Sweden and Switzerland will have to reassess their plans to gradually shut down nuclear power industries. Energy is about to re-emerge as one of the most important industries in coming years. Investors should benefit from what may be spectacular re-ratings in energy stocks as well as some speculative opportunities in alternative energy sources.

INTEREST RATES AND BONDS

- **Yet further cuts in short-term interest rates are possible**
- **Long dated bonds in US and Europe are showing inflation jitters**
- **Japans bond market still months away from the short of the decade**

The Fed may not have finished its rate cutting cycle as yet. Despite inflationary pressures the

Fed could still lop another 100 points off short-term rates. However that may not be necessary and it would probably worry the bond market. Therefore any additional rate cuts by the Fed, should they occur, would probably be reversed following two consecutive Quarters of economic improvement. As for the ECB it continues to advertise for economists but could really do with a good P.R. firm. Duisenberg and his acolytes took a hard line on prices only to do a sudden U-turn in May claiming "monetary developments no longer pose a risk to price stability". Of course Eurolands inflation has continued to edge higher, not least because of the euro's weakness. With Q1 GDP coming in below the already downwardly revised official forecasts, there is a contracting growth argument for lower rates. The UK's risk of recession will increase if the Bof E does not continue to lower rates.

Inflation rates have been nudging upward for months due to higher energy costs and now gold has stirred from its slumber. This has led to long dated bonds being sold down as the market fears a threat of stagflation due to over aggressive easing to combat slower growth.

The charts below for US Treasury long bond and the UK Gilt 5% 2009 (shown below) clearly illustrate the weakening of these markets as they discount a pick up in inflation over the next year or so.

The chart for the US Treasury long bond clearly shows a break down through the recent uptrend. The uk gilt also illustrates a very similar break down although the declines may well pause at or around these levels for a little while now

USTREASURY(weekly)



UKGILT5%2009(daily)



Paradoxically, JGB remain much lower with the market retracing over half its recent sell-off. These bonds continue to be supported by the BOJ, Japanese investors hedging against their domestic deflation and capitalisation weighted bond funds. The danger period will arrive when investors see a genuine economic recovery for Japan. The first hint on the charts will come when Japanese bond yields rally to beyond 1.5% on 10yr JGB's. At that point we can enter the great JGB short trade I have highlighted in recent issues. As yet this trade could be many months away and we must content ourselves with simply stalking our prey.

GLOBAL STOCK MARKETS

- **Interest rate cuts have put the bear into torpor**
- **Markets likely to range for months**
- **Japan and technology the best bets over 5year view**

Alan Greenspan has acted very effectively and timely to avoid a Japanese style debt deflation spiral. Historically the best gains for stock markets have occurred during the global cycles of monetary easing and higher rates have caused bear trends. The bullish effect of lower short term rates has only been negated in severe deflations. Greenspan's actions have avoided this danger by his speed and decisiveness in slashing rates. In Europe the ECB jeopardised growth by delaying too long before its u-turn on 10th May. Nevertheless, given the high correlation for Europe's stock markets with the US, downside risk should be limited to a retest of the March lows, at least until investors start to discount the next rise in short term rates which should be many months away. "Don't fight the Fed" has long been one of the market maxims, especially following 5 rate cuts (250 basis points) in less than 6 months. **Thus although one should historically be expecting upside action there is reason to expect this cycle to be sub-normal compared with previous rate cutting cycles.** While problems of growth, valuations and debt are not unique to this cycle, they should not be dismissed lightly. GDP growth a year from now is extremely difficult to forecast but high energy costs are a major concern and would not rule out knock-on effects from the burst TMT bubble, even though the crash of '87 had little economic effect, no doubt due to the decisive monetary easing that followed. Very high valuations in the West result from investors over optimistic expectations following many years of returns above the historic mean. This cannot be maintained without the "new paradigm" a hypothesis that stretches credulity. Corporate debt, encouraged by the fashion for leveraging corporate balance sheets, remains worrying particularly during a global slowdown. I believe the charts reflect these factors, showing considerable overhead supply reflected in the huge trading ranges above current declines, and as yet insufficient base development where prior weakness has occurred. I suspect that we could see many months and possibly years of ranging activity during which the earlier excesses are unwound. This could create an almost market

neutral environment, punctuated by rallies and sell offs in response to interest rate cycles. If so, index tracker funds as offered by certain high profile entrepreneurs and promoting by a Govt obsessed by charges and not performance will be a major disappointment. Good fund managers should have their opportunity to show their mettle. If any stock market outperforms in this environment it is likely to be the Japanese provided the Govt does not backslide on reforms once again. Koizumi was elected on a reform package but if he loses support due to an even weaker economy over the next year or two, which is a real possibility, there are many among the LDP old guard who would love to take his scalp. Meanwhile Koizumi hit the ground running by appointing a non-conformist cabinet. Japanese companies continue to restructure and many are competitively valued on a cash flow basis. The cash rich public, which bought stocks in the late 80's with a gusto to rival the NASDAQ mania of '98 to early 2000, is out of the market today. When they eventually move back into stocks (the pre condition is a clearly established uptrend and an end to deflation) Japanese equities should outperform all other major markets.

Global chart review

The Dow Jones has followed its downside failure in March with a test of the 2 year bands high. This should prove to continue to provide at least temporary resistance and although a break may signal a new all time high it would probably be difficult to maintain

Dow Jones (weekly)



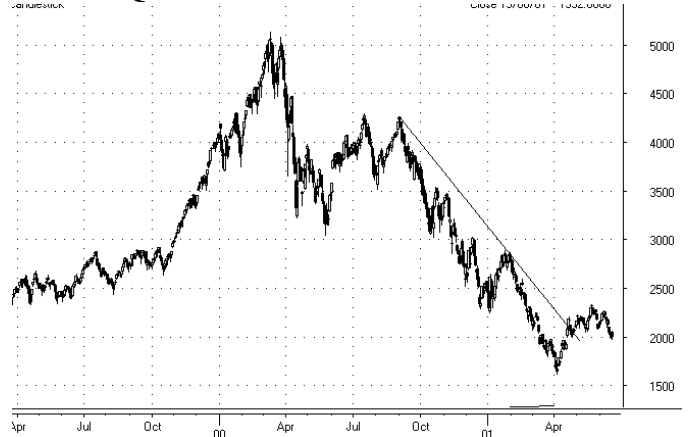
Interestingly the Dow Jones Utilities index has run strongly on to new highs over the last 9 months as investors have dumped "growth" stocks. Part of this performance is simply fashion and partly a catch up from years of underperformance. What it does highlight is the sectoral and rotational nature of current market conditions

Dow Jones Utilities(monthly)



The NASDAQ is currently consolidating its April May recovery gains and appears to be beginning what may prove to be a lengthy base building process. I suspect the low for this market is in and any breach of the 1600 level will prove to be temporary. However I would not be surprised to see a retest of this level. In the meantime I suspect the index may well be capped by the overhead supply evident above 2250.

NASDAQ



The Nikkei has not maintained its April May move perhaps dragged back by yen strength. The lack of follow through suggests that further ranging is likely with the key area to watch is either a break above 14500 or a higher low above 12000. We suspect the Nikkei will be toilsome for some months yet but will ultimately prove to be the strongest market over a 5yr view.

Nikkei (weekly)



Ftse 100 continues to range below the 6000/6600 overhead supply and could do so for some while. Certainly any move above 6000 will produce only snail like progress, as this trading band will provide major resistance. In the meantime we believe that the low of around 5300 should hold. The potential for a strong advance may well be deferred for some months. The other European indices may well give a clearer clue as their declines are chart wise very orderly

Ftse100 (weekly)



As stated last month the DAX and the CAC are both exhibiting very similar consolidation characteristics. The clear and regular downtrends

evident on both will provide very clear and powerful trading signals as and when the trends break. In the meantime the current sell off (20/06) will enable us to tell if the lows are in yet for most of the western markets. If the March lows hold then we have the set up conditions for a strong technical rally on most global markets

CAC (weekly)



DAX (weekly)



SUMMARY

In conclusion most markets look likely to range for some time but some excellent short term trading opportunities may well arise. My personal favourites are long Dax and CAC on breaks above 6250 and 5600 respectively. The Nikkei and the NASDAQ would signal interesting long trades on breaks above 14300 and 2250.

Finally any long term positioning may take a few years to prove fruitful but we favour the now bombed out TMT's and Japan

CURRENCIES

- The Yen's contra-trend rally is over

- **Euro still in decline against the dollar**
- **The pound looks set to weaken further vs the dollar**

Back to square one for Hayami and the yen –

In March, Japanese monetary officials worried the yen was weakening too rapidly. Their jawboning triggered a medium term reaction, as short positions were unwound (including mine). This recreated one of Japan's bigger problems – a currency much too strong given the ongoing deflationary slump. Further jawboning ensued, this time to weaken the yen, particularly against the euro. Markets have taken note and charts indicate that the yens technical rally probably ended on 1st June at 118.28 and 99.98 against the dollar and the euro. Traders may well remain wary for some time, given the euro's flaccid performance and concern over global growth.

However economic problems for the US and Europe are mild compared to Japan's continuing malaise. As for Hayami while emotionally attached to a strong Yen, he can't ignore an economy that contracted 0.2% in Q1 and BoJ's latest comment: "adjustments in economic activity are gradually intensifying as production is declining substantially, reflecting a fall in exports". The Bank repeated its concern that weak demand will extend Japan's deflation; even as the Yen weakens against the dollar and oil prices remain high. It has pledged to keep interest rates close to Zero until prices have clearly ended the 20 month slide. Meanwhile, Prime Minister Junichiro Koizumi has promised to reduce wasteful government spending and compel commercial banks to dispose of bad loans amounting to trillions of yen, even though these steps could slow the economy further in coming months. Needless to say, Japan's enormous budget deficit continues to balloon. Against this background, if Japanese investors continue to save rather than spend and invest, the BOJ will be compelled to increase the supply of yen in circulation dramatically. Short yen against the US dollar and other reserve currencies remains a promising trade, in terms of interest rate differentials and capital appreciation potential. Some temporary resistance can be anticipated

between current levels and the year's earlier highs but downside risk should now be limited to brief reactions and consolidations. we expect the US dollar and the euro to be much higher against the yen in 12 months time

YEN/DOLLAR(daily)comexinverse



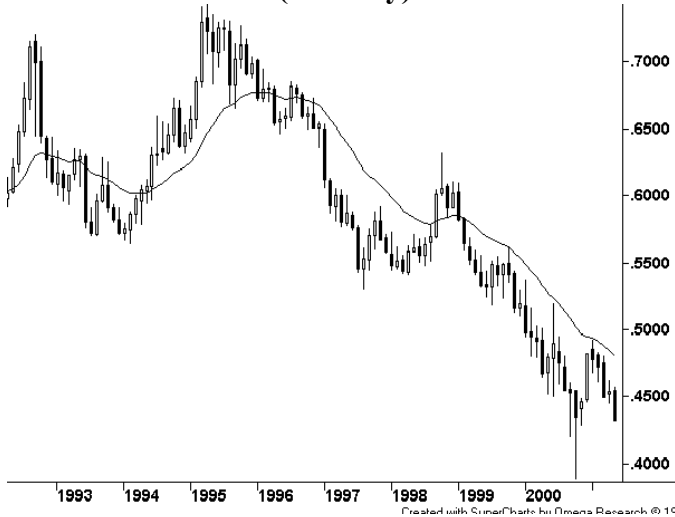
STERLING/YEN



The Euro is still sinking against the dollar and the chart below shows the long term picture against the Dmark. The euro rolled over gently to retest the first explosive leg of the recovery evident in late 2000 (see the monthly buying spike). The fall has been much more gradual than the advance and we suspect that this is a clue to indicate that selling pressure is beginning to ease. The primary trend is still down but major support was established at the Oct 2000 low and should cushion downside risk and may well be the beginning of base formation. Watch for a break of the long-term primary downtrend at around 0.95 to signify higher prices and trend reversal.

The euro may well be held back during this year due to “black economy” cash being converted into hard dollars before the demise of the Dmark at New Year. We think the euro will find it hard to mount a sustained recovery beyond \$0.90 during this process.

DMARK/DOLLAR(monthly)



Sterling has broken to new lows against the dollar and as yet looks set to continue to trend lower. The pound is vulnerable to a typical Sterling crisis due to a growing trade gap, a Government that has Europhile tendencies and planning massive public spending increases just as the economy is slowing. It does look like the Iron Chancellor may follow Jim Callaghan’s fate back in ’67.

The chart below clearly illustrates the pounds latest bout of weakness which looks set to continue as we have a clear downtrend combined with a downside break out of the triangular consolidation pattern. The pound could be shorted with a stop at around \$1.42 if weakness continues, but beware a snap back rally.

DOLLAR/POUND (daily)



The euro is gently trending lower against the pound in a trend channel at present. I suspect a break through the range at €1.62 would lead to a test of the €1.55. It looks the more likely scenario due to Forex dealers suspicion of the UK Govts intentions on actively devaluing the pound in order to allow entry into the Euro and to pander to the devaluationists masquerading as pro-euro business leaders. I would short the pound on such a break with a stop at €1.64.

Sterling/Euro (weekly)



Summary;

1. **Recommence short yen vs dollar**
2. **Short sterling vs dollar**
3. **Short pound vs euro on break of €1.62**

COMMODITIES

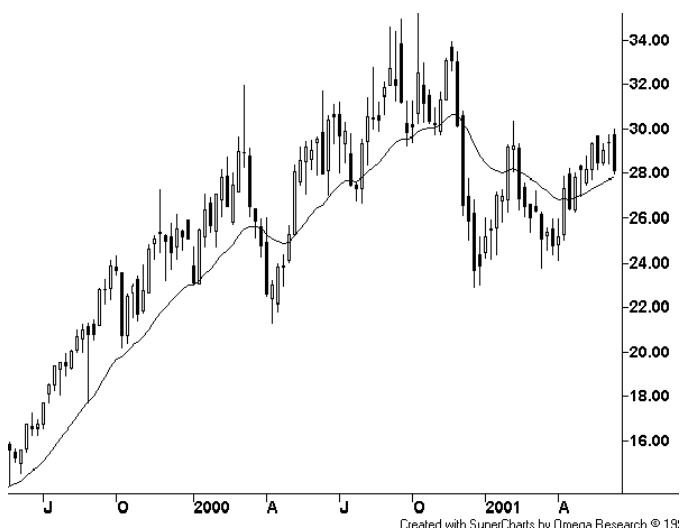
- **Oil remains high supported by OPEC supply cuts**
- **Soybeans rally strongly after last months comments**

- **Cotton hits historic lows**
- **Tin falls despite backwardation**
- **Nickel fails to follow through its price surge**
- **Sugar also has backwardation and may only be pausing**
- **Gold- the fundamentals are improving**

OIL is still trading at or near \$28 despite a global slowdown and this is entirely due to price control by OPEC. This is exacerbated by the western worlds complacency towards energy since the price of oil first slumped in 1985. Western Govts have avoided angering the various interest groups and nimby's and have avoided building new refining capacity and actively decommissioned Nuclear power generation.

California now has much publicised rolling power cuts like the UK did in the bad old 70's. That new demon of the "Liberal left" Bush has seen through all the bull and has ordered new refining capacity, further extraction/exploration and more nuclear generating. However new capacity takes time to come on stream so for the interim OPEC will have some power over prices and hot spots will occur in the Heating oil and natural gas markets.

Brent crude oil(weekly)



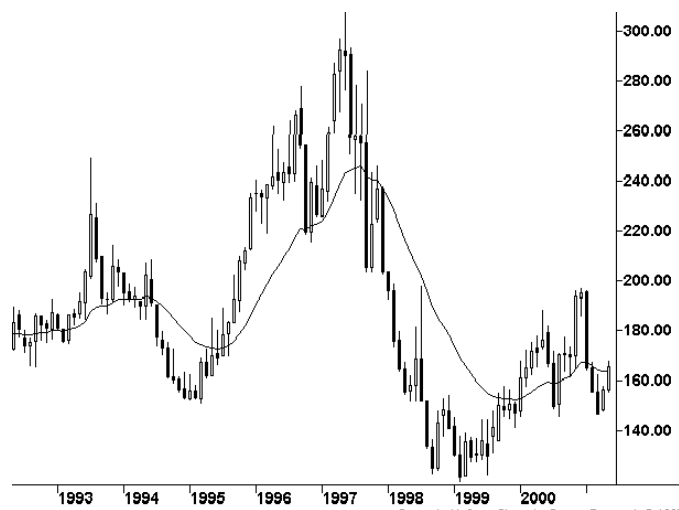
Crude prices look a bit toppy but have found support at the \$24/\$25 area twice this year and as such continued ranging is likely.

Soybeans have rallied strongly since last months tip about a possible rally due to backwardation. which still persists. Although the current run looks like it may be due a consolidation (watch a break below 165 to stand aside but new highs would be significant) the monthly chart shows that the price is still historically low.

SOYBEAN MEAL (daily)



SOYBEAN MEAL (monthly)



Wheat (corn is almost identical) which we show below has traded near historic lows for some time now and as yet there has been no upward dynamic BUT any break above \$300 would be extremely bullish..... we may have to bide our time though, so adopt a wait and see approach.

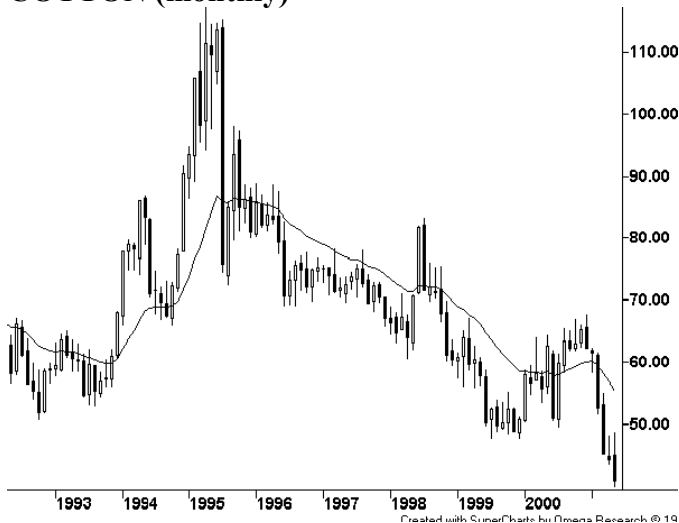
WHEAT(monthly)



COTTON

We always find any market that hits a new historic low or high very interesting as some bubble activity or over reactive selling has occurred creating set up conditions for a possible contra-trade. This rule applies more to commodity markets than any other. Thus cotton hitting new lows is of immense interest as one can simply note and watch awaiting developments. As the chart below shows cottons bear has seen multi-year lows and is now below 40.00 on the daily chart. It is looking very oversold now.

COTTON (monthly)



Both TIN and Nickel have backwardation at present and as yet continue to fall back The strong move up in Nickel highlighted last month has, as predicted last month “petered out”. However the sell off as yet has not eradicated the backwardation present between the cash price and the 3month price (backwardation is a higher cash

price than future price indicating excess short term demand) So what is the market telling us in both these metals? We suspect that further short-term rallies are due but we’re not convinced the overall trend is about to reverse into bull mode

NICKEL (weekly)



TIN (weekly)



SUGAR as can be seen below has already had a strong move and appears to be pausing in the up trend. A move above \$9.50 could well signal a resumption of the up trend



GOLD

As stated in this publication for many months once gold broke out of its downtrend a fast move to around \$300 was likely. However we did not anticipate how fast this move might be and how volatile the action would prove to be. we personally bought gold on the break but made only a little profit due to the rapid retracement.

The important fact is however that gold is at long last showing signs of a pulse and is slowly ending the bear.

We suspect gold will range gently higher from now on with \$340 being the first resistance cap if any strong rally should explode like last months.

Gold will draw solace from a behavioural and generational change in the attitude towards inflation. People and Central Bankers are now more afraid of deflation and so over the current slow down will err on the side of too much rather than too little monetary stimulus. Fearing deflation the Fed is currently easing aggressively and a future fear of inflation which may monetise gold

Gold (weekly)



FINALLY

As ever we welcome all your comments and e-mails and any investment or trading stories. I (amc) apologise for the late production of this issue but I have been sunning myself in the Med.

GOOD HUNTING

BEST REGARDS

Andrew McCarthy & Andrew Bartles