QUICK PIVOT

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STOCK MARKETS

Our research has been dealing with two aspects in the markets. One is the All-One-Move (AOM) and the action has become extreme. This has been on for a couple of weeks and now the excessive condition is irrevocable. As the saying goes--the tattoo machine does not have an eraser.

The other aspect has been timing and our Gold/Commodities Index (GCI) has usually been a reliable indicator. But, the action in commodities has not been coordinated but has come in compulsive surges. This has interrupted the uptrend that would have provided a valid signal. The irony is that the GCI will go up, providing the signal, and then soar.

Although our advisory research has been dealing with the foreseeable future since 1980 sometimes we are too early on a call.

However, Ross's work on the Dollar Index has a longer track record than what we have on the GCI. The Downside Capitulation signal on the DX has been reliable. The following couple of pages reviews the lead from the signal, which can be up to 10 days. That's for the reversal in currencies and in the stock markets.

An intermediate decline has been expected to follow.

COMMODITIES

"Investors Thirsty for Commodities – Seen as a Safe Haven"

This was from today's Financial Post and such exclamations are likely universal. The accompanying move in the CRB (commodities) chart is also exclamatory. The action is very close to generating a daily Upside Exhaustion signal. Within the sector, wheat recorded the reading on its spike into early August. As of today, sugar's ETF (SGG) registered an Exhaustion. The last such signal on the CRB occurred on the top day on the cyclical high in 2008. We take this as an "irrevocable" condition that can only be relieved by a decline.

Even the simple RSI is at 80, which is the highest since 2008. This is interesting because the clamor about commodities, which has the Fed's blessings, is the most urgent since the record high for the CRB in the fateful year of 2008. Commodities are now at 300, which compares to 294 at the January high and to 474 at the record high. It looks like a big test of only the January level, but with considerably more emotion made worse by the huge tout from the Fed.

An intermediate decline will likely follow.

CURRENCIES

We should go back to the Downside Capitulation for the dollar registered at 80 in early August. Ross noted that if it wasn't a major low the bounce would carry to 83 and then test the low.

The following reviews the record:

The downside Capitulation Alerts starting on October 1st in the US Dollar Index are a normal precursor to an interim low in the currency and a concurrent top in gold and mining stocks. We are at the ninth trading day since the first alert. Previous currency reversal have been in place by the 10th day. (Charts were included in the October 4th edition of ChartWorks)

- Nine of the occurrences since 1975 saw the Dollar rally back to the 20-day exponential moving average, followed by a test of the low (*quite often a 'Spring' of the support*) and then a larger rally back to the 50-day ema.
- Seven times saw a rally straight to the 50-day ema.
- Three had rallies capped at the 20-day ema and then continued lower.

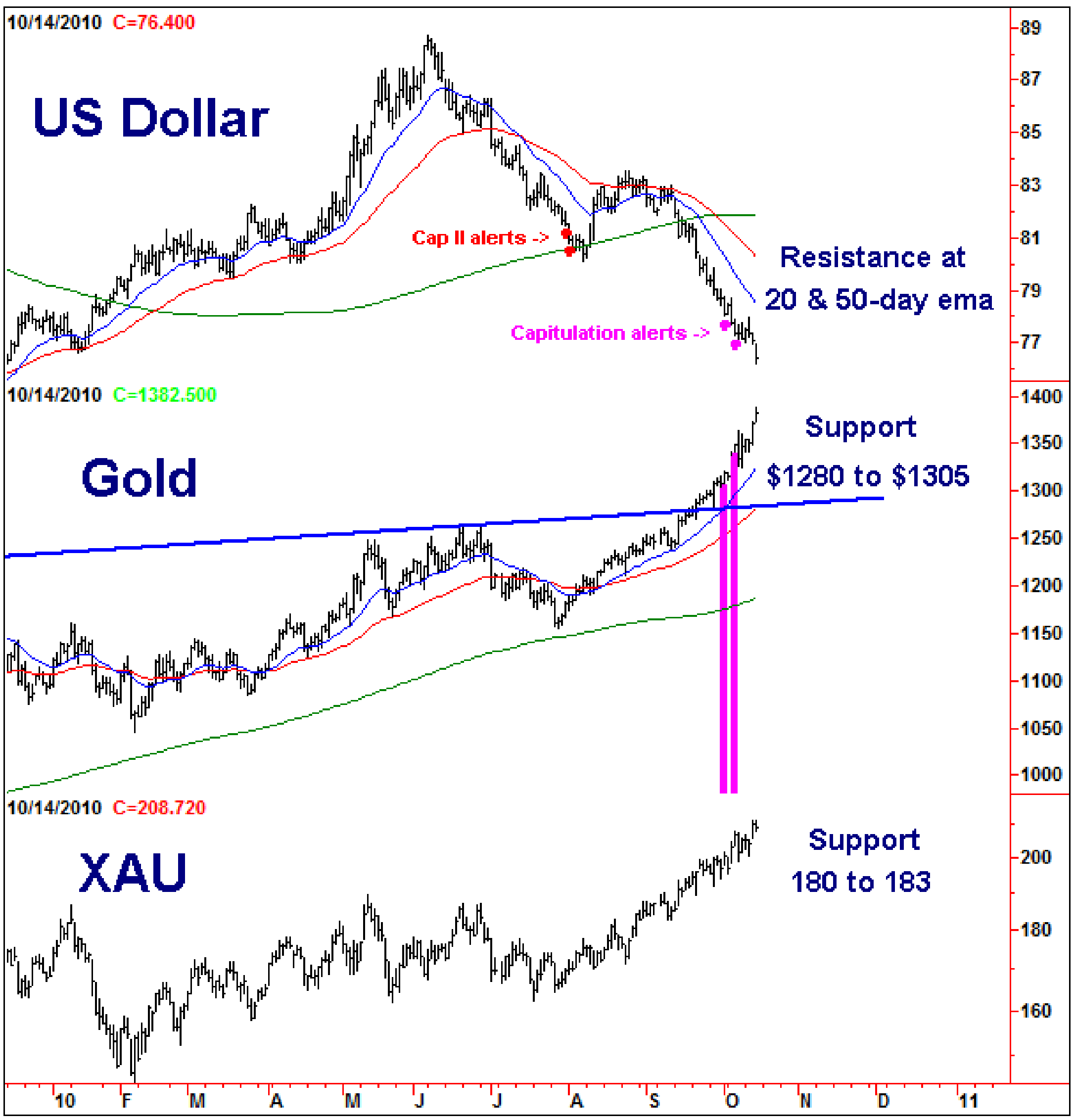
The moving averages currently sit at 78.50 and 80.25.

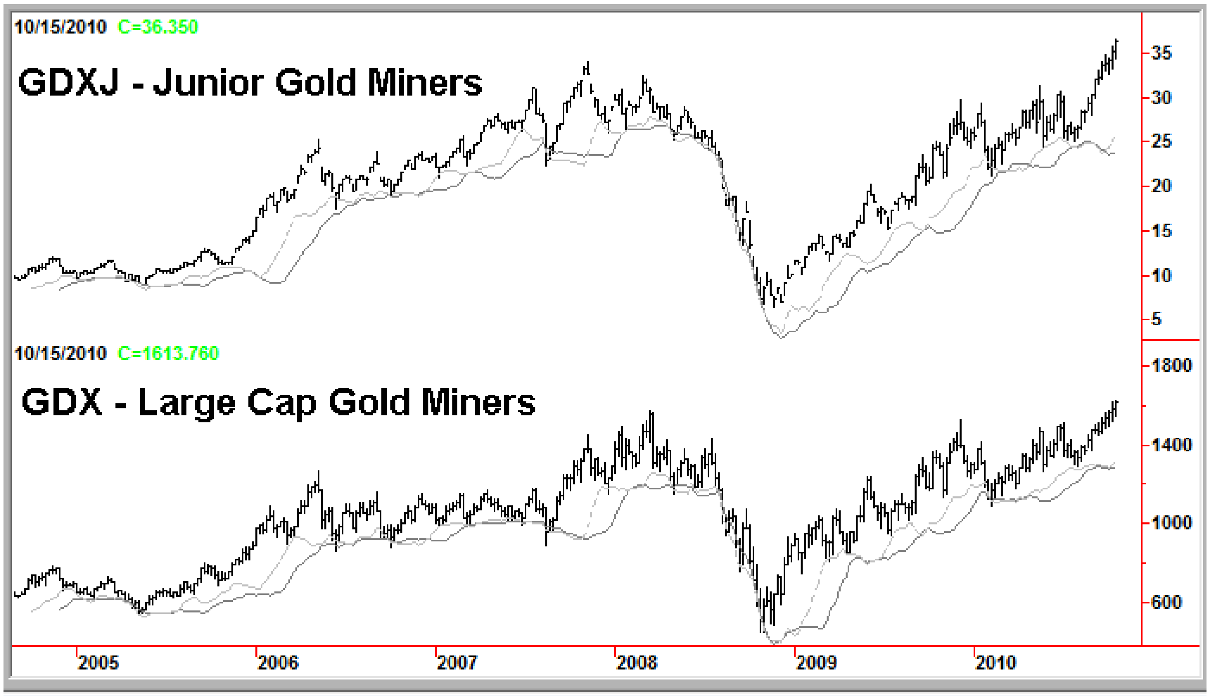
Capitulation alerts and subsequent trading days to an interim low in the Dollar and concurrent highs in gold and the XAU

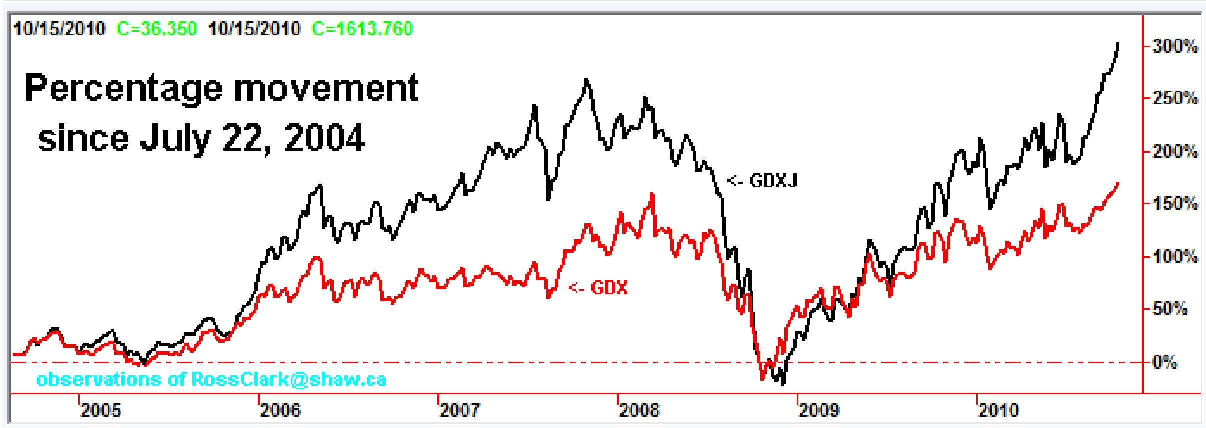
First day	Days to bottom	Days to top	
of alert	US Dollar	Gold	XAU
7/11/1977	9	18	18
8/14/1978	2	0	0
10/18/1978	8	8	8
7/18/1979	4	4	0
11/29/1985	0	0	0
2/19/1986	9	3	4
7/2/1992	10	11	10
10/25/1994	1	0	0
3/7/1995	0	6	na
10/8/1998	6	0	0
6/25/2002	3	0	0
5/12/2003	10	7	7
1/5/2004	4	4	0
1/23/2004	8	8	0
5/5/2006	5	5	3
4/16/2007	6	3	0
7/17/2007	5	5	4
10/31/2007	5	6	4
10/1/2010	9?		

The gold and mining stocks (*Homestake until 1983, then XAU*) topped in the same time frames as the Dollar. A correction in bullion should find good support in the range of $1280 to $1305. The stock indices have supports as follows:

	First support	Secondary support
XAU	183	180
HUI	480	460
GDX	53	51.25
XGD.TO	23.60	22.80
ZJG.TO	18.20	17.35







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The charts are interesting and supportive of an intermediate change in the currency markets. This is confirmed by some sentiment numbers. Our bottoming pattern on the DX worked well at the low of 70 in early 2008. Then the Daily Sentiment reading had declined to 6% bulls. On the next one at 74.23 in late 2009 bulls were down to 3%. Now, with the dollar working on what could be an important low at the 76 level sentiment is again down to 3 percent bulls.

On a series of pattern-bottoms the lows have increased from 70 in 2008 to today's at 76 – as the sentiment reading has become more extreme in dropping from 6% to only 3%.

On the move to yesterday, the Canadian dollar almost made it to par. The consumer and financial historian inclinations of this writer says "great!". But the C$ will likely decline on the currency change to the 97 level.

INTEREST RATES

As the saying goes, politics makes for interesting bedfellows. Some asset prices that usually trade opposite to each other have been rising together. In June the bond price was 124.25 yielding 4.14% and the CRB was at 249. Now the numbers are 133.34 and 3.83% -- with the CRB up to 300.

What's happening, of course, is price inflation in as many asset classes as policymakers can accomplish. Trouble is that they only understand inflation in the Consumer Prices and still don't understand inflation in stocks, long treasuries and corporate bonds.

After bouncing off the 130 level, the long bond was likely to test the high at 136.84 and it made it to 135.34. The latest surge in stocks and commodities took it down to 132.6.

Should stocks and commodities decline next week, the bond can give the 137 level a good test.

In the corporate sector, junk has declined in yield to 11.05% which compares to the best obtained in the party to April. This was 10.88% with the spread at 621 bps over treasuries. Now the spread is at 722 basis points.

Are treasuries out of line, or is some caution coming into the high-yield market? Time will tell.

GOLD SECTOR

The ChartWorks has been frequently covering opportunities in bullion prices and gold stocks.

Of importance is the forecasting that the gold/silver ratio can provide. A turn to going down indicates a rally in stocks, commodities and corporate bonds.

This was the case in August when the rise in the ratio did not get through 68. Breaking above that level would have indicated another – even minor – phase of contraction. In looking ahead, rising through 68, along with some other indications, would signal some credit problems.

Declining to 55.9 today has been instrumental to the party.

In looking at it the other way, the silver/gold ratio reached an RSI momentum peak at 80. This is now being tested and a decline in momentum would suggest a turn down in the ratio which would signal a setback in most markets.

Quite likely a turn would be anticipated by silver stocks underperforming the move in the bullion price.

INFLATION

Each of the asset rallies prompts serious concerns that hyperinflation is inevitable as the dollar slides to zero.

Art Cashin at UBS has an outstanding reputation as a trader and a wit. His Wednesday article provides a competent summary of the Weimar inflation. It is worth adding that leading economists in Germany fiddled around with the real money supply and wrote that the government should issue more. Real money supply was not growing fast enough for those economic savants.

After destroying the middle class, policymakers ran out of the will to keep the mania going and quit.

With the US still having the largest credit market in the world, bond vigilantes will prevent the Fed and Treasury from actually going to the real printing press debasement.

At some point the public and the markets will persuade desperate policymakers to quit their madness.

	FRI	MON	TUES	WED	THUR NOON
OCTOBER	**8**	**11**	**12**	**13**	**14**
BBB Spread	369	---	363	354	----
Treasury Curve	341	---	344	347	345
Base Metal Prices	674	692	691	707	708
Dollar Index	77.4	77.2	77.5	77.3	76.6
Gold	1347.2	1353.8	1350.5	1372.1	1373
Gold/Commodities	364	360	358	361	----

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Art Cashin On The Coming Hyperinflation

We present today's thoughts by Art Cashin on the coming hyperinflation (and **no**, it does not mean very high inflation - it means a complete and total collapse in the monetary system - which is what Ben Bernanke is attempting to achieve), without commentary.

AN ENCORE PRESENTATION

(Today we will revisit one of the most devastating economic events in recorded history. It all began with the efforts of a few, well-intentioned government officials.)

Originally, on this day (-2) in 1922, the German Central Bank and the German Treasury took an inevitable step in a process which had begun with their previous effort to "jump start" a stagnant economy. Many months earlier they had decided that what was needed was easier money. Their initial efforts brought little response. So, using the governmental "more is better" theory they simply created more and more money.

But economic stagnation continued and so did the money growth. They kept making money more available. No reaction. Then, suddenly prices began to explode unbelievably (but, perversely, not business activity).

So, on this day government officials decided to bring figures in line with market realities. They devalued the mark. The new value would be 2 billion marks to a dollar. At the start of World War I the exchange rate had been a mere 4.2 marks to the dollar. In simple terms you needed 4.2 marks in order to get one dollar. Now it was 2 billion marks to get one dollar. And thirteen months from this date (late November 1923) you would need 4.2 trillion marks to get one dollar. In ten years the amount of money had increased a trillion fold.

Numbers like billions and trillions tend to numb the mind. They are too large to grasp in any “real” sense. Thirty years ago an older member of the NYSE (there were some then) gave me a graphic and memorable (at least for me) example. “Young man,” he said, “would you like a million dollars?” “I sure would, sir!”, I replied anxiously. “Then just put aside $500 every week for the next 40 years.” I have never forgotten that a million dollars is enough to pay you $500 per week for 40 years (and that’s without benefit of interest). To get a billion dollars you would have to set aside $500,000 dollars per week for 40 years. And a…..trillion that would require $500 million every week for 40 years. Even with these examples, the enormity is difficult to grasp.

Let’s take a different tack. To understand the incomprehensible scope of the German inflation maybe it’s best to start with something basic….like a loaf of bread. (To keep things simple we’ll substitute dollars and cents in place of marks and pfennigs. You’ll get the picture.) In the middle of 1914, just before the war, a one pound loaf of bread cost 13 cents. Two years later it was 19 cents. Two years more and it sold for 22 cents. By 1919 it was 26 cents. Now the fun begins.

In 1920, a loaf of bread soared to $1.20, and then in 1921 it hit $1.35. By the middle of 1922 it was $3.50. At the start of 1923 it rocketed to $700 a loaf. Five months later a loaf went for $1200. By September it was $2 million. A month later it was $670 million (wide spread rioting broke out). The next month it hit $3 billion. By mid month it was $100 billion. Then it all collapsed.

Let's go back to "marks". In 1913, the total currency of Germany was a grand total of 6 billion marks. In November of 1923 that loaf of bread we just talked about cost 428 billion marks. A kilo of fresh butter cost 6000 billion marks (as you will note that kilo of butter cost 1000 times more than the entire money supply of the nations just 10 years earlier).

How Could This All Happen? – In 1913 Germany had a solid, prosperous, advanced culture and population. Like much of Europe it was a monarchy (under the Kaiser). Then, following the assassination of the Archduke Franz Ferdinand in Sarajevo in 1914, the world moved toward war. Each side was convinced the other would not dare go to war. So, in a global game of chicken they stumbled into the Great War.

The German General Staff thought the war would be short and sweet and that they could finance the costs with the post war reparations that they, as victors, would exact. The war was long. The flower of their manhood was killed or injured. They lost and, thus, it was they who had to pay reparations rather than receive them.

Things did not go badly instantly. Yes, the deficit soared but much of it was borne by foreign and domestic bond buyers. As had been noted by scholars….."The foreign and domestic public willingly purchased new debt issues when it believed that the government could run future surpluses to offset contemporaneous deficits." In layman's English that means foreign bond buyers said – "Hey this is a great nation and this is probably just a speed bump in the economy." (Can you imagine such a thing happening again?)

When things began to disintegrate, no one dared to take away the punchbowl. They feared shutting off the monetary heroin would lead to riots, civil war, and, worst of all communism. So, realizing that what they were doing was destructive, they kept doing it out of fear that stopping would be even more destructive.

Currencies, Culture And Chaos – If it is difficult to grasp the enormity of the numbers in this tale of hyper-inflation, it is far more difficult to grasp how it destroyed a culture, a nation and, almost, the world.

People's savings were suddenly worthless. Pensions were meaningless. If you had a 400 mark monthly pension, you went from comfortable to penniless in a matter of months. People demanded to be paid daily so they would not have their wages devalued by a few days passing. Ultimately, they demanded their pay twice daily just to cover changes in trolley fare. People heated their homes by burning money instead of coal. (It was more plentiful and cheaper to get.)

The middle class was destroyed. It was an age of renters, not of home ownership, so thousands became homeless.

But the cultural collapse may have had other more pernicious effects.

Some sociologists note that it was still an era of arranged marriages. Families scrimped and saved for years to build a dowry so that their daughter might marry well. Suddenly, the dowry was worthless – wiped out. And with it was gone all hope of marriage. Girls who had stayed prim and proper awaiting some future Prince Charming now had no hope at all. Social morality began to collapse. The roar of the roaring twenties began to rumble.

All hope and belief in systems, governmental or otherwise, collapsed. With its culture and its economy disintegrating, Germany saw a guy named Hitler begin a ten year effort to come to power by trading on the chaos and street rioting. And then came World War II.

We think it's best to close this review with a statement from a man whom many consider (probably incorrectly) the father of modern inflation with his endorsement of deficit spending. Here's what John Maynard Keynes said on the topic:

By a continuing process of inflation, governments can confiscate, secretly and unobserved, an important part of the wealth of their citizens. By this method they not only confiscate, but they confiscate arbitrarily; and, while the process impoverishes many, it actually enriches some…..Those to whom the system brings windfalls….become profiteers.

To convert the business man into a profiteer is to strike a blow at capitalism, because it destroys the psychological equilibrium which permits the perpetuance of unequal rewards.

Lenin was certainly right. There is no subtler, no surer means of over-turning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million is able to diagnose….By combining a popular hatred of the class of entrepreneurs with the blow already given to social security by the violent and arbitrary disturbance of contract….governments are fast rendering impossible a continuance of the social and economic order of the nineteenth century.

To celebrate have a jagermeister or two at the Pre Fuhrer Lounge and try to explain that for over half a century America's trauma has been depression-era unemployment and deflation while Germany's trauma has been runaway inflation. But drink fast, prices change radically after happy hour. And, tell Fed Chairman Bernanke that it was the "German Experience" that caused many folks to raise an eyebrow when he alluded to the power of the "printing press" a few years ago. But, rest assured that no one would let it happen again.