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WEEKEND REPORT (02/08/09)

There isn't a lot of good news floating around out there. It's "earnings season" and a good balance sheet is harder to find than the last dodo bird. Even though analysts have lowered their respective projections to obscene levels, in most cases it's not low enough. On Friday alone we saw analysts projecting a 525,000 drop in non-farm payrolls while the report came out at 598,000, the highest since 1974. The unemployment rate jumped from 7.2% to 7.6% as job losses were spread out across the economy. Also, it was learned that job losses in 2008 exceeded three million and that's with government book keepers! Imagine how high it would be if someone actually published an accurate account. Finally, things aren't getting any better for the consumer, as consumer credit fell by US \$6.6 billion in December versus expectations for a \$3.5 billion drop. November was revised down to an \$11 billion drop from a \$7.9 billion, and that is the largest since they began keeping records in 1943.

Things continue to deteriorate and yet analysts continue to speculate if the worst is out there and we've finally seen a bottom. I might be willing to expect a bottom if this were a recession, even a sever one, but that just doesn't seem to be the case. I think the United States has entered a depression, and my only question is whether or not they are leading or following the rest of the world toward economic chaos. Notice this is different than coming out and saying they are the cause of the problem; of course they are the cause of the problem. They sold hundreds of trillions of dollars of worthless paper to the rest of the world and now it is coming back to haunt them, but that doesn't mean they'll go over the cliff first.

This could very well explode first in Europe or Asia, and *then* in the US, once the rest of the world realizes they don't have any reserves.

The entire world is faced with a credit/financial crisis and there is no easy solution. The United States is trying to resolve the problem by pouring trillions and trillions of fiat dollars down a bottomless banking hole and as



you can see on this five-year chart of the Banking Index, not much has changed. As bad as this chart is, there is still more bad news. Of the trillions of dollars given to the select few financial institutions, I think it would be fair to say that not one penny filtered through to the general public. Citibank received more than US \$300 billion and still fired 80,000 people, so who are they saving. Then we have to deal with how the money was issued. It was reported yesterday by the Chairperson of the TARP Oversight Committee that Mr. Paulson gave more the US \$250 billion of

taxpayer money to banks in return for US \$175 billion in assets (marked at face value). When someone asked the Department of Treasury about it, they issued a terse statement saying they “saved the financial system”. Now you know why Paulson was insisting on immunity.

So, the US spent \$3 to \$5 trillion dollars and has nothing to show for it. What is the rest of the world doing about the current crisis? They have also poured billions of Euros, Yen, Yuan, and Swiss Franc’s into a bottomless pit, and if the following chart of Barclays Bank is any indication, they are



not any better off than the Americans. Judging from what I have read about in Spain, Italy, and Ireland there is no trickle-down effect here either. There is one difference though between the US and the rest of the world, and that has to do with the rate of savings. The rest of the world

saves anywhere from 10% (Europe) to 30% (China) of their income, while the US has maintained a negative savings rate for years.¹

Finally, I would like to call your attention to a recent phenomenon, I call it that because I don't have a good explanation, and I've been following with some interest. Take a look at the following chart for the Baltic Dry Index:



This Index is important because it measures the demand for shipping capacity versus the supply of dry bulk carriers. Because dry bulk primarily consists of materials that function as raw material inputs to the production of intermediate or finished goods such as concrete, steel, and food, the index is also seen as an efficient economic indicator of future economic growth and production. The **BDI** is termed a leading economic indicator

¹ I suspect this changed recently and Americans are now finally beginning to save.

because it predicts future economic activity. After losing more than 90% of its value in just six short, painful months, the Index has risen from the December 2008 low of 663.00 to Friday's closing high of 1,498.00. That is more than a 110% gain in less than sixty days! So this begs the question: is the BDI predicting an economic turnaround?

In order to find a reasonable explanation, I want first to look at the US equivalent of the BDI and that would be the Transportation Index:



Whatever signs of recovery that one might want to see in the BDI are clearly not reflected in the Transportation Index, as it posted a new bear market low just one week ago. Likewise you would expect to see signs of

\$WTIC (Oil - Light Crude - Continuous Contract (EOD)) INDX © StockCharts.com

6-Feb-2009

Op 41.00 Hi 42.68 Lo 38.60 Cl 40.17 Chg -1.00 (-2.43%) ▼



an economic recovery reflected in increased demand for oil and the resultant higher price for crude, and that is not the case. So what is the explanation for the rise in the BDI? My best guess is that China is buying up selected raw materials needed to feed its population, while at the same time keeping their workforce active. This is not reflected in the rise in commodities prices because overall world demand is still declining. Again, this is just a guess and I would welcome your opinions.

The financial markets are always full on conundrums and another that has captured my attention for quite some time involves the path of the US dollar. The rise did not surprise me and I even projected it due to the onset



of deflationary pressure, and I know there is no “dollar handbook” where you can look for behavioral guidelines, but I am somewhat surprised at the current resilience. Every market action/reaction carries with it a message about some future event. My job is to try and decipher that message and thereby profit by an accurate interpretation. For more than two months I have been getting mixed signals that I have chalked up to distribution, but something keeps nagging at me as if there is more to it and I am missing the big picture.

Ask yourself the question what can make the dollar sustain a rally over a longer period of time and you’ll come up with a short list of answers:

- The US has stopped printing dollars and is going to live within a balanced budget,
- Most of the world's debt is denominated in dollars and that puts upward pressure on the greenback,
- The US is viewed as emerging from a recession and their economy is in the process of turning around, or
- As bad as things are, the rest of the world's fiat currencies are viewed as an even bigger risk than the dollar, especially since the dollar was the reserve currency for decades, and that remains engrained in the minds of billions of people.

From the beginning of the dollar reaction, I maintained the dollar would rally for a three to six month period as the rest of the world tried to accommodate their dollar denominated debt payments. Once this was done, the dollar would then continue the seven year decline that began back in 2001.

Several days ago I received an e-mail from a client asking me if I thought the Euro could be in danger of collapsing. That single question caused a little light bulb to go on and the fog to lift. I was living in Italy when the Euro first came out and I had all but forgotten my prediction that it would never last. As part of our human nature we are ethnocentrically oriented and that will not change any time soon. If you expect that historical enemies could live together with one currency, one set of laws, and one economy then you just don't understand human nature. Yes, you can unite in order to overcome some natural disaster or resolve a specific problem, but I don't think you can come together on a permanent basis. Too much water under the bridge! Going back to the dollar, perhaps more than a rising dollar we are seeing a falling Euro (or Yuan) and that is causing people to search for greenbacks. Old habits die hard! I know that in Peru, as well as several other Latin American countries, the switch back to the dollar has been compelling and clear cut. Before they were searching out Euros or local currencies, but now they want greenbacks. I also know that sixty-five percent of all debt in Latin America is in dollars, while seventy-five percent of all income is in the local currency, and that exacerbates any problems due to the world wide crisis.

Right now the March US Dollar Index has been range bound, trading between good resistance at 87.53 and strong support at 85.32, and once the



dollar breaks out of this range we'll have the answer to the question of which ship will sink first. You can see from the red and blue dashed trend lines that I have drawn in that the trading range is being compressed, and in a bear market the odds favor a break to the downside. Meanwhile, the tertiary reaction to the upside (solid red and blue lines) continue to rise and will break out to the upside if the Euro is in trouble. On Friday we saw that

SUPPORT

RESISTANCE

US DOLLAR

85.32
 84.61
 84.05

86.02
 86.50
 87.53

the March US Dollar Index futures contract fell .71 to end the session and the week at 85.64. The intraday low was 85.35 and just above the strong support at 85.32. By all rights, and under normal market conditions, this support should not hold, but we'll just have to wait and see. Also, it is hard to comprehend, but we must be constantly aware that the Euro could possibly be in worse shape than the dollar.

Other paper assets will not fare well in the current environment and that includes the stock market. Don't kid yourself into thinking a rising dollar would be good for the US markets. The last thing a debt ridden economy like the United States wants to see is a stronger currency. That increases their debt in real terms. The Dow Jones has been ebbing and flowing over



the proverbial line in the sand now for several weeks. Depending on who you ask, that line is the Fibonacci support at 8,144 or the psychologically important 8,000 not that it matters all that much. What is important is that the primary trend is down and will remain that way as long as the Dow stays below 9,063. On Friday the March Dow futures contract closed up 260 points at 8,254 and a long ways below 9,063.

Right now the government is doing everything possible to change the trend from bearish to bullish, and one of the things they have in mind is to reestablish the uptick rule. For years you could only sell a stock short when the price ticked up, but that was eliminated several years back. Now some folks want to reestablish the rule in the hope it will stem the decline. In my opinion it will change nothing over the long run, but could produce a short term rally and that might have already started on Thursday in anticipation of the change. It is too early to tell. The market certainly isn't

	SUPPORT	RESISTANCE
<i>DOW JONES</i>	8,241	8,315
	8,144	8,455
	7,940	8,679

rallying due to general market conditions. If such a change is made then I would expect to see the reaction continue to 8,455 on the low side and 8,850 on the high side. If no such change is made then the current reaction should run its course Monday with a high between 8,315 and 8,455. Once the reaction comes to an end, it will offer yet another good shorting opportunity. Change in the rule or not, we will test strong support at 7,470 and I believe the market will fall a lot lower.

Given everything I've said about the dollar, the Euro, and the Dow, is there something you can do to protect your wealth? I can answer that question with one word... gold! I believe we are about to enter the worst phase of the depression that has already begun and the only way to defend yourself is with gold. Almost no one has been talking about it but all of the sudden several large institutions came out late this week and recommended

it. Until now, gold has quietly climbed a wall of worry with little or no fanfare and that's how I like it. *On Friday the April gold closed up .10 as it*



ended the session and the week at 914.30 after numerous attempts to push it back down below strong support 912.30. Note that this is the second consecutive close above this number, and that is quite bullish! I have posted a daily chart for the spot price of gold and you can see that the trend is clearly up. Pay particular attention to the blue arrow I inserted just above the 850.00 mark. This highlights the fact that the 50-dma is about to cross back above the 200-dma, and when that happens it will be very bullish indeed.

I can't tell you how much I like gold right now, but I can tell you that I like silver even more. Take a look at the daily chart for silver below and you'll see that the spot silver price has broken out to the upside:



Two weeks ago the March silver announced its intentions when it moved above strong resistance at 11.68 and then this week it broke through good resistance at 12.57.² Now the March silver is up against strong resistance at 13.35 but I suspect we'll move through it within a week or so. To my way of thinking, I continue to see silver as the cheapest thing out there and

² On Sunday night I will post all the Fibonacci numbers for the March Dow, March US Dollar, March oil, April gold, March silver, and more on the website. These will serve as a valuable roadmap for the concerned investor.

a good way to protect yourself from the coming financial tumult. For an unbiased idea as to silver's upside, take a look at the Point & Figure chart posted below:

Silver - Continuous Contract (EOD) (\$SILVER) INDX
 06-Feb-2009, 16:00 ET, daily, O: 12.865, H: 13.18, L: 12.74, C: 13.16, Chg: +0.41 (3.22%)
P&F Pattern Double Top Breakout on 16-Dec-2008
 Traditional, 3 box reversal chart
 Prelim. Bullish Price Obj. (Rev.): 21.5
 © StockCharts.com



You'll see that there is a bullish price target of 21.50 and that is a lot higher than Friday's closing price. I am the first one to tell you that I am biased, but I don't think you can own enough gold and silver at this point in time and the coming events will prove me right.

Dow Theory Analysis SAC
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Feb. 08, 2009

A few well chosen words from one of the wealthiest and most intelligent men in Mexico:

Gold: The Protector and Creator of Jobs

Hugo Salinas Price
Feb 6, 2009

Some readers may ask themselves, "What has gold to do with protecting jobs? Gold hoarders are certainly not creating jobs, and hoarding more gold will not help at all."

Gold has everything to do with the loss of jobs in the US, and gold has everything to do with recovering jobs for the US economy.

Let me go back to the 60's. During those years, the US and the world were on a Gold-and-Dollar Standard.

Back in the 60's, countries were very careful about maintaining a constant monetary balance between their exports and their imports. They all wanted to be in a situation where they would export more than they imported, so that they would have increasing balances of gold or dollars in their Treasuries.

To state this more correctly, they all wanted to export more than they imported, *except the United States*.

The US didn't care very much about maintaining a balance between exports and imports, because the US was able to pay for its deficit in trade (more imports than exports) by simply sending more dollars overseas.

Many economists warned about this trend, which was accompanied by a constant loss of gold during those years; some countries, notably France, refused to hold more and more dollars. The French asked for their gold - at \$35 dollars an ounce - and this caused great disgust in Washington, D.C. and New York.

Nothing was done to stop the trend. In 1971, Henry Hazlitt, a good conservative economist, warned that the dollar would have to be devalued - that it would be necessary to raise the number of dollars which would be needed to obtain an ounce of gold - some months before the dam broke and the US was faced with the need to devalue, because the US stock of gold had become much too small.

What Mr. Hazlitt never imagined, was that instead of devaluing - which was the advice of economist Paul Samuelson, Nobel Prize winner, published the week before August 15, 1971 - Nixon followed the advice of Milton Friedman and simply "closed the gold window". The US would henceforth not deliver any gold, at any price, to any foreign Central Bank who might wish to invoke the right to redeem its dollars for gold, according to the Bretton Woods Agreement of 1944.

Since that date, all world trade - or the better part of it - is carried on in dollars which are nothing more than fiat money. Since the rest of the world's currencies were tied to gold through the dollar, all the currencies of the world also became fiat money - fictitious money, backed by nothing. That includes the Euro, of course.

What happened after that fateful date has overturned all order and harmony in economic relationships between the nations of the world.

Countries around the world began to accumulate more and more dollars as credit expansion in the US went forward, implacably. Central Banks had to accumulate these dollars in their Reserves, whether they wanted to or not. (Not having sufficient dollars would force other countries to devalue and destroy savings. The US cannot run out of dollars, it manufactures them.)

With no loss of gold to restrain the US and force it to stop expanding credit, US imports surged and exports waned. The monetary difference was "paid" in dollars.

Free trade was extolled by the US; every country that wanted to be in the good graces of the US had to bow to "free trade".

Free trade is a good thing - but not for a country that is providing the world's fiat money. This "free trade" was called "globalization", meaning that the US could, and did, buy everything it wanted in the world, in any amount, at any time, by simply paying dollars for it.

There was no restraint to US credit expansion. It was a lovely time to be young and an American.

However, free trade means you buy where it's cheapest, and the cheapest place to buy, in recent decades, was China, South East Asia and India; the oil required to fuel the US economy was cheap and bought with dollars which it cost nothing to produce.

Thousands upon thousands of products and floods of oil came across the oceans to the US, and also to Europe, which began to pay in Euros for some of its imports: Euros which also cost nothing to produce.

US manufacturers, facing this competition from Asia, decided to move their factories to Asia instead of waiting for certain bankruptcy by competing against much lower-cost production.

That was how the US was de-industrialized.

It happened because gold was eliminated as a limit on credit expansion and money creation.

Had Nixon not gone off gold in 1971, China would have taken generations to create its industrial base. It would have been necessary for China to accumulate capital slowly, because its exports to the US would have been limited by the need for the US to pay up with gold for the amount by which Chinese exports exceeded its imports from the US.

The Chinese would have had to *buy* as much from the US, as they *sold* to the US; and since they were so terribly poor, there was not much they could have bought from the US.

Their growth would have been slower, but they would not now be facing over 20 million unemployed, as their markets dry up.

The US would never have allowed China to drain *US* gold from the Treasury by selling more to the US, than the US sold to China. But since payment was in *fiat dollars and not in gold*, the destructive effect of huge Chinese imports was not considered important by policy makers. And so, the US sailed into unemployment and had a great time doing it. Only now, that the party is over, are the grim facts visible: no jobs! Manufacturing is decimated.

The fiat dollar - unanchored to gold - was the greatest strategic gift that the US could have made to China. Now, they have a huge industrial base and the US has Oh, so little!

The damage is done. How to recover the industrial base of the US ? Not by slogans such as "Buy American ", nor by protectionism.

What is required is to recover economic balance between the nations of the world so that they all can balance their exports with their imports. This is not done by protectionism, a false remedy to joblessness.

The world needs to return to *gold as the international means of payment*. All imbalances must be paid, monthly, in gold. No fiat money "payment" allowed!

If a nation does not have gold to export, it must do without or *manufacture* what it needs, itself: there you have the clue to restoring jobs in the US and in Europe. This is not "nationalism", it is simply good economics.

The US has to limit its imports drastically, not by protectionism and tariffs, but by returning to the *Gold Standard*. Jobs will mushroom in the US beyond what anyone can dream as soon as *its market must buy locally or not buy at all*, for thousands upon thousands of articles. A return to gold, will achieve that aim very quickly, to be sure.

The Gold Standard is the friend and protector of the worker and of the investor, as well as the basis for harmonious relations between the nations of the world.

And by the way, the current financial disaster in the US is directly attributable to Nixon's decision to "close the gold window", because a monetary system based on gold is an obstacle to the criminal credit expansion perpetrated by the bankers. Gold based money puts shackles on bankers, forcing them to be careful. A fiat money system *enables financial criminality* - it's as effective in restraining criminality in finance as tying up a dog with a string of sausages.

Feb 4, 2009

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