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Global Strategy and Investment Trends by David Fuller www.stockcube.com

Stocks will outperform government bonds now that interest rate cuts have commenced.

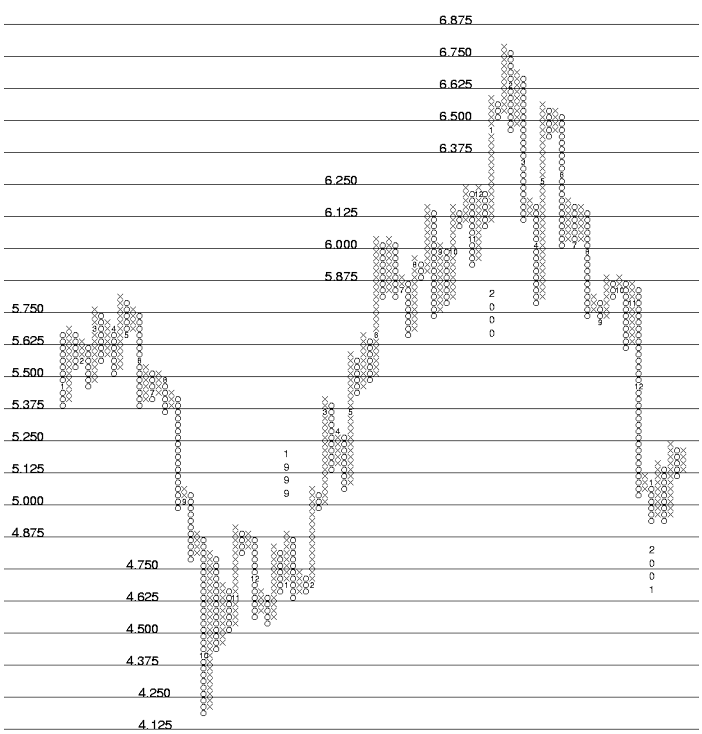
Interest rate cuts are bullish for stock markets

'Don't fight the Fed' - For my money, this venerable Wall Street adage deserves top rating, on a par with 'Buy-low-sell-high'. When the world's most influential central bank presses the monetary accelerator, some of those excess funds find their way to the stock market, the cost of borrowing declines and sentiment improves. Share indices in other countries usually follow the lead. When the Fed hits the brakes - watch out. Of course many of us have to relearn these lessons in a new cycle because changes in monetary policy seldom suit our book at the time. This is a behavioural problem. The challenge for all of us is to "stay in the zone", as one astute subscriber mentioned. In other words, we profit when in tune with the trend. Once out of the zone, losses accumulate and our confidence erodes. The tricky bit is to recognise important trend changes, which can challenge even the best readers of charts. Objectivity and experience help but often it isn't easy, especially if markets are volatile, reflecting general uncertainty. I find it helpful to shift tactics in line with any dynamic evidence of trend change, even though it will usually signal no more than a short to medium-term reversal. Inevitably there are many more of those than major tops or bottoms. Nevertheless these lesser moves are opportunities and we don't have to know (can't know for certain) if the major trend has reversed until much later. So, moving from the theoretical to the specific, where does this leave us with the NASDAQ? Well, that 14% gain and key day reversal on 3rd January, when Greenspan cut rates, certainly rang a bell for me! How often do we see action like that? I think we have seen the NASDAQ's low, as subscribers already know from the FMP updates. I'll give upside scope the benefit of the doubt - for all stock markets - until I see the current rallies countermanded by clear downward dynamics. Meanwhile, you may be interested in the latest views of that thoughtful, astute subscriber quoted in FM198, who accurately forecast that the NASDAQ would fall further. Following my bullish assessment on 9th January (FMP135, NASDAQ 2396), he sent me a lengthy email citing a variety of technical, behavioural and fundamental reasons why this most widely followed index would fall further. If he's wrong, it's because short-term rates are coming down, the Fullermarkets World Market Indicator has given a buy signal and stock markets are now 'climbing the wall of worry'.

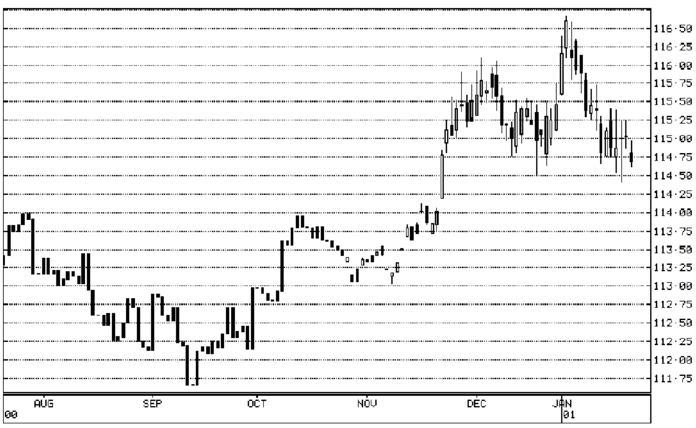
The sun rises for Japan as the yen sinks - There is only one remaining financial person in an influential position who does not accept that a weaker yen is required before Japan can fulfil its economic recovery potential. Unfortunately for the Japanese, he happens to be Governor of the Bank of Japan. Masaru Hayami is the Harold Shipman of central bankers. For those who do not see the British press, Shipman is the UK's leading serial killer, having poisoned over 300 patients, according to estimates. Lest you suspect my comparison is an exaggeration, consider the economic suicides in Japan, the bankruptcies, deflationary contraction and rising unemployment. Of course Hayami isn't entirely to blame in a country increasingly renowned for its corrupt and incompetent politicians and bureaucrats. However as the man in charge of monetary policy he is one of the main architects of Japan's long malaise. Subscribers are very familiar with the history. Fortunately, all bad things come to an end. The yen is now in a downtrend against other major currencies. Hayami doesn't like it, judging from recent comments, but events are moving beyond his control. This is good news for Japan. A weaker yen and much needed increase in money supply, when it occurs, will fuel Japan's long-delayed recovery. The Japanese stock market and global GDP growth will also benefit.

Bushwhacking - It looks as if all that belittling of Dubya by pseudosophisticates has been inspirational. The new administration hit the ground running, to coin a phrase. On first impressions the new team looks more professional than most of Clinton's appointments. I maintain that Bush will be good for the US economy. As for the dollar, which has taken a breather against most other currencies, there were rumours that US Treasury Secretary Paul O'Neill would have devaluationist tendencies. I think this would only be true if O'Neill felt there was no other means to spur the US economy. Clearly he doesn't, judging from recent comments at his Senate confirmation hearings: "Let me say at the outset, I am in favour of a strong dollar. I can't believe that anyone would think to the contrary." Don't expect a bear market for the greenback.

US 10 Year Bond Yield (0.025)



UK Gilts (Mar LIFFE) (Daily)



Interest Rates and Bonds

■ **Further rate cuts are inevitable and they will not be limited to the US.**

■ **Quality long-dated government bonds will lose their appeal as rates come down but there should be some recovery scope in corporate issues, including speculative debt.**

Greenspan's rate cuts on 3rd January were timely and decisive. As a good market psychologist, the Fed Chairman knows it is important to send a clear and unequivocal signal when the consensus view is becoming alarmist. We saw him do this during the 1998 financial crisis and there was nothing gradualist about his cuts in early January 2001. With the Federal Funds Rate currently at 6%, Greenspan has plenty of room for manoeuvre and will press the monetary accelerator as required, lowering short-term rates by at least another 50 to 100 basis points this year. He will not be concerned about inflation over the next few months, despite a rebound in petroleum prices due to recent production cuts by OPEC's cartel. He will be relaxed about labour shortages - a lagging indicator - because more US companies are downsizing than hiring. Whereas tech specialists were scarce a year ago, there are plenty available today due to the dotcom meltdown. These people will find new jobs without too much difficulty, often in traditional companies wishing to upgrade their 'clicks and mortar' strategies. Consequently Greenspan will remain focussed on the global economic slowdown and the debt problems this uncovers. The UK's Monetary Policy Committee is likely to commence rate cuts in the next few weeks. So should the European Central Bank, although they may fall behind the curve. There is a leadership problem with so many countries represented and despite bullish talk, confidence in the euro is no more than skin deep.

Risks in high quality long-dated government bonds are increasing, now that rates are coming down. These bonds easily outperformed stock markets last year and were highly profitable for anyone using leverage. Yields have now fallen to their lowest levels since the 1998 financial crisis, discounting the economic slowdown now occurring. For yields to move meaningfully lower in coming months, investors would have to shun equities, fearing that declining rates will not revive global GDP growth. While statistically possible, this is an unlikely prospect. Instead, cuts in short-term rates should increase confidence, leading to profit taking in quality long-dated government bonds as investors switch to shorter maturities, higher-yielding corporate and or speculative debt. They will also buy equities. As economics move into the next upswing, bond yields will rise on inflationary considerations. If perceptions change slowly quality long-dated government bond yields could retest or even extend their lows but the next significant move is likely to be upwards.

Strategy for bonds - From an investment perspective I would be taking profits in long-dated government bonds. If you are required to stay with debt instruments or prefer this area, I would move conservative funds into shorter-dated maturities, from 3-year instruments to bills, subject to your risk profile. Quality-rated corporate bonds are a more speculative alternative and I am indebted to my colleague Mark Glowrey for suggestions in the next paragraph. As for junk bonds, it may be a little early in the cycle but there will be rallies for many of these issues as confidence returns. As for futures, there may be two-way trading opportunities but I would reduce exposure, at least until bond prices are in clear downtrends. Following up on my own positions, I sold all my 30-year US Treasury bonds a little too soon in late December. I was actively trading UK 10-year Gilts on a Baby Steps buy-low-sell-high basis last month but closed all longs in these and also Bunds the day after Greenspan cut rates. I commenced repurchasing a little too soon on the subsequent reaction and will certainly stand aside in the event of a top-testing rally or take the loss if these instruments break chart support for more than a day or two.

"Corporate bond markets continue to present opportunities. USD 3 month LIBOR is standing at 5.61% while the 10 and 30 year US Treasury Bonds stand at 5.17% and 5.55% respectively. High quality credit spreads continue to improve. We track the 10 year "swap" spread as a proxy for high quality non-governmental debt. From a high of 140 bp over US 10 year Treasury Bonds in August 2000, the spread has tightened to 89 bp over, recently making a significant move in response to the Fed's cut. Tighter swap spreads indicate improving confidence and should also be viewed as positive for equity markets. Lower-rated credits have also generally shown improvement. December's A2 rated 8 5/8% 30 year issue for British Telecom has benefited from both tightening spreads and a stronger underlying Government Bond market. The bond, issued at 99.80, is now trading at 107.5, giving a yield to redemption of 7.96%. For investors looking for a good income, we currently favour the HSBC (series I) USD subordinated perpetual floating rate note. This bond is rated at A3 and currently priced at 81.5 to offer a running yield of around 158 bp over LIBOR. The bond also offers a 5% floor (or minimum coupon), effectively an imbedded option on which holders will benefit in the event of lower interest rates.

"Some of the widest spreads are to be seen in the Tech and Telecom sector. The considerable issuance of the last few years has left a pool of high-yielding debt with deteriorating credit quality. Amongst these are: Lucent (rated A3, on credit watch negative) $6.45% March 2029 currently at 76.80 (8.66% YTM), Apple (rated BB) $6.5% Feb 2004 currently at 95.12 (8.34% YTM), Dell (rated BBB+) $7.1% April 2028 currently at 92.35 (7.78% YTM) and Level 3 (rated B3) 11% March 2008 currently at 99.23 (11.15% YTM)."

Global Stock Markets

- **"Don't fight the Fed". Greenspan's rate cuts are bullish for the US stock market.**

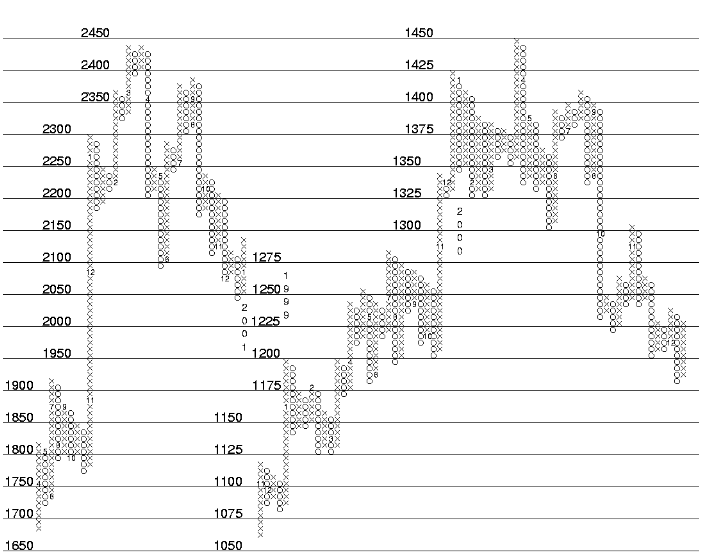
- **Improvement on Wall Street will help other markets but Europe's relative prospects are probably overrated, especially if the ECB delays in lowering rates.**

- **The yen's decline will eventually help Japan's economy and stock market to recover but investors should hedge the currency risk.**

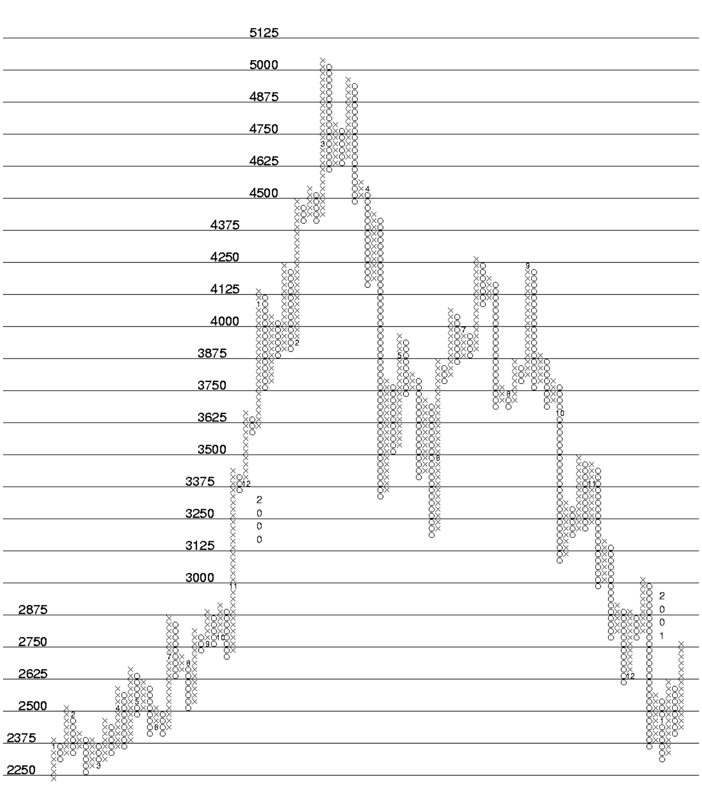
The best rallies usually occur when interest rates are coming down. The exception to this rule is when so much economic damage has occurred that confidence is shattered and stock market prices reflect the long-term deterioration. In this comparatively rare situation, valuations fall to historically low levels. It happened on Wall Street from 1929 to 1931. Japan's stock market decline has been a less extreme example. Could this be the US market's fate in 2001? I certainly don't think so because Greenspan moved quickly and aggressively, which is just what the previously slumping NASDAQ required. Moreover, the Fed will continue to ease monetary policy as required and with the Federal Funds Rate currently at 6%, they could lower this by at least another 200 basis points without jeopardising real (above inflation) interest rates. A correction in the US dollar has occurred since October and there has been talk of a possible collapse. This is unrealistic given the yen's continued vulnerability and uncertainty still overhanging the euro. Meanwhile, the dollar's reaction will help operating profits for US multinational companies. For Wall Street, Greenspan's rate cuts have begun to change perceptions, with investors starting to look beyond the bad economic news towards the second half of 2001, when profits should be rising once again. One of the oldest and most reliable market adages is, "Don't fight the Fed".

A firmer US stock market would be a net plus for Europe but don't expect superior market performance. Currently, it is fashionable to favour European equities over Wall Street, partly because tech sectors are less of a factor and the euro has finally rebounded. Sure, the NASDAQ's slump was more frightening than Europe's reactions but where do we go from here? On interest rates, we should recall that while Greenspan tightened to slow the US economy, there was no equivalent growth surge in Europe, which remained weaker. The ECB hiked to support the euro and contain inflation, jeopardising growth prospects in the process. While Euroland was probably growing at just over 3% by yearend, most of this was due to export earnings boosted by the weak euro, which is now appreciating.

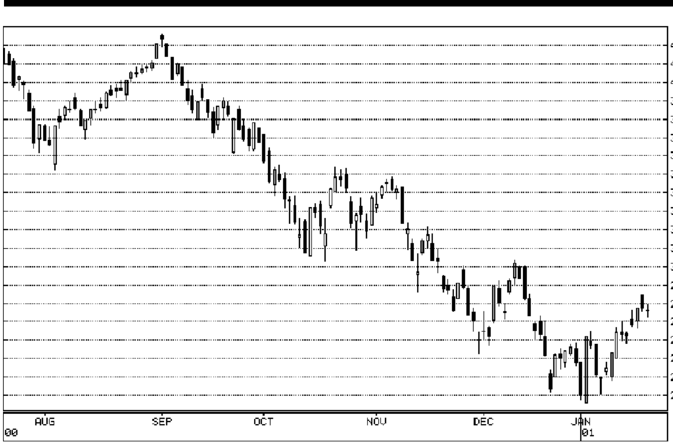
FWMI (10pt) and MSCIWI (5USD)



NASDAQ Composite Index (25pt)



NASDAQ Composite Index (Daily)



Domestic growth was much slower and with unemployment still twice that of the US, it is not clear why personal consumption should now expand sufficiently to offset the inevitable deterioration in operating profits for exporters. Confidence in the euro expressed by the Euroland officials is a public relations exercise because they fear a retest of the lows more than a too strong euro. I doubt the euro will be under heavy pressure during at least the first half of 2001 but given the ECB's experience over the last two years, it may leave rates too high for too long, further damaging growth prospects during a global economic slowdown. Finally, European stock markets have a higher proportion of defensive shares relative to the US. These did very well from March 2000 until yearend. However defensive shares are not likely to dominate performance tables as interest rates decline and investors begin to discount stronger growth following a contraction. There may also be some complacency in Europe, whereas the US market experienced more selling prior to Greenspan's rate cuts on 3rd January. Consequently, US stocks are generally on more conservative valuations than their European counterparts. In conclusion, I think Europe's stock markets will follow the lead from Wall Street but aggregate performance is likely to lag.

GDP data will mostly 'surprise' on the downside during the first half of 2001, especially in Japan. The economic news will not be encouraging during the next few months as global growth continues to contract. While most eyes are on the slowing US juggernaut, Japan's slide back into recession is the more serious problem, compounded by net deflation. All the fiscal spending packages of recent years have bought little more than ballooning government debt. This situation is unnecessarily grim because there is no mystery as to what Japan needs - a rapid expansion of money supply (M2+CD), which is currently growing at a meagre 2.2% per annum, and a much weaker currency. While the BoJ remains intransigent regarding money supply, the yen has fallen sharply since mid-November. I regard this move as inevitable and maintain Japan's currency will fall a lot further against both the US dollar and euro this year, punctuated only by the inevitable technical rallies within its downtrends against all other major currencies. If correct, this should be the good news enabling Japan to break out of its long deflation before yearend and commence a sustainable recovery. A strengthening economy for Japan would be anticipated by the stock market but investors may wish to hedge the currency risk, especially as this also provides an attractive rate of interest.

Chart review of topical and representative stock market indices - The point & figure charts shown are based on closing prices and taken from our website service - www.fullermarkets.com. Anyone interested in this chart service, which is updated daily, should email research@fullermarkets.com. Price levels mentioned below refer to market closes.

The Fullermarkets World Market Indicator (2136), did not maintain a break under the May low at 2090 and now it has broken the progression of lower rally highs by pushing above 2110. This is a short-term buy signal and 2030 is now required to reverse scope for an additional recovery. The FMWI is unweighted and calculated in local currencies.

The Morgan Stanley Capital International Indicator (1227) is questioning its downward bias by moving above the mid-point of the late-November to late-December's small range. Further improvement would be signalled at 1240. However this pattern cannot support more than a technical rally - potential that would be negated at 1175. The MSCII is capitalisation weighted and calculated in US dollars.

The US NASDAQ Composite Index (2740) has broken its short-term downtrend having bottomed on 3rd January with one of the better ending signals - a dynamic key day reversal. It has now rallied marginally further than any technical rebound since the early-September high near 4250 and is close to exceeding the preceding step's mid-point. This would indicate a further loss of downward momentum and if support is now encountered near or above 2625, an additional recovery will not be long delayed. Some psychological resistance can be anticipated around 3000, which is also near the December high. **The Standard & Poors 500 Index** (1334) - *not illustrated* - shows the first higher highs and higher lows since September's failed challenge of the March high. A close at 1290 is needed to question somewhat higher scope, which would be reaffirmed at 1350.

Japan's Nikkei 225 Stock Average (14032) fell just as persistently as it rose from its 1998/99 base. That important low should provide at least temporary support. A positive sign would be a close at 14100, breaking the 4-month progression of lower rally highs. However this pattern cannot support more than a technical rally at present and the base building may be lengthy.

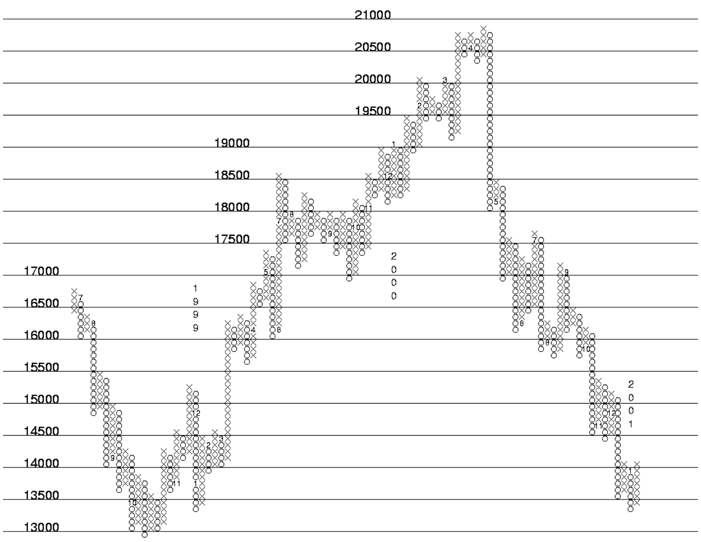
Taiwan's Weighted Price Index (5847) shows an overall loss of downward momentum following an accelerated decline, including the biggest rally since April's failed test of the February 2000 peak. This is clear evidence of base building, which should eventually support a significant recovery for this NASDAQ-related market.

Sweden's OMX Index (1100) - *see page 6* - has been on the defensive ever since the accelerated peak in March. However the best rally since August provides the first evidence that demand is returning. A close under the psychological 1000 level is now required to reaffirm the downtrend.

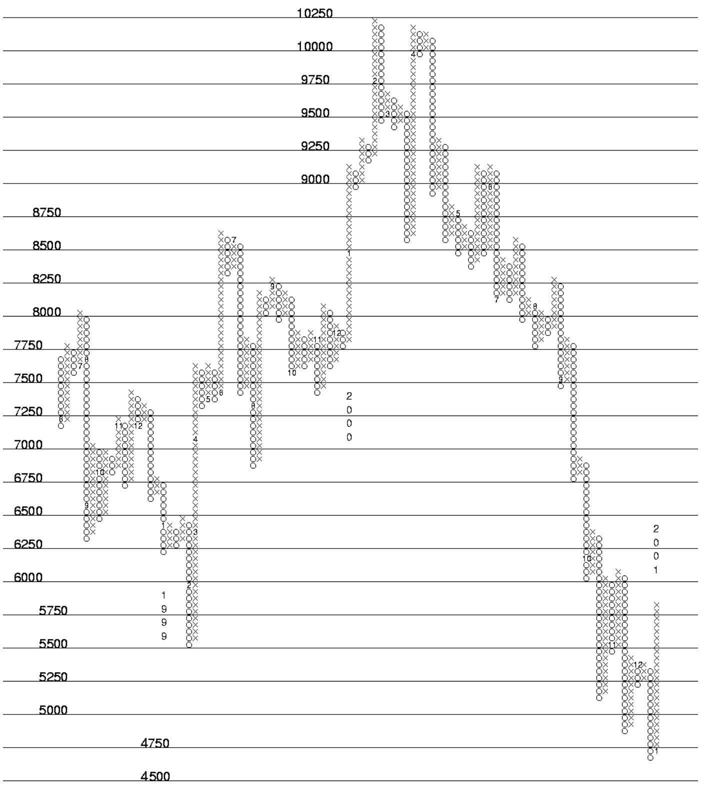
Italy's MIB 30 Index (44506) - *not illustrated* - has not maintained its break under lateral trading near 43600, dating back to April. A close under 42000 is now required to offset some additional test of overhead trading, which is substantial.

The UK's FTSE 100 Index (6232) - *not illustrated* - remains quiet within its long range but has shown relative strength on a global basis. This pattern is difficult to predict other than saying we will probably see more of the same.

Nikkei 225 Stock Average Index (100pt)



Taiwan Weighted Price Index (50pt)



However the recent failed break under 6125 and a higher high are mildly encouraging.

Strategy for stock markets - I'm feeling less wary now that Greenspan has commenced cutting rates. Obviously this does not solve all economic problems at a stroke but I believe a psychological Rubicon has been crossed. Many investors know that the most bullish market phases occur when short-term rates are falling. Stock markets should now have a firm bias, until people suspect that the next move will be for central banks to hike rates. A big decision for active investors in equities concerns old versus new economy stocks. I favour the TMT group; initially, quality low multiple sector leaders that are beginning to

Final Summaries of Year 2000 Recommendations

List of Recovery Shares from FM190
'Boring' Old Economy Stocks To Beat The NASDAQ
UK Low-P/E, High-Yield Stocks
Twenty-five shares listed. Biggest winner, Bellway +84.03%. Loser, United Industries -74.07%. Average Gain/Loss +22.84%. NASDAQ Composite Index -41.20%.

US Low P/E, High-Yield Stocks
Seven shares listed. Biggest winner, Philip Morris +112.41%. Loser, PG&E -52.06%. Average Gain/Loss +19.32%. NASDAQ Composite Index -41.20%.

List of Recovery Shares from FM191
UK Low P/E, High-Yield Stocks
Nine shares listed. Biggest winner, Hepworth +71.95%. Loser, none. Average Gain/Loss +41.57%. FTSE 100 Index -1.63%.

US Low P/E, High-Yield Stocks
Five shares listed. Biggest winner, Pennzoil-Quaker +16.47%. Loser, Xerox -71.66%. Average Gain/Loss -11.53%. S&P 500 Index -9.13%.

Japanese Low P/E, High-Yield Stocks
Five shares listed. Biggest winner, Tokyo Gas +23.95%. Loser, Osaka Gas, -6.56%. Average Gain/Loss +7.15%. Nikkei 225 Index -23.20%.

Recommended Tech Stocks with Earnings from FM193
Blue-Chip Tech Stocks
Six US and one Finnish share listed. Biggest winner, none. Loser, Intel -46.91. Average Gain/Loss -29.13%. NASDAQ Composite Index -25.63%.

Tech-Wreck Recovery Candidates With Earnings
One UK and one German share listed. Biggest winner, none. Loser, Sema -54.99%. Average Gain/Loss -32.71%. NASDAQ Composite Index -25.63%.

FMP116 05/07/00 Share Recommedations
Four Value Stocks to Benefit From Lower Oil Prices
Two US and two German shares listed. Biggest winner, Volkswagen +46.03%. Loser, DaimlerChrysler, -12.03%. Average Gain/Loss +7.65%. Dow Jones Industrial Average +1.97%.

Recommended Tech Stocks with Earnings from FM194
Blue-Chip Tech Stocks
Two US shares listed. Biggest winner, none. Loser, WorldCom -48.24%. Average Gain/Loss -38.27%. NASDAQ Composite Index -27.90%.

Tech-Wreck Recovery Candidates With Earnings
Two UK, one French, one Dutch and two US shares listed. Biggest winner, Alzan +22.84%. Loser, Getronics, -53.54%. Average Gain/Loss -16.85%. NASDAQ Composite Index -27.90%.

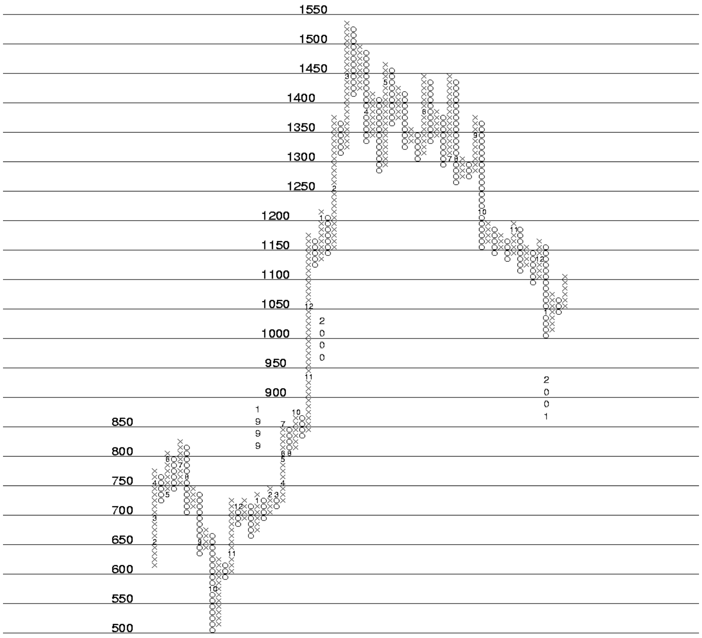
Recommended Stocks from FM195
Blue-Chip & One Tech-Wreck Recoveries
One UK and four US shares listed. Biggest winner, Sara Lee +20.61%. Loser, Compaq Computer, -31.24%. Average Gain/Loss +3.25%. S&P 500 Index -8.50%.

Japanese Bank-Wreck Recoveries
Four shares listed. Biggest winner, Bank of Yokohama +0.21%. Loser, Sanwa Bank, -11.81%. Average Gain/Loss -5.31%. Nikkei 225 Index -14.18%.

Recommended Stocks from FM196
UK Old Economy & TMT-Wreck Recoveries
Five shares listed. Biggest winner, Diploma +31.71%. Loser, Durlacher, -65.14%. Average Gain/Loss -24.63%. FTSE 100 Index +0.15%.

Recommended Stocks from FM197/198
Tech-Wreck Leader Recoveries
Five US shares recommended. Biggest winner, Micron +46.70%. Loser, Intel -11.96%. Average Gain/Loss +14.03%. NASDAQ Composite Index -5.97%.

Sweden OMX Index (10pt)



show relative strength. These were the most oversold before Greenspan cut rates on 3rd January. In contrast, I would avoid defensive stocks for a while because they did comparatively well from March until yearend. In the rate-cutting environment, I also like financial stocks. Additionally, I would choose companies that will benefit from an easier US dollar and avoid their euro-zone counterparts. In terms of global weighting, I would go against the consensus, preferring the US to Europe because valuations in the former are now often lower. Bombed out Asia should see a further recovery. Taiwan is my favourite from this region because it has discounted recession, tech disasters and bellicosity from China. However it isn't a very accessible market for non-locals. The next big decision on Japan should be to buy, while hedging the currency risk, which provides the additional advantage of an attractive interest rate differential. However it may take time for the Nikkei to build a base because the political/economic situation is in such a mess. As for the share tables, I have decided to close these on an annual basis in line with the Stockcube Research policy. The table summaries show relative performance through January 19th 2001. If I retained anything from last year's lists it would be the 5 techs re-recommended late last year - Altera, Intel, Micron, Motorola and WorldCom. My favourite stock market sector at present is Semi Conductors. In my futures trading, where I am chagrined not to have done better, I am in danger of showing a profit on the NASDAQ long, now protected with a stop. I have an in-the-money trailing stop on a Swedish OMX long, purchased following Greenspan's rate cut. This will expire on 26th January, while I am in the States. I have been nibbling at the Nikkei on easing since the end of November and currently show a small loss on the overall position.

Currencies

■ **The US dollar, euro, sterling and Australian currency should resume their uptrends against the yen following a pause.**

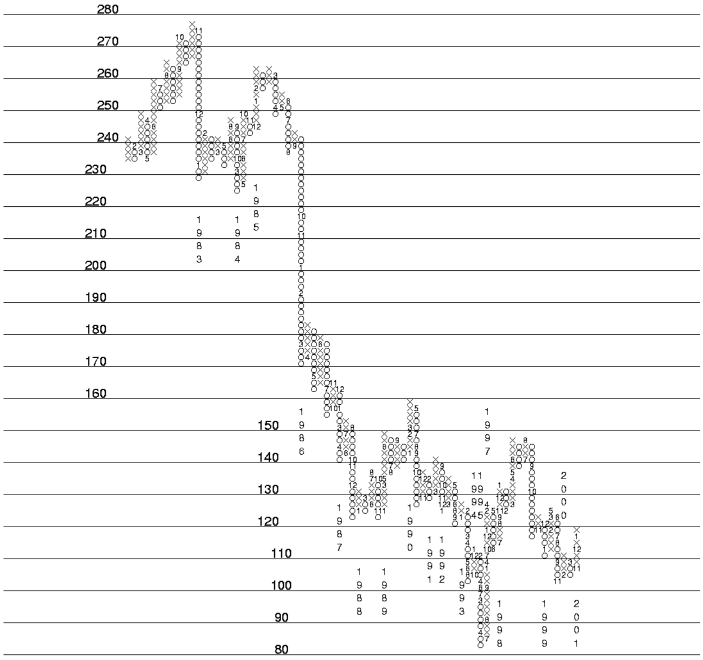
■ **The euro has backed away from prior resistance against the US dollar. It will probably range for months, without a big move in either direction.**

■ **The Australian dollar has rallied back to resistance against the US currency.**

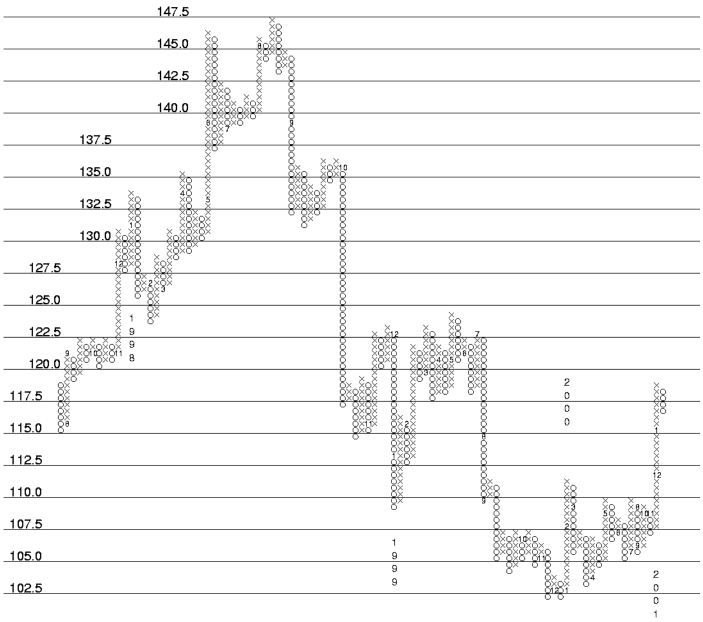
Another significant advance against the yen will occur following the present consolidation. All other reserve currencies surged against the yen from November until early January. However the Japanese currency won't fall every day and some short covering has occurred recently. This has checked short-term uptrends against the yen near previous resistance but they are likely to be resumed in coming weeks. Now that Japan's currency has clearly commenced an overall decline few people have any reason to hold it. There will be some demand from international investors as they venture back into Japanese stocks but most investment managers will want to hedge against a devaluing yen. Some of Japan's exporters and multinational companies may repatriate capital as needed but they are now even more likely to push funds offshore. The Bank of Japan is under pressure to increase the supply of yen and some of this money is certain to find its way overseas. Now that the yen is no longer appreciating many Japanese investors will prefer higher-yielding euro and US dollar investments. The question is how far will the yen fall over the next few years? Obviously no one knows but the charts add to our perspective. A technical premise, that I offered several months ago, was that if I were right about significant upward potential for the dollar and other currencies against the yen, the initial move up from bases would be explosive. The strength of this move has even surprised many of the yen bears. See also the very long-term point & figure chart on a ¥2 scale, showing dollar/yen history since February 1982. On this scale the November to early-January rally hardly registers, although it is the biggest advance since 1998. Might all the ranging activity since late-1987 be a base, just as we saw for the dollar against the mark and Swiss franc on long-term charts that often appeared in these pages? I believe so, although the dollar/yen pattern is more volatile. Considering the economic background over the last decade, would it be unreasonable for the dollar to reach ¥150 to ¥160 as I have often suggested? I don't think so. Moreover if the US economy remains considerably stronger than Japan over the next few years, which is a possibility, why not ¥175 to ¥200?

The euro should stay out of the casualty ward this year but a powerhouse it isn't. Has the euro really metamorphosed in a few months from an experiment gone wrong into the safest long-term haven for the world's investors? I don't think so and a clear consensus is usually a contrary indicator. What we have seen, once again, is that multilateral intervention works, although usually not at the first attempt. After the leading central banks stepped in last September the euro slipped a little lower a month later before staging its biggest rally ever. Recently, the crowd was confidently forecasting US$1.00 to US$1.10 versus the US dollar. Instead, it has rolled over in a corrective phase. There is some chart/psychological resistance in the US$0.97

Japanese Yen per 1 US Dollar (2)

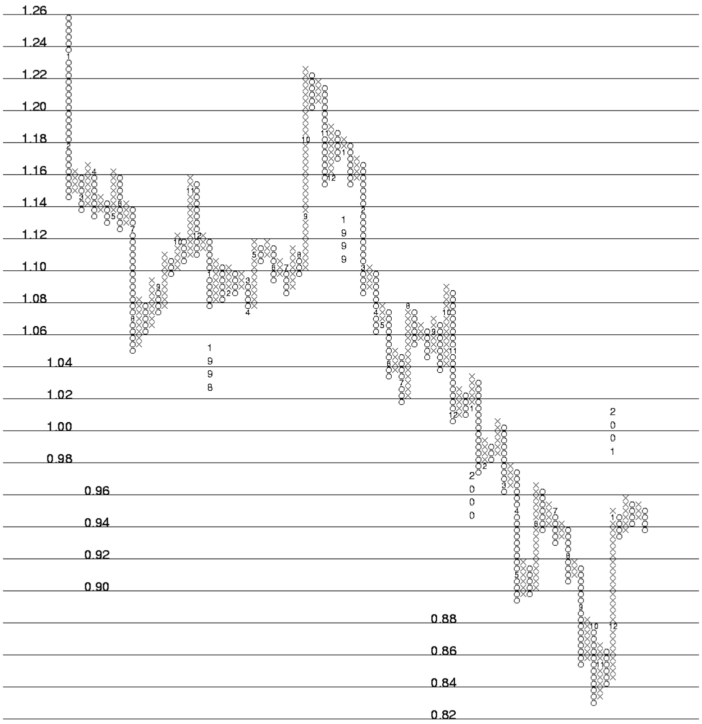


Japanese Yen per 1 US Dollar (0.5)

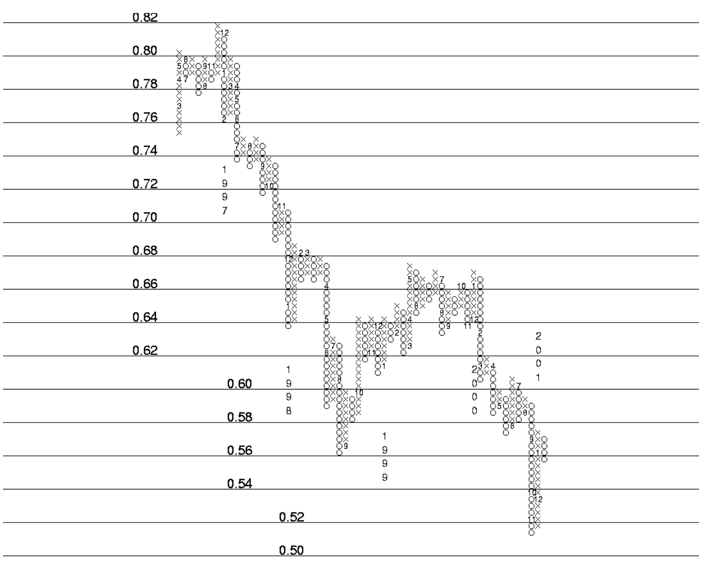


US Dollar / Japanese Yen (Daily)

US Dollar per 1 Euro (0.004)



US Dollar per 1 Australian Dollar (0.004)



Australian Dollar / US Dollar (Daily)

to US$1.01 region that I do not expect to be cleared easily. Forecasts of a resurgent Euroland economy as the US slowed appear either hubristic or the triumph of hope over experience. The single currency's rally is better for US exporters than their European rivals. Germany's IFO survey of business confidence has declined for the 7th consecutive month. Yes, short-term US rates are coming down but this should ensure an economic recovery when Euroland is still slowing, especially if the ECB delays too long in lowering the cost of borrowing. Do you think Europeans will welcome the surrender of their national coinage in favour of euro money in January 2002? I wouldn't bet on it. My hunch is that ranging will predominate, with few dramatic moves in dollar/euro over the next few months. I also suspect the single currency's best chance of exceeding parity with the greenback is in the first half of 2001. Peering much further ahead, I would not be surprised to see the dollar resume its long-term bull market in 2002.

When I visited Sydney in October for the ATAA, everyone was talking about US$0.50 versus the US dollar. There is a rule of thumb with consensus targets, which are often round numbers and therefore psychological barriers - don't wait for them to be reached. Delegates at TCS in Sydney will remember discussing this. The Australian currency fell to US$0.5071 before rebounding strongly on a key day reversal. This sparked a sharp rally, which has now faltered beneath the mid-April to August range. While this region may be further tested, I think overhead trading would make any additional recovery by the Australian dollar against the greenback more laboured.

Strategy for currencies - In recent months my favoured positions have been high-yielding currencies for their recovery potential against the yen. Following the strong November to early-January advance, these have rolled over in what I suspect will be no more than short-term consolidations. The money-control decision has been whether to use tight or loose stops. Generally, I prefer the latter unless a mature trend is clearly accelerating. One needs to give a position breathing room unless it is very overextended. I find tight stops more stressful, especially as one can too easily be shaken out of a good trend that has only hesitated. In this situation one can always buy back as the trend resumes but often people do not. Our daily currency service closed out longs against the yen as short-term uptrends lost momentum. The trick now will be to buy back in timely fashion, assuming you share my view that the yen will fall a lot further. I suggest either Baby Steps accumulation of the dollar, euro, etc on easing or the more conservative strategy of waiting until the next sign of strength. With the former one risks coming in too soon, while a reactive strategy can be late if the market moves quickly and decisively. Personally, for ease of monitoring I have confided my trading to - dollar/yen and euro/yen. My positions in the latter have been smaller and I trade it more actively due to earlier volatility. I took profits too soon and am currently out of euro/yen, but looking to re-establish on a setback, although I may defer due to travel commitments. With dollar/yen, I leveraged up further, protected with a loose in-the-money trailing stop. I took a tactical decision not to commence lightening near the first psychological/chart resistance at ¥120, although with hindsight that would have been a good idea. My bet is that we will not see big corrections, relative to gains, until currencies are considerably higher against the yen.

Commodities

■ **OPEC's decision to cut production has stemmed the decline in prices and will be a drag on global GDP growth, a problem compounded by the surge in natural gas.**

■ **The grain and soybean complex is basing and demand will be boosted by the increasing ban of meat and bone meal feed for livestock.**

■ **Cocoa and coffee have joined the list of agricultural commodities recovering from historically depressed prices.**

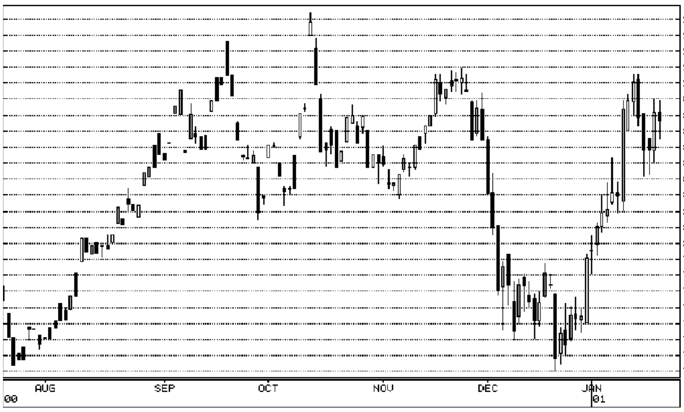
■ **Prices for most industrial metals are likely to remain soft for a while longer, in line with the global economic slowdown.**

The OPEC cartel can keep prices higher for a while longer. The price of crude oil had fallen sharply from its October-November highs but rebounded on yearend news that production would be cut by 1.5 to 2 million barrels a day. It had gained 13% from its December lows when a supply reduction of 1.5 million barrels was ratified by the cartel on 17th January. Gasoline had rallied more, retesting last year's highs. However gas and heating oil only managed to lose downward momentum, perhaps because merchants had bought forward in anticipation of winter demand from the Western Hemisphere. There is no doubt that OPEC will keep petroleum prices higher than would have otherwise been the case. While this will lead to redoubled efforts from oil importing countries to find additional sources of energy and increase supplies, especially by the Bush Administration, that takes time. Meanwhile, the cost of petroleum products will weigh further on global GDP growth, particularly for developing countries. Unfortunately, the option of switching to cheap natural gas is no longer available since this alternative fuel rocketed in price since November, before easing somewhat recently.

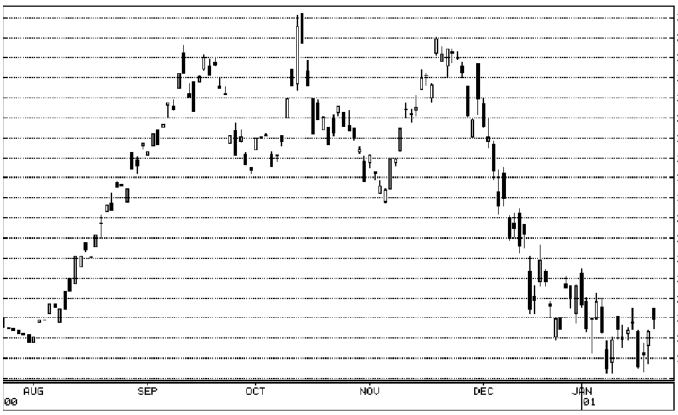
The grain and bean story is becoming interesting. Prices are still historically low and have shown evidence of base formation development for a number of months. The bearish factor is supply because US reserves are reasonably high. Also, the most recent reports on Brazilian and Argentine corn and soybean crops, plus US winter wheat are favourable. While much of this is already discounted, it is likely to lengthen the basing process. Demand is certain to rise because of the increasing ban of meat and bone meal livestock feed. While Europe banned MBM for cattle some time ago, due to mad-cow disease, until very recently it was still being fed to pigs and poultry. Countries that do not ban MBM feed will find it very difficult to export their livestock products. Since the critters have to eat, they will

Crude Oil (Mar NYME) (Daily)

Gasoline (Feb NYME) (Daily)

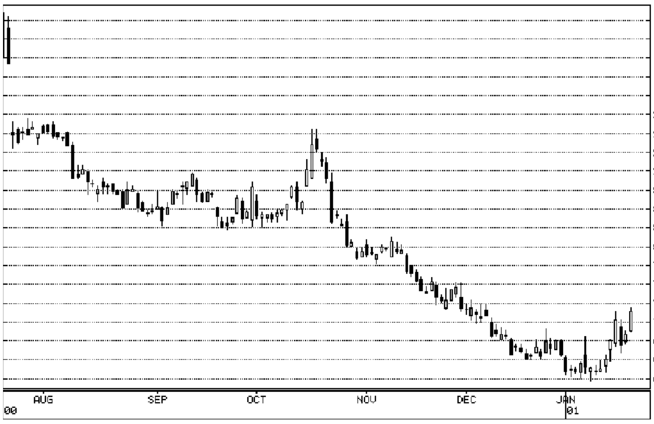


Gas Oil (Feb LIFFE) (Daily)



Soybeans (Mar CBT) (Daily)

Coffee (Mar CSCE) (Daily)



Pork Bellies (Mar CME) (Daily)

be fed more corn, soybean meal and wheat. I do not think markets have fully discounted this additional demand, which could be substantial. However the key variable for commodities is always supply because it is more volatile than demand. Currently, this appears adequate to meet demand that can only rise, despite the global economic slowdown. The biggest influence on agricultural commodity crops is weather, principally too much or too little precipitation. You don't have to be a meteorologist to notice that weather patterns are becoming more turbulent. I suspect the chance of a crop scare over the next eight months is at least 50/50. In that event, prices for corn, soybean and wheat futures could rally sharply.

The outlook for cocoa and coffee has also improved. It couldn't have become much worse with prices at record lows only a couple of months ago. Needless to say supply has been abundant but this is always the case at market bottoms. The question is what will change? Supply, because cocoa and coffee are produced in some of the world's less stable regions. Political tension in the Ivory Coast, an important supplier of cocoa, has delayed deliveries sufficiently for a small backwardation to appear. This has led to short covering and a scramble for supplies by processors. Coffee's recovery has been led by the robusta contract (LIFFE) following a climactic downward acceleration in November and early December. Here also a small backwardation has appeared and the arabica contract (CSCE) has bounced following a new contract low on 9th January. Among the bullish influences is the prospect for a supply retention programme of 20%, led by Columbia, Latin America's second largest producer. Also, the recent earthquake has caused delivery problems in El Salvador and coffee mills in neighbouring Guatemala were damaged. While these are short-term factors, both are sufficient to change market sentiment and fuel an additional rebound. Looking further ahead, Brazil is the largest producer of coffee. Last year the trees were slightly damaged first by drought and then by cold weather in certain regions. Consequently they will be more vulnerable this year. The time of greatest risk for Brazilian coffee is between May and July. Any threat to this year's crop would spark an additional recovery following a period during which coffee roasters have been accustomed to buying only for their immediate requirements in a falling market.

Pork bellies could rally but further but slower demand may weigh on most metals for a while longer. Using lateral thinking, if humanoid carnivores are worried about mad-cow disease they will eat more pork and poultry. Fast-food restaurants such as McDonalds are anticipating the change in demand and offering more meals featuring bacon, which as we all know, certainly adds flavour to a chicken sandwich. Pork bellies (Mar CME) have an interesting chart, showing a climactic sell off in August followed by ranging in a probable base formation, which could be in its latter stages. Bullish clues are the speed with which prices have been rallying relative to the declines and higher reaction lows since October. In contrast, base metals show mostly inconsistent chart patterns, often with a downward bias. The fundamentals suggest ample supply and less demand in line with the global economic slowdown. A sustained upturn requires production cuts and/or stronger GDP growth. The latter is unlikely before the second half of 2001. In the precious metal sector, gold remains under pressure due to economic factors and forward selling by producers. However it is historically very cheap and the US dollar is no longer weighing on prices. Therefore we can expect occasional upward spikes on short covering, as occurred for silver recently, even if the final lows may not have been seen. Platinum and especially palladium have seen phenomenal advances, primarily due to minimal exports from Russia. Demand is now slowing, particularly from the automobile industry and prices for both metals are extremely vulnerable to any increase in supply.

Strategy on commodities - I have been more active in commodities recently than for a very long time, concentrating solely on accumulating longs in markets that look very oversold on the charts. Following up on positions previously mentioned, I decided not to roll my January (CBT) soybean long forward, more by luck than analysis. This was fortuitous because the price fell back sharply within its base on supply news. Consequently I recommenced buying, a little too soon but in small quantities using my Baby Steps tactic of nibbling first in the March contract and latterly in May as prior support levels were tested. Logically, I should let some of this position go in the event of a bounce. Wheat's rebound within its base enabled me to protect this position with an in-the-money stop, effectively giving me a free ride in the March (CBT) contract. I considered taking at least partial profits as the October high was tested but didn't - tactically a short-term mistake as wheat has eased, although it is still well above my stop. I'm tempted to repurchase corn, first mentioned in these pages several months ago, as it led the recovery but retraced almost half of its gains recently. Even if my hypothesis that the US grain and bean complex is in a base building stage, the appropriate tactic is Baby Steps range trading, similar to our dollar/yen and euro/yen strategy from early until late 2000, at least until these patterns are completed and step-sequence trends develop. I didn't buy cocoa (mentioned last month) because I didn't want to pay $60-$70 more than the December low at $707 (Mar CSCE), even though it was still cheap. Bad decision because it romped over $1000. If you bought, well done! I did establish a good position in coffee (Mar CSCE), which I also mentioned in FMP134, and will introduce an in-the-money stop on any further gains. Similarly, I bought pork bellies (Mar CBT) and will use the same strategy mentioned for coffee. Cotton, lumber, gold and silver are cheapest among the industrial/metal commodities but I am only watching. We produce a brief technical comment on most commodities every day. Email research@fullermarkets.com and they will send you a sample if you specify the markets of interest.

The Global Economy

■ **Greenspan's decisive action on rates will cushion the US economic contraction, with evidence of improvement from mid-2001.**

■ **Talk of stronger European growth relative to the US for a sustained period is delusional.**

■ **Japan will continue to lag but the weakening yen is opening an escape route from the deflationary spiral.**

■ **Another round of OPEC supply cuts risks reviving and prolonging the oil crisis.**

The US economy faces some debt problems but remains in an enviable position overall. During the equity bull run of 1995-1999, US CEO's were rated on the basis of their share performance. Consequently they leveraged their balance sheets by issuing debt, which was often used for stock buyback programmes. Coupled with some questionable accounting practices, particularly regarding the treatment of employee stock options, this policy inflated corporate earnings. In Geckoesque fashion, business schools embraced this new creed, proclaiming, "Leverage is good"! Sure, when the economy is motoring along but the debt chickens come home to roost in a slowdown, as we are now seeing. Greenspan is obviously concerned about company debt levels, which had pushed up corporate bond yields and troubled the stock market for many months. We should not be surprised if there are some eyebrow-raising defaults. Personal debt is also high in the US but the smaller problem by far, provided consumers do not take fright and stash cash under the mattress, à la Japanese. Greenspan understands these risks more than most and has already shown a willingness to move aggressively in slashing rates. President Bush's tax cuts will also boost confidence among both businesses and consumers, although we do not yet know the timing or extent of this fiscal stimulus. These measures will not just sustain the US economy's resilience - it will become even more competitive. Inward investment will still be attracted by the world's most tax-efficient and unfettered major economy. Immigrants, offering both skills and energy will seek to earn their way in the USA, and they will be accepted.

Europe's economic machine is unlikely to fire on all cylinders. The problem is the system, not the people. Yes, there has been some helpful deregulation and a somewhat less onerous tax burden but the Europe's efforts to catch up always resemble the commuter running to catch a train that has already left the station. At the bottom line, it is harder or more expensive to launch, staff and run a business in Europe than the US. In other words, it is more difficult to make money in Europe, whether as an entrepreneur or young person joining the job market. There may be beneficial or at least acceptable tradeoffs, in terms of welfare and quality of life, but claims that Europe will now outgrow America over the next few years remain delusional or hubristic. The euro's rebound is desirable, globally, but it will help US businesses more than their European counterparts. Euroland's economy is less self-contained than the States and while the former's recovery was helped by exports, this market is shrinking due to the US slowdown. The ECB will always be less secure and more of a political football than if it represented a European federation, for which there is limited public support. One money supply for 12 culturally and linguistically different states is a crude monetary system, especially without mobility of labour. Euroland's economic cycle is a little behind that of the US but growth is now slowing. Remember, the Federal Reserve raised interest rates to slow growth - the ECB did so to support the euro and check inflation. There is a risk that they may leave rates too high for too long and Euroland's unemployment is still twice that of the US. As for the euro, watch for widespread anxiety and dissatisfaction as the January 2002 deadline approaches, when national money is supposed to be scrapped for euro paper and coinage.

Finally, Japan is playing the yen card. I don't want to be labelled a Japan basher and actually, I am a great admirer of this nation's many achievements. However for a developed country, it has also set records for political ineptitude during the last 15 years. Japan's deflationary spiral will become a textbook example for future generations studying economics. The mistakes are not unusual but the surprise, at least for me, is that they occurred in a democratic country and the world's second largest economy. Part of the problem is that Japan remains a one-party democracy. This is a recipe for cronyism, pork barrelling, arrogance, corruption and incompetence, which we have seen in abundance. Since veteran subscribers are well versed in this saga, I'll briefly summarise the main economic events. In the late 1980s Japan stoked the biggest property bubble in history, on borrowed money of course. Once the Emperor's garden was valued higher than the State of California, the Government sensed trouble and appointed a new governor at the BoJ as executioner, with the sole objective of squeezing monetary policy - a task performed with such relish and for so long that it tipped Japan's economy into a deflationary spiral. A new governor was appointed who eventually slashed interest rates to zero in an effort to check this decline but the damage to business and consumer sentiment left the BoJ "pushing against a piece of string", to quote Keynes. Massive fiscal spending packages, largely on construction, just managed to keep the economy afloat. Unfortunately, bridges to nowhere and paved riverbeds are not the building blocks for a sustained recovery. The yen was allowed to soar in 1995 and this reinforced the destructive deflation in which prices, output and profits fell. Intervention sent the overvalued yen on a downward path but as this began to resuscitate the economy, the Government slapped on a consumption tax, with fatal effect. Umpteen more spending packages produced a few signs of economic revival but the yen soared in 1999-2000 as Japanese investors panicked out of euros while businesses sold trophy properties in the US and repatriated capital from foreign subsidiaries, to shore up the parent companies' balance sheets. Enter Masaru Hayami - the Harold Shipman of central bankers - whose monetary tough love included sterilising the MoF's intervention efforts, a refusal to boost money supply and a hike in rates! With help like this the economy is back in recession, the Nikkei testing its 1998 low and the Government's budget deficit has soared over 125 per cent of GDP. As if that weren't enough, Japan's obsession with preserving its national homogeneity is creating a demographic time bomb. According to the OECD, which is inclined to optimism, tax rises and spending cuts equivalent to 10 per cent of GDP would be required to check the ballooning public debt burden. Needless to say that won't happen soon because it would cause an outright economic depression in Japan. Proving that it is never too late to learn, even Hayami now acknowledges, "As corporations and banks go ahead with restructuring, pressure from structural adjustment will hold back the economy. Thus we cannot expect a robust economic expansion." At long last, Japan is doing the obvious and letting the yen go. It will probably fall much faster and further than the euro during the first 20 months of its existence, eventually enabling the Japanese economy to stage a sustainable recovery.

OPEC's latest supply cuts will prolong the global economic slowdown. Unfortunately, the good news for oil importing countries on supplies was short-lived. Prices plateaued in September and fell sharply during December. However this slide in response to supply increases and somewhat lower demand was checked by news that OPEC's cartel was to cut production by 1.5 to 2 million barrels a day. Gasoline has had the sharpest rebound, approaching its former highs, while heating and gas oil have lagged. OPEC will be aware that with the global economy in a slowdown phase, partly due to higher oil prices, they risk undermining their market. However like any commercial supplier they will put self-interest first, reacting more quickly to what they perceive as low rather than high prices. There is also the unstated agenda of pressure on importing countries over the Israeli/Palestinian impasse. Consequently the 'oil crisis' remains an ongoing problem and a tax on business and consumer spending for the oil-importing countries. Supplies from outside the OPEC cartel will increase but this takes time. Meanwhile there is no longer any respite in switching to natural gas, which soared to record highs near $10 (Feb CBT) in December. Last month's decline in oil prices helped to lower inflation data. Increasing energy costs will now cause an inflation blip but the long-term effect will be deflationary because of the restraint on global growth.

And Finally…

The Chart Seminar 2001 - Bloomberg's current London Auditorium is being phased out so we are deciding on a suitable new venue and should have details shortly. I expect to have a two-day chart-reading seminar on 10th & 11th May and another in London on 29th & 30th November. These will have a Bloomberg data feed for up-to-date market examples. We will hold a third TCS in Zurich on 12th & 13th July. If you would like to receive confirmation of dates and venues, or would like us to send details to a colleague, client or friend, please email sarahhewett@fullermarkets.com.

New stock market service - Subscribers to equities sections of fullermarkets.com can now enjoy our daily *Point & Figure Stock Picks*. Investment signals such as base breakouts, confirmed rallies and reversals after downward extensions, are triggered on a daily basis and our comments are emailed with supporting p&f charts. For a free trial to fullermarkets.com, which also includes Fullermoney Plus Online, daily updated charts and our weekly reports, please email: research@fullermarkets.com.

Travel - I leave for the States on 23rd January and should be back in London on the 29th.

The target date for FM201 is Friday 23rd February.

"I believe the future is only the past again, entered through another gate.

Arthur Wing Pinero

Best regards - David Fuller

Fullermarkets a division of Stockcube Research Limited Suite 1.21 Plaza 535 Kings Road London SW10 0SZ UK
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