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Global Strategy and Investment Trends by David Fuller http://www.fullermoney.com

A stock market correction has commenced

Many indices are rolling over following the October rally. Short-term indicators are overbought and a number of markets are encountering resistance near their September highs. Notable exceptions are some of the emerging markets. Signs of near-term technical deterioration are an upside failure by Japan's Nikkei and two comparatively sharp down days for its Second Section Index, following some acceleration. Barring a late recovery, we are also seeing some downward dynamics among the European indices today, including the UK's FTSE 100 Index.

What is worrying investors? Interest rates. First we had US Treasury Secretary John Snow's comments on rate increases earlier in the week. More significantly, minutes from the Bank of England Monetary Policy Committee's last meeting indicated that 4 of 9 members voted for a rate hike. Consequently strategists have revised their expectations for the BoE's first increase, now expected next month rather than February next year. They are also talking about an increase of at least 100 basis points over the next 12 months. While this may or may not happen, expectations of higher interest rates are understandably bearish for equities. Valuations present another concern. Stock markets are no longer cheap following the best rally in 3 years, and some commentators claim that US valuations have returned to bubble levels, especially against the background of 'hedonic' accounting. Some strategists, myself included, have never expected more than a good medium-term rally for Wall Street, within a secular bear market.

Is this the end of the global stock market rally? Probably not, although it could be. I expected a wobble or two in September and October, and we are certainly seeing that. My hunch remains that despite rate hike fears, the medium-term rally for stock markets could carry into 2004 before establishing a significant peak, due to improved sentiment and liquidity. However I have taken protective action today.

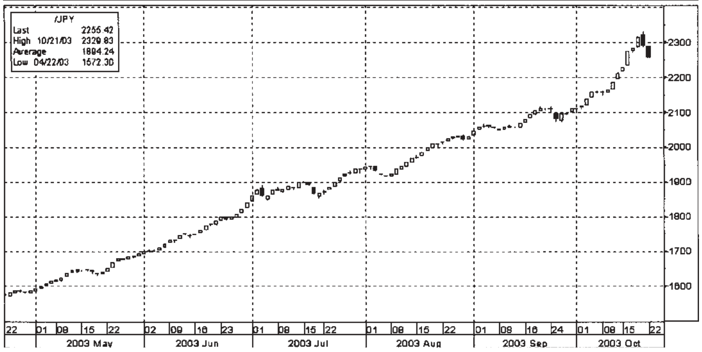
How I'm playing it. I closed my Nikkei futures long today - a position that I commenced building in May at 8060. I have also opened short positions in UK FTSE and German DAX futures, effectively hedging a significant portion of non-gold exposure to equities. Tactically, I will protect these shorts with in-the-money stops, if/when they show a cushion of profit. Captive fund managers may wish to increase the proportion of their funds in defensive stocks.

I'll post a number of index charts on my website later today.

Best regards - David Fuller

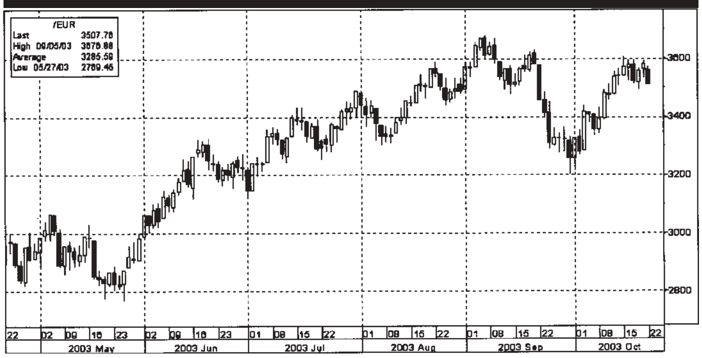
Charts by Bloomberg

Tokyo Second Section Index: 2255 (Daily)



UK FTSE 100 Index: 4273 (Daily)

German DAX index: 3507 (Daily)



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