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THE INTERNATIONAL INVESTMENT LETTER



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Searching for future trends

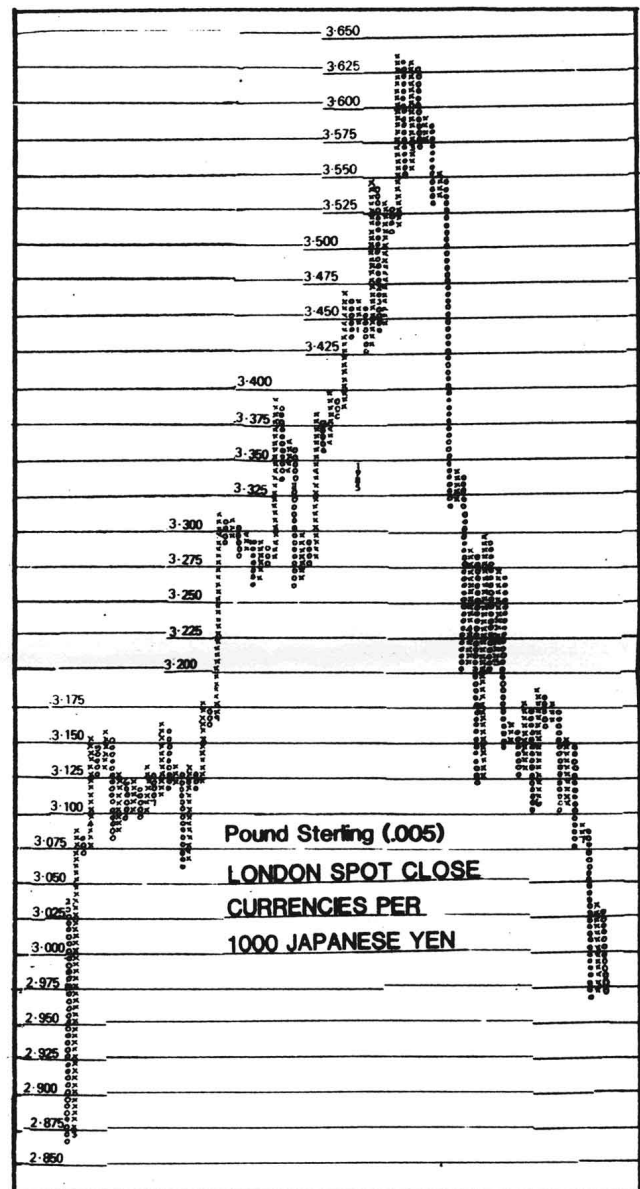
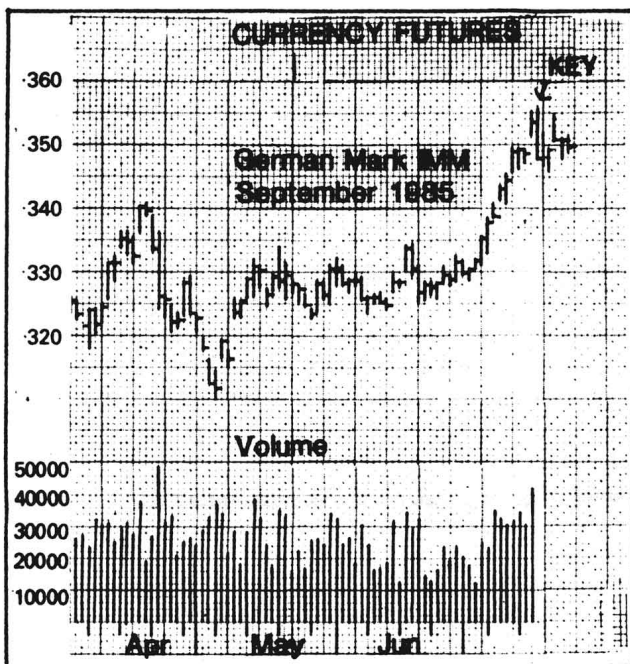
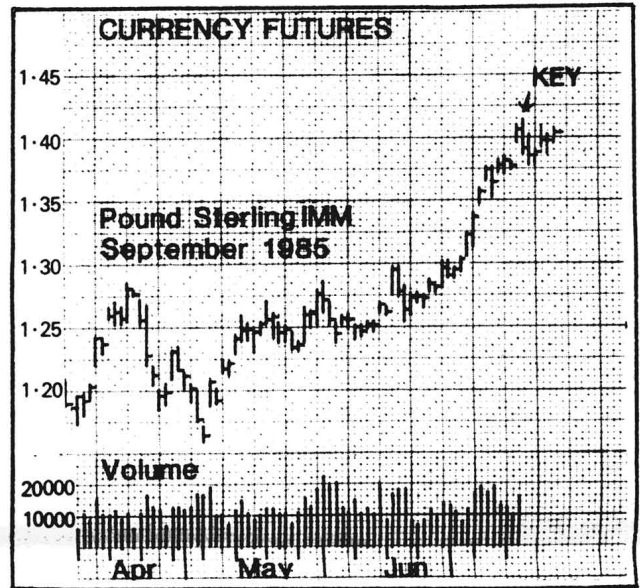
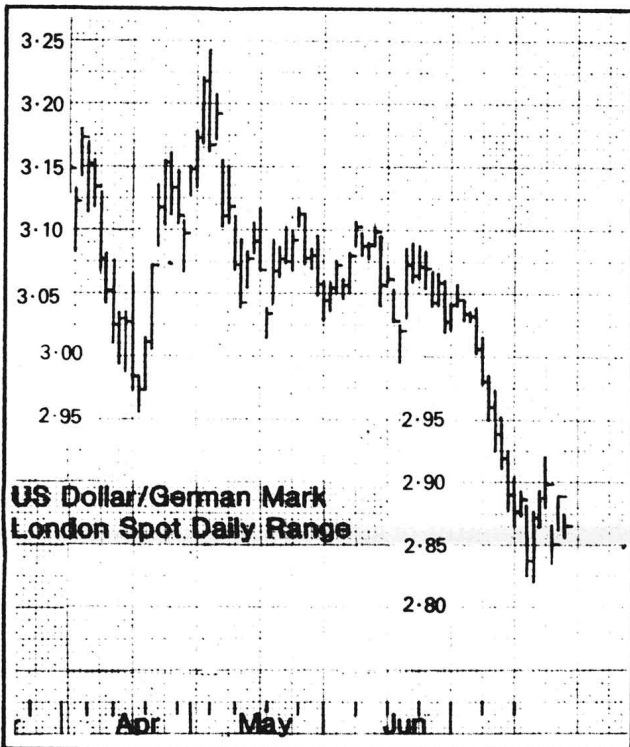
The dollar bear market rolls on

The dollar's type 1 accelerating top in February was followed by a brief period of sideways churning prior to an initial collapse from DM2.95. The subsequent technical rally of just over 50% was short lived, followed by two months of sideways ranging before the **decisive break below the psychological crunch point at DM2.95.** These were classical technical developments as taught at The Chart Seminar, recognizable to anyone with a working knowledge of charts and anticipated in recent issues of FM and Chart's weekly publication, CURRENCY.

What next? The dollar fell for ten out of eleven days during this month's downward step, creating a short term oversold condition which has led to a technical rally, but don't expect much of a recovery. Initial resistance can be anticipated near the April low at DM2.95 and heavy overhead supply is evident above DM3.00. That trading band centred on DM3.05 represents stale bulls who are long and wrong. Anyone holding dollars at a loss will be keen to lighten positions on a rally while many others would sell short. We can expect a small sideways ranging pattern between approximately DM2.80 and DM2.95 over the short term, followed by another downward step. It would take a strong rally above DM3.05-DM3.12 to neutralise downward risk - very unlikely. The dollar remains a sell against all other reserve currencies on small rallies.

The reciprocal chart of the September mark contract shows a key day reversal between \$0.356 and \$0.348, coinciding with the mark's recent short term overbought condition. This is a minor key compared to the dramatic running key day reversal that climaxed the mark's accelerating downward trend in late February. The mid-July key followed an advance of only two weeks, representing the completion of the right hand extension to the overall base formation. This chart shows extensive underlying support below \$0.335 that may not be challenged for the duration of the mark's recovery. Currency speculators could still buy mark futures on small reactions into the \$0.345 to \$0.338 region. These positions could be protected with a mid-point danger line (MDL) stop at \$0.329.

Sterling futures (IMM) also show the running key day reversal in February and the minor key in mid-July, coinciding with the pound's short term overbought condition (see CURRENCY page 61). Sterling futures, which trade at a small discount to spot rates, can be purchased in the \$1.38-\$1.33 range, protected by an MDL stop at \$1.26. I do not expect to see the support evident below \$1.30 challenged.

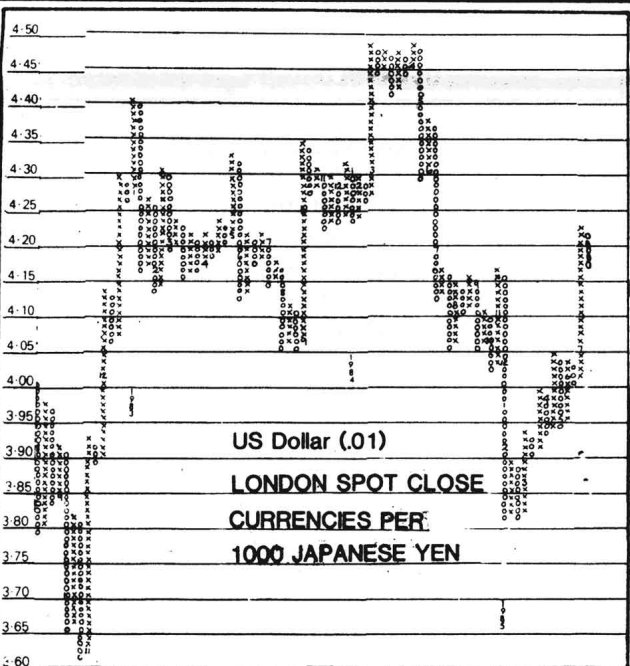
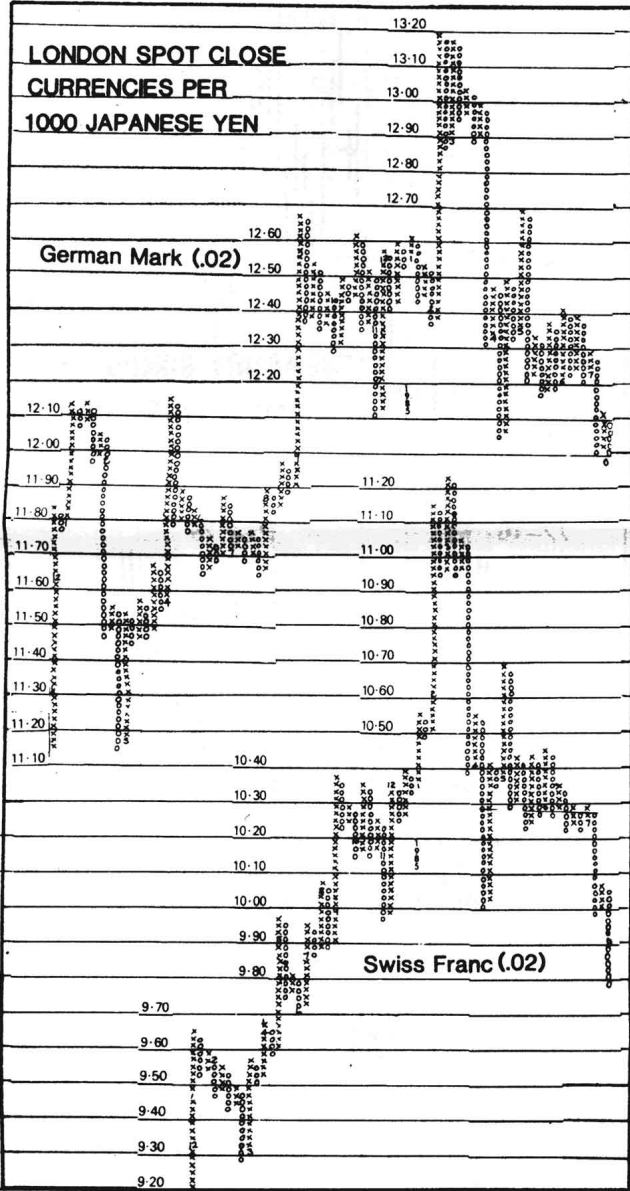


The yen – “undervalued” but weak chart

I frequently hear that the yen is undervalued, whatever that means. Presumably this is in reference to Japan's enormous trade surplus but we all know that currency fundamentals are a “will o’ the wisp”. The reciprocal to Japan's surplus has been America's yawning trade deficit, which did not prevent the dollar from soaring in 1983-1984. A comparison of real returns does not solve the fundamental conundrum because Japanese Euro-currency interest rates have remained static near 6.25% for ages while the yen has performed like a watered down version of the dollar. In other words it followed the dollar's advance against all other

currencies, albeit at a slower rate, and peaked against European reserve currencies in February/March '85.

Charts usually reveal the answers to fundamental

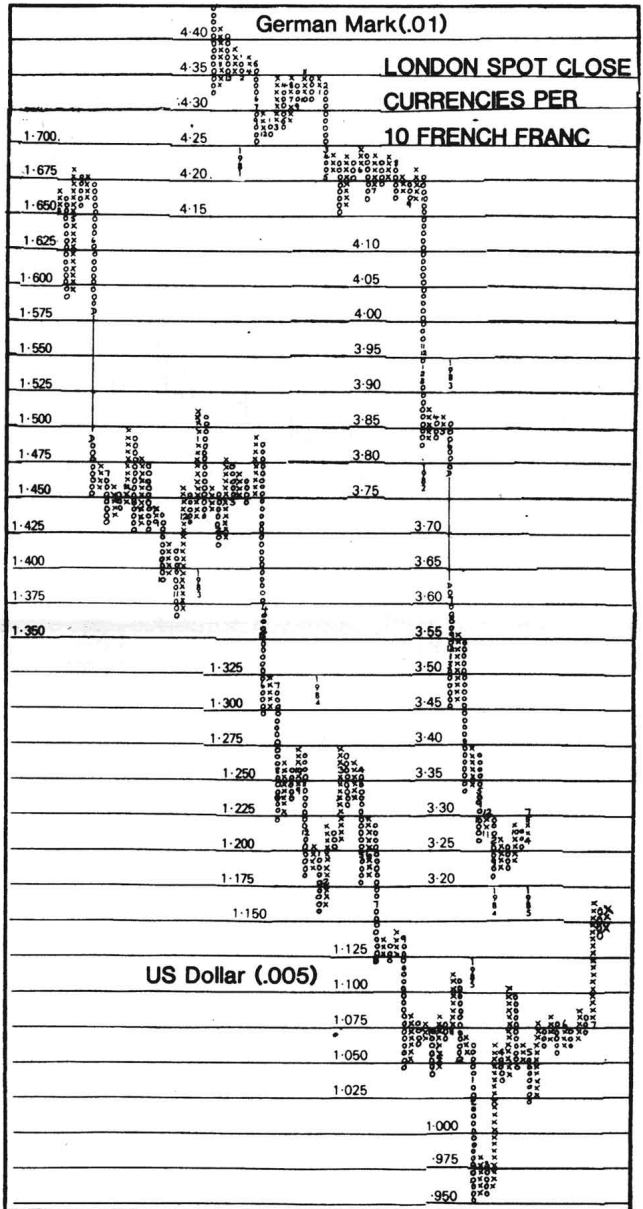


riddles and the yen has unmistakable type 3 top formation characteristics against the mark and Swiss franc. These formations, revealed by churning, time and size of pattern, look totally different from any of the congestion areas that formed during the yen's long advance.

The yen's chart against sterling conformed to an orderly staircase upward trend until the March break back below £3.475 confirmed a type 2 top formation characterised by a severe reaction against the prevailing trend. The rapid decline, now conforming to an orderly staircase downward trend, has already retraced the final fifteen months of the yen's bull market; however, there is no evidence that the yen has bottomed against sterling which has been the strongest reserve currency since February. The yen's only bullish chart pattern relative to other reserve currencies is against the dollar, where an orderly staircase upward trend has been unfolding since March.

The French franc – a recovery candidate

One of my rules of thumb is never to back a socialist



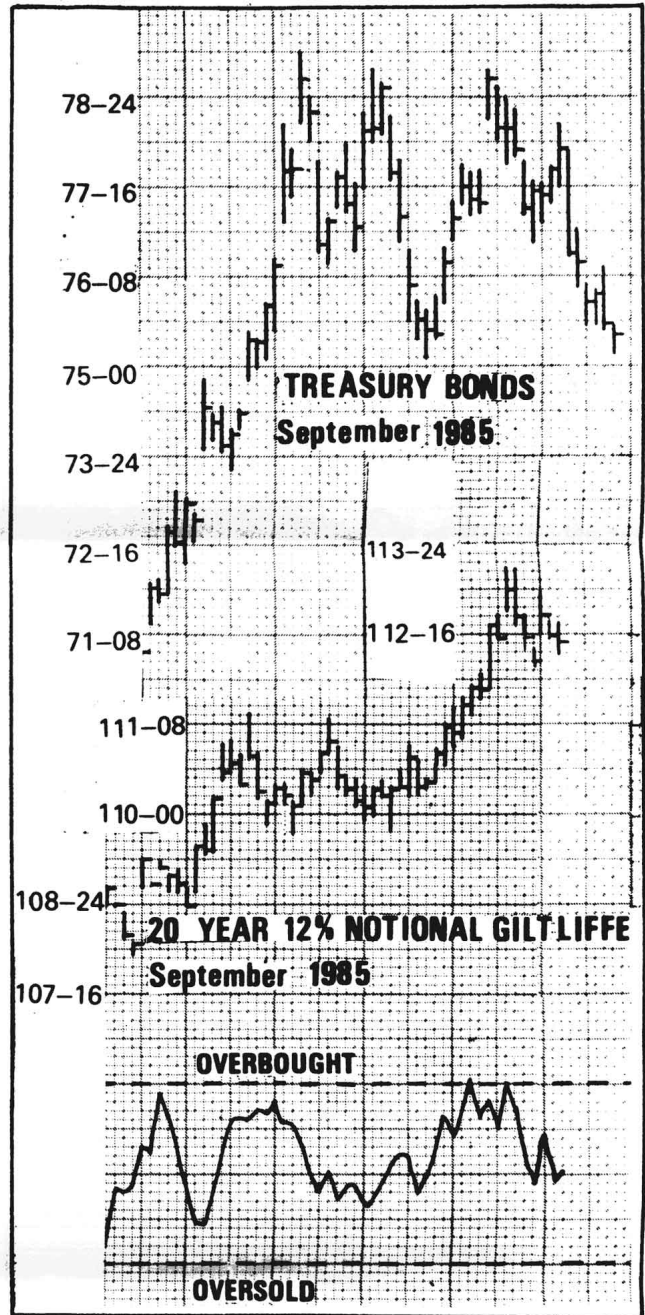
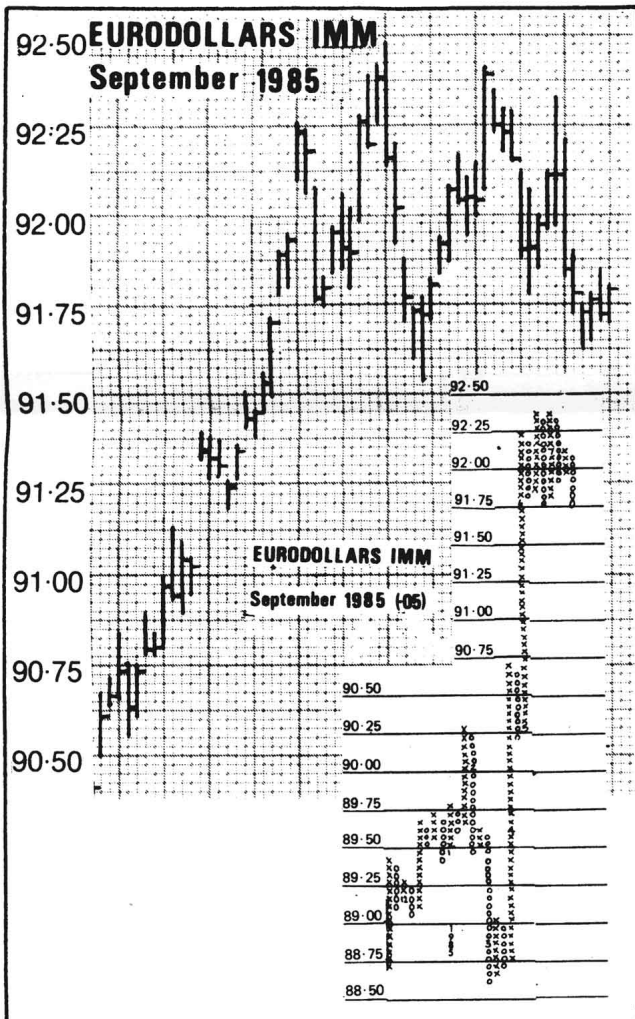
currency, but I can't argue with the French franc chart. As a delegate at last month's Paris venue for The Chart Seminar said: "Maybe France won't have a socialist government after the next election." I'll resist the political forecast but have no hesitation in saying that the franc has completed its type 3 base against the dollar and should now find support above \$1.100 per 10 francs, prior to a further recovery.

Type 3 base characteristics are also apparent against the mark, if you look carefully. This suggests that any future realignment of the French franc within the EMS would be upwards.

US interest rate futures churn in type 3 tops

Those running key day reversals that I pointed out in FM14 stalled the bull market in US interest rate futures. Subsequent attempts to break through to new highs resemble spinning wheels as these markets expend a lot of effort getting nowhere. September Eurodollars should challenge the June reaction low at 91.53, which is unlikely to provide more than tentative support.

This may be no more than a temporary shakeout but traders should use small rallies within the present ranging pattern as selling opportunities. Protect short



positions with a stop at 92.50, which should be lowered to 92.10 on a test of the June low and 91.75 on a move below 91.25. From there on stops should be lowered on a congestion area MDL basis looking for a target in the April-May trading range between 90.75 and 90.13.

Treasury Bond futures have also boiled over providing further evidence that last month's floor of 8% for one year Eurocurrency interest rates (illustrated in FM14) will continue to hold for a few more weeks, at least.

In contrast UK 20 year 12% Notional Gilt futures finally broke decisively up out of their large type 3 base formation as forecast in FM13. These gains are now being consolidated in line with the recently overbought momentum indicator, but I do not expect a decline back below initial support at 111-08. Given sterling's continued strength there is still plenty of scope for UK interest rates to fall further over the intermediate term.

The only negative factor which prevents me from being a more enthusiastic bull of Gilt futures is the contango.

Commodity bears hold sway

Despite over 20 years of working with charts on a daily basis, the persistency of market trends never ceases to amaze me. Dollar quoted commodities have been locked in downward trends for years, frequently punctuated by technical rallies, but a genuine bull market has yet to emerge. Disinflation throughout the industrialised countries provides a fundamental rationale for weak commodity prices, but only the discredited advocates of global depression envisaged the extent of these moves.

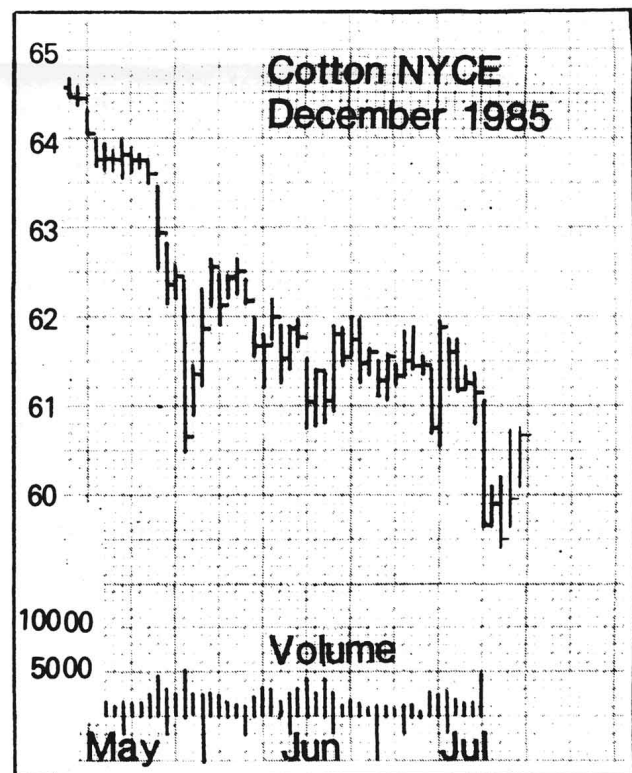
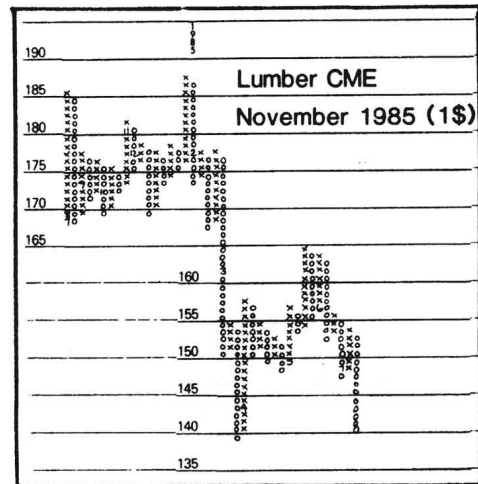
During much of 1983-4 the futures markets were difficult for speculators to handle primarily because of the large pools of capital managed on self-destruct moving average systems. These so-called computer systems succeeded only in triggering each other's buy and sell signals in knee-jerk fashion, compounding the number of whip-saw reversals. Now that most of the commodity funds have been retired wounded or show advanced symptoms of anorexia nervosa, commodity price action has returned to normal.

We have had a lot of fun and our share of profit at Chart Analysis in picking off tired rallies or riding breakouts from big congestion areas. Most of these recommendations are issued through Prestel (daily), COMMODITIES (weekly) and COMMODITY TRADING RECOMMENDATIONS (selectively). This last service, also known as CTRs, is the most detailed including entry levels, stop points and targets. The profits over losses ratio is currently better than 2 to 1 and the average net profit exceeds the average loss including dealing costs. Significantly, our profits on long positions have been in financial futures while the four commodity buy recommendations issued this year have all lost money. In comparison none of the closed out short recommendations has lost money, although one of our current open bear trades, Oct. platinum at \$262, shows a loss at present.

A number of FMs have asked me to write about commodities more frequently, which suits me, having traded them actively for over fifteen years. I have always liked the leverage and low dealing costs. Commodities have a wildly speculative reputation but they can be handled conservatively provided you never stray from my three golden rules of trading: 1) always make your own decisions; 2) never open a position without simultaneously entering your stop and 3) don't let your positions exceed your sleep level.

Turning to specific commodities, many people have lost money or missed profitable trades by pre-empting the end to the bear markets. We know they won't go on forever, and the lower prices fall the better an eventual recovery will be, but no one knows today when the primary downward trends will end. Until we see selling climaxes or evidence of sustainable recoveries, the odds will continue to favour bear trades.

The two latest additions to our CTR bear portfolio



were Dec. cotton on the break below 60.5¢ (see daily bar chart) and Nov. lumber (p & f chart). Cotton is possibly the more risky of the two because of its susceptibility to weather changes during the current USA growing season, therefore I recommend a stop at 62.2¢ to protect short sales in the 60¢ to 61¢ range. This stop should be lowered to 61.4¢ on a break below 59¢ and to 60.8¢ below 58¢, and thereafter on an MDL basis, looking for a minimum target of 56.4¢.

The lumber chart shows a logjam of overhead supply which should produce a downward break before long. Nov. lumber can still be shorted in the \$140s for a target of \$127. I have recommended a stop at \$157, to be lowered to \$150 on a move through \$140 and \$147 below \$135.

Incidentally, I find that clients always want targets, and I like to have a clear idea of market potential. However, the biggest or most consistent moves usually exceed our expectations. Therefore I often shun arbitrary targets on my own trading and use

trailing MDL stops until triggered, or the market accelerates, in which case I will start to take profits.

There is not much to add on precious metals since my comments in FM13. Palladium, the weakest of the big four, fell to my target of \$91 and has not bounced much above that level in subsequent trading. Gold, silver and platinum staged moderate rallies during this month's downward swoop for the dollar, but this looked anaemic compared to the March rally. The psychological support level for gold bullion at \$310 has barely held. Two consecutive London closes below that level would indicate a test of the February low to follow. Critical upside levels are less obvious but I think bullion would have to break above \$325-\$330 and hold that gain for a few days to turn sentiment bullish. Watch the dollar for clues.

CAWI buy signal

After devoting most of FM14 to a review of world stock markets, I'll just update where necessary in this issue. The most important development was the move to new high ground on the Chart Analysis World Indicator. This reversed the early June sell signal and makes overall risk analysis easy. The global bull market trend for equities continues provided CAWI holds above 240 against its current level of 255 – see FM14 or our chart library, INTERNATIONAL, for weekly readings. A move below that level would be a confirmed sell signal.

Naturally performance varies considerably among individual markets. Unaccustomed to sterling's strength UK shares remain a no-go area. It will be interesting to see if any support is encountered near the roundphobia points at 900 (FT-30) and 1200 (FT-SE). I'll stick with FM14's conclusion – any rally is a selling opportunity.

In contrast, Wall Street crept further into new high ground despite a temporarily overbought reading. The three best things going for the US stock market are extensive underlying support, only moderate portfolio gains which deters would-be profit takers and a lot of nervous pundits. I will keep buying S & P futures on reactions and taking profits on the rallies until sharp upward acceleration or downside MDL violation occurs. The new higher MDLs that you should watch are: 1310 (DJIA), 182 (S & P 500), 108.5 (NYSE) and 227 (ASE).

Among continental European bourses, Holland's orderly staircase upward trend continues and the new MDL is 175 for the ANP-CBS Industrial Index. However, the previously accelerating German FAZ Index has lost upward momentum and I am raising the danger point to 470. The Italian and Swiss indices remain very strong although the former is due for a consolidation of recent gains. The SBC danger point is now 450. Sweden remains a no-go area due to the large top formation, but Norway is pressing against an upside break point at 344, while the danger level is 320. Denmark has surged again but may encounter resistance near the Jan. '84 closing peak at 225. The Belgium MDL remains at 2250, while Spain is

beginning to move through its upside MDL point at 110, neutralising downward risk.

In the Far East, Japan and Hong Kong have extended their gains following recent consolidations. The new MDLs are: 12500 (Nikkei Stock Average), 980 (Tokyo NSEI) and 1540 (HK Hang Seng), although I would not like to see a break much below 1640. Singapore's Straits Times Index broke the January low in a bear trap but rallied straight back. FMs should nibble at cash rich stocks on down days.

Finally, South African and Australian industrials have benefitted from their comparatively weak currencies. The new Australian All Ordinary MDL is 870, while I would not like to see a move much below 1075 for the SA Rand Daily Mail Industrial Index. The SA Gold Index is easing towards its 1984-85 support levels between 925 and 850. Remember, it pays to buy **these shares when others are panicking out**. I won't be able to resist if they move much lower. Australian mining shares have steadied above the 500 crunch point on the Metals and Minerals Index.

Despite the improvement in CAWI, I won't make any new buy recommendations this month, except to bid for Genting – see share portfolio review.

Share portfolio review

Further gains have enabled me to raise closing stops for most shares in the FM portfolio, reducing exposure and ensuring greater profits. Skis Rossignol was stopped out for a negligible gain after costs and unfortunately Genting was stopped out for a loss of 6% before commissions, as Singapore's shake-out defeated my tactics. This was a mistake as evidenced by the share's quick recovery. Genting's underlying technical strength is reconfirmed by its ability to rally strongly relative to other Singapore shares. FMs should buy Genting at S\$5.75 or better.

FM8 recommended a 50% purchase of the eventual SA gold share position, to be increased on a decisive break in either direction. I am hoping for a downside flush out to complete the purchases, but wait for it.

Pride and prejudice

Among the many very knowledgeable delegates that I met during The Chart Seminar – Europe '85, was the foreign exchange department head from a Swedish banking group. He wryly commented that the smartest decision he could have made five years ago, when the dollar's long bear market ended, would have been to sack all his forex dealers, replacing them with new kids who had absolutely no experience. Apparently it took the old team eighteen months to recognise that the dollar was in a bull market. Needless to say the bank paid dearly for their re-education.

This conversation took place during the Stockholm venue in early June, when the dollar's trend was the subject of considerable debate. I couldn't resist asking the banker for his view at the time, to which he replied: "I suspect this would also be a good time to replace our dealers."

FM Share Portfolio

	Market	Share	Price Then	Closing Stop (c/s)	Price Now	Strategy
F M 7 S E P T	Australia	Dunlop	A\$1.87	A\$2.14	A\$2.55	raise c/s to A\$2.24
	France	Skis Rossignol	FF1372xc	FF1400	stopped out	
	Germany	Deutsche Bank	DM356	DM544	DM580	hold/unchanged
	Holland	Nederlandsche Middenstandbank	FL149	FL172	FL216	raise c/s to FL190
F M 8 O C T	S. Africa	Vaal Reefs	R173	none as cushioned	R175	hedge by shorting Oct COMEX futures
	S. Africa	Randfontein	R210	with hedge	R205.50	if London bullion closes below \$310
	S. Africa	Kloof	R71	profits from	R78	for two consecutive days.
	S. Africa	President Brand	R60.5	April COMEX	R49.75	
	S. Africa	Harmony	R28	short (\$340.4 to \$312.5)	R26.10	
F M 10 J A N	U.S.A.	General Electric	\$63 ³ / ₈	\$57	\$63 ³ / ₈	raise c/s to \$58
	U.S.A.	McDonald's	\$57 ⁷ / ₈	\$60	\$68 ¹ / ₄	raise c/s to \$61
	U.S.A.	Johnson & Johnson	\$37 ¹ / ₄	\$35	\$47 ¹ / ₂	raise c/s to \$44
	U.S.A.	Merrill Lynch	\$32	\$27	\$35 ³ / ₄	raise c/s to \$30
F M 11 M A R	Germany	Daimler-Benz	DM626	DM805	DM850	hold/unchanged
	Switzerland	Ciba Geigy (Bro)	SF2860	SF2900	SF3500	raise c/s to SF3100
F M 11 M A R	Switzerland	Swiss Reinsurance	SF9500	SF11250	SF12500	raise c/s to SF11750
	U.S.A.	Safeway	\$31 ³ / ₄	\$31 ¹ / ₂	\$32 ⁵ / ₈	hold/unchanged
	U.S.A.	Gillette	\$58	\$56	\$63 ¹ / ₈	raise c/s to \$58
	U.S.A.	Warner Lambert	\$37 ³ / ₈	\$38	\$44 ³ / ₄	raise c/s to \$39
F M 12 A P R	Singapore	Genting	S\$5.75	S\$5.40	stopped out	
	U.S.A.	INCO	\$14	\$11	\$14 ⁵ / ₈	raise c/s to \$12
	Hong Kong	Cheung Kong	HK\$15.0	HK\$15.00	HK\$18.10	raise c/s to HK\$15.50

I was reminded of that conversation while enjoying a drink with FM and technician, Chris Farley, in Vienna last month. We were introduced to a bejewelled and heavily Rolexed foreign exchange dealer from one of the largest US banks. Chris asked him what he was doing with the dollar (DM3.08 at the time). The forex dealer replied that he was buying. Chris asked what would cause him to change his mind, and was told that he wouldn't because the dollar was still bullish. In answer to the next questions as to what he would do at DM3.03 and DM2.95, the dealer replied that he would buy more. Not a man to readily drop a line of questioning until satisfied, Chris persisted with hypothetical levels down to DM2.85. Each time the dealer said that he would buy more because the dollar always bounced back.

Allowing for cocktail hour bravado and the fact that no dealer would be permitted to run a mounting loss, the story shows why most people who did well for themselves, their clients, company or bank, in the dollar on the way up, will lose heavily on the way down. People don't like changes that they have not anticipated. The unexpected is unsettling and therefore resisted. Most market participants don't recognise an onrushing trend change until it has flattened them.

The Chart Seminar – Europe '85 I have described my whistle stop tour of seven cities as a fascinating,

amusing, exhausting and exhilarating experience, enabling me to see old friends and make many new ones. Beforehand the conference experts said that we would not attract enough delegates at £495 to host seven venues. They were wrong. It was Chart's most successful European tour ever, and I think we provided good value.

Here are some relevant statistics. Most delegates were encouraged to attend by someone from a previous year's venue. In response to the question: "Would you recommend this seminar to someone else?", negative answers formed only 0.6% of the total replies. On a scale of 1 for poor to 5 for excellent, the seminar documentation consisting of workbook, chartbooks, etc., had an overall rating of 4.48. My rating as the speaker was 4.74, down slightly from my best ever 4.84 rating during last autumn's USA tour. I could have slipped but suspect this was due to a small number of delegates who were not totally fluent in English.

Although none of my two day seminars are exactly alike because I never use notes and tailor the material according to delegate interest, I felt that Europe '85 was my strongest tour for three reasons: seventeen years of lecturing experience, more emphasis on delegate participation, particularly during market analysis and strategy sessions, and because I ask delegates to provide all the working examples. I am never happy with

speakers who outline a theory and then produce a convenient example to support the method. After a theoretical session I ask delegates to name a currency, stock, bond, commodity, etc., of interest to them and test the theory against the relevant chart. If we have already covered their markets. I'll ask a delegate to pick a random page in one of our chart services for analysis. I believe that analytical methods that can't withstand testing in markets cited by delegates aren't worth the time of day.

The good, the bad and the ugly that's mentionable

The most bizarre incident occurred on the second day of the first seminar, when a previously missing delegate staggered in looking like Lee Marvin in 'Cat Ballou'. He paid with a rubber cheque, slept on the table (something I seldom allow) and fortunately left quietly at the first coffee break. How did such a colourful character find out about The Chart Seminar? Through the Wall Street Journal – honest!

Edinburgh was more attractive, at least in the sunshine, than I remembered, particularly the old sections. The Sheraton Hotel was OK, but I may go back to the recently refurbished Caledonian next time. Cousteaus at 109 Hanover St. was a reasonable fish restaurant. The mussels were best, but the old boys serving weren't up to the task. The highly touted Prestonfield House is a nice place to visit but I wouldn't want to eat there again – very expensive for so-so food and service.

Copenhagen is a beautiful city and I will hold my next Scandinavian seminar there. In addition to the more famous sights I enjoyed the distinctive stock exchange tower capped by four affable looking dragons with intertwined tails. For male FMs who like tall blondes (who doesn't) Copenhagen has more per square mile than any other city. I would like to improve on the SAS hotel – any recommendations?

Fun city Stockholm isn't, and you also pay more for less. The Sergel Plaza Hotel was attractive and the staff meant well, I think, but the place was run like Faulty Towers. Fortunately I was ably supported by one of Chart's wonder women who was always calm and collected with the delegates but kicked plenty of hotel management butts to ensure that things happened on time. Question: Can a 5'2" Englishwoman make a hotel Catering Manager cry? Yes but it's not a pretty sight. The nicest restaurant that we tried was an informal, friendly place called Clas Pa Hornet at Surbrunnsgatan 20.

My Dutch friends tell me that Amsterdam is a city in decline and it seemed jaded, but not the Amstel Hotel, which combines old world charm with good service and great food. The fish dishes are excellent, particularly the eel. Restaurant de Boerderij at Korte Leidsedwardsstraat 69 was a genteel place with excellent service. I confess to gagging on the highly prized raw herring, filleted under your nose and served au naturel, but my companions were made of sterner stuff. I am still looking for a good Indonesian restaurant in Amsterdam, any recommendations?

Vienna has to be one of the world's most genteel, civilized cities. If I search for a fault, one could find

Vienna dull after a while, but it is a wonderful place to rest, enjoy the opera and dine. Vienna is inexpensive, the standard of service in restaurants is remarkable and their best wines are delicious with a slightly spicy flavour, but no hint of anti-freeze. My favourite restaurant was in the charming, small old world hotel, Konig Von Ungarn, at Schulerstrasse 10. I would happily stay there on another visit, but was in the Hilton this time due to the seminar. This has an excellent restaurant, The Prinz Eugen, but it is expensive by Viennese standards. I was delighted to stumble across a Hu Nan cuisine restaurant (hard to find in Europe) of the same name, at Seilerstratte 14. Try the Hu Nan specialties.

I did not have time to see much of Geneva. The lake view is attractive with its boats and the waterspout, and I suspect the surrounding countryside is outstanding; however, there are too many nouveau riche visitors and I didn't find any good restaurants. Recommendations please.

Paris remains a city of contrasts, embodying the best and worst aspects of the European life style. On a drive through Paris one encounters the most spectacular architecture and the worst traffic jams. The Champs Elysees is a haven for poseurs but so many of the back streets are charming and unpretentious. What Paris does best few other cities can equal, but the inefficiency is appalling. The Sofitel Hotel was indescribable – Can FMs recommend an interesting hotel that is also suitable for seminars? One often hears that an Englishman is never unintentionally rude, but a Parisian concierge can elevate studied insolence to an art form. Gormandizers have pushed prices at the 'in' restaurants beyond any rational value for money basis but they remain fully booked months in advance, yet one can walk into any number of delightful bistros and have a superb meal, a classic wine, and spend very little. The one name restaurant that we tried, Marius et Janette, was disappointing. However we stumbled across two unknown places, Le Verdi at 36 Blvd des Italiens, and Le Coupe Chou, 9 et 11 rue de Lanneau, to which I would happily return.

Mermaid race won by De Haas The first person identifying the young woman in FM14's photo was new friend and FM, Jan De Haas, of Bradford and Moscow fame, who I met at the Amsterdam venue of The Chart Seminar.

Stop press

Treasury Bond futures have just led the move below June's reaction low and are at 74-16 as I write. There is no chart support above 72-16 and further confirmation of technical vulnerability would be an inability to rally back above the 75-00 to 76-00 region.

Bond losses are good for gold which is threatening to break above the \$325-\$330 band that I mentioned earlier.

Long term forecast – end July '85's South African gold shares prices will look a steal in two to three year's time.

Best regards
David Fuller