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In its 18th year

Fullermoney

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

Overhead supply will make further near-term gains by global stock markets difficult to maintain but the 21st September lows should hold during a pullback and consolidation phase.

The post-11th September seminal event is a new alliance between the United States and Russia

The Bush/Putin relationship is based on mutual friendship, need and commonsense. I find it fascinating and reassuring that two unprepossessing presidents, who owe their office to patronage, have initiated a significant new thaw in the post-Cold War era. No one thinks George W Bush would be president today if it had not been for his Father's political contacts. Boris Yeltsin plucked Vladimir Putin from obscurity to be his successor, ensuring that the incoming government would not harry him over financial impropriety. Putin was clearly ambitious and after a hesitant start, appeared to favour a partial recreation of the Soviet Union, if only to restore national pride. Disturbingly, he soon cracked down on freedom of the press. Encouraged by former KGB associates and the military, Russia under Putin was antagonistic towards the West in most spheres of influence, notably the Balkans. However the Russian President has become a pragmatist, recognising the limitations of readopting a bankrupt ideology. While Russia's economy has recovered in the last two years, thanks to increased oil exports at higher prices, Putin understands the limitations of a commodity-based economy. He has seen China develop as a diversified manufacturing power and join the World Trade Organisation, while Russia has only its military complex. Putin aspires for Russia to become a prosperous developed country, and for this he needs the West's technology, capital and entrepreneurial skills. September's terrorist attacks gave Putin a window of opportunity to dramatically improve his relationship with the United States and he has certainly done so.

Putin was the first leader to telephone President Bush and offer condolences after the attacks on 11th September. He then ordered Russia's armed forces not to go on alert in what would have been their standard response to the US military emergency. Most significantly, he overruled his generals in not opposing landing rights and troop deployment by the US military in two of Afghanistan's border states, Tajikistan and Uzbekistan. Putin had already developed a personal bond with Bush before the September attacks, which is far closer than his relationship to Bill Clinton. Bush, to the concern of some Western pundits, had said, "I trust Putin; I can see into his soul", a comment reminiscent of Margaret Thatcher's, "I like Gorbachev - I can do business with him", which helped to initiate the Cold War thaw. Putin has moved more quickly than Gorbachev, consolidating his new relationship with the US in a series of bold and unexpected steps. At Brussels for a NATO meeting in early October, he reversed a 52-year doctrine by withdrawing objections to the alliance's expansion eastward into Baltic States. Putin then closed both a large Soviet-era surveillance post in Cuba and Russia's remaining deep-water naval base in South East Asia, while considerably softening his opposition to the US Administration's missile defence programme. Simultaneously, he was re-equipping the Northern Alliance with tanks, munitions and personnel carriers. More recently, Putin has rebuffed OPEC's request for meaningful production cuts. Had he not done so and if a supply squeeze succeeded in lifting prices, this could only further delay a global economic recovery.

The US and Russia are natural allies if they can overcome remaining suspicions from the Cold War era. Cynics will say that Putin is an apparatchik and opportunist who did little more than bow to the inevitable on NATO and also US plans for a missile defence system, cut some overheads by closing the outdated listening station and navel facility, help his own cause in Afghanistan, while refusing to voluntarily reduce dwindling income when everyone could see that OPEC was cheating on quotas because the cartel had lost control of the oil price. All right, Putin will not do anything that he does not feel is in his own interests, just like any other politician. Following the former Soviet Union's disastrous intervention in Afghanistan, he wanted to extend Russia's influence in Central Asia. Consequently, he has backed the side everyone knew would win, once America was committed to removing control of Afghanistan from the Taliban and bin Laden. However I believe these two easily underestimated politicians, Bush and Putin, recognise the many advantages if they can work together. They need each other's cooperation in the war against Islamic terrorism and there would certainly be no gain from reviving the Cold War. The US needs Russia to be a stable source of oil, so that it can be less dependent on the Middle East. Also, America does not want to be overly dependent on China and South East Asia in terms of overseas manufacturing. The former Soviet Union countries are potentially another China in terms of a low cost, educated and skilled labour force. As for the Russian economy, it needs US expertise at every level, to clean up pollution, industrialise, overhaul agriculture, while developing a modern, hopefully democratic, society. Tony Blair has been quick to recognise the US/Russia *entente cordiale* and would like to be part of it, particularly as the leading influence for a like-minded Europe. The UK could certainly be part of a tripartite alliance. It has long been the US's staunchest ally and Blair has recently proposed a new role for Russia within NATO. Putin acknowledged this by saying, "Moscow highly esteems the practical reaction of the British leadership to the Russian president's repeated suggestions on the need to alter the mutual relations between Russia and the Western alliance in response to new challenges". Whether Euroland has the vision to see the former Soviet Union as its China, in terms of opportunity, remains to be seen. Monetary union has caused it to turn inward and Euroland seldom speaks with one voice.

Despite mutual need and benefits, the new US/Russia alliance could not have occurred without their friendship. Bush and Putin have a lot in common. I don't mean the earlier career differences, although Bush knew something of the intelligence service before becoming a politician because his Father once ran the CIA. Both presidents have acknowledged former drinking problems and they share an enthusiasm for physical fitness today. Consequently they have the same athletic appearance and probably worked out together at Crawford, or would have liked to, time allowing. Bush and Putin have a shared interest in spirituality. Both appeared overwhelmed by office in the early months but are increasingly relaxed and confident behind the microphone today. They obviously appreciate each other's sense of humour and the body language speaks volumes. While the folksy Bush has put his arm around other leaders, Putin responded in kind and both spoke of their friendship. Even their wives are similar and obviously get along. At an informal press conference in Crawford, Putin's response to Bush was remarkable, especially given post WWII tensions between the US and Russia: "Of course, it is very important to be born under a happy star and to have destiny facing your way. And indeed, I'm in agreement with the president, perhaps, God was looking quite positively on this. But there are different approaches to addressing such kind of problem. There are people deeply religious who usually say that God knows what is to befall a nation of people or a person. But there are people, no less devoted to God, but who still believe that the people, a person, should also take care of their own destiny and lives. And it gives me great pleasure to deal and work with President Bush, who is a person, a man who does what he says".

Putin wants this relationship with the US to develop and the consequences will be far reaching. By agreeing to help the US in its time of need, he is the architect of this latest thaw in the relationship of two countries that have regarded each other with mutual suspicion for over 50 years. The Russian President signalled his intent with an unprecedented speech in which he traced the history of Russian assistance to the US, from Catherine the Great to the present. However Putin has taken domestic risks by helping America in its Afghanistan campaign. Russian public opinion was against the bombing and a portion of the military remains suspicious of any involvement with the US. Therefore Putin needs positive results to consolidate his position at home. This should not be difficult. We can expect increased American capital and technological assistance for Russia's oil industry, and throughout the central Asian region as well. If the US and Russia can view each other as allies, decisions on the location of pipelines for delivering oil and natural gas to Europe and also to ports for the US become less problematical and more cost effective. This will make it easier for America to proceed against the shared problem of Islamic terrorism, including eventual security for Israel and provision for a Palestinian state. Both the US and Russia have every interest in reducing their nuclear arsenals, and as allies they could lower the risk of nuclear proliferation, terrorism and accidents. If Bush helps Putin to modernise his economy, this would be a boost for democracy and growth throughout the region, ensuring that Russia remains one of the more promising emerging markets for investors.

Interest Rates and Bonds

■ **The cycle for lower short-term interest rates is drawing to a close.**

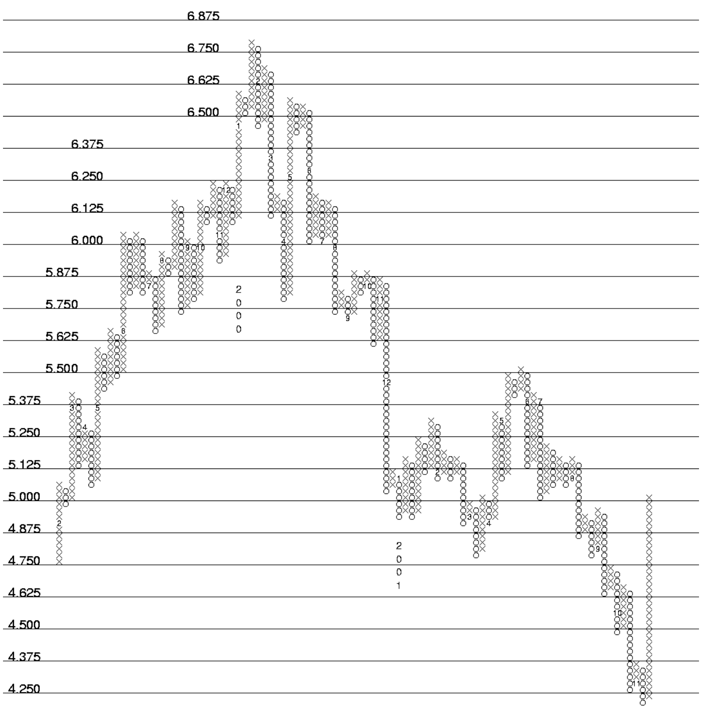
■ **US 10-year government bond yields have bottomed for this cycle at their October 1998 low.**

Greenspan would not hesitate to cut rates again, if necessary, but he may not need to. The Fed Chairman has sliced 450 basis points off the Federal Funds Rate this year - the most dramatic monetary reflation for many years. Combined with a significant fiscal stimulus from the Bush Administration following the 11th September attacks and the earlier tax cut, Greenspan may decide that rates are already low enough at 2 percent. There is some evidence that the US economy is bottoming, helped by lower oil prices. Consumer sentiment is improving due to the stock market rebound and the absence of further terrorist attacks. Consequently the greater economic problems lie elsewhere, in Europe where Germany is dragging the region into recession and in Japan with its worsening deflationary spiral. With short-term rates for Euroland and the UK at 3.25 and 4 percent, respectively, further cuts are very likely. With zero interest rates, Japan is dependent on monetary reflation to check its destructive deflation.

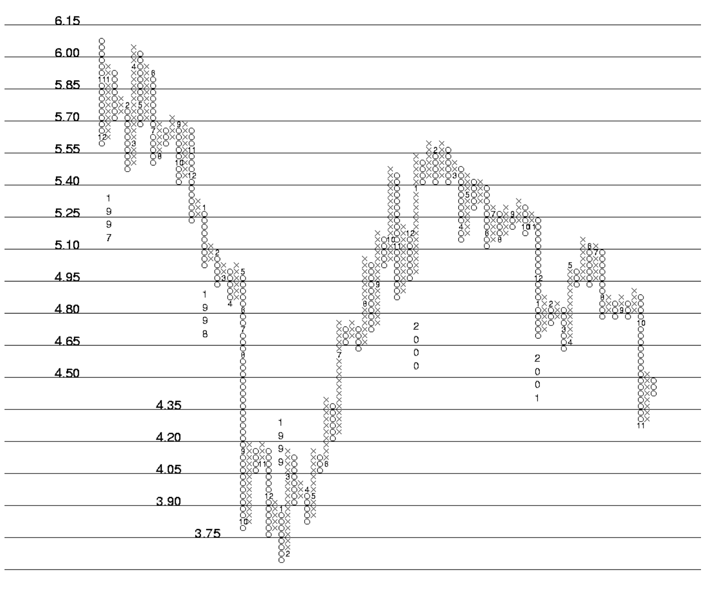
US 10-year government bond yields have surged after falling to within only 0.025 percent of their October 1998 low (*see www.chartanalyst.com or our chart book for that previous floor*) on rate cuts and deflationary concerns. That was an important support level and the rebound has been even more dramatic than we saw three years ago. US long-dated government bond yields have clearly bottomed for the cycle. However having risen very rapidly to a yield of nearly 5 percent and an area of potential resistance on the chart, we can expect a partial retracement, possibly coinciding with a stock market correction, and a lengthy base extension phase. This should eventually support somewhat higher levels but since there is very little chance that 1999's GDP growth surge will be repeated in the next few years, US long-dated yields will probably peak in the 5.5 to 6 percent region, well beneath their January 2000 high of 6.775 percent. Euro-bund 10-year bonds did not fall as far relative to their September 1998 to June 1999 base but they have steadied above that area. This chart pattern is far less conclusive but, now that US bonds have reversed, support from the former trough evident between 4.17 and 3.63 percent for Euro-bunds should cushion downward scope in the event of any further weakness. Currently a close at 4.53 percent is required to indicate a further recovery towards potential resistance evident from 4.62 percent.

Strategy for bonds - From a conservative perspective, my strategy since FM200 had been to favour short maturities - from 3-year government instruments to bills. Last month, in view of the substantial gains in this sector, I recommended lightening positions on strength and also using tight trailing stops to lock in most of the profits on remaining positions. These would have been hit as prices for short-dated issues peaked in the first half of November and fell sharply. Going forward, my recommendation for conservative investors would be to hold only 3-month bills for safety, and corporate bonds for higher yield and capital appreciation, as confidence should improve given prospects for a US-led economic recovery in 2002. I would not buy government bonds following their setback, even though they should rally somewhat, because US yields have clearly bottomed. Professional speculators may be able to justify longs in bond futures for a bounce, anticipating some retreat to this sector when stock markets correct their recent rally. However this is now a dangerous game because the next big move in US short-term interest rates will be upwards. Instead, I would rather wait for a rally by interest rate futures and then look to short.

US 10 Year Bond Yield (0.025)



Euro-bund 10 Year Bond Yield (0.03)



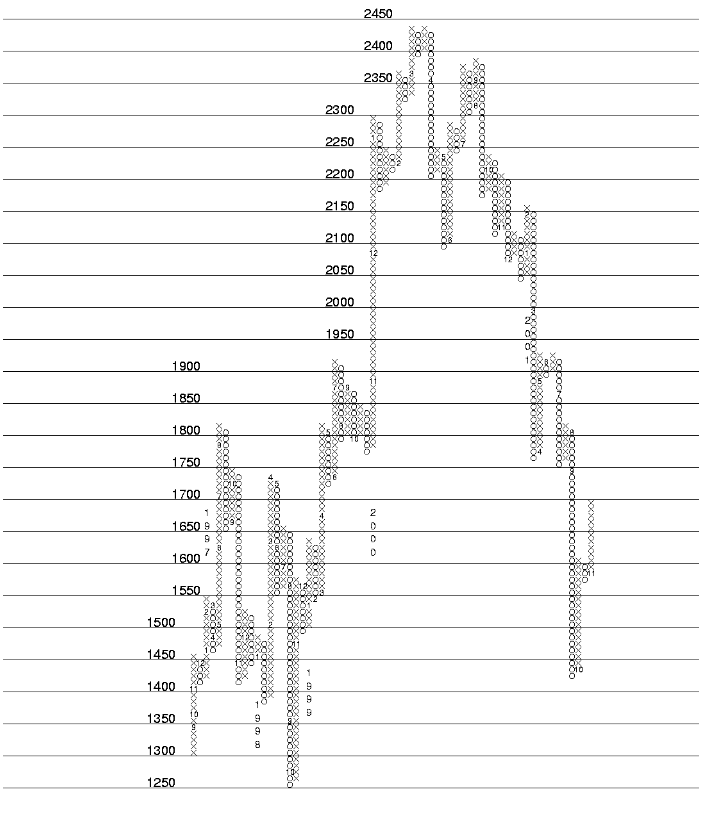
Global Stock Markets

■ **Strong rallies improve fundamental perceptions and the economic background is likely to be somewhat better than previously feared.**

■ **Since last month's question about the bear market appears to have been answered, should we ask if the bull market is almost over?**

Now the earnings glass is perceived as half full. Everyone knows 4Q 2001's corporate earnings will be weak generally but the strong rally since 21st September has encouraged investors to look further ahead. Earnings in 3Q and 4Q 2002 will be stronger, by virtue of all the write offs during the second half of this year, even if the global economic slowdown persists. However, there are very good reasons to believe that a US-led economic recovery will commence during the first half of 2002. Prior to the terrorist attacks on 11th September, only the US Federal Reserve had cut short-term interest rates aggressively but other leading central banks have now followed this lead. Even more significantly, with the OPEC cartel now in disarray, fiscal restraint caused by high costs for energy has been reversed into a considerable stimulus for the global economy. Consequently, another major attack by terrorists is required to delay next year's US-led upturn. A few weeks ago many investors perceived this risk to be high and they also feared serious setbacks in the coalition's counteroffensive. However, al-Qaeda's attacks in New York and Washington appear to have required years of planning and training, and the US was caught off guard. While terrorism can never be completely eliminated, we can assume that al-Qaeda operatives or their potential imitators will no longer be able to move about with impunity. No one should be complacent about the risks, particularly while known terrorists remain at large, but investors can assume that state-sponsored terrorism is on the way out. Overall market sentiment has moved from the extreme pessimism found at lows to cautious optimism.

Chartanalysts' World Market Indicator (10pt)



Technically, we have more evidence that the lows for indices on 21st September will hold but markets have completed most of their near-term upside scope. The front-page headline in my September issue (FM208) was, "Global stock markets have seldom been more oversold". In a subheading last month (FM209) I asked if the bear market was over? I concluded that it certainly could be, despite the ongoing terrorist threat, and that we had seen a low of at least medium-term significance (3 to 6 months). Two months following 21st September, most stock market indices have registered bull market advances, defined by some as a minimum 20 percent recovery from a low, which the DJIA achieved on 19th November. However most indices have seen much larger gains, partly because they fell considerably further from their 2000 peaks than the Dow. Many have now rallied over 30 percent, led by the German DAX at 47 percent. Perhaps we should be asking if the bull market is nearly over? The short answer is no, although I suspect we have now seen most of the initial recovery. Panic selling followed by short covering produced a V-shaped low, giving way to a more gradual, ranging upward extension in line with my FMP157 update. Hedge funds and futures traders probably dominated September's V-portion of the reversal. However other institutional investors have been moving steadily back into the market since late October. Consequently cash reserves will have been reduced and most leading shares have rallied back into overhead resistance. Confidence only two months following a major bear market low is ephemeral. Investors will find much to worry about: corporate profits, valuations, the extent and sustainability of economic recovery in 2002, the crises in Argentina and Japan, not to mention the next and more controversial stage of the war against terrorism following Afghanistan. In conclusion, any additional near-term gains by stock market indices should prove difficult to maintain. I expect them to spill over into corrections before long, during which at least one-third of the rallies are retraced in base extension phases. Nevertheless given all the liquidity sloshing around and the impressive technical action recently, the 21st September lows should hold, assuming we are not nuked in al-Qaeda's dying fling. Thereafter base extensions should support somewhat higher levels in 2002, at least until investors begin to discount the next rise for short-term interest rates. As for the longer-term picture, I maintain that the super-cycle bull market ended in 1999/2000. Therefore new all-time highs of consequence for indices are likely to be few and far between over the next decade or more. Instead, I would not be surprised to see a series of medium-term bull and bear markets, within broad trading bands. These would mostly occur in line with monetary cycles, as we saw during the late 1960s and 1970s.

Chart review of topical and representative stock

market indices - *The 3-box reversal point & figure charts shown are based on closing prices and taken from our website. Anyone interested in this chart service, which includes analysis and is updated daily, should register online at www.chartanalysts.com. Price levels mentioned refer to market closes. The charts were updated through 23rd November's closes. Figures for indices in brackets were taken Tuesday morning on the 27th.*

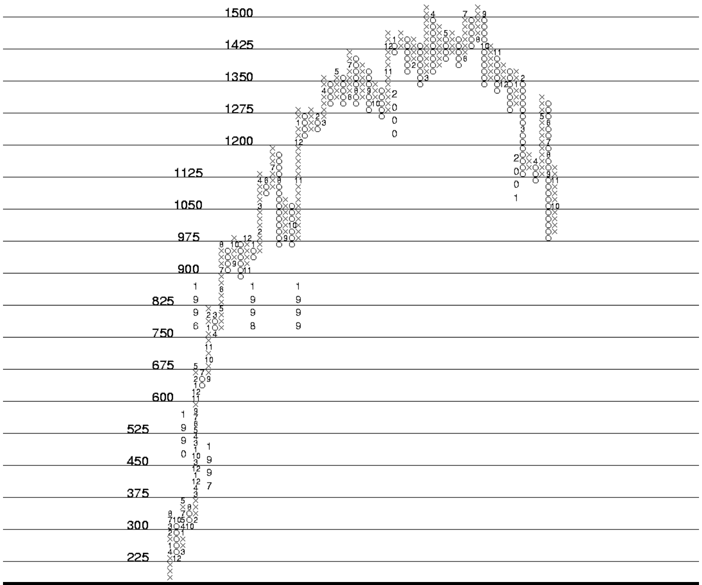
Chartanalysts World Market Indicator (1690) has powered ahead once again following a brief pause. While overhead resistance commences at 1750, on past occasions when CWMI registered a higher high and a higher low, following a sell off, there were further gains to follow. *CWMI is unweighted, based on 15 national indices and calculated in local currencies.*

The US's Standard & Poors Composite Index (1157) has pushed into initial overhead resistance and is testing the overall downtrend following a brief consolidation. While this and increasing overhead supply should make upward progress laboured, a decline back below 1050 is required to reaffirm resistance. **The NASDAQ Composite Index (1941)** is approaching its medium-term downtrend and supply evident above 1975. This should also make upward progress more difficult but a decline to 1650 is needed to reaffirm major resistance in this area.

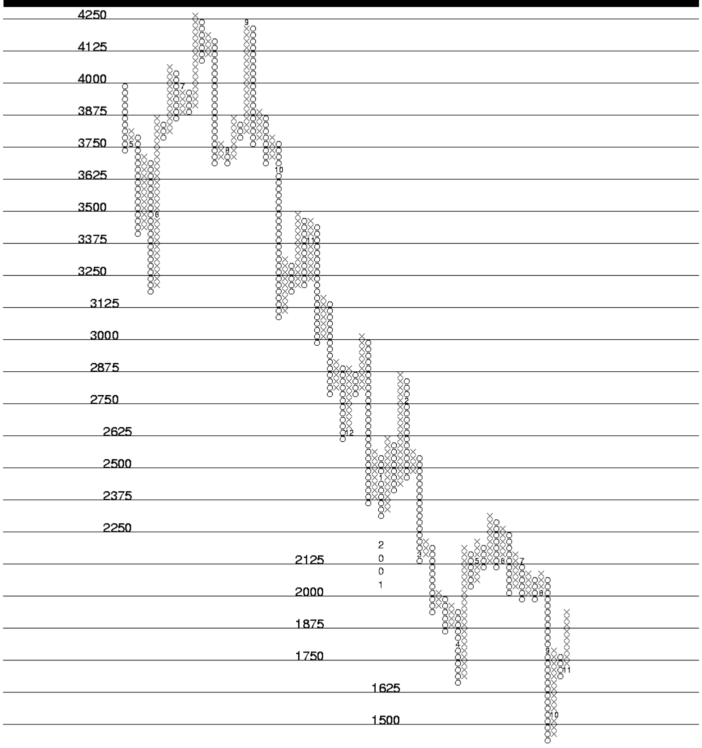
Japan's Tokyo Topix Index (1079) steadied above the September low but is lagging in the global recovery. A break above 1100 is required to signal further gains following the climactic decline from mid-May to mid-September. Conversely, a slide beneath the psychological 1000 level that was not quickly reversed would question the base building hypothesis.

Australia's All Ordinaries Index (3291) has consistently outperformed the world this year and has now retraced nearly three-quarters of the July to September decline. While at least temporary resistance can be anticipated as the former peak up to 3420 is approached, a reaction in excess of 6 units of scale (60 points from the rally high) is required to show a loss of momentum, confirmed by a lower low.

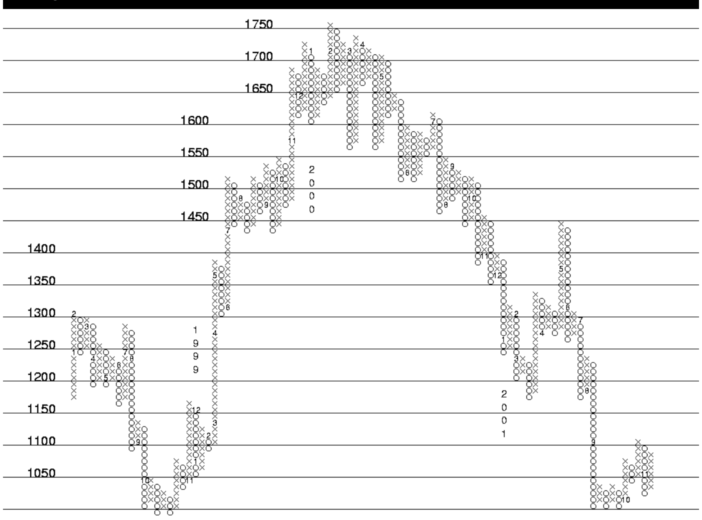
S&P 500 Composite Index (15pt)



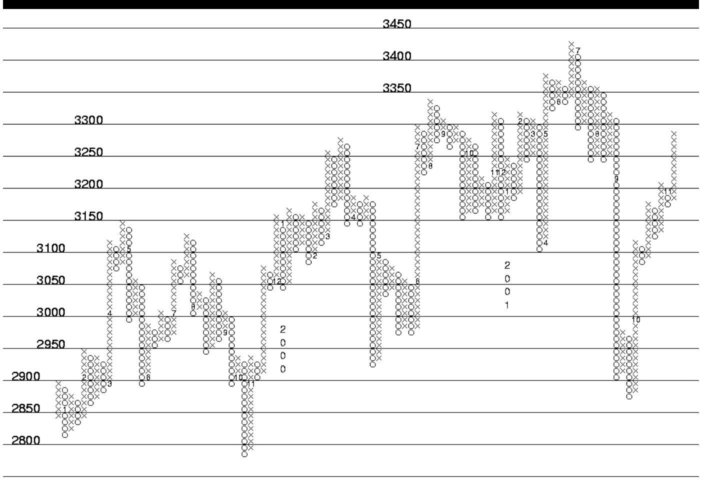
NASDAQ Composite Index (25pt)



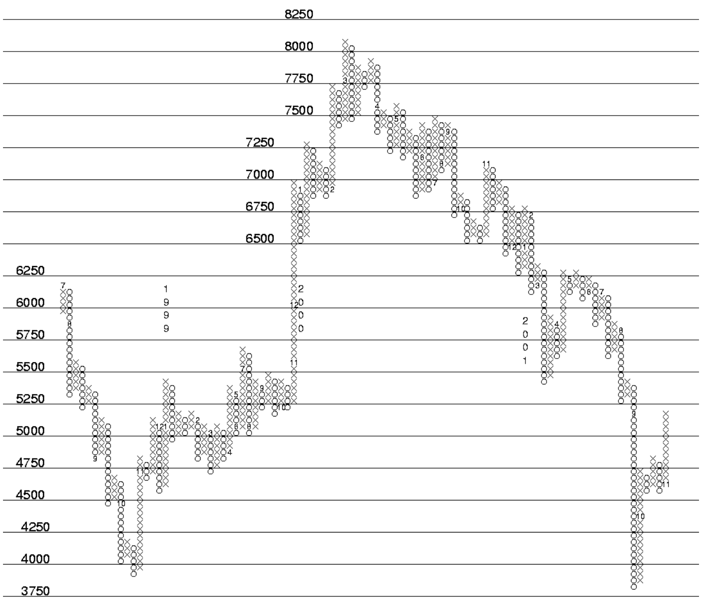
Tokyo Topix Index (10pt)



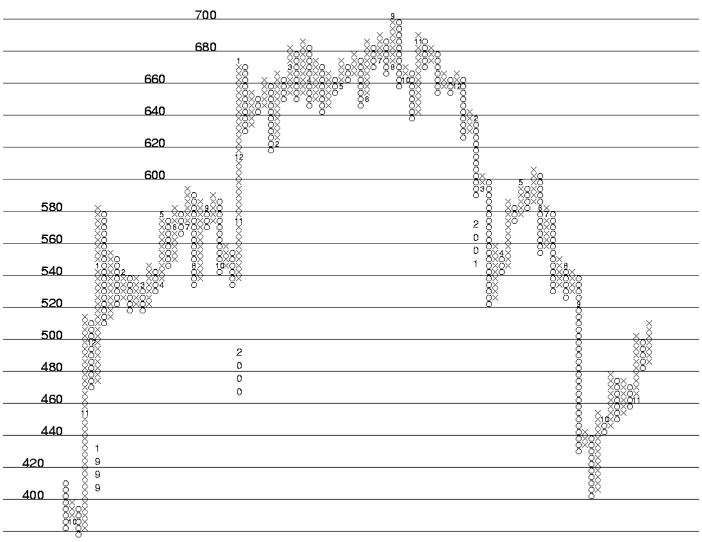
Australia All Ordinaries Index (10pt)



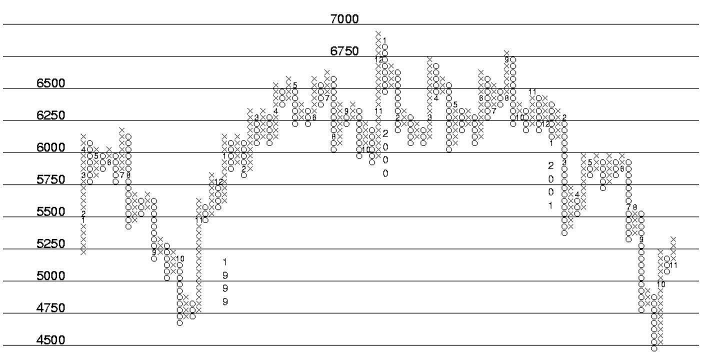
Germany DAX Index (50pt)



Netherlands AEX Index (4pt)



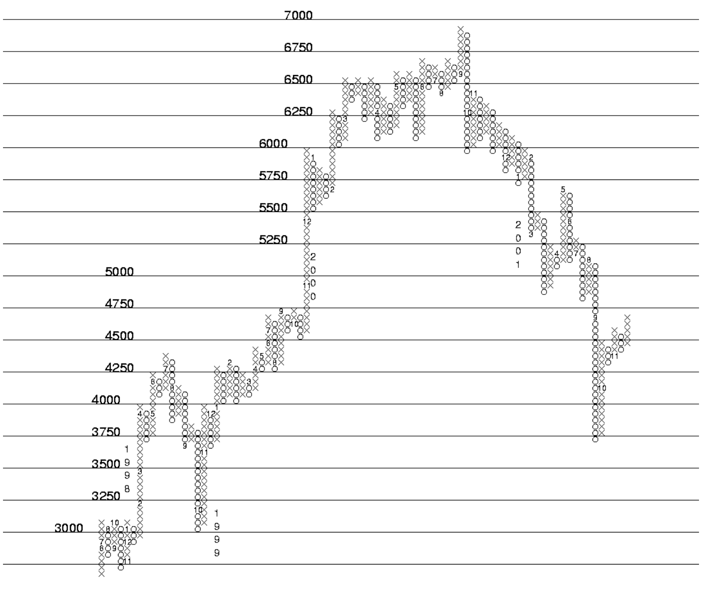
United Kingdom FTSE 100 Share Index (50pt)



Germany's DAX Index (5097) has seen the best recovery among major market indices but is approaching overhead supply evident above 5250, which should impede upward progress. Nevertheless, a sharp reaction is required to confirm a loss of momentum beyond a pause.

France's CAC 40 Index (4564) has seen its recovery

France CAC 40 Index (50pt)



slow and resistance from both the downtrend and overhead supply evident above 4800 are formidable hurdles. Nevertheless, a reaction of 4 units of scale (200 points from the high) is required to indicate a further loss of momentum, confirmed by a lower low.

The Netherlands' AEX Index (505) is approaching supply evident above 520, which should inhibit upward scope. However a close at 476 is currently required to signal a loss of form by breaking the sequence of higher lows and also registering a larger reaction than any since the September low.

The UK's FTSE 100 Index (5291) has rallied back to formidable overhead supply but a decline below 5000 is required to indicate a loss of form beyond a pause.

Strategy for stock markets - Continued strength has provided further evidence that the bear market ended on 21st September. However the easy gains for indices and leading stocks have already occurred, at least until base extension consolidations are well underway. Nevertheless, there is institutional money on the sidelines, waiting for buying opportunities. This may keep stock markets firm for a while longer. I would not chase stocks or futures that have led the recovery and I'd be inclined to take profits if their uptrends loose momentum and/or consistency. If buying, I would favour high-yield issues that have lagged to date. These would include a number of smaller capitalisation companies. However I will not be issuing further buy recommendations without a pullback and base extension phase. Of my three conservative UK selections recommended last month - Northern Foods, Boots and Scottish & Newcastle, the latter two are still in my recommended buying ranges 625p to 585p and 525p to 495p, respectively. I'm holding the Atlantis Japan Growth Fund as a long-term recovery candidate. It is certainly outperforming the Japanese indices but I am not tempted to add because the discount to NAV has declined to 9.23 percent and Japan's indices have lagged in the global recovery to date. I'm disappointed to hear that Ed Merner, the manager, has removed AJG's 25 percent currency hedge. However I chose Merner's fund because he is a proven stock picker. I short the yen myself. From a speculative perspective, I have no long positions in futures at present and am lightly shorting stock market indices on strength, looking for pullbacks.

Currencies

■ **Conversion of European notes has continued to weigh on the single currency but the flow becomes euro-positive in January.**

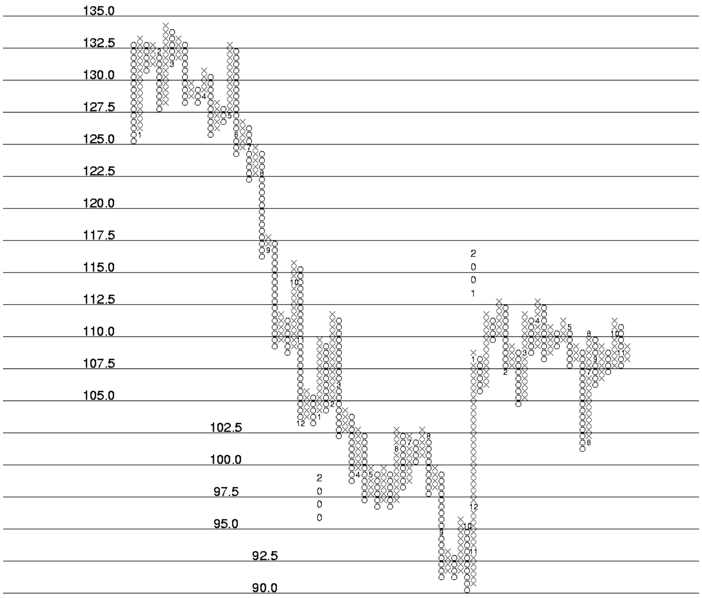
■ **Base extensions against the yen are in their latter stages and will support strong advances for all reserve currencies over the medium to longer term.**

The euro is friendless at the moment, aside from Tony Blair, but the next significant move will be upwards. Traders haven't liked the chart because the single currency has drifted lower. Economists don't know when there will be an economic uptrend for Euroland because Germany is leading the region into recession. No one has any confidence in the European Central Bank, which has been consistently wrong on forecasts, slow to cut interest rates and arrogant in its pronouncements. Meanwhile, the main reason for the single currency's recent weakness is the one-off cashing in of Europe's national currency notes prior to the release of euro paper on 1st January. Many billions in paper money from criminal activity, the black economy, East European hoardings and tourist cash continues to be converted mainly into US dollars, plus some Swiss francs and a little sterling. These people do not want to deposit their notes in bank accounts and they cannot yet acquire euro paper. However, this cash flow reverses from euro-negative to euro-positive in the New Year. No one knows how heavy the flow will be because there are few precedents and none on a remotely similar scale, but it should contribute to a steadier euro in the first half of 2002. Charts support this hypothesis, showing developing bases for the euro, which is currently drifting towards the lower side of its pattern against the US dollar. Any further near-term weakness, should it occur, is very unlikely to exceed the \$0.86 to \$0.84 region and few traders will want to be short euros just prior to the new paper's availability. I expect it to at least test resistance in the \$0.95 to \$0.96 region next year and would not be surprised if it even moved briefly above parity at \$1.00. However, aside from the important factors of price transparency and the removal of currency conversion costs among Euroland member states, there is no other certain advantage for the euro, which has yet to win the hearts and minds of the public. There are obvious disadvantages, including a single monetary policy regardless of individual country economic performance, a stability pact designed for good times only and a charter for the ECB that focuses only on prices. The US economy will recover before Euroland and this coupled with rising US interest rates in the second half of 2002 should strengthen the dollar once again.

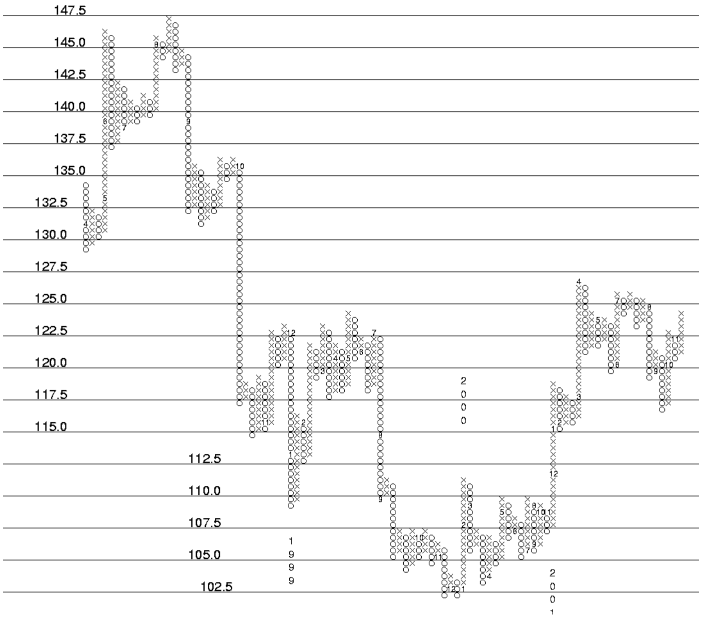
The trouble with base extensions is that they can take a long time to complete. While no one is bullish of the yen, because it yields nothing and the Japanese economic crisis is worsening, not many people are short because the currency remains rangebound. There are two main reasons for this - capital repatriation by Japanese companies to shore up their balance sheets and an insufficient supply of yen in circulation, judging from money supply growth of only 3.6 percent (M2+CD). Japanese firms are liquidating overseas assets, from property to bonds, because they need the money. Meanwhile, Bank of Japan Governor Masaru Hayami is operating a disastrous monetary policy, despite zero short-term interest rates, for an economy experiencing a deflationary spiral. The same thing happened in the US, only worse, following Wall Street's crash in 1929. America's economy did not break out of its deflation and start to recover until the dollar was devalued against gold in 1934. Today there is no gold standard and the yen is a freely floating currency, but it too will have to be devalued before Japan can sustain an economic recovery. This will eventually occur regardless of what the BoJ does, because on Japan's present course bankruptcies will eventually trigger a capital flight. However the sensible policy would be for the central bank to announce an inflation target and print money until it is achieved. Hayami has said that he will not do this and his term does not expire until 20th March 2003. Judging from the charts, the yen will resume its decline against reserve currencies well before then and possibly within the next several weeks, perhaps coinciding with an improvement in the euro's relative performance. Currently, the Swiss franc, US and Australian dollars are trading close to their 2001 highs against the yen. The euro and sterling are likely to follow their lead. Confirming breakouts will indicate commencement of a major advance against the Japanese currency.

Review of currency point & figure charts - *These and hundreds of other 3-box reversal closing basis charts are*

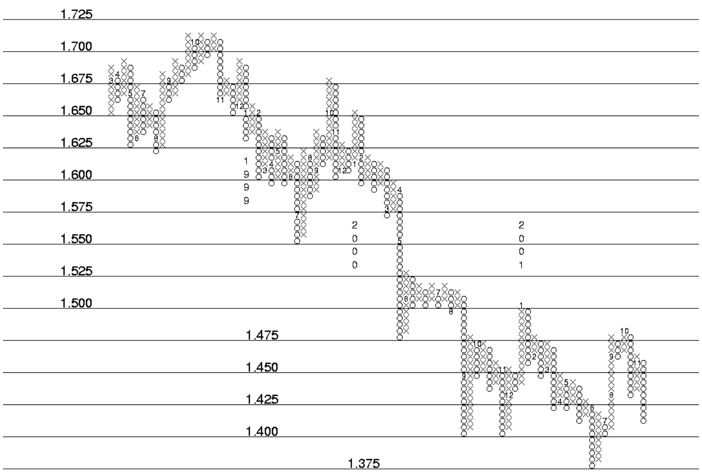
Japanese Yen per 1 Euro (0.5)



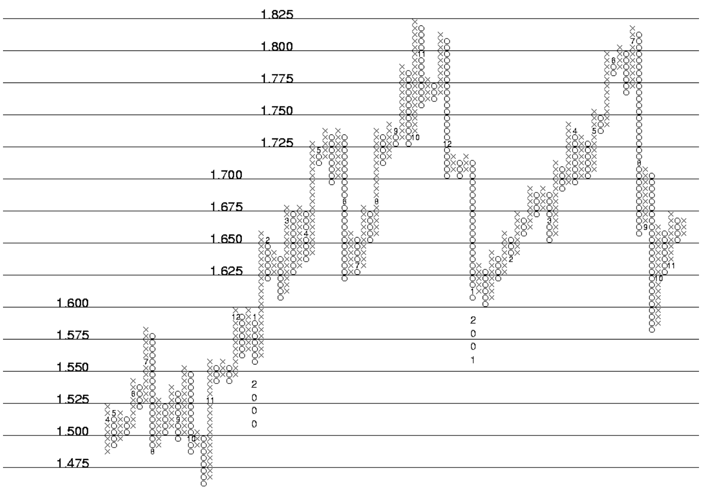
Japanese Yen per 1 US Dollar (0.5)



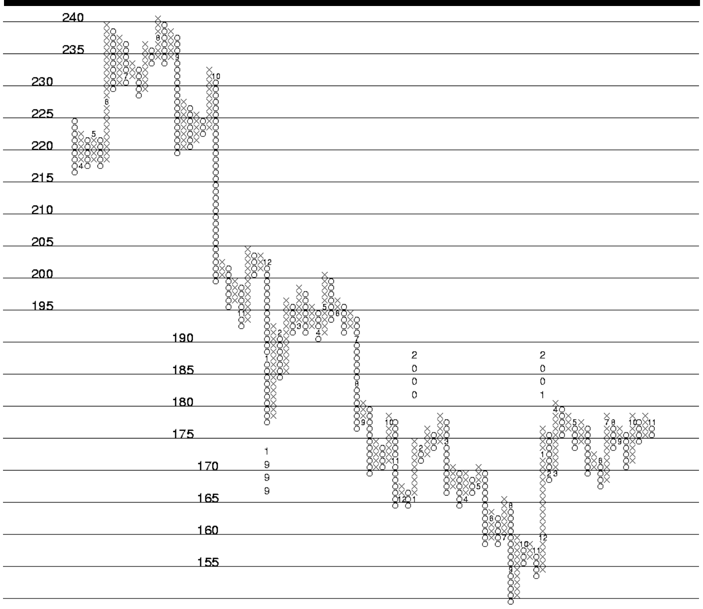
US Dollar per 1 Pound Sterling (0.005)



Swiss Franc per 1 US Dollar (0.005)



Japanese Yen per 1 Pound Sterling (1)



available on our website www.chartanalysts.com and are updated daily. All comments refer to closing levels for US trading hours.

Euro/dollar ($0.8780) - *see previous page* - The euro has eased further since breaking under its September and October lows. A move to $0.908 is required to offset some additional test of the 2000/2001 troughs and signal a recovery towards the upper region of this developing base, which remains capable of supporting a medium-term recovery.

Euro/yen (¥109.16) - Significantly, the early-October gains broke a progression of lower rally highs within the right-hand extension phase of this base. As reaction lows have also been rising following the shakeout in May, we can assume that demand is gradually regaining the upper hand, even though October's push above ¥110 was not maintained. A move to ¥107 is needed to indicate a more lengthy retrenchment but we are more likely to see support near current levels, followed by a successful challenge of the January and April highs near ¥112.5. Once they are decisively taken out, there is very little chart resistance until ¥122.5.

Dollar/yen (¥124.22) - After a brief consolidation the dollar has resumed its push towards the upper side of its

March to November range. The overall pattern, dating back to January 1999, resembles a large base with H&S characteristics, now in its latter stages. A move to ¥120 is now required to delay a successful test of the upper boundary near ¥126. This pattern should support a test of the 1998 highs up to ¥147 in coming months, and further gains over the longer term.

Sterling/yen (¥175.14) - Although the pound backed away from lateral resistance near ¥178 once again, a move under ¥170, which seems unlikely, is necessary to indicate more than temporary resistance here. The overall pattern, dating back to November 1999 also has H&S base characteristics. More importantly, it appears to be in its last stages and a sustained break over ¥180 should signal a minimum run to the ¥190 to ¥200 region.

Sterling/dollar ($1.4095) - The pound has fallen back to the lower side of its September 2000 to November 2001 trading band and should encounter at least temporary support between $1.40 and $1.375. However the overall chart pattern has been characterised by lower rally highs since a peak was established near $1.71 in late 1998. Therefore sterling is still in an overall downward trend, albeit gradual, against the dollar.

Dollar/Swiss franc (SF1.6662) - Once again the dollar is ranging higher after a sharp fall from resistance near SF1.82. The revealing characteristic of this pattern is that the greenback falls within its broad range since January 2000 much more quickly than it rises. This indicates that selling pressure is dominant and the current rally will probably encounter resistance well beneath the highs, leading to a retest and probable break of September's low near SF1.58 in coming months.

Strategy for currencies - A further sell off by the euro and Swiss franc would create a low risk buying opportunity but the better purchase would be against the yen. Short yen against reserve currencies remains the big macro opportunity in my view. The reasons are not hard to understand and are very familiar to readers of this publication. However many people suspect that it won't happen because it hasn't happened, other than the excellent run commencing around this time last year. That was triggered by central bank support and the BoJ intervened again, at the MoF's direction, when the yen strengthened following attacks on the US in September. Significantly, Japan bought both dollars and euros around ¥116 and ¥106, respectively, well above the intervention levels in 2000. Consequently we have a rising floor and, judging from the charts, an open door on the upside once confirmed breakouts occur. It is the size and similarity of these patterns that suggests huge potential, which I believe could take the dollar and euro to ¥200 in the next two to three years. Tactically, the ranging base extension stage has created problems for currency traders and investors, although there has always been the consolation of favourable interest rate differentials during adverse moves. The most profitable strategy in recent months, which I have not always followed, is to buy whichever reserve currency has weakened most against the yen, using the Baby Steps tactic, and then lighten positions on rallies, awaiting another reaction. For instance, the US and Australian dollars provided the best buying opportunities in late September, while the euro and sterling fell back against the yen in November as the two dollar currencies rallied. Consequently, I lightened dollar/yen positions while building up euro/yen and sterling/yen. While I mainly trade these three against the yen, the Australian or Canadian dollars and the Swiss franc are equally viable candidates, subject to timing. A change of tactics will be called for as breakouts above this year's earlier highs occur. I will leverage up, buying on strength where I previously preferred to purchase only on setbacks during the ranging phase. I'll simultaneously use trailing stops, in case there are upside failures. However if currencies continue to rise against the yen, as I suspect, I'll raise stops and average up again, not lightening positions until advances begin to appear overextended.

Commodities

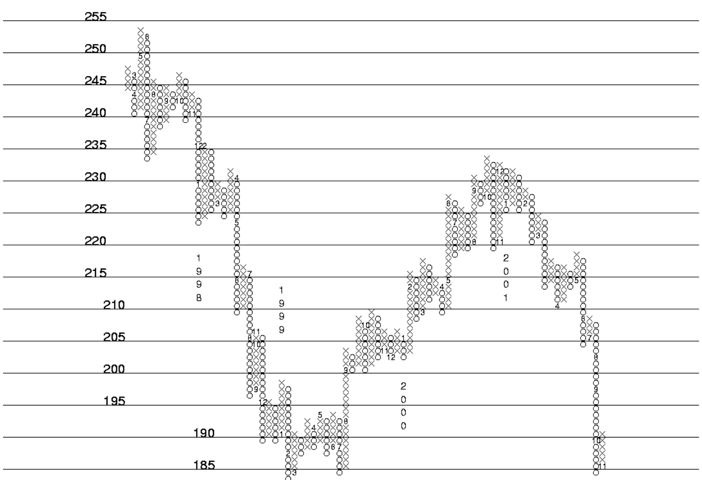
■ **The CRB Index accelerated to its 1999 lows where support has been encountered.**

■ **The OPEC cartel has self-destructed, as they always do, this time with a little help from Russia.**

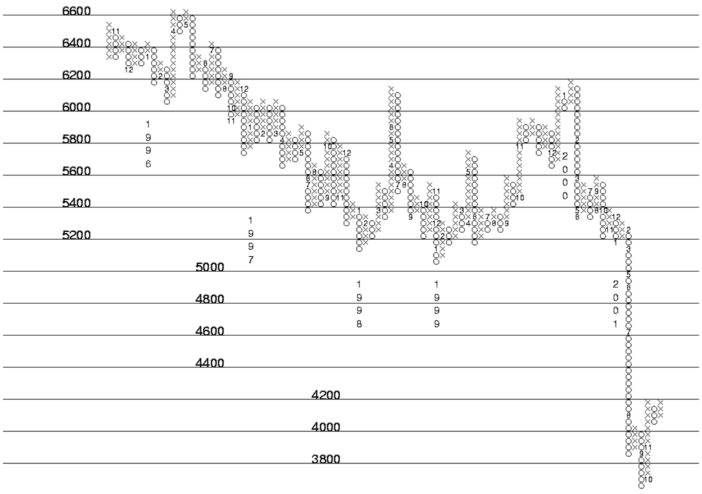
■ **Production cuts by base metal producers have checked declines near historic lows and a bottoming out process is now underway.**

The CRB is a 'mixed bag', weighted in favour of petroleum contracts plus the US grain and bean complex. Nevertheless it is indicative of overall trends among commodities. Having peaked at 233 in October 2000, the CRB rolled over in a top formation and ranged lower prior to a climactic downward acceleration in September and October 2001. That was a trend-ending signal and the CRB has steadied near its February and July 1999 lows. I know all the talk is of deflation but judging from the chart, the CRB Index has bottomed for at least the short to medium term. If this is too optimistic, a decline to 182 would suggest somewhat lower levels.

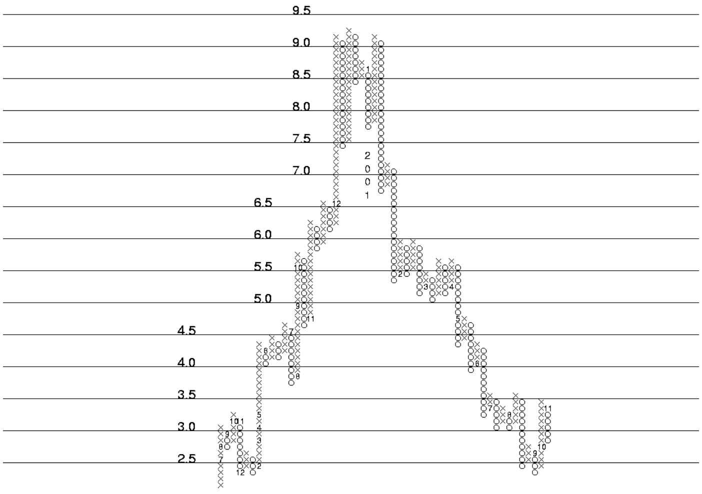
CRB Index NYFE (1)



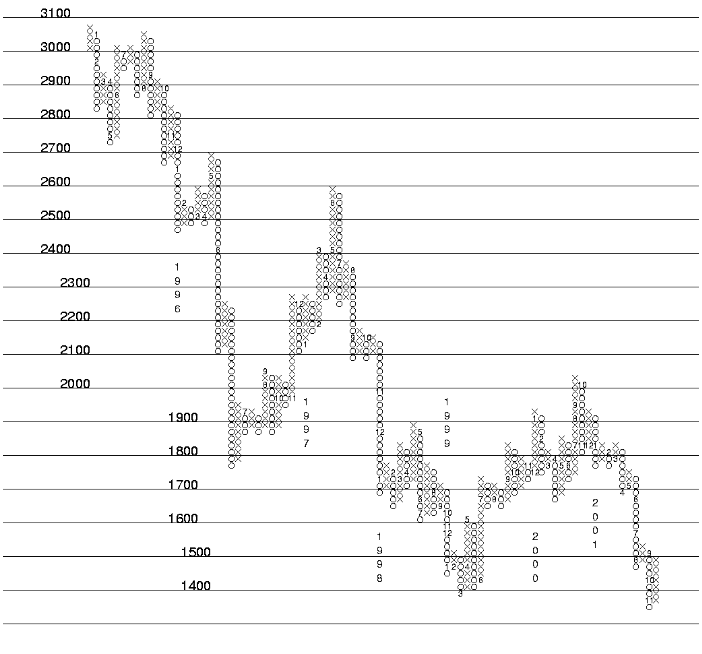
Tin High Grade LME 3 Months (40USD)



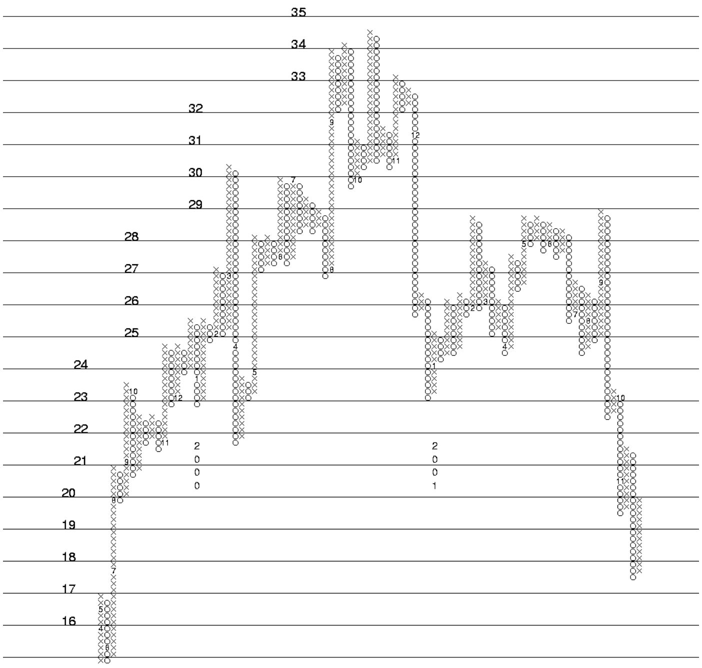
Natural gas NYME 2nd Continuation (0.1USD)



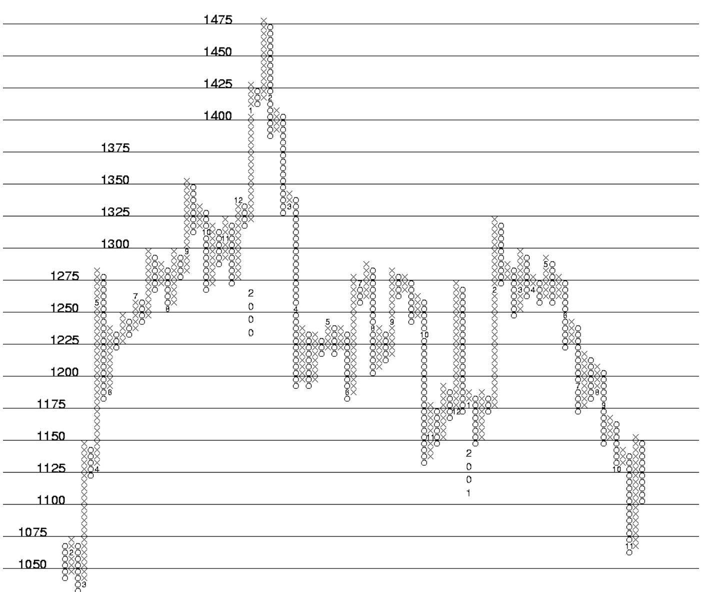
Copper Grade A LME 3 Months (20USD)



Crude Oil IPE 2nd Month Continuation (0.2USD)



Aluminiuim Alloy 3 Months (5USD)



Oil cartels can only succeed for 2 to 3 years, at most. They work best when the price of oil is low and demand high, as we saw in 1999. Cheap prices for petroleum encourage demand and discourage output from high-cost producers, few of which belong to OPEC. Against this background production cuts by the cartel can triple prices or more but it doesn't last. High energy costs cause recessions approximately 18 months later, as we saw in 1974/75, 1980/82, 1990/91 and 2000/01. Economic slowdowns reduce demand for oil and encourage substitution, notably for natural gas. More importantly, high prices eventually and inevitably lead to increased production from countries that are not part of the cartel. As this increased supply weighs on the market, OPEC members recognise that they are losing control and exceed their agreed quotas, as we have seen in recent months. Today, they are talking about further cutbacks of up to 1.5 million barrels a day, but only if non-OPEC producers reduce output by 500,000 barrels. Russia is the biggest of these producers by far and it won't play ball because Vladimir Putin is developing his new alliance with the US. He can afford to pass on a temporary boost in revenue because oil accounts for only 25 percent of Russia's revenue, against 80 percent or more for the OPEC states. Putin is accumulating credits with the West and looking ahead to far more lucrative deals. OPEC would like oil to be in the $25 to $30 barrel region. Instead, the new price band will be mainly in the $15 to $20 region, at least until traders have cause to fear supply disruptions from the politically vulnerable Middle East.

Base metal prices have been an inevitable casualty of the global economic slowdown. Last month I mentioned that Phelps Dodge was lowering its production of copper. Subsequently, other metal producers have announced that they are cutting output, as we have seen on previous occasions when prices are historically depressed. This action is more a matter of necessity than the formation of a cartel. Mining and refining companies cannot go on producing if they are losing money. It would make more sense for them to buy and stockpile their own metal. Futures prices spiked upwards on the news, breaking their medium-term downtrends. Those initial rallies are not holding, because demand is low, but base metals appear to have commenced the bottoming out and base building process, prior to a further recovery as the global economy improves.

The Global Economy

■ **The US Federal Reserve is not "pushing on a piece of string", as many have feared and America's GDP in 2002 will exceed the IMF's latest forecast.**

■ **Lower oil prices along with this year's interest rate cuts will enable the US to lead Europe out of recession next year.**

■ **Japan is not yet implementing the radical measures required to break its deflationary spiral**

Significantly, economic expectations have caught up with reality. In fact, the pendulum of sentiment among pundits may have swung too far, in terms of bearishness. The post-11th September environment has been cathartic for most economists, enabling them to abandon embarrassingly optimistic predictions for GDP, including house views at major institutions, the ECB, IMF and World Bank. There is a behavioural dynamic - a 'born again' pessimist is generally more bearish than on-track forecasters in a downturn, and vice versa. Among the evidence is IMF Managing Director Horst Koehler's prediction on 15th November that the US economy will grow only 0.7 percent in 2002. Today, no one expects Japan to somehow muddle through and radical measures to break the deflationary spiral are increasingly called for. Talk of Euroland's insularity from a global slowdown, still fashionable only a few months ago, has been exposed as a cruel myth. We no longer hear of a 'V-shaped' recovery for the US. Has there ever been a 'V-shaped' economic recovery in a sizeable, developed country? Judging from stock markets, which are much more volatile than underlying economic activity and frequently form a 'V-shaped' pattern, the extremely bearish GDP forecasts will be short lived, Japan possibly excepted. Everyone knows data for 4Q 2001 will be horrific, due to post-11th September trauma, accelerated corporate layoffs and write offs. In recent months I have often been asked if the US Federal Reserve is "pushing on a piece of string" - Keynes analogy for interest rate cuts during a major deflation, such as we have seen in Japan during recent years. The short answer is no. I maintain since 11th September that the US's recession would be steeper because of the terrorist attacks but of shorter duration. Following Greenspan's 450 basis point rate cuts in 10 stages, plus the Bush Administration's sharp increase in subsidies and fiscal spending, America now has a 'guns and butter' economy. Combined with substantially lower petroleum prices than we saw in mid-September, this is unequivocally pro growth and should make nonsense of Koehler's forecast above. While most historic economic data is likely to remain negative for a while, the jump in US retail sales for October is likely to be the first green shoot of recovery.

The importance of oil below $20 a barrel cannot be overemphasised, because no other factor contributed more to the global economic slowdown than OPEC's supply cuts. Welcome to the Bush/Putin alliance - undoubtedly the most significant development following 11th September. The Russian President had already helped to undermine OPEC - in his own country's commercial interest - by significantly increasing oil production over the last two years. This provided a vital boost to the Russian economy and although oil revenues are now falling, Putin looked beyond what could have been no more than a marginal gain in price had he yielded to OPEC's pressure and cut production. Instead, his eye was on the infinitely larger prize - financial, economic and even military cooperation with the US. Lower energy prices are essential to put a floor under the global economy. Today, the massive tax increase imposed by OPEC on corporations and the public in petroleum-importing countries during most of 2000-2001 has been reversed. Consequently, it would probably take a nightmarish event by terrorists, such as a dirty nuke or successful attack on nuclear power or reprocessing plants, to prevent a US-led economic recovery next year. Sadly, the previously unimaginable is now just possible, although hopefully a declining threat in what should soon be the post-bin Laden era. Lesser attacks such as the anthrax letters, also hit growth but should more occur, the effect will be diminishing. Americans are learning to live with domestic terrorism, as have the British for decades in response to IRA bombings, or citizens of most Continental European countries where disputes have also led to attacks on innocent civilians. Euroland's eventual recovery is destined to lag behind the US because of the ECB's stubbornness in delaying far too long on rate cuts and also because budget deficits leave less room for a fiscal stimulus. Additionally, Europe's seemingly more caring employment policies only delay the rise in unemployment that will occur, to the disadvantage of employers, while guaranteeing that more people stay out of work for longer. The UK is in a somewhat better position with employment and regulatory policies that fall between those of Europe and the US. However Labour's drift is towards the European model and taxes are certain to rise next year, with National Insurance the most obvious target.

As for Japan, tragically, there is little sign that Prime Minister Koizumi is advocating growth-oriented policies, let alone embarking on the radical strategy detailed in FM209. Worse still, BoJ Governor Masaru Hayami appears not to understand the reasons for Japan's deflationary contraction, let alone recognise the monetary means for ending this crisis. Consequently he is in serious breach of the BoJ's primary mandate, which is to maintain price stability. It is absurd for Hayami to claim that the BoJ has done all it can by lowering rates and buying bonds, implying it has no tools left to help the economy. Inflation and deflation are always monetary problems. Hayami can print money, which should not be recycled through the debt market but used to purchase property and stocks, as I have recommended. This would break the deflationary grip and Japan could commence a sustainable economic recovery within a year, provided the much-discussed structural reforms were implemented from a position of strength. Without the specified monetary stimulus, a depression beckons for Japan. Everyone with a basic knowledge of economics understands this but under the current rules Koizumi cannot sack Hayami until his term expires on 20th March 2003, and so far he has been unwilling to legislate against his rogue central banker. While domestic and international coercion has nudged Hayami in the right direction, it remains a case of too little too late, evidenced by a contraction in Japan's money supply for October (YoY) from 3.7 to 3.6 percent (M2+CD), woefully inadequate during a deflationary spiral. Unfortunately, Japan is still governed primarily by weak, incompetent politicians and bureaucrats.

And Finally…

www.chartcraft.com - Chartcraft, founded in 1947, is probably the oldest technical research company in the world and it has been part of the Stockcube Research group since December 2000. Its new website covers over 10,000 stocks, indices and indicators for the US markets, plus a daily commentary. I recommend that you have a look, take the site tour and check out the other free information. Subscriber access to the site is a bargain at only $29.99 per month or $299.99 per annum. Chartcraft also produces a number of hard copy publications. Our other websites are www.efmtech.com, www.chartanalysts.com, www.fullermoney.com and more are on the way.

The Chart Seminar, final venue until Spring - My last two-day workshop on Behavioural Technical Analysis, will be in London at Le Meridien Waldorf Hotel, Aldwych, on 29th and 30th November. It should be lively because the markets could not provide a more interesting and controversial background. Everything of interest to the attending delegates will be analysed. For details of this and future seminars, visit www.chartanalysts.com or contact Helen Gent, tel: (0)20 7351 5751, email helen@stockcube.com.

The target date for FM211 is Friday 21st December.

"Compare two men, both billionaires. One develops relatively cheap software and gives hundreds of millions of dollars to charity. The other sponsors terrorism and genocide. So why has the U.S. government spent more money (*in the previous administration*) chasing down Bill Gates over the past 10 years than Osama bin Laden?"

Rueben M Tuck, Hong Kong, IHT letter 2nd November 2001, my italics

Best regards - David Fuller

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