The CJ Investment Newsletter

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A Correction or Worse?

Purpose

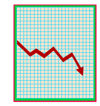
This is a reissue of previously disseminated information.

The *CJ* Investment Newsletter deals with the entire spectrum of securities investing, including cash (money market funds), bonds, equities and options. It will evaluate the overall investing environment and then discuss the relative allocations of these asset types, as well as strategies to implement within them. Essentially, it reflects what I'm actually doing with my clients.

These letters are not sent "cold." Either I know you or someone you know gave me your name. Yes, this letter *is* a sales tool. It communicates how I apply my investment strategies, so that you can decide, without any sales pressure, if my thinking is compatible with how you want your money invested. If you're not already a client, I would like to discuss your *becoming* a client. Please call me for more information.

However, that's not its only purpose. Even if you never become a client, if you want this information, I want you to have it – for a while, anyway. My hope is that providing this information and teaching you what I think is important when investing may help you. Please contact me if you have any questions or comments. I'd love to hear your reaction to my letter.

Quick Look

Market	Next Expected Move
?	

- My most trusted market commentary sources all agree the market should turn down soon.
- The big question: Is this a correction of an ongoing bull market or a new bear market leg?
- If the market does turn down, what's the most likely scope(s) of the move?
- Despite efforts to keep its growth under the radar, M0 (the monetary base) exceeds $2 Trillion again. Money multipliers are near all-time lows.
- The administration's proposed budget will extend the bad times and insure future inflation and/or high interest rates – both economy killers.
- It seems impossible for Washington, DC to understand that REAL spending control and lower taxes is the only way a free market economy can really recover. Their hubris, denial, hypocrisy and profligacy are simply unbelievable.

Time for a Market Downturn

My most trusted reading sources for understanding the markets and their moves all agree that it's time for a market downturn. Actually, they are also in agreement that the downturn is not a correction of a bull market, but

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is instead a resumption of the bear market begun in late 2007. Mauldin is less clear about this than the others, but, reading between the lines, I believe this is also his posture.

I understand their arguments and don't disagree with them. However, such a consensus among them sets off my contrarian "radar" to some extent. Even the best of us rarely "nail" reading the markets and when "everyone" agrees, things rarely play out as "everyone" thinks they will. For that reason, and because my technicals don't really support the new "bear market leg" hypothesis (they don't deny it either), I'm going to withhold judgment on what the true nature of the upcoming downturn is.

Still, I do believe a downturn is imminent based upon my own technical studies. The DJI has rallied to recover almost 50% of the downturn since the 3/9/09 low (over 4000 points), the highest recent recovery being in the mid-50's percentages. All of this has happened without a correction of any significance. This is quite an extended move to have had no real correction. Experience and generally accepted market theory indicates a correction (at least) is long overdue.

Most long-term readers will remember that a correction normally takes back from 1/3 to 2/3 of the previous market move, with the "average" being around 50%. The timing of corrections can be tricky, depending upon whether the correction is a correction of a primary or a secondary move. A correction of a primary move will generally be very sharp and rapid. A correction of a secondary move (which is itself a correction of a primary move) may be slower, since it moves in the direction of the primary trend.

In effect, this could give us some idea of what kind of downturn is coming if it materializes now. A sharp, rapid correction would lend credence to the idea that the upward trend of the market since 3/9/09 is, in fact, a new bull market. A slower, sustained downtrend would support the idea that the rally since last March was simply a (massive) correction of an ongoing bear market.

Even if the downturn ends up as a correction of a bull market, the scope (size) of the correction looks to be sufficiently large to warrant lightening up or selling out of certain positions as a means of protecting capital when the downturn actually materializes. Should the downturn end up being a new bear market leg, we will find cash positions much more comforting than watching wealth disappear as investments continue to decline.

In light of this, we intend, if possible, to be "quicker at the trigger" to sell than we were in Q4 of 2007 and Q1 of 2008. Even though we were positioned for a bear market and we fared much better than most investors and the markets in general, we did not escape unscathed. This time, I hope to be more responsive.

Things are Not as They Seem

Many of you know I do many different studies of market and economic data as a way of trying to follow the trends and respond to them appropriately. It's one of the reasons for the performance differences shown on page 4.

Some of you may remember that I do a study where I try to compare the performances of the major indices versus some measure of "constant value." With all major world currencies not backed by specie, this can be somewhat problematic. What I have done is this: I take the major averages and divide them by two different factors to arrive at two different measures:

- The US$X (US Dollar Index). This gives us the performance of the index restated by the relative performance of the US$ to other major currencies.
- My calculated Gold Index. This measures the relative performance of the index versus a true constant value – an ounce of gold. The index value is divided by the percentage change in the price of gold in US$ since August, 2001.

Remember, the value of an ounce of gold never changes; it's always an ounce of gold. Only the units it is measured by change – that is the currencies in which it is priced. For what it is worth, gold was around $250/oz in 8/01 or about 23% of the roughly $1100/oz it is now. That's how much value the US$ has lost in less than a decade.

Here are the current (frightening) results on 1/29/10:

• DJI	10067.33
• DJI/US$X	7999.50
• DJI/Gold Index	2682.64

Do you still believe the government when they tell us there is no inflation? Draw your own conclusions, but it is clear that the DJI at 10000 in 2010 is NOT the same value as the DJI at 10000 in 2000.

By the way, in current government doublespeak, gold was around $850/oz when Obama took office. Guess that means Bush was responsible for 71% of the increase in 8 years and Obama for 29% in one year.

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Asset Allocation Percentages
CJ Current Suggested Ranges

Dow Theory Market Phase: **BEAR**
Appropriate Current Allocation: **DEFENSIVE**

Asset Class	**Conser-vative**	**Aggres-sive**
Money Market Funds	70-10%	55- 5%
Long Positions:		
Bonds & Bond Funds	30-60%	40-60%
RD Stocks	0-10%	0-10%
Growth Stocks	0%	0%
Gold Equities/Funds	0-20%	10-30%
Bear Market Funds	0- 10%	5-20%
Aggressive Positions:		
Shorts and/or Options	0%	0- 5%

Notes:
Income generating portfolios may not conform to the above guidelines. If income is the primary purpose of a portfolio, income needs are met *first*, then other allocations are made.

Up to 50% of bond/bond fund positions should be in international (non-US) bonds. Such bonds will provide higher interest paid on the face due to the additional *perceived* risk of foreign bonds, as well as providing hedging gains as the dollar declines against foreign currencies due to Fed monetary policies.

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I'm sure they're both quite proud. In a more just world, they should both be arrested for destruction of property – ours – along with their cohorts in both houses of Congress, the Fed and the Treasury.

Spending Control is the Only Way

This is not encouraging, but, if Austrian economics, common sense and history are right, there is only one way for the market to stop plunging, the economy to recover and our assets to stop losing value over the long term. Our representatives in Washington, DC must stop spending more than they receive in taxes (deficit spending) and the Fed and the Treasury must stop enabling them to do so via debt issuance, money creation and artificially low interest rates.

Really, the hubris of these people (both parties) is truly disgusting. While preaching to us they have the "religion" of spending control, they chastise us for our lack of thrift even as they overspend in amounts unimaginable to any person with common sense or any sense of responsibility.

Obama is only the latest in a long line of Presidents acting in this fashion. In my lifetime, the only President who did not act this way was Ronald Reagan. Small wonder that America experienced one of its greatest wealth-creation runs in his second term and the two decades to follow, in spite of more bad behavior by his successors. Obama does seem to have the desire to be the "greatest" of these Presidents, however. How much hubris and arrogance does it take to talk about his predecessor's profligate ways (in which he's right), then proceed to exceed his predecessor's worst year's profligacy by 200% in the first year he has an opportunity?

It's difficult to believe politicians still think we're gullible enough to continue to believe them and to believe in them when they continue using the same poison that made us sick as a cure. We've been using Keynesian techniques and tools since 1937, with the exception of Reagan's first years in office. Look where we are; where the economy is; what the value of the US$ is. Why do they continue to believe that acting in the same way will produce different results? This behavior is the very definition of insanity.

The point that can't be missed here is that, as they have for decades, the government is using inflation and debt to finance current fiscal programs they are too cowardly to collect taxes for currently. The problems this creates are:

- This strategy cheats creditors as debt is paid off with cheaper US$ than were borrowed. Creditors won't allow themselves to be cheated forever.
- This strategy cheats US citizens not close to the source (the Fed), which generally amounts to middle class and poor Americans losing asset values though constant inflation. So, the least able pay the highest price for this behavior.
- If overused, it can destroy a currency from lack of faith in the government and/or the currency by business and international partners and consumer behavior when a currency's value is unreliable.

Are we nearing the "tipping point" where people no longer believe in the US$ and it collapses? Maybe. It's sobering to remember many great empires were brought down by debt issued to finance deficits.

It has to stop. Parties be damned, we need to vote every irresponsible person out of office until we have what we deserve – a fiscally responsible government. We won't be truly free again until we do.