The CJ Investment Newsletter

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Market Assessment & Gold

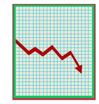
Purpose

The *CJ* Investment Newsletter deals with most of the spectrum of securities investing, including cash (money market funds), bonds, equities and derivatives. It will evaluate the overall investing environment and, from time to time, discuss the relative allocations (including avoidance) of these asset types, as well as strategies to implement them (individual stocks or bonds, CEF's, ETF's, open-end mutual funds, and derivatives). Essentially, it reflects what I'm actually doing with my clients.

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.

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 analyze the markets and economy, as well as 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 contact me for more information.

Quick Look

Market	**Next Expected Move**
?	

- Overall market assessment, including dealing with difficulties in using traditional market analysis tools.
- Gold investing in light of its continuing price drop.

The Big Story

Before getting into the technical analysis of the market, I would like to share a brief overall assessment of the markets for the benefit of newer readers and a review for continuing readers to provide context for the technical analysis (TA) assessment to follow.

In the last few *CJ Newsletters (CJ's)*, we have explored several reasons why I believe the markets are unhealthy, despite a nearly uninterrupted run-up since the last major market bottom in 3/2009. If you haven't read the February, April and June 2013 issues of the *CJ*, some of my assertions will seem more reasonable and supported if you do read them. They appear on the TCM website.

The largest overarching problem is similar to attempting to treat a cancer patient with anabolic steroids. The patient may look and feel better. He/she may gain weight and regain his/her natural skin color. To all

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outward appearances, the patient appears to be getting well. The catch? *Anabolic steroids don't cure cancer. They may, in fact, accelerate the course of the cancer. The patient still has cancer* and, despite feeling better, will probably not live as long as he/she would have had he/she never been treated with it, except, perhaps, in the very final stages leading up to death.

- The patient is the economy, including the investment markets.
- The cancer is excessive governmental business burdens though taxation, regulation and manipulation. *Especially* manipulation.
- The steroid is the massive monetary creation by the Fed in a vain attempt to fight the laws of human nature and counteract the "cancer" created by other parts of our governments. Especially since 3/2009.

That's where I believe we are. I don't trust this market and I haven't since the "artificial" bottom that occurred on 3/2009. (See last month's *CJ* for the 3/2009 sandpile bottom explanation.) Having gone through a multiyear recession and a "slow growth recovery" (ha ha) since that time, little has happened to fundamentally improve the economy to justify the 125+% increase in the DJI since then. It's simply the result of steroids (massive Fed monetary injections). One might add that is a familiar territory if you look around; it looks a great deal like the run-up to the 2007 peak followed by the 2008-9 crash. Except, of course, the markets are at even higher levels, with even less below them for support. Just like Wile E Coyote running suspended in mid-air.

It's why TCM has been extremely defensive with client and personal investments since then. TCM has targeted 25% cash, small ETF hedges against the upcoming crash, and securities with significant real cash returns as a way of protecting clients from the fall that, in my opinion, is inevitable, but perhaps not imminent. TCM has also taken extreme caution when entering any new positions, especially ones whose returns are based upon appreciation instead of cash yield.

Of course, it's undeniable that the markets have appreciated. Way beyond what I would have believed possible. Many of the reasons for this were covered in the above referenced *CJ's*, along with many of my other newsletters over the last few years. But the core problem caused by the Fed's excessive monetary printing is the economic and market distortions explained over the last few months and years in previous *CJ's*, also explaining the massive (unsupported) rise in the stock markets. (See the 2/2013 *CJ* for explanation, especially the "Super K" concept.)

My conservative investment stance is based upon history. While I called the 2007-8 peak and had clients prepared as much as possible for that fall, the new higher distortion levels caused by the Fed actions has crippled many traditional fundamental and TA market tools (discussed previously, including in last month's *CJ*) which could help predict when the next crash might occur. I know of no one, including myself, who could now reliably predict when the next crash will occur. We know it will happen and that it will be bad, but the Fed's distortion of economic forces through its monetary actions makes even the best market analysts' crystal balls too cloudy to read. (As explained several times this year, I created compensating calculations for my *CJC Indicator* late in 2012 and started using them in 2013, creating my new *CJC2 Indicator* in order to restore accuracy to my primary timing tool from the Fed created distortions.)

Governments Do NOT Encourage Commerce

This might be an appropriate time to make an assertion that may be surprising, but should actually be obvious. Beyond the basic functions of protecting private property rights and doing what they can to insure economic transactions are uncoerced, ***governments do NOT encourage commerce***. Period. If you doubt this in any way, please read the famous booklet, "The Law" written by the brilliant Fredric Bastiat in the mid-1800's when a more free capitalistic USA gave him hope for mankind's and womankind's futures.

When a politician or economist suggests otherwise, what they are really describing is that the government(s) may choose to lighten the tax and/or regulatory load that currently burdens business. Put another way, by removing some existing government obstructions***, business is discouraged less, not encouraged***. Often, the chosen sectors or the economy in general will respond to the lighter load by expanding, creating jobs, etc. Until, of course, the politicians in the government decide to close the "loophole(s)" and reburden business! This happens when the pols need tax revenues to buy votes or choose to belittle opponents *audacious* enough to think a more free market country may actually be good for its economy and citizens.

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After all, as Al Gore said, "It's the government's money."

Technical Market Assessment

While many American professionals use the SPX as a proxy for the stock market, many, including me, use the DJI. After all, the DJI 30 industrial giants' annual production represents approximately 20% of the US economy, the last I heard.

The DJI was one of the first, if not THE first market index ever constructed. In addition, Dow Theory was the first major TA method I'm aware of. Constructed by Charles Dow himself over 100 years ago, charting and comparing the movements of the DJI and the TRANS (then the "rails") was the first "reliable" TA method. TA simply means using charts to interpret the movements of a market and to provide some guidance as to future movements from that study. The simplest TA charts are simply price and volume data. Virtually all the more sophisticated TA techniques calculate derivations of the core price and/or volume data.

(The next few paragraphs are highly technical [nerdy] and may delve deeper into this subject than you may care to. If this is so, please skip ahead to the last paragraph in this section.)

Applying my *CJC2 Indicator* (*CJC2*) to the weekly DJI, the preponderance of cyclic action indicates declines from current or previous tops. There is also a large bearish divergence currently in play with my special MACD. The daily DJI is less clear, with at least one long cycle clearly in ascension. There is a bearish divergence, but it is not as long, nor as clearly present as in the weekly chart. The weekly SPX presents similarly to the DJI, except that it has one major cycle in ascension and another cycle that should bottom in Q1 2014, providing even more lift. The daily SPX appears to have all major cycles in descent, although a couple of the mid-level cycles indicate another small bounce could occur prior to a major downturn beginning.

Generally, a bear market is considered to have occurred when a market index declines by 20% or more from its market peak. When coming off a market bottom, a bull market would happen when the index appreciates 20% or more from the preceding market bottom. Retracement levels do not use absolute percentage declines or increases. Instead, retracement levels are based upon the *range between the previous peak and bottom.*

For example, if an index rose from 100 to 150, then began to decline, the decline is a *retracement and is expressed as a percent of the previous move*. If the index is now measured at 140, then the retracement of the previous rise could be expressed as (150-140)/(150-100) = 10/50 = 20%. Similarly, if an index declined from 150 to 100 and rose again to 125, the retracement of its previous decline could be expressed as (100-125)/(100-150) = <25>/<50> = 50%.

Accurate targets are difficult to provide. However, my current *CJC2* charts indicate the following Fibonacci retracement levels are important (all are rounded approximations):

- The DJI: 14230 would provide 14.6% retracement of the rise since 3/2009, 13410 would provide 23.6% retracement, 12080 provides 38.2%, and 9950 retraces 61.8%.
- The SPX: 1530 & 14.6%, 1440 & 23.6%, 1290 & 38.2%, and 1050 & 61.8%.

Of these retracement levels, the most important is the 61.8% level, then the 38.2% level. In Fibonacci thinking, the *golden ratio* of 61.8%, ubiquitous in nature, is the strongest retracement level for support purposes in a market downturn. Should it be breached, there is no meaningful support to prevent the retracing of the entire move since 3/2009. That is, back to about 6550 or so. The 38.2% level is the second strongest; its breach is of major import also.

(Reentering the English language…)

The timing of such moves becomes problematic. Crashes are generally not smooth and they usually happen much more quickly than the previous rise did. I would be surprised if the entire downward move would not be complete just prior to the 2014 elections (5+ quarters). Common sense also indicates that if the markets do decline past the 38.2% retracement support level, markets and the economy would clearly be major issues and factors in the 2014 mid-term elections. The pols won't be able to focus their discussions entirely on their social agendas in 2014!

TCM Gold Investing

After a long price decline by gold, the *CJC2* indicated that gold had reached buyable bottom a couple of days after gold reached a closing low of
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$1,388 on Monday 4/15/2013. A "buyable bottom," at least to me, indicates that a purchase of a security has a higher than average chance of appreciating without declining much further. "*The*" bottom for a particular move can only be determined after the passage of time.

Because I was and am suspicious of this market anyway due to all the governmental manipulations and because the *CJC2* indicated there was a *chance* this downward move in gold had another leg, TCM placed most clients into a 5% position of a physical gold CEF (closed end fund). This position represented actually only ½ of what I eventually wanted TCM clients to have in their portfolios. If gold presented itself at a lower level, the other ½ could be purchased then. If it went up, the remaining ½ position could be "bought on a dip."

When making moves of this sort, I rarely try to "catch a falling knife," as the old saying goes. I will usually wait a couple of days to see if the investment rallies before actually entering the position. I followed that same caution this time also. Of course, this technique, at best, only provides some short-term protection against decline.

After an initial rally, the price of gold has declined further. My initial readings of this decline indicate that gold has now retraced almost exactly 61.8% of the rise ending around $1950 in 9/2011. It also coincides perfectly with the longest (and strongest) daily cycle and the second longest weekly cycle on my *CJC2* charts.

Which means, TCM clients will buy that other ½ position in the physical gold CEF when gold begins to bounce.

Some reasons for doing this are:

- Having reached the golden retracement level on a perfect cycle bottom is almost as strong of a signal as this technical analyst thinks exists in this world.
- No one that I have heard or read has provided a sound, reasonable explanation of just why gold would have experienced such a decline. Sorry, just saying "lack of demand" is NOT an explanation.
- Many or most significant worldwide currencies are being competitively devalued in the context of a low or no yield bond world.
- Therefore, cash becomes a wasting asset, albeit a *safer* wasting asset than stocks, bonds or real estate as interest rates begin to back up (rise).

The combination of these economic factors converging simultaneously means there will be "no place to hide" for stocks, bonds and real estate until the imbalances and distortions created by worldwide governmental and central bank manipulations are at least partially cleansed. The enormous printing of money will degrade its value; that simply can't be avoided. It's only a matter of time.

Bonds will lose massive amounts of current value as interest rates back up (to more normal levels) and they are discounted to maturity using interest rates 200% to 700% higher or more. Just moving short-term rates to 1% from 0.125% implies a discount 800% larger.

Real estate will not go untouched, either. As sensitive as real estate prices are to changes in interest rates, the downward revaluation of real estate equity in the face of rising interest rates will hit homeowners and equity stakeholders in larger projects hard.

Finally, we should expect ***stocks*** and indices who benefitted from the "Super K" phenomenon described in the 2/2013 *CJ* to revalue downward as that effect reverses from the other events described above.

Why? The enormous amounts of *debt* floating around the world. Most currencies have been borrowed for years now as part of a *carry trade* where money could be borrowed cheaply and invested in instruments, particularly stocks and bonds, where a higher return could be realized and the differences pocketed. This is usually an institutional game, but when large players sell to repay debt owed as the carry trade reverses, stocks will decline from their selling and crowd behavior from smaller investors should enhance the decline.

It appears to me that human nature would not allow us to run from *all* things financial. It would be much more likely that people would run *toward* something that would offer better wealth protection and preservation. What might that be? What has served as a storehouse of value *and* a medium of exchange for longer than anything else in history, predating even some governments, especially *modern* governments? Precious metals and gems? Some fungible commodities?

I believe now, more than ever, as world governments have pushed *wrongheaded* fiscal and monetary policies to ridiculous, unsustainable levels, precious metal investing, especially in gold and silver, may prove to be one of the few havens left to TCM investors. TCM clients will have at least a portion of their portfolios invested in these things for both protection and return. Cash will still play a big role. Investments generating cash returns will be held for now, but watched carefully.