Alan M. Newman's Stock Market
CROSSCURRENTS

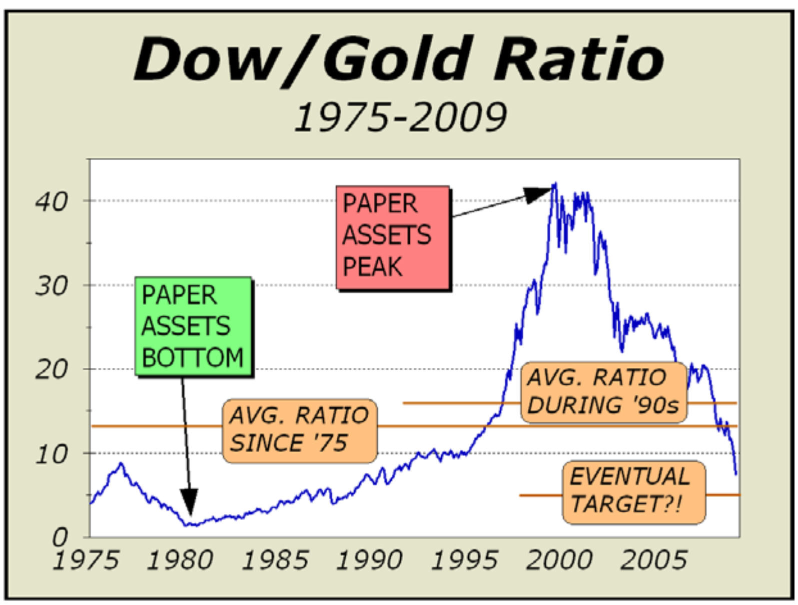
U.S. STOCK MARKET OUTLOOK for MARCH 9, 2009
DJIA 6594 - SPX 682 - NASDAQ 1299

LONG TERM: DOW/GOLD RATIO STILL HEADED LOWER. GOLD STOCKS WILL EVENTUALLY EXCEED THEIR OLD HIGHS. LEVERAGE HAS FINALLY LOST ITS APPEAL; MARGIN DEBT CONTINUES TO CONTRACT. ***- NEXT ISSUE - MARCH 30, 2009 -***

When All Else Fails To Glitter.

Immediately after the terrorist attacks of 911, we declared a super bull market for gold and have since remained in the bull camp with forecasts of far higher prices for bullion. In subsequent reports, we stressed that while 911 may have been the catalyst at the time, the principal rationale remained the threat of a derivative fiasco far worse than that of Long Term Capital Management in the autumn of 1998. Over the last few years, we have attempted to update our reports on gold and derivatives quite often.

However, our last look at gold was in the September 8, 2008 issue, as significantly more important developments in U.S. stocks began to take precedence. When Lehman Bros. was allowed to collapse into bankruptcy, the sheer mass of the derivative daisy chain exerted a gravitational force unlike any seen before in stock market history and created the financial equivalent of a black hole. Any entity that was a counter party of Lehman's structured product portfolio was thrust into a position of uncertainty. Consequently, any entity that was a counter party to a counter party of Lehman was similarly thrust into an uncertain environment. The threats we had written about years before had finally arrived. An unspeakable financial catastrophe was at hand. And nearly six months later, the catastrophe continues to unwind, with grave consequences.



When Lehman Bros. filed for bankruptcy on September 15, 2008, gold was $750 per ounce, but traded 20% higher in only seven trading sessions and by February 19, 2009 traded above $1000 per ounce, a 33% explosion. As fears about the future remained on an inclined path, gold reflected uncertainty and fear. As long as uncertainty remains a major part of the equation for investors, stocks will see only temporary gains at best. *When all else fails to glitter, gold will continue to shine*.

If you compare the chart at left to the one shown in the September 8th issue, gold's most recent bull leg stands out. *As of the print high for bullion on February 22nd, the Dow/Gold ratio fell to only 7.43, the lowest level since January 1991 when the Dow had just entered a brand new bull market*. For years, we have shown a "target" for the ratio of 5 to 1 even when the ratio was ABOVE 30 to 1. A ratio of 5:1 was deemed by many observers to be impossible in their lifetimes. After all, if the Dow was headed for 15,000, as many expected, a 5:1 ratio would mean gold at $3000 per ounce—unthinkable. And if gold went as high as $1000 per ounce, a ratio of 5:1 would require the Dow at 5000, also unthinkable. Yet today, the rapid collapse in stock prices has resulted in so much anguish that Dow 5000 no longer seems impossi-

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ble. There still seems to be little if any belief that gold could trade as high as $3000 per ounce. *We see no reason to dismiss the possibility.*

Our second chart below left clearly illustrates the difference between the market for stocks and the market for bullion is the most pronounced in three decades. When stocks began to recover from their 2002 lows, all cheered the birth of another bull market. The more significant truth was that stocks were still in the midst of a more emphatic trend; a secular bear market. We pointed out gold's superior position on many occasions with this same chart, insisting the performance of each of the two markets was destined to reverse over time. By the time we created this chart in late February, the Dow was 16% below its 2002 low close (see highlighted arrows) and on the same day, gold was trading up 169%.

As time has passed, we have offered higher resistance levels, based on our third chart at right below, *using prices levels adjusted for the effects of inflation*. Until recently, our resistance levels progressed steadily upwards as inflation, albeit modest, took a toll. However, from July to December 2008, the consumer price index (CPI) declined each month before finally rising nominally in January. Nevertheless, the CPI is still down 4% from July, which means our resistance levels have actually declined since our September '08 report. Even so, resistance at roughly the same level as in January 1988 was taken out with room to spare. The recent pullback from the February surge above $1000 per ounce does nothing to tarnish the precious metal's potential.

The next step is the February 1983 peak which equates to $1058 per ounce at this time. Once gold trades emphatically above, there is essentially no resistance until the levels that match the 1980 peak, which would place bullion well over $1800 per ounce. *However, if inflation returns, the final resistance level will be even higher*. We expect uncertainty to rule the financial markets for at least another year-and-a-half and that should provide all the boost gold requires to continue in bull mode.

5 Selected Popular Gold Issues

	Old High	Current Price	Upside???
ABX	$54.74	$28.82	+89.9%
GG	$52.65	$29.95	+75.8%
AEM	$83.45	$50.79	+64.3%
KGC	$27.40	$16.70	+64.1%
NEM	$62.72	$40.44	+55.1%

Of course, gold stocks have not traded in a vacuum and have been subject to the same bear rigors as all other stock issues. Eventually, this should change as inflation returns with a vengeance as the preferred method of dealing with the credit/debt crisis. In our most likely scenario, the five gold stocks in the above table appear to offer excellent potential for the long term and will eventually exceed their old highs, *likely with much room to spare*.

The Downside: *Incentivized*

A March 5th Bloomberg story by Caroline Salas and Shannon D. Harrington tells you all you need to know about Wall Street's propensity and ability to slit our throats. In their example, "*Amusement-park operator Six Flags Inc. and automaker Ford Motor Co. may be pushed toward bankruptcy by bondholders trying to profit from credit-default swaps that protect against losses on their high-yield debt.*" We have long railed that as it was in the Roaring Twenties, it has been exceedingly easy for short pools to pile on and create untenable long positions in individual issues. The mechanics are downright depressing and almost always work.

The only instance we have ever been able to document of a failed contrived short position was in the stock of Stutz in 1920 (see http://www.cross-currents.net/stutz.pdf). If you're curious to know more, John Brooks' Once In Golconda (ISBN-10: 0471357537) is a comprehensive compilation of the events leading up to and including the Great Depression and includes *several dozen* references to short pools. After the economy completely collapsed, the SEC was created, short selling on upticks was put into place and the street promised to put on a new face. *That was then*.

In the intervening decades, Wall Street's powerful lobby once again controlled the game. The SEC faltered in its mission, deregulation ensured the playing field would be tilted against investors and the uptick rule was stifled without a whimper. Thus, we now live in an environment where the "negative-basis trade" thrives, adding to the crisis in confidence. Before we go any further, we are the first to claim the economy was way too leveraged and in need of

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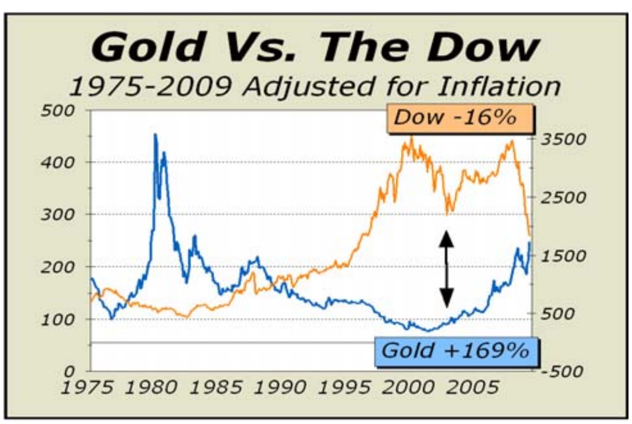

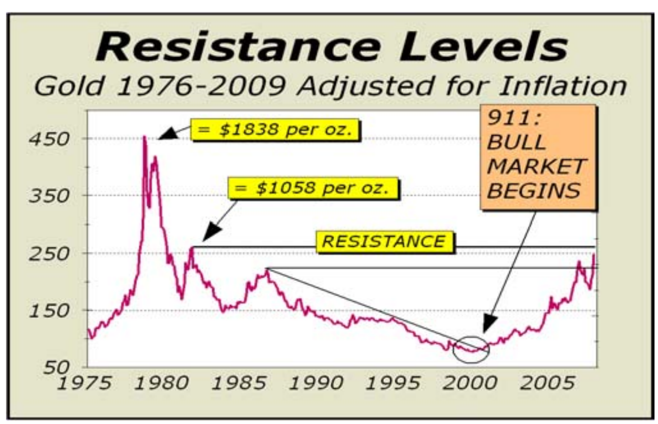

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correction, but we also are eager to demur; *bankers and brokers led the way to excess, not consumers*. The banking industry (read mortgages), particularly in California, created a situation that had no choice but to proliferate and collapse based on its own idiotic assumptions. The process that allowed the packaging and re-packaging of loans (including those for credit cards and auto loans) and associated bets against those loans (read SWAPs), *guaranteed* the great unwinding that commenced last year.

There is now so much money devoted to betting on the downside and pressing those bets that the downside has been in the equivalent of a feeding frenzy. The cycle goes on and on. In the Bloomberg article we referred to, "*investors could buy Six Flags bonds at 20.5 cents on the dollar and credit- default swaps at 71 cents. If the New York-based chain defaults, the creditors would receive the face value of the debt, minus costs*." A downside bet would be a winner, no matter what the outcome is to be. This is not just plain vanilla arbitrage, where fleeting opportunities are erased by adjustments in the marketplace. This is one of thousands of instances where the crisis in confidence continues to play out and wreak havoc. Simply put, there is now no justification for confidence in a turn in valuations or the economy because the downside bets are far more attractive. As one investment manager was quoted in the Bloomberg article, '*Now, you have to consider the possibility that you might have this large holder of CDS incentivized to see it go into bankruptcy. It's something that's going to come up more and more.*' Incentivized! The thought is chilling and a lot of what you have seen in the last year, since the implosion of Bear Stearns is just that, the incentives of entities to *engineer* the downside, if at all possible. It's all about money. Vast sums have already been made and much more is possible if a very worst case scenario can be molded from the scraps that are still available. We hasten to remind our readers that somehow, put options to sell Bear Stearns at $5 per share were created only days before the collapse when BSC still traded at $54. No one in his or her right mind would ever trade for at least a 92% decline in that short a time frame without advance knowledge. Need we say more? *The collapse of Bear had to have been engineered.* And now as our entire auto industry stands on the brink, "basis" traders hold all the Aces. Yes, they can still make out just fine if companies survive but they will have to wait for years for debt to mature. In the meantime, they stand to make the most money in the shortest time if companies default. One academic quoted in the Bloomberg article commented, "*the creditor really doesn't care whether or not the company goes under.*"

There is likely a light at the end of the tunnel, but it is also likely far down the road. We are hopeful that things are not all as bad as they appear, but clearly, our views on the bear market lasting until the fall of 2010 make a lot of sense in the current environment.

The Great Unwinding In Action

We were able to update our charts at the very last minute, as we waited for FINRA to update their margin stats on Friday. The data for NASD firms do not add much to the mix but we'd prefer to paint the broadest possible strokes, as you see illustrated below.

Without any doubt, the leverage thesis has, for the time being, lost all validity. From the July 2007 peak of over $416 billion, margin debt has collapsed by 51% to $204 billion. Given comparable declines in price of well over 50%, just about anyone who was fully leveraged during the time the bear has raged has very likely been wiped out. When regulation T requirements (http://tinyurl.com/c7xe7q) cannot be maintained, customer stock is sold *perforce*, wherein lies a large portion of the price decline to date.

The good news is that as margin debt declines, there will likely be less *forced* selling. The annual percentage change in margin debt has already far outpaced the collapse from the horrible 2000-2002 bear market. This annual change indicator is unlikely to give up much more ground, although total margin debt should indeed, fall another 43%+ to roughly the $115 billion mark before a bear market bottom.

Mutual fund cash ratios surged in the month of January to 5.8% as most of the more than $9 billion in net cash inflows remained in cash reserves, rather than spent on stock. Our most likely case target for mutual fund cash ratios is still roughly the 6% level. Given that somewhere north of 90% of Americans are still employed, some money is bound to make its way into stocks, despite the frightening impulse for many to sell everything. Wall Street has woven its spell of buy for the long term quite well. There are some who have no choice but to continue to believe the system works.

Additional reading, see "The Great Unwinding," Pictures of a Stock Market Mania, January 2008 (http://www.crosscurrents.net/archives/jan08.htm.

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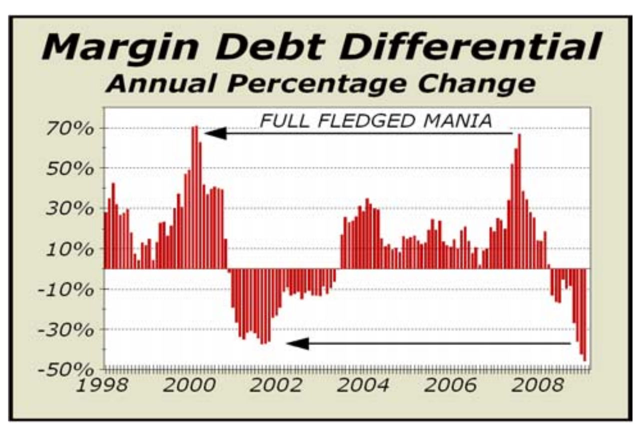

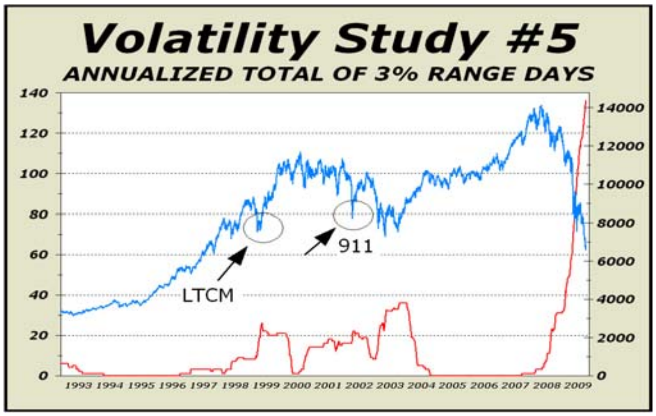

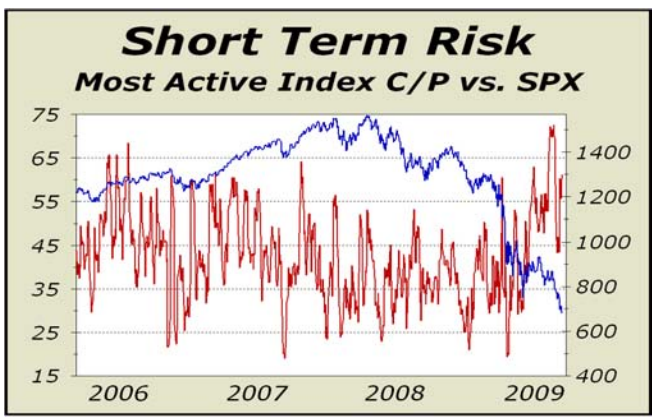

Alan M. Newman's Stock Market

CROSSCURRENTS

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Alan M. Newman, Editor

We're blown away every time we see the chart at top left. We've never seen an environment like this but it's easy to understand. When volatility is *this* extreme, almost no one is going to stand in the way of the trend. Thus, the downside becomes a foregone conclusion and a feeding frenzy of short selling consumes everything in its path. Over the last year, the range between high and low exceeded 3% better than every other day. Every one of the last dozen trading sessions has seen a larger than 3% range, only three of which were up. A *sustained* upside is not possible until the 3% range days stop occurring.

One positive sign is a continuing modest divergence provided by Nasdaq. At center left, despite the penetration of the November 21st price low, cumulative Advance/Decline volume has remained above the low. This indicator needs to turn up before the divergence can be interpreted as meaningful.

We still see mixed signals from our emotion indicators. There is no doubt that those buying the most active index put options are paying WAY too much, however, far too many calls are being bought in relation to puts. Risk is still too high.

Last One Out, Please Turn Off The Lights

The crisis in confidence has taken many forms, from the enormous sums of money lost by wealthy hedge fund investors to those burned in the Madoff and Stanford Ponzi schemes. How bad has it been for smaller investors? Plenty bad. Brent Hunsager's piece in the Oregon Business News (see http://tinyurl.com/acmj9q) is evidence that the rapidly dwindling demand for stocks has gone far beyond wealthy investors. According to Mr. Hunsager, the lone national association of investment clubs, has seen its membership drop 80% in ten years. There were nearly 37,500 clubs with a total membership of close to half a million in 1998, but the latest tally only six months ago estimated 9500 clubs nationwide and only 95,000 members. Given the last few thousand Dow points on the downside, we can safely presume membership has declined far more significantly.

From what we can see of the huge contraction of the investor base, we're very close to a bottom and at least a temporary turn in the tide. However, there will probably be a long base building process that should take as long as a year-and-a-half before the next bull market erupts in full force. As for the crisis in confidence, it will likely end when it appears there is no hope. Ironically, that's what the arena looked like last week.

Dan Sullivan & The Chartist

The Chartist's Dan Sullivan has a great article about timing versus buy-and-hold in his February 5th issue. If copies are still available, this is definitely worth your dime and time. As well, Mr. Sullivan's commentary in the February 26th issue of The Chartist is a MUST read. Call his office at (562) 596-2385.

☑☑☑☑☑

THANKS TO:
CARRIE MASON-DRAFFEN
NEWSDAY
FOR COVERAGE
OF OUR COMMENTS

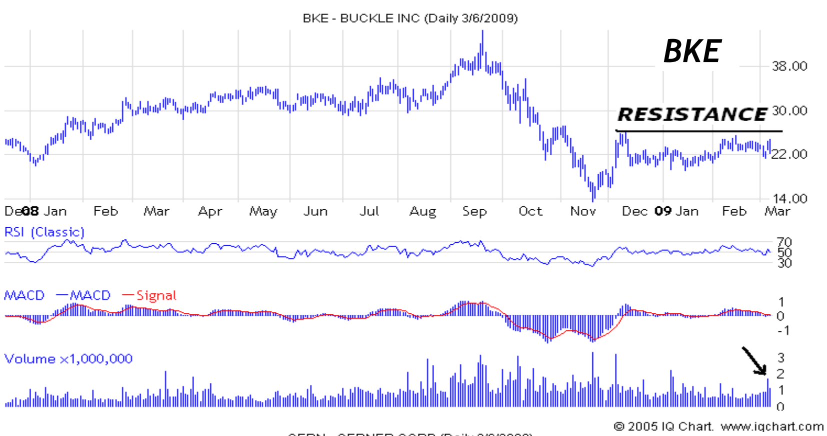
☑☑☑☑☑

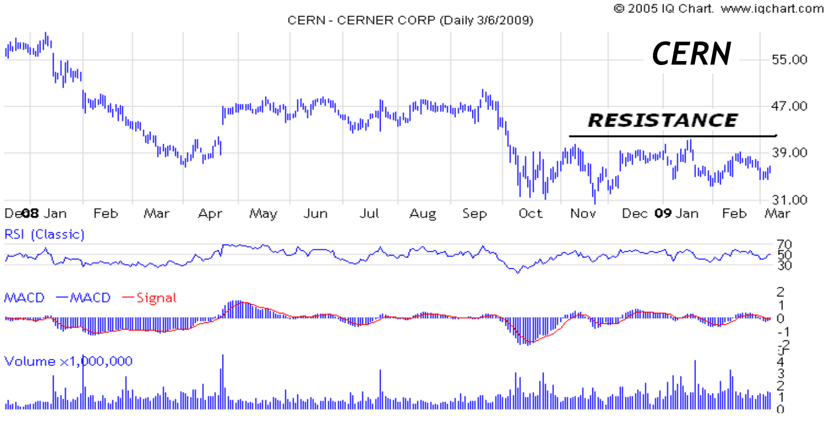
- Rationales & Targets -

We expected no more than a 5% downside to unfold after our last issue but the news background deteriorated significantly. ***Far more importantly, as we discussed earlier, the downside has been incentivized***. We now understand why our emotion-based indicators show such a wide discrepancy, why the most active index put buyers are spending much more for their downside bets than they should be. ***We have somewhat of a self fulfilling procedure in place now.***

In a Special Update to subscribers, we took "baby steps" in the Trading Stance, adding 5% longs in both PRXL and ESRX. We were proved wrong only three days later as the Dow plunged and is now some 700 points lower. At this juncture, we will wait for the market to assert itself before any further considerations of additional steps. It is way too late and too expensive to play the downside. For many years, we have considered that Alan Greenspan's immortal pondering of "irrational exuberance" on December 5, 1996, deserved the ignominy and poetic justice of an eventual return to where the Dow closed that day at 6437. ***We're almost there.***

Stocks crashed 32% in only one month into the October low and an additional 26% in two months. In addition to the incentives that are keeping traders negative, the broken mechanics of our short sales system continue to do long term damage to the capital markets. But at some point, they will rally and when they do, the stocks with the best charts should perform quite admirably. Admittedly, they are few and far between but the two below are holding their ground in the most perilous environment in decades. Buckle Inc. (BKE) rose 8% on Thursday on double Wednesday's volume, a sign of strong support. Cerner Corp. (CERN) actually traded up last week and Friday's rise was an excellent sign.





Jon Stewart: CNBC Gives Financial Advice
http://tinyurl.com/aj5u9p

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The Psychology of the Market

Investors Intelligence: 3 Wk. Bull/Bear Ratio 0.7 Pessimism
AAII: 3 Week Bull/Bear Ratio: 0.4 Near Panic
Mutual Funds: 5.8% cash: Turning Fearful
Crosscurrents Emotion-Based Indicators:
Confusion Reigns—Bulls & Bears both confident

Intermediate Term Forecast

DOWNSIDE SHOULD BE PLAYED OUT
UPSIDE POTENTIAL = 28%
DOWNSIDE RISK = 3%-4%
BEST REWARD/RISK RATIO IN YEARS

Crosscurrents '04 Investment Stance
AVG. GAIN FOR ALL POSITIONS +17.0% Vs. DJIA +1.9%
Crosscurrents '05 Investment Stance
AVG. GAIN FOR ALL POSITIONS +32.0% Vs. DJIA –0.6%
Crossscurrents '06 Investment Stance
AVG. GAIN FOR ALL NEW IDEAS +29.2% Vs. DJIA +16.3%
Crossscurrents '07 Investment Stance
AVG. GAIN FOR ALL NEW IDEAS +53.5% Vs. DJIA +6.4%
Crossscurrents '08 Investment Stance
AVG. LOSS FOR ALL POSITIONS –14.3% Vs. DJIA –.33.8%

Crosscurrents '09 Investment Stance

RETAINED FROM PREVIOUS YEAR OR EARLIER
Newmont Mining (NEM) 15% LONG -1.5%
Vimpel-Communications (VIP) 5% LONG –47.9%
China Medical Tech. (CMED) 5% LONG -41.6%
Paraxel Int'l. (PRXL) 5% LONG -27.9%
AVERAGE LOSS –20.3%
Vs. DJIA –24.9% SPX –24.4% Nasdaq –17.6%
"Retained" ideas priced from inception
Percentage gains (losses) include dividends

POSSIBLE ADDITIONS FOR 2009

Pfizer Inc. (PFE) 5.2% dividend yield
Altria Group (MO) 8.3% dividend yield
AT&T Inc. (T) 6.9% dividend yield
ShengaTech Inc. (SDTH) 4 P/E - China/Speculative
Potash Corp. of Saskatchewan, Inc. (POT) 6 P/E
Express Scripts Inc. (ESRX) - 10.4 forward P/E
Frontier Communications Corp. (FTR) - 13.9% yield
Suntech Power Holdings Co., Ltd. (STP) 6 P?E - China
TransMontaigne Partners LP (TLP) - 13.8% yield

NO POSITIONS TAKEN YET

Crosscurrents '09 Trading Stance

Express Scripts (ESRX) 5% LONG –21.3%
Paraxel Int'l. (PRXL) 5% LONG –26.0%