

Notes From the Rabbit Hole ©



Peter Newell's illustration of Alice surrounded by the characters of Wonderland. (1890)

In Lewis Carroll's *Alice's Adventures in Wonderland*, Alice follows a mysterious white rabbit into a rabbit hole to enter 'Wonderland', an absurd and improbable world inhabited by many strange characters.

June 6, 2009

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NFTRH36

A Recap Before the Good Stuff

As promised on the [blog](#), NFTRH36 charts out buy points for several favored gold stocks. There are seven in all this week, mostly in the small to intermediate producer category, but also charted is our favorite explorer and favorite senior. As well, the HUI is charted for potential support levels and bull market status from a daily, weekly and big picture monthly perspective. Suffice it to say, beyond the expected correction currently in progress, NFTRH remains bullish and looks forward to reloading certain positions.

With ten gold sector charts in all, there is little room for additional images. As the report proceeds along, I will add graphics only if absolutely necessary to the analysis. But for now, let's recap the state of the stock market and the macro picture.

US Markets

The Dow and S&P 500 continue to hover around our initial target zones for the sentiment rally, which called for a rise above the SMA 200s. There is a notable decline in volume over the last month, which could imply that some smart money wise guys are cashing in their chips.

The BKX bank index continues to consolidate in ratio to the S&P. This could be a pause before fresh highs, which would lead the markets to our more optimistic targets (roughly correlated to SPX 1010-1020) or it could promptly become an actualized bearish divergence. There is not much more room for BKX to under perform without triggering an end to the rally.

Either way, the short to intermediate term risk remains high in the markets because everyone is now becoming aware of the supposed improving economy, with improving defined as ‘things suck just a bit less than they did a few months ago’. Mmmm, I have got to get me some of those fundamentals.

The play, as I see it right now, is that any coming downside will be the result of a badly needed rebound in the dollar and in long term US Treasury bonds. This would be counter the real trends, which means that stocks have a chance to decline near term into the would-be right side shoulder of a bullish inverted head and shoulders pattern, which would bode well for the fall and into 2010.

We will look at this potential bullish scenario going forward, but first things first. Stocks should decline soon for the more healthy longer term scenario to come into view and in this regard ‘healthy’ is defined as ‘stocks will make a higher low from March and then proceed on to under perform gold, gold stocks and commodities as the results of despicable inflationary policy go on to lift all boats. Currencies may keep up appearances against one another, as most are facing varying degrees of abuse by their respective governments, but the real action will once again be in actual ‘things’ of value.

First however, we will stick with the view that holds out one more deflationary dunk before it is time to strap in for the long inflationary haul.

Global Markets & Commodities

I just looked at a daily chart of copper, and I did not see anything bearish there. In fact I saw a beautiful bottom and a nice consolidation. So I pulled up a weekly and saw a retrace nearly complete to the early 2007 lows (potential resistance) and a 38% Fibonacci retracement completed at current levels. The point is, NFTRH can only go by what it sees, and what I see is a still bullish looking commodity against our bearish near term plan. Fundamentally, my friend Otto, formerly very bullish on copper, has been quite bearish. I have seen him routinely post material on his highly recommended IKN [blog](#) that is contrary to the would-be reemergence of a real China Story, part 2 at this time.

Speaking of China, its market along with a good chunk of the rest of the world, remains strong. Hope really is making good on its attempt to gain the big bid. The commodity indexes CCI and CRB have both come to measured targets off of nice bottom patterns and the DBC etf, noted on the blog, is just about there as well. Crude oil has apparently set its sights on the optimistic target of a 38% retrace of its all time highs, to the high 70’s.

US Dollar and US Treasuries

This is where investors should be looking first and foremost. I am aware of the investment merits of vital resources (commodities) and in ascending economies (BRIC, etc.) and hopefully NFTRH will one day have the chance to actually *invest* in these areas for the long haul. That is because, as the death of the dollar cultists chant (day after day, month after month and year after year), the liabilities of this nation are impossible to quantify, let alone repay. Therefore, its currency and its Treasury bonds are intrinsically worthless and subject to the lone economic ‘fundamental’ remaining, inflation policy.

But how worthless were they in October of 2008? The short term risk is high in stocks and commodities because the short term risk is high of a technical USD and treasury bond rebound. Plain and simple. Get a world of hoppers off sides and then to their utter gall and disbelief, deflation impulse, round II.

Failing that, it is off to the inflationary races and the inflation argument has the fundamentals on its side. So it must be respected. But NFTRH will stick with the ‘risk is high’ mantra until it is proved wrong, and with the action in the dollar late last week, the call for reversal from a historic and critical downside level (recall the monthly chart shown on the blog) is on track. The caveat being that the daily trend in the buck is still down.

The government really could use a period where it is able to call in some of the goodwill it has created with its hyper liquidity and manufactured stock rally. In other words, the government needs to reload the inflationary gun and another deflationary impulse would be convenient to their needs.

Gold Stocks AKA the ‘Good Stuff’

I would like to lead off with a look at the gold sector as a whole before looking at some of our favorite miners. If things play out to the script as I see it, there will be more opportunity to follow additional gold miners and explorers in preparation for what I think could be a fine bull market; potentially Nasdaq 1998-2000 fine.

The gold sector is the one on which I am bullish in the nearest term and with the greatest intensity. That is because the gold stocks have now *proven* to benefit fundamentally during deflationary episodes as NFTRH claimed would be the case back in Q4 of 2008. In fact, if we get another deflationary impulse (as opposed to an actual structural and ongoing deflation) before inflation is allowed to break out of the barn, the gold miners will stand head and shoulders above everything else.

As with the previous cycle however, the point might then come where the gold stocks begin to under perform things like energy and base metals as their costs once again begin to rise in relation to their product. But that is way out on the horizon. The dynamic

however serves as a warning that the fundamental case for gold stocks depends on gold once again resuming its rise against assets like oil and base metals in the near term.

As for the sector, let's start out with the daily HUI and work our way up to the monthly. As you can see, the current pullback is barely a blip in the huge rise from the October lows and the November double bottom. The HUI has done a lot of good work this spring in pounding its way through the resistance that we had defined as the 350-360 area and right on cue, is pulling back to avoid some unhealthy upside blow off dynamics. A pull back to the SMA 50 would purify the sector quite well. Will it get there? It is not necessary, but in alignment with the weekly chart it would be a nice buying opportunity in my opinion.



The following weekly chart shows strong support at our old friend, the EMA 75, which not so coincidentally is nearly identical to the level of the daily SMA 50. This is further evidence that if you want to be aboard the gold stocks, and if you get this opportunity, you should be buying and putting your worries aside, at least as much as one can ever put worries aside in the markets. I will likely have some powder remaining for that level and will be buying.

The general weekly chart could not be much more bullish, turning down from our logical resistance level (crown of overhead from 400-500) and giving would-be investors another chance. Will they be brave enough to take advantage while being negatively reinforced?



The monthly HUI and its EMA 18 further illustrate just how bullish this sector is. I am not advocating readers wait until the exact downside targets to enter. I personally will be buying in stages, adding to a still healthy collection of small gold stocks and upon the monthly MACD signal going positive, I may plan to tone down the trading and just strap in for a one or two year period. In that regard, following the monthly chart are seven of our top gold stocks charted for buy points, for anyone interested in gaining exposure.

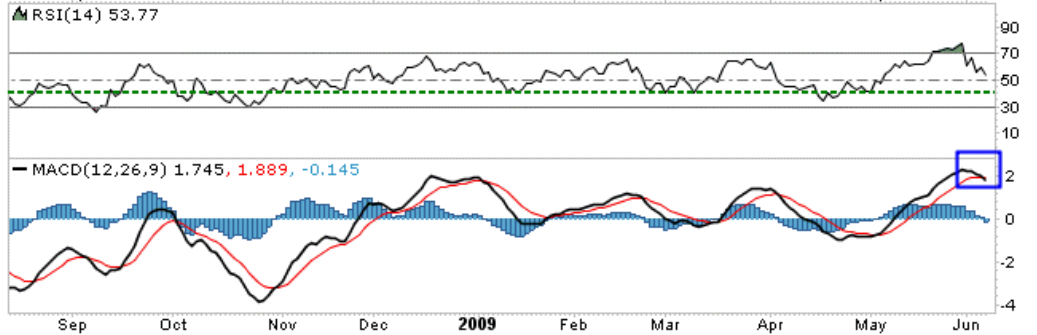
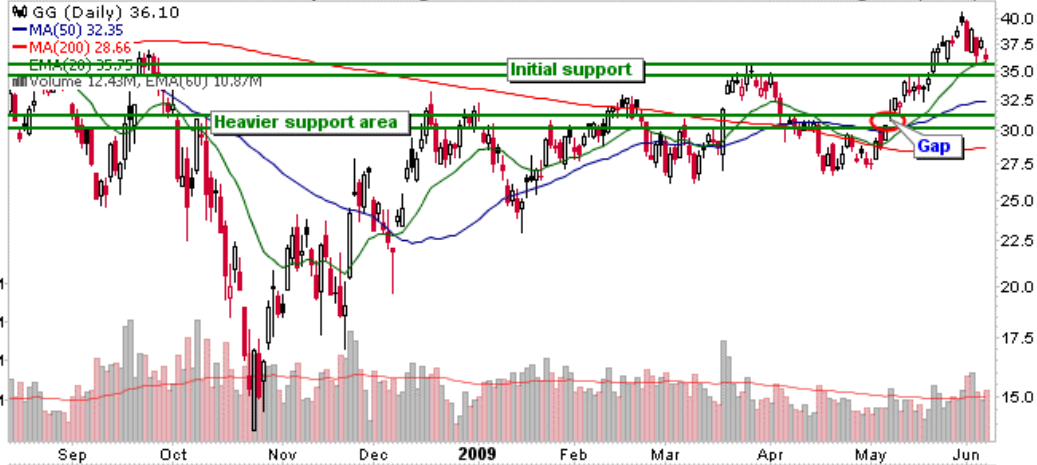


GG (Goldcorp, Inc.) NYSE

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5-Jun-2009

Open 36.37 High 37.05 Low 35.80 Close 36.10 Volume 12.4M Chg -1.66 (-4.40%)

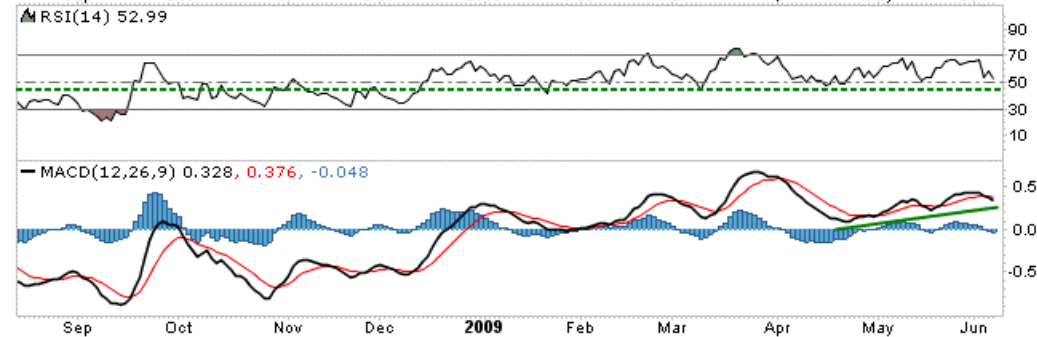


MFN (Minefinders Corp. Ltd.) AMEX

© StockCharts.com

5-Jun-2009

Open 8.74 High 8.88 Low 8.46 Close 8.66 Volume 463.9K Chg -0.33 (-3.67%)



JAG (Jaguar Mining Inc.) NYSE

© StockCharts.com

5-Jun-2009

Open 8.13 High 8.24 Low 7.79 Close 7.91 Volume 95.3K Chg -0.41 (-4.93%)

JAG (Daily) 7.91

MA(50) 6.40

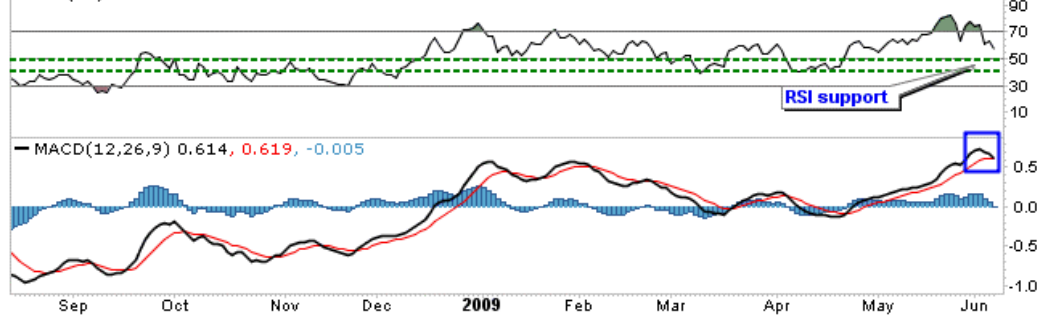
MA(200) 5.07

EMA(20) 7.64

Volume 95.32K, EMA(60) 183.52K



RSI(14) 56.84



NXG (Northgate Minerals) AMEX

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5-Jun-2009

Open 2.21 High 2.27 Low 2.16 Close 2.20 Volume 2.6M Chg -0.11 (-4.77%)

NXG (Daily) 2.20

MA(50) 1.66

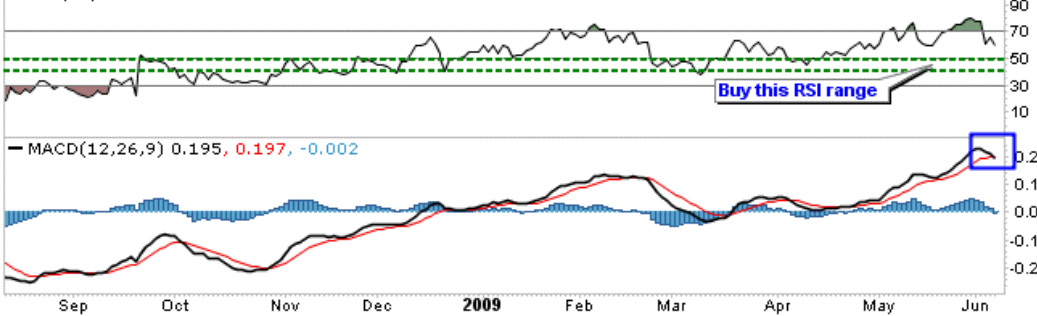
MA(200) 1.21

EMA(20) 2.07

Volume 2.62M, EMA(60) 2.62M



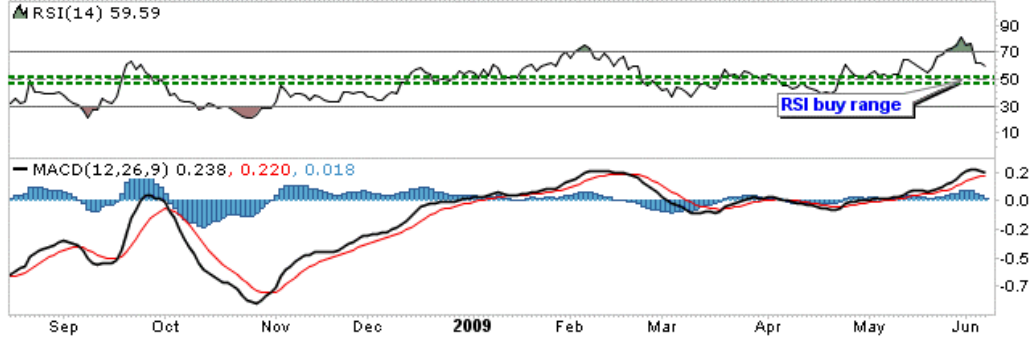
RSI(14) 60.08



NGD (New Gold Inc.) AMEX
5-Jun-2009

Open 2.69 High 2.81 Low 2.62 Close 2.67 Volume 1.6M Chg -0.07 (-2.55%)

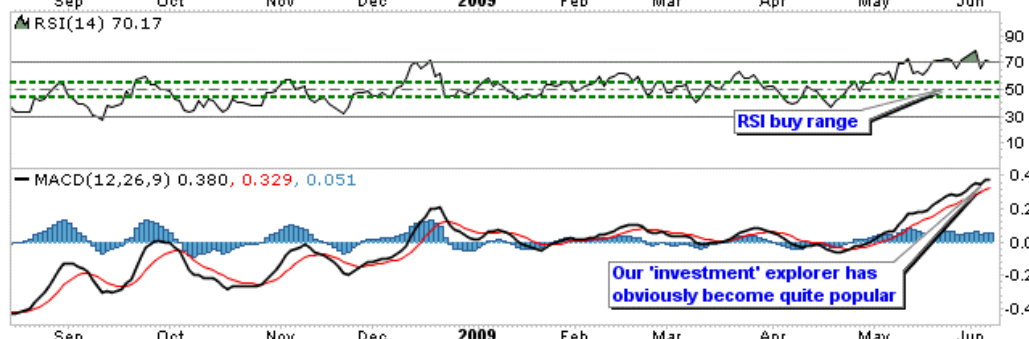
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FRG (Frontier Development Group Incorporated) AMEX
5-Jun-2009

Open 4.18 High 4.18 Low 3.79 Close 4.10 Volume 623.8K Chg -0.05 (-1.30%)

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Please pardon the format as I realize it is a bit inconvenient to have to scroll back up to the charts for reference, but this is the best way conserve space in today's letter. Below are short comments on 1-7.

- 1) Goldcorp (GG) was a consistent member of the NFTRH portfolios off of the ridiculous 2008 hysterics. I hope for the chance to buy this stock back near the SMA 50.
- 2) Minefinders (MFN) did not become quite as over bought as some miners, despite its fabulous gains. This is part of the reason I took an initial position back in the stock last week. I buy 'all in and around' corrections and bottoms. The next buy level looks to be at around the trend line/SMA 50. One might save powder however in case some downside hysterics get whipped up. MFN can move hard, in both directions.
- 3) Old favorite Jaguar Mining (JAG) shows a clear line of 'no-brainer' support near the SMA 50 that your letter writer will not hesitate to buy if given the opportunity.
- 4) NFTRH superstar Northgate Minerals (NXG) shows a no-brainer of its own at around 1.50, but it may never get there. I will consider myself lucky to buy back in at around the SMA 50.

- 5) New Gold (NGD) says 'buy me at the SMA 50'.
- 6) Fronteer Development (FRG), NFTRH's favorite stock will present opportunity to add to current positions at the 'no brainer' SMA 50, if we are lucky. Someone on the outside looking in at this gem might consider taking a tracking position higher and scaling in on opportunity.
- 7) Dynasty Metals (DMM.to) is a former NFTRH holding, bought on the prescient recommendation of Otto at IKN. A NOBS report was also presented for early NFTRH subscribers. It was sold 'too early' but fabulous gains were recorded none the less. Now we find Otto's fundamental gem on the decline to the noted measured target. If given the opportunity, it will be added back given no new negative news cropping up.

Wrap Up

Not much has changed over the last week other than the gold stocks have finally provided a glimmer of short term turbulence. This makes me more bullish, not less and I plan to take advantage of it. This would ideally happen at lower levels per the HUI daily, weekly and monthly chart synergy.

The broad markets and commodities continue so float around on hope and a good story. I am currently leaning about 60%-40% toward the story that holds out longer term bullish potential in certain emerging (ascending) markets and in certain domestic and global sectors. But as with what is happening to the gold stocks now, it would be better for the health of markets to get a correction going sooner, rather than later. NFTRH bullishness ratio on commodities, pending some deflationary scares in the interim rises to probably about 80%-20% for the longer term.

Meanwhile, all eyes on the US Dollar and long term Treasury market.

Portfolio Notes *(portfolio notes edited for NFTRH sample editions)*

The capital preservation portfolio made not a single transaction this week and stubbornly sits on its 95% cash and t-bill/short term treasury funds. Gold/precious metals stock holdings are

██████████ The latter two are part of the 'little ones' contingent not previously mentioned because I have not sufficiently researched them. But they appear to be cheap lottery tickets doing well at this time and with the portfolios reduced as they are, I figured I would mention them although not recommend them at this time. NFTRH's positions are small, obviously.

The speculation portfolio holds 66% cash and a host of smaller gold miners including [REDACTED] and explorers [REDACTED]

[REDACTED] was sold again for an okay short term profit of around 9%, if memory serves. There is some other riff raff kicking around in this portfolio that may one day go to zero or hit the lottery. The positions are commensurate with the risk. Finally, as noted in this week's email update, an initial position in the [REDACTED] was taken without undue hopes for success. It is better that way.

Final Thought

Patience remains the most valuable commodity in the short term. There is a lot of noise out there, including the small din being made by NFTRH and the blog it is associated with. It is best to watch near term events but manage the information with a bigger picture game plan and *contingency* plan.

What is happening in the USD and Treasury markets are serious business. Lean the wrong way and you are leaning contrary to some very powerful forces. Looking ahead, I have no doubt that policy makers are going to be exposed as the economic remote-controllers that they are as the macro system ultimately finds a way to organically heal itself. But those in power are not going to go easily.

They need to re-load the inflation gun and that would involve a rise in their currency and in their t-bonds. Be on guard for this. If this scenario is wrong then it will be time to adjust to a world of inflationary fears breaking out. If it is right however, a lot of commodity and stock market participants are going to be caught on the wrong side of the trade.

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