

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.

July 8, 2009
Biiwii.com
NFTRH40

Real Time Review

Since today's report is being written during market hours, I thought I would use this abbreviated edition of NFTRH to review our most important markets and 'sign posts' in real time before getting back to the normal format in NFTRH41 this weekend.

Precious Metals

The weekly chart of the HUI illustrates why I tend to become abrasive in my criticism of the gold bug 'community'. With some exceptions the analysis tends to talk about assaults on certain levels (like HUI 400 in the case of the rally into May) and the bullish potentials beyond as opposed to the risks of correction that increase markedly during a furious rise.

This is no doubt because of the potentially superior macro-related fundamentals of the gold sector, but is also born of deeply held beliefs by these people that they are righteous in their battle against corrupt monetarists who work daily to further poison the system. All well and good, but unless you don't mind taking regular 20% to 50% haircuts, you will tune out the righteous gold bug community at times of high risk and always remain in position to capitalize when they start the inevitable process of regurgitating their shares. This is why NFTRH raised the risk profile at HUI 360-400.



Now we endure the downside that follows and wait for the more bi-polar elements of the ‘community’ to begin to get restless, or better yet, flat out emotional. As noted several times, the daily SMA 200, currently at around 289, is in play. Will HUI get to that level? We do not control the markets so I cannot say for sure, but I continue to await this opportunity with dry powder. The same is true for the ‘no brainer’ level of 250 and its long term support.

As for today’s action, HUI continues with its correction and while certain die-hard are probably feeling frustration, this is all normal and healthy activity. The corrections in this sector can go on for an inconveniently long time. Inconvenient that is, if you are not prepared for them.

NFTRH continues to be very bullish on this sector because of the deflationary backdrop that is currently directing policy makers into predictable actions with regard to money supply and most especially because the gripping global economic contraction forces gold higher in ratio to assets that are positively correlated to the economy. These assets of course include oil and other energy sources, base metals and materials. It is the ‘pushing on a string’ policy that fuels gold mining bottom lines. BUT...

Deflation Impulse on Deck?

Let’s return to our big picture monthly chart of the 30 year treasury bond yield and its 100 month exponential moving average. As the inflation trade – one more kick at the can for the commodity and resources promoters – exploded upward in Hope ’09, NFTRH noted the critical 100 month EMA as one of the signposts by which we are being guided. A sustained break above that level would have likely invalidated NFTRH’s current ‘one

more deflation impulse' stance. However, rates have dutifully turned back down as policy makers get an opportunity to reload the inflation policy gun (news items are appearing now regarding potential additional stimulus), leaving the commodity and resource believers in a precarious position.



A corresponding chart of gold is included to show that the metal has certainly not been disadvantaged by the ongoing story told by the \$TYX; a story of a structural deflationary urge met every step of the way by monetary authorities climbing ever further out on the limb of moral hazard known as unsound monetary policy underpinned by nothing but confidence. Confidence is in a bear market.

Stock Market

The S&P 500 appears to be making good on its bearish potential today as the longer it remains below the neck line, the more firmly it locks and loads the measured target of the Head & Shoulders top (noted support area). In fact, today would most likely be the reversal day if this was to prove a false breakdown and thus far, it is not looking good.



But of course, beyond the short term correction that has been in the cards for weeks now, we still have the bullish potential of a more intermediate time frame, the parameters for which will likely be reviewed once again in NFTRH41 this weekend. But for now, things are looking on track, depending on one's perspective.

US Dollar



What self-respecting deflation impulse would not include a moderate to strong rise in the all but left for dead US dollar? The dollar is of course another of our important signposts and the monthly chart above shows why the 78 level is so important. Sure, the buck declined well below that level as the global inflation trade prepared to implode after sucking in all who would believe. But the impulsive reversal back above that level brought on the historic events dubbed Armageddon '08 here at NFTRH that literally brought on a world of financial and economic pain.

The dollar has held this support area in conjunction with commodity and resource promoters attaining a fever pitch and the above noted 100 month EMA holding as resistance on the long bond's yield. Now we watch closer than ever going forward – with a daily view likely in NFTRH41 – because if we get another strong deflation impulse, it could be the last one before inflationary policy begins to erode the deflation story as something to believe in longer term.

Wrap Up

Just as Armageddon '08 provided intense opportunity to make money by leaning opposite the direction in which compelling forces were trying to push us, what lies ahead may provide a similar opportunity. The difference being that it is very possible any coming opportunities to buy fear and loathing may be the last ones in a long while, for the gold stock sector first and foremost and possibly for other areas as well. What sprung from Armageddon '08 was hope, as predicted and chronicled ceaselessly here and on the [blog](#). Risk on the fly is now apparently transforming into actualized correction. Beyond that, we must focus on what comes next.

While it was not mentioned above due to its prevalence on the [blog](#) recently, remember that the all-important Gold-Silver Ratio is not bullish for markets and has not been so for some time now. This is a short term negative for gold stocks along with nearly everything else. A contraction phase appears upon us. This will ultimately fuel the gold miner bottom lines, but first, misperceptions and market sentiment must be sorted out.

Thank you for bearing with this abbreviated version of NFTRH. As mentioned, we will be back on track this weekend with NFTRH41 going back to the normal format including portfolio notes, commentary, more extensive views of relevant markets, assets and indicators. Perhaps we will look at some individual precious metals stocks as well. Meanwhile, if you have any questions, comments or input feel free to pop me an email.

Note: Please do not redistribute NFTRH in part or in full without contacting me first. Thank you.

Biiwii.com and NFTRH terms & conditions: <http://www.biiwii.com/about.htm#Terms>