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Gartman

The Gartman Letter

Friday, January 6, 2006

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SPOT GOLD: A Bull Market in Full... Even Shortest Term: This chart, in 15 minute segments, shows that gold's bull trend holds strong.

OVERNIGHT NEWS:

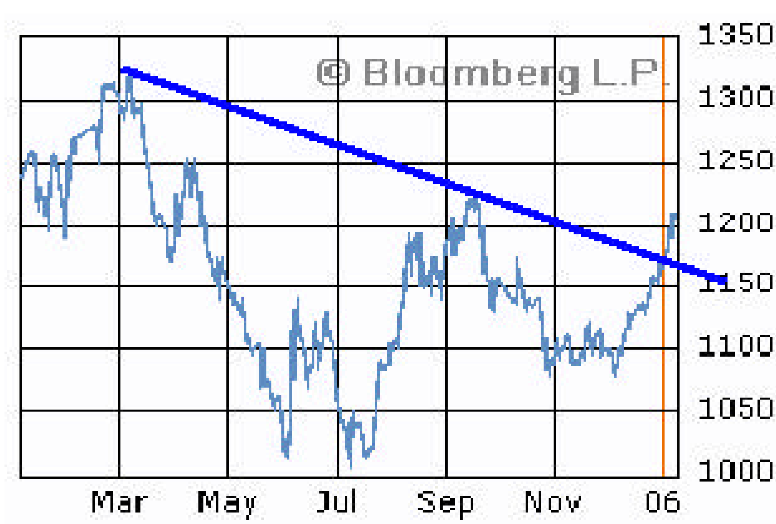
☑**THE FOREX MARKET IS RATHER STABLE** as it prepares for the release later this morning of the monthly US Employment Situation Report and the non-farm payrolls portion of the report. As is usually the case prior to the release of this report, positions have been reduced and the level of apprehension has been increased. We, as always, shall be out of the office when the report is released, and shall return fifteen to thirty minutes later to see what the figures were and what effect we think they should have... and then we shall match them to what the markets have done and we shall either be stunned, amused or wholly without interest. We know not which.

COLLEGE BASKETBALL BEGINS IN EARNEST: This weekend, college basketball begins very much in earnest and the brave, stout-hearted men of NC State take on the hated Tar Heels of the University of North Carolina Saturday afternoon. All good men and true shall *"Pull for the 'Pack"* 'gainst the Heels so that good shall vanquish evil once again and order in the universe shall be restored.

We know only that the consensus is for an increase in non-farm payrolls of perhaps 200 -225 thousand. We know also that this month's figures shall be a bit more important than other monthly employment figures for it is the one that the new FOMC shall rely upon at its upcoming meeting. The debate is raging that the Fed is so much nearer to ending its tightening policies, and today's figures shall give fuel to either camp. A figure above 250 would suggest that the Fed has a good deal more tightening to accomplish before its task is done, whilst a figure below 200 would suggest that the Fed has only perhaps 50 bps (two meeting's worth) of higher rates before its task is finished.

THE CANADIAN DOLLAR v. THE US': A Massive "Outside Reversal" Yesterday: Perhaps it is a "one off" technical situation that will simply fall into oblivion, but we absolutely must pay heed to the "Reversal" traced out yesterday... after a multi-year run in the C$'s favour!

We are of the first camp, believing that this economy is very, very strong and that the Fed's toughest task lies ahead, not behind. We have said in almost every speech we have given in the course of the past several months that the gravest problem businessmen and women here in the middle Atlantic states face is a lack of employable workers. Labour here is tight and getting tighter. It is the same, we are told in the Midwest; it is the same, we suspect, in



CHINESE STOCKS: The Bear Has Ended; The Bull Has Begun: This chart, of the Shanghai Composite Index, tells a great story of a very concerted bear market that finally ran its course back in July-August of this year and which has now been ended with the movement this week upward through the defining downward sloping trendline. Weakness back to this line should be bought, with the intention of holding that position for a very long while. When we enter we'll be buying the CHN closed-end mutual fund traded on the NYSE for that shall give us the easiest and most liquid avenue for exposure to China.

the East and we've no doubt but that it is the same out West. The data is skewed because of the holidays, and because Hanukkah and Christmas came at the very same time this time, making data just that much more suspect than usual Further, we must note that as internet sales at Christmas continue to rise apace, retailers who might otherwise have put a huge volume of seasonal workers at work were likely more reticent to do so this year, wreaking havoc with seasonal adjustment factors. We are always reticent about putting forth any "guess-timate" on this figure given its history of massive revisions. We are even more so this time given the holidays involved. We know only that we are standing very firmly upon the sidelines, unwilling either to buy or to sell the US dollar against the EUR or the Yen... or against any currency at the moment for that matter. As our old friend Brad Rotter once so famously said when asked his opinion of the US bond market as we stood on the top step of the CBOT's bond futures' pit and stared down into that great maw, "I'm flat and I'm nervous." We are flat and we are very nervous:

Mkt	01/06 Current	01/05 Prev	US$Change	
¥	116.10	116.15	- .05	Yen
Euro	1.2089	1.2101	+ .12	Cents
SFr	1.2785	1.2795	+ .10	Centimes
£	1.7545	1.7550	+ .05	Dollars
C $	1.1665	1.1485	+ 1.80!	Cents
A $	.7465	.7470	+ .05	Cents
NZ$	.6840	.6855	+ .15	Cents
Peso	10.600	10.560	+ .40	Centavos
Braz Rl	2.2860	2.3300	- 4.35!	Centavos
Ruble	28.67	28.74	- .07	Rubles
Yuan	8.0668	8.0657	+ .11	Renminbi

Prices "marked" at 10:30 GMT

The Canadian dollar has fallen quite inordinately in the past twenty four hours, having gone to a new high vs. the US dollar yesterday morning and then closing very badly indeed.

We think this ominous, for the C$ has traced out the most dramatic of "reversal" days we have seen in the forex market in a very, very long while. The market, for whatever reason, has chosen suddenly to pay attention weak natural gas prices and mark down the C$ on that news. We think that explanation "reaches" far too far, and instead suggest that the real reason for the C$'s weakness was the stunning decline in the Purchasing Manager's Report release for December. It fell 17 points to 48.3, thus taking it below the "magic" 50 level. We've not the ability to look back at this data, but we cannot recall a more serious fall in this figure than was this one. We and everyone else were caught wholly off guard... hence the precipitous drop in the currency and hence the reversal day. There are few technical signals that we pay more heed to than this, but we pay heed to reversals at the end of long extended uni-directional trends. This reversal fits that bill... ominously well.

Finally, French President Jacques Chirac, in what shall be his last year in public office (and we shall be writing at length as the year goes on of the eventual election there that shall likely pit the urbane, oh so elegant, but never-elected-to-office, Mr. Dominique Marie François René Galouzeau de Villepin against Mr. Nicholas Sarkozy for control of the centre-right and likely then to become the next President) took to the airwaves at the year's beginning to tell the French people essentially to "be happy/don't worry." Not wishing to be flippant, we do believe very strongly that a nation's leader has a duty to keep the people optimistic about the future. Simply put, pessimism doesn't sell well, nor should it. Understanding that, President Chirac said to the people of France,

> *We must, I think, do away if possible with this foible of only seeing the negative, of spending our time in a sort of permanent self-flagellation... France is a great country and we have full reason to be proud of it.*

He's right of course. France is indeed a great country, but she is caught now in a demographic problem that we fear can erupt once again at a moment's notice. We've said before and we shall say it again: the rioting that swept through the Parisian suburbs in November was but the first step in an "Intifada" there. The huge, youthful, unemployed, and ill-educated Islamic population there sees its life in France as one of near hopelessness and frustration. It is but a matter of time until the next round of rioting begins anew. President Chirac should be lauded for his attempt to raise the level of French psychology from "self-flagellation" to optimism, but we fear that worse, not better, lies ahead.

☑**COMMODITY PRICES ARE WEAK** and in some instances are materially so. Certainly we can say that of nat-gas, which has fallen over 15% since the start of the year, and which fell 6.7% yesterday! Silver has fallen 3.3% in the past twenty four hours... material in anyone's "book." Soybeans are down 2.2% and copper is down 1.8%. The only "bright light" was that of coffee which is up nearly 10% for the month-to-date and which has risen 6.2% in the past twenty four hours.

Our interest, however is primarily upon the precious metals, where we remain long term bulls of gold. In our commentary yesterday, with gold trading a good deal higher, we said that we'd not be surprised to see spot gold trade down to the $525 - 527 level and find support. It traded down to $522 earlier today in Asian dealing; it has since bounced rather sharply from those lows. As the chart of spot gold at the upper left of p.1 would suggest, the trend in the very shortest term (as well as in the longest) is upward. We strongly suspect that the lows at $522 shall be important interim lows and should not be taken out. We shall add to long positions then this morning upon receipt of this commentary, buying spot gold at the market. Those who cannot do so should buy either gold futures or await the opening of ETF and/or of gold share dealing on the NYSE and AMEX later this morning:

	01/06	**01/05**		
Gold	529.60	532.10	-	2.50
Silver	8.85	9.05	-	.20
Palladium	260.00	268.00	-	8.00
Platinum	984.00	988.00	-	4.00
Gld/Slvr Ratio .	59.84	58.79	+	1.05
DJ-AIG Comm Index	169.03	171.82	-	1.6%
Reuters/Jefferies CRB	335.80	338.49	-	0.8%
Goldman Sachs Index	6638.2	6736.5	-	1.5%

☑**CRUDE OIL IS STABLE; NAT-GAS IS WEAK** and the weekly inventory figures caught everyone by surprise yesterday. Firstly, this is of course January and in January we always... ALWAYS... see a net movement of nat-gas out of storage; except this year it didn't! This year there was a net in-movement of 1 Bcf of nat-gas into storage. We shall admit that this is a very small figure and it is prone to revision of course, but given that the market was looking for a net loss of 50-53 Bcf, this was a stunning surprise. Such are the "benefits" of warm weather; demand for nat-gas and heating oil have collapsed. Gasoline and distillate inventories rose also, with distillate rising 2.1 million barrels against the consensus' "guess-timate" of +0.7 million. Gasoline inventories rose 1.4 million barrels; however, given that there was no reasonable consensus as to what they would do, this was far less bearish than was the rise in distillates. At this point, we should note that crude inventories fell and that demand remains at record highs, likely as refining margins remain high.

Looking at a weekly chart of crude oil we are convinced that the bullish trend remains firmly intact, and we remain convinced that we are to trade crude oil bullishly, buying Suncor Energy as our surrogate long position. Being bullish of Suncor over the past three years has served us well. We see no reason to believe that it shall serve us ill going forward. Those not long of crude/Athabasca should use yesterday's weakness to become so. We trust this is clear:

Feb WTI	unch		63.15-20
Mar WTI	down	1	63.93-98
Apr WTI	up	2	64.42-47
May WTI	down	1	64.73-78
OPEC's Crude Basket (01/03)			$56.60
Henry Hub Nat Gas			$9.29/MMBtu

Finally, as an aside, friends brought to our attention the fact that Suncor Energy earlier this week sold its billionth barrel of crude oil. It is hard to believe, but Suncor has been in existence since the late 60's; however, for most of that period it was an uncommonly unprofitable enterprise. The cost of production was high (but was moving lower) while the price of crude itself was far, far below that cost of production. It has only been in the past several years that those "paths" crossed, with the cost of production falling below the price. Now, however, Suncor is selling a bit more than 260,000 bpd, and it is hoped that it will be producing 0.5 million bpd by sometime between 2010 and 2012.

☑**SHARE PRICES HAVE CORRECTED A BIT** in the past twenty four hours, with our Int'l Index losing 13 "points," or 0.2%. However, given the severity of the market's advance in recent sessions some modest correction seems not only inevitable, it seems necessary. We have included a chart of the Shanghai Composite Index in the "lead" position at the bottom of p.1. We are now quite certain, from a technical perspective, that the long bear market there ended five-six months ago, and that a new bull market has begun. We shall focus our attention upon the Xinhua Index' ETF, FXI, and upon the China Fund (NYSE: CHN). Our preference shall be upon the latter than the former, but we'll not argue with those preferring the ETF.

We also remain long of "all things Athabasca," but consider this a position in energy rather than a position in equities. That having been said, we have suggested purchases of Suncor primarily and of Birch Mountain secondarily... or as we have said, "ancillarily." SU made a new multi-year high earlier this week; yesterday it corrected. No one should be surprised. We are, however, somewhat bemused by the recent weakness in BMD. Normally, we would at this point be suggesting selling SU and swapping it for BMD at the margin; however, the manner in which BMD trades in recent days keeps us from doing so. We shall need to see some ability for BMD to hold before we'll make any move to increase our exposure there. Again, we trust we are clear:

Dow Indus	up	2	US$	10,882
CanSP/TSX	up	7	C$	11,508
FTSE	down	24	Stlg	5,691
CAC	down	4	EUR	4,835
DAX	down	7	EUR	5,517
Nikkei	up	3	Yen	16,428
HKong	down	49	HK$	15,278
Aus SP/ASX	down	23	A$	4,791
Taiwan	down	16	NT$	6,694
NZ SX50	down	11	NZ$	3,365
TGL INDEX	**down**	**13**	**-0.2%**	**7,020**

☑**ON THE POLITICAL FRONT** the **Canadian federal election** lies only a short while ahead (actually, 'tis the 23rd of this month) and for the first time in quite some while we are actually reasonably enthusiastic about the prospects for the Tories there. In the previous election, the Tories succeeded in running such at horrible campaign filled with one almost comic disaster after another that they were able to snatch defeat from the certain mouth of victory. If it had not been so funny it would have been sad; but it was funny and it was disastrous and the

Liberals were able to retain their position heading the government in Ottawa even if only by the barest of margins.

This time, however, the Tories are running a far more professional campaign. Rather than attack the Liberals for the latter's corrupt practices (always a rather poor campaign platform anywhere), this time the Tories are actually putting forth real programs that are directed to smaller government, less intrusive government, more free market policies than in the past. It is a breath of fresh political air, and it seems to be serving the Tories well.

CURRENT MAKE-UP OF CANADIAN FEDERAL PARLIAMENT:

Liberals	*133 Seats*
Conservatives	*98*
Bloc Quebecois	*53*
New Democrats	*18*
Independents	*4*
Vacant	*2*

The election draws very near and we have no idea how the seats shall be apportioned after the votes are cast and counted, but we are certain that the Conservatives will have gained seats and will likely have a few more than 100 seats, while the Liberals shall likely have lost several and may fall below that of the Conservatives. The big question shall be how well the Tories do in Quebec, where they may even win a seat or two at the expense of the Bloc, and how well the NDP does, perhaps ending with 20 - 25 seats.

Finally, **Pat Robertson is an idiot!** His comments regarding the wrath of God being visited upon Prime Minister Sharon are shameful. We are embarrassed that we do our television remote broadcasts from his studios; we are embarrassed that he's been a member of our country club!

GENERAL COMMENTS ON THE CAPITAL MARKETS

☑ON NIGERIA AND HER EVER PRESENT ETHNIC PROBLEMS: When concerned about energy one must always be aware that at any moment the situation in Nigeria can become seriously problematic at a moment's notice... sooner even! We must always remember that Nigeria is really nothing more than a figment of British imagination, rather like Iraq; that is, there is no historic reason for Nigeria to exist as it does presently, for it is really nothing more than an amalgam of various tribal areas pasted together out of British imperialism of the 19th and 20th centuries. There are no natural boundaries that differentiate Nigeria from Cameroon to its southeast except perhaps for the rather modest Mapdara Mountains. Certainly there is no real boundary between Nigeria and Niger to its north. On Nigeria's west, the Okpara River forms a small portion of the boundary between Nigeria and Benin, but it flows and bounds for only a rather short while; the remainder of the boundary is simply one set by man, not by nature. For all intents, Nigeria is simply what the British said it was, and it remains so today, with dozens... no hundreds.... of tribes forced to live with one another under the flag of this one nation. Indeed, the only real geographic boundary maker is the Niger River, and it flows directly through the country, not on either border.

As far as tribes are concerned, there are two very dominant ones: the Hausa and the Yoruba. Both have nearly 10 million people, so these are not small ethnic units. The Presidency and the most important ministries of the government seem always to be controlled by these two tribes. Indeed, President Obasanjo is Yoruba. The third largest tribe, the Ibo, live in the southeast, and it is there that Nigeria's oil wealth exists. The Hausa (often referred to as the Hausa-Fulani) live mainly in Nigeria's north and are primarily Muslims: the Ibo live in the southeast, and the Yoruba in the southwest. After these three major ethnic groups there exists several hundred smaller "tribes," all vying for what power they can within the federal government.

When Nigeria broke away from British direct domination in the 60's and declared its independence, the Ibo moved swiftly to break away even from that decision, creating their own nation of Biafra. The Biafran Civil War, fought between '67 - '70 ended with the secessionist movement defeated and the Ibo dominated "nation" returning forcibly to the control of the federal government. In what we see as the inevitable "payment" for their secessionist past, the oil wealth of southeast Nigeria has been expropriated by the federal government, creating an uneasy and readily problematic political tension between the Ibo and the other tribes of Africa. All too often, that bubbles over into actions taken by various Ibo protest organisation against the oil facilities there. What seems to be anger with Shell and other oil companies is really latent anger between the Ibo, who see their wealth dissipating, and the federal government run by the Hausa and/or the Yoruba.

So, once again we are seeing calls by the Ibo for a renewed secessionist drive to re-create Biafa. We read of attempts by Biafan separatists to restore the Biafan currency. We read and hear of attempts to force out political figures imposed upon them by Abuja. We read of attempts to impeach a local south-eastern Governor who had demanded that his state receive a "fairer share" of its oil wealth. We are fearful always that we shall come into the office one morning to find that Nigeria has erupted in civil war; that her oil facilities have been blown up; that her oil exports have stopped and that fighting is everywhere. We hope we are wrong; we fear we are not and our clients have been put on alert, for that is our duty: to worry when others don't. We are.

☑WHAT IS THIS GUY SMOKING?: Populations in the industrialised world are now, or very soon shall be, reaching the "Tipping Point" and will soon be making their way toward steadily lower numbers for the very, very long and likely un-forseeable future. We have talked about this problem for many years and we do indeed see it as the most serious problem facing the industrialised world in the coming decades. Once again, simply put, the civilised/industrialsed word refused, for whatever reason, to replicate itself. Birth rates in Japan, Italy, Germany, France, et al are now far below the duplication rate, and there is no urgency on the part of any of the governments to face this problem. Indeed, there seems every intention to sponsor a continuation, and even an engendering of, these dangerously low rates of population "growth." We strongly suggest that those with an interest in this problem to read Ben Wattenberg's enormously insightful book, *Fewer*, on this topic. It is eye-opening.

In simplest terms, it does indeed take a young and growing population to keep an economy moving ahead... especially if all of the other countries that one trades with are in the same serious predicament. It would be possible if one country's birth rate fell as long as its trading partners' birth rates were rising, for at least in the latter countries there would be continued demand for the exports of the former. However, if all see their birth rates falling and their demographics shifting downward, then all are in the same difficult predicament that none can extricate themselves from. Thus, we found the recent article by Mr. Victor Mallet of *The Financial Times* entitled *"Smaller Is Beautiful When It Comes To Population"* to be sheer folly. Mr. Mallet has in the past been rather keenly insightful on so many other topics that we find his position here to be truly quite sad.

Mr. Mallet, in his article, applauds the recent report that Japan experienced the first real year-on-year decline in population in modern history last year. He calls that news "excellent," and trots out the old Malthusian fears that unless the population of the world is brought under control famine and starvation shall be the world's future. He takes the Indian government to task for continuing to press for a larger population, while he lauds the Chinese government for its "one child" doctrine. Mr. Mallet is wrong... and rather badly so.

Firstly, if we have learned anything in the past thirty some years of watching markets and reading about them we have learned this: the world's farmers (and especially those in the industrialised world) are stunningly, wondrously, fabulously clever at learning to use new technologies to continue to produce more and more and more food to meet the demands of increasing populations. No where is that clearer than here in the US where the numbers of farmers presently are less than 1% of those at the turn of the 20th century and yet the amount of food produced is higher by many multiples, with an abundance rather than a deficit of grain and livestock production. Over the course of the centuries, farmers have gone from using scattered seed casting, to drilling; they've gone from no fertiliser usage and tiny crops, to crushed bone for fertiliser, to guano, to small amounts of nitrogen, to fertilisers spread in pinpoint accurate fashion from machines directed by GPS systems! We know only this for the future: that how it shall actually un-wind is anyone's guess but that progress has been the history of the past and further progress shall be the "history" of the future.

Mallet argues that the world is finite; that its prospects are sum-zero going forward and that progress is impossible unless population is managed downward. Mallet is a Malthusian and he is wrong.

RECOMMENDATIONS:

1. Long of Three Units of Gold/short of Three Units of Crude oil: The ratio is 8.38:1 this morning and we are more and more certain that a multi-year shift in the gold/crude ratio is upon us and we shall be adding to the trade sooner rather than later.

2. Long of Four Units of Silver/short of Four Units of Gold: This trade has proven to be, shall we say, "problematic." It moved immediately for us; it moved agains us; it moved violently for us, and now it is moving against us... formidably. We shall hold tight, but this one has cost us both mental and real capital.

3. Long of One Unit of Gold: We've given this trade plenty of room from the outset, for this is our "insurance" gold. We had been reticent about adding to this position heretofore, but we are not reticent now. Indeed, **we are buyers of another unit of spot gold upon receipt of this commentary** (cf. our discussion above in the body of our letter).

4. Long of One Unit of Soymeal: We have talked bullishly of "grains" for some while, and two weeks ago we bought soy meal. For those who cannot trade futures, we note that Bunge's shares correlate rather well with soymeal, although not perfectly, and until proven otherwise, Bunge (NYSE:BG) is the "derivative" grain trade.

5. Long Two Units of "All Things Athabasca:" We've been involved with the Tar Sands consistently for three years. We've been longer than presently at times past, and we've been at times wholly un-invested when we thought that right. However, on balance we have been bullish of Athabasca and we are again. The only question is "How" and/or of what "venue" are we to be long. We preferred exposure to Suncor Energy, but we have also suggested Birch Mountain Resources as an "ancillary" position. We've traded back and forth between the two in recent weeks, and we've been very fortunate for having done so. For our own positions we are long of more Suncor now than we are of Birch Mountain. Now we sit tight, awaiting an opportunity to add to the position.

We've begun the year on an "up" note, and are, in the only two accounts that we manage, up 2.1% thus far.

Good luck and good trading, Dennis Gartman