

# The GLEASON REPORT

## Market Timing for Investors Identify Turning Points in Asset Classes

February 2009

[www.gleasonreport.com](http://www.gleasonreport.com)

**Stocks: OUT**



**Bonds: IN**



**Gold: IN**



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- Gold, Commodities, Bonds

This issue can be linked to at: [www.gleasonreport.com/emails/2009-02-tgr.pdf](http://www.gleasonreport.com/emails/2009-02-tgr.pdf)

### Status of the TGR Timing Models

**STOCKS:** Out of all stock asset classes

**BONDS:** In VFICX only and Short Term bonds. Out of long Treasuries.

**GOLD:** In gold

#### Important Information :

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Year to Date Asset Class Returns			
Symbol	Asset Class	YTD Return	Model Status
PCRIX	Commodity Futures	-2.50	OUT
VGSIX	REIT	-17.40	OUT
VFINX	S&P500	-8.40	OUT
VMFXX	Money Market	0.11	IN
VBMFX	Bond Index	-0.72	ONLY IN VFICX
VGTSX	International Stocks	-12.00	OUT
VISVX	Small Cap Value	-13.00	OUT
VBISX	Short Term Bond	-0.10	IN
GOLD	Gold	5.70	IN

analysis shows gold to be over priced at \$928 but massive buying in Europe is pushing it higher. I'm not saying gold will fall. It's a very difficult asset to predict because it spins in a wide orbit around its point of equilibrium. My model only forecasts direction from the buy point and not specific price points.

### Stocks

Global stock markets all show a similar chart pattern. They're off their extreme lows and going sideways – waiting. Employment news is worsening but is a lagging indicator and shouldn't be seen as predictive of stock prices. The driving force for stocks in the months ahead will be the trend of earnings. My model is out of all stock indexes. Reits are doing terrible as retailers leave malls and the office market contracts. International stocks are negatively impacted by the rising dollar.

### Bonds

The bond market remains dangerous across the entire spectrum. Treasury bonds pay next to nothing. **I own an allocation to VFICX (1/6/09 @ \$8.63) which holds high quality corporate bonds yielding over 6%. It's up 0% year to date whereas the bond index is down -.72.** There's a large spread between corporates and treasuries and I expect VFICX to pay its coupon this year with perhaps some capital gain. It's possible I'll exit the fund within a few months if market conditions and my model continue to show increasing risk.

### Gold

I'm in gold and it's the only broad asset class in an uptrend. Gold is a commodity but is also real money and a safe haven destination. My

### Recent News

I was recently interviewed for the financial site RealMoney.com by columnist Hewitt Heiserman. The discussion was about market timing and my outlook for the markets. RealMoney is a popular subscription site for the advanced investor. [You can read the story published on 1/26 here.](#)

In the 1/23/09 interview you'll see that I predicted the stock market would rise about 5% or more in a bear market rally from the S&P500 level then of 815. That's what happened and the market rose 7% over the next week. So, why didn't I send subscribers an alert? I was 80% certain the market would bounce higher but didn't have enough data to be sure. Since then conditions have deteriorated.

I've wrestled with ideas on when to alert subscribers of opportunity. I have no idea who 95% of my subscribers are and I'm very concerned about inducing speculative mistakes by people who don't understand the need to enter and exit quickly. Over the last year, my alert signup email addresses have shifted gradually to banks, financial advisory firms and mutual funds. I suspect most of these firms are looking for contrary opinions while gathering various market perspectives. That's fine with me.

My concern is that unsophisticated investors will read my alerts and bet the farm or act in a reckless manner. Some people may prefer to act with extreme caution and don't want alerts or only want to check my opinion against other ideas they're receiving. Some investors want fast information and see missed opportunity if they don't get alerts quickly.

### **Subscription Service – [Sign-up Page](#)**

This is an historical time in American finance and investment decisions made over the next year will have a huge impact on the financial security of many people. I take this role very seriously and am deeply concerned about the welfare of the average working investor whom I view as my preferred customer.

Many families have lost huge percentages of their savings over the last few years by slavishly following the bad advice of commission financial advisors. Some re-invested on January 1<sup>st</sup> and are already down 10% in 2009. The mantras of Buy & Hold, Stocks for the Long Run, and Stay the Course are idiotic slogans dreamed up by Wall Street to sucker in the small investor. Believing this garbage has cost people enormous sums of money.

I fully retired several years ago and don't need to ever work again. This is possible because I can avoid losing money in the financial markets. I avoided the 2001 meltdown, did well in 2003, and avoided the 2008 market collapse. My free market timing service has done a pretty good job for people. I'm at a crossroads where I need to continue to expand my timing service or end it and move onto new things. Truth is, this market timing is hard work and I put much effort into it.

I've decided to switch to a subscription service for the alerts while continuing to provide the newsletter free. The annual fee will be \$125/year which is about half of what most financial services charge. This, will allow me to

invest in research and databases and improve my timing methods. It will prevent casual readers from making mistakes with alerts they don't understand. [The sign-up page is now active on the Gleason Report web site.](#)

Paid subscribers will get the newsletter on the 1<sup>st</sup> of each month and market timing alerts as they become available. Non-subscribers get the newsletter on the 15<sup>th</sup> of each month and get the alerts 30 days after issuance. This allows the casual reader to get the benefits of my research in order to build portfolio allocations.

I have no intention of changing the tone of my newsletter to the drab, institutional safe-speak so common to professional publications. If things don't work out for me on this venture, that's no big deal. It will give me the push I need to pursue other ideas I've got cooking on the back burner.

### **Other Notes**

I'd suggest that you don't believe anything you see on the web that I supposedly have said without confirming it on my web site. For example, I saw a company conference call transcript where the caller said he was with Thomas Nogales Financial, LLC. [He questioned the CEO of Computer Task Group about their quarterly results.](#) His questions were good enough but I don't know this person. Perhaps the transcriber heard them discussing my newsletter offline and it got mixed in.

Next month my web site will switch to [www.gleasonreport.com](http://www.gleasonreport.com) and alert emails will originate from that domain. It's a long story but the Thomas Nogales (acronym of Gleason) name was pseudonym I used while doing my original research and I never got around to changing it.

I read every emails received but can't respond to all of them personally. I'll respond to most

questions in a Q&A section at the bottom of each month's newsletter.

### **Consensus Forming on the Stock Market**

The commentators I read in various publications generally agree that the economy may see a recovery starting in the second half of 2009. This idea is supported to some extent because broad economic indicators are not declining at the terrifying rates of late 2008. Many of the measures are moving sideways and the consensus seems to be that with continued fiscal stimulus things will gradually turn up but it will take one or two quarters.

That's a nice theory but what if the sideways movement is just a plateau that precedes another decline? If forced to guess, I'd say the stock market is going lower. I can't forecast out very far but my guess is we'll be fortunate to see a weak recovery in 2010.

### **The Great Debt Transfer**

After thirty years of non-stop spending and borrowing the tide has turned. The American consumer is broke and can't buy from the car companies who are broke and in hock to the banks who are broke and need loans from the government – the lender of last resort who is also broke. Circuit City went broke and can't pay its strip mall rents so the Reits that own the malls are losing money as even more retailers go under. We are on the cusp of a large wave of corporate bankruptcies and consolidations and there's no way to stop it.

The founding fathers of America were idealists and altruists. At a rare point in time these wise and worldly men came together and designed the framework for this great nation. It's been going downhill ever since.

American politicians today are totally corrupted by the campaign contribution system. To become a player in Congress you have to be on the take from moneyed interests. That's why guys like

congressman Ron Paul have little influence. Your congressman is likely no different from former Illinois governor Blagojevich. Washington politicians shake people down all the time – it's how the town is run. You could sit your congressman in a room with Gandhi, MLK and Mother Theresa all pleading to do what's best for the people and they'd still do the wrong thing if offered \$5,000.

### **Who's Running America?**

Criminologists will tell you that 6% of the population is afflicted with a severe psychological problem called anti-social personality disorder. The worst cases are true sociopaths and near 100% of these people end up in prison. You can't reform them because it's genetic – mom and dad are not to blame. Milder cases may go into politics or do very well in large business organizations where their egomania and pursuit of self interest without regard to others is rewarded. A sociopath can lie and never feel regret – they're incapable of caring about the emotional pain in those they injure. When I was doing fraud investigations, I'd see this ego driven certainty and deeply rooted dishonesty in some senior executives. When you mix egomania with intelligence you get guys like our recent past presidents.

This little factoid is important and no laughing matter as we look at what the politicians will do as the financial crisis expands.

There's two paths to handle America's debt problems. One way, and the right way, is to allow the economy to step down to its equilibrium point. In other words, we must let the real economy emerge. It's a smaller than people think. That means we let the business failures happen and job losses pile up. That isn't going to happen because politicians are elected officials and will cave in to pressure and money interests.

The government solution is to bail everyone out and eventually transfer all bad corporate debt, pension fund obligations, municipal debt, and hinky mortgages onto the government balance sheet. And, from there, monetize it. This is what they are already doing. To accomplish this task, the government first considered letting the Fed take on the bad debts. That idea didn't go far. So, now they've come up with this "[aggregator bank](#)" idea. The assets will be purchased by the Treasury at a bloated price with the hope of later selling them to foreigners or wealthy speculators. It's a clever way to disguise a fire sale of America's asset base. Patience and reform is needed; not a give-away.

What is this aggregator bank entity? Think of it as a giant Excel spreadsheet where every bankrupt city, pension fund or company gets an entry. Debts will be offset between the various deadbeats on the spreadsheet and what can't be directly cancelled will be sold off to bargain hunters with the rest absorbed by the taxpayer. That's what it will come down to. Your debts won't disappear, only Wall Street's.

Congress has other plans for you. Mortgage debt and consumer debt will be alleviated through tax relief and various credits and benefits. You may think this sounds absurd but one way or another the debt must be made to disappear. If the debt doesn't go away fast then the world wide asset value collapse will continue. They want to turn the corner on deflation in order to inflate the system. Prices must go up and especially the stock market. Obama is going to zap America with spending from his Debt Death Star.

Here's the important thing to understand as the crisis continues to unfold. The problem is about survival - the government's survival, not yours. The Obama plan to spend \$822 billion won't change a thing. It's pure folly and a waste of money and will not prevent the economy from sliding. This idiocy is being pushed by Wall Street and big money interests. It's a total lie that

giving money to these greedy bastards is the way out for your friends, family and community. They will spend trillions trying to prop up a system that wants to contract. The stock market may recover like it did in 2003 but it will decline again. Eventually the US economy must be allowed to contract.

I criticized Bush for wasting \$1 trillion on the Iraq War over five years. Obama will squander that in one year. Stimulating the economy by targeted spending leads to graft and political payoffs to the constituencies of a corrupt congress. If spending is what they want, it would be far better to give the money to the people so they can pay down debt or have some dental work done. Why not send people a debit card with a one year expiration date?

### US Debt

The chart below is for 2007. It shows the federal debt at \$9 trillion. In 2008 it hit \$10.3 trillion. As a percentage of GDP, debt was 65% in 2007. It was 73% in 2008 - the same level as 1950 when the US was in deep hock because of WWII. The situation today is actually much worse than 59 years ago.

All those kids born in the 1950s are now close to collecting social security and placing more financial demands on the government through Medicare. The population was rapidly expanding fifty years ago and the tax base was expanding. Now the birth rate is much lower and the tax base is contracting.

From 1950 to 1960, America used increasing tax receipts to pay down the debt and in the 60s and 70s we used inflation. Ronald Reagan had to stop the stagflation of the 70s so he switched from printing money to printing debt. You can see this clearly on the chart as debt took off in 1981. The great stock market gains from 1982 to 2000 were due to leverage made possible by expansion of government debt, personal debt,

and the scaling up of the banking industry. The increasing productivity Greenspan touted in the 90s was a byproduct of expanding debt leverage. It goosed up the productivity numbers, wages and stock markets around the globe.

The kiss of death for the financial system was planted on Uncle Sam's lips when George Bush refused to accept the 2001 stock market decline and doubled the national debt from \$5 trillion to \$10 trillion. Look at the solid line as gross debt skyrocketed after 2000. George couldn't wage his oil wars if the public mood was sour about the economy. He was warned in 2002 not to do this by some of the best finance minds in

America but a lust for glory and his foolish over-confidence doomed us. Congress went along with it because spending money gets them re-elected. The wars in Iraq and Afghanistan

are failures but the debt continues to soar. What a legacy.

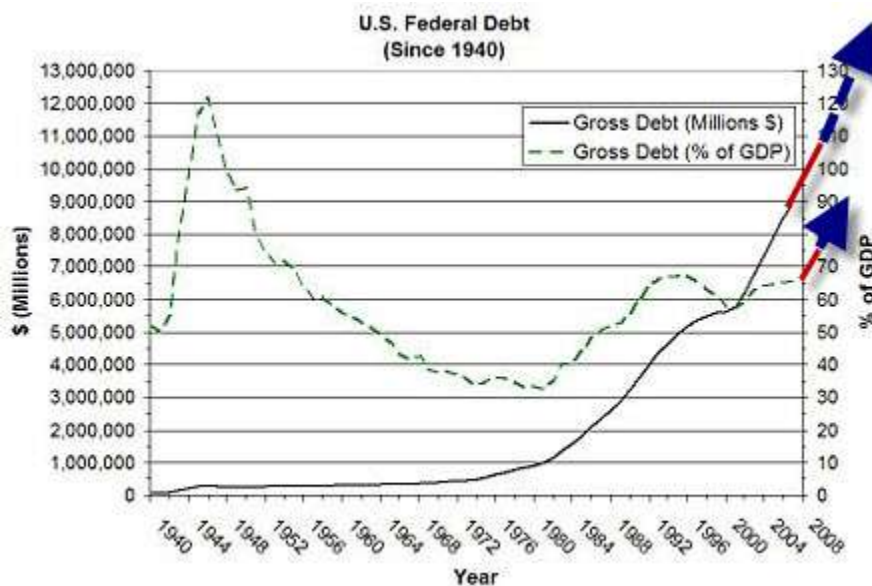
The Bush debt expansion started in 2001. I put his debt in red for 2008. It rose to \$10.3 trillion and debt as a percentage of GDP went to 73%.

Obama has been dealt a hopeless hand as president. If he stops spending and borrowing the business sector will implode. So, he'll continue spending because he's a politician and probably as mentally disjointed as your congressman. I've plotted his spending trajectory in blue on the above chart. This is

based on his public statements about intended debt growth. He'll take debt to \$15 trillion and debt as a percentage of GDP could hit 90% or higher. Within four years, total debt could exceed annual GDP. It will ramp up even faster now because GDP is in decline.

The situation today is quite dire. We can't continue to issue debt because the world is choking on it. Gold is strong while everything else is so weak because investors aren't being fooled by the phony deflation fears.

In 1948 when debt was 90% of GDP we were exiting WWII and world was in a shambles.



America was the only game in town. The world won't continue to buy America's debt because it can't. There isn't that much free cash available any more. The Chinese have accumulated \$2 trillion US dollars over a decade and can't double it again. Therefore the

FED will print money by buying bonds. This creates money because as the Fed buys Treasury and corporate bonds it pays for them with cash thus pushing more liquidity into the system.

It's now a waste of time to plead for financial responsibility. We're in uncharted territory and this government debt will end in disaster for the dollar. I don't see any way out of it but can't predict when it will happen.

### The Inflation/Deflation Debate – Again

The discussion continues about whether the US will go into a period of inflation or deflation in the decades ahead.

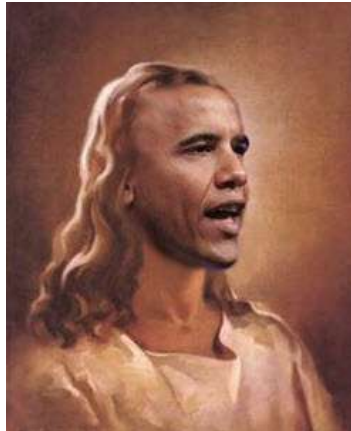
The US national debt trajectory is unsustainable. Some believe we'll face decades of recession and deflation as the debt is whittled down. Others believe we face extended inflation. Others say war is possible as nations vie for control of resources and try to position themselves as the dominant economy.

I understand the different arguments and see the truth and logic expressed by various commentators. I just don't see how the deflation argument holds much water. Deflation is only likely under a gold standard where the money can't be corrupted.

### Hope Springs Eternal

America has a new president. Obama is a smart and articulate American. Obama is generating a lot of positive buzz. I think he's handling the comical Joe Biden quite well by [putting him in charge of improving things for the middle class](#).

*"It's a new day for workers," said James Hoffa, president of the International Brotherhood of Teamsters, who attended the ceremony with other union leaders. "We finally have a White House that is dedicated to working with us to rebuild our middle class. Hope for the American Dream is being restored."*



A lot of the recent Obama optimism is helped along by a sense of relief that the nation has rid itself of George Bush. Like the flushing of a toilet the waste goes away and the bowl fills up with clean, clear water. In the swirl of pure, shimmering water we see an apparition - the confident face of a savior; why it's Barack Obama rising from the river Jordan. Obama, the man who is going to save us. His supporters say this is change you can believe in.

Well, here's what I believe. American citizens are headed for a big down step in lifestyle.

### Change You Should Believe In?

Optimism is unrealized hope. Believe the slogan if you want but I think the joke will be on you. Bush, Bill & Hillary, Cheney and Greenspan and the whole crew of politicians, past and present, know it.

I'd like to be optimistic too but when it comes to money and markets I think it's best to be cautious. I suspect that in four years we'll be hitting the flush lever again with a another sigh of relief.



Obama can't turn this thing around by spending money. Thirty years of debt expansion created massive amounts of phony asset values. It's deflating in value. The volume of existing bad debt is simply

beyond anyone's ability to know and I firmly believe nobody in Washington really understands the extent of the problem.

If Obama is realistic, his best unrealized hope is for things to first stabilize. To accomplish that he'll spend whatever it takes (his own words) to stop the decline. Within a few years our national debt will approach \$15 trillion dollars. That's 15,000 billion dollars. The government will have bought up the bank debt, pension fund debt, state and municipal debt, corporate debt and massive amounts of mortgage debt. They've already said they'll do this – it's not even a maybe – it will happen.

As this process goes on and on and on, you have to believe that the system will totter on collapse. How can any nation possibly service that debt load. It would require a stupendous future level of economic growth to ever pay it off and at the very time that US demographics are moving toward saving and away from spending. What will happen to our corporate sector and our industries as things move away from consumption? Many firms will go out of business. The contraction will be huge and the stock market will reflect it.

Let's assume a best case scenario that the government is able to issue more bonds and things stabilize at \$15 trillion in debt.

There are three ways to get rid of the deficit.

1. Pay it off in good money through saving, taxation and reduced government services
2. Default on the debt
3. Monetize it

Now, you can hope all you want but I'm telling you #1 all alone is politically impossible. There is no way the debt will ever be paid off only with good money. #2 is diplomatically unacceptable under any circumstances. It will take a combination of severe cuts to social services; tax

increases on big earners, taxes on energy, taxes on inherited wealth; plus inflation extending over probably twenty years.

Some people like to believe that we'll have a decades-long deflation with falling prices and a depression. Perhaps this idea of a deflationary 2<sup>nd</sup> Great Depression has its genesis in the idea of a religious penance as payment for our greed. I don't think our future is deflation. Our national debt is denominated in dollars; not Euros or gold. It will be paid off in dollars and you'd have to be damn naïve to believe those future dollars won't be of the inflationary variety.

### History as a Guide

England was the big world power in the 19<sup>th</sup> century. They were always in wars or putting down insurrections like the Boer War. After WWII they were broke. It only took 30 years for them to go from giant squid to sushi. The subsequent decades after 1930 saw major parts of the empire walk away and other nations pass England by.

In 1895 the gold in a British gold Sovereign had a purchasing power value of £1. In 2009 that same sovereign was worth £175. The difference is inflation.



Over the 115 year period, that works out to an annual inflation rate of 4.7%. And remember, England was on the gold standard for most of those years. England was also in recession for many of those years but it wasn't deflationary for price levels. There is no gold standard now. Money is printed whenever they want so how can there possibly be a long term deflation.

The case of Germany is well known. After WWI, Germany's surrender terms stated it had to pay reparations to the allied powers. US general George Marshall warned the European powers that placing excessively punitive terms on

Germany would not have a good outcome. They ignored him. The terms were indeed oppressive and the German politicians eventually buckled and began to print money. They paid off the reparations with bad money because they could get away with it. The collapsed economy brought about political extremism and Hitler. You can't separate politics and economics.

The best case for US inflation is probably the case of England and the worst case is Germany. That's why I think we'll have 5-7% inflation for the next twenty years to whittle down the debt load. I'm not in the hyperinflation camp at this time.

I strongly suspect Obama and later presidents will do what has to be done if the gradual inflation path fails. They'll mistakenly make every attempt first in good faith to stabilize the economy by feeding the banks. Then will try to gradually increase inflation to the 5-7% range to dissipate the debt over a couple of decades. Alan Greenspan suggested the same outcome in his recent autobiography, *Age of Turbulence*.

Our creditors will go along with this for a while because it's the best anyone can hope for. This assumes the Fed can control the system and things go according to plan. I must say in all honesty that I don't think it will succeed or be a smooth transition.

### **Here's Proof of Their Intent**

The proof of future inflation is right before your eyes. The tipoff to the absurdity of long term deflation is the new concept of an "aggregator bank". This entity that the government is discussing is a super bank that will take on all the bad debt in the country. So, what will they do once it's all on the books? Pay it off in gold? Nope. They'll sell off some assets to foreigners and to our own bailed out banks for pennies and the rest they'll simply monetize. Poof, it's gone.

Look who will head the Treasury -Tim Geithner - the guy who forgot to pay his tens of thousands in taxes. He will head tax collection. He's in that job because he worked for the IMF and was a Fed governor and knows his way around the system. Obama isn't going to raise your income taxes because people would point the finger at Timmy. He'll tax estates, cut Medicare, force corporations to close their offshore tax haven dodges and find indirect ways to tax. He'll cut your Medicare benefit by imposing means testing. If a 70 year old has \$100k in the bank, she won't qualify for government health services. Sorry kids, no inheritance, I need a gall bladder operation. You are going to be squeezed from every side but they won't raise your income taxes.

[As for financial responsibility, here's what Obama said.](#) *"He said his administration will begin confronting the issues of entitlement reform and long-term budget deficits soon after it jump-starts job growth and the stock market."*

He's saying he'll be fiscally responsible once the stock market goes back up and unemployment is no longer a big problem. The corollary to Obama's statement is he's saying he won't be fiscally responsible until things improve. If things keep going down, he'll never be responsible and that, my friends, means spending and inflation. This is how politicians talk when they're sending a message to Wall Street. And that's why gold hit \$900. Yet the deflationists say prices will go down and we'll have a prolonged recession for decades. Sorry deflator-guys - I don't think so. If you believe in long-term deflation, I suggest you hoard dollar bills in a suitcase under your bed. Check back with me in ten years on how that worked out.

Let's go deeper into the land of make believe and assume for now that Obama's plan will work.

### **When Will Inflation Hit?**

Will all the spending result in inflation? If you pour water into loose, dry garden soil, the liquid is soaked up for quite a while. Then, suddenly, the water pools on the surface as the ground becomes saturated. The government will pour money into the economy until the inflow of cash catches up with the destruction of asset values. As some point inflation will suddenly appear and catch everyone by surprise.

The December 2008 inflation rate was under 1%. We could see a negative monthly rate occasionally over 2009. But just wait. Inflation is coming like Spring follows Winter.

You have less than one year to get positioned. You don't want to be in bonds when it hits. You will want to be in commodities but not yet.

### **Will the Bond Market Choke?**

The effective Fed Funds rate is now zero and the interest rate on three month treasury bills is zero. [On January 29<sup>th</sup> Vanguard stopped new investment into its money market funds.](#) Say what? True - can't pay interest on new money.

Rates can't go any lower so the feds will continue to issue debt and spend until the economy stabilizes. They will then gradually raise the Fed Funds rate but this won't happen until the inflation rate rises. The Fed Funds rate will move up gradually with inflation but will likely remain a bit lower. Thus, there will be a disincentive for holding cash. They hope money will flow into the stock market. That may happen but speculative surges in other asset classes will also result. This means volatility.

As long as the 10 year treasury bond exceeds the rate of inflation, the bond market will remain stable. Thus, debt buyers will accept bond yields of 8% while inflation is at 6.5% and things will roll merrily along. Of course, older bond issues will be clobbered as rates rise. However, once the target inflation rate is hit, long bonds will

settle down and earn a percent or two more than inflation. If inflation exceeds the 10 year bond rate, all hell will break loose.

I would not own the 10 year Treasury Bond because rates will rise at the first whiff of inflation. For now, corporate bonds, on the other hand, are selling at a huge spread premium over the tbond. For example, the 5 year A rated bond is yielding over 6% and AAA 20 year bonds are yielding 5%. That's a huge spread over the 2.6% rate on tbonds. These corporate rates could drop in 2009 providing a nice capital gain.

Whatever happens to bonds, the stock market won't like inflation one bit.

### **Stocks and Inflation**

All asset classes are discounted by the inflation rate to some extent but stocks are impacted heavily. "Inflation is hell on equities", said renowned investor John Templeton.

The recovery in the economy – I should say re-stabilization, will come at the expense of stocks. As the inflation rate exceeds the market's dividend yield, dividend stocks will be stifled. The stock indexes will suffer. There will be periodic advances and regressions in inflation. Hope will push stock prices periodically higher only to see them again decline. Stocks could trend higher over time but buy and hold investors will see poor inflation adjusted returns.

An inflationary environment is a market timers dream come true. I think we'll have excellent swing trade opportunities during inflation.

### **Where to Put Money Now**

My model is out of stocks and has just a tiptoe in corporate bonds. I'm in gold. Cash and gold have been the right place to be for 2008.

There are three likely outcomes to our financial crisis.

1. US debt and money printing explodes and the world financial system morphs into something new with much less dollar dominance. A trade currency is created with a weighting of less than 50% greenbacks to replace the dollar standard for buying commodities. This amounts to a devaluation of the dollar and US consumer prices will soar as foreign goods will cost more.
2. The dollar standard holds. This assumes other nations remain financially weak and inflate their currencies along with the dollar. The US whittles down its \$15T debt with twenty years of inflation at 5-7% and other nations do the same.
3. Energy wars and chaos. Nations align with regional power blocks centered on America, Russia and China. Resources are taken and controlled by threat of force. World trade plummets along with living standards.

I believe #1 is very possible if #2 fails. Both of these options mean much higher inflation. Deflation is very unlikely.

[George Soros discussed the inflation topic recently and said the trick will be restraining inflation over the transition.](#)

*Soros said the United States needed "radical and unorthodox policy measures" to prevent a repeat of the Great Depression of the early 20th century that include recapitalizing banks and writing down the country's accumulated debt.*

*Also, he said, it should create more money to offset the collapse of credit and then rapidly pull that cash out of the system when inflation*

*emerges. The government would have to be very nimble in the timing of such moves, he said.*

*"If they are successful...the deflationary pressures will be replaced by the specter of inflation and the authorities will have to drain the excess money from the economy almost as quickly as they pumped it in. Of the two operations the second one is going to be, politically, even more difficult than the first," he said.*

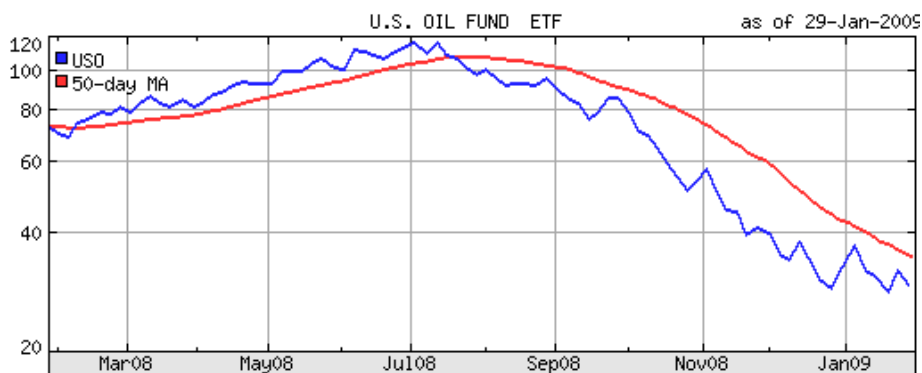
Soros doesn't discuss the \$15T debt but it's on everyone's mind.

If the global system is able to turn the corner on deflation, recovery will come with inflation. The timing of this event may be one of the most important periods of your financial life. An inflation boom will first appear in commodity prices.

This means you must get a portion of your assets into inflation hedges at the right time. Change I can believe in could come fast and if you're not positioned it will cost you dearly. Timing is everything. Stay away from stocks for now. My stock model should catch the turn very quickly. If you don't trust market timing then wait for earnings to firm up and the broad economy to improve. Avoid treasury bonds – they don't pay anything.

If the forces of deflation are not controlled, commodities will continue to fall.

I don't have a timing model for oil so my observations are speculative. I'm paying close attention to oil prices as tracked by USO. Oil is the dominant commodity and everyone must have it. It's been in a sideways



trend for the last month but I'm still not certain it's at a bottom.

### **Gold and Inflation**

Some people believe gold will push over \$2000 in a few years. They might be right but I think gold is properly priced at \$800 and that's good news for you. I derived this value by two different methods consisting of averaging purchasing power into the future from prior periods.

Now may not be a good time to buy gold for speculation. It's ok to buy now to obtain a core gold position (even at \$900) if you don't own any. Why is it good to own core gold if I don't expect a fast boom and it's over priced? Gold benefits from inflation or chaos and it will continue for years. The global financial crisis is a monetary problem.

You'll have to read between the lines here. First, please understand that I don't dislike Obama and I believe his cabinet appointments are largely competent people. They want to do what's best for America but are constrained by the political process and the disaster handed to them. Some people compare Obama to Abe Lincoln. Well, honest Abe inflated the money supply during the Civil War. He said it had to be done. The Obama team will do what must be done to fix the US economy because the nation's survival is at stake.

The US debt problems are so huge that a reasonable person is justified in wondering if our economic system can survive in its present form.

At some point, if the public loses confidence and starts hoarding gold, the government may place a federal sales tax on gold sales or require a 1099 filing every time you sell gold to a dealer. Abusive government actions like this will be supposedly justified by the government's need to control speculators but the real objective will be

to penalize wealth preservation. These actions would introduce disequilibrium into the gold market thus setting up huge volatility moves. Private sales would occur above the spot price and a black market would ensue.

Owning a gold ETF like GLD is fine but makes you captive to the anti-speculator types in Obama's government and their coming tax heist. They could apply an imputed tax on paper gains to stop money leaving the dollar.

The broader issue for the world is one of a systemic collapse of the US dollar dominated financial system. The dollar will still exist but its role as the world reserve currency will certainly end. We can postulate that the world will likely go along with the Obama stimulus plan for now but things could change very quickly. We can see the early signs of this in Europe. Fear is spreading and wealthy people are buying gold and driving up the price. Investors will demand a more stable currency system.

Obama can't just print and spend money. He must show a path toward stability of the US financial system. He must explain how the US debt will be handled. As inflation rises, Obama will need to skim off dollars from the inflating asset prices to fund the federal budget while reducing costs by cutting services. I expect means testing for obtaining Medicare. In addition, estates will be hammered with very high inheritance tax rates. The WWII generation is in their 80's and the boomers are in their 50's. That's a lot of money. They'll grab whatever they can see and the reverse is also true.

You may wish to deal with Kitco for gold – they're the best online dealer I've found. [Check out the 1oz bullion bars](#). Bars have a very low markup compared to the bullion coins but are often out of stock. I had previously recommended Monex but there's a problem with junk mail and calls from marketers. This is an

unfortunate problem with many investment services and if it happens I never do business with them again. TGR has never and will never sell subscriber names or email addresses. TGR doesn't accept advertising.

### Prepare For Uncertainty

A sustained economic recovery may not be possible. In that case, it's essential that your assets and family are properly protected from the chaos that could result from an economic breakdown. The FBI estimates that [criminal gangs in the USA have swelled to an estimated 1 million members](#) responsible for up to 80% of crimes in communities across the nation, according to a gang threat assessment. This problem will expand and will be most pronounced in larger metropolitan areas but even rural areas won't be immune. As jobs are lost some people will turn to crime and drug dealing.

I'm not saying this will happen but I do believe preparation is wise. I've written before about having a cache of food and medical supplies to last for several months. Food shortages could occur if there's a breakdown in the global monetary system.

### Q & A:

In this section I answer questions received by email over the last month. I can't respond individually to most emails any more due to the volume so I'll summarize them here.

**Q.** In your [September 2008 eletter](#) you discussed market timing using a moving average and the leading indicator from OECD. Is this indicator called the MEI on their website? Is the level of 100 significant?

**A.** Yes, it's the MEI and they track it for various nations. The 100 level means nothing. Look at the change in the indicator not its absolute level. You'll have to play with the index and the

indicator to figure this out. This isn't a timing method but more of a broad economic trend indicator that should keep you out of serious trouble. I don't describe the technique exactly but if you have an aptitude it should jump out at you.

**Q.** I'm a non US citizen although I have a Schwab trading account in the US and would appreciate if you could point me in the right direction to build a balanced portfolio "smart #1" based on your book as I believe I cannot invest in the Vanguard Funds or similar.

**A.** My book lists comparable ETF products that track the Vanguard index funds. Other ETF products are also very good as long as they tightly track the asset class. You can determine this by [charting the Vanguard fund and the ETF together on this page](#). In this case I'm comparing SPY to Vanguard's Reit fund. The funds don't move closely together over all time periods and thus cannot be substituted.

**Q.** Given the current state of the markets, do you recommend any one or two of your portfolios over the others, for someone who is just getting started with your program at this historic period in investing? For one starting at this time, should one immediately place cash in the various asset classes designated by the portfolio? Should one average in? Should one wait for specific signals from you to time the better point of entry?

**A.** The choice of portfolio depends on how much stock and bond allocation you want and if you care to invest in commodities. When buying, I go all in but some prefer to average in. At this time, the passive investor should avoid all stock funds for the next six months. There's no rush to get in. Don't invest in stocks until my stock model signals a buy for the broad S&P500 index. Commodities are very different. They could spike with inflation or a dollar decline. A non-commission financial advisor can help with selecting specific allocation percentages. If they suggest placing 70% into stocks, knock on another door.

**Q.** Do you issue buy and sell signals for ALL asset classes that you use in your portfolios? According to your observations, for example, it seems ludicrous to be in bonds for the foreseeable future. What does one do if one is in a Safety portfolio? Take the bond money out and put it in cash/money market?

**A.** The portfolios discussed in my book are for passive investors who don't want to time the markets. You probably don't need a commission financial advisor if you use my portfolios since they outperform most pension funds. For those who do wish to time the markets, I only track the broad S&P500 asset class. Other US stock classes are highly correlated with the S&P500! When in stocks I diversify across stock classes to optimize returns.

I don't time Reits or commodities. For those asset classes I use a more simple method which is speculative. When out of an asset class I put that allocation into cash. I don't recommend over-weighting an asset class if you're a passive investor.

Bonds are a broad market. In 2008 treasury bonds did very well but most other bonds lost money and my model was out of bonds. My bond model forecasts the broad direction of interest rates. I will look at yield spreads and try to suggest a segment of the bond market with a good risk/return profile.

**Q.** Your model is in corporate bonds, and I've seen some positive comments from you on junk bonds; neither of these assets are among those that you identified for your portfolios. Do you nevertheless issue recommendations/buy alerts for them (and any other recommendations outside of your designated asset classes) at appropriate times?

**A.** I did mention junk bonds in 2007 and early 2008 but don't track them using my bond model. It was a speculation that failed. I was wrong in

not being specific about that and have since changed my policy.

My bond model went positive in January 2009 but only corporate bonds met other criteria. I am in VFICX and no other index or bond fund. I discussed TIPS in November 2008 and identified opportunity there but it wasn't a bond model play and has done ok. When I see extreme divergences in rates between bond classes I'll discuss it. An investor has to do their own analysis on these topics or hire a fee-paid financial advisor (non commission) and discuss these ideas to determine if it's an appropriate investment.

**Q.** Whenever you issue sell signals, what do you think about selling AND going short? For example, had one exited the long side as you recommend and then bought the ETF to short SPY (SH or SDS), one would have of course made money on the down side as well.

**A.** Historically, shorting using my stock models would have been a very successful strategy. It's up to the reader what to do. I personally never short the indexes because I'm risk adverse like most people. If I had shorted and gone all-in following my models, I could be sipping cappuccino today with George Soros in Davos. Risk tolerance is probably hard-wired into individuals and the most successful investors have a high tolerance for risk/low-fear and good analysis methods.

**Q.** Your model is currently in gold. For your portfolios, is this a good time to open a position in gold? It seems a bit extended. Should one wait for a pullback to some point? Do you issue buy alerts to start or add to positions for assets where you are already in the market?

**A.** I think everyone should own some gold. I agree that gold is pricey at \$928 but the trend is up and I can't predict the high only the direction from my buy point. My model, when it sells, should catch gold close to its peak – within 15%. That's as good as I can do. My gold model went

positive at \$328 several years ago and gold keeps chugging upward with a lot of volatility.

**Q.** Hey Tom ..... I know you're an honest and above board kind of guy. I see that the Dividend Stock section has disappeared from the website. I also know that the purchases haven't worked out any better than the overall market as a whole, and led down by GE first and foremost. I have "bragged: you up to many people, about how different you are from so many other financial websites I had run across in the past .... and how they always emphasize their winners and hide or "disappear" their losers. Don't let me down here -- in my most humble opinion I think it would be good to make some small mention of the dividend stock purchase section "disappearance" in your upcoming newsletter -- just to keep yourself and your site different from all those "other guys".

**A.** I removed the dividend stock section from my web site. My stock picks from early in the year didn't work out. Actually GE was a bad idea and ATT lost money too. I should have exited them when my stock model said to get out. I still personally own PNW and APU as dividend plays and they're neutral considering the dividend income but still down a bit. I commented in a prior newsletter that going forward all recommendations not based on market timing models will be presented as speculations. In the investing field you learn through pain and I never stop learning.

I've decided to stick with market timing of the indexes and avoid individual stocks. At the micro level I don't have any advantage over the market. If interested in dividend stocks you may wish to check out [www.dividend.com](http://www.dividend.com) and try a short term subscription. Morningstar.com also offers a dividend stock newsletter.

My historical market timing results for stocks and bonds is on the web site going back many years. So far, my stock timing is 100% but there's no guarantee such a streak will continue.

Interest rates are more difficult to time than stocks but I've done well. I've done well with gold too but it's very volatile.

### **Summation**

Stay out of stocks for now. It's perfectly ok to sit in cash and gold. At some point you'll have to act and take financial actions that could be very stressful. The world financial system is about to change.

Buy & Hold is not a good strategy if what you hold goes down. I believe in asset allocation but supplemented with market timing to avoid losses.

Best Regards,  
Southwest Ranch Financial, LLC  
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Tom Gleason, Manager & Researcher

Author of: [How To Invest If You Can't Afford To Lose](#) (Free download on the website)

Tom Gleason has degrees in finance and information systems. He's worked as a bullion dealer, fraud investigator, real estate appraiser and financial analyst.

[Previous eletters for the past year can be viewed on the TNF website.](#)

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