

June 28, 2005

As always, thanks to Dr. Bob...John, the latest from Bill Gross is out. He talks about the lack of "real" yield and why he's going long duration. He seems to be in the "liquidity trap" camp of which I am a member.

Fire! By Bill Gross

June 28, 2005

John Mauldin's ... Thoughts From The Frontline

Outlook for Rates and the Curve

by Douglas Greenig (6/10/05)

June 28, 2005

As always, thanks to Dr. Bob...John, he tells it like it is:

"The Dutch example confirms that for consumer spending to slump in the wake of a fading housing bubble, house prices do not need to fall at all. It is sufficient that they stop rising, thereby depriving households of new wealth effects and the associated borrowing facilities.

Therefore, major housing bubbles imperatively end in a hard landing. A second major adverse influence on economic growth implicitly arises from the sudden cessation of the building boom. **Yet the worst looming problem is always the potential damage to the banking system through escalating bad loans."**

CRIPPLING "WEALTH"

Kurt Richebächer

June 26, 2005

As always, thanks to Dr. Bob... John, as I've mentioned a few times over the past couple of years, the housing component of the US CPI measure is really not indicative of the actual house price inflation. This is the first article by a newspaper or magazine publisher that actually brings up the subject:

Compliments of the New York Times...

How Home Prices Can Be Hot but Inflation Cool

By Daniel Gross

June 26, 2005

Compliments of the Financial Times

John Dizard: Gold breaks out but the best is to come

I have been rather annoyed by the recent rise in the gold price. I have started writing a book on gold and wanted its price in the big currencies to go nowhere, that is to say, a little up, a little down, for the remainder of the year.

Then, starting at the beginning of 2006, I wanted it to begin a gradual rise, with that increase becoming dramatic in the autumn of that year to coincide with the book's publication. That was the plan.

Instead, gold has begun what the technicians call a "break-out" against the euro, the dollar and now the yen. I take some comfort in the belief that this is the beginning of a multi-year bull market in the metal, which probably means a bear market in almost everything else.

The trigger event in the recent break-out was the defeat of the European constitution in the French referendum. Technicians and traders who had been plotting every little squiggle of the dollar price of gold suddenly noticed that the euro, which had traded in tandem with gold since its inception, had become decoupled from the metal.

It was only last week, however, that the dollar price of gold briefly broke above the key level of \$443. Martin Pring, a cautious technical analyst, says: "That move above \$443 breaks an important uptrend line for gold. But it is not just the dollar price; gold in global terms is doing well." Gold traders tend to be technicians, rather than fundamentalists. The huge above-ground supply of gold means that attempts to judge the metal's prospects by looking at mine production against identifiable demand for fabrication will not work very well. It is investor sentiment that is important.

Kevin Grady, who manages trading for Refco on the floor of the Comex in New York, confirms: "It was the break-out of gold in euros – that is what everyone is looking at."

For years gold trading had been a game of mine owners hedging their production by selling gold short in the dealer market and on the exchanges. Their relentless shorting of their own product crushed the last generation of goldbugs.

Mr Grady says: "The mines are now out of the picture. Investors are feeling comfortable trading gold because the mines won't sell against you." Most of the mine short sales were effected through the over the counter dealer market. As one such dealer in London says: "At its peak, mine hedging [short sale positions] was about 120m ounces. Now I think it is lower than 50." The traders say every sell-off

in gold is taken as an opportunity by the miners to buy gold to cover their short positions.

Why were the miners selling gold short in the first place? It was a cheap way to borrow money to cover their capital expenditures. Mines could borrow gold at low interest rates through central banks, intermediated by bullion dealers. They could pay it back from mine production in future years. During the gold bear market of the 1980s and 1990s, short selling production made it possible for mines to lock in good margins. This hedging kept the gold dealers in business for 20 years of thin investor demand.

Now the investors are back. According to Mr Grady: "Retail used to be one contract, two contracts, or five contracts. Now retail is 50, 100, or 200 lot blocks." A single gold futures contract on the Comex requires original margin of \$1,300. There are apparently a lot of individuals who can throw \$130,000 at a gold position on the exchange.

This has been made easier by the introduction of electronic order handling. Customers can enter orders, get them filled on the floor, and have that reported to them in 10 to 16 seconds. That is faster than flipping houses in Florida.

There has also been more activity on desks of the over the counter dealers. As their customers among the mining companies gradually de-hedge and reduce their positions, they are replaced by sellers of commodities indices. The sellers of the indices, which now have capitalisations of \$50bn-\$60bn, need to hedge their sales to customers with purchases of the components, which include gold. European institutions have been significantly increasing their participation in the indices.

The gold mining stocks have not been attracting the new interest that the metal itself has. Shares peaked in November and then took a dive. They have recovered since but not yet to the highs of autumn. "The shares have been moving about three times the rate of the gold price," says Cesar Bryan, the manager of the Gabelli gold fund. "Since the recent gold bottom in May, the metal is up about 5.5 per cent and equities are up 16 per cent."

That makes sense. With hedges taken off, companies' earnings are leveraged to the metal price.

I still think a big rise in the gold price is at least a year away. Central banks need to give up on raising or even holding rates and then try to reliquify their way out of asset deflation.

That's when the real fun will begin.

June 23, 2005

John Mauldin's ... Thoughts From The Frontline

The Idea of Europe

June 23, 2005

Thanks to Mark Hugh Sam of Sellers Capital in Chicago for this excellent piece...

Value Investor Insight

June 20, 2005

John Mauldin's ... Thoughts From The Frontline

What's Worrying The Chairman?

June 20, 2005

As always, thanks to Dr. Bob... John, in Hussman's weekly letter he gives us a very reasonable way of the return expectations one could get from Google. He also compares fluid dynamics with stocks....

Fluid Dynamics, Boundary Conditions... and Google **By John P. Hussman, Ph.D.**

June 17, 2005

John Mauldin's ... Thoughts From The Frontline

Public Pensions, Public Disasters

June 17, 2005

Thanks to Dr. Bob for this fascinating bit of intelligence... John, a great 1 page review of Fed's issues at hand:

Comstock Partners

They even mentioned Greenspan's speech and the amount of paragraphs devoted to housing! (Even though I counted 7)

June 16, 2005

Thanks to Dr. Bob for this fascinating bit of intelligence... John, okay I promise this is the last piece I'll send you about the housing bubble. The Economist actually does a pretty good job in summarizing. It is evident that the world is in a most precarious situation if house prices even just level off. Since, it seems that EVERYONE is in on this housing bubble talk I think we are still a ways off from the peak, believe it or not (I'm allowed to change my prediction aren't I?). One of my favourite quotes of all is one from Keynes. "Markets can remain irrational longer than you can remain solvent."

The Economist...

In Come The Waves

June 16, 2005

Thanks to Dr. Bob for this fascinating bit of intelligence...

John, I was just doing a little digging and found that Bill Gates personal portfolio is only invested in a handful of companies and a few are Canadian (in fact 3 out of 13 major holdings are Canadian but make up 33% of the equity component of his portfolio!). Any non-Microsoft investments are handled by an individual by the name of Michael Larson and under the umbrella of Cascade Investments LLC out of Kirkland, Washington. He has a background in managing bonds (makes sense as the majority of Gates personal investments (about 70%) are in short-term government and corporate bonds).

Not surprisingly he has a stake in Berkshire Hathaway (since he's on the board and a personal friend of Buffett). He has a 5.3% stake in CNR (second largest shareholder) and his largest equity holding at 30%! He also has just over 5% stake in Four Seasons Hotels. The third is an interesting stake in Pan American Silver (7.7% stake and the largest shareholder). Larson is a director and Bill Fleckenstein is also a director.

...just thought this was quite interesting.

June 13, 2005

John Mauldin's ... Thoughts From The Frontline

Triple Waterfalls: excerpt from Basic Points

June 13, 2005

Contrarian Chronicles By Bill Fleckenstein

Straight talk on what the Fed has wrought

June 11, 2005

Compliments of Welling@Weeden

ADHD... Time Horizons & Underperformance By James Montier

June 11, 2005

John Mauldin's ... Thoughts From The Frontline

Whither Europe and the Euro?

June 9, 2005

Compliments of Dr Bob...John, spurred on by GOOG, here's a white paper looking at subsequent returns for companies that sported high PE ratios back in the "nifty fifty" era. Conclusion? Returns were sub-par --- apart from the odd ones such as Walmart.

The Nifty-Fifty Re-Revisited

June 9, 2005

Compliments of Dr Bob...John, this may be beating the dead horse but here's more stuff which shows how close we are to the peak:

Buying into 'virtual realty' by Scott Cohn of CNBC
Investors go online to buy into hot housing markets

"Bozzo says his Florida Web surfing is pay off. Over the last four years, he has made well into six figures by buying and selling Florida real estate online, and almost all of it has been sight unseen."

"I like to spend about an hour looking at different properties," Bozzo says, adding that he visits a number of different real estate sites every day. "This is something I'm looking to do for the future of my family."

June 9, 2005

An Interview with Warren Buffett in 1974

June 6, 2005

Compliments of Dr Bob...John, here's the front cover of most recent issue of TIME:

....
to having housing bubble pop:



Classic stuff you see at any market peak (particularly for mainstream magazine that is not BUSINESS in nature). Just to give you another example, the US Trade-Weighted dollar is up 6.8% since the Newsweek cover showing the spiraling dollar appeared. Another one is the “Death of Equities” cover in January 1973 (the bottom for equity markets at that time).

Check out the sub-titles: “Will your house make you rich?” and “Super-hot

markets”.

This will end badly.....

June 5, 2005

Compliments of Dr Bob... I can't believe this was dated yesterday, it's something one would have seen in March 2000...

MarketWatch by Paul B. Farrell

Day-trading retirees? They're blowing bubbles
Irrational exuberance is back and 'I'm mad as hell'

June 5, 2005

Compliments of Dr Bob...John, Fleckenstein in his weekly, quotes a guy named Derman who was a “quant” at Goldman Sachs up to 2002. This is quite interesting because it's in line with what I was describing to you last week in my rant that Wall St. tries to employ “physical” and “concrete” models to somehow create “can't lose” investment models.

"In physics, you are really playing against God, and He sets the laws once and for all, and you are trying to figure them out, and He doesn't really change them too often. And if you figure out what the laws are, then He kind of gives up and says, 'You're right.' In finance, you are really playing against God's **creatures, people like us, who value assets based on their ephemeral feelings.** ... They overshoot, they undershoot, and they sometimes don't know when they've lost the game. They keep on trying to play, and they keep trying to change the rules on you."

Emphasis is mine.

Contrarian Chronicles

Intel keeps rising, but that doesn't make it safe

June 4, 2005

Thanks to our friend CK for this fascinating article from Chinadaily.com

Will America lose its AAA credit rating?

June 3, 2005

Compliments of the Wall Street Journal

CGM Realty, the No. 2 performer among real-estate funds over the past three years, with an average annual return of 32.03%, recently eliminated a position in home-building stocks that had been as large as 75% of portfolio assets in the second half of last year. Portfolio manager Ken Heebner explains that he sees "a very serious bubble" in the market for expensive homes, which some investors are buying without down payments and with interest-only financing.

"We are seeing dangerous speculation that is going to lead to a severe price relapse in high-end homes" and potentially hurt the home-building stocks, he says.

June 3, 2005

Can the Fed Find the Sweet Spot? by John Mauldin

June 3, 2005

NPR...

Is the red-hot housing market a bubble about to burst?

Madeleine Brand talks to Yale University economics professor Robert Shiller about the fate of the national housing market.

Shiller calls the housing market a "bubble" -- meaning prices are out of touch with economic reality -- and predicts the market will collapse.

The only question, he says, is when.

June 3, 2005

Compliments of Dr Bob... John, a good summary of some of the main issues for US economy:

Compliments of contraryinvestor.com... **Cycle Paths**

They ask the question whether we are in a standard business cycle or in a credit cycle. In my opinion, both cycles are evident (which they fail to consider). Firstly, the corporate business cycle is clearly apparent from the manufacturing and industrial recovery since the end of the "recession" of 2001. But there is a CREDIT cycle as well and that's coming from the consumer. The MAIN issue I see going forward is what will happen when the business cycle turns down. In other words, when the next recession comes will the consumer have the tools (low short-term interest rates, tax cuts and home equity to tap) to "protect" them again from the

inevitable downturn? The answer to me is a clear NO. I just can't imagine how bad it will be when the corporate side of the economy hits the next recession along with a housing and debt bubble that is in the process of popping. In my opinion, it won't be pretty.

June 2, 2005

Compliments of Dr Bob... John, I think the top is almost here.

"I don't want to sell too early," says Walsh, a real estate broker in her 50s. "But I don't want to get clobbered, either. But if I roll the dice (and win), it is an extraordinary opportunity to really make money."

Some homeowners delay sale in hopes of higher profit **By Adam Shell, USA TODAY**

Kandy Walsh owns a second home near Tucson that has appreciated \$200,000 in five months, and she's ready to sell it. But not just yet. The reason: She's betting that if she waits six or 12 months more before selling the new 2,200-square-foot home in a gated golf-course community, she can make even more money.

"I don't want to sell too early," says Walsh, a real estate broker in her 50s. "But I don't want to get clobbered, either. But if I roll the dice (and win), it is an extraordinary opportunity to really make money."

Walsh's strategy amounts to "market timing," which one normally associates with nimble stock market traders.

The risk, of course, is that if the overheated market suddenly implodes and home prices take a sharp drop, a big chunk of the "paper profits" would be wiped out.

This type of behavior is the latest sign of speculation in today's frothy housing market, says Gary Kaltbaum, a money manager and host of the nationally syndicated radio show Investor's Edge. It's a sign that a bubble mentality is forming. It's a sign many people still believe housing prices will continue to rise at a feverish pace forever.

"All these signs tell me that we are in the late stages of a housing mania that is reminiscent of the dot-com stock market bubble," Kaltbaum says. "People are paying prices that have no relation to where housing prices were in the past, in the hopes that someone will pay a higher price. And that is a definition of a frenzy."

Frenzy or not, Tom Au of Union City, N.J., plans to hold off putting out the for-sale sign on his 550-square-foot condo for at least three more months in the hopes of snaring an additional \$20,000.

"If I hold on to it a little longer, I can make more," says Au, a private investor at a

money management firm. "The value of similar residences have skyrocketed in the last six months, so it almost seems foolish to wait another three months. But three months can make a difference of 10% to 20%."

Au also has a cushion. He bought his place in 1987 and is sitting on a gain of about \$120,000. "If I lose, I am still playing with the house money," he says.

Harry Poarch, a retiree from Tulsa, sometimes second-guesses his decision to accept a verbal offer to sell his condo in Alexandria, Va., for \$340,000; he bought it for \$156,500 in 1989. He says a real estate agent told him he could probably get \$360,000. "There's a good chance I could have gotten more," says Poarch, 71.

But booking profits might turn out to be a good decision.

Katlbaum offers this advice to folks holding out for more money by postponing a real estate deal they can profit from today: "Don't be a minute too late to sell, because when the market turns, you won't be able to get out. When the tide turns, there will be no one left to buy."