

# MAEDEL'S

## EQUITY MARKET ANALYST

### All signs point down?

MARKET BULLETIN  
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Last June 11th when the Dow was at 10,155 I noted that a bottom looked to have been formed based on the record setting exodus of investors from US equities, apparent extremely negative sentiment, oversold technical readings and the record levels of cash on the sidelines and in non-financial companies treasuries. In short I wrongly anticipated a major exhaustion in sellers. The market did subsequently move higher, in total the Dow's top to bottom rally was from 9,617 to 10,535 (Friday's close 9,596). Since then the trend has turned decisively down and the former support levels taken out. In DJIA terms a fall from 9,596 to between 8,800 and 8,000 now appears likely.

In last November's issue "The Bubble That Broke The World" I built the case that a painful economic slowdown was likely to resume this summer (now) and how Europe and the US deals with the slowdown will be critical in whether we enter into a deflationary spiral or a 1970s style stagflation? To be honest, German Chancellor Angela Merkel surprised me when she agreed to a US \$1 trillion bail out plan for the PIIGS something that was illegal according to Maastricht and goes against a longstanding German fear of debt monetization. I expected that the inflation-phobic Germans would never allow this. Seeing this red line crossed so quickly increases the probability of accelerating inflation as the UK is already experiencing. We will need to watch carefully to see how the FED, Obama and the ECB now reacts to the next few years of decelerating (or negative) economic growth, accelerating debt levels and skyrocketing unemployment.



Barrick Gold's chart has formed a symmetrical triangle which in theory can break out upwards or downwards. If upwards it will also need to be accompanied by greatly expanding volume. If down, it can initially fall on little volume - as we used to say on the trading floor "stocks need volume to go up but they can fall under their own weight".

I think it is a good bet that as the economic growth decelerates, a worsening Federal deficit (and state and local government budget shortfalls) will make massive levels of QE inevitable. An approaching wave of government layoffs will add to the slow down, just as tax increases subtract a percent or more from already anemic GDP growth. Also looming is a potential reduction in consumer spending when the Bush tax cuts expire. Consumer's act in anticipation and buying something today because they will pay less in taxes is a powerful motivation. Take the tax credit meant to stimulate real estate sales which ended April 30th. The following May new sales plunged by 33%, the largest drop ever.

So if people are buying in 2010 to beat next year's higher taxes, how much will 2011's consumption be reduced? If the experience in real estate or the cash for clunkers program is any indication, this is just one more reason to expect a slow down. Unfortunately its not the only reason for a double dip and in a report to go out next week I'll go into detail.

The prospect of more quantitative easing may be why the dollar has begun to fall even though treasuries have been rocketing. One other reason for the sudden dollar weakness (and support for the Euro) is the re-establishment of currency swap agreements between the FED and the European Central Bank giving the ECB an unlimited US dollar credit line with which to support the Euro.

All these development's makes gold's future look pretty good, and when big gold miners like Barrick finally break out to new highs, the junior gold producers should then begin to take off. But until that happens my strategy is to keep a high level of cash (50%) and accumulate near-production or producing gold growth stories and emerging biotech while looking for other opportunities.

In the mean time I think it is important to note where the leadership has come from during the past rally as it, from a technical perspective, can give us good insight as to what we should be accumulating during the ongoing sell-off. Gold certainly is among the top performing sectors.

Biotech stocks have done even better. Note the Amex Biotech index below. After completing five waves in a major trend up and exceeding its 2008 previous record highs by 20%, the index is now correcting and looks set to test the old highs at 900; still above its 2008 high. I think that if this occurs it will be a great time to begin adding to our portfolio as the biotech revolution accelerates. In the meantime the Dow Jones Industrials looks ready to test between 8800 and as low as 8000. This will likely mean many small companies will see bids and liquidity vanish for the next few months - giving us an opportunity to accumulate some real bargains.

