

# OUTSIDE THE BELT-STREET - SPECIAL EDITION

JUNE 2004

Special Edition

## PARABOLIC RISES... AND WHAT COMES AFTER

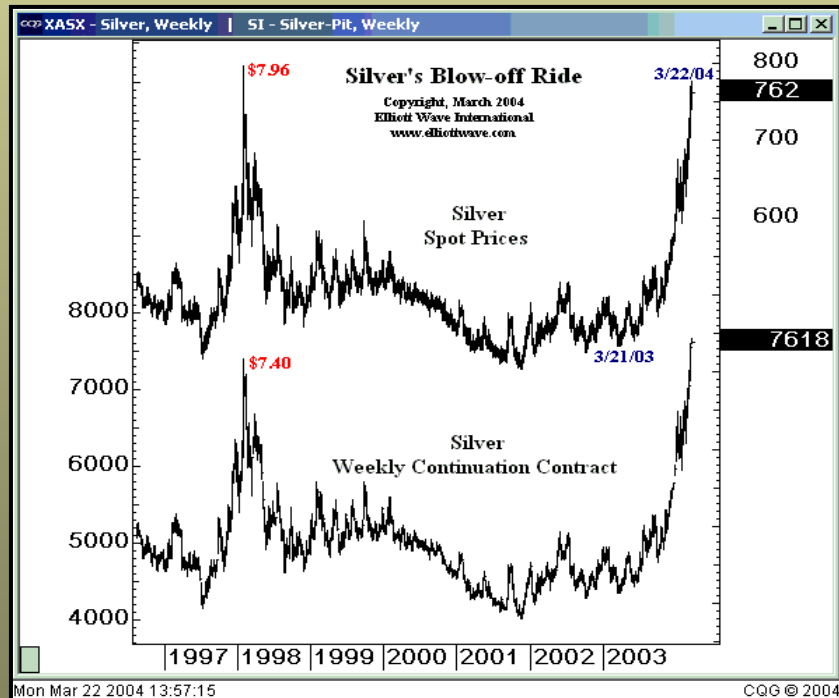


The way you see a market depends on your view.

The chart to the right is a classic illustration of a parabolic rise. It reveals the movement in the price of silver leading up to the March 2004 high (used with permission of [www.elliottwave.com](http://www.elliottwave.com)). As more and more bullishness set in, the rise became more and more speculative and vertical.

One way to get a clearer perspective on where a market could be headed is to compare it to the past and to other similar market patterns in history. One such pattern in the markets is called the Parabolic Rise.

This is where the velocity of the market or trend continues to pick up pace until the trend is almost vertical rather than horizontal. This presentation will compare various markets that have gone through a parabolic rise and what happened after the rise stopped going vertically up. Some of them, I am certain you'll recognize. We will also look at parabolic rises that have not played out yet.



As you can see from the chart on the first page the price of silver closed at \$7.62 on March 22,2004. Ultimately it topped out a few days later at \$8.31. Within 5 weeks the price had fallen to \$5.50. So it's decline was as sharp down as the climb up on the other side of the rise.

The other graph below should be even more familiar. In late 1999 and early 2000 the NASDAQ took on a parabolic rise. Because of this, even though the NASDAQ has seen a substantial rise since October 2002, it does not compensate for the sharp decline it saw especially from March 2000-April 2001. On March 1,1999 the NASDAQ Composite closed at 2,295. One year late the parabolic rise took the index to a closing price of 5,048 on March 10,2000. Because of the sharp ascent, the descent would take it to a close of 1,638 on April 2001.

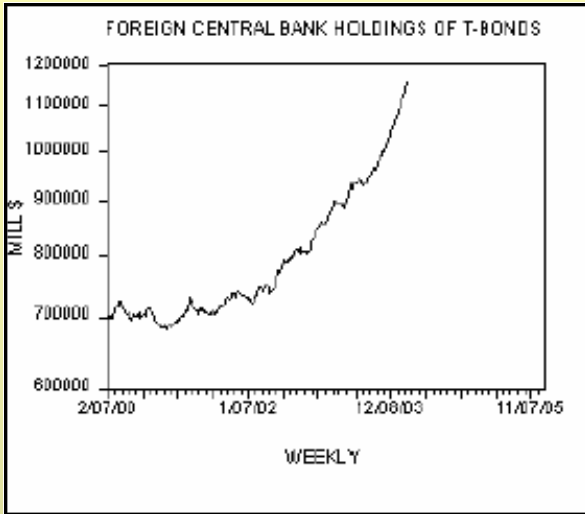


Are there any parabolic rises occurring around us today?



So from these two illustrations, is there anything we can see that should concern us about the current state of the markets? Are there any parabolic rises occurring around us today?

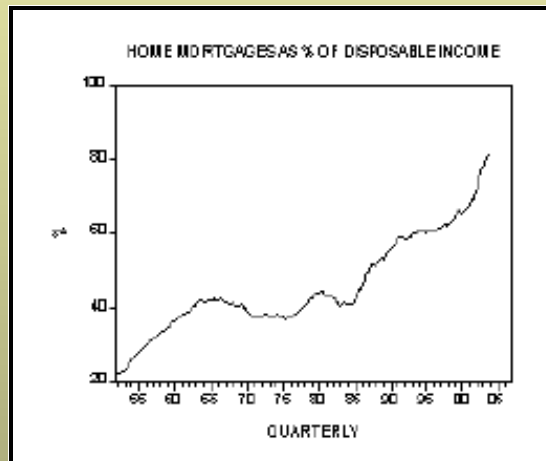
The first chart was taken with permission from Michael Hodges website, The Grandfathers Economic Report, <http://mwhodges.home.att.net> and the other three were prepared by Dr. Frank Shostak, an adjunct faculty member of the Ludwig Von Mises Institute, [www.mises.org](http://www.mises.org).



So let's just review each of these rises and see where they could be leading us. The first one would tell us that at sometime in the future the roll of an ever expanding government, daily going deeper and deeper in debt, must turn the other way. This debt increase can only be accomplished with the help of the other nations of the world. In the last quarter, the US broke history in seeing our national debt taken to a point where more of it is owned outside the US than inside. Figures from the Federal Reserve reveal that 50.6% of liquid Treasuries were held by foreign investors at the end of the first quarter. (Federal Reserve, June 17th 2004)

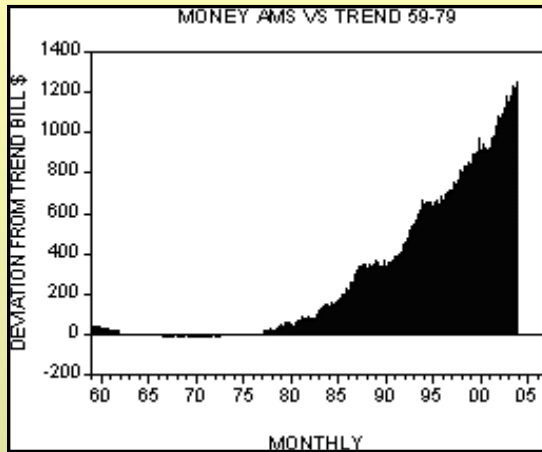
If these countries, primarily Japan and China, stop buying as many dollars to keep their currencies artificially low in order to help their exports and economic picture in the short term, what would happen to our ability to fund our massive spending?

"For the year, so far, the major stock averages have done little. But don't despair, we have asset inflation. Wait, you may not have it in your neck of the woods, but we sure have it here in San Diego, which also happens to be the least affordable market in the nation. In San Diego, the median resale price for listed San Diego County homes in May 2004 was \$448,000, an increase of 35.56 percent from a year ago. Every lousy little "shack" here in La Jolla sells for a million bucks or more. I've never in my life seen such sheer insanity in housing." *Richard Russell, age 79, www.downtheoryletters.com, June 21, 2004. (Mr. Russell began his newsletter in 1958.)*



From May 2003 to May 2004 the Market Composite Index has declined by 61% and the Refinance Index has declined by 82%.

With an economy that is driven by over 70% of our GDP coming from consumer spending, what would happen if the real estate industry were to see home lending and borrowing hit a top? On May 21<sup>st</sup> of 2003 the Mortgage Composite Index (MCI), which measures the number of mortgage loan applications for purchases and refinancing, increased to 1562.8. The Refinance Index (RI), measuring only refinance activity, was 8351.1. This was up substantially from May 29, 2002 when these numbers stood at 502.9 and 1425.8, respectively. This meant that in approximately one year's time the amount of lending in the home mortgage and refinance industry had seen increases of 210% on the composite and 485% on the refinance index. Clearly these numbers were not sustainable. For this reason, it should be of no surprise that these numbers dipped to 600.6 and 1479.4 by June 16<sup>th</sup> of this year. This is a decline of over 61% on the MCI and 82% on the RI. So why haven't home prices come down? Not all parts of an economy or market move exactly in tandem. Clearly, if the lending has fallen this much, and the prices of real estate have taken us to parabolic levels, then it should not be assumed that home prices cannot decline sharply, but only when will they decline and by how much. Consider the example above, of home prices in what I consider to be one of the most parabolic states in the country when it comes to home prices. Ironically enough this state is also home to the famous Silicon Valley.... remember.



The last parabolic rise, shown on this page, is in the money supply. But this is something that has really gone on so long, it is hard not to picture that the Federal Reserve would not just print more and more money in order to keep the economy going. They have been increasing the money supply for so long that we have just grown up believing that this is the way life is suppose to be. But what if were to get to a point where foreigners didn't want to fund our overspending and we reach a point where we begin lowering not increasing our levels of debt? What impact will that have on an economy that still today is driven by over 70% coming from consumer spending?

As I have stated in my writings since the DVD was produced in February of this year, if you are not talking about how to make money in a down market with your advisor (s), and this is NOT LOSE LESS, then you are taking very large risk due to the events affecting the various markets worldwide. If you think this sounds a bit theaterical consider the words of Jeremy Grantham of Grantham, Mayo, and Van Otterloo and Co. , a 35 year veteran to the money game. "We face the broadest overpricing of all assets yet recorded: global equities, global bonds...and with few exceptions, global real estate. By far the most important single market, US equities, is particularly overpriced."

Source-Richard Russell's remarks, June 24,2004 ([www.dowtheoryletters.com](http://www.dowtheoryletters.com))

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