



**June 25, 2009**

## **Mid-Year Issue, Part 1**

# **The REAL Winner of the Global Currency Wars**

Even though gold has been in a correction during these last few months, it is important to step back and see how it has out-performed every other currency since this decade, century, and millennium began.

I've always found it good to take the start of a year, or mid-year, as a period to reflect on the longer term trends that tend to get forgotten in the hurly-burly of day-to-day life.

When I first recommended gold and gold stocks back in the mid-February 2002 issue (<http://www.weberglobal.net/members/FebMidmonth.pdf>) the reason was the trend I saw of currencies cheapening themselves against their trading partners. You can call this competitive devaluation. This had not been seen since the Great Depression, and to me, even back then, was a signal that the world economy was heading into tough times.

It now seems like every day brings new developments in this trend. Yesterday, the Swiss Central Bank intervened massively to make its franc cheaper against the euro. Swiss trade with the euro zone accounts for a huge part of its economic activity. And though the country is still doing well on the surface, people there are bracing for harder times to come. Of course, "harder times" is relative: Switzerland is not about to turn into Zimbabwe. But they clearly see the very high Swiss franc as an obstacle to economic growth. Indeed, the currency is quite high on Purchasing Power Parity basis. This means that the same things in Switzerland cost much more than those exact same things in other places. A movie ticket for a mid-week afternoon showing of a new release costs Sfr 18 (US\$16.60), and a Burger King Double Whopper without cheese goes for Sfr 9.40 (US\$ 8.65). These same items ---and it only makes sense to compare the exact same things-- would be half in the US.

In other parts of Europe, I think the currencies are overvalued as well. In the Baltic states (Latvia, Lithuania, and Estonia), I think we'll see currency devaluations against the euro, to which all are tied. And even the euro has been rising against the Japanese yen. Yesterday, on the same day the Swiss central bank was massively selling its own currency to try to cheapen it against the euro, the European Central Bank "created" a record one-day amount of EUR 442 billion (USD 622 billion) and pumped it into the banking system. That's nearly two-thirds of a trillion dollars in one day!

That's the backdrop for this piece below. You can talk about or trade the merits of one paper currency against the other, but they've all been falling against gold. Put another way, every person on earth over the past decade, regardless of where they live, would have made hundreds of percent in terms of their own currency had they just owned gold.

### **Every Country Wants a Cheaper Currency**

Since about 2001, whenever any currency rises too much, the local manufacturers or farmers ---or anyone who lives by exporting--- start to scream about it. Their local governments respond by doing all they can to lower the value of that currency, having it fall in value and thus making exports cheaper, all this in the hope that the domestic economy will become better.

Pick any period so far this young century and you'll see how this is true. For instance, right now you see it in those countries whose currencies have soared the most in the last few months.

Let's focus on the recent highest flying currencies. The New Zealand dollar has soared 23.6% against the USD from mid-March through mid-June. That's the best three month performance for the Kiwi dollar since way back in 1971, when currencies began floating against each other.

And over 2009 as a whole so far, the strongest currency has been the South African rand, which has soared 18.3% against the dollar since January 1, the best performer of all the 16 major currencies. Other currencies that have been strong have been the Norwegian krone and the Canadian dollar (both up 13% since 2009 began) and the Australian dollar (up 14.6%).

It should be no surprise that all these countries have been making noises and taking action to try to reverse that trend. Take New Zealand. This is a country that depends on exports, especially agricultural exports. Total export prices have plunged 8.2% from 2008s last quarter to 2009s first quarter. This is not an annualized rate, either, but a quarter to quarter drop. If continued at that rate, it would mean a 33% fall in export income over the year. According to Fonterra, the world's largest dairy exporter, New Zealand farmers have suffered a 12% drop in milk prices over the last few weeks. The dairy industry accounts for 20% of New Zealand's export earnings.

As the New Zealand Herald in an article on June 16 put it:  
*"That (the plunge in income for NZ dairy producers) explains why Reserve Bank Governor Allan Bollard (New Zealand's version of the Fed's Ben Bernanke) last week called the exchange rate rise against the US dollar 'unhelpful' and a 'real risk to us' as the country endures the deepest recession in three decades."*

The same article goes on to quote the head of the New Zealand Manufacturers and Exporters Association, John Walley: *"We don't see any green shoots in our markets both at home and abroad. And the high exchange rate is strangling any 'shoots' that are poking their heads up."*

The New Zealand monetary authorities are doing all they can do to cheapen their dollar. That includes slashing interest rates to just 2.5%, which is a shock to those of us who remember Kiwi interest rates as being the highest in the world. They are printing money and talking about actively intervening in the currency markets to sell their dollar short. New Zealand's Finance Minister, Bill English, just came right out and said that his government would prefer a weaker currency.

I could go on and on. The Australian Treasury Secretary, Ken Henry, just announced in language as radical as finance ministers usually get: "If today's high exchange rates continue, that would imply downside risk to the economy." However, I don't sense as grave concern at the rise of the Aussie dollar that I do with the people of New Zealand about their currency. It thus would not surprise me to see the Kiwi fall vs the Aussie, or, put another way, the Aussie falling less than the Kiwi.

Going to Canada, their central bank just announced that the "unprecedentedly rapid rise" of the Canadian dollar may "fully offset" any hope for economic recovery.

South Africa's central bank has just announced that they have a policy of buying US dollars in order to cheapen their Rand. Their version of Bernanke, Tito Mboweni, said that although he used to be against intervention in the currency markets, the soaring South African rand has caused him to change his mind.

You can see why. Exports and domestic retail sales are plunging due to the high Rand. The unemployment rate is now 23.5%, the highest of all 61 countries tracked by Bloomberg. Interest rates have been slashed this year from 7.5% to the current 4.5%, but this is not enough for the Union of Metalworkers, which has threatened to strike if interest rates are not cut more.

Finally, Norway. Here is a European country, yet it does not use the euro, keeping its own currency. This currency has risen by 13% so far this year against both the euro and the USD. So are they happy about it in Oslo? Not very.

The strong currency has hit demand for Norway's exports hard. In response to this, companies have cut staff, which in turn cuts domestic demand. Also, big companies laying off people is a very un-Norwegian thing to do. The world's second largest newsprint maker, Skogindustrier ASA has just announced job cutbacks. This has been something of a shock, even though the decline of news papers should have been a warning. News papers just don't want to pay higher prices for newsprint when the currency these products are denominated in has risen so much this year.

Prime Minister Stoltenberg, up for re-election this September, has said that supporting the labor market through this crisis ---Norway's first recession in over 20 years (that one when the oil price plunged back in the 80s)— is his very top priority. He has pledged whatever money it takes to try to stimulate spending. And though no one has said publicly as far as I know that they want a lower krone, the central bank has cut interest

rates fully seven times in the last eight months. It is now down to 1.25% and stands ready to go lower.

And remember, this is just a snapshot of those currencies that find themselves the strongest risers so far this year. At any given time in the last few years, whichever currencies that have been strongest have screamed about it. A year ago, with a euro at \$1.60, Germany --a huge exporting company--- basically said they wanted a cheaper euro. They got it: it fell to \$1.23 within months, but is now drifting back up. The UK wanted its high flying pound, then \$2.10, to fall to boost domestic and foreign demand for its goods. It got its wish: within months the pound had plunged to \$1.45. And on it has gone for a few years now.

A few years ago Americans were angry that the Chinese had such a cheap currency and forced it to float. In the four years since that happened the Yuan has risen about 24% vs the USD, and you don't hear so many American threats. (Of course, this could also be because China owns so much US debt and America does not want to antagonize its largest lender.)

### **But What Do These High Currencies Decline Against?**

As all the countries with unwanted strong currencies move to cheapen them by printing more money, slashing interest rates, or just "talking" it down, the question remains, just what are those high currencies declining against?

If you answer, "against the currencies of their main trading partners", well, yes, this is true. But it is only temporary. If they are successful in this, then those other currencies, the trading partners, don't want their own currencies to go too high, so at some point they try to cheapen their own currencies.

It has become an endless round-robin game, except to call it a "game" is a little perverse. All holders of currencies suffer in the decline of the purchasing power of their money. You go lower, but then your partners go even lower, and then you have to cheapen your money yet more...it's an endless cycle that really doesn't help the world economy in the long run.

But there has been one money that has benefited from all this huge trend. Moreover, it has benefited by giving profits of hundreds of percent --minimum-- to anyone on earth who has owned it since 2000. It is the oldest money of all, a money that has been used long before any of the other currencies were even dreamed about and will be used long after all of them are memories in history books. It is a money that cannot be printed at will and artificially cheapened. And even though all central banks own it, it is the creature of none of them.

I'm speaking, in case you haven't guessed, about gold. Sure, you can play the currency market. I've done it for over 35 years now, and have done nicely. You can buy a currency that is way too cheap and wait, getting paid nice interest while you wait. At

least you could have done that until recently. Now no matter what currency you hold you get paid nearly zero.

More important, if you sell one currency and buy another, you are not assured of huge, 100% gains like you were until last year. I bought the euro in 2001 when it was 83 US cents, and sold it last year just about the time it rose to \$1.60. So with the interest during those 7 years, it was a nice double. I bought the New Zealand dollar back in early 2002 when it was 40 US cent and sporting a huge interest yield. I also made over 100% in a few years when the currency rose to nearly 80 cents and the great yields compounded.

But since last year I see no currency where the prospect of its doubling is apparent. So all the talk about currency trading is something I would ignore. Traders don't usually make money in the long run with 5-10% fluctuations.

Far better for most people to take a position in a currency that will benefit from this trend of competitive devaluations and stick with that.

And thus we get back to gold. Not too long ago, gold was money, and had been for recorded history. US dollar bills stated on them that they were good for, say, 20 dollars worth of gold. But that tie has been cut for the last several decades.

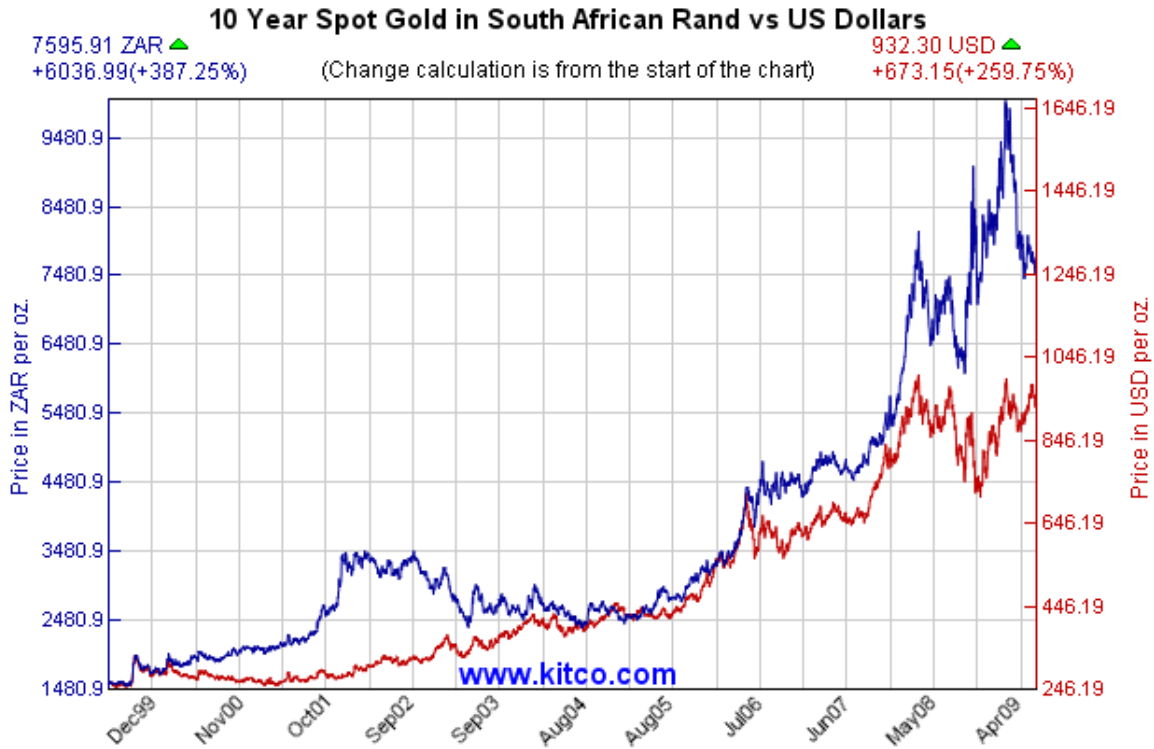
I've been an investor since 1971, when I was 16. I've never had any other job. So I've become more attuned than most to new trends on the world economy. And even while I was selling my US dollars and buying cheap euros back in 2000-2001, I started to notice this trend of competitive devaluations.

In my newsletter back in early 2002, what had been a strictly biotech letter was finally able to talk about any asset area. When I first publicly recommended gold back in the February 15, 2002 issue, gold was still just under \$300. But the reason I recommended it and gold stocks was precisely the trend I had seen of countries cheapening their currencies against their trading partners in a competitive race to the bottom.

Shall we now see what gold has done in terms of the major currencies of the world since then?

We've just been talking about the South African Rand (ZAR). It has been the strongest currency so far this year.

It is a big gold producer. Yet look at the price of an ounce of gold since 2000 in terms of the Rand.



On this and the other charts below, courtesy of kitco.com, always look at the right side of the chart. This will show the particular currency. The blue line tracks the currency. The other currency, the red line, with the left side index, is always gold in terms of the US dollar.

### Up 381% for South Africans

You see that back in 2000, when this competitive devaluation trend began, it took only about 1,500 ZAR to buy one ounce of gold. Late last year, you needed about ZAR 10,000. Now since then the rand has strengthened, and indeed has been the strongest of all major currencies this year. You can see this by the last fall down on the chart. Today it takes less ZAR to buy that same gold ounce than it did back late last year. Currently it takes only about ZAR 7,500. But still, looking over the last ten years, the rand has certainly cheapened in terms of gold, or to turn it around, gold has soared by hundreds of percent in terms of the rand. To be exact, at this writing gold has risen no less than 380.9% against the rand and this even though the rand has strengthened in the last few months.

But with all the screaming going on in South Africa about their recently "strong" currency, look for the value of the ZAR to drop, not just in terms of other paper currencies, but in terms of gold. That blue line should be going north again, after the short, sharp rally in the last few months.

## Up Nearly 200% for Australians

No let's go to another currency which has risen sharply this year, the Australian dollar (AUD). Again, look at the right hand side index, and follow the blue line.



Another major gold producer, whose currency you would think would hold its value against gold better, the 10 year chart of the AUD shows another story.

Ten years ago it took only AUD\$375 to buy one gold ounce. A few weeks ago, that same ounce would have had to take about AUD\$1,550. In the last few months, with the Aussie dollar stronger against nearly all other currencies as well as gold, it takes less of the Aussie to buy these. Right now it "only" takes AUD\$1,178 to buy an ounce of gold. But even so, with the recent "strong" Aussie, gold has risen 195% in terms of the Aussie dollar during the last decade.

## Up 300% for Brazilians

You see the pattern. The Brazilian Real (BRL) has also been a success story recently, and people have started to buy it. Yet in terms of gold its value has pretty much consistently plunged over the last decade. Gold has soared over 300% in terms of the BRL:



**Up "Only" 178% for Canadians, But 260% for Americans**

Now the next chart is very interesting. It is the chart of gold both in terms of the Canadian dollar and the US dollar over the past decade. You see that the Canadian dollar has held its value in gold much better than the US dollar has:



While gold has risen "only" 178% in terms of the Canadian dollar since 1999, it has risen fully 260.5% against the US dollar. No wonder there have been calls for the end of the USD as the reserve currency of the world. It just hasn't shown long term strength. Sadly, there is no paper currency ready to take its place. Any change in the USD's status is probably decades away.

### Up 200% for the Chinese

The Chinese currency (CNY), for example, is not yet even internationally traded. Until July of 2005, it was tied to the US dollar, so the chart below has both CNY and USD being the same line until then. But since then the CNY has risen about 24% against the USD, so it doesn't take as much more of that currency to buy a gold ounce compared to the USD.

That's another way of saying that the Chinese currency has held its value in gold better than the USD. If this continues and the Chinese economy keeps growing, it may be only a matter of time before the CNY becomes a major and perhaps the major world paper currency. It is already the world's biggest gold producer, and the central bank buys 100% of the gold produced.



The chart shows this: gold has not gone up in value against the yuan as much as it has against the USD.

Still, as great as the Chinese economy has been over the past decade, as powerful as it has become, gold has still soared about 200% in terms of the yuan. But that's still not as much as the 260% it has in terms of the USD.

## Up 360% for Russians

A big gold producing country which has come up in the world is Russia. But its ruble (RUB) has collapsed in terms of gold.



A decade ago only RUB 6,000 would have bought one gold ounce. A few weeks ago it took RUB 36,000. The ruble has rallied a bit, and today it "only" takes RUB 29,186 to buy that same gold. So the gold has done better in terms of the ruble over the decade than it has against the US dollar. Gold has soared 358.5% in rubles vs being up 260.5% in USD terms.

## Up 417% for Mexicans

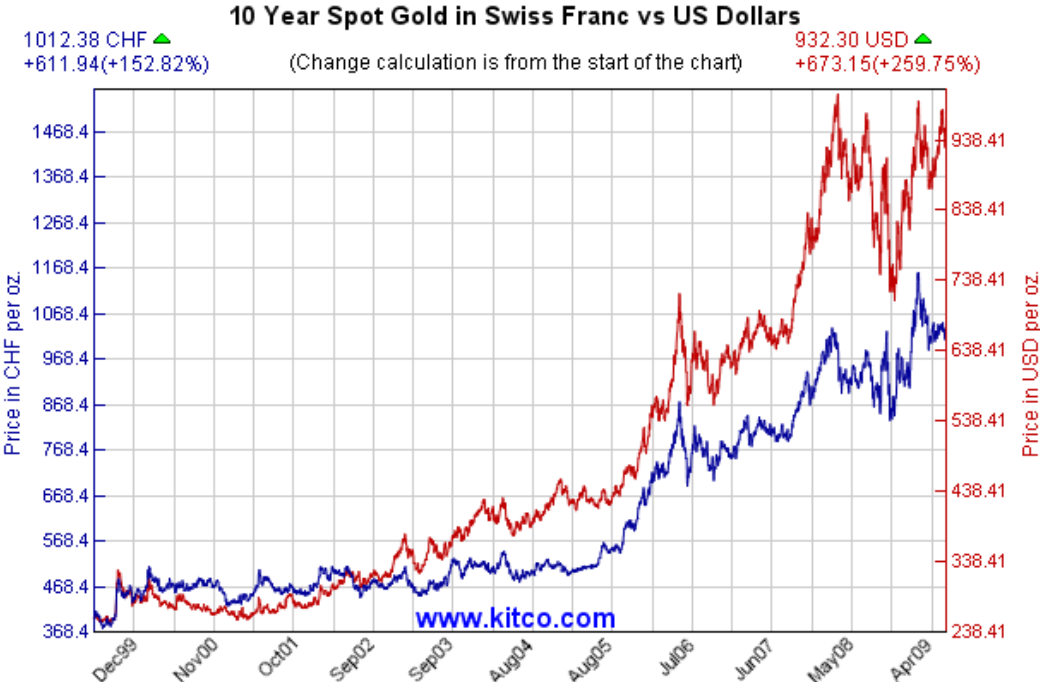
To wind down this global tour, I want to show you gold against a currency that has really lost value over the decade. This is Mexico (MXN). Until just recently, gold had soared by over 500% in terms of the Mexican peso, which paradoxically is a major gold producer and the world's biggest silver producer. The peso has also risen a bit in terms of many currencies in the last few weeks: gold now has risen "only" 417% in peso terms over the past decade.



### Up 155% for Swiss.... and Look At Gold Vs Stocks...

Finally, I want to show you gold in terms of a currency that has long been regarded as the strongest on earth, the Swiss franc. For decades, the Swissie has risen against the US dollar. When I started investing, the Swiss franc was only about 22 US cents. Now it is over 90 US cents.

But that means nothing to gold. Even the franc has plunged in value in terms of gold:



Gold has risen almost 155% against the Swiss franc. A Swiss who just turned in all his cash and stocks into gold back ten years ago would have done very well.

In fact, just to check the Swiss stock market index shows that the last decade has been even worse against gold than just the currency. But this is also true against virtually all stock market indices in the world. Just being in cash has been better than being in the global stock indices since June of 1999. Just to take the Swiss market as an example (and many have been worse), on June 19, 1999 it closed at 7,190. Ten years later exactly it was 5,330.

Think about what this means. The Swiss stock market has fallen 25.9% in Swiss currency terms over the past decade. Put another way, just holding the Swiss franc would have meant a gain of 35% against putting it in the Swiss index. And yet over that same period, gold has risen 155% against the same Swiss franc. So when you consider how much gold has risen in terms of most stocks markets, the rise in the value of gold has been staggering.

I'm just using the Swiss stock market as an example. I could do the same with all the other major stock markets, and it wouldn't be too much different. Switzerland is a rich country, but if gold has soared compared to their stocks, you know something extraordinary has been going on.

Yet I'll bet you that not one person in 10,000 sees this.

You have it within your hands now to be that one.

### **Updates on Bear-Market Rally Shares: COP Sold at 14.2% Profit**

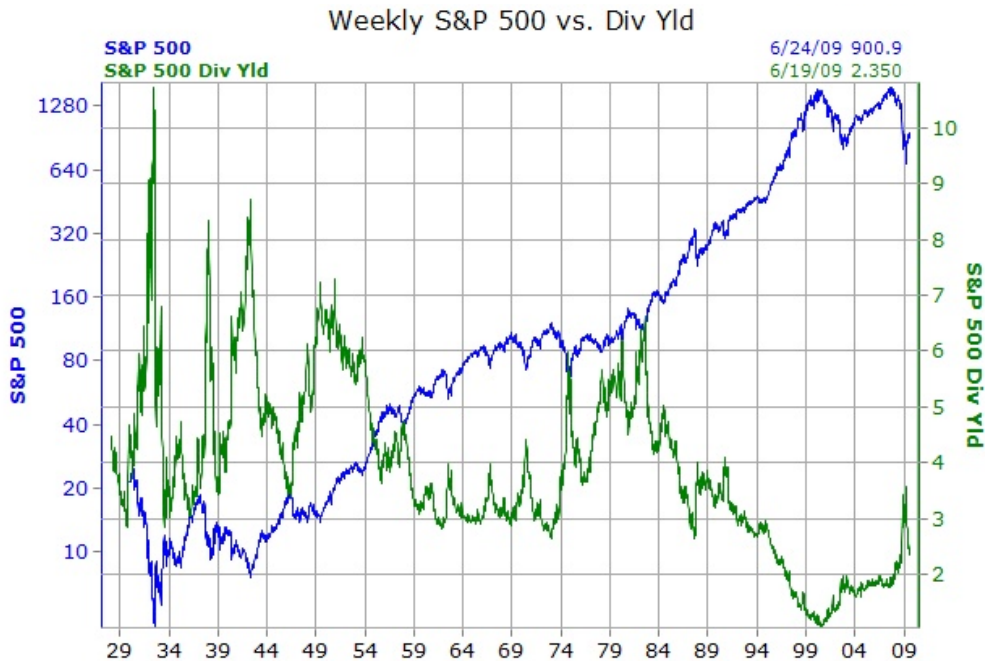
The global rallies in the stock markets that started last March look increasingly tired. However, one of our choices for rally stocks, Bio-Rad, has recently made a new high for the move. We have thus moved up our trailing stop to \$68.86, which is 11.5% below the recent new high. The recommended price was \$59.93, so we are assured of some profit here.

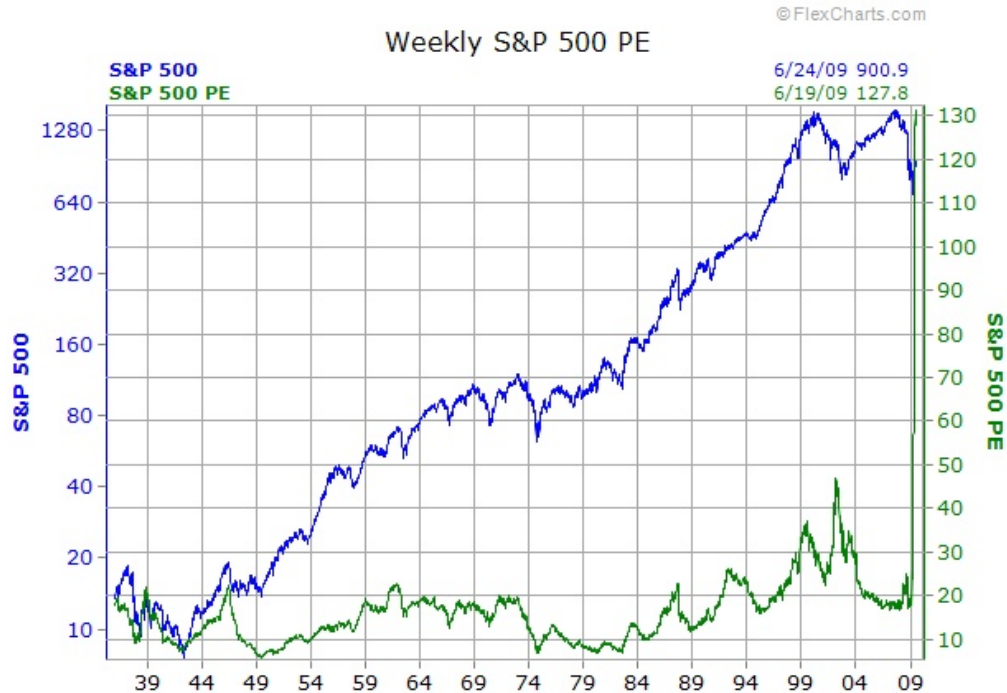
We have captured profits when Conoco-Philips (COP) fell below its trailing stop at the close of trading on June 22. Sold at the next morning at a price of \$41.10, this means a profit, including dividends, of 14.2%. This was meant to be a play on rising oil prices. While a 14% profit over three months is not a horrible return, in retrospect I should have advised just buying oil directly. Oil has done much better than the companies that produce and refine it, much as gold itself has done better than the companies which produce and refine it. I should have recommended a direct oil ETF like OIL or OLO instead of COP.

Finally, the trailing stop on DIA, the Dow Jones Industrials ETF, remains the same at \$78.15.

Again, this is just using our 11.5% TS. If you had a tighter TS, you might have already been sold out of the DIA. And who knows, this might turn out to have been a smarter move. Both the Dow Industrials and especially the Dow Transports have shown weakness recently.

No one knows how long this rally will last. It is possible that the Dow will fall back, but not break below its March 9 lows, and start to move up again. This would be bullish, but I still think bullish over only the shorter term. I still believe that we are fated to see the March lows broken at some point in the future. By any normal measure, stocks are still too highly priced to be great values. The dividend yield on the S&P 500 is now 2.35%, and that is down steeply from the 3.6% yield when this rally began in March. Moreover, the P/E ratio on that same index is now an astounding 127.5, which has soared from the roughly 35 when this rally began in March. It has never been higher-priced since records began back in the 1930s.





This is why I remain very suspicious of this rally. The best we can hope for is to claw out some trading profits, which we have so far done with EOD and COP, and should also do with BIO and DIA.

The core of everyone's portfolio should be short term cash and precious metals. The first, even though it has lost value against gold over the last decade, is to protect against deflation and a sharp correction in the precious metals prices. As for gold and silver, the argument for them is clear, and detailed in this issue.

This ends Part 1 of the mid-year issue. I will send out Part 2 on or about July 1. Part 2 will have the Portfolio Recommendations.

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