



Here Comes Inflation –Mike Swanson

Over the past few years something has gone terribly wrong with the system. People are questioning the strength of America. Government has grown in size to the tune of trillion dollar deficits. Last week President Obama engaged in a war against Libya that cost over \$100 million a day with no real tangible results or any sign that he is close to anything that can be called a victory against Gaddafi. More Americans now work for the government than work in manufacturing, farming, fishing, forestry, mining, and utilities combined.

Millions are unemployed. Wages are stagnating. Housing has yet to begin a recovery. And the government debt just grows bigger and bigger. Yet the banks are prosperous again. Corporations are posting positive earnings thanks to rising productivity - in other words they have found ways to generate more work out of their workers without paying them more. Wall Street is poised to celebrate a great first quarter for earnings. The economy is growing yet the standard of living for

the average American is not - in fact over the next year it is going to get worse.

The reality is there are people benefiting in this economy even though this is not an economy that seems to be based on real production, but on moving paper around and growing even more debts. The Federal Reserve helped to spawn a bubble in real estate and a ballooned economy revolving around massive bank leverage and debt after the 2000-2003 bear market. That edifice all collapsed and now the Fed and the government has created something akin to growth - hey it shows up in positive headline GDP numbers - through deficit spending and Fed money printing.

So far this hasn't yet cost



Quote of the month:

“The thought that you can create a economy by inflating is an illusion” Former Fed Chairman Paul Volcker

the American people anything. The debts have piled up and the money printing has been in overdrive, but you cannot say that anyone has really suffered from this, except perhaps people crazy enough to try to bet against the price of gold through short-selling.

That is about to change. And the change is coming with one simple word - inflation. For the past year the Fed money printing has helped drive money not only into US stocks, but into commodities, such as food and oil. Eventually such price increases hit those that produce consumer goods. At some point though those producers pass on their higher costs to retailers who then charge higher prices to consumers to protect their profit margins.

Within a few short months all US consumers are going to begin to get slammed by inflation, and if I'm right it is only just going to be the start of a trend that will last for several years and mean a lower standard of living for the average American.

This isn't just me saying this.

Last week the head of operations for Wal-Mart stated that US consumers will face "serious" inflation in the coming months for clothing, food, and other products. Bill Simon, the CEO of Wal-Mart told USA Today, that the inflation is "going to be serious" and we're already "seeing cost increases starting to come through at a pretty rapid rate."

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John Long, a retail strategist for Kurt Salmon, predicts that the price increases will start in June. "Every single retailer has and is paying more for the items they sell, and retailers will be passing some of these costs along. Except for fuel costs, US consumers haven't seen much in the way of inflation for almost a decade, so a broad-based increase in price will be unprecedented in recent memory."

Over the past 12 months wage income for American workers rose by 1.7%. At the same time consumer prices have risen an estimated 2.6%. Prices have already been going up faster than wages. People haven't really taken big notice of this, because this has been a slow trend over a year, but this trend is going to accelerate. In February alone the consumer price index rose by half a percent.

The Fed has kept interest rates at zero and engaged in quantitative money printing to keep the borrowing costs of companies and the banks they work for low and to make the stock market go up. But doing so has also had the side effect of making commodity prices rise too. And now that rise is going to impact everyone.



This is the cost of money printing. This is the cost of trillion dollar bank bailouts, useless wars, and government deficit spending out of control. The bill has been long due and

is now going to be paid for not by the banks and corporations that have benefited from the bailouts and government spending, but by the American people - and those that will be hurt the most and thereby will end paying the most will be the working poor and the unemployed who will have a hard time paying higher prices to buy food, buy gas, and to shop at Wal-Mart and didn't even get any benefit from the rise in the stock market.

It is that rise in the stock market that has caused most middle and upper class Americans to simply sit there and accept the bailouts and growth of government. They may have grumbled a little bit about it on a philosophical level, but as long as the stock market went up most have never cared enough to do a thing about it.

You can see this right now. If we want to make real money in the financial markets together than we have to think ahead of the curve six to twelve months down the road and anticipate what is likely to happen - and that trend now is inflation. But most people do not think ahead at all. The stock market has gone up twelve days in a row so most investors are not worrying about anything at all. All they know is that they are happy to be making money.

The move the past few weeks in the stock market has been one of the most unusual moves I've ever seen. I didn't find it surprising to see the stock market pullback in the first half of March, because it got to an extremely overbought condition with some signs of a top coming in back in February. Even in bull markets you often get pullbacks down to the 150 or 200-day moving averages at least once a year, and usually twice a year, to make for a good buy point for investors.

But what was unusual is how fast the stock market rallied back up to its February highs after it bottomed in March. I really have never seen anything like it. Typically when the market falls that much that fast it spends a few weeks stabilizing and building a base to a launch a new big rally off of. A bounce and then fall to new lows with panic is typical - and a healthy thing during a correction - and if that doesn't happen often the market will bottom and the pause for a week or two weeks and then start to go up.

But this market simply bottomed and went straight back up nonstop. I said before it happened that the odds of that happening were about zero and I still believe this, because if you go back at the US stock market you'll have a hard time finding an instance of something like that ever happening.

In fact I don't know of one. Where I have seen that type of action happen before though is in commodities when they are in a bull market and have one last correction and then go through a final blow off top rally - that move is often a big one and can last from weeks to months. For example gold had a very short lived correction in November and December of 2005 and then went straight up for about six months where it made a top for almost two full years.



What happened with gold in 2006 and when I have seen similar movements occur in other commodities is that these moves happen as the last move of a cyclical bull market cycle. You get a final sharp correction that ends and then the market goes straight back up and blasts off for a climatic top. After the other previous corrections the market would pause for some time and base build before moving higher. But in this final correction so much more money and bullish speculation comes into the market that it just turns on a dime and goes right back up - and then blasts off into what people feel is an epic move.

What is interesting too is that these moves often appear to make no technical sense and end up fooling the professionals. I was bullish on gold and made big bets on gold stocks that helped make a huge return in the hedge fund I was co-managing in 2005 (it ended the year in the top 35 out of 5,000 plus hedge funds ranked by hedgefund.net that year), but I sold out at the end of 2005 and didn't buy back in on that last correction, because it happened so fast and differently than the ones that came before it.

This time the US stock market surprised me with how quickly it turned on this correction. I talked with Ike Iossif who interviews dozens of market commentators for his marketviews.tv site, and he told me that almost everyone he talks with was expecting the market to base or fall again before it moved higher too - and these are people who use all sorts of different methodologies to analyze the market.

However, if you judge by the emails I have received from regular investors over the past six weeks almost no one has been or is bearish on the stock market - at least when it comes to individual investors. I've only seen a few people express any caution or

doubts and most of those are people I have spoken with too personally in the past and consider to be more sophisticated when it comes to managing their money - they have already made lots of money over the years and are successful.

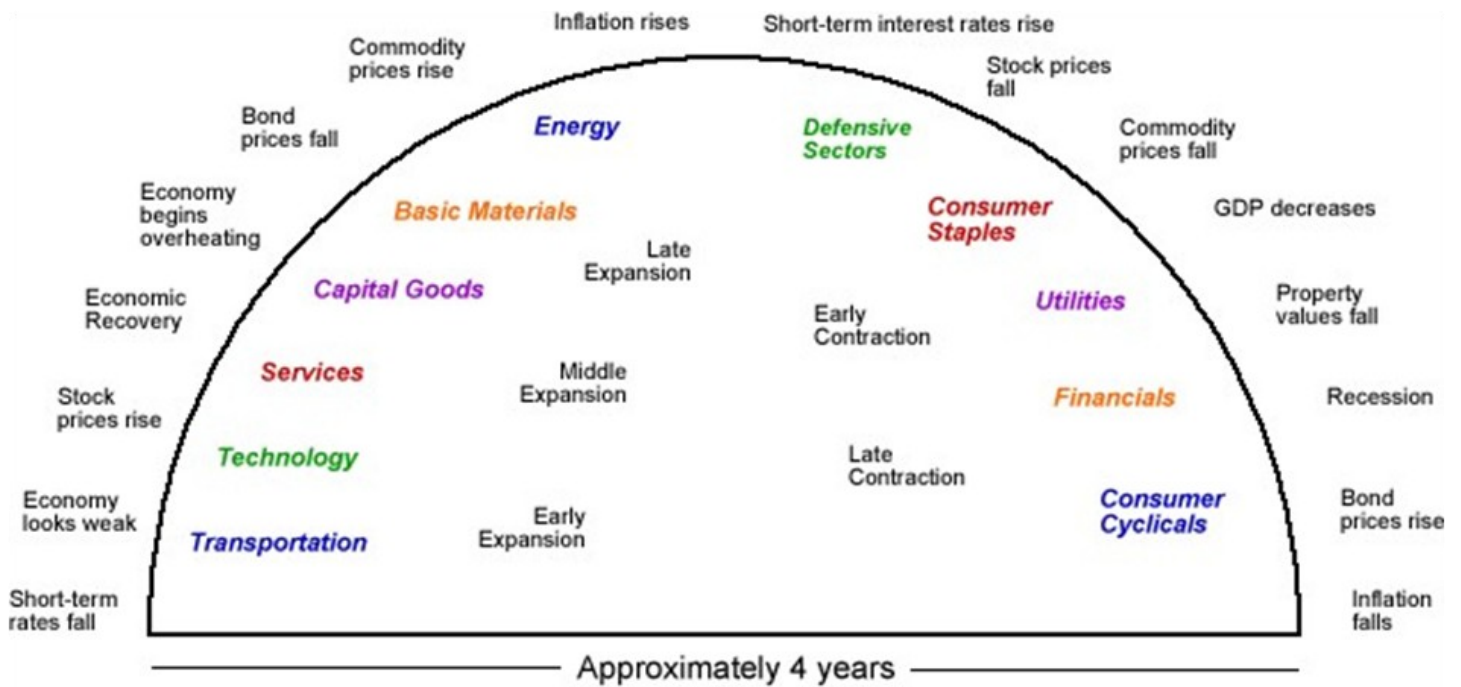
Ironically that is something that happens a lot at the tail end of a bull cycle - the experts sell out too early while the masses who really don't know as much continue to make money. The problem is in the end they never sell and eventually get crushed.

Think back to 1999 and 2000. Many famous hedge fund managers and professional investors shunned Internet stocks while newer investors, and I was one of them, flocked to them. For a period of time there were even articles critical of Warren Buffett for this. But in the end the Internet bubbleheads blew up while the slow and steady players stayed in the game and are still in it.

Now I'm not saying that the stock market is going to top out here or is about to collapse. I still think we are in a cyclical bull market, but this bull market has been going on now for two years and we should consider ourselves to be entering the final one third of it. This recent action looks to me like the type of action you see in a final blow off rally in a bull market - and that final last rally could last for weeks - or more likely months on end. It could even go on for the rest of the year.

I see coming inflation as another sign that we are in the latter stages of this bull market.

Take a look at the graphic on the next page.



Standard Business Cycle

What you are seeing here is the standard cycle of an economic business cycle with the economic activity written on the outside of the circle and the stock sectors that tend to perform the best at any given point in the cycle on the inside of the cycle.

too. After the market peaked in the fall of 2007 the energy and precious metals sectors outperformed the market for a year, with oil and energy stocks making new highs in the summer of 2008 while the rest of the stock market was already in a deep bear market.

I'll get to some specific charts in a moment, but since the beginning of this year energy and commodity related stocks have been among the top performing sectors of the stock market and right now appear to be poised to go up the most for the rest of this year.

Now this graphic only shows you the order of sector rotation and doesn't say anything about duration nor does it tell you the reason for this sector rotation pattern.

Money rotates from sector to sector in a bull market. There are times when one sector leads and others lag and money shifts from one sector to another and all of this happens in a historical pattern. What I want you to notice in this graphic is that typically in a market cycle it is the oil, energy, and inflation related sectors that do the best towards the end of a bull market.

To make a long story short towards the end of a normal economic expansion employment grows and wages rise. Inflation picks up too thanks to higher wages and also because there is more money circulating in the economy with fewer places to go. At some point the Fed decides it must fight inflation and raises interest rates, which eventually causes a top in the stock market and a slowdown in the economy.

This happened in the last bull market

Now we aren't in a normal economic cycle, because we aren't in a real economic expansion. Real estate prices haven't gone up, wages have been stag-

nating, and employment has been terrible. We're in a post collapse economy with growth driven by pure money printing and government spending. The economy is still wobbly and is really just surviving thanks to money pumping.

What this means is that the Fed is still scared of weakness and knows the country is burdened by massive debts. It knows higher interest rates could throw everything out of order again.

So if inflation does come the Fed is likely to continue to keep interest rates low for as long as it possibly can. It will pretend inflation isn't real or will continue to talk about greater risks to the economy than inflation.

Fed fund futures contracts are not projecting any rate hikes from the Fed until 2012 - and there is a good chance that the Fed won't want to raise interest in any meaningful way until AFTER the next President election, because it doesn't want interest rate increases to become part of the political debate - and let's face it in President Obama they have an obedient pet.

What is more historically the Fed has ignored inflation until it has trickled down into wage increases. From World War II till now in just about every business cycle the Fed ignored inflation until wages went up. Due to the lack of jobs in the US it will be a long time before workers will be able to pressure their employers for higher wages to offset inflation. If the Fed sticks to its historical pattern it will ignore inflation and pretend it doesn't exist up until the point that wages start to go up - then it will jack up rates and slow the economy down to push down the workers and keep them in their place. Way back in 2000 when Alan Greenspan

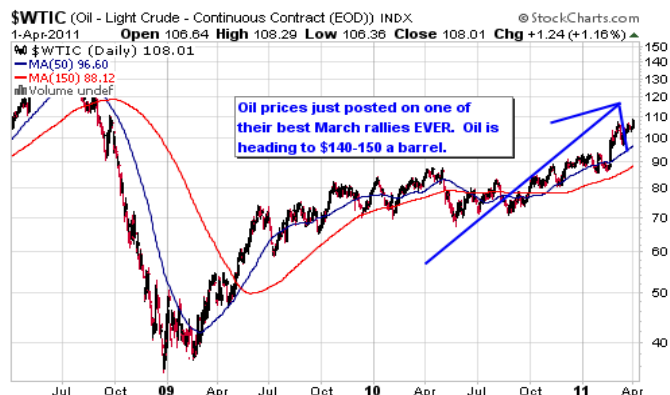
started to raise rates he actually told Congress that one of the reasons he was doing so was because people were starting to make too much money.

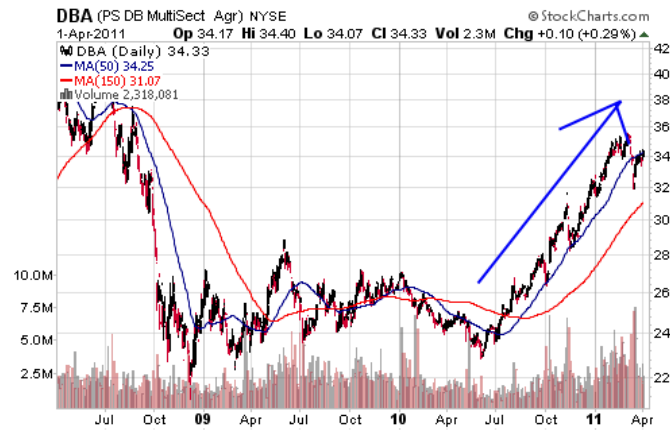
The Federal Reserve is owned by international bankers and operates on behalf of them. To the Fed everything else is secondary.

You may disagree with some of what I'm saying or be a big fan of Bernanke, but I don't think you can disagree with where I am going with this - inflation is coming and the Fed is going to ignore it for as long as possible. Most US bear markets have started AFTER the Fed has raised rates several times. The Fed probably won't start to raise rates until next year so there is no need to get overly concerned about a new bear market coming right now.

However, I still think we are in the final third or so of this bull market and as bull markets mature they change their character. I take this recent market action over the past few weeks as a sign of that. As bull markets mature you have to be more selective about what stocks and sectors you invest in - and in this case it is energy and commodity related sectors that provide the best profit potential going forward.

Historical sector rotation patterns suggest this and so do the chart patterns of these sectors.





The DBA agriculture ETF has been on a nonstop rally since July - the time that the Ben Bernanke first announced his plans for his quantitative money printing program.

In most energy bull markets oil producing stocks go up first and then money flows into alternative energy sectors as the bull move matures.

That money went into commodities and helped fuel increases in food costs across the world. These food increases helped contribute to the riots and revolts in the Middle East and are damaging the US empire.

If you remember back to 2008 the last hot speculative sector was solar stocks.

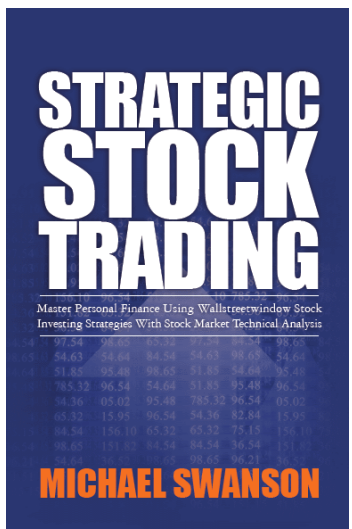
The higher food prices have not impacted Americans yet, but are soon about too.

I really like the GEX and ICLN alternative energy ETF's as buys here, because they are just breaking out of a stage one base and I expect them to be among the best performing sectors of the entire stock market over the next twelve months.

DBA broke out of a stage one base last fall and is now in a full blown bull market with no signs of stopping.

As for individual stocks Andy and Kevin have highlighted some in the following pages and I'll be talking about more of them on the website.

Energy and agriculture stocks are the places to be going forward.



Stocks to Consider— Andy Emerson and Kevin Amos

What's hot now and what's going to get even hotter? Commodities . In the following pages we're going to highlight several stocks from gold, oil, steel and others sectors that we feel are the best place to take positions.

Inflation is the next big thing and these sectors already know it. Some of the following stocks are in a stage two advances which have now consolidated for months like AUY and GG (gold stocks) and look poised to take the next leg up in the coming months. Then there are the oil and steel stocks that are coming out of stage two bases on nice volume pickup and look to add on huge gains in the coming months or years.

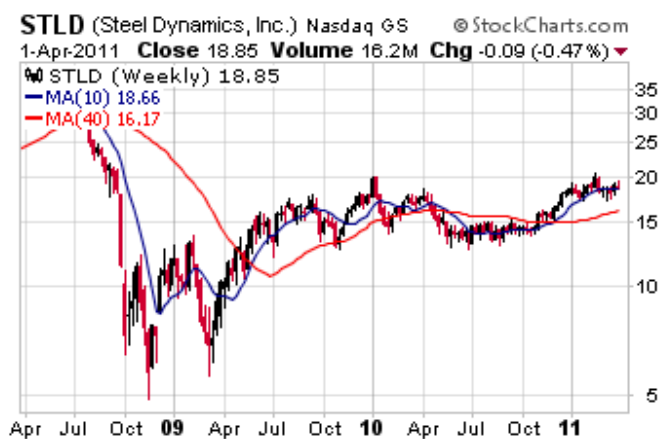
If we're going to pay up at the pump and then the grocery store we might as well take advantage of these sectors.



Buy range on SA is \$31.00 to \$32.50. Trading stop should be placed at \$29.99, investment stop at \$27.99



Buy range on GG is \$46.00 to \$48.00. Trading stop should be placed at \$45.49, with the investment stop at \$43.99



Buy range should be the breakout above February's high.



Entry point on AUY should be between \$11.50 and \$12.25. Trading stop should be placed at \$11.49, investment stop at \$10.99



Buy range on UXG is \$7.00 to \$8.00. Trading stop should be placed at \$6.74, investment stop at \$5.99



Buy range on ABX is \$49.50 to \$51.00. Trading stop should be placed at \$47.99, Investment stop placed at \$45.99



Entry point on IAG is \$20.00 TO \$21.50. Trading stop should be placed at \$19.49, investment stop should be at \$17.99



Buy point on PCX is \$22.00 TO \$24.50. Trading stop should be placed at \$21.99, investment stop at \$17.99



Buy point on SVM is \$13.00 \$14.00. Trading stop should be placed at \$11.99, investment stop at \$9.99



Buy point on CENX is \$17.00 TO \$18.00. Trading stop should be placed at \$15.99, investment stop at \$13.99



Buy point on ZINC is \$15.50 to \$16.50. Trading stop should be set at \$14.99, investment stop at \$11.99



Buy range on XTXI is \$9.50 to \$10.00. Trading stop should be at \$8.99, investment stop at \$7.99



Buy range on TGA is \$14.00 to \$14.50. Trading stop should be placed at \$13.49, investment stop at \$12.49



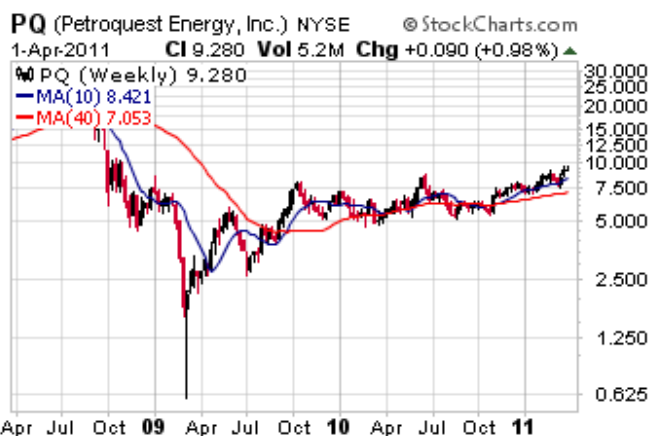
Buy point on MHR is \$7.25 to \$7.75. Trading stop should be placed at \$6.99, investment stop at \$5.99



VLO just broke out but it's still a buy placing stops under last months lows.



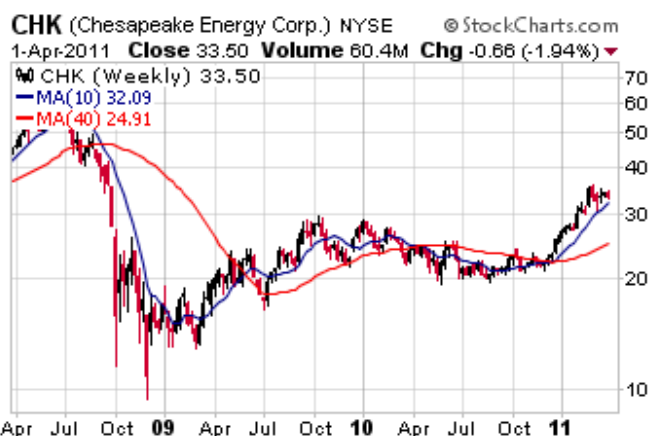
Breakout out above fifty. Good looking stock.



PQ is a buy on pull back in the 9.00 range. Already broke out but looks really good even in this position.



CPE is consolidating very nice and appears soon ready to take this years highs.



CHK looks really good and consolidating very nice after a big move up last few months. A buy here placing stops under 30.00



Breakout above last weeks highs. Nice consolidation.



Utility stocks pays good dividend buy on pull back near 14.50

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