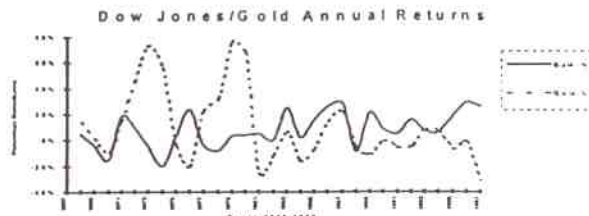


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Long Wave Student Sees Stock Market Plunge & Possible \$2,000 Gold

Ian Gordon is a broker with a major Canadian brokerage firm. Admittedly, he is not a household name – at least yet. That might change if he is reading the current stock market cycle properly. Ian is a student of the Kondratieff Cycle. To many of you, Kondratieff may be about as unknown as Ian Gordon. After all, the establishment has chosen to ignore this great Russian's work, even though a very accomplished Harvard economist, Joseph Shumpeter, said that "The Kondratieff Wave is the single most important tool in economic forecasting."

As a student of the Kondratieff cycle Ian is absolutely convinced that we have already reached the peak of the greatest bull market in stocks the world has ever seen. He is equally confident that now is not the time to allocate most of one's portfolio into stocks and bonds. Ian has graciously agreed to be interviewed by your editor so that you can benefit intellectually and hopefully financially from his wisdom. It was on Friday, June 4th that the following conversation took place with Ian from his Vancouver office.

Q - Ian, you named your newsletter the Long Wave Analyst. Why did you select that name?

A - The long wave is a synonym for the Kondratieff cycle, which is a long economic cycle of approximately 60 years discovered by Nikolai Kondratieff in the 1920's.

Q - Can you give our readers a little background on Kondratieff?

A. Kondratieff was a Soviet economist who was asked by Stalin to determine how long it would take for Capitalism to fail. Unfortunately, after he studied historical commodity prices, trade and industrial production in the capitalist countries, he discovered a long business cycle that would ebb and flow, but couldn't break. Since this was not what

Stalin wanted to hear, Kondratieff was thrown into a gulag where he perished.

Q. So I guess that Kondratieff's fate was the result of his honesty and truthfulness, since it didn't suit the Russian establishment's views and justification for its existence. Of course here in America, where we long for truth, we can count on leaders like Bill Clinton to act more honorably. In any event, could you provide our readers with an overview of the Kondratieff cycle?

Since the Kondratieff cycle is a long cycle of approximately 60 years, it is often difficult to pinpoint our exact position on the cycle. However by using PK Walls' analogy by splitting the cycle into 4 seasons of the year, we can view our position at any point in the cycle more clearly. Kondratieff

A. Yes.

Q. So you have declining prices and consumers have a field day?

A. Right. And that's a characteristic of autumn. It's a disinflationary period in the cycle. The summer period of the cycle is the inflationary period and the spring is the very benign period of inflation. Winter is characterized by DEFLATION or rapidly falling prices.

Q. If we are within 10 years from the end of the current Kondratieff cycle, what season are we in right now?

A. Well, I think based on those seasonal characteristics that I just related to you, there can be no doubt that we are fast approaching the end of our autumn season. In fact I think there is technical evidence that the U.S. stock market has already made a top.

Q. Could you tell our readers what some of that evidence is?

A. Well I'm talking purely from a technician's standpoint now. I believe that the orthodox top, if we use Elliott Wave analysis, was made in July 1998. Just as the orthodox top of the previous summer peak was made in 1928, not 1929. And the correction in October was the "A Wave" correction. The high which I believe was made in late May this year was the "B Wave high. I believe that was a high because at that point in time we have a key point reversal on both the Dow and S&P.

Q. O.K., for our non-technician readers, can you tell us what you mean by a "key point reversal"?

A. It is simply when a weekly bar makes a new high but closes below the close of the previous bar of the previous week. That is a very, very strong indication that the trend has been reversed.

Q. So your feeling is that this great bull market is over?

A. I feel that we have already come to the end of autumn and autumn is nearly always signaled by a stock market crash.

Q. So a stock market crash is what we have to look forward to here? Thanks a lot Ian!

A. Well, if we use the previous autumn – 1929 – even if we are to look at values say 1929 stock values vs. 1999, using things so simple as PE ratios, book values and so on, we see that we are excessively overvalued in 1999 compared to 1929. But using 1929 is a good example because it was the end of the previous autumn period. The Dow topped on September 3rd, about six weeks before the crash started. By the middle of November 1929, stocks had fallen by 50%.

Q. Amazing! Stocks fell by 50% in just a few months. But didn't the Dow actually fall by something closer to 90% until this stock market debacle was all over?

A. Yes! The ultimate result by June-July 1932 was a decline of 90% from its September 1929 high.

Q. Amazing! But you hear most analysts talk today about corrections. They believe bear markets have been eliminated forever. We are only going to have corrections – you know – on the order of 10%, 15%, 20% and then we will inevitably move toward new highs. Investors these days cannot fathom even a 50% decline, never mind a 90% fall in prices. And you know if you go back over the century, the only time we have had a decline anything like a 90% fall was during the 1929–1932 down period. How does the magnitude of the 1929 decline compare to these crashes that took place during the winter of the previous Kondratieff cycles?

A. The 1874 autumn decline was about a 40%. During the autumn season ending in 1819 stocks plunged 80%. So the autumn is really characterized by a significant loss in stocks values. But the one

Q. So what's going to happen then? Will there be a flight to gold because investors will have lost confidence in paper money?

A. Well, that's what happened during the 1930's. While the Dow was losing 90% of its value during the 1929 to 1932 time frame, Homestake Mining for example rose in value by 300% without any corresponding rise in the price of gold, which was fixed at \$20.67/oz.

Q. Right you are Ian! Our readers know all about that. As you know, I actually received daily stock price data from Homestake dating all the way back to 1888. From that I provided the results of a statistical study I carried out in which I allocated 15% of an hypothetical portfolio to Homestake Mining shares and 85% to the Dow Jones Industrial Average. I assumed that at the end of each year, investors would begin the year with 15% allocated to Homestake and 85% to the DJIA. What we found was that this gold exposure not only virtually eliminated the huge 90% decline suffered in the DJIA, but that the portfolio containing Homestake performed significantly better than the straight DJIA portfolio. In fact, as late as December 1998, the portfolio containing Homestake was still worth 25% more than the one without Homestake despite the fact that gold has been in a 19-year bear market. So you are definitely preaching to the choir on this issue. Actually, Roosevelt revalued gold from \$20.67/oz. to \$35 oz. Do you remember when that took place? Not that you were around at that time, but...

A. Very funny! The year was 1933. I was born about 9 years later. Investors knew they could take their paper dollars to a bank and receive an ounce of gold in exchange. Therefore, the dollar was as good as gold. A vast majority of Americans chose to take gold rather than paper because so many U.S. banks were closing their doors. So Roosevelt confiscated the private ownership of gold and at the same time he revalued gold to \$35 per ounce which is where it stood until 1971 when Nixon defaulted on this obligation.

Today, with the dollar having no backing by gold, the demand could be enormous. In fact when you look at the public purchases for gold now, it is already up 1,400 times since 1996.

Q. So that's the off-take of gold coins in North America, right?

A. Right. And in the first quarter of 1999, North American demand for gold coins rose 141% to 32 tons! So Americans, and to a lesser extent Canadians, are already starting to accumulate gold.

Q. And that coincides with the autumn or winter seasons?

A. Yes, with the onset of the winter cycle and that is why I believe the world's central banks are doing anything and everything they can to keep down the price of gold. They want people to believe that fiat paper is more valuable than gold itself.

Q. I think you might be right about that. While you are talking about this enormous demand in gold, the media and government are acting as though no one except a few radicals want or should want to invest in gold. What we do hear is that "gold has lost its luster" or that it no longer serves as an effective insurance policy against all kinds of political and economic chaos. We hear all kinds of stories about governments and central bank gold sales, most of which are spoken of but never take place. So your belief is that this is an orchestrated effort to keep people believing and hence remaining in paper money rather than gold?

A. Right. And I mean so it was – it has always been that way. Whenever governments have introduced a fiat system, governments have always tried to convince people that paper is more valuable than gold.

Q. And of course, all those paper systems have ultimately failed throughout history. Right?

A. Yes, they have.

higher than at the inflation peak of 1920, even though the U.S. was in the Great Depression!

Q. Wow! People were just scared they were not going to get their money back, even from Dow Jones blue chip companies right? So the default risk was perceived to be very high. Investors had the spit scared out of them, right?

A. Right. Bear in mind that the U.S. will have only two options open to it when the winter season begins. It can either raise rates to attract money or start the printing presses rolling to accommodate credit needs.

Q. But of course if rates rise to any substantial level it will further devastate economic activity.

A. Right. So they will almost certainly monetize the debt by printing money, just as Japan is now doing. That will spell disaster for the dollar and it will also provide an extremely bullish picture for gold.

Q. Yes, and the thing that concerns me however, is the possibility that when we have that kind of economic chaos, what the government may do is choose to make ownership of gold illegal as it has done in the past under Roosevelt. Uncle Sam may in fact make house to house searches for gold.

A. I think they may very well do that again. But that in part is why owing gold shares makes a lot of sense. For instance, if you own gold shares you own gold in the ground owned by the company. So a lot of people buy gold shares in lieu of gold.

A. Well, if everyone buys gold shares, who is going to buy the gold? I guess internationally there will be demand for gold no doubt and there will be people who buy gold underground. Some will keep the yellow metal off shore aware from the tyranny of Uncle Sam or hide it in their vaults, right?

A. Yes, and what I also believe you will see is a shift in national ownership of gold so that the Chinese for example who currently hold \$145

billion in foreign currency reserves but only 3% of that is in gold will be buyers. On two occasions that I am aware of, Chinese officials have come out publicly in favor of increasing their gold ownership to approximately the same levels as Germany and France. That would mean something like 35% to 40% or \$40 or \$50 billion worth of gold transfers to the central bank of China. And don't forget, the Japanese, who do not hold much in the way of gold as a reserve currency. So I think what you are going to see is the economic power shift from North America to Asia at the start of the next Kondratieff cycle, just as we saw the power shift from England to the U.S. at the start of the current cycle that began in 1949. There has already been some evidence of that. In 1989, the Japanese stock market was bigger than New York's and 10 of the largest banks in the world were all Japanese. And that was the same kind of evidence of the U.S. overtaking Britain as the number one economic power at the start of the current cycle.

Q. Of course, you realize that most people believe your views (and mine) are a little off the wall. What do you have to say to such critics?

A. All I am trying to do is to take a look at an economic cycle and provide an investment framework within that cycle. Bear in mind that the Kondratieff cycle holds considerable credibility for people who care to look seriously at it. No less an economic genius than Joseph Shumpeter, the famed Harvard professor, has identified the Kondratieff Wave as... "the single most important tool in economic forecasting." Shumpeter has done the definitive studies of long term economic cycles and the interrelationship of long and short cycles. Yet few people seem to care now.

Q. Why do you think it is so difficult for people to recognize these cycles? You lay it out so clearly in your newsletter and of course other people like Shumpeter have spoken about it. Why is the long cycle disregarded by so many people, when it appears to be so clearly intact today?

A. I'm not selling my newsletter. I do share it with my clients. But I welcome a challenge from anyone who seriously thinks they can refute my views. I'd love to be wrong because we are quickly approaching a very unhappy time in the cycle.

Q. Ok. So in my newsletter, I will put the challenge out to those who would suggest the old

laws of nature no longer apply to market patterns, to contact you. Would that be OK?

A. That's fine. I look forward to it.

THE END

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