

New Year's Rally for Suckers, Hold Onto Gold!

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You have to imagine the hedge fund professionals playing it cool while the Dow rallied by 2.9% on the first day of the New Year. Only they know the size of redemptions that they need to fulfill after the rush to the exit at the end of 2008.

The numbers still look awful and the Dow is way too high given the outlook for losses. But is this rally a few days or a few months? That is harder to tell. Indeed, the sensible investor has sold and is hoarding cash. Indeed, that is a problem for the Fed and its stimulus plans. Until people can see a real upside they are likely to hold onto cash and take cheap money and sit on it, ditto the banks.

If you are looking for green shoots of recovery there are few in sight. Lower commodity prices, particularly oil, and some improvement to the credit markets provides a glimmer of hope but the downturn in the global trade cycle looks awesome for 2009.

No I am afraid any rally in stock prices will prove a sucker's rally—and it will not be long before something happens to trigger the inevitable sell-off by the hedge funds for their redemptions. Once that starts, it will be quite a big down leg.

Will that also be bad for gold and silver? That was the lesson of 2008, but confidence in the dollar is beginning to wane with the size of bailouts and stimulus packages and the implications for the bond market. It would be unwise to place too much faith in the greenback, and better to at least hedge with precious metals. The rush from the dollar to gold could be very quick if history is any guide.