THE INDICATOR

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ECONOMIC INDICATOR SERVICES

Stock market
An interesting market. EIS over the last five years has consistently called the market up, suggesting a peak in the first quarter of this year. It has been interesting to see the market go slightly beyond psychologically important barriers at this time. Cycles seem to work that way.

Economic forecasting is not about trying to foretell the future; it is about understanding the past. The purpose of this is then to factor in possible future scenarios into our business planning. We are then best placed to take advantage of future events. More often than not, the future events will at least 'rhyme' or resonate with the past. There are two very distinct scenarios playing out now.

Scenario I: The US has just witnessed a rise in the Dow of over 10% in three weeks of trading. 10000 to 11000. There is now not one US economist even countenancing the possibility of a downturn in the US within the next two years. At such times, disaster planning should be considered. A bit like insurance really, which plans for an event that is generally exceedingly unlikely.

A substantial US market correction must be at least allowed for as a possibility now, (first time we have spoken of this) though it is not what EIS is forecasting. A US market collapse is exceedingly unlikely, but also possible, though the US Federal Reserve still has room to increase liquidity by lowering interest rates and / or increase the money supply at a moments notice, if world conditions really got out of hand.

Note particularly however, that the lower inflation, not what most observers were expecting, has forced fund managers to over extend their stock market buying. A very dangerous situation should inflation reverse trend.

Scenario II: Continued growth and a market bull run. This is decidedly possible. It may be noted that in Australia, if we get two more years of 3 to 4% growth, it will be the first time since records have been kept (1850's) that Australia has experienced 9 years of unbroken growth. Then we will really see commentators suggest the boom / bust cycle has been overcome.

Is it possible that the West, notably the US, has exported its recession to Asia ? With intense competition and new technology keeping wages and prices down, boom times for the US powerhouse manufacturing sector could easily continue for some time.

Our tip is for a sideways market for some months now. It is an interesting time. The attached chart (inside) annotates some of our thinking. There is no doubt the US economy is powering along, suggesting the bias on interest rates is now up in that country. There is also no doubt that should world fundamentals get even worse, the US federal Reserve is in a position where it could lower rates if it wanted to. This will put a

cont. page 2, col 2

Gold
For more than 250 years gold has underpinned the worlds financial system. (The biggest reason being that governments or ruling monarchs were found to be financially untrustworthy, and also because banks were not independent of government.)

Arguably the most conservative of all nations, Switzerland, has just voted to end the backing of its currency, the Swiss franc, by gold. This news was expected, so the gold price had already factored it in. The Swiss will now sell down their holdings by half - 1300 tonnes.

As we go to press, England will now do the same. This did surprise the gold market, but should not have caught EIS subscribers unaware. We have said for some time that gold looks set to be demonetised. If this is so, pressure on price will be extreme. EIS believes Reserve Banks may be manipulating the gold price somewhat to reduce price pressure and effect an orderly sell down of their immense holdings. (This is just an opinion and we have no proof of the claim.)

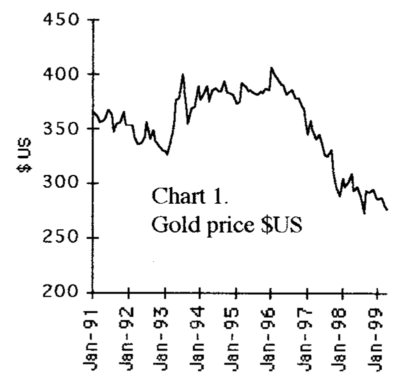
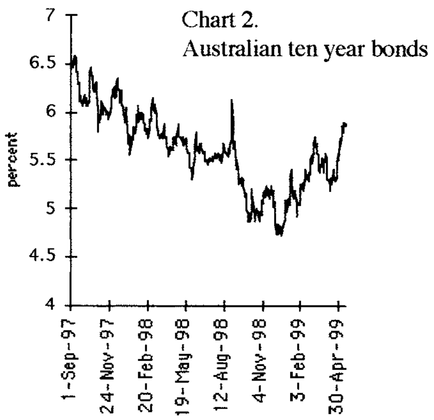


Chart 1.
Gold price $US

Propérty.
We côntinue with our forecast that the property sector will remain buoyant. But the first warning signs of overheating are present. Measured against national income, land price is getting to the stage where it is slightly out of balance and becoming uneconomic for productive activity to afford. (Chart 3.) A ratio of land sales price to national income of 25% or more has historically been the first indication of the top of the decade cycle boom. There is some way to run yet though in our view. Our economy is doing well, consumer spending remains high, bars and nightclubs are busy. There is no shortage of money around.

The combination of low inflation, lowering interest rates (with some stability now), profound structural changes under way, the move into inner city living,



new technology etc, are making this cycle much harder to forecast. It is also producing an unsustainable stock market rise.

Interest rates
Note the latest turn of events in the stock market; the inklings of a commodity share price run (or is it a bounce off way oversold conditions ?) always last in the cycle prior to an interest rate rise or three, then the peak of the stock market, and final shift into property. At least that's how its run in the past. The cyclical stocks like Boral, Hardie and CSR appear to be running now, which would be expected under this scenario. Interest rate sensitive stocks (banks etc) have had quite a setback as well this month. Is the decade cycle resuming its proper order ?

The mood of the market is suggesting improving world fundamentals. The is not what EIS would be expecting, but the mood of the market should not be ignored. The next official move in US interest rates, the rates to watch, may well be up. It is unlikely that Australia would follow this move. Note that US stock market valuations are stretched, to say the least.

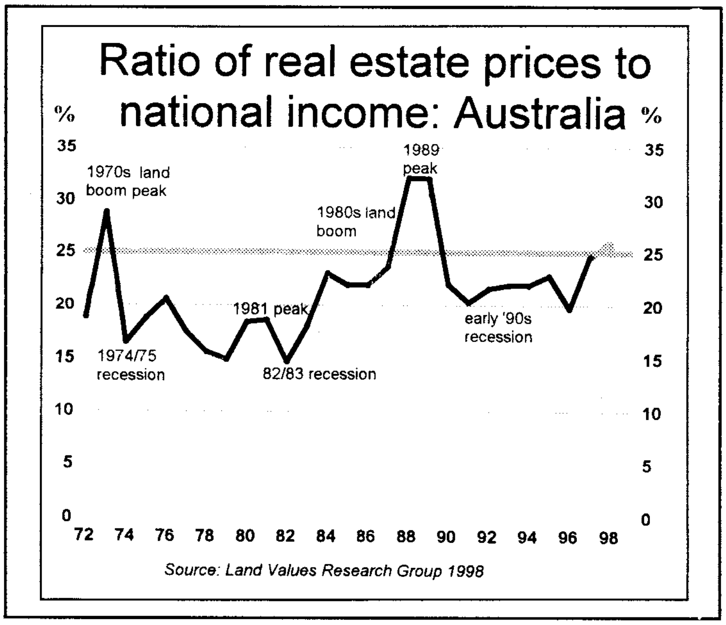
from page 1.
strong floor under the stock market. It will be interesting to see which happens first, interest rates up or down. Given the absolute uncertainty of the looming Y2K problems (does anyone really know what will happen at midnight December 31), authorities will be doing everything in their power to ensure as little uncertainty as possible in the markets. (Though substantial volatility can definitely be expected.) EIS simply cannot see a rise in rates in the last half of this year, no matter how high the US stock market goes.

Therefore;
Business planning calls for locking in surpluses, maintaining strong company balance sheets, (this is what all the best performing stocks have done this decade, so too most Western governments,) and building reserves. Make hay whilst the sun is shining, and put some of that hay safely away.

Signs of a move into top gear.
A keen study of history reveals all the classic signals of an economy in full swing;
~ rampant gambling (average per person loss in Australia is $634 yearly)
~ Warren Buffet tells shareholders he "sees nothing on the horizon to attract his $15 billion cash reserve. (And continued cashing up of Australia's best known punter you know who)
~ Highest ever debt levels (average per person debt in Australia stands at $3600.
~ mailed invitations to "wealth" seminars practically every morning
~ shades of 1989 in the local auction rooms (though more discreet at present)
~ luxury car registrations are at their highest point since 1989, so too thoroughbred horse sales.

This is likely to go on for many months yet though.

Chart 3.



Items of interest

"*U.S. Internet heavy weight America Online Inc. (AOL) has surpassed all Wall Street profit estimates for the 3rd quarter by posting a US $117 million operating profit or 11 cents per share. The recent 3rd quarter results have far outstripped the previous year 3rd quarter results of US $39 million of 4 cents per share. AOL is America's No.1 online service provider with revenue of over $1 billion on a customer base of 16.9 million members. AOL announced in November 98 that it intended to acquire Netscape Communications Corp. for $4.2 billion and recently closed the acquisition at US $10.2 billion*". Investorweb 1/5/99

Just over half of US companies within the S&P beat analysts expectations of profit. A similar story unfolded for Australian industrial companies. This puts a reasonable floor under our market for the time being. Expect to see a lot more share funded internet buyouts as surging share prices are used to great affect.

After the aborted James Hardie float in the US, the Hardie Chief Executive Dr Keith Barton had this to say " *Wall Street's fickle nature meant that any adverse economic signal - even a small rise in interest rates - spooked investors, particularly in interest rate sensitive areas such as small to medium-sized building stocks. Anything slightly negative spooks the market. After an eight year run, they're expecting its's the end of the cycle*".

Wall Street's spin-doctors are spinning faster than the share markets these days. They've got to justify their multi-million dollar salaries so they can't just say what the old hands on the trading floor are saying....that no one has the faintest idea what on earth is going on....So they're rushing along with rationalisations behind the herd as it sweeps from one direction to another." Brian Hale, The Age, 3/5/99

An observation recently made to EIS from one of our more artistic business associates:

"*Two weeks is a long time in show business. Did you notice Cameron Mackintosh (UK production group Cats, les Miserables, Phantom of the Opera, Miss Saigon etc) are pulling out of Australia. Closing an office of 23 highly skilled staff in Sydney.*

Andrew Lloyd Webber (also UK) pulled out after the Sunset Boulevard fiasco about a year and a half ago. Livent Productions (from Canada) will probably disappear after Showboat closes in Melbourne.

I guess folks ain't spending their hard earned on a big night out at the theatre anymore. We have had a great run from 1985 to 1998, but may be another example of cycles at work. Anecdotally it is said feel good musicals do best in down periods.

I guess a night out at the Casino or the races with food and booze is more the latest style. The urge to gamble must to some extent have been egged on by wins in the markets over the last few years. Further evidence of irrational exuberance and the wealth effect!

Anyway Cam Mac can see some kind of writing on the wall and is pulling back. Interesting. They closed their Hong Kong operation just before the partial meltdown there in 97."

It has been our experience that moves in art often precede a trend in economics.

Bloomberg reports 14/5/99

"*The US overseas trade shortfall is on target to top last years record of $169 billion as consumers demand has sent imports to record levels. Exports have been hurt by anaemic demand overseas*"

Note where the 'worsening deficit' stage sits on the decade cycle clock.

Commodity prices

EIS has long forecast 1999 / 2000 as the time period for commodity prices to bottom from the Kondratieff wave effect. We believe they have now troughed. The longer term price wave should now turn upwards for the next 25 years or so, should price history repeat. (A very long term, slow process.) If so, our dollar will steadily begin to reflect this fact, and a move by our dollar back to approximate parity with the US dollar, 1 to 1, over the next five years is possible.

The cycles

Historically, markets have generally witnessed four phases to the decade business cycle; a bear market in shares coming from anticipation of a looming recession. The drop has been around 20 to 30 percent, lasting around 18 months; a recovery out of recession, (a strong bull run often); a mid cycle slowdown, 3 to five years out from the recession; then a late cycle lift taking markets to new highs at the peak of the boom, 7 to 8 years after the recession low. This can be seen in the US Dept of commerce official dating of cycle peaks and troughs, page 4.

When looking at these figures, note the extended cycles due to war. We have another major conflict now in Yugoslavia, big enough to involve extensive military activity and expand the cycle further. (Are people betting on a prolonged conflict, hence the move into resources ?) War is generally bullish for stock markets (sadly).

Note on page four; the figures printed in bold italics are:

~ the wartime expansions, being the Civil war, World Wars I and II, Korean war, and Vietnam war
~ the post war contractions, and
~ the full cycles that include the wartime expansions.

(From the US Department of Commerce, Survey of Current Business, October 1994, table C51.)

US Business Cycle Expansions and Contractions

Contractions (recessions)start at the peak of a business cycle and end at the trough.

BUSINESS CYCLE REFERENCE DATES		DURATION IN MONTHS			
		Contraction	Expansion	Cycle	
Trough	Peak	(Trough From Previous Peak)	(Trough to Peak)	Trough from Previous Trough	Peak from Previous Peak
December 1854	June 1857	--	30	--	--
December 1858	October 1860	18	22	48	40
June 1861	April 1865	8	**46**	30	**54**
December 1867	June 1869	**32**	18	**78**	50
December 1870	October 1873	18	34	36	52
March 1879	March 1882	65	36	99	101
May 1885	March 1887	38	22	74	60
April 1888	July 1890	13	27	35	40
May 1891	January 1893	10	20	37	30
June 1894	December 1895	17	18	37	35
June 1897	June 1899	18	24	36	42
December 1900	September 1902	18	21	42	39
August 1904	May 1907	23	33	44	56
June 1908	January 1910	13	19	46	32
January 1912	January 1913	24	12	43	36
December 1914	August 1918	23	**44**	35	**67**
March 1919	January 1920	**7**	10	**51**	17
July 1921	May 1923	18	22	28	40
July 1924	October 1926	14	27	36	41
November 1927	August 1929	13	21	40	34
March 1933	May 1937	43	50	64	93
June 1938	February 1945	13	**80**	63	**93**
October 1945	November 1948	**8**	37	**88**	45
October 1949	July 1953	11	**45**	48	**56**
May 1954	August 1957	**10**	39	**55**	49
April 1958	April 1960	8	24	47	32
February 1961	December 1969	10	**106**	34	**116**
November 1970	November 1973	**11**	36	**117**	47
March 1975	January 1980	16	58	52	74
July 1980	July 1981	6	12	64	18
November 1982	July 1990	16	92	28	108
March 1991		8	--	100	--
Average, all cycles:					
1854-1991 (31 cycles)		18	35	53	53*
1854-1919 (16 cycles)		22	27	48	49**
1919-1945 (6 cycles)		18	35	53	53
1945-1991 (9 cycles)		11	50	61	61
Average, peacetime cycles:					
1854-1991 (26 cycles)		19	29	48	48***
1854-1919 (14 cycles)		22	24	46	47****
1919-1945 (5 cycles)		20	26	46	45
1945-1991 (7 cycles)		11	43	53	53

* 30 cycles.
** 15 cycles.
*** 25 cycles.
**** 13 cycles.

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Has the US this time really eliminated the business cycle ?

spi (SPI) Bar Daily 05/14/98 to 05/14/99
12 Month High 3165.00 12 Month Low 2360.00 Scale 1 inch = 105.58 Zoom Level 2
20 bar MA1 5 bar MA2 34 bar MA3