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OUTLOOK

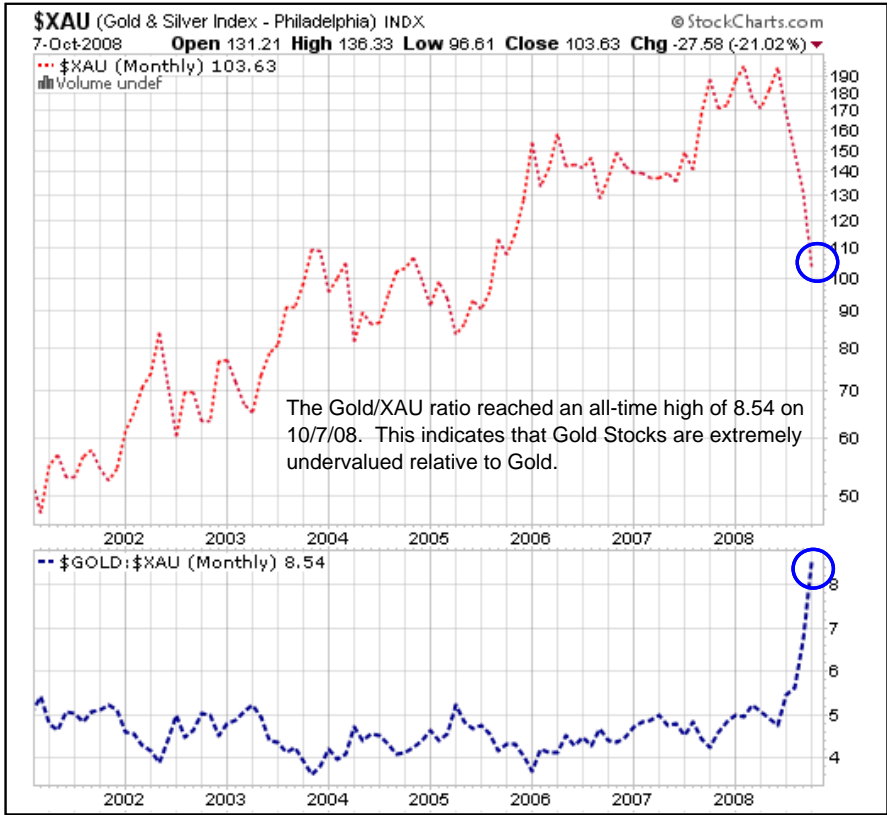
"A Screaming Buy in Gold Stocks"

10/7/2008

We are without a doubt in unprecedented times in the financial markets. We have seen quite a few corrections in our time but this one is different. Our systems for multiple markets are producing oversold readings that are off-the charts, far beyond what we have seen in the past. On first glance, it would seem to be the buying opportunity of a lifetime. But on closer observation, we must realize that these are unprecedented times with the closing of major financial institutions, freezing of credit across the globe, and a collapsing housing market. So how does one approach this type of market that appears so undervalued yet so dangerous?

First off, it pays off to have some type of edge which can improve your chances of winning on your trade. Secondly, one needs to have some form of risk management to keep losses under control in this volatile market. With this mind, we think a prudent approach to entering a position is to average into a position with a set allocation in mind. So what markets are worth entering at this time? Our choice is Gold Stocks. Never in history have Gold Stocks been so undervalued relative to Gold. If we look at the ratio of Gold/XAU, we can see that the ratio hit 8.54 on 10/7/08. This is far and above the highest reading we have ever seen which means that Gold Stocks are a "screaming buy" relative to Gold. To put this in perspective, Gold is almost \$900 as of October 2008 while the XAU is currently trading at 2005 levels when Gold was about \$400. In the near term, we expect to see some reversion to the mean with the XAU significantly outperforming Gold on the upside. Within the next 2 months, we expect to see the XAU advance to 115 or more.

Mark Yuan, CFA





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