

The Strategic Global Investors Newsletter™

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10 January 2004

No. 63

Overview

As reminder to our readers in the October newsletter I wrote: *Even during the current difficult political and business climate in Europe, the dollar will remain in the 1.16-1.18 trading range for the next 30 days. After that if the Fed and the U.S. government do not change their monetary policy, we will see deterioration in the exchange rate of the dollar to 1.20-1.25 against the Euro.*

Now here we are with the dollar exchange rates against the Euro at \$1.26 per Euro. Of course the Fed did not change its policy and the U.S. government could care less about the U.S. dollar. The government needs money, a lot of money to operate. Today billions are borrowed monthly to manage the U.S. government and the same is valid for state governments. Consumers also are borrowing at record pace. If savings continue to drop faster than investment needs and government spending grows, we will see a great contraction with deflation, massive unemployment and a free fall of the US dollar.

This crash will make the last great depression look like a Sunday picnic. Few economists predict this scenario, but I think we are getting close to moment of the truth because around the world there are too many discrepancies in developed countries and too many uncertainties in developing countries. The fall of the dollar is unsustainable. If it continues, it will rocket financial markets worldwide. If the Euro exchange rate reaches \$1.45 to \$1.50 against the dollar, interest rates in the U.S will increase at least 200 basis points (2%) in no more than 120 days. Other countries will stop buying U.S. Treasury bonds and demand a massive increase in interest rates because the country risk will increase. If you think this is unrealistic just take

a look at the massive debts, and trade deficit that the U.S. has today. In addition the trillions of dollars borrowed by U.S. consumers are creating a secondary overhang because salaries are not increasing and real estate has been purchased with horrendous borrowing. Homes today are purchased with an average of 10% down. A family living with two salaries cannot afford to lose a job, because they generally do not have any savings to cover hard times. Today for most people losing their job, means losing their home. So the glass it is half empty or half full depending on which side of the economic equation you are. As a result of upcoming economic turmoil and these debt overhangs unwinding, we believe that over the next 2 years opportunities will present themselves that will probably not be repeated for the next 10 to 20 years.

The stock market

The U.S. stock market will be bullish until the end of July 2004. After that date we will see a slowdown in stock pricing and a reverse of the market by October or November 2004. The main reason of another run up in prices is that many multinational companies have made a lot of money in Europe, Canada, and Australia, because of the falling dollar. The dollar fall will end at the end of this year one way or another. As stated earlier the European Central Bank will intervene in the market lowering interest rates and selling Euro's, when the dollar exchange rate hits \$1.30 to \$1.35 per Euro. In addition interest rates will increase in the U.S. making investment in U.S. Treasury bonds more attractive. Moreover, I think that the price of crude oil has peaked.

What to do.

I think that from now on investors should proceed with caution. It is better to stay put than run the risk of bad investments. On the currency front if in the last twelve months you did not purchase some Euro's, Canadian dollars, or Australian dollars, then you should consider diversifying into one of these currencies. We believe that there is also a unique opportunity in purchasing Hungarian Florin. We believe that the best option would be to purchase short-term bonds A-rated or better denominated in Hungarian Florin. In addition you should have invested as hedge against inflation and currency devaluation, in gold stocks. I always maintained about 5% to 7% of our portfolios in gold stocks. Do not buy just because you have cash. There are always stocks that you can buy, but you have to look harder. You have to do your homework harder to search for these stocks. And my best suggestion is that you edge your position with puts and calls. In any event depending on your portfolio it is better to very selective and wait for the opportunities that will be available at the end of this year. Many stocks now are fully priced or over-valued.

List of favored stocks

Life Sciences: ABC*, ABT*, AXCA, ARDM, ARQL, ASTM, AVE*, BEC*, BIO* BRL*, CEGE*, CHIR*, COR, DNA*, DVSA*, DSCO, GSK*, GILD*, IVX*, KG*, LLY, MYLN*, MCK*, MLNM*, NTY*, NicOX, NBIX*, NRM.TO, PRCS, PPDI*, SRA*, SCLN, SYT*, and WPI*.

REIT's: GLB, KIM, ASN, HMT, LTC, O, and VNO. Only preferred convertible shares.

Other stocks: ATG*, COP*, EGN, EWJ.

Our preferred list of mutual funds:

BGRFX, OAKGX, RYSEX, VGENX, VSEQX, VGSTX.

* Shares with options.

Indexes: DJI 10458.89 - NASDAQ 2086.92 - S&P500 1121.86 - Russell2000 575.20
Amex BTK 499.70 - 10-Year Treasury Bonds - 40.86 U.K. FTSE 100 4466.30 - U.S. dollar-Euro 1.27

HAPPY NEW YEAR TO YOU

Dario A. Bianchi

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Post Office Box 27736 • Fresno, CA 93729 - USA • Tel: (559) 431-6860 • info@sienafinancial.com
www.sienafinancial.com • www.capitalife.com

