

Intelligence report

The United States

The US trade deficit may have shown signs of stabilization, but not sufficient to assure worries of reduced interest in US assets. In March, net foreign purchases of US treasuries plummeted 86% to 3-year low of \$3.1 billion amid a broad decline in demand from both official and private accounts. In addition, foreign central banks were net sellers of US treasuries for the first time in a year at \$6.3 billion. Slowing US demand may reduce import growth and help stabilize the trade current account deficit, but that is unlikely to slow the necessary import of petroleum, especially as the share of these imports accounts for 14% of total imports, up from 6% 4 years ago. Most analyst predict an oil price over the next six months between \$65 and \$75 per barrel.

Real estate

In April 2006, the median price of an existing single-family home was 5.9 times the median family income; in 1990, it was 2.7 times the median family income. So, the run-up in real estate values relative to income to record highs is the driving force behind the sharp decline in housing affordability. Interest rates are unlikely to plunge in the near term. So, either median family incomes have to rise rapidly or housing prices have to fall rapidly to make housing more affordable again. The construction companies are getting creamed in the stock market. Normally the stock market is six to nine months ahead of the real market. In the past nine months home prices have been reduced by an average of

no more than 5%. Now watch out for a rapid decline in home prices starting in October 2006 and going forward until middle 2007. I predict a decline of between 5% and 15% from today prices. The decline will depend in the geographical area of the United States. Since you cannot have the cake and eat it too, like many investors and consumers had in the past five years, this it means that consumer spending will decline.

Europe

With few exceptions such as the U.K. Ireland, and Spain, in the past five years the European tried unsuccessfully to revive the economy. Germany supposed to be the locomotive of Europe and instead his economy was similar to other countries with high unemployment, and a stagnant economy. Now with the new government, Germany is doing a little better. Italy and France are still mired in stagnation. As I wrote many times on my previous newsletters the problem for European companies and investors is red tape. There is more money available in Europe than in the U.S. this is due to low level of consumption, and higher savings rate. All this cash will not be invested in the economy in creating jobs, unless the E.U. governments develop new and more favorable investment regulations, which will not happen in the foreseeable future.

China and India

The majority of investors are very bullish on China, and few on India. It has become an article of faith that China's economy is booming. The economy is growing rapidly. But growth and size alone don't tell you how healthy an economic entity is. The basic problem of the Chinese economy, as in many Asian nations, is that the banks have not made loans with business considerations in mind. They made loans for political reasons and to maintain social stability. As a result, they were invested in enterprises that did not make enough money to repay the loans. Frequently, rather than bankrupting the business or writing off the loan, the banks lent more money to the business -- so that it could repay old debts, and there was an appearance that the loans were viable. The Chinese financial system now is sinking under nonperforming and underperforming loans. This month the rush to oversubscribe the Bank of China IPO is a big mistake by Western investors. Many Western analysts are all writing about the problem and calling for reforms that the Chinese cannot possibly implement in time to make a difference. As in 1989, I advised investors to stay out of the Japanese market due to a build up of bad loans and a huge real estate bubble, or to short the Nikkei index, now you should stay out of the Chinese market. It could take another year or two before big problems will be difficult to control. Investors are warned.

On the other hand India is growing slowly because of political and economic reforms proceeding too slowly. Bureaucracy is still too heavy on businesses. This could be a disadvantage in the short term, but if reforms will proceed steady it will bring a booming economy without the risky course taken by authoritarian China. In addition, as a bonus in India you have a democracy, which encourage self reliance and freedom of expression. Unfortunately for western investors there are few financial analysts following small and medium-size companies in India. That it will change with time.

The Stock Market

With this economic scenario the stock market will be trading back and forth for sometime. I believe that the stocks will trade down about 10% to 12% from today levels and up a maximum of 10% within the next six months. With volatility increasing opportunities are in the options market. You should learn to use ETF's and specially the one with options. I am bullish on health care stocks of medical devices and drug delivery systems.

The Currencies Market

Please consider this: Since 1960 the money supply has risen 34.6 times, but consumer price levels have only risen 6 times. That means there is 34 times more money circulating through the system, but prices are only 6 times higher. In any other time or any other country, this imbalance would have caused hyperinflation and led to a massive default by now. Some believe such a thing can't possibly happen in the United States. The economy is too big. The dollar's status as the world's reserve currency is too secure. Long time confidence in the U.S. economy has only exacerbated the

monetary and fiscal wastefulness that has fueled the U.S.'s debt-addicted bubble economy. Here is what is happening lately. Net foreign capital flows into the US fell 34% to a 25-month low of \$46.7 billion in April from a revised \$70.4 billion in March. The \$46.7 billion in net capital flows fell short of the \$63.4 billion trade deficit for the same month. In addition, net foreign purchases of US stocks tumbled 66% to \$6.5 billion, the lowest since November 2005. To translate in few words it means the international financial community and investors start to loose faith in the mighty dollar. If OPEC countries start to trade commodities in Euros we will see a steep decline in the value of the dollar.

In reference to the Japanese Yen. Many analysts now think the Bank of Japan will increase interest rates. I believe the increase will be very modest, to a maximum of 50 basis points (0.50%) from now until end of 2006, more likely 0.25%. It might increase another 25 to 50 basis points next year. This will not change the scenario in exchange rates. Japan in the past 15 years has flooded the market with Yen causing investors borrowing in Yen and invest in another currency, and even with its trade surplus and huge dollar holdings, sill holds one the largest account deficit to GDP of the industrialized nations of this planet. I believe that the trade range for US dollar and yen will be from 110 to 115 yen per dollar in the foreseeable future. We are still borrowing JPY and invest in other currencies. This month the dollar recoup form a minimum of 1.2960 against the Euro, trading today around \$1.2630. Other currencies such as the Canadian dollar reached new high against the dollar at \$0.9115 before to correct to today around \$0.89. As in the past two years I am still bullish on the Canadian dollar which I believe it will reach parity with the US dollar. My favored currencies now are the Canadian Dollar, the Danish kronen, the Swedish kronen, the Norwegian kronen, the Swiss Franc, and the Australian dollar. Our global model portfolio is made of 40% to 45% in US dollar, 20% to 25% in Canadian dollar, 10% to 15% in Danish kronen, about 10% to 15% in Euro, and about 10% in Australian dollar. Since I consider gold the best currency of all, I also included about 7% in gold, or gold mining stocks in this portfolio.

Health Care

A word on health care. I spend long hours doing research on health care and nutraceutical companies. If you are a smart investor you want to be healthy. You need your mind sharp because investment decision can cost you dearly if you do not have all your neurons fired in the right directions and your body fit. It seems a trivial issue but is as important to investing as the home work you do before to invest. Here are some simple suggestions. Exercise moderately every day, take supplements such as vitamin b complex and omega 3, eat the right foods which means a balanced diet with a lot of veggies and brown rice. I believe that the ideal diet is different for each one of us. Moreover, I also believe that we need about 40% to 50% carbohydrates, about 20% to 30% fats (mostly vegetable fats) and about 15% to 20% protein. Invest time in reading about healthy issues and forget about all the fashionable diets that come and go from the market. Health

care is not about Viagra, or taking drugs to resolve dietary problems. It is about take responsibility of your own body. With increasing costs related to the management of chronic diseases and people getting fat and obese, we need more than ever to take care of ourselves. Financially speaking if you do not take care of yourself you can literally go broke. Prevention is the magic word in health care today.

Preferred stock list

Life Sciences: ABC*, ABT*, ANX, ARQL, ASTM, BCR*, BEC*,BDY*, BIO* BMET*, BRL*, BSX* CEGE*, CEPH*, CRL*, DGX*, FLML*, HAE*, KG*, KND*, MAXY*, MCK*, MIL*, NTY*, NicOX (Nuveau Marche' France), NUTR*, NVO, NVS* OCR*, PPDI*, RMD*, RNAI*, SHPGY* SONO* SYT*, STKL, USNA* WPI* ZMH*.

REIT: EQR*, GLB, HCP*, HCN, IGR, HMT*, HR, HRP, KIM*, PCL*, TCO*, TRC, PSA. Also preferred convertible shares in EQR, HRP, and TCO.

Gold: BVN* GFI*, GLG*, GOLD*, NEM*, FOR (listed TSE).

Energy & Others

ATG*, BHI*, CHK*, CMI*, COP*, HBC*, LFC*, MOT*, MMM*, MKC* UNFI* USU*.

Our preferred list of ETF, open and closed funds:

BGRFX, EMF, EWJ*, GLD, IGR, PBW*, PHO*, RYSEX, TAREX, VGENX, VHGX, VSEQX, XLE*, XLU*.

* Shares with options.

Indexes: DJI 11,014.55 - NASDAQ 2,129.95 - S&P500 1,251.54 - Amex BTK 650.45 - Russell2000 693.07 - 10-Year Treasury Bond 51.28 - U.K. FTSE100 5,597.40 - Nikkei 225 14,879.34 - Amex Gold 294.38
\$-Euro 1.264 - \$-Yen 115.17 - \$-CAN 89.07 - \$ - AUD 73.84 \$- BP 1.852

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