

## ENERGY AND PRECIOUS METALS HAVE MUCH FURTHER TO GO

We are approaching the end of July and beginning of August, a monthly transition time that tends to see stocks strengthen. A trading rally may ensue. However, here is an interesting observation from Jim Miekka at the *Sudbury Bull and Bear Report* (727) 866-8682. The third weeks of July, August, September, and October are high percentage losers.

Late last year when I began warning that the stock market would not be kind this year, I also warned that all the ships would initially fall with the tide. That has been the case ... but the second part of that warning is that the commodity issues will recover. The others will not. I stand with that.

Our energy stocks have not performed that well recently, even with crude oil hitting our \$81 objective earlier this month. There are a couple of reasons for that. One is that the overall market has been weighing them down, and another is that selling begets selling.

The market is in denial concerning energy, and it believes that the middle length line is the longest. The truth is, high energy prices are not temporary. They are permanent. Energy issues are good buys, but you will have to exercise patience.

A couple of our energy trusts have cut dividends, and that is due to low natural gas prices. Low gas prices,

though, are a temporary situation, and the worst is over. The summer is hot, and it takes gas and coal to run those air conditioners.

**Shiningbank (SHNUN-TSX-C\$21.05)** has a significant natural gas production - about 30% - and it just purchased **Find Energy**. This will increase both their production and their reserve life. I think it is a good deal; but with natural gas prices this low for this long, they cut the dividend by 2 cents.

We are in the investment phase of the commodity bull market, when it is still cheaper to buy your neighbor's assets than explore for new ones. I think we will see a lot more acquisition activity among raw material producers.

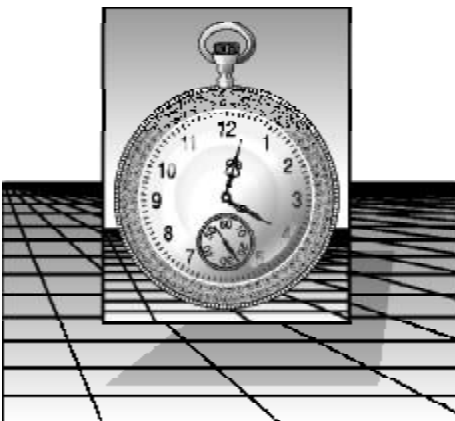
Another recent buyout is **Barrick's** bid of \$14.50 for all outstanding shares of **Nova Gold (NG-AMEX-\$16.17)**. Since the price has risen well above Barrick's offer, I suggest we hold for awhile and see what develops. Could there be another buyer out there?

Crude oil has settled back a little after hitting \$81 basis December futures. My next short term objective is \$86, but crude is taking a well-deserved rest first. There is support at \$75 December; and once we see the sellers satisfied, the next move should bring our energy trusts along for the ride.

The next issue will be published August 10.

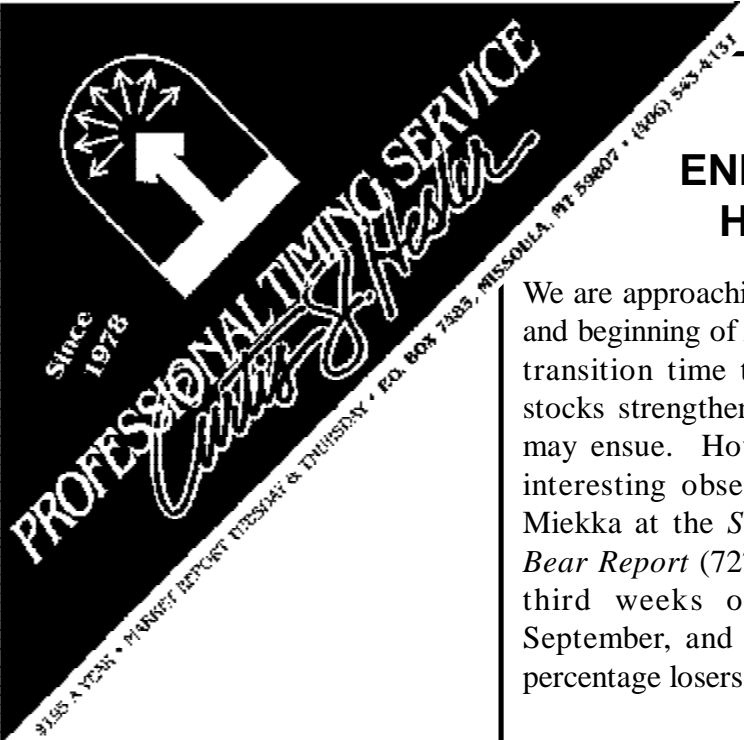
- **Headwaters and Fording are nearing important, longer term support levels, and I expect improvement in their price action.**

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Once it becomes apparent that crude prices are solidly in the \$80 range and are not going back to \$40 or \$50, the investment scene will heat up. One reason will be because this next crude rally will be accompanied by higher natural gas prices. How soon? I expect this by year's end or during the first quarter of 2007.

### **Let's talk a minute about our problems.**

Two in particular are **Headwaters (HW-NYSE-\$21.32)** and **Fording Coal (FDG-NYSE-\$26.71)**. I have positions in both of these myself; so believe me, I am not ignoring what has happened with their prices recently.

Headwaters is suffering from a fear that their construction-related business will suffer and, more importantly, that they will lose the beneficial effect of the Section 29 tax credits granted to the synfuel industry. So, we are left here with a gamble.

How bad will the building business get as the Fed seeks to control asset prices? Will Congress in their infinite wisdom decide to halt incentives to an important energy-related industry that produces liquid fuel from coal? Congressional and Federal Reserve decisions are scary to think about.

I am going to gamble a bit further that Congress will be pressured by a fit of good sense and will extend the Section 29 tax credits. I could be wrong here, but we desperately need to liquefy coal. This is a technique that was used by Germany in the war, and Headwaters holds the leading modern technology.

Other countries like China are interested in coal gasification, and we need to be also. The U.S. has a lot of

coal. Synfuels are an answer to \$100 plus crude oil, which I believe we will see by the end of 2007. Unlike electric cars, solar, etc., synfuel is an answer that can be effective very soon.

Headwaters should have support at \$20.00. I have put it on HOLD on the buy-and-hold list. We need to wait and see. Furthermore, from a technical standpoint, it is very oversold here with developing positive divergences forming in both MACD and its RSI.

The next problem child in our stable is Fording Coal. This is a bit of a puzzle. They are profitable, their earnings are rising, and they have settled some labor issues that have been hanging overhead. Their growth rate is projected by VectorVest at +26%, and they are forecast to earn \$4.22 over the next 12 months. All the fundamental stuff seems to be fine.

The biggest negative I can find is that the stock is falling. I think part of this is general market weakness and the fact that coal is out of favor presently. Some of this is negative momentum caused by its own weakness. Sellers are selling because the stock is falling. This can feed on itself.

Here is my take. I expect they should be able to pay 80 cents a quarter, which is \$3.20 a year. This is conservative in light of earnings forecast at \$4.22. This is a trust, and most of their earnings should be paid out as dividends. The price of coal will be improving in the next 18 months as well, and part of my bet is that coal gasification or liquefaction will be gaining interest in the future.

As the hot summer dwells on, coal demand will increase along with natural gas demand since they both are principal fuels used to produce

electricity. Fording should find technical support at the \$24 - \$25 level. Like Headwaters, it is very oversold.

There are no positive divergences yet, but this is not the time to sell. My advice is to go easy if you are adding to current positions. Let's see if it can hold up above its \$20.00 support level before getting overly aggressive with this one.

Headwaters and Fording are nearing important, longer term support levels, and I expect improvement in their price action. I am going to hang on to mine awhile longer, but I will continue to update the situation on the Web site hotline.

Gold and the mining stocks are pulling back, as expected. We still have a downside expectation of \$590-\$600 for gold basis December and 133.00 for the XAU. The XAU is there, but gold has a little ways to go yet.

It is natural to hear a lot of negative things about commodities when prices fall back, but this is a big bear trap. Don't get caught. Hold your positions and buy during weakness.

I have a cyclical low due for gold in early August, so I don't think we will see this reaction last too much longer. Crude oil is going to reach \$100 in the next 18 months, and gold is going to double its old 1980 high of \$873.

I am not sure how soon this all might happen in gold, but it doesn't matter. What does matter is that you do not get caught up with popular viewpoints espoused by the media. Don't buy into their argument that the middle length line is the longest. Commodities are going higher, and this is a good time to be investing in them.