

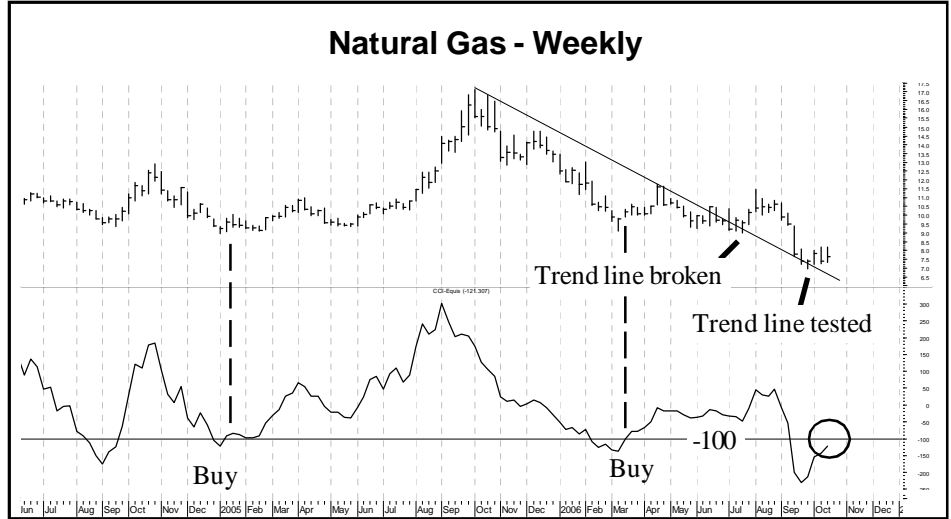
Commodities Prepare To Advance

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Chris Foster

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The next issue will be published November 2.

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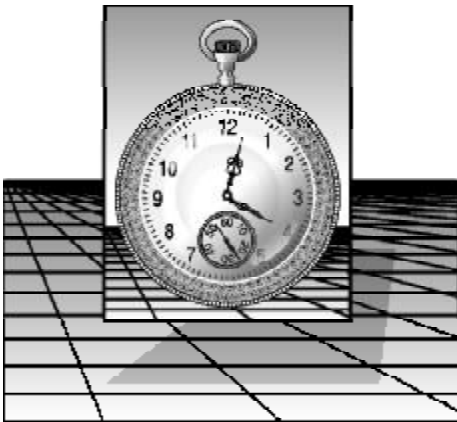
The decline in commodity prices has been the consequence of speculators making mistakes ala the Amaranth fiasco rather than supply exceeding demand. According to Morgan Stanley, global supplies are three to five years behind demand.

Markets cycle and bull markets suffer corrections. Sometimes, selling encourages more selling - as the Amaranth disaster points out - but panic always fools investors. As we begin looking toward 2007, we find ourselves sitting at the cusp of a new rally phase in the commodity bull.

Let's start with a look at natural gas. The chart shows the weekly picture along with the Commodity Channel Index, or CCI. When the CCI falls below -100 and rises back over -100, a buy signal is given. Amaranth and the panic that it caused pushed the CCI to extremely oversold readings, but we are now at the threshold of another crossing over -100.

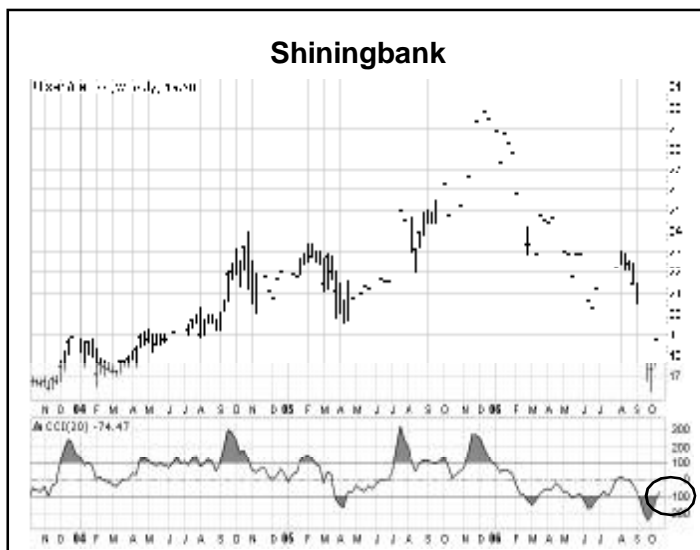
I showed you the above chart back in March when it last produced a buy signal. That signal was followed by a rally, but not the rally that we were hoping for. Some will be better than others. Due to the extremely oversold levels seen lately, weather patterns that point to an unusually cold and long winter, declines in domestic natural gas production, and saber rattling which is about to begin in Iran, the next natural gas rally may well be a doozy.

Shiningbank (SHNUN-TSX-C\$19.20) is a good shot at exploiting this. Note on Page 2 that the CCI on Shiningbank is about to break back over -100. You can follow this at stockcharts.com using the symbol SHN/UN.TO and setting the appropriate parameters. Remember, these are weekly charts and this market is volatile. Patience is an asset. I have Shiningbank on our buy-and-hold list



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with a current downside buy price of C\$17.00. There will be some overhead resistance at C\$20.00, so don't get overly excited. If you already have some and want to add to your position, the C\$17.00 price is a good place to do that. If you are looking for a new position, buy a little under C\$19.00 and see if you can't buy some more at the C\$17.00 level.

Shiningbank also produces crude oil, which makes up about 23% of their production. Although crude oil has corrected about 25% since topping out in July, its technical position is bullish now. As pointed out in the last mid-month letter, it has corrected back to support and is forming a base here. I wouldn't be surprised to see more backing and filling near term, but the next ride will be to the up side.

There is no doubt that some of the price action we have seen since last summer has been orchestrated to make voters feel as good as possible. Falling gasoline prices go a long ways in doing that. It isn't important in the eye of the public that crude prices are still significantly higher than they were at the last two elections. Linear thinking produces the vision of \$1.00 gasoline simply because prices have been falling lately. The resulting expectations, although contrived, go a long ways to getting folks re-elected. All of the powers that be with the greatest influence on our government are from the oil industry – Rice, Cheney, Bush, the House of Saud, etc. None of these people have a long term interest in low crude prices.

The military is apparently turning a new “green” leaf. The U.S. military uses about 440,000 barrels of oil per day, which is a bit more than the Prudhoe Bay produces when the pipeline is functioning. Consequently, the military is looking into renewable energy sources, and other energy-saving approaches. New types of fuel derived from both natural gas and coal are being considered. New ship designs are on the drawing board. They are investigating all sorts of ideas.

This is not because they fear they can't afford to pay for \$200 crude oil. Price is not an issue with the military. It is because they fear they might run out of fuel. Supply is the problem. Don't let current storage figures cause you to lose sight of the long haul. Our biggest problem down the road may be lines at the gas station and brownouts on the electricity grid rather than price. Energy prices are going higher. I expect to see crude back to \$70 by Valentine's Day and at new highs by the end of 2007. Of course, some geopolitical event concerning North Korea and/or the Middle East could easily push these numbers ahead.

I will have more details and some charts concerning the seasonality in gold prices for you in the November letter. Suffice to say that typically and ideally, the metals put in strong, seasonal lows during November. At this point, the \$560 low basis December looks pretty solid, but it is still early for gold to launch into its next up leg. Consequently, another last ditch stab at \$560 would not surprise me. We can't have a big gold rally hitting the news right now, can we? That could conjure up all sorts of discomfort and conversations about inflation while folks wait in line to vote.

If we get a dip here, traders can buy **Royal Gold** (RGLD-OTC-\$28.51) at \$24.95 or better. This will be a trading position, and it will carry a sell/stop at \$22.95. If the sell/stop is hit, you will simply liquidate the position and not sell short. This is a trading position, mind you - not a long term, buy-and-hold recommendation.

The stock market looks precarious to me, as it has for a couple of months. Higher prices do not make it a safer bet. We don't have anything concrete to report as to exiting our best/worst six months Rydex positions. It is too early for that. The worst six months officially terminates at the end of October; and as it is, there are no MACD setups to talk about ... yet. I will update the timing of our exchange to the best six months strategy on the hotlines, and I will have the latest for you on the status of the Annual Asset Allocation Model in the November letter.