



Financial Market Tsunami

By CK Wong 2005.11.03

<http://www.ck-wong.ca/money%20matters/financial%20tsunami%2020051103.pdf>

Introduction

US interest rate is rising. Yield curve is inverting. Avian Flu could cost U\$280B. Oil and gas price move up and down 20%+. How do small retail investors survive the financial tsunami?

Professional Market

Financial market has been very volatile. The monopole financial market disappeared. The term monopole is borrowed from quantum physics. I mean one single well defined evenly distributed and predictable environment. Rather the market is a binary system with one white dwarf and one black hole. Both could destroy you easily by sucking you in. The lines of force are complicated.

Sprott Energy Fund has enjoyed its success: more than 120% gain at its peak since its conception in April 2004. It is managed by a group of brilliant people who knows the financial as well as the energy. They are not following the market trend but successfully foresee the future. One transaction the group did in May was purchasing 12 million shares of Uranium Participation at the IPO price of C\$5 and sold 4 million shares around July. The price was not published but the market price was about C\$6.

The fund is not a hedge fund. To benefit the volatility of the market, the fund obtained the status to hedge.

They also have the foresight to invest in coal; not Fording Coal Income Fund but the other junior.

I could list their credential on and on. The point is to demonstrate how good these people are.

Just after the Gains Day (September 22), it hit the height of C\$22. Now is about \$19.50. One would ask why don't they take some of the money off the table? They may. I could not confirm that. However, these brilliant people could not avoid the volatility. They have the gut. They have the research. They have the tools. We, small retail investor, don't.

Forces of Nature

Market movement, up and down, is part of the nature of the market. For a healthy bull market to continue its journey, it needs to down or sideways to work out the gain. This is the nature of the market. When the bull market goes down, it could be the end of the bull

or just a correction. No body really able to have 100% confident to say one way or the other. This is why we need the help of the professional, the real McCoy not those salesmen. They could react fast when the direction is confirmed. We also need their knowledge to analysis whether the financial result of a certain transaction is reasonable.

In Donald Coxe's October Broadcast, he explains that hedging is not necessary a bad thing. It is a bad thing if you use this vehicle without proper mitigation. He uses Barrack Gold as an example. In the late 80 to 90, gold's future price is always higher than the spot. It is reasonable to sell it in the future to get the money for capital and buys the spot. However, the current situation does not have cheap spot gold so that hedging practice is bad.

Don comments on Encana's hedging activities. In the case of Encana what it tried to do is to lock in the future natural gas price at U\$9 mcf when it was about U\$5-6 to ensure there is sufficient funding to support the Tom Brown property purchased in 2004. No body can foresee the natural gas price could be as high as U\$15 this year.

Pengrowth Income Trust did the same thing. To guarantee the distribution, some of its natural gas production and oil production have to be sold at a future fixed price. This is common business practice. On their Q3/2005 results, it has reported distributable cash increased from \$104M 2004Q3 to \$162M 2005Q3. You can argue that may be no hedging could boost it to \$300M. Perhaps. It is risk management. It has to be done by the right people.

When these companies doing the common practice which one does it right and which one does it wrong it is hard to tell by layman like me. By reading report, you could not tell how good the management team is. I don't know these people. One could say Sarbanes Oxley will keep them honest. Unfortunately, like Terry Matthew says *if they are honest, you don't need Sarbanes Oxley. If they are crooks, they will sign anything.* I need the professional to tell me they are honest people.

We need the professional to pick the right horse.

“Insider News”

There is no such thing as insider news. The real one will never be known by anyone. Otherwise the SEC will call on you. However, all companies help investor conferences. Thanks to the equal information access legislation everyone could attend. The time, date, location and phone number are on the news. I guess if they did not bounce me, they don't bounce you too. It is illegal to deliver privileged information to a specific group of people. So you can get what they announce from the press release. However, the question and answer will be different story. There are a lot of gems. You need the profession to ask the right question to draw the right scenario. Again, you need the profession.

I give you another example. Gold Corp has been included in the S&P/TSX 60 at the end of October. This will force the index fund to buy the stock to match the index

performance. The price of Gold Corp has a ride since September. I would not say there is any leak. Good analyst would certainly be able to identify the situation and do something to anticipate the market. Again you need the professional.

Canadian Natural Resources has two decades of block buster performance. Most recently it was down from C\$60 to C\$43.55. In the last two days, it gains more than 20% and stands at C\$56.11 because it has this huge oil sand project. How could I maintain my sanity? I need profession.

I think you get the idea. But please do not confuse professional financial advisor with financial product salesmen.

Resources

[1] Donald Coxe's weekly conference call.

<http://www.bmoharrisprivatebanking.com/webcast.asp>

[2] Pengrowth Energy Trust announces Third Quarter 2005 Results, Business Wire 2005.11.03, <http://biz.yahoo.com/bw/051103/20051103006203.html?.v=2>

[3] Bird Flu "could push world into recession"

<http://thescotsman.scotsman.com/international.cfm?id=2192022005>

[4] Sarbanes Oxley Act Forum <http://www.sarbanes-oxley-forum.com/>