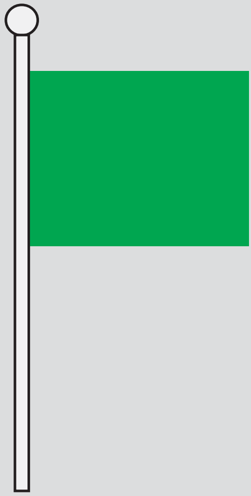
The Financial Research Center, Inc.

Money Forecast Letter



THE COMING YEAR COULD BE THE MOST IMPORTANT YEAR FOR AMERICAN MONEY AND FINANCE IN ALMOST 100 YEARS!

JANUARY, 2010

Financial Research Center, Inc.

Money Forecast Letter

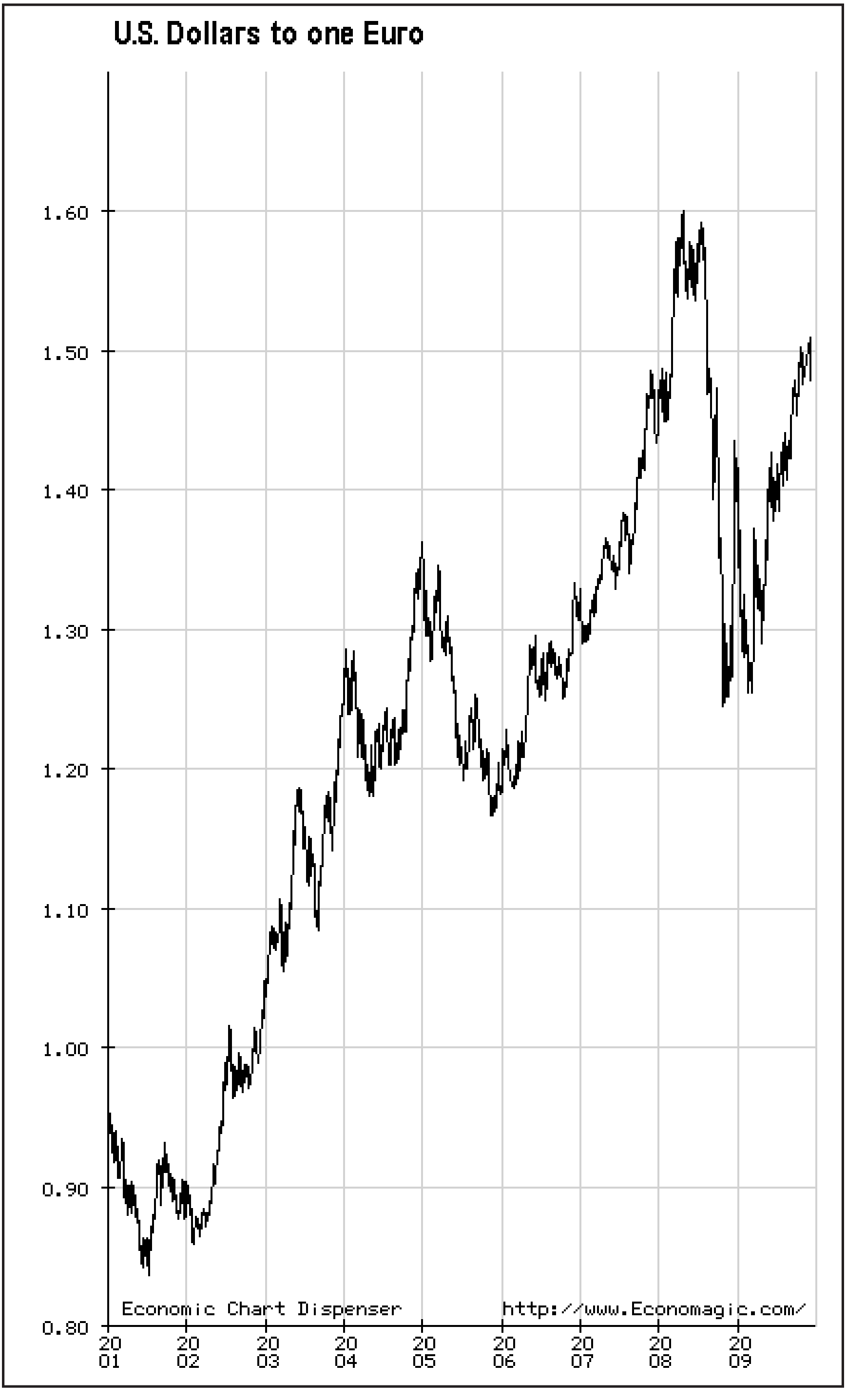
January, 2010

Holliston, Massachusetts - December 15, 2009

WHILE I URGE YOU TO ENJOY AND INVEST IN THE RETURN TO PROSPERITY HERE AT HOME, I ALSO WISH TO CAUTION YOU THAT RADICALS IN WASHINGTON, D.C. ARE WORKING ON LEGISLATION THAT COULD UNDERMINE THIS PROSPERITY. THE CHANCE THAT THEY CAN BE EVEN PARTIALLY SUCCESSFUL IN THIS EFFORT MEANS YOU NEED TO BE PAYING CLOSE ATTENTION TO WHAT THEY ARE TRYING TO DO. DEPENDING ON HOW MUCH SUCCESS THEY ENJOY IN THE COMING YEAR, 2010 COULD BE THE MOST IMPORTANT YEAR FOR AMERICAN MONEY AND FINANCE IN ALMOST 100 YEARS!

It had been my intention to dedicate this letter to discussing all the ways it was becoming clearer that the recession that had dogged this country for 18 months or so had come to an end and examine the exciting implications for your finances

The FRC Money-Forecast Letter is published monthly. Send subscription to: Financial Research Center, Inc., P.O. Box 6170, Holliston, MA 01746-6170. Phone: 1-800-542-5018. Annual subscription fee is $240 U.S.


U.S. Dollars to one Euro
1.60
1.50
1.40
1.30
1.20
1.10
1.00
0.90
0.80
Economic Chart Dispenser
http://www.Economagic.com/
20 01
20 02
20 03
20 04
20 05
20 06
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in 2010. But, before turning to this happy topic I feel it necessary to take a few minutes of your time to review what is going on in Washington these days and give you a preview of what they will be doing in the early weeks of 2010.

The Democrats who control Congress are well aware that their filibuster-proof majority is a temporary thing. They are aware that history suggests they will lose a substantial number of seats in the coming off-year election, no matter how popular the president and his policies are. Because of this they are feverishly working to rewrite the laws and regulations that impact money here in America. How it can be earned; how it is invested; how it will be taxed; how it can be saved; how it can be spent. Pending legislation would even let Congress decide whether an American company would be allowed to continue to operate if it should do something which displeases their masters in Washington, D.C. Most frightening of all, Congress is attempting to gain control of the Federal Reserve Bank, so they can have a direct say on how much money gets created. While the legislation is just now beginning to move through Congress it is clear that, if successful, it would bring the biggest changes to American banking and finance since the Federal Reserve Bank was created back in 1913.

Last month we used the letter to give you a history lesson on all the battles that have taken place over the past 220 years in an effort to create a stable banking system. We did this because it is obvious that we are about to live through another epic battle over just who controls money in this


Japanese Yen to one U.S. Dollar
135.0
130.0
125.0
120.0
115.0
110.0
105.0
100.0
95.0
90.0
85.0
Economic Chart Dispenser
http://www.Economagic.com/
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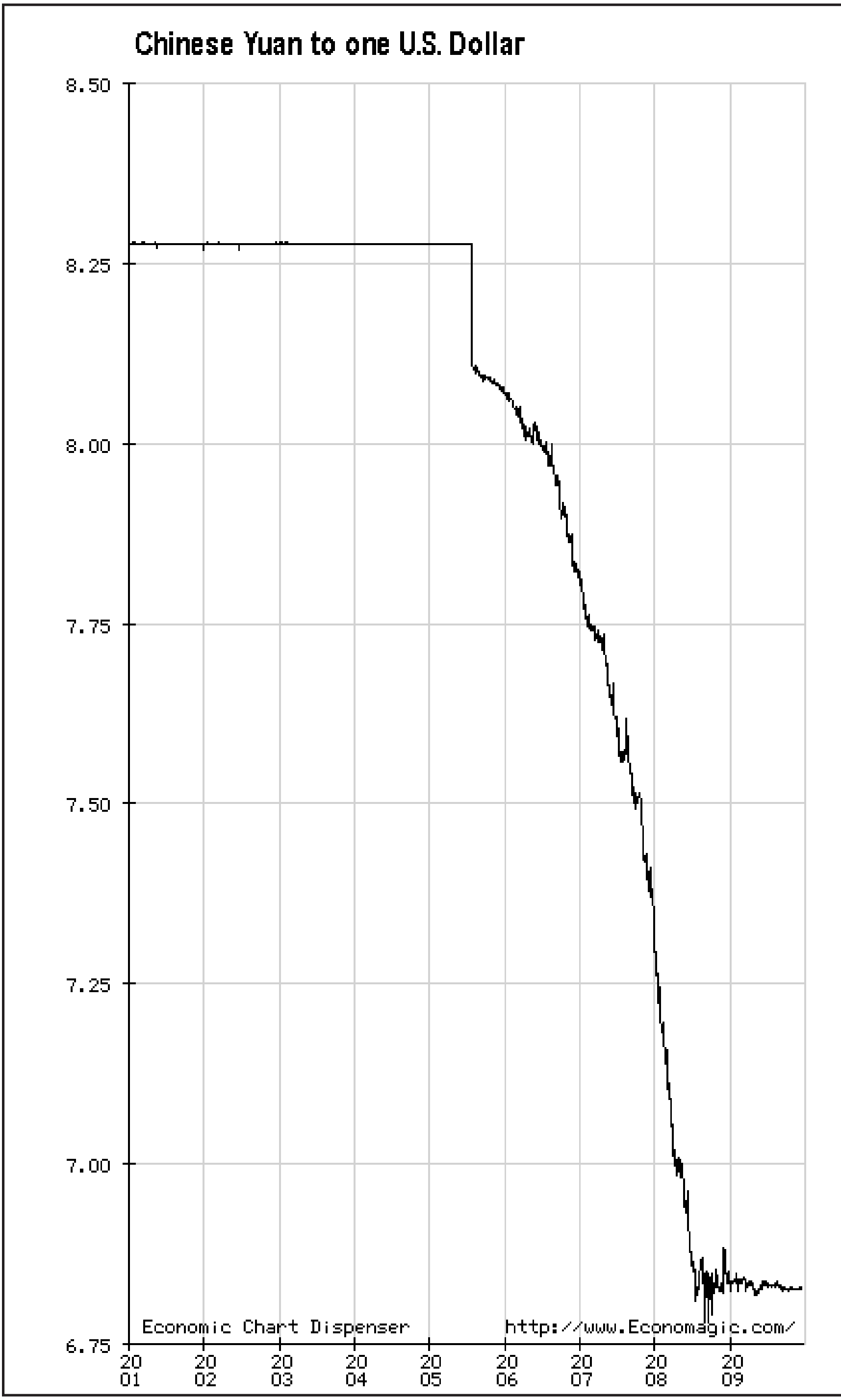
country and we wanted you to be aware of just how important the answer to this question is.

We wrote about some of the giants in American history: Alexander Hamilton, James Madison, Andrew Jackson and John Pierpont Morgan among them. These were men who longed to make America great and, right or wrong, had big ideas on how to achieve that goal. Today we have small minded men and women attempting to remake America into a country that is decidedly something less than great. The House of Representatives has just passed a bill seeking to rewrite the rules that govern banking and financial markets. The bill was mostly written by Rep. Barney Frank (D-MA) who chairs the House Financial Services Committee. Mr. Frank, who used to be my Congressman, is not a stupid man. In fact he is one of the brightest members of Congress. But Mr. Frank holds the wrong chairmanship. His talents would be best put to use if he could chair a committee on unintended consequences. It was Rep. Frank who pushed legislation that expanded the reach of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). These two quasi-public entities allowed banks to offer mortgages to a huge number of unqualified buyers, helping fuel the housing bubble and greasing the skids for the economy when that bubble finally burst. Fresh from denying that he had anything to do with the housing market disaster Mr. Frank is now attempting to bring his vision of how our capitalist system should be strictly regulated - by left-leaning bureaucrats determined to protect people from themselves - to fruition.


Chinese Yuan to one U.S. Dollar
8.50
8.25
8.00
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7.50
7.25
7.00
6.75
Economic Chart Dispenser
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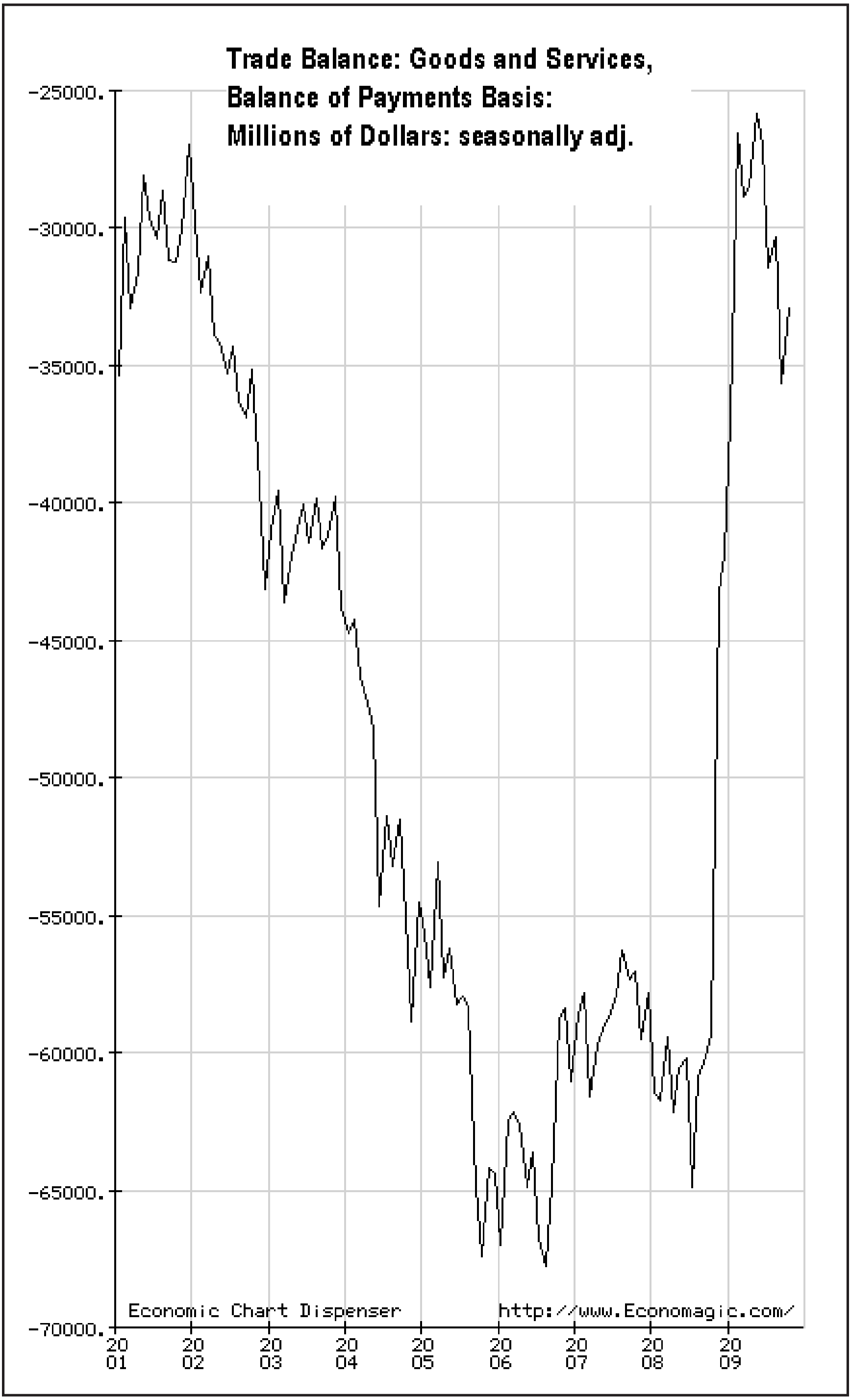
The bill passed by the House is never going to become the law of the land because wiser judgment can be counted on from the members of the Senate who have yet to pass their version of financial reform. But buried in this House bill are some disturbing amendments that just might make their way into any compromise bill the Congress hopes to hammer out in the first half of 2010. They are being obscured by the debate over the creation of a Consumer Financial Protection Agency. This part of the legislation is mostly unimportant. It simply looks to reorganize the agencies that are already protecting consumers. But many of the lesser known parts of the bill are down right dangerous. Chief among the amendments sure to cause endless troubles for the country is the one calling for Congress to audit the Federal Reserve and bringing stricter Congressional oversight to the bank. It seeks to politicize monetary policy, something the Congress back in 1913 worked doubly hard to prevent. Tellingly, Chairman Frank is among the chief critics of this part of the bill. He rightly understands what many members of Congress - especially Congressman Ron Paul of Texas - a man dedicated to destroying the Central Bank at all costs - do not: The Federal Reserve is already audited by the comptroller general and the Government Accountability Office. These are in addition to the audits that the Fed conducts on its private bank members using an outside accounting firm. Frank and many other members of Congress understand that the Federal Reserve provides an important firewall between money and politics. Without such a buffer the country risks becoming just another banana republic like Venezuela where the annual inflation rate is


Trade Balance: Goods and Services,
Balance of Payments Basis:
Millions of Dollars: seasonally adj.
-25000.
-30000.
-35000.
-40000.
-45000.
-50000.
-55000.
-60000.
-65000.
-70000.
Economic Chart Dispenser
http://www.Economagic.com/
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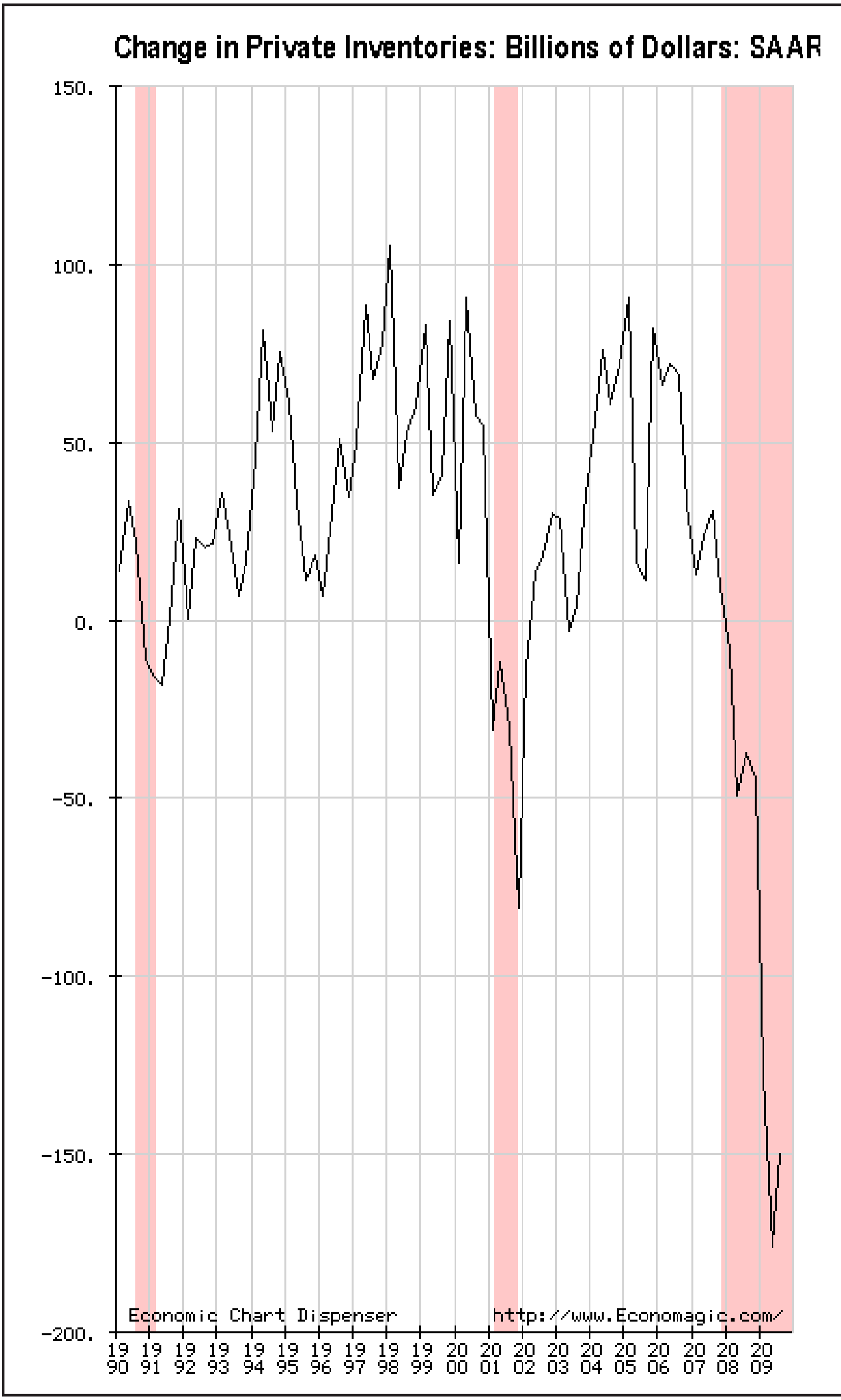
2008
2009

currently around 30% . This is apparently what populists politicians like Ron Paul want. I think it is imperative to the long term health of the nation that these populists be stopped cold. The importance of the coming debate and vote in Congress cannot be overestimated.

The bill would also allow the government to pass judgment on the wisdom of allowing big financial corporations, whether they were in danger of collapse or not, from operating if the federal government deemed them “too big” to exist. Never in the history of the country has such power been in the hands of government. The Obama administration, delighted to discover that the bailout funds they authorized earlier this year can be re-channeled into a slush fund with which to reward political supporters, has asked Congress to include a new $150 billion dollar tax on large financial institutions such as Goldman Sachs and J.P. Morgan Chase & Co. to create a new bailout fund.

Republicans, all of whom voted against the bill, and the 27 Democrats who voted against the bill, rightly point out that the legislation would create another massive bureaucracy which, in the end, would only lead to a reduction in credit creation and higher joblessness. We add to this the unintended consequences of making it impossible for the Fed to act in a timely manner to fulfill its role of lender as last resort. The legislation would specifically forbid the Fed from supporting private companies during times of financial panic like it did during the Panic of 2008. During the panic the Fed invoked its authority under Section 13(3) to provide


Change in Private Inventories: Billions of Dollars: SAAR
150.
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50.
0.
-50.
-100.
-150.
-200.
19 90
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19 93
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Economic Chart Dispenser
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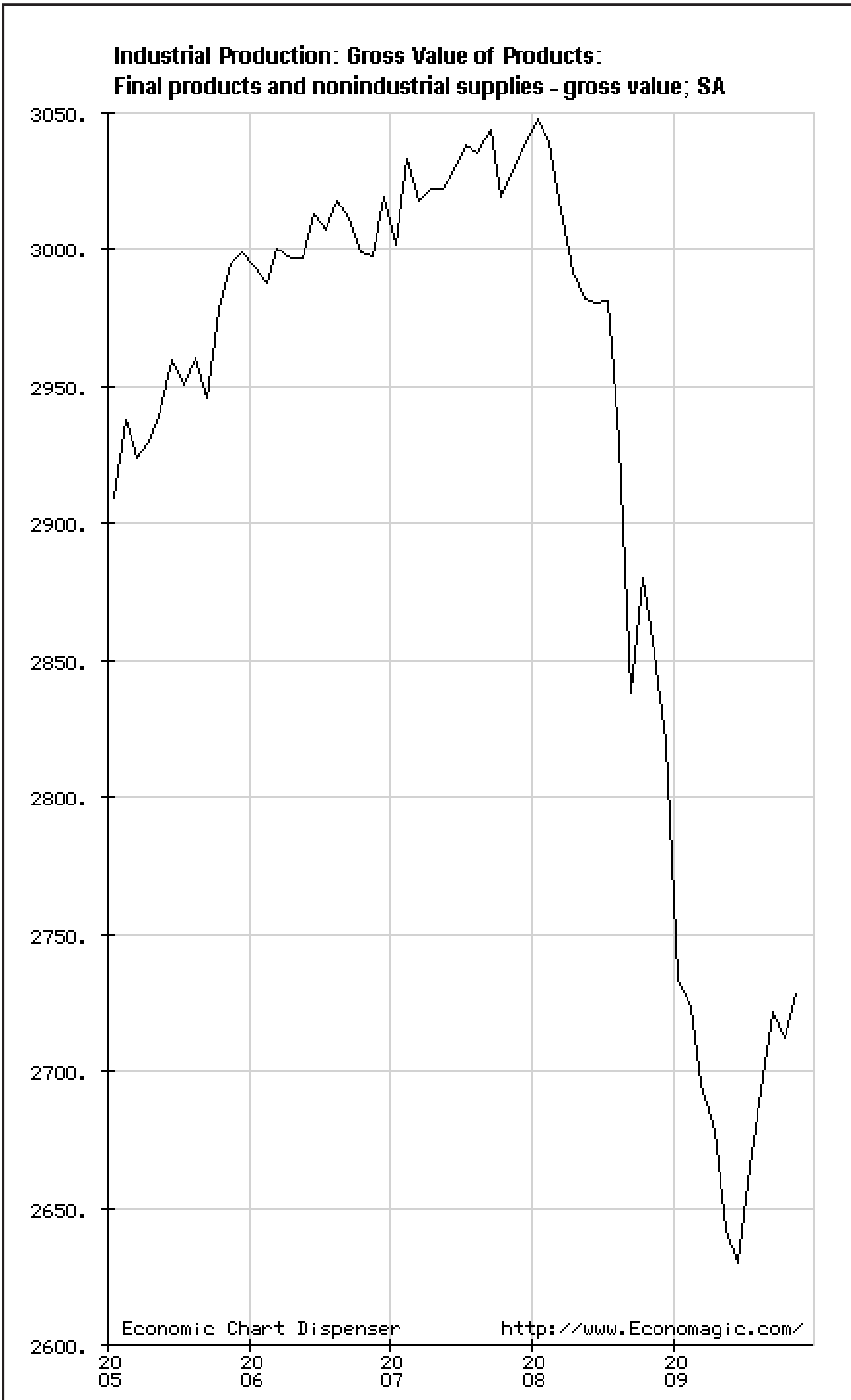
financial assistance to companies who found they were not able to access the credit needed to keep them from failing. The new law would create a Federal Oversight Council and charge it with the task of monitoring anything and everything that touches the financial community. The bill would only make it possible for the Fed to act after the President has declared an emergency, the Treasury Secretary announced his approval of any Fed action and two-thirds of the newly created council signed on to the deal. Even then the Fed would be prohibited from taking any actions that directly lent assistance to an individual company. Close your eyes for a moment and imagine what kind of shape the U.S. economy would be in right now if such rules had been in place last October.

I cannot conceive of a more dangerous piece of legislative micromanagement short of appointing the Treasury Secretary to be the head of the Federal Reserve.

The Senate counterpart to Barney Frank is Christopher Dodd (D-NJ). Senator Dodd shares with Mr. Frank a belief that the U.S. economy would be far better off if it was run by Congress and the financial reform bill he has just introduced has many of the same onerous restrictions on the capital markets. When it comes to the Fed, Senator Dodd wants to take reform one step further. His bill would change the way that regional Fed directors are chosen. Currently these directors are chosen by the commercial banks from the


Industrial Production: Gross Value of Products:
Final products and nonindustrial supplies - gross value; SA
3050.
3000.
2950.
2900.
2850.
2800.
2750.
2700.
2650.
2600.
Economic Chart Dispenser
http://www.Economagic.com/
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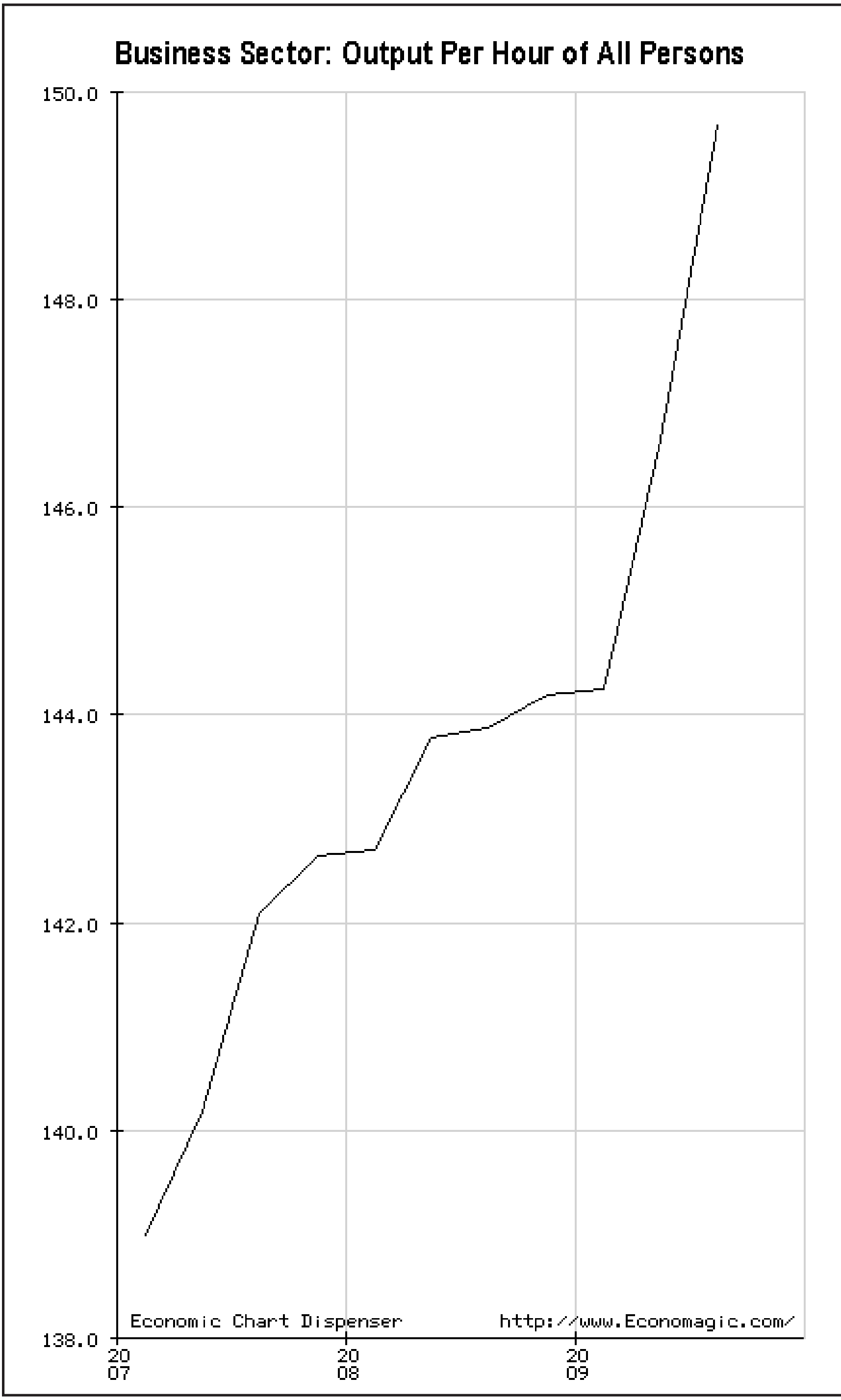
2009

individual districts. The Dodd bill would have them chosen by the Board of Governors, making monetary policy more reliant on voices from Washington, D.C. rather than from bankers across the country.

Don’t be distracted from this important legislation by all the hoopla surrounding the health reform and climate change bills.

While these bills are important and their passage will effect the quality of life for Americans for decades to come, the financial reform bill has the potential to destroy the stability of America’s financial institutions. Thanks largely to the efforts of the Federal Reserve, the country has been spared the painful experience of a financial meltdown and resulting depression. You would think that this would be a time to be celebrating the things that worked to keep us from falling into the abyss. Instead we have a sizable portion of Congress that seems intent on punishing those who did their job well and rewarding those who made the bad decisions that lead us down the path to financial panic in the first place.

I believe that when the dust settles and a financial reform package is brought up for a vote next year many of the most damaging parts will have been stripped out. If they are not I believe that the bill will fail to muster the votes it needs for passage. With solid Republican opposition the Democrats must count on nearly unanimous support within their own ranks to assure passage. It appears to me that, when the votes are counted many of the 50 or so moderate


Business Sector: Output Per Hour of All Persons
150.0
148.0
146.0
144.0
142.0
140.0
138.0
Economic Chart Dispenser
http://www.Economagic.com/
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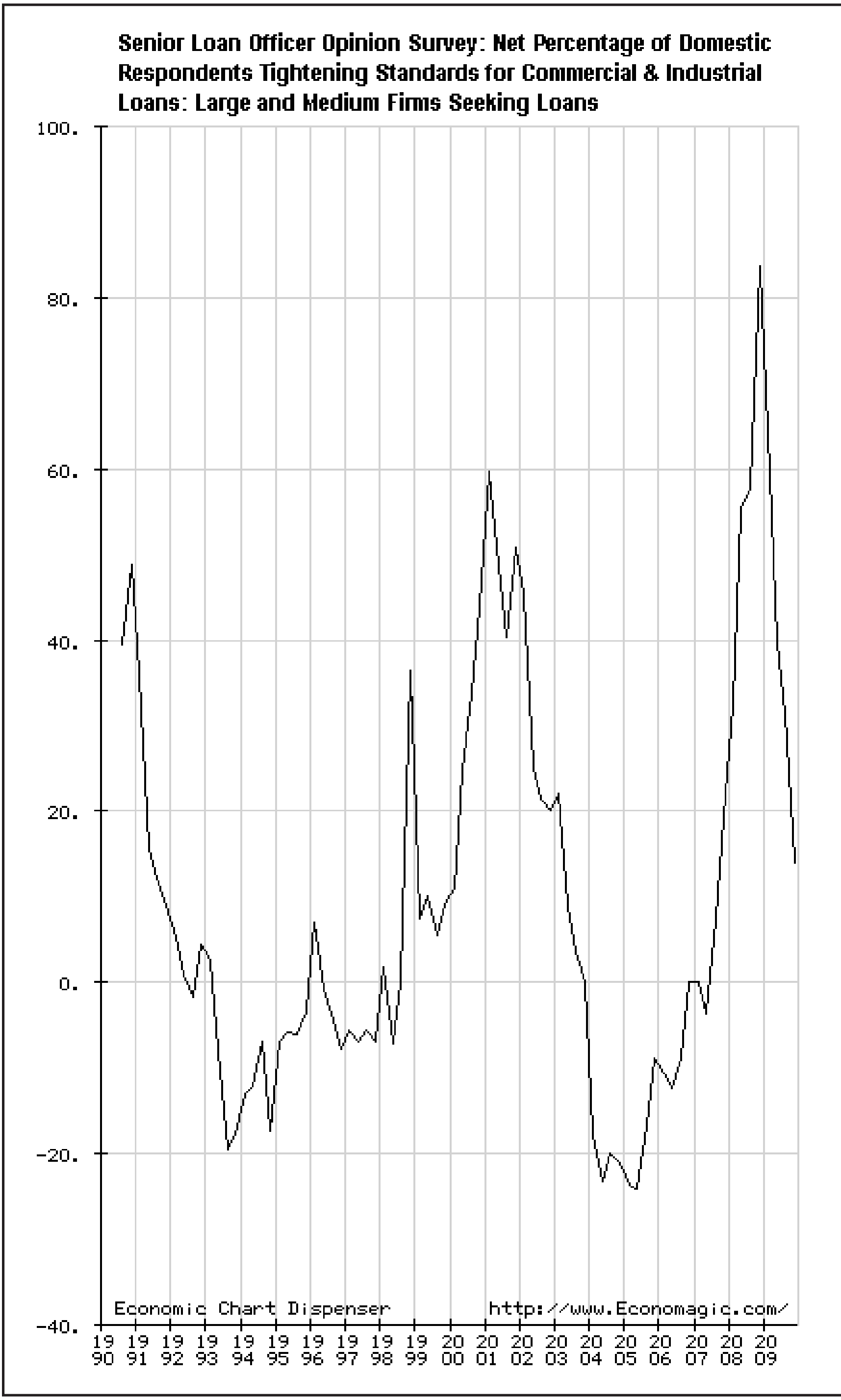
Democrats in the House will abandon this deeply flawed legislation. But the final vote is still months off and there is no telling just what kind of carrots and sticks the Democratic leadership will be willing to use in an effort to gain passage of this bill. A bill they know they will not get another chance to bring up for a vote before next year's election greatly reduces their power to control legislative priorities.

I will most assuredly be revisiting this subject many times in the coming months in effort to keep you apprised of its chances for success.

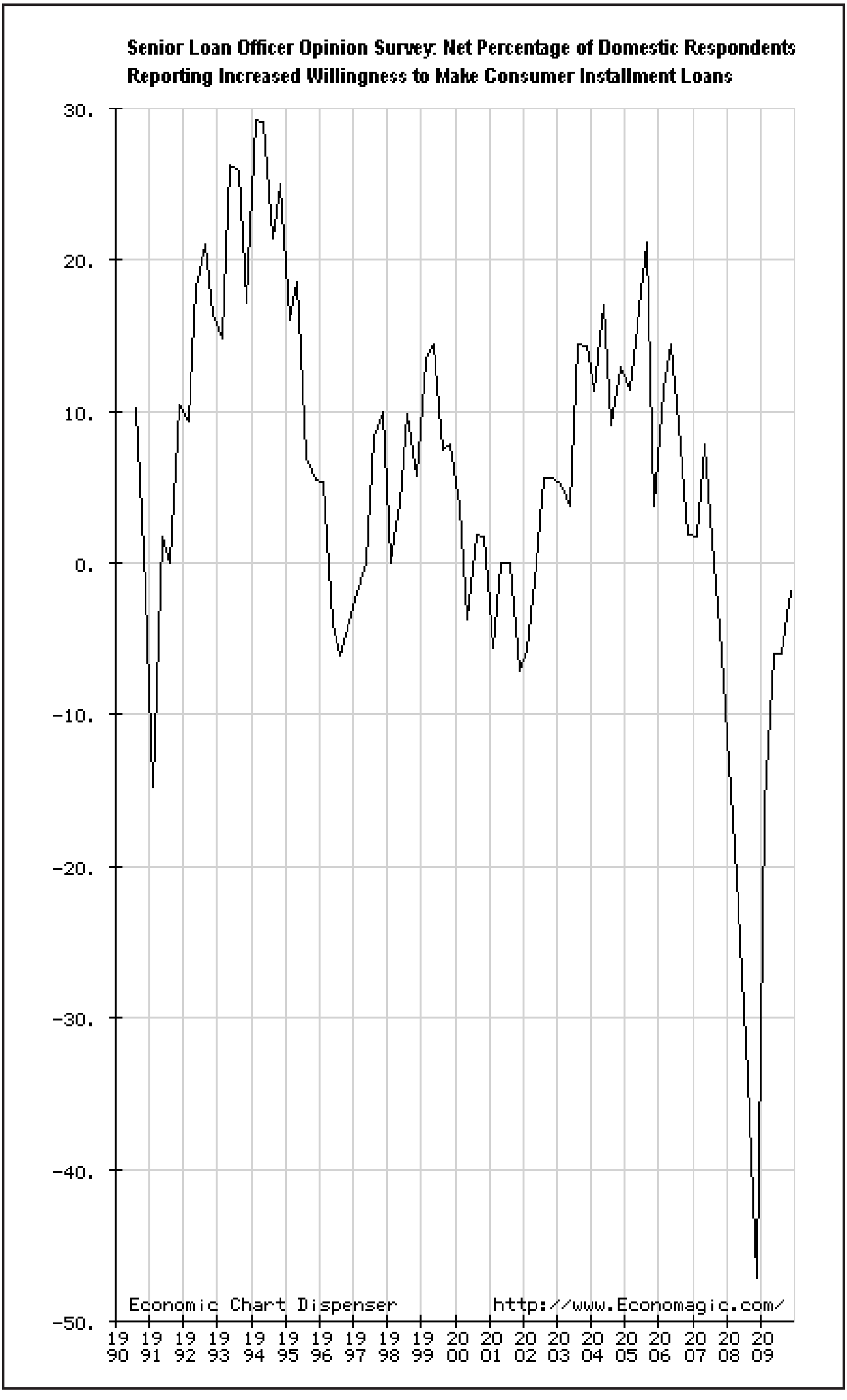
Let's now turn to the subject I most wanted to write about this month, the unfolding recovery and its prospects of surprising people with its strength and durability. The Obama administration, a big believer that the recession would allow them to force big changes here in America, has suddenly decided that there is little upside to pretending that things were bad and getting worse. Rapidly dropping poll numbers may have made the President move a little faster on this than he wanted to, but better late than never. Every day brings fresh evidence that the recession is over and that a recovery has begun. Larry Summers, the President's leading economic advisor made the rounds on television last weekend and let everybody know that he can now be sure that the recession is over. That suggests that the Obama administration is scared to death that they would look like fools if they continued to claim that massive government intervention was needed to save the economy from ruin, just weeks before GDP reports come out that might show the U.S. is enjoying


Senior Loan Officer Opinion Survey: Net Percentage of Domestic Respondents Tightening Standards for Commercial & Industrial Loans: Large and Medium Firms Seeking Loans
100.
80.
60.
40.
20.
0.
-20.
-40.
Economic Chart Dispenser
http://www.Economagic.com/
1990 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009

annual growth rates of 5% or better.

There are two parts to this recovery story. Both have been underplayed by the national media. The average media outlet is staffed by people who are very good at coming up with the names of Tiger Woods' latest paramour, but are not all that good at understanding economic concepts like balance of trade or industrial production figures. In addition, the media has willingly bought into the line of thinking that assumes that America is finished as a great economic power. Every story that appears in print or on television starts with the assumption that America's best days are behind her - the future belongs to China and India and Brazil. But this foolish assumption has blinded these reporters and analysts to the facts on the ground.

Take a look at the first three charts I have reproduced for this letter. They show you what has been happening to the U.S. dollar over the past decade. The weakening dollar has been the subject of any number of articles. Nearly all come to the same conclusion, that the weak dollar is proof that the U.S. is washed up. I could not disagree more! Back during the Clinton administration it was believed that the quickest way to achieve prosperity was to strengthen the dollar and flood the country with low cost imports. This thinking helped China and Japan and most other Asian countries with large manufacturing capacity to steal market share from American companies and forced many U.S. manufacturers to close up shop. Six million manufacturing jobs were shipped overseas as a result. But starting early in the G.W. Bush


Senior Loan Officer Opinion Survey: Net Percentage of Domestic Respondents
Reporting Increased Willingness to Make Consumer Installment Loans
30.
20.
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0.
-10.
-20.
-30.
-40.
-50.
Economic Chart Dispenser
http://www.Economagic.com/
1990 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009

administration the dollar was allowed to begin falling. It was an orderly decline. So much so that most people in America didn't even notice what was happening. But our trading partners did. They were extremely unhappy by the direction of the dollar and took steps to halt and in some case try to reverse the decline. All failed. The Europeans could never find a way to keep their undervalued currency from appreciating against the dollar. Starting in 2005 the Japanese attempted to save themselves from continued economic hardships by forcing the yen back down against the dollar. They had success for about two and one half years before they too succumbed to economic reality and were forced to watch as the dollar started falling against the yen once again. By the start of 2009 the Japanese were stuck with the reality that they would no longer be able to drive their economy by exporting goods to America. Even the Chinese, the country most successful at manipulating their currency to keep it massively undervalued compared to the U.S. dollar, lost its battle to keep the yuan permanently undervalued. Bowing to reality they too started letting the dollar fall against their currency.

The falling dollar produced almost immediate results. The U.S. trade deficit, which had been growing larger every year peaked in 2005. By 2006 the deficit began to shrink. In 2006 the surging price of oil turned the trade deficit back up, but the recession that followed this spike in oil prices zapped all the strength from the U.S. consumer. The plunging price of oil combined with America's new found desire to begin living within our means led to a startling reduction in the trade deficit. In just six months the number was halved. It has long been assumed that once the economy recovered from recession American imports would quickly begin to outpace exports. But the three currency charts show you why this will not happen. After a rush to safety following the financial panic foreigners seeking the relative safety of American assets began to unwind these positions. This has led to a retracement against other currencies by the dollar. As we move forward in this recovery that dollar weakness will help preserve America's ability to compete for orders around the world. I stand by my assertion back in my October letter that the weaker dollar has made it likely that the U.S. trade deficit could soon turn into a trade surplus. This has enormous implications for growth here in America. All of them good ones. While the doom and gloom set wishes to wring its hands over consumer spending (which, by the way, showed surprising strength last month) they are missing the bigger picture. This recovery is being led by American manufacturers who are being called upon to restock the shelves not just of American companies but ones overseas as well.

Take a look at the chart on page 10. It shows you changes in private inventories over the past twenty years. Note that each time inventories <u>contracted</u> for an extended period of time this country suffered through a recession. The inventory contraction of 2008-09 is by far the most severe one we have experienced in a while and it easily explains the severity of the recent downturn. But history suggests that the bigger the reductions in inventory the bigger the build up needs to be once the recession ends. The most recent data also suggests that, at long last, the drawdown of inventory is finished. I believe that the coming months will see the private inventories number make a mad dash back to positive territory. The chart on page 12 backs up the inventory chart. After a year and a half decline industrial production turned on a dime and began climbing several months ago. This suggests that America's factories are much busier than people think. The chart on page 14 tells the story of why this dramatic turnaround in production is going to herald in a new age of higher corporate profits. After months off relentless budget cutting American business is lean and mean. The workers who have survived the cuts are motivated and, in most cases, the best workers the company had before the slowdown began. The results can be seen in the chart. Output per hour is up nearly 10% despite the huge reduction in the workforce.

That means higher margins and more profits per dollar of sales. I have seen many fools discuss this recovery and bad mouth the numbers because they fail to measure up to pre-recession levels. They haven't a clue what the three charts we have just shown you mean. Corporate America does not need to achieve the same level of sales seen back in 2007 to achieve 2007 profit levels. Lower costs will see to that. Those who fail to grasp this simple concept are destined to miss out on the early stages of this recovery and the bull market that is sure to accompany it.

Much is being made these days about

banks and their unwillingness to lend.

The last two charts should put your mind at ease on this point. The chart on page 16 shows the willingness of bankers to loan to big and medium size businesses. Note that the net percentage of senior loan officers who say they are tightening credit has been dropping precipitously and is nearing the point where the index will turn positive The same survey results can be found for small businesses. The trend is moving quickly in the direction of more bankers loosening that are tightening The chart on page 18 shows the net percentage of senior loan officers who report a willingness to extend credit through consumer installment loans. After plunging for three years this number is about to turn positive again as well.

While it is currently fashionable to sell this recovery short - before it has even had a chance to prove how strong it can be - I am convinced that the underlying factors that determine the strength of an economic recovery are signaling strong growth in the coming quarters. The businessmen who trust in the strength of this recovery will be the ones who ramp up production first or who take the chance of ordering more goods in a belief that the demand for them will be there. These will be the companies that make the highest profits. Investors who trust in the strength of this recovery will be the ones willing to invest in those companies early and they will reap greater profits than those who sit on the sidelines and wait for more proof.

- Adrian Van Eck

ADRIAN VAN ECK EXPLAINS WHY HE OFFERS HOTLINES

In the summer of 1990 , Adrian finished
His monthly Money Forecast Letter,
Put it in the mail and flew off to
Washington, D.C. for an appointment.

Adrian was in the office of the Secretary of Treasury when an aide rushed in and breathlessly announced that Iraqi armor and troops had just crossed the border of Kuwait. Needless to say, the planned meeting was cancelled, as first President George Bush summoned his cabinet officers to an emergency meeting at the White House.

The economy was suddenly turning upside down and Adrian wished he had a way to communicate with his readers. On the flight back to Boston, he decided it was time to supplement the in-depth analysis and forecasts in his monthly letter with a time-value weekly hotline.

At first he provided a voice message. That proved impractical and it was soon replaced by a fax version. More recently he added an E-Mail version, which is today the choice of 5 out of 6 hotline subscribers.

If you do not yet take Adrian's hotline on Money and the Economy, please turn over and sign up now.

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