

Today's Notes:

1. Rest a Little Longer

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What does little birdie say, In her nest at peep of day?

**"Let me fly," says little birdie,
"Mother, let me fly away."**

"Birdie, rest a little longer, Till the little wings are stronger."

**So she rests a little longer,
Then she flies away.**

-Alfred Tennyson.

When I was a little lad my dear mother used to paraphrase Tennyson, when I was restless and anxious to tackle the world,

"Miguelito, rest a little longer, till your little wings are stronger; then you'll fly away."

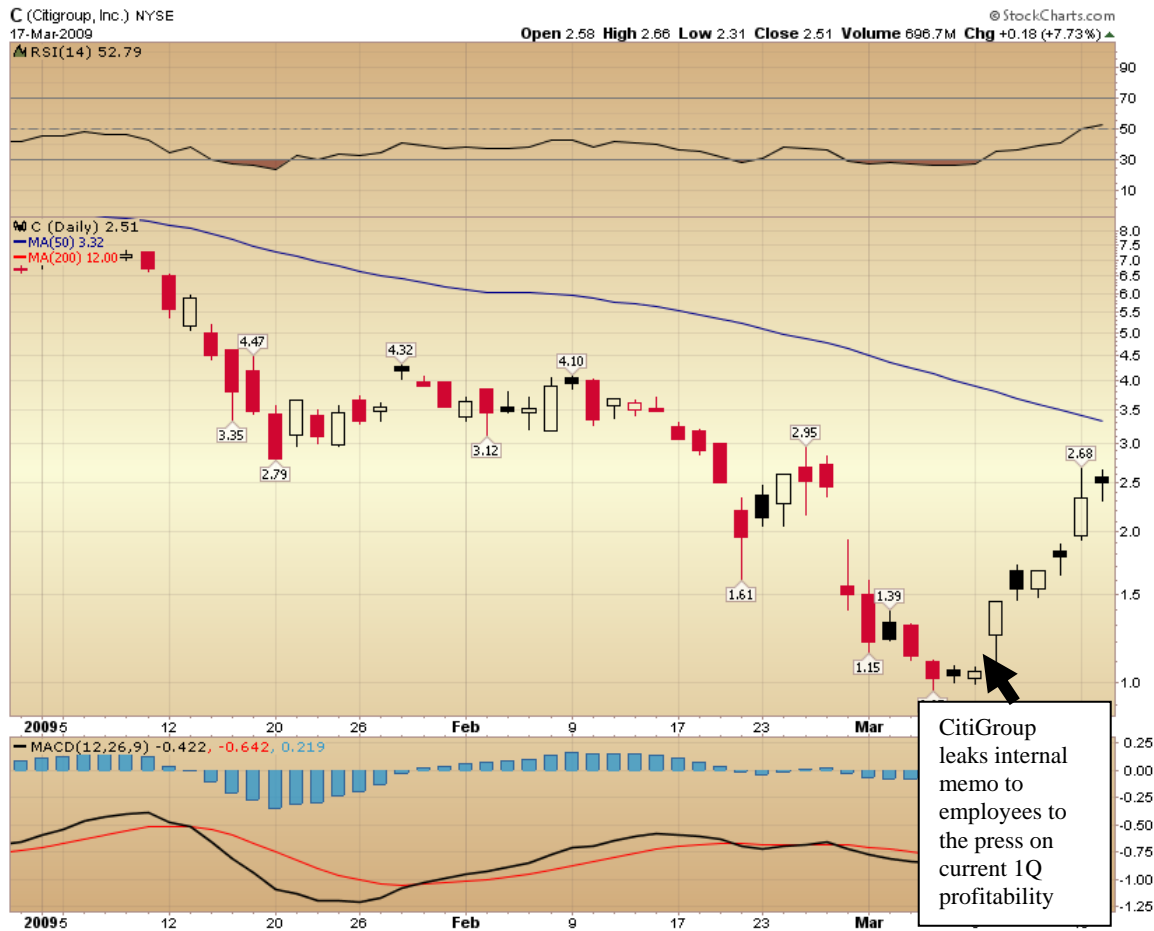
I well remember her advice. Perhaps mothers should run our economic affairs?

This AM we have an equity market that, for the past 6 days has, run away to the upside. The Dow Industrials have increased by 14.6% (950 points). Everyone is feeling better. The market psychology has changed, for the better. Spring is in the air. I cannot tell you how much I have yearned to write something positive for the past nine months. Alas it has been impossible.

Recently a glimmer of hope has appeared. Or has it? It is true that at the market's close last evening the Dow (and most other global equity indexes) had gained 14.65% in 6 consecutive trading days. This took the Dow Industrials off their lows of 6469. The rally has resulted in a 14.6% return. In each of three past Dow bounces there has been a catalyst. On Friday November 21st Mr. Obama announced the nomination of Timothy Geithner to Treasury Secretary. The equity market swooned and stocks went bid. They did not look back for 1400 points. Last week, (March 10th), Citigroup executives leaked an internal memo to the press suggesting the bank was profitable in the quarter-to-date. CitiGroup had "broken the buck" on March 7th.

The reaction was immediate. The markets (worldwide) in a frightening knee jerk were so thirsty for good news, in this parched equity wasteland post-July 2008, that they rushed the barriers. CitiGroup shares soared from \$1.00 to \$2.52, a nice gain for some, particularly after all the talk of bank nationalization from Dodd et al. in Washington.

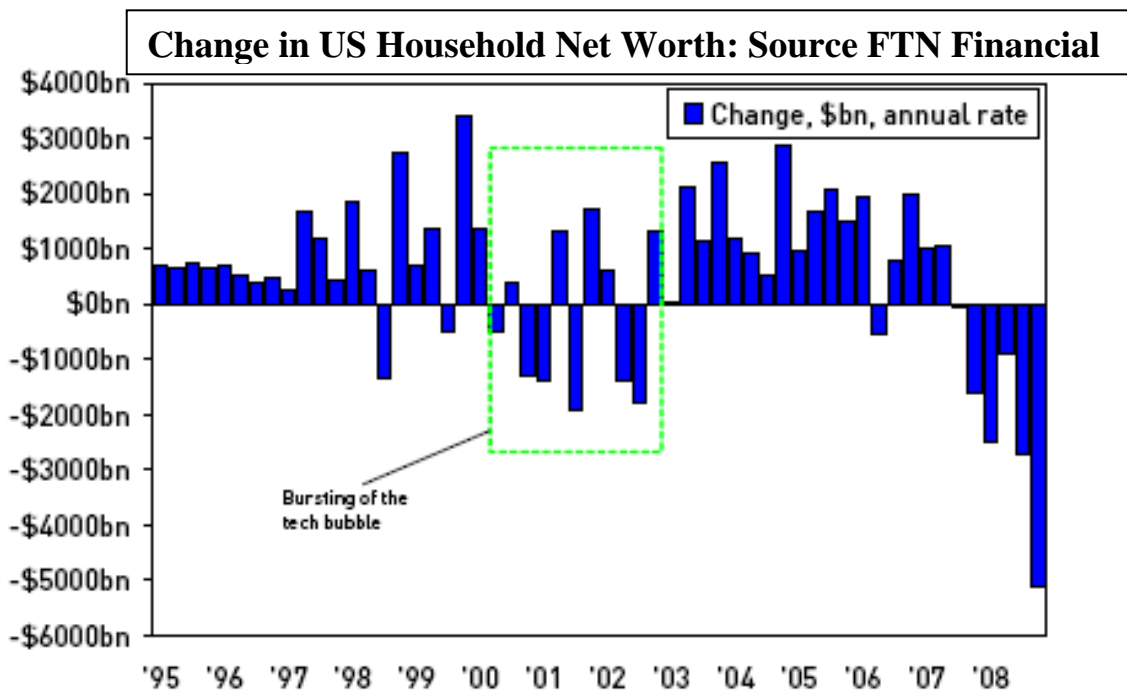
Now the question is whether this is a new bull market or another 18% to 25% bear market rally. Of course only time will provide the answer. Capital markets often anticipate the economic cycle.



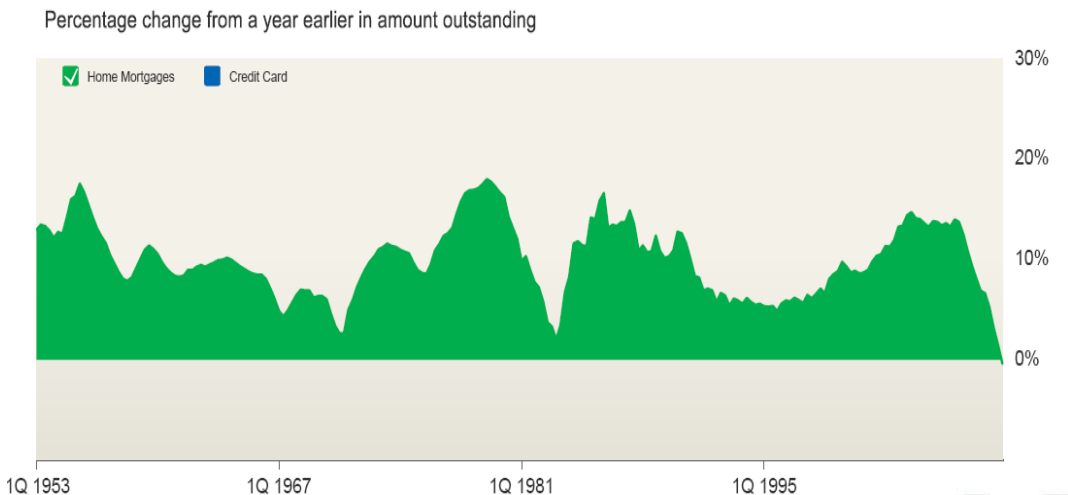
Unfortunately, we still see a rapidly deepening economic malaise in the world. The IMF forecast a much lower Chinese growth rate, this AM, a decline from 8% to 6.5% for 2009. In Washington all focus is inappropriately on the \$135 million in AIG bonus structure. CEO Edward Liddy will testify before the House committee. We hope he takes a moped to Washington. To Mr. Barney Frank, what about the **billions** of dollars of US taxpayer money paid to foreign banks by AIG?

In a spate of “Keynesian animal spirits,” the Obama Administration has instigated a serious trade dispute with our third largest trading partner, Mexico. The dispute centers on 98 Mexican transport trucks that have been denied free access to our highways. Protectionist sentiment is growing every day, everywhere just as it did in the 1930s.

We have not yet seen a convincing Treasury plan on how to deal with toxic assets in the banking system. Secretary Geithner will unveil a plan on Thursday. It had better be well thought out and convincing or this rally will end, ‘not with a whimper but a bang.’ Finally American’s net worth has fallen, in the incredibly short timeframe of 8 months, nearly \$5 trillion (YOY) through the end of February according to Chris Low of FTN Financial. This is a massive hit to the world’s most prolific consuming superstructure.



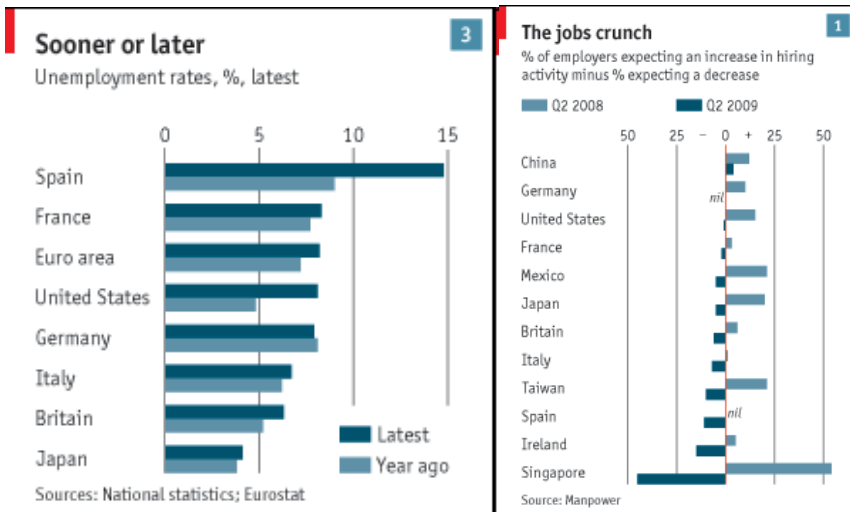
Growth (YOY) in US Mortgage originations is at post WWII lows.



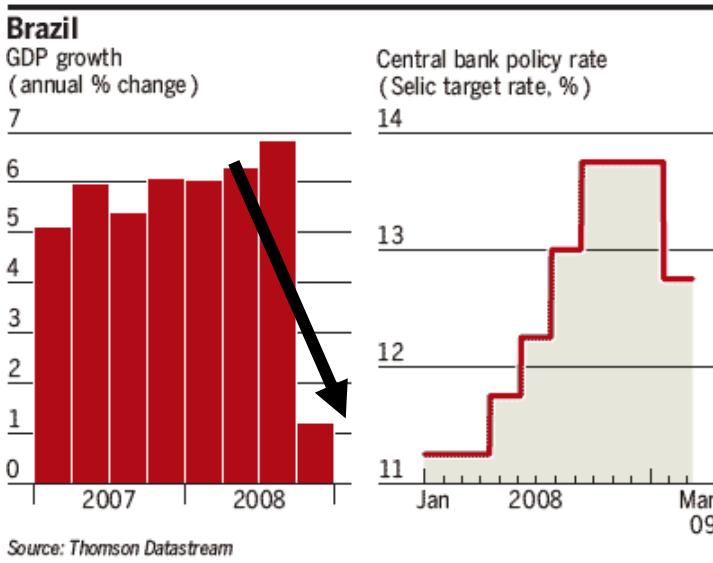
The Great Contraction appears to be a once in a century phenomenon.

Unemployment in Britain and Russia, this AM, are now seriously deepening. Russia's unemployment rate is 8.1%. There are stirrings amongst the normally complacent Russian population. While the Brits have been ahead of the Americans and complacent Europeans (nationalizing Northern Rock, reducing rates and quantitative easing) in this Mother of all Crises, their banking and housing problems are an order of magnitude worse than here.

The Europeans are complacent and slow to act. Unemployment is likely to grow. In fact the global nature of unemployment (*Economist, March 17, 2009*) expectations is a conker, to say the least. Jobs are disappearing everywhere at an accelerating rate.



Even isolated and once insulated Brazil, one of the original “BRICS,” is now feeling the pinch.



My points are:

- 1) Oversold global equity markets are climbing many “walls of worry.” This in itself is very impressive. Dow 9,000 would be even more impressive.
- 2) The broadness and extent of the economic decline has been underestimated by almost every actor in this global play. Take a look at Alcoa and you will see a company buying back shares far too early in the decline of the capital markets.

- 3) The world has not yet decided to work together. That is obvious. Wars have always and everywhere been ubiquitous results of this failure.
- 4) We are rapidly approaching the point where Mother Nature must take charge and liquidate the toxins in this financial atmosphere. Perhaps all the central bankers have done is to postpone the economic reckoning.
- 5) Liquidity traps abound as money is printed and rates approach zero. We expect to see the US FOMC begin “Quantitative Easing” if not today – soon.
- 6) The **Great Question**, as yet unanswered is; **will it be inflation or deflation?** At present we are tipping precariously into a deflationary phase despite all the firepower aimed at the world’s economies. This AM PIMCO’s Bill Gross warns the world, and Europe in particular, that **deflation** is the great threat.

An examination of central bank monetary policy shows that the great “race to the bottom” in interest rate policy is almost over. Even the Swiss have thrown in the towel and competitively devalued their noble Swiss Franc.

All this will end in due course. However it is not yet half time in this game. **Might I suggest that you “rest a little longer?”** I have been besieged with requests from investors most anxious to join the fray. At my speaking engagements investors will approach and plead for a “green light.” Please rest a little longer. I know that all of us have lost 30% to 80% on the equity markets. That includes large and small cap stocks, Discovery and Value / Growth stocks, banks and insurance companies, GM, GE and your important IRA / pension legacies. Even venerable Harvard University’s endowment lost 35% and must increase tuition and delay plans. There are no pockets of paper wealth that have been left untouched.

However if you have reduced debt and raised cash, as I have respectfully requested for the past two years in these Morning Notes, you are now rapidly gaining the “driver’s seat.” I think gold will now pull back (\$860). Silver will follow. These declines will provide important buying opportunities. Second, there are now many of my Discovery shares that are classic “Penny Dreadfuls.” Except that their assets are world class. If you can be convinced that balance sheets can hold with adequate liquidity, these are the stocks you should be tracking. You know my Discovery names by now.

By the way I will be lead presenter at the Federal Reserve’s (FFIEC) meeting in Arlington Virginia on April 21, 2009. I plan to publish that presentation once finished.



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