Rohr Report

TrendView

BRIEF UPDATE: FIXED INCOME

Wednesday, October 11, 2006 (08:00 CDT; 09:00 EDT; 13:00 GMT)

OVERVIEW

Very brief again today, as technical levels and trend views are the same as yesterday's *TrendView* GENERAL UPDATE and Monday's *Capital Markets Observer*. Of course, there will likely be little further major price movement today as the markets await this afternoon's release of minutes from the September 20th FOMC meeting. Even then, unless there is something startlingly different than expectations of a balanced discussion, tomorrow afternoon's Beige Book release is the more current and likely more critical trend influence.

While that is the case fundamentally, the technical situation is now critical based on the tension between the initial T-note failure below its mid 107-00 previous major UP Breaks and current trend support, and the fact that even as bad as the Bund has acted over the past several sessions it is only near its own low 117.00 previous major UP Breaks (with a Tolerance to 116.80 once again.)

Whether the T-note can rescue itself back above the mid 107-00s is problematic, and the weekly down gap yesterday (107-19.5/-14.5) creates extra initial resistance. Yet, it still takes a weekly Close in the Bund below the 116.80 Tolerance of the low 117.00 area support to turn the two long end upside leaders back into aggressive failures that will undoubtedly have a further pernicious effect on the other fixed income if it occurs.

On the economic background, we find the plain spoken views from the Reserve Bank of Australia are often among the most useful observations, and Governor Stevens' speech this morning on 'Economic Conditions and Prospects' was another clear summary of the world situation as well as conditions in his country. He points out something which we have noted for some time that will likely mitigate any sustained weakening of energy prices and inflation: The US economic softening is occurring right into strong economies elsewhere, which include Australia, Japan, Europe and especially that other energy guzzler, China.

His concise view on the potential for the US slowdown to affect the rest of the world relates well to that: "Of course, forecasts can be wrong. The US might slow more than expected, perhaps because of larger dampening effects of the housing downturn. Another way it might eventually slow more than expected, as pointed out by the IMF's recent *World Economic Outlook*, would be if persistent inflation pressures required further monetary tightening."

That just about sums it up. Either the spillover from the marked cooling of the US housing market weakens the balance of the economy much more aggressively, or interest rates will likely need to rise. This confirms the recent sentiment from some others in the Federal Reserve System which we have noted previous.

It seems that a prominent previous member of that team is also skeptical that the housing market's retrenchment will have much further effect, as it may well be very nearly complete. It was actually a bit of a surprise to hear him comment on it, yet Mr. Greenspan's comments on Monday were nothing if not broad. In addition to his views on why it will be hard to bring energy prices down by very much in the near term, he also explicitly stated what many of us had inferred from the 1994-1995 interest rate tightening discussion in the 'history lesson' that was his "*Economic Flexibility*" speech at the NABE September 2005 dinner: The Fed knew it would need to continue to raise rates to levels which would cause an actual recession in 1997-1998 if the equity market bubble was to be defused.

Under the 1997-1998 circumstances, we understand why they chose to restrain themselves instead of risking a massive global recession. We wonder if Mr. Bernanke and Company will feel as justified in letting any further extensive equity market rally ensue in the current global economic environment. The Financial Times article on Mr. Greenspan's recent comments is attached, including our markup of some of the highlights. The text of his original NABE "*Economic Flexibility*" speech is available on the **Sample Reports** page of our website (www.rohrintl.com), just below our September 28, 2005 ***TrendView*** **BRIEF UPDATE** noting that his observations likely meant the FOMC was going to need to hike rates much further into early this year than many observers had expected in the wake of Hurricane Katrina.

The one other observation today is on the US data release yesterday which likely added to the pressure on fixed income from all of the other strong news early this week in the wake of that shock from the BLS CES revision last Friday. While not often trend decisive, the US Wholesale Inventories (AUG) were quite a bit stronger than expected. This number is a bit of a two edged sword, and an inventory build can sometimes reflect sluggish clearance of previous production.

Yet, in this case the sales figures were also quite strong, which leads us to believe that inventories are being built in anticipation of strong activity to follow. The year over year sales increase continued to outpace inventory growth by a margin of 12.5% to 9.7%. What this means to the balance of the reporting calendar this week is that Friday is the beginning of the punctuation in the middle of the typical mid-month US reporting vacuum (with inflation numbers to follow next week.) One of the key numbers due for release on Friday is the Advance Retail Sales for September.

While always an important number, whether it is now above or below some fairly tame estimates (headline up 0.1%-0.2% and ex-autos flat to down 0.1%) will be a very interesting further insight after what was a much more robust August than was expected. The data points are beginning to reveal how the US consumer really feels on their return from summer holidays, and in the wake of the US housing retrenchment.

We hope you find this helpful.

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