Rohr Report

TrendView

GENERAL UPDATE: FIXED INCOME/EQUITIES/FOREX/ENERGY

Friday, May 14, 2010 (from Thursday's Close)

Key Views

▪ **BIG Package with predictably big bounce, but DJIA back below 10,800 is a problem. The most important trend perspective right now is the progression of the equities sequence, and whether they can extend near term strength (DJIA back above 11,000) in the wake of the major EU sovereign debt rescue package. And the decision day is here!** There are multiple reasons for this; some big picture, and some near term. And as most participants are well aware of the major cross currents, as well as the technical evolution being more critical today, we will be brief on the general 'macro' background. That said, we will expand upon key elements of the Triple-G 3x3 Threat that are relevant to individual near term decisions, and discuss it at length next week. The first and most important of these is the upside and downside of the rescue package; which was just that, and not a panacea.

From our perspective (and we presume that of no small number of our readers) the current EU/IMF/ECB action differs markedly from quantitative easing (QE) and liquidity program of the Fed and Bank of England. That is due far more to context than the sheer monetary size of the intervention; especially considering that the Q (quantity) of QE is subject to some significant alteration when deemed necessary. The difference that might spell equities' success or lapse back into a bear (or at least a major correction) is the fiscal side of the equation. Even in the dire straits the Fed and Bank of England dealt with back in 2007-2008, 'sovereign debt' was still some sort of ethereal threat lurking in the shadows, yet which had never assumed any concrete manifestation which might derail the credit and equities markets. As such, the US 'lender of last resort' and its cohorts in England were free to engage in wholesale liquidity provision in the name of the greater good without triggering any sovereign debt crisis at the time.

And that was while allowing fiscal stimulation in the US and UK, even as the Fed allowed further expansion of its balance sheet through US dollar swap lines to mitigate shortages elsewhere. Those are now reinvigorated even as the Fed was supposed to have begun shrinking its bloat; more of the best laid plans, and all that. Yet, due to the context of the current rescue package, the ECB has no latitude to allow fiscal stimulation on the order allowed (indeed encouraged) by the Fed and BoE. Indeed, just the opposite is true. ECB capitulation into the government bond purchase form of QE means it will be taking obligations of the most distressed borrowers onto its balance sheet. And that is after the political class and the ECB both singularly failed to prepare the German populace for the forced evolution of EMU into a partnership that is now much different than what they bargained for. Which is why the ECB will be constrained to demand austerity from its weak sisters instead of allowing or encouraging fiscal largesse.

Of course, what all this has to do with the equities trend is the conflict between near term economic data strength and the coming drags from the Austerity Craze. The cross currents are so far flung as to leave the only reasonable path the one we almost always choose in any event: allow the market to communicate its inferences from the data and expectations today.

▪ **And today is particularly important because of the lack of economic data elsewhere prior to release of April US Retail Sales. While we questioned the efficacy of analysis of 'rearview mirror' data during the buildup of the crisis into the end of last week, this is one of those junctures where it is important once again, both as indication and as a trigger.** As the question moving forward is whether resurgent developed economies like the US and UK will see enough 'final demand' (as the central bankers like to characterize consumer sales) to offset the likely lower demand from countries hit with fiscal tightening. Oops, we forgot: the UK is among those economies now as well. In fact, Governor King's post-Quarterly Inflation Report comments have highlighted the degree to which he encourages accelerated fiscal adjustment; and made no secret of the Bank's willingness to extend monetary accommodation to smooth that process. (Which is the reason the up trend in short money forwards remains intact.)

And the question surrounding US Retail Sales is whether the surge in March was merely the benefit from an early Easter. Yet, even if the figure is as strong as expected (most importantly the ex-Autos & Gas 0.4% anticipated monthly gain) the market response will be telling. It is no secret that markets are creatures of anticipation. And now that the salutary crisis mitigation aspect of the BIG Package has been discounted over the past several days, the other aspects of it are going to be more telling. Of course, if the US numbers are weaker than expected, it will be easy to expect a bad finish on the week. After such a strong recovery rally that would reinforce the degree to which the failures from major resistances two weeks ago might indeed signal a larger near term reversal than the bulls are anticipating at present.

Even before the sovereign debt crunch central bankers (some shrill hawks notwithstanding) were very cautious on the timing of any actual monetary accommodation withdrawal. It was no secret that Mr. Bernanke preferred a dovish stance, and the Bank of England consensus was clear in each of the recent Quarterly Inflation Reports. They seemed to know what some in the analytic community (present writer included) sensed: significant structural weakness beneath the surface of strong monetary accommodation risk reflation rallies in equities and commodities. That structural weakness now being made palpable by the Greek debt dilemma has finally taken tangible form that will ripple through the final demand of many other countries which wish to avoid the fate of the guinea pig.

▪ **And that is why the near term fate of the equities is so important. Aside from the sheer psychological implication of a weaker view of the economic future if they falter, there is another more diabolical aspect: erosion of the fiscal calculus of debt rescue plans if that anticipation of a weaker economic future turns into self-fulfilling return to a credit crisis.** In that regard, whether **DJIA** can hold without too much slippage below 10,800 (or even better Close back above 11,000) is likely tied in with the success of the beleaguered euro holding no worse than the **EUR/USD** 1.2500-1.2450 support (interestingly slightly below last week's panic treading low.) While which might lead is unsure, any DJIA lapse back into an aggressive down trend will most likely upset the euro, where the next support below 1.2450 is more likely the 1.2000 area instead of the 1.2330 October 2008 trading low.

And the equities influence on other asset classes is likely fairly straightforward as well (with the exception of the Gold; more on that below.) As noted above, other than the ongoing inflation mantra of the central bank hawks, the fixed income likes everything seen from central banks. Even on yesterday's retest the **June T-note** has held 118-16 support, in spite of the fact that the underlying support might have been as low as 117-16. Yet another sign of the bond market resilience in the face of relatively strong economic news and buoyant equities. It was therefore no surprise when the market got the bid back late yesterday as equities waned.

▪ **The ultimate indication of whether equities have rolled over into a much weaker state for the near term (and possibly intermediate or even long-term) will be whether the DJIA closes far enough back below 10,800 today to confirm this week's rally was no more than a temporary, if very sharp, reaction. And the key level will be the 10,730 January high.** That is due to much more than the fact that would put the market back into that entire lower range where it acted so poorly last week. The 13 week moving average is around 10,750, and a close below it after ranging back above 10,800 this week would be a sign of just how much the upper levels of this week's rally were nothing more than a correction that fail to get back above the more important resistance in the 10,950-11,000 range. There is also the matter of weekly MACD having just turned down in any meaningful way last week on most equity markets, and whether or not the most resilient sister **DJIA** continues to reinforce that by respecting technical resistance this week is very important this early in an attempt that downturn. In a much broader scope, this is very much akin to the rally back after the initial failure from the very major 11,250 resistance two weeks ago saw DJIA fail from no better than 11,200 on its late week rally.

It is also the case that last week's virtually instant drop to the next major support in the 10,000 area did not in fact satisfy the overall 'trend reaction' correction down to that lower support. While enriching some of the bears, it was less gratifying and more so sort of a giggle on the back of that obvious trading dislocation. As such, a rollover to a more bearish tone from these levels would still signal the more orderly and gradual trend reversal for a test of lower support is still in order. As noted previously interim levels in the DJIA are 10,600 and 10,400 this side of the general 10,000 area support; which now extends down to the panic trading level in the mid-9,800 areas seen last week.

▪ **Beyond that it is mostly about the technical levels in each market, except to note the divergence between Gold and black gold, as in Crude Oil. The only reason that the yellow metal might be as strong as it is in the face of equities weakness is sheer panic. And that further reinforces our view that the general economic signs are indeed either already weakening, are anticipating a turn to the downside as reflected in lower energy prices.** A very smart man once said that all **Gold** is actually Fools Gold, due to the imperative that even the biggest surge in gold prices requires that one sells this otherwise unproductive asset (in fact a cost sink.) It is the only way to take advantage of any gains that might have been achieved during the 'haven' buying which drives the yellow metal higher during inflationary and politically unsettled times. In our experience, it is indeed the case that once the real economic weakness sets in, Gold does indeed fall back markedly. And in spite of the fact that we believe in the case for greater inflation and political turmoil down the road, the market is looking a bit rich right now.

That is for the combined reasons of its technical condition right into what we perceive is the major sea-change in the short- to intermediate-term economic outlook. The **June Gold future** neared $1,250 at the highs yesterday, and that is close to an important oscillator threshold of $150 above weekly MA 41. While at times (most recently in March 2008 and late last year) it has exceeded that overstretched condition to the tune of another $50-$75, it would currently take a weekly Close above 1,280 to convincingly overrun both the oscillator resistance and the chart topping line across the March 2008 and December 2009 highs (which is indeed right into 1,275-80 in the near-term.) That crude oil has weakened markedly just as the Gold pushed up is a clear sign to us the yellow metal surge is panic buying that will be offset if a weaker economic psychology takes hold. And the **June Crude Oil** does seem to reinforce the worst instincts for the economic outlook right into the face of the equities recovery. That it not only failed its higher support around 83.50-82.20 but has seen serial violations of 80.00, 77.50, and now even the 75.00 area would seem to point toward a test of the major pullback lows into the 70.00 area.

- **As we have already discussed the DJIA technical parameters above, what follows is the summary for the key resistance and support levels for the S&P 500 other asset classes:**

June 2010 S&P 500 Future:

RES: **1,166-70;** 1,175; **1,180;** 1,197; **1,206-10; 1,214.50-1,217; 1,225**
SUPP: 1,150; **1,147-42 (January highs);** 1,135; **1,125; 1,105-00;** 1,080

June 2010 Long-Dated Government Bond Futures:

US T-note: RES: **119-06; 120-00; 121-08;** 122-00; **123-16; 125-00; 127-00**
SUPP: 118-00; **117-16; 116-16; 115-24;** 115-00; **114-14;** 113-00

UK Gilt: RES: **116.80-117.00; 118.30-.50;** 119.30; **120.00; 120.50-.82;** 121.50
SUPP: 116.00-.30; **115.00-.30; 114.15-.00; 113.34;** 112.90; **112.00**

Bund: While the major 'haven' bid is gone in the wake of the rescue package plan to fund the weak sisters' bond markets, the strong sister still has a remote potential above the 127.00 area for a major blow off if equities fail key supports on economic weakness.

RES: **126.53-127.00; (oscillator) 129.00; 131.00-.50; 133.40-134.00**
SUPP: 125.60-.40; **124.50-.70; 124.00; 123.00; 122.50; 122.20;** 121.70

June 2011 Short Money Forward Futures:

Eurodollar: RES: **98.80; (oscillator):** 98.95; **99.10;** 99.25-30; **99.50-.60**
SUPP: **98.635; 98.53-.50; 98.44-.42; 98.35-.31; 98.27-.24; 98.15**

Short sterling: RES: **(oscillator):** 98.65; **98.85; 99.15; 99.30; 99.50**
SUPP: **98.45;** 98.35; 98.15; **98.05-.00;** 97.96; **97.91; 97.78-.75**

Euribor: RES: **99.00; (oscillator):** 99.22; **99.35; 99.50-.60**
SUPP: **98.85; 98.65-.63;** 98.58-.56**; 98.50; 98.42;** 98.38; 98.32; **98.28**

Foreign Exchange:

USD INDEX: RES: **.8600; .8700;** .8850; **.8960; .9000-50; .9230-60;** .9400; **.9600**
SUPP: **.8380-.8420;** 8220-50;**.8140-50;** .8075; **.8000; .7950;** .7900;

EUR/USD: RES: 1.2750; **1.2887;** 1.3050; **1.3250; 1.3400; 1.3650-85;** 1.3750
SUPP: **1.2500-1.2450 (incl. oscillator); 1.2330;** 1.2000; **1.1850; 1.1700**

GBP/USD: Both here and in the EUR/USD last week's panic low did not quite reach the true underlying support. As such, it will be very interesting to see whether this market actually closes below 1.4400 and the EUR/USD finishes below 1.2450 if equities weaken.

RES: 1.4750; **1.4850-00; 1.5000-1.4950;** 1.5120; **1.5250;** 1.5370
SUPP: **1.4400; 1.4060-00; 1.3655; 1.3500; 1.3050-00**; 1.2700; **1.23-1.22**

USD/JPY:	**RES:**	93.00; **93.75; 95.00; 98.00;** 99.00; **100.00-.60; 101.45; 103.50-.70**
	SUPP:	91.80; **91.00-90.70; 90.00-89.70; 88.70-.50; 88.15;** 87.00
AUD/USD:	**RES:**	**.9000-.8950;** .9150; **.9250; .9407;** .9500; **.9610-50;** .9700
	SUPP:	.8850; **.8800; .8600-.8550; .8450-00; .8320; .8150; .8000-.7950**
USD/CAD	**RES:**	1.0200-15; **1.0230-50; 1.0300-25; 1.0400;** 1.0575: **1.0700-50**
	SUPP:	**1.0100; 1.0050; 1.0000 (major Negated DOWN Break); .9954**

June Energy and Gold futures:

Gold:	**RES:**	**(oscillator): 1,250; 1,275-85 (topping line); 1,300; 1,320**
	SUPP:	**1,221 (old high); 1,200;** 1,190; **1,165-69 (old gap); 1,142-45**
Crude Oil:	**RES:**	**75.00-74.50;** 76.20; **77.50-.00; 78.80-.50; 82.20-83.50;** 85.00
	SUPP:	73.50; 72.50-.00; **70.00-69.50; 68.50 (Dec 2009 low); 65.00**

We hope you find this helpful.

-Rohr
(www.rohrintl.com)
