



Rockefeller Strategic Currency Briefing[©]

Monday, August 18, 2008
Price Quotes as of 5:00-6:00 am EST
www.rts-forex.com

	SPOT	CURRENT POSITION	SIGNAL STRENGTH	OPEN DATE	OPEN RATE	POSITION GAIN/LOSS
YEN	110.21	SHORTYEN	STRONG	07/23/08	107.84	2.15%
UK	1.8663	SHORT POUND	STRONG	08/04/08	1.9685	5.19%
EURO	1.4735	SHORT EURO	STRONG	07/30/08	1.5603	5.56%
EURO/YEN	162.39	SHORT EURO	WEAK	08/12/08	163.90	0.92%
EURO/UK	0.7893	SHORT EURO	WEAK	07/30/08	0.7868	-0.32%
UK/YEN	205.70	SHORT POUND	WEAK	08/12/08	209.19	1.67%
SWISS FRANC	1.0949	SHORT CHF	STRONG	07/28/08	1.0349	5.48%
C\$	1.0594	SHORT CAD	STRONG	07/28/08	1.0191	3.80%
A\$	0.8709	SHORT A\$	STRONG	07/30/08	0.9479	8.12%
MXP	10.1746	LONG PESO	WEAK	01/31/08	10.840	6.54%

Position Gain/Loss (%) is calculated on the difference between Open Rate and Spot. The Gain/Loss is hypothetical—we do not claim to execute trades at these levels. Note that Gain/Loss does not account for the cost/earning of carrying a position, which can be substantial. It is therefore unrealistic and not comparable to a true Gain/Loss accounting of real-world trades done at the same levels. The purpose of the Gain/Loss entry is to show roughly whether the current forecast is right. **This morning briefing is an information service, not a trading system. All trade recommendations are included in the afternoon report.**

What's Happening This Morning: The dollar performed sedately on Friday, opening in New York around 1.4742 and closing at 1.4701 from a daily range of 1.4757 and 1.4656—not too hot and not too cold. Overnight in Asia, the dollar first made a new highest high (1.4641) but then lost ground to 1.4768, which is a higher euro high than on Friday. A higher high is always worrisome, but the “reason” is said to be pulling back on impending housing and inflation reports this week (Bloomberg). “Traders are adding to bets the US housing slump and widening credit-market losses will keep the Fed from raising interest rates this year.”

Interest rate hikes? The dollar has not been rallying on expectations of rising interest rates. It has been rising despite the near-certainty of rates being held the same. Instead we might look to oil rising on the fear that the latest tropical storm (Fay) will turn into something serious. That was certainly the case in Japan overnight, where the dollar edged back against the yen on rising oil prices. Market News links the dollar drop directly to the rise in oil and other commodity prices during the Asian session. Gold in particular rebounded 1.2%, lifting the A\$ with it.

Offsetting any oil-induced dollar weakness may be tomorrow's ZEW survey of financial experts in Germany, which could easily push the euro down a bit more as the ECB's seeming indifference to growth comes back into the spotlight. Perhaps 90% of the dollar's moves these days is down to oil, but that still leaves 10% for other factors, and relative growth prospects is a category that has to be on that list.

Technical Notes: Everything is bouncing counter-trend a little. The one that might have some legs is the Australian dollar, and don't forget, for reason nobody can figure out, the A\$ leads the euro. The slope of the linreg channels is too steep. It's sensible for prices to correct to create new highs so that the slope gets to a sustainable angle. Conventional wisdom (from Gann) has it that 45 degrees is a good slope.

Separately, see the gold chart. Gold closed at \$786, well under the channel bottom and on an opening gap down. We think it can bounce up strongly, to back inside the channel, even it turns out to be a dead-cat bounce. Gold is not important *per se* but some traders think it always has an inverse relationship with the dollar. This is demonstrably stupid but never mind—if some people think it and others are trying to trade in anticipation of “the crowd,” we will get gold up, dollar down, at least for a few days.



Financial Crisis: We don't have much actual news, so the press is manufacturing some. The front page of the WSJ has a story saying time is running out for Lehman Bros, which will report earnings in about two weeks. It may show a loss of \$1.8 billion or more, according to analysts. Funny, in June everyone said Lehman was toast, but the US disallowed naked short selling and rumor-mongering, and we haven't heard those bells tolling in a while. Oh yes, and Lehman raised \$6 billion in June. This is not to say Lehman is okay or will survive or anything like that, just that some market players are bad-mouthing one of the big Wall Street names.

Recession Watch: We get the housing starts data tomorrow, probably a drop of 9.9% in July for the fewest units in 17 years, according to the Bloomberg survey. We also get the PPI, probably a rise of only 0.5% in July after 1.8% in June. In the US, PPI doesn't feed CPI directly and so it is not considered a policy focus. See the calendar below for other events. Not on the calendar is the 3-day Kansas City Fed beanfest in Jackson Hole, Wyoming. We often get really interesting papers presented on this occasion, not to mention sound-bites.

It was as Jackson Hole last year that Fed Gov Mishkin said a housing crisis is different from all other asset-based crises (like stock market crashes) because it affects consumer behavior more profoundly and in a longer-lasting way. At the time, we actually plowed through the Mishkin paper on your behalf, Dear Reader, and found him more convincing than the self-promoting Roubini (featured in the NY Times Magazine this past weekend).

Unfortunately, both of these guys are missing a key point, that underlying credit woes to a greater extent than ever was simple dishonestly on the part of lender and borrower. We can blame ratings agencies and securitization and accounting rules that allow off-balance sheet accounting, but the paper is rotten because the loans were bad and the loans were bad because a shockingly large proportion of people think the way to win is to cheat. Every generation bemoans the loss of moral fiber of the current generation, but golly, \$1 trillion in losses kind of proves it, doesn't it?

The Main Event: The yield on the 10-year note fell to 3.852% from 3.892% the day before. Fixed income analysts offer a plateful of explanations, including safe-haven buying of US notes and bonds by folks who do not like Russia's behavior. Also, says a Market News analyst, "...while the Fed is doing everything it can to help domestic

Wall Street firms, many cannot figure out why the European Central Bank and the Swiss National Bank are not doing more to offer dollar liquidity to European firms. It is clear that many structured problems are on the books at European houses and the bid/cover on recent TAF auction in Europe show a huge demand for dollars. Yet the dollar funding provided by ECB and SNB is paltry..." If another shoe is going to drop, it may not be in the US.

The Other Main Event: The other main event is reserve diversification, which is expected (by some) as a response to the twin deficits in the US. When will the rest of the world decide the US has too much debt, good markets notwithstanding? The Treasury capital flow reports help a little in seeing how foreigners view long-term portfolio opportunities in the US. The latest data is for June, and shows a drop to \$53.4 billion from a deeply revised \$83.2 billion in May. Forecasters generally thought it would be about \$60 billion, which is about the monthly trade deficit.

The total TICS inflow, which includes short-term securities (12 months and under) rose to \$53.4 billion from a crummy \$12.3 B in May, also revised. And remember, in May and June the dollar was still falling, so clearly foreign investors wanted dollar assets anyway. Strangely, they were still buying Agencies, which includes Fannie/Freddie (\$21.5 billion) as well as regular Treasuries (\$28.3 B) but they were sellers of equities (\$1.8 B). Well, US investors were sellers of foreign equities (\$1.6 B).

TICS expert Woolfolk at Bank of New York notes that the liquidity crisis that caused short-term outflows over the last year seems to have subsided. Another point to notice is that Chinese "net investment into the US fell to \$14.6 B in June from two consecutive monthly records of \$36.9B in May and \$34.3B in April



reflecting increased intervention activity this year.” Third, the world can be divided into “haves” and “have-nots,” with the “haves” dominated by emerging market exporters like China and Brazil, and the oil gang, The ‘have-nots’ have to scramble to get liquidity, and they get it from their dollar “savings accounts.”

Other Markets: The Sept NYMEX crude oil contract hit a new low of \$111.34 and closed down on the day before at \$113.77. This looks lovely on the chart but the update is not to nice—overnight Tropical Storm Fay is over Cuba and causing oil companies to evacuate some deep-water facilities in the Gulf. It will hit Florida if it hits anything. The price rose as high as \$115.35, although it’s back to \$114.16 at 10 am in London. Meanwhile, the damaged pipeline in Turkey will be back in a day or two, although somebody blew up a bridge in Azerbaijan. Separately, Bloomberg reports that commodity investors are fleeing. A Lausanne money manager of \$8.5 billion in commodities said investors are withdrawing some funds after a drop in prices.

Japan: The Nikkei rose 146.04 points, or 1.12%, to 13,165.45, following Wall Street, on bargain-hunting and the weak yen. The NKS writes that conditions elsewhere may be easing and so even if the domestic recession looks bad, the outlook is okay for a country so outward looking. The BoJ starts a two-day meeting tomorrow, but nobody expects any rate changes or even much of a comment, although it may downgrade its assessment of the economy in line with last week’s Cabinet Office assessment. Analysts universally think a resumption of “normalization” of interest rates is stalled as the economy enters recession or near-recession.

One potential bright spot is wages, which rose for the 6th consecutive month in June by 0.4% y/y (after a drop of 0.6% the previous month). It may not be enough to offset higher food and energy prices, with consumers already pulling back from spending. Besides, the gain is due mostly to bonuses, which is a one-time thing that people can’t count on. In fact, the traditional summer bonus fell this year for the first time since 2002, according to the Keidanren.

Europe: The ZEW research institute will publish its index of investor and analyst expectations tomorrow before the US open. It is forecast, according to Bloomberg, to come in at -62 in August from -63.9 in July, the all-time low.

The Bank of France reported that confidence among manufacturers fell to the lowest in 5 years in July, 92 from 95 in June. The forecast was a tamer 94. Slower demand from other EU countries is the cause (and the French trade deficit is growing, having hit a record €5.6 billion in June).

Britain: Rightmove reports that house prices posted the biggest annual decline in August since at least 2002, down 4.8% y/y. Some analysts take this as proof of recession. The British Chambers of Commerce said the economy will be flat or contract in the next two or three quarters. We get the official data on Aug 22. To add to the mix, the FT reports that a survey by Lloyd’s says confidence in the nation’s business prospects fell to the lowest level in at least six years, according to a survey of more than 200 companies. The index of sentiment on the next 12 months fell to 22 in July from 32 in June.

Foreign Affairs Tidbit: The Russian experiment in Georgia is supposedly over, with nobody having a clue as to how much money might have flowed into the dollar on the safe-haven idea. Poland is happy that it had started talks with Nato and it was quick to finalize things last week—it, too, has looked into Putin’s eyes and saw the same thing that neighbors always see in Russian eyes—rape and pillage. In the 1980’s, there was literally not enough food in Warsaw because it was mostly taken to Russia.

We imagine the next meeting of G8 will be interesting. Russia never qualified as Member 8 of G7 in the first place, and while there is something to be said for keeping your enemies closer, its capriciously authoritarian ways are truly, deeply frightening. Assuming there is outflow from Russia, who is the beneficiary? At a guess, Brazil.

Note on Canada: We always joke that we want the US to invade Canada so we don’t have to forecast that darn currency, which we get wrong nearly all the time. The C\$ has been the bane of our forecasting



existence for over 30 years. Sometimes it moves in sync with the US dollar, sometimes it trades as a commodity currency, and sometimes it moves en masse with every other currency. Market News offers some interesting remarks. In Sync? No. “Dollar-Canada, at the peak seen earlier this week around C\$1.0730, was up 18.4% from the 130-year lows near \$0.9060 seen last November. The turnabout lower in the loonie was largely due to contagion jitters due to an expected slowdown in the U.S. economy and the fact that Canada is the U.S. largest trading partner. The U.S. slowdown had clear implications for Canada so much so that the Bank of Canada lowered interest rates in tandem with the Fed, although not always at the same time or with cuts of the same magnitude.

“Now, a month later, with commodity prices tumbling on concerns about less global demand due to a world-wide economic slowdown, it makes sense to see the Canadian dollar come under pressure, traders said. One Canadian dollar trader said a break of the August 2007 peak at C\$1.0865, now viewed as key resistance, would suggest scope for a move to the psychological C\$1.1000 level... Nevertheless, there may be a limit to dollar-Canada's upside, if too many players hop on board the same trade.” The C\$ at parity may be too far. If commodities continue to sell off, the C\$ has to stay under pressure. One trader says “if the U.S. dollar happens to decouple from commodities and rally anyway, the downside for the Canadian dollar may be limited.”

Or, if the US economy is actually rebounding, the C\$ can benefit, too. Or not. From the Canadian perspective, the biggest risk is the US, says another analysts. In particular, the Fed is expected to hike (when it can) while the BoC is seen in cutting more—this is a divergence no commodity can bridge.

Figure it out if you can.

Outlook: It's only normal to expect a pullback in a two-week rally. Prices simply do not move in a straight line indefinitely. We thought we saw it coming last week but it was only the slightest of burps, perhaps because the market is quite thin due to summer vacations. Is it true that the bigger the move, the bigger the correction? Yes, probably, but each one is slightly different and anyone who says it will be 23% or 38% or some other number is full of hot air. A lot depends on the reason for the correction.

Any old reason will do, whether it's a good one that justifies a counter-trend move or not. This time, if it's a temporary rise in the price of oil and other commodities, it will be taken seriously—but those markets have their own dynamics, too. We are still trying to understand why oil fell so hard, and if the oil market traders think those are good reasons, the oil slide will continue. We say that if oil breaches the most recent lowest low from May 1 of \$110.30, the next stop is sub-\$100 and the dollar is golden.

The main economic consequence of falling oil is a reduction in inflation and inflation expectations. That takes heat off the Fed but more importantly, it takes heat off the ECB and thus makes a cut in Q1 a more reasonable forecast. While normally we want to see the Fed in hawkish mode, it also serves to see the ECB is more dovish mode. Note also that falling inflation globally hastens expectations for rate cuts in Australia and the UK.

To think about the bigger picture, consider two pieces of data in one breath—last week it was reported that the eurozone economy contracts for the first time ever since the euro came into existence in 1999. On Friday, the Reuters/University of Michigan index of consumer confidence *rose* to 61.7 in early August from 61.2 in late July. So, correction or not, we want to stay focused on the opportunities for the dollar to hang on to its rally (instead of looking for reasons for it to end).

Wall Street Journal Economic Calendar

Monday, August 18, 2008



1:00p.m. Aug NAHB Housing Market Index: Previous: 16.

Tuesday, August 19, 2008

7:45a.m. ICSC Chain Store Sales Index For Aug 16: Previous: -1.1%.

8:30a.m. Jul Producer Price Index: Expected: +0.4%. Previous: +1.8%.

8:30a.m. Jul PPI, Ex-Food & Energy: Expected: +0.2%. Previous: +0.2%.

8:30a.m. Jul Housing Starts: Expected: -10.9%. Previous: +9.1%.

8:55a.m. Redbook Retail Sales Index For Aug 16: Previous: -1.9%.

5:00p.m. ABC/Wash Post Consumer Conf For Aug 17: Previous: -50.

Wednesday, August 20, 2008

7:00a.m. Aug 16 MBA Mortgage Application Survey Refinancing Index: Previous: -4.2%.

Thursday, August 21, 2008

8:30a.m. Initial Jobless Claims For Aug 16 Week: Expected: -5K. Previous: -10K.

10:00a.m. Aug Philadelphia Fed Business Index: Expected: -13.5. Previous: -16.3.

10:00a.m. Jul Conference Board Leading Indicators: Expected: -0.2%. Previous: -0.1%.

10:00a.m. DJ-BTMU Business Barometer For Aug 2: Previous: +0.1%.

Friday, August 22, 2008

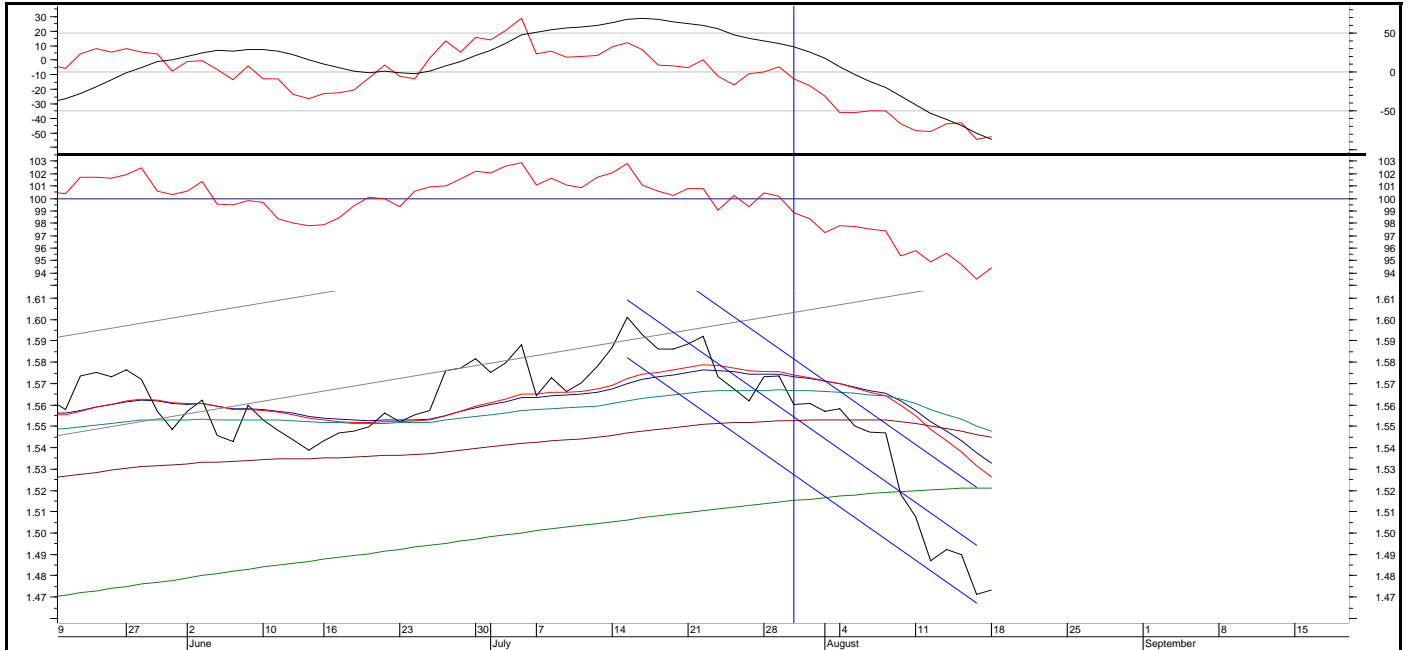
There are no economic indicators scheduled for today.



Chart Legend: Top Box: Relative strength index. Center Box: Momentum. Bottom Box: 5 am spot price in Black. Short-term moving average in Red, long-term moving average in Dark Blue. 55-day MA in Teal. 100-day in Dark Red, 200-day MA in Green. Active linear regression channel in Blue. Previous linear regression channel or competing linear regression channel in Gray. Linear regression forecast in dotted blue. Linear regression alone in double black (occasionally). Key previous high or low horizontal line in Dark Yellow (occasionally). Hand-drawn support or resistance in red (occasionally).

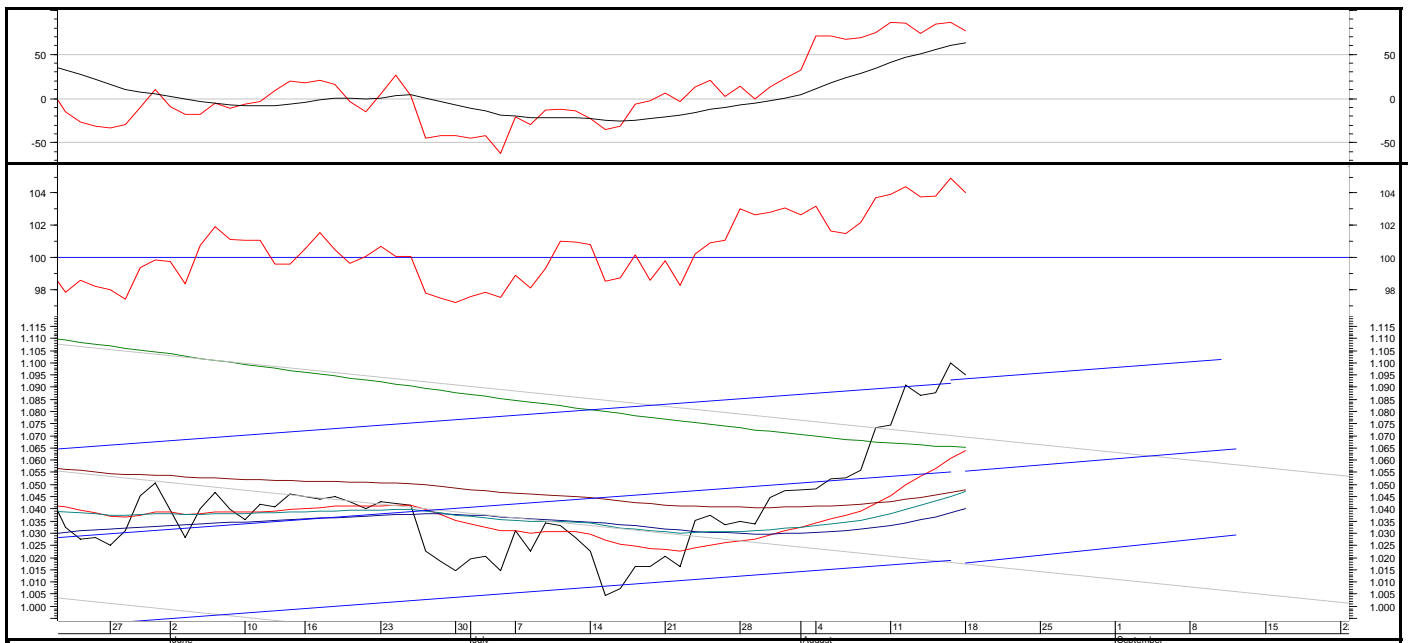
Vertical Blue lines mark dates of signal change from buy to sell or sell to buy. Futures data courtesy of Reuters. Charts prepared in Metastock.

EURO



The euro is bouncing a little. The slope of the channel is unsustainably steep, meaning we need a higher high to flatten it out.

SWISS FRANC



The dollar/CHF is dipping a small amount but remains over the channel top.

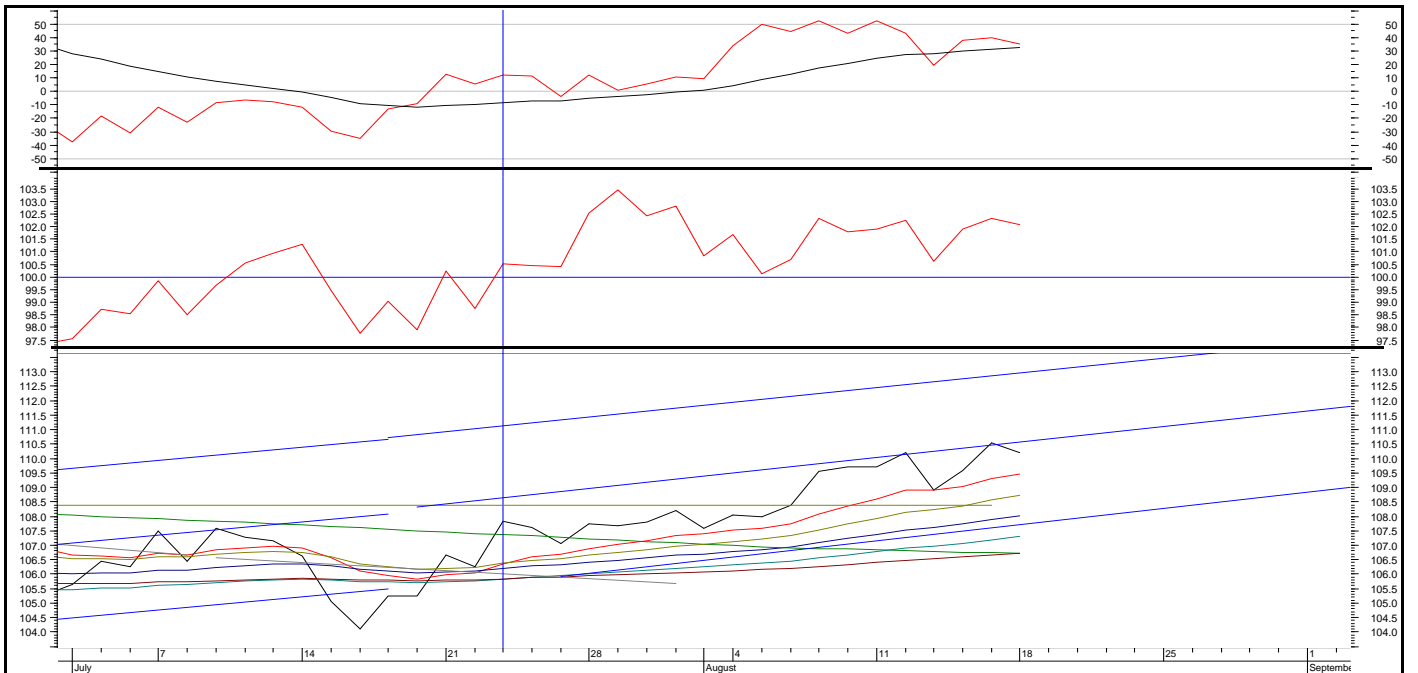


UK POUND



Sterling is hooking upward and really “should” rise to a level back inside the channel.

JAPANESE YEN



The dollar/yen is failing to break the linear regression line (center of channel).

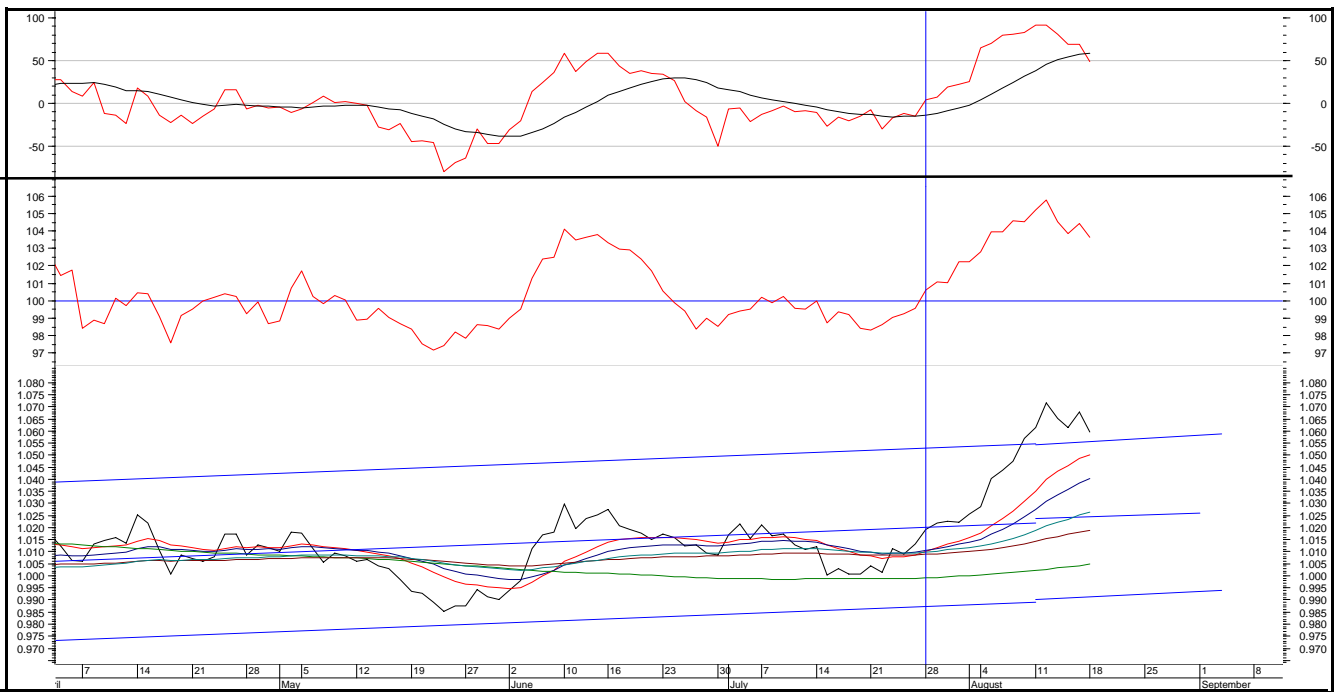


AUSTRALIAN DOLLAR



The A\$ is bouncing up and refusing to match the Jan low.

CANADIAN DOLLAR



The USD/CAD is retreating toward the channel, which is normal.

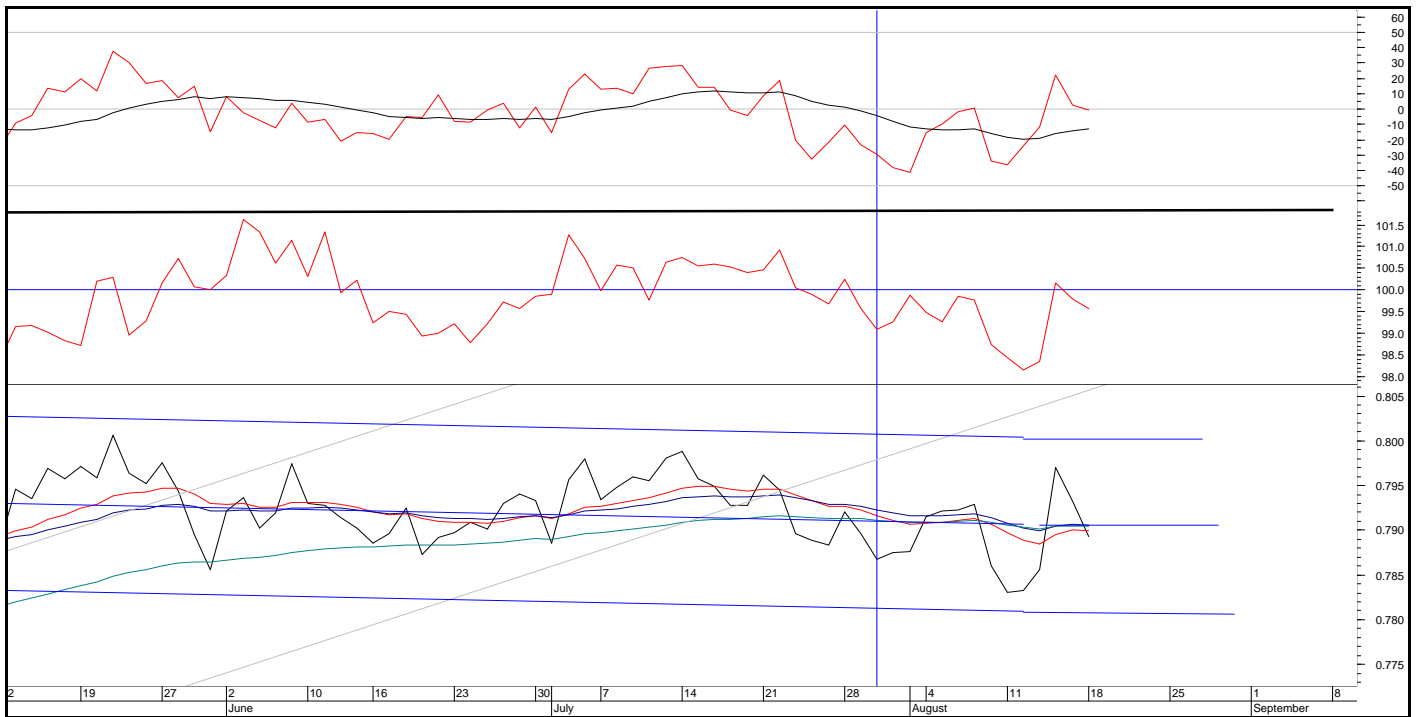


EURO/YEN



The euro/yen is nearing the green 200-day moving average at 162.22 again.

EURO/POUND



Euro/GBP fell under the tangle of moving averages.

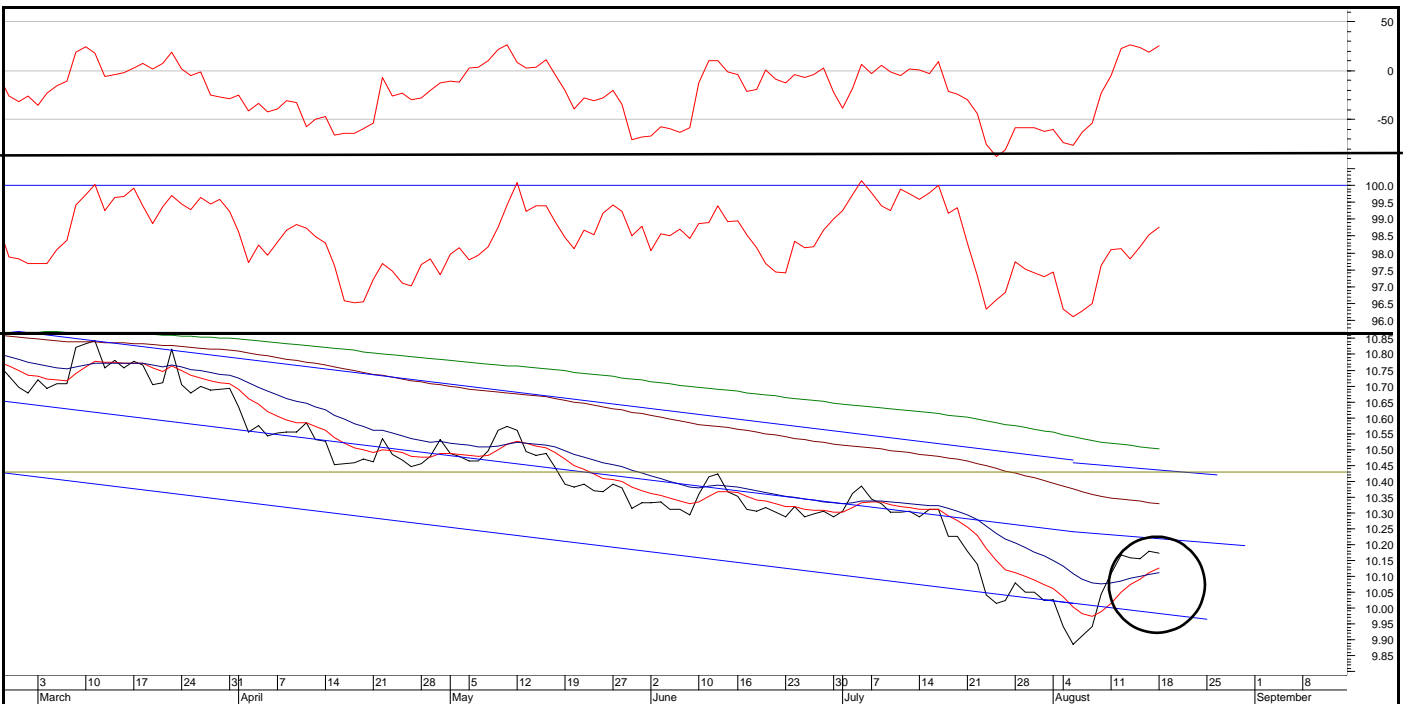


POUND/YEN



The pound is rising just as momentum is bottoming and RSI is rising off the oversold level.

MEXICAN PESO



The dollar is losing some steam without crossing the linreg line. We do have the moving average crossover but that is not enough to buy into a full dollar rally—we need momentum, too.

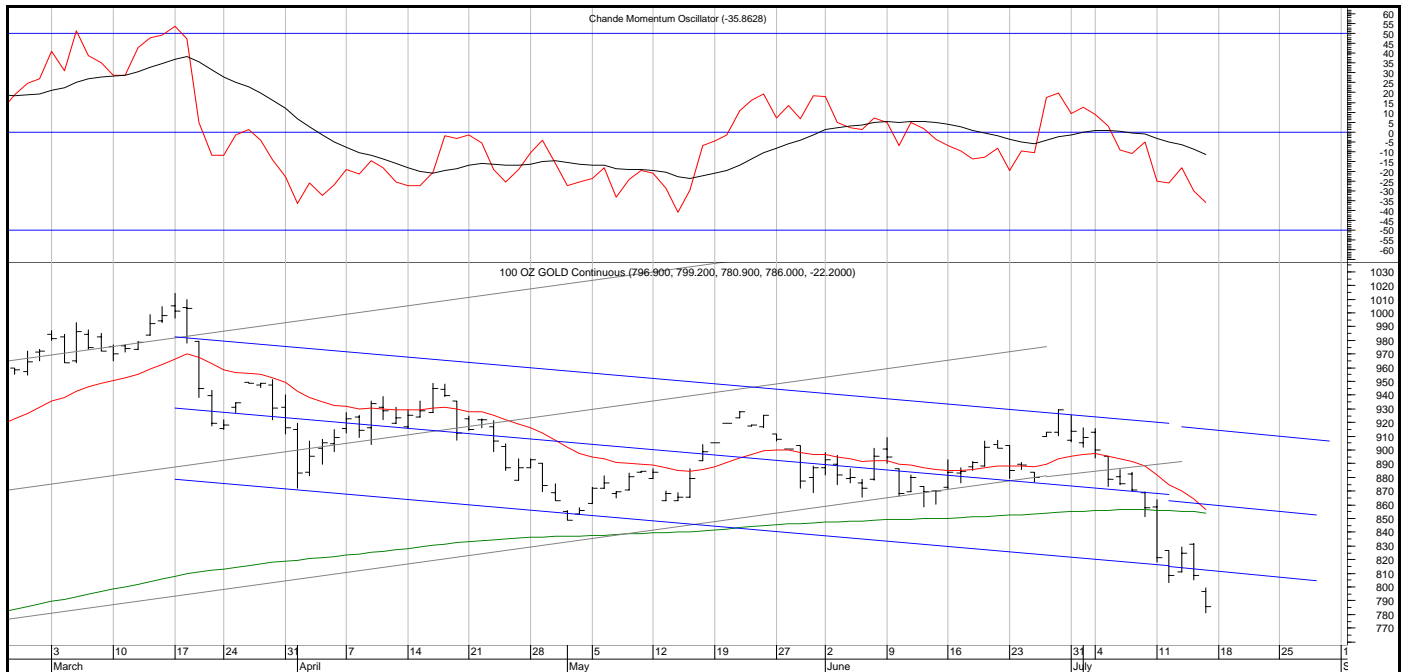


REUTERS 10-YEAR NOTE YIELD INDEX



The index made a new low and we felt forced to draw the downchannel as the primary (blue) one.

Reuters GOLD Continuous Contract



Gold closed at \$786, well under the channel bottom and on an opening gap down. We think it can bounce up strongly even it turns into a dead-cat bounce.

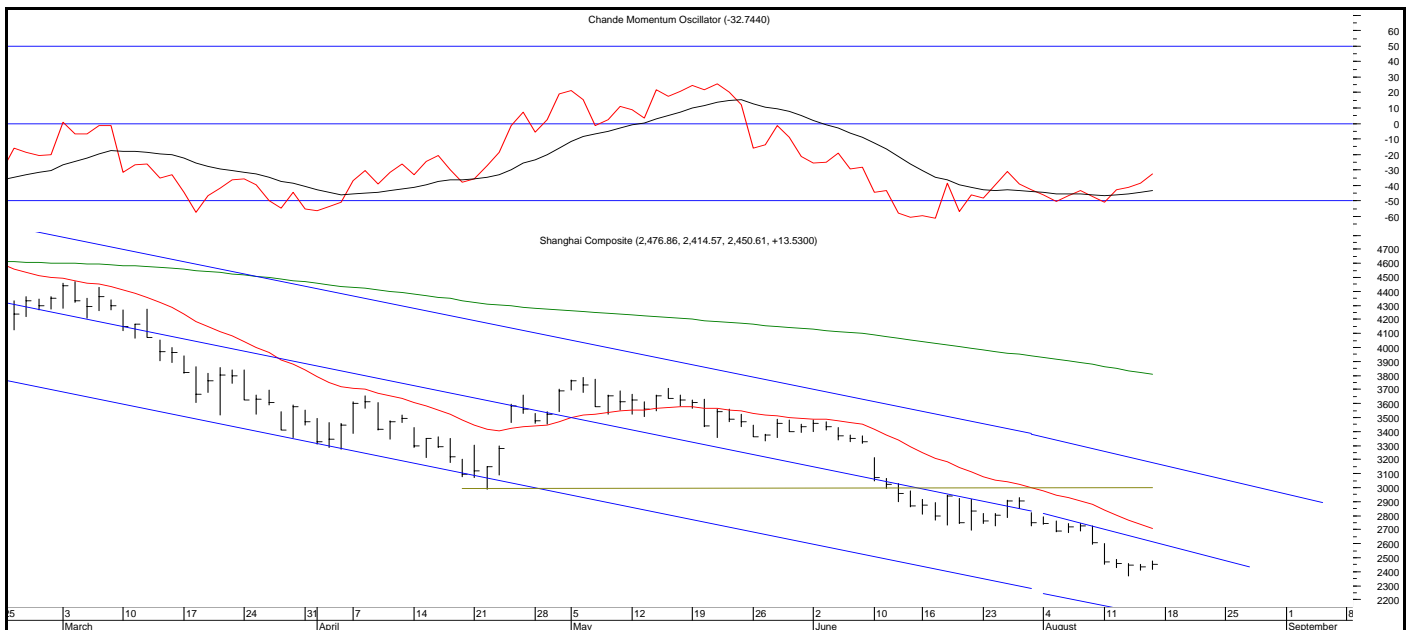


NYMEX Light Crude Oil (Continuous Futures Contract)



Oil made a new low of \$111.34, touching the green 200-day moving average, and closed lower at \$113.77. It is nearing the old low (gold line) from May 1 (\$110.30).

Shanghai Composite



The index is up a little but we have seen a rounded bottom before.