



	SPOT	CURRENT POSITION	SIGNAL STRENGTH	OPEN DATE	OPEN RATE	POSITION GAIN/LOSS
USD/JPY	83.14	SHORT USD	WEAK	12/23/10	82.98	-0.19%
GBP/USD	1.5473	SHORT GDP	WEAK	12/21/10	1.5497	0.15%
EURO/USD	1.3104	SHORT EUR	WEAK	12/21/10	1.3151	0.36%
EURO/JPY	108.97	SHORT EURO	WEAK	12/23/10	108.76	-0.19%
EUR/GBP	0.8468	LONG EURO	STRONG	12/15/10	0.8466	0.02%
GBP/JPY	128.65	SHORT GBP	WEAK	11/24/10	131.33	2.04%
USD/CHF	0.9689	SHORT USD	STRONG	12/14/10	0.9624	-0.67%
USD/CAD	0.9939	SHORT USD	WEAK	12/13/10	1.0086	1.48%
AUD/USD	0.9972	LONG AUD	WEAK	12/14/10	0.9993	-0.21%
AUD/JPY	82.89	LONG AUD	WEAK	12/09/10	82.55	0.41%
USD/MXN	12.2085	SHORT USD	WEAK	12/23/10	12.2995	0.75%

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 FX briefing is an information service, not a trading system. All trade recommendations are included in the afternoon report.**

Executive Summary: The dollar rose strongly on rising 10-year note yields after ADP estimated private sector job growth at nearly triple the other forecasts, 297,000 jobs. Equities and commodities rallied on the idea of a robust US recovery, extending to Japan, where the Nikkei rose 1.44% overnight, led by exporters (and the weaker yen).

What's Happening This Morning: The euro has fallen from the high on Tuesday at the US open at 1.3434 to 1.3088 at 5-6 am EST today, but watch out—it's not a no-brainer move, at least not until it surpasses the last intermediate low at 1.3050 from 12/23. Yesterday the momentum of the downmove leveled out a bit, with the close at 1.3155 from the open at 1.3209, or only about 50 points. In fact, we probably need to suspect a corrective bounce at some point soon—big moves never go in a straight line for long.

Market News notes that the euro edged higher during the Asian session on a press report that China signed a \$7.3 billion deal with Spain. This seems to be a total fiction—see below. It may be noteworthy that German industrial orders rising 5.2% in Nov failed to help the euro.

In the UK, data is first good, then bad, having an exaggerated effect on the pound. The news-driven rate changes are a cause and an effect of a nearly unreadable chart. Technical indicators are about equally divided between buy and sell. The latest is the service sector PMI, down to 49.7 in Dec from 53 in Nov for the first drop since April 2009. Sterling, which was creeping up yesterday in the US session from the open at 1.5447 to 1.5563 at the end of the Asian session overnight, collapsed back to 1.5462.

European Financial Crisis: News is coming in dribs and drabs. Market News reports that Spanish newspaper El Pais says China is willing to buy around €6 billion in Spanish bonds, but without naming names. The story may be a follow-on to the visit yesterday by Chinese Vice-Premier Li Keqiang's to Spain when he told FinMin Salgado that China will continue to buy Spanish debt based on economic conditions. The El Pais report "said that China is willing to buy as much Spanish debt as its combined purchases of Greek and Portuguese bonds. Portuguese media reported in December that China told visiting European officials of a willingness to buy €4 to €5 billion in Portuguese sovereign bonds." In other words, the Spanish newspaper is reporting a deduction



as a news story. The FT reports that after the “awkward” Portuguese auction yesterday, “The negative view of the eurozone peripheral sovereign bond sector show little sign of clearing ahead of a busy month for issuance. The yield on 10-year Spanish paper is up 4 basis points to 5.35 per cent and those of Portugal are up 10 basis points to 6.75 per cent. A €9 bn auction of French long-dated bonds saw reasonable demand, with yields reflecting the move higher in the secondary market.”

Bloomberg seems to be the only news outlet “following” the Irish bank story, noting that back on Dec 14, Soros had said in the FT that the next Irish government “is bound to repudiate the current arrangements.” Soros said the protection of senior bank bondholders is “politically unacceptable” and called for the 5.8% rate to be paid by Ireland on the bailout money, should be lowered to avert the risk of destroying the “political and social cohesion of the EU.”

What story? Yesterday a Soros spokesman declined fresh comment. Moreover, the 5.8% interest rate seems to be wrong. Market News says today “EC chief Jose Manuel Barroso warned that the coming months will be ‘very challenging’ for the euro zone generally as the EU’s executive branch raised the first €5 billion for Ireland’s EU-IMF bailout, the Irish Times reports. The commission said last night that the issuance spread on the loan was fixed “at the tight end of the initial price guidance” at mid-swap plus 12 basis points, meaning it will pay an annual interest rate of 2.59 per cent for the money, the paper says.”

Silly question—why are the newswires reporting what newspapers report instead of going to the sources? Even Reuters notes that “The Spanish government declined to comment on the report. China has been increasing its holdings of European government debt, including that issued by Spain, vice commerce minister Gao Hucheng was quoted separately as saying on Thursday. In a statement on the commerce ministry’s website, Gao also said that China was confident in Spanish and European financial markets and that it was also confident that they would be able to overcome Europe’s debt crisis. Gao accompanied Li on his trip to Spain this week. On Thursday Li leaves Madrid, where he has been on a three-day visit, before traveling to the United Kingdom and Germany. The El Pais report echoes remarks Li made earlier this week but it is the first to give a figure. El Pais could not confirm the 6 billion euro figure with Li, but spoke to Gao, who said that any transaction would be decided on by the date and size of any public debt issue.”

Today the FT reports that an EC commission will report on the proposal for private investor haircuts in bank bonds—not sovereign bonds. We are unclear on how this applies to Ireland, if it does. Ireland is borrowing €85 billion, with €10 earmarked for banks and €25 for reserves. Bloomberg says “Ireland’s bailout money starts to arrive next week, with investors expressing skepticism about the country’s ability to repay its debts by driving the cost of insuring against default to a record.... Irish bonds have rallied since the country secured the bailout on Nov. 28 and as the European Central Bank bought the country’s securities. The extra yield investors demand to hold Irish 10-year bonds rather than the German benchmark has narrowed to 609 basis points from a euro-era record of 680 reached on Nov. 30. That’s still 10 times the decade’s average. The cost of protecting Irish debt against non-payment for five years with credit-default swaps has more than doubled to a record 629 basis points in the past six months, according to CMA prices in London. That implies a more than 40 percent chance that the nation won’t repay investors on time, CMA said.”

National elections in Ireland will probably take place in March. This is the election to which Soros refers—he expected the current government to fall. “Even without the bailout, Ireland’s debt interest payments were expected to consume 20 percent of tax revenue in 2014, rising from 8 percent in 2009, the government said on Nov. 24.”

An opinion piece in the WSJ is probably going to be influential: “A fresh, grisly decline in the euro is seen as a near-certainty as pressure on the currency builds. The euro climbed towards the end of last year, against the dollar at least. But that had nothing to do with a turnaround in sentiment on the common currency, and everything to do with traders unwinding negative bets as they shut up shop for the holidays. But don’t forget that over that period, the euro remained under record-breaking pressure against the Swiss franc, and other regional favourites, such as the Swedish krona. Now, traders and investors are properly back in action, and they’re itching for an excuse to hammer the euro lower against the buck yet again.



“With good reason, too. Despite all the summits, Chinese support, and fine words in 2010, the powers-that-be failed to come up with any permanent solution to the fiscal and debt-related stresses that have pinched some of the euro’s members. No one truly believes that the euro’s crisis of credibility, and some would say, survival, is over.” The writer goes on to say that deflation is the key—if the US falters and deflation gets a grip, the dollar could fall on its own merits regardless of sentiment toward the euro. We say the list of threats to the dollar is much longer than just one entry, including gridlock on restoring fiscal prudence when the debt ceiling comes up for the vote late this quarter.

Eurozone Economy: Data is mixed. Retail sales fell in Nov by 0.8% m/m and 0.1% y/y, the weakest since April last year. The Oct-Nov average is a drop of 0.5%. But economic sentiment rose to 106.2 from 105.1 (revised) in the EC survey, with consumer confidence down to -11 and industry confidence up to 4 from 2. Somehow retail sector sentiment is up to 4.6 from -1.5 in Nov. How can consumer sentiment fall and retail sector sentiment rise?**Equity Markets:** The Dow rose 0.27% and the S&P rose 0.50% on the ADP story. In Japan, exporters led the Nikkei up 1.44% and the Hang Seng rose 0.12%. The Shanghai fell 0.51%. In Europe today, the FT reports the ADP forecast infected everyone—“European bourses have built on initial gains, helping push the FTSE Eurofirst 300 index up 0.9 per cent to its best level since September 2009 as US equity futures point to the S&P 500 advancing further from the fresh 27-month peak notched on Wednesday.”

Other Markets: Oil closed up at \$90.30 from \$89.38 but it back down to \$90.13 at 6:30 am EST. The recovery yesterday is attributed to the ADP forecast of rising payrolls, despite the Energy Dept report that crude oil inventories fell 4.2 million barrels during the latest week, almost double the amount expected. The WSJ notes that there is often a draw at year-end “to reduce their year-end tax bill. They then usually spend the next several months raising inventories. U.S. oil stockpiles have fallen about 30 million barrels over the last eight weeks, according to the DOE. Large builds in gasoline and distillate stockpiles, which coincided with winter storms across the northeastern U.S., outweighed the drop in crude stocks. The DOE said gasoline stockpiles rose 3.3 million barrels last week, with analysts forecasting a 600,000-barrel increase. Stocks of distillates, including heating oil and diesel, rose 1.2 million barrels, bigger than the 500,000 barrels seen by analysts.”

The Main Event: The yield on the 10-year T-note rose to 3.483% from 3.342%, breaking minor upside red resistance.

US Economy: The Fed’s weekly report on commercial and industrial lending is a bright spot—up 2% from the Sept low to \$1.24 trillion at year-end, according to the WSJ. If the trend continues it could imply better jobs growth. Today’s jobless claims may reinforce that idea. Goldman Sachs analysts say “Only six times since 1967 have jobless claims declined as sharply as they have since August... If historical patterns hold, that could put U.S. job creation upward of 180,000 a month in 2011.”

This is in keeping with the new ADP forecast for tomorrow’s private sector payrolls report, a whopping 297,000 jobs in Dec compared to most forecasts of about 100,000 and 92,000 in Nov. It’s the 11th month of gains and job growth is almost entirely in the service sector, according to ADP (270,000). Some silly people are projecting that if the number is right and job growth continues at that pace, the Fed will be hiking rates in no time.

Oh, please. First of all, it’s a forecast, not a true data point. Last time ADP was wildly off, and in fact, ADP is usually wildly off. Analysts say ADP has the best track record of them all but it’s still awful. Secondly, Nomura points out that ADP itself questions the methodology. According to the FT, ADP wrote: “ADP’s National Employment Report estimates a gain of 297 thousand for private payroll employment in December. Can that be right? There are reasons to be suspicious that are related to normal problems with seasonal adjustment.”

The service sector index rose to 57.1 in Dec from 55 in Nov, more than forecast and the 12th month of increases. It’s also the biggest monthly gain since May 2006. But note that the employment component fell to 50.5 from 52.7 and separately, Challenger Gray had reported layoffs likely to be 32,004 in Dec, less than 48,711 in November and the lowest monthly total since June 2000.

Fun Tidbit: The Senate will have the US Constitution read on the floor today. This is supposed to remind everyone that they are engaging in conduct far beyond what the framers imagined. Well, yes. That’s why some of the language is so vague and general—the framers intended the founding document to be amended as



conditions changed, and even did the first ten amendments themselves. But the whole world recognizes that the Constitution was a brilliant idea and it can never do harm to read it again.

Emerging Markets: The “currency war” idea is taking hard form in Brazil, where today the central bank imposed a reserve requirement on banks’ FX positions in the dollar/real, which Reuters names a “bold step to curb the strength of the local currency.... The real BRBY opened 0.6 percent weaker on the local spot market but was later bid only 0.3 percent down at 1.680 per U.S. dollar. Like many attractive emerging economies across Latin America and Asia, Brazil has struggled with currency appreciation that has made its exports more difficult to sell abroad and flooded the country with cheap imports.

“The immediate reaction in Brazil’s currency market was relatively muted given that banks will have three months to get ready for the new rules, meaning there was not a mad rush to reduce positions. [A trader said] ‘It should have a limited impact because the bank gave the market some time to adjust... It won’t necessarily change the trend -- it could hold the market back a little.’ In contrast, when Chile launched a massive dollar-buying plan earlier this week to curb the peso, the country’s currency suffered its biggest one-day plunge in more than 25 years. But the Chilean peso opened firmer for the first time since Monday’s shock announcement, gaining 0.37 percent to 493.20 per dollar on Thursday.”

Outlook: Today we get to evaluate a slew of revised payrolls estimates. Nomura has 165,000. Market News revised to 160,000 and reports the new forecast range is 98,000 to 225,000, but that will change before day’s end. As always, when the actual headline number comes out tomorrow morning, if it’s as ADP forecast, we will probably see profit-taking and thus a dollar drop. In other words, we all know the ADP forecast is for the private sector only but the ADP number gets conflated with the headline number. We could get a giant rise in private that is more than offset by a drop in government jobs... If the headline is worse than the ADP forecast—as it well might be because the Labor Dept headline number includes the government sector—we must expect the usual spike down but then up as the private sector component is judged against the forecast. In short, it’s hard to see how the dollar will not be sold off on the report, so then we have to wonder about buying on the dip.

The bigger story is the half-truths, deductions and lies about China buying European paper. To a certain extent this is China playing cat-and-mouse with the US over the dollar’s reserve currency status. China has the money to rescue all of the Europe, but of course it would be foolish and expensive to do so.

Then there is the ping-pong game of risk-on and risk-off that we have seen this week so far. Risk is back on because of seemingly hopeful signs for the US economy, which is good for things like oil, the dollar and Japanese exporters (and hence the Nikkei) and bad for things like gold, but golly, what happened to the old intermarket correlation assumptions? Oil is “supposed” to drop if the dollar goes up. We are not yet convinced the euro is toast, despite strong evidence in the form of a shockingly large move in such a short time. The first week after the new year is often messy and this one certainly qualifies. Probably the best correction to watch is the AUD, where the fallout from floods in Queensland is probably being overrated. Of course, we are permanently biased in the AUD’s favor so take that idea with a grain of salt.



Daily Morning Chart Package

Chart Legend

Top Box: Chande momentum oscillator (relative strength index).

Center Box: Momentum (today's close divided by the close x days ago) or MACD.

Bottom Box: Previous Trading Day Open-High-Low-Close.

9-day or 10-day moving average in Dark Blue.

20-day moving average in Red

55-day moving average in Turquoise.

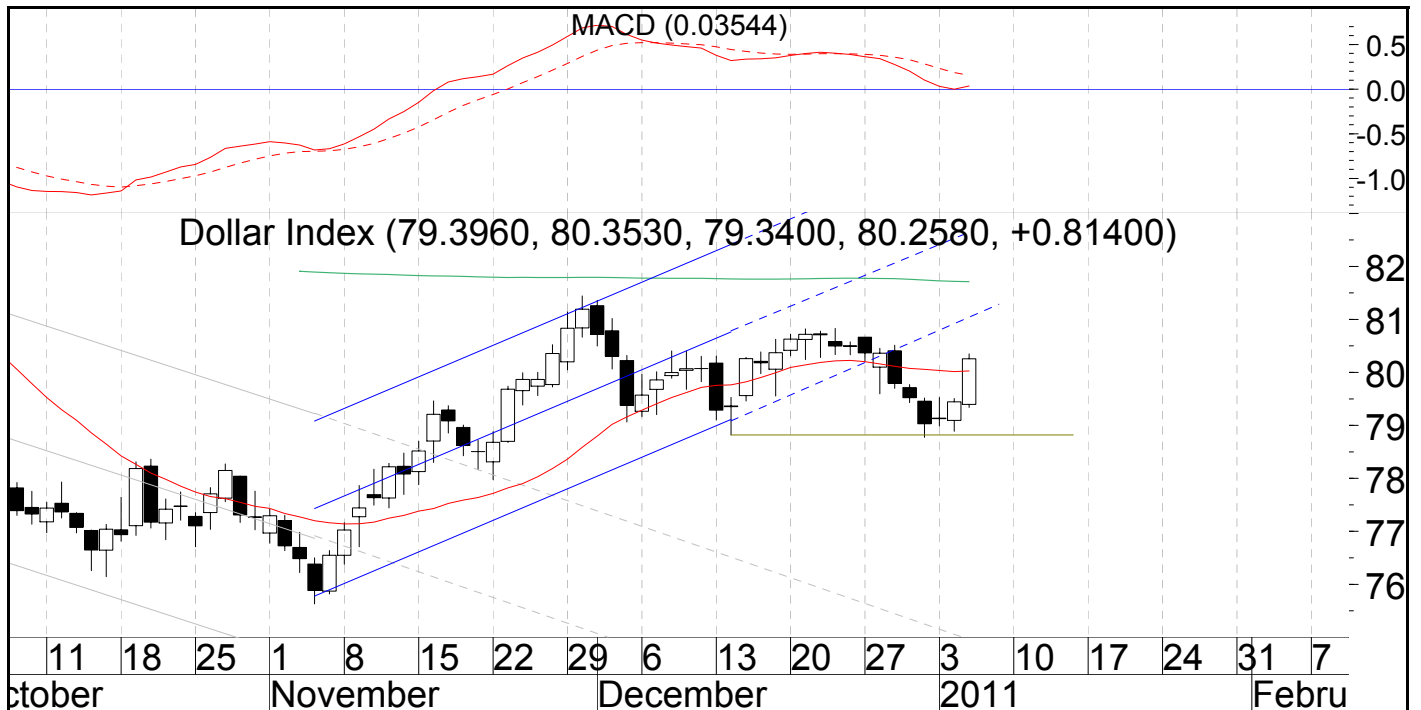
100-day moving average in Dark Red

200-day moving average in Green.

Active linear regression channel in Blue. Previous linear regression channel in Gray. Competing linear regression channel in Red. 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.

Spot data from eSignal at 6 pm close, except EUR, GBP, JPY, CHF, CAD and AUD, whose prices are from 4 pm. Futures data courtesy of Reuters. Charts prepared in Metastock.

Dollar Index



The dollar index put in a big-bar recovery upmove. This can be a pullback from a double bottom or the real deal. The close is over the 20-day, always promising.



EURO/USD



The euro closed lower and under the 10 and 20-day moving averages just as they are crossing to the upside... We restored the downchannel. Note that the euro is still over the green 200-day.

USD/SWISS FRANC



The USD closed higher on another very big bar and closed over the 20-day. It's an upside channel breakout but does not yet qualify for a signal reversal on other grounds.



UK POUND



The pound made a lower low and closed under the 20-day but still over red support. We guess the down-channel will rule but it's a toss-up.

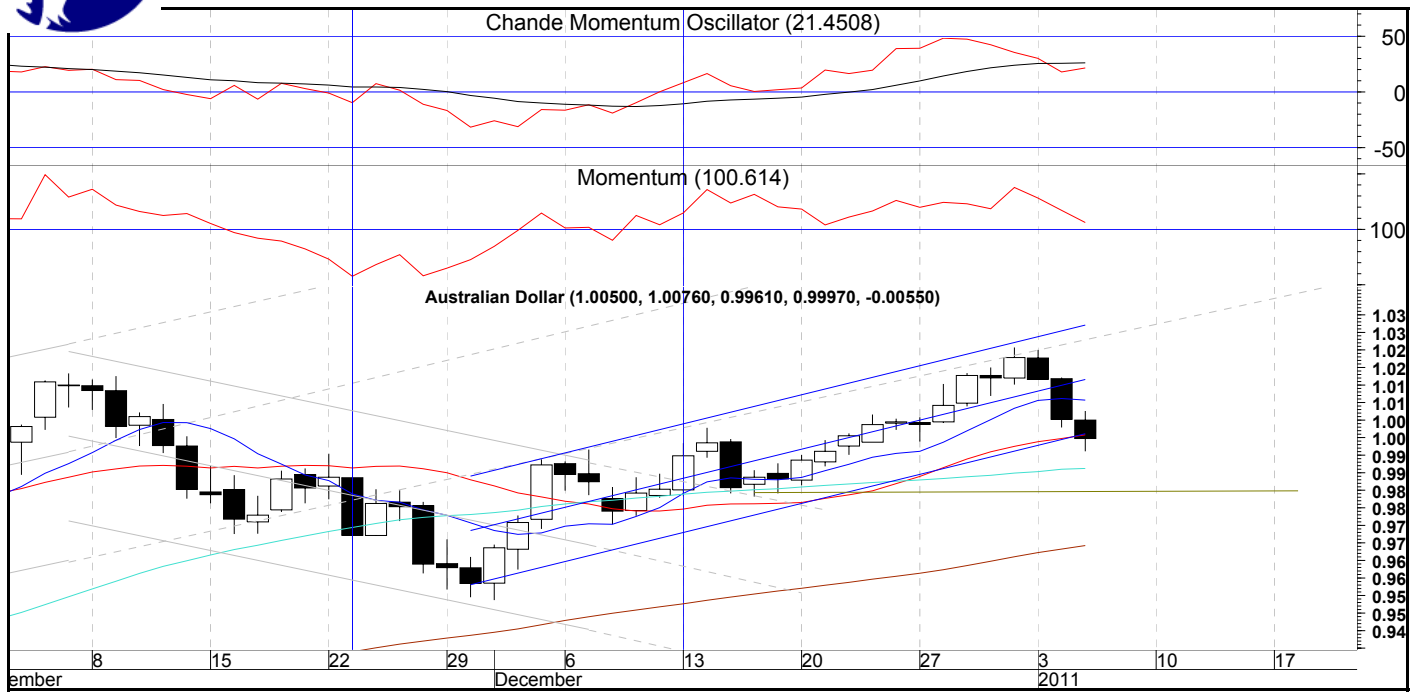
USD/JAPANESE YEN



The USD/JPY closed higher for a third day on a very big bar, and closed over the 20-day. It is near the channel top and it remains to be seen whether it will break out to the upside. Momentum looks promising.



AUSTRALIAN DOLLAR/USD



The AUD closed lower for the third day and under the 20-day, while a little under the channel bottom. This is on the cusp of a reversal signal. The last low is 9832 (gold line).

USD/CANADIAN DOLLAR



The USD closed lower on an inside day and bisecting the old-low line that formed support for months. Momentum continues to fall.

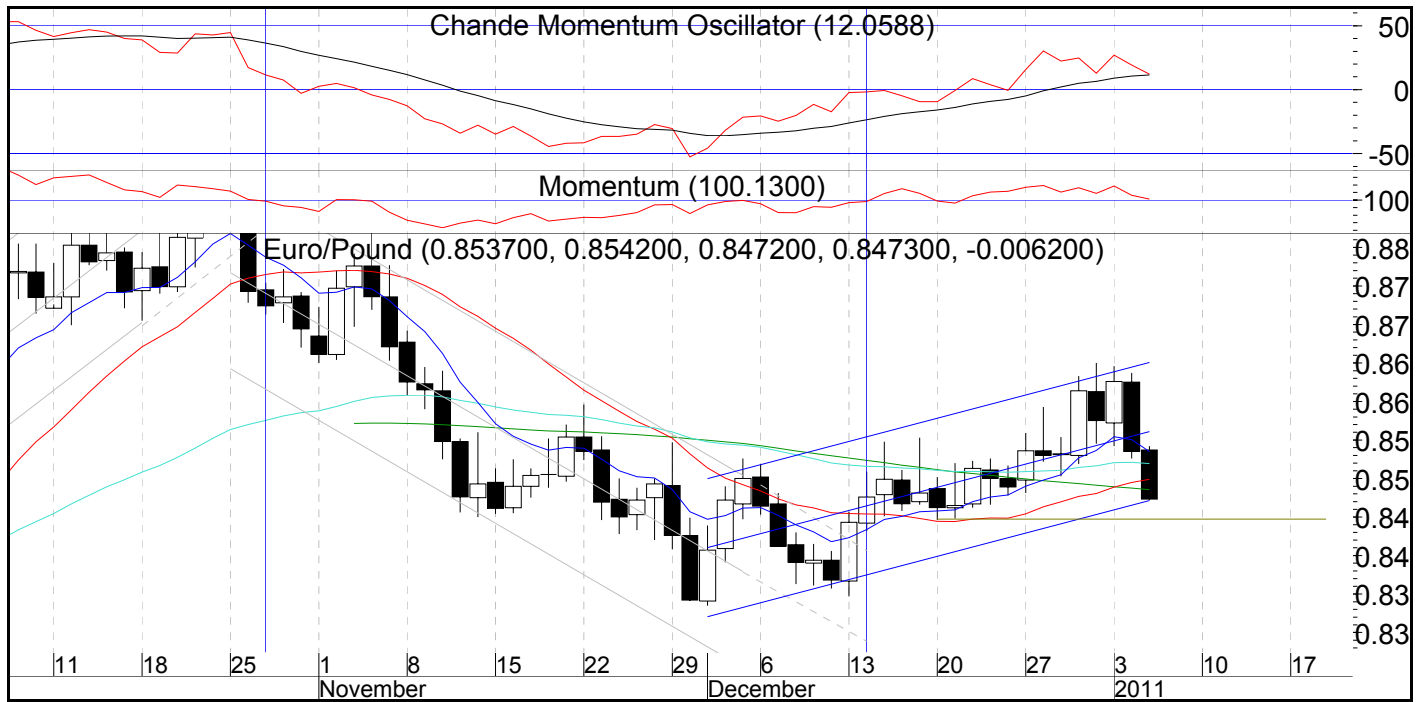


EURO/YEN



The euro/yen closed higher on an inside day with the high touching the 20-day and momentum nearing the crossover point.

EURO/POUND



The euro/pound closed lower for a second day on a big bar. The close is under the 20-day and at the channel bottom. The old low is 8446 from 12/20.



GBP/JPY



The pound/yen closed higher for the 4th day with strongly rising momentum, and at the channel top. A signal change might be coming.

MEXICAN PESO



The dollar made a lower low and closed under the range line.

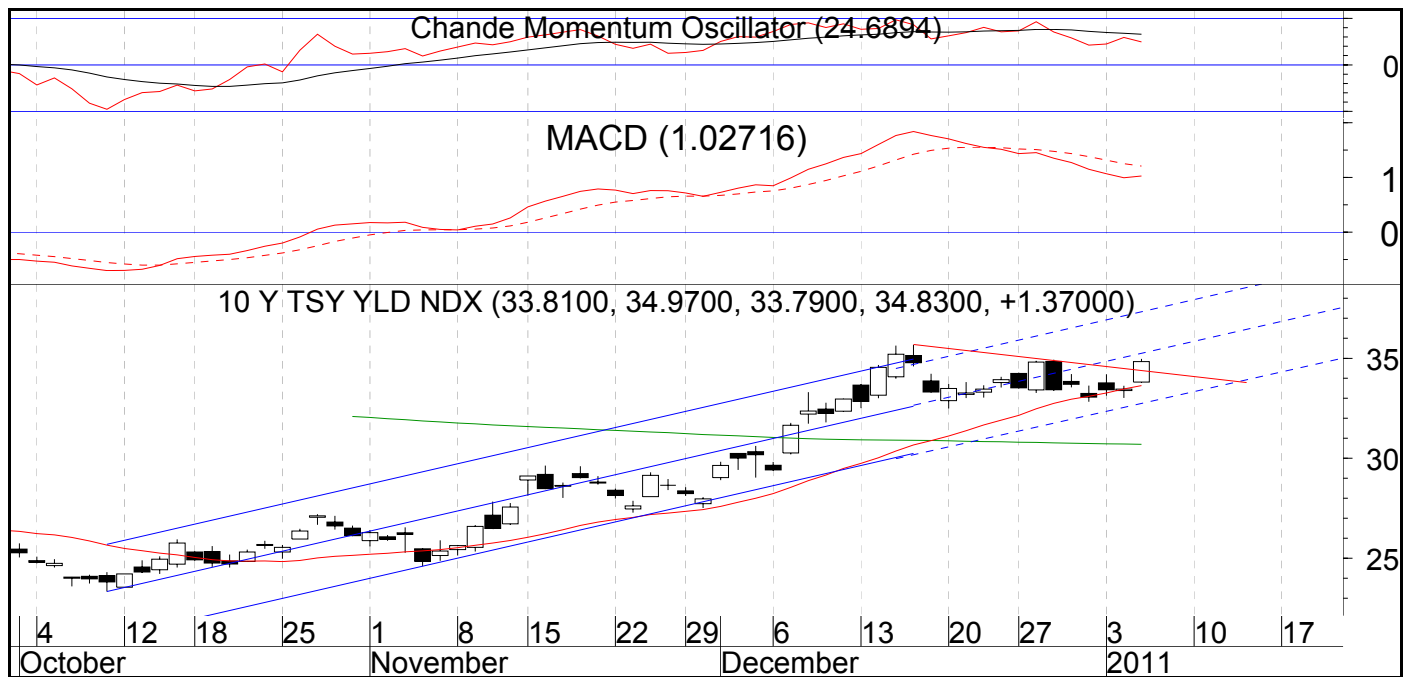


AUD/JPY



The AUD/JPY closed higher, over the 20-day, and on an engulfing bull candlestick. Very messy.

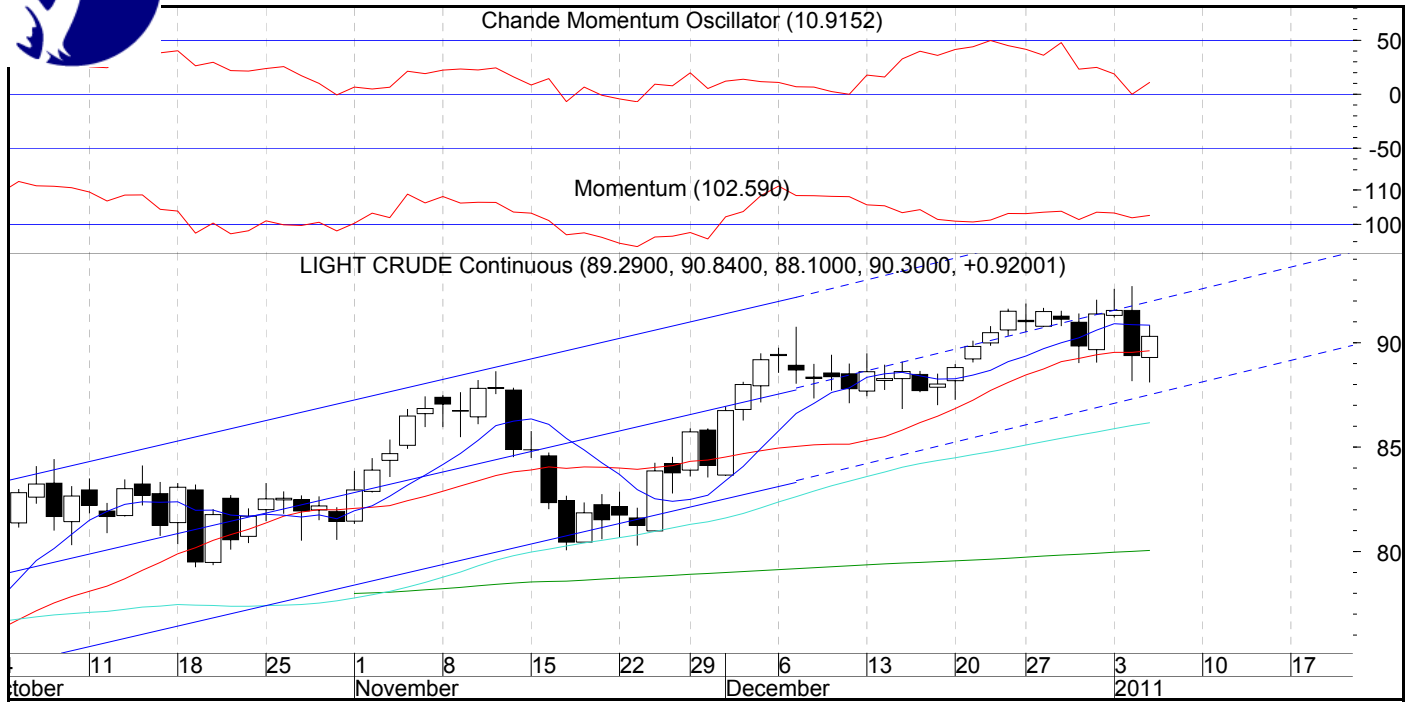
10-Year Note Index



The index closed higher at 3.483% from 3.346% and over the red 20-day and red resistance.



NYMEX Light Crude Oil (Continuous Futures Contract)



Oil made a lower low but closed higher at \$90.30 from \$89.38.

Gold Continuous Futures Contract



Gold closed lower at \$1373.40 from \$1378.50 and under the turquoise 55-day.

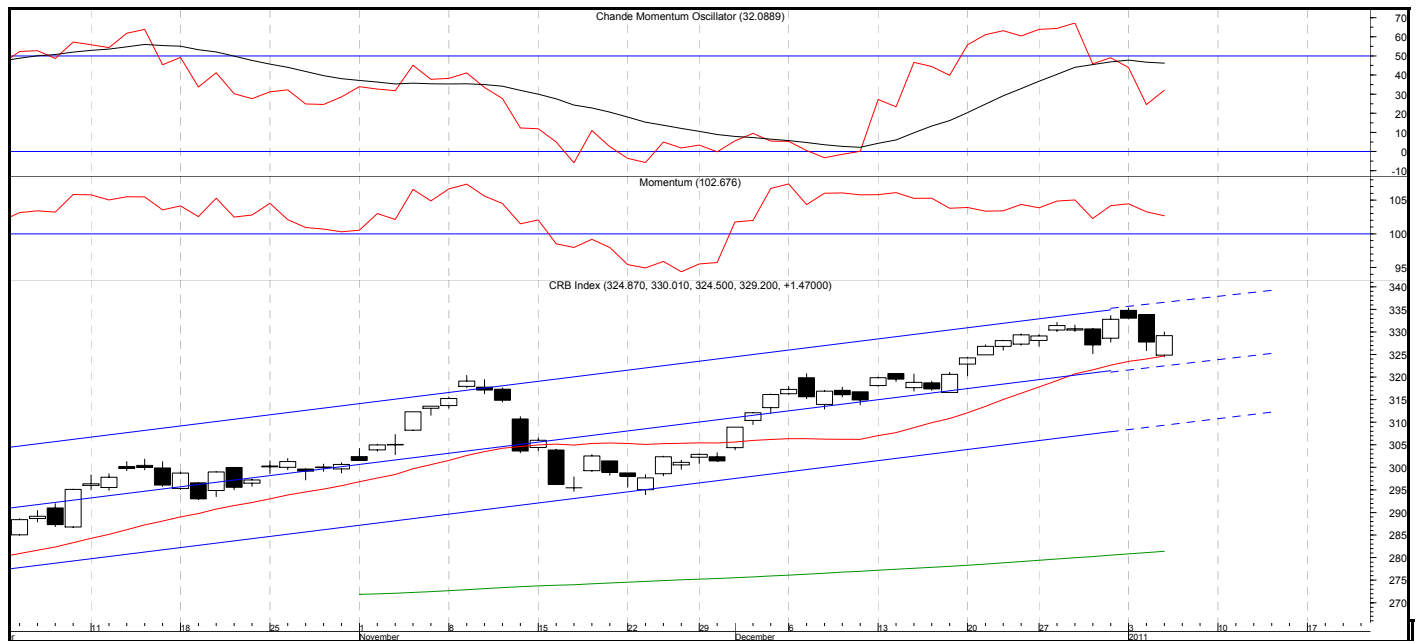


S&P 500



The S&P closed higher at 1276.56 from 1270.20. MACD looks healthier.

CRB Commodities Index



The index closed up at 329.20 from 327.73.