Rockefeller
Strategic Currency Briefing©

Monday, June 1, 2009
Price Quotes as of 5:00-6:00 am EST
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	SPOT	CURRENT POSITION	SIGNAL STRENGTH	OPEN DATE	OPEN RATE	POSITION GAIN/LOSS
YEN	94.67	LONG YEN	WEAK	05/15/09	95.20	0.56%
UK	1.6391	LONG UK	STRONG	03/23/09	1.4538	12.75%
EURO	1.4222	LONG EURO	STRONG	04/30/09	1.3308	6.87%
EURO/YEN	134.65	LONG EURO	STRONG	04/30/09	130.04	3.55%
EURO/UK	0.8675	SHORT EURO	WEAK	04/10/09	0.8974	3.33%
UK/YEN	155.18	LONG UK	STRONG	03/13/09	138.13	12.34%
SWISS FRANC	1.0633	LONG CHF	STRONG	04/30/09	1.1338	6.63%
C$	1.0810	LONG CAD	STRONG	03/23/09	1.2364	14.38%
A$	0.8122	LONG A$	STRONG	03/13/09	0.6585	23.34%
AUD/JPY	76.9000	LONG A$	STRONG	NA	NA	NA
MXP	13.0673	LONG PESO	STRONG	03/17/09	14.200	8.67%

Note to Readers: Today is the 19th anniversary of the RTS Morning Briefing! Thanks to the subscribers who have been with us from the beginning.

Summary: The dollar is falling across the board on the continuing rise in risk appetite, which got a boost from seemingly happy events in US-Chinese relations on TreasSec Geithner's visit to Beijing. See "China" below. The Hang Seng rose a whopping 4%. Still off on the sidelines is an upcoming amendment in Germany that will force fiscal contraction, making the contrast with the profligate US even more stark.

What's Happening This Morning: The dollar is in a terrible rout, with the euro rising from 1.3791 last Thursday to 1.4170 before the close on Friday (at 1.4130). Overnight, it kept going to a new high of 1.4247 after Europe came in, getting awfully close to the technical level 1.4185, which is the 50% retracement of the euro's move down from July's high at 1.6040 to the November low at 1.2329.

Financial Crisis: The Dow closed up at the last minute Friday by 1.15% and the S&P by 1.36%. Everyone finds this very odd just ahead of the GM bankruptcy today that puts the government in the awful position of owning 70%. As the WSJ points out today, the failure puts the government in a "thicket of conflicts" never seen before. "The federal government is likely within weeks to emerge as the principal owner of a storied U.S. corporation whose factories and products touch the lives of tens of millions of Americans. It will simultaneously serve as the company's regulator, tax collector, customer, pension backstop and lender." There's no way this can end well. Meanwhile, Ford is pushing to gain advantage, exactly as a competitor is supposed to do, while Chrylser may emerge from bankruptcy as early as today.

In Japan, the Nikkei rose 1.63% and the FTSE 100 is up 1.34% this morning. Risk appetite was not dented by General Motors. This is a strange development that nobody would have believed even a year ago. The only explanation we can find is that everyone lost so much money is the equity drop during the crisis that risk appetite is voracious, and the GM saga played out over such a long period that it got built in and was anything but a shock.

The FT has a story on how the majority in investors are actually very skeptical about the equity market rebound. A new report by Barclays Capital shows that only "17.5% of the 605 investors interviewed for its quarterly FX investor sentiment survey – including central banks, asset managers, hedge funds and international corporate customers – think risky assets have further to rise." In fact, 6 of 10 say it's a bear-market rally. "Just 4.5 per cent of respondents believe the trajectory of the global economy over the next year will be "V-shaped" – indicating weakness followed by a sharp recovery. The majority, 69 per cent, believe the path of the global economy will be either "U-shaped" or "W-shaped", meaning that growth will remain weak for some time before a gradual recovery begins, or that a recovery will prove temporary and renewed weakness will set in." A large 91% are light or average on holdings, while only 9% have positions they term "large" or "at limit."

Crisis Fallout

In the US, the Q1 GDP revision was to –5.7% from –6.1% in the earliest of the releases, but while better, this was not as good as the -5.5% forecast, and thus a negative. Exports were higher than originally reported but consumer spending was revised down. Corporate profits rose 3.4% q/q after falling 16.5% in Q4.

The May NAPM-NY Business Conditions Index rose to 361.6 from 356.0 in April, with current conditions up sharply to 61.3 from 28.3 in April and the 6-month outlook up to 56.1 from 51.2, the first monthly gain since January 2008. But the May Chicago purchasing managers index slipped to 34.9 from 40.1 in April and against 42 forecast. New orders fell to 37.3 from 42.1 and employment fell to 25.0 from 31.8 in April.

The final May University of Michigan consumer confidence index increased to 68.7 from 67.9 and more than 68 expected. Current conditions rose to 67.7 from 66.2, expectations rose to 69.4 from 69.0, one-year inflation expectations rose slightly to 2.8% from 2.6% and the 5-year inflation expectations rose to 2.9% from 2.8%. Hmm, the survey respondents don't fear inflation, how curious.

In Japan, average monthly total cash earnings per regular employee fell 2.5% y/y in April, which marks a deceleration from -3.9% in March, although it's the 11th drop in a row. In real (inflation-adjusted) terms, the average total wage fell 2.4% y/y from -3.7% the previous month), down for the 15th consecutive month, according to Market News.

Global Recovery

Both the Japanese and Chinese stock markets were cheered by good data from China that may indicate recovery on the way. According to Market News, "The semi-official CFLP PMI dipped in May but suggested that China's manufacturing sector continued to expand last month despite widespread fears of a contractionary reading. The PMI produced jointly by the China Federation of Logistics and Purchasing (CFLP) and the National Bureau of Statistics slipped to 53.1 in May from April's 53.5, the first fall since the record low seen last November.

"Meanwhile, brokerage CLSA reported that its PMI suggested the pace of the expansion of the Chinese manufacturing sector picked up slightly in May, building on the signs of recovery seen the previous month following the dramatic slump in economic activity at the end of 2008. The Hong Kong-based brokerage said that the headline CLSA China Purchasing Managers' Index rose to 51.2, a slight increase on April's 50.1, which was the first reading above the 50 break-even point since July 2008."

In the eurozone, the May manufacturing PMI rose to 40.7, a 7-month high from 40.5 in the flash estimate. France got 43.3 from 43.2 in the flash, while Germany got 39.6 from 39.1 and Italy, 41.1 from 37.2 in April, the biggest monthly rise ever, according to Market News.

Policy Response

In Germany, a constitutional amendment is in the works (to be voted on July 12) that will limit the 16 regional governments from running fiscal deficits and limit the structural deficit of the federal government to 0.35% of GDP by 2016. The FT reports that FinMin Steinbrueck says this is a historic change in the management of the German economy, which is almost an understatement. Elections will be held Sept 27 and the incoming government will have to scramble to "plug the holes." This year, the deficit will be multiples of the new "debt brake." A "ruthless crackdown" could be coming.

Note that in the US, according to the Congressional Budget Office (the closest thing we have to a neutral source), the US deficit will be 12% of GDP this year and gross debt will be over 100% of GDP by 2017 (not counting unfunded liabilities in Soical Security and Medicare). Never was the contrast in political will and probable economic outcomes so stark. If Keynes is right, economies need deficit spending to bootstrap their way out of recessions, so we would havr to guess the US will get bigger and faster growth. But nobody will beat the Germans on fiscal rectitude. What does that mean for the euro?

The Main Event: The yield on the 10-year note closed down at 3.465% from 3.672%. See the chart—the drop is horrendous. A drop in yield, of course, means a rise in price. Market News reminds us that the Treasury auction schedule from the quarterly refunding statement on April 29 is for $481 billion in Q1, $361 billion in Q2, and $515 billion in Q3.

Other Markets: The oil futures contract closed at $66.31 from $65.08 and is at $68.10 at about 7 am ET, for reaosns that defy sanity. We know supply is overflowing and total global demand is down, except for China, so what's going on?

China: TreasSec Geithner, speaking in China, positioned China as an equal to the US in terms of leading the world out of recession. He said a sustained global recovery depends on the combined efforts of the US and China to overhaul their economies. We're pretty easy-going about this kind of thing, since we knew he was going to tickle the Chinese under the chin, but we find it a shocking statement, and the FT treats it as the top story of the day by placing it first on the home page of the FT website. We say the FT is right—it belongs there.

Geithner said "How successful we are in Washington and Beijing will be critically important to the economic fortunes of the rest of the world." Perhaps it's a ploy--Geithner seems to be giving China equal status with the US in return for being able to make normally unpopular remarks about greater flexibility in the Chinese FX regime.

Certain implications come immediately to mind, like the Fed being under pressure to manage bond yields and the Treasury at pains to manage the dollar to avoid displeasing China. And yet we thought the Fed wanted bond yields low to nurture the housing market recovery while many believe that inflation is both necessary and unavoidable to goose the economy, and that's a dollar negative without a correspondingly higher yield. You can't really do both. Congress got left out of the equation entirely, and those egomaniacs never like that, while Japan is probably fuming, if politely. On the bond/dollar front, it's interesting that so far none of the implications have hit home.

Not to stretch the point, but a newish hedge fund loosely associated with Black Swan's Taleb is betting on a return of 1970's-style hyper-inflation by betting on "options tied to commodities such as corn, crude oil and copper, as well as options on stocks such as oil drillers and gold miners," according to the WSJ. Speculation-driven rises in these prices are bad for China, which has to pay for them, too, but good for China in that inflation drives consumers to spend more and spend it faster on the goods that China exports to the US, which may someday soon include autos. But at the same time, hyper-inflation would drive the dollar and bond prices down, bad for holders of dollar-denominated reserves. The one good thing about the outlook for this hedge fund is that neither Taleb nor his former partner running the thing have ever actually made any money as investment managers.

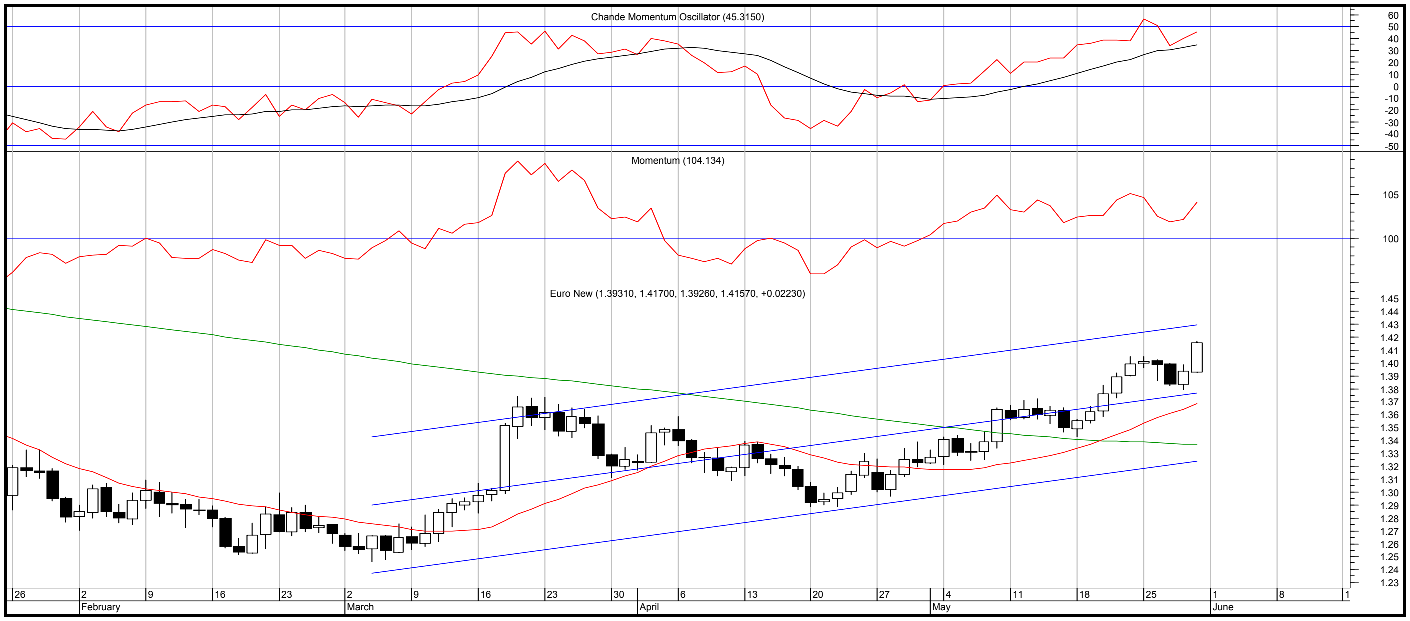
Outlook: Data on the US economy may be taking a back seat to Big Picture analysis, especially the outlook for massive debt issuance and its implictions for the reserve status of the dollar, whatever canoodling Geithner is doing with the Chinese. The Chinese are very, very smart—smarter than the US in these matters, or at least more coherent. They have to like US support for bigger Chinese particiaption in global financial institutions and the like, but they are not going to sell their birthright for a mess of pottage. They will not be deaf, for example, to the S. Korean announcement last week that the country is diversifying away from the dollar—and the US military is what defends S. Korea!

This week we get a lot of data but the biggie, as always on the first Friday of a new month, is payrolls. Nobody is expecting a respite from gloom and doom on this front, with the Market News estimate at a loss of 530,00 jobs in May, with a forecast range of -625,000 to -495,000. The unemployment rate is expected to rise to 9.2% in May from 8.9% in April. We get the ADP Macro estimate for the private sector component on Wednesday. If Market News is right, the May number will be less bad than April (-630,000) but still a horrific number, so can it be good for the dollar on the FIFI growth story? Well, no, not really, although by then the market may be interested in getting a little less short dollars, so it could appear that way.

We respect technical limits like the 50% retracement level (1.4185) named above, but we respect market sentiment even more. Just when you think a currency has gotten overbought and toppy, more players come on the scene. We think the dollar will pull back a little as it always does after a gigantic rout like last week's, but we see no reason for the market to change its mind. It's not yet a dollar "crisis" because nobody is calling it that yet, but in reality, it is a crisis, and for the same reasons we have seen before—giant deficits, potentially impending inflation. The market is asymmetric in its treatment of the news when the dollar is on the defensive, like now—bad news is exaggerated and good news gets brushed off. We would not be surprised to see 1.4750-1.5000 in the near future.

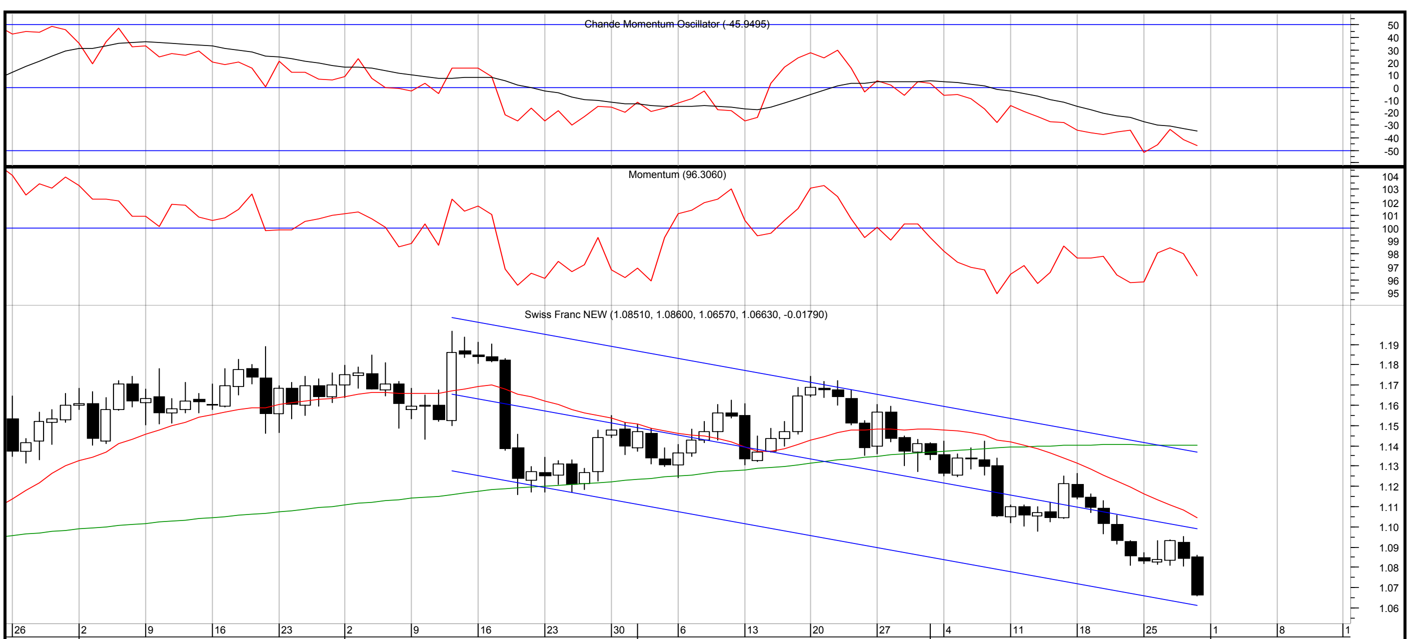
Chart Legend: Top Box: Chande momentum oscillator, which is a relative strength index. Center Box: Momentum. Bottom Box: Previous Trading day price. Short-term moving average in Red, long-term moving average in Dark Blue. 55-day MA in Teal. 100-day in Dark Red, 200-day MA in Green. Active linear regression 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/USD



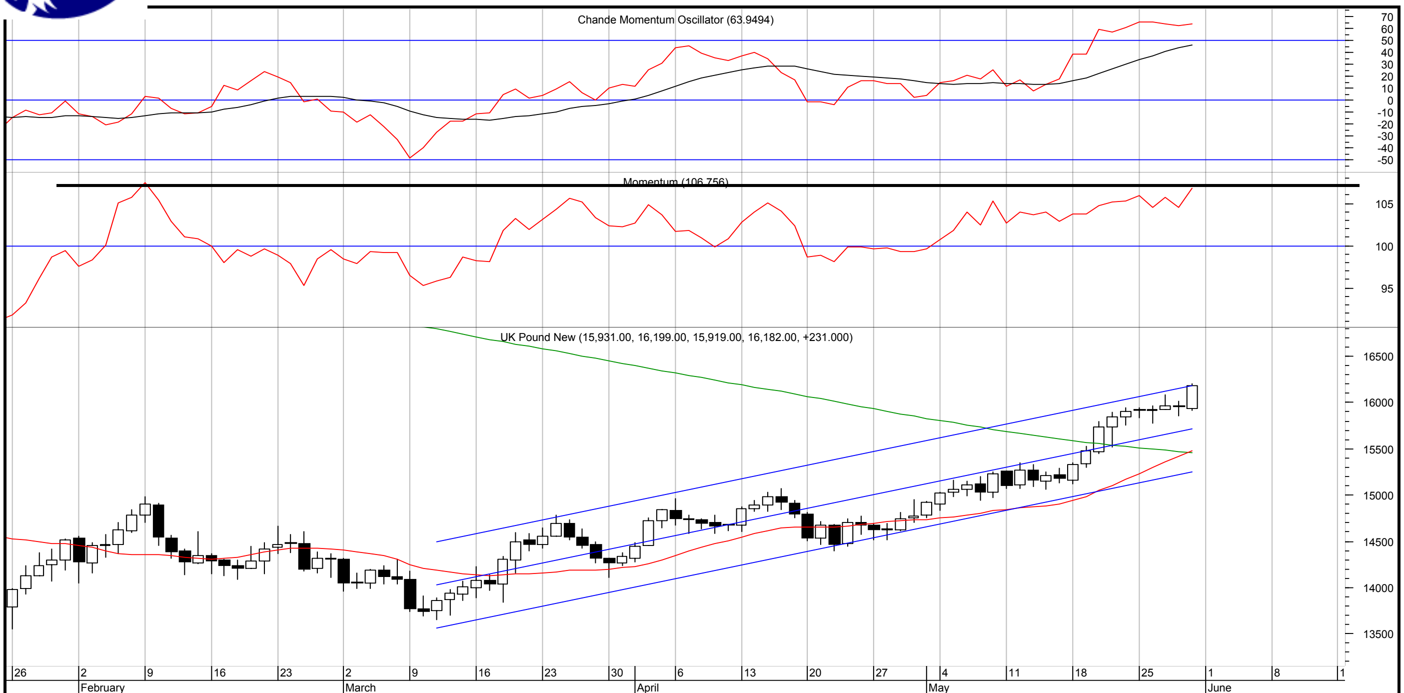
The euro made a giant move up on Friday.

USD/SWISS FRANC



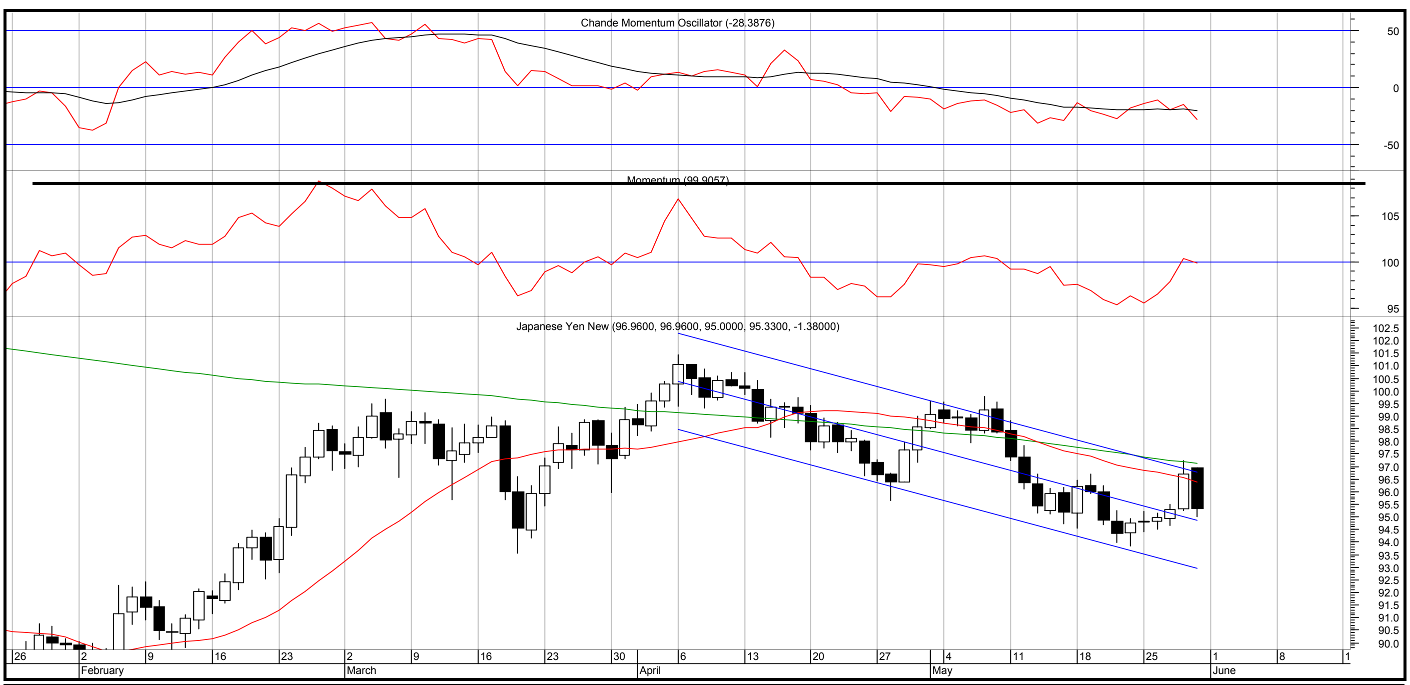
The dollar is running away to the downside.

UK POUND



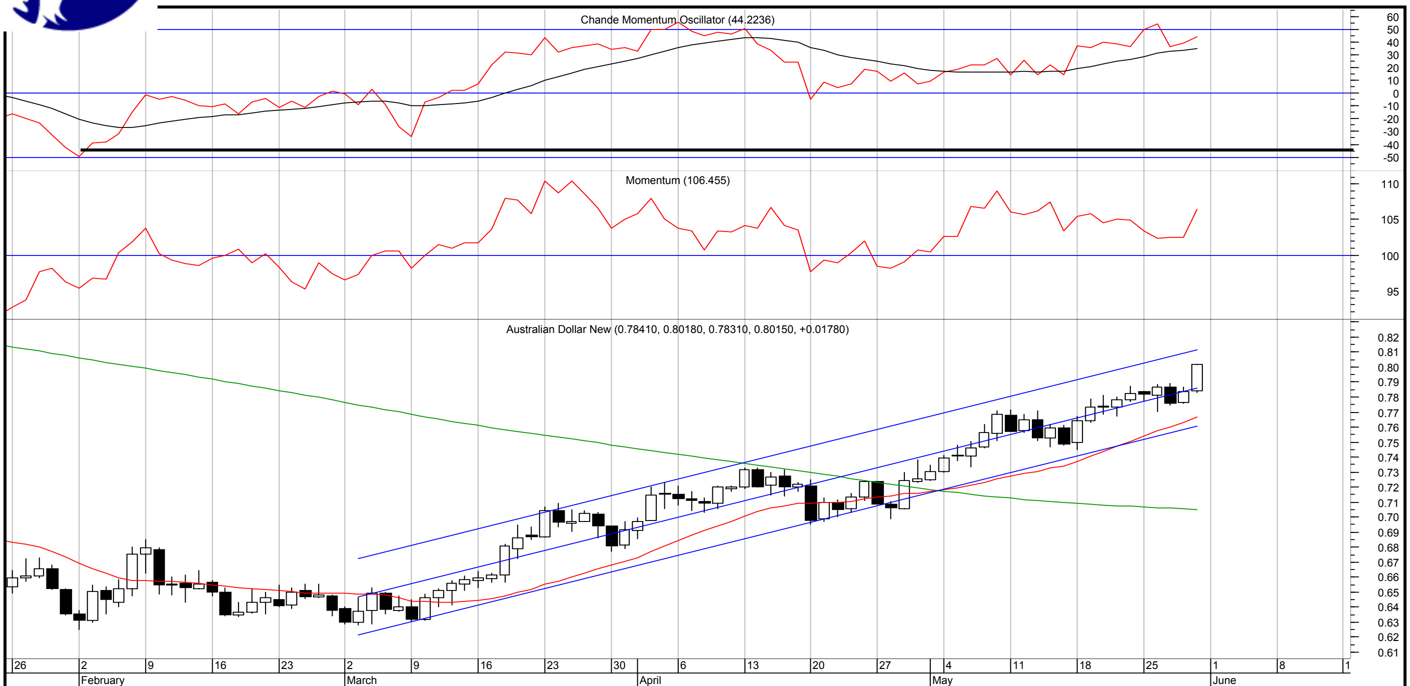
The pound is overbought.

USD/JAPANESE YEN



The dollar/yen is confusing—a big day up and then an equally big day down.

AUSTRALIAN DOLLAR/USD



The A$ is on a runaway rally.

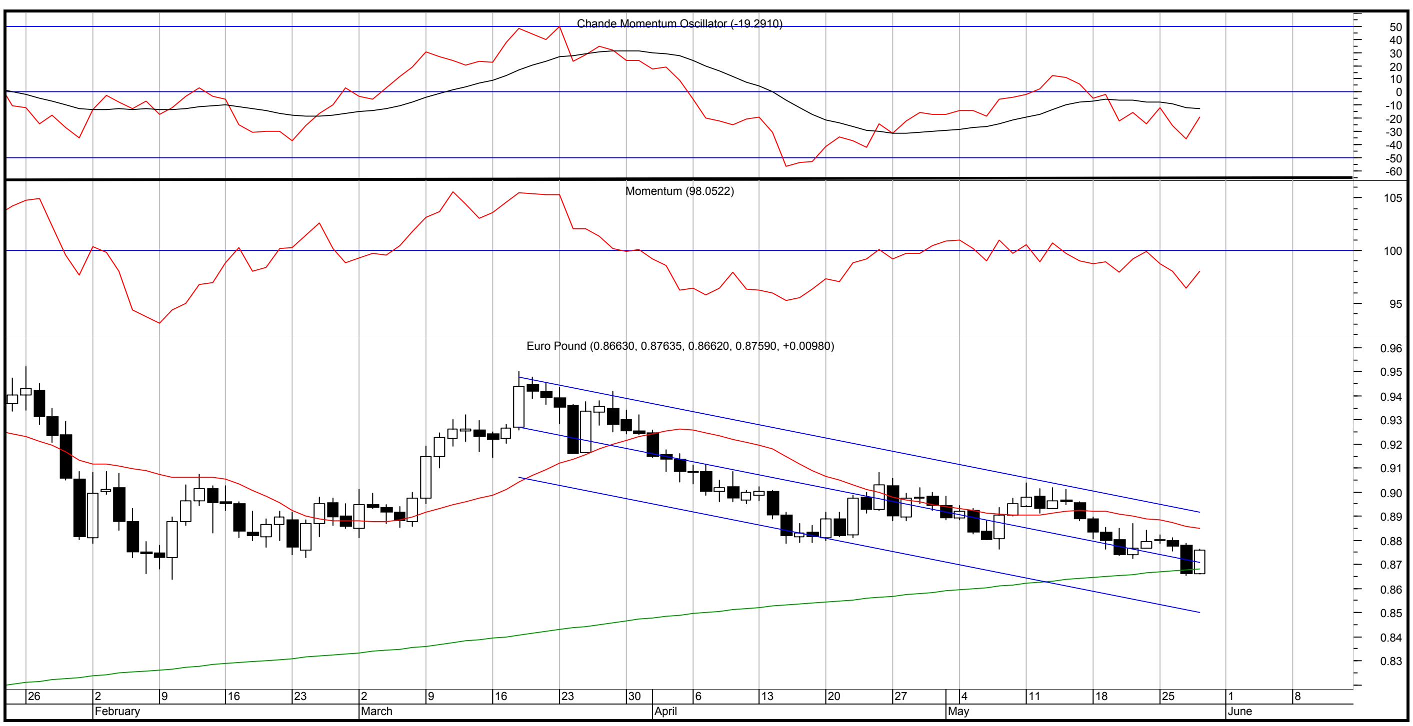
USD/CANADIAN DOLLAR

The USD/CAD is getting oversold.

EURO/YEN

The euro/yen is on the linreg but with no real body and a doji bar, meaning indecision.

EURO/POUND



The euro made a lower low but a terrific close, hence the rise in momentum and RSI.

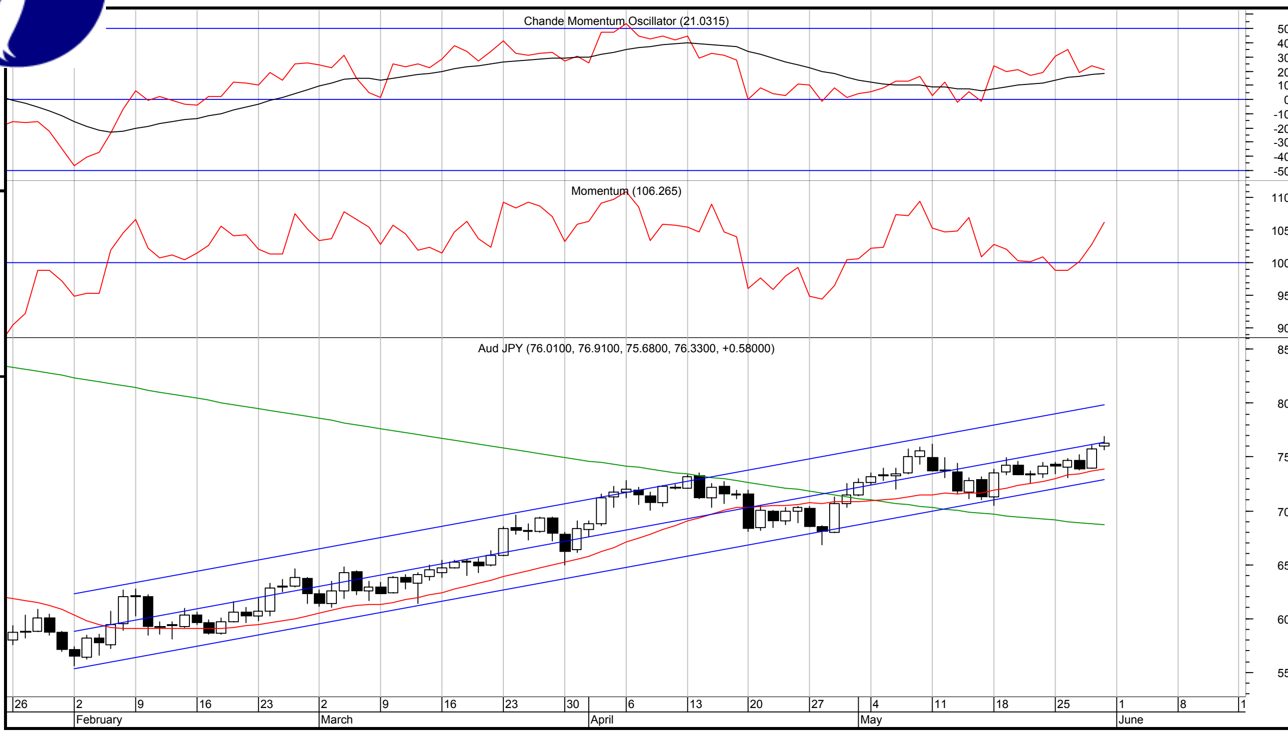
GBP/JPY

The pound/yen put in a higher high but a doji bar.

MEXICAN PESO

The dollar/peso is making an effort to rally and is pressing against the hcannel top.

AUD/JPY



The AUD/JPY is on the linear regression but put in a doji bar on Friday (open and close about the same), meaning a lack of decisiveness.

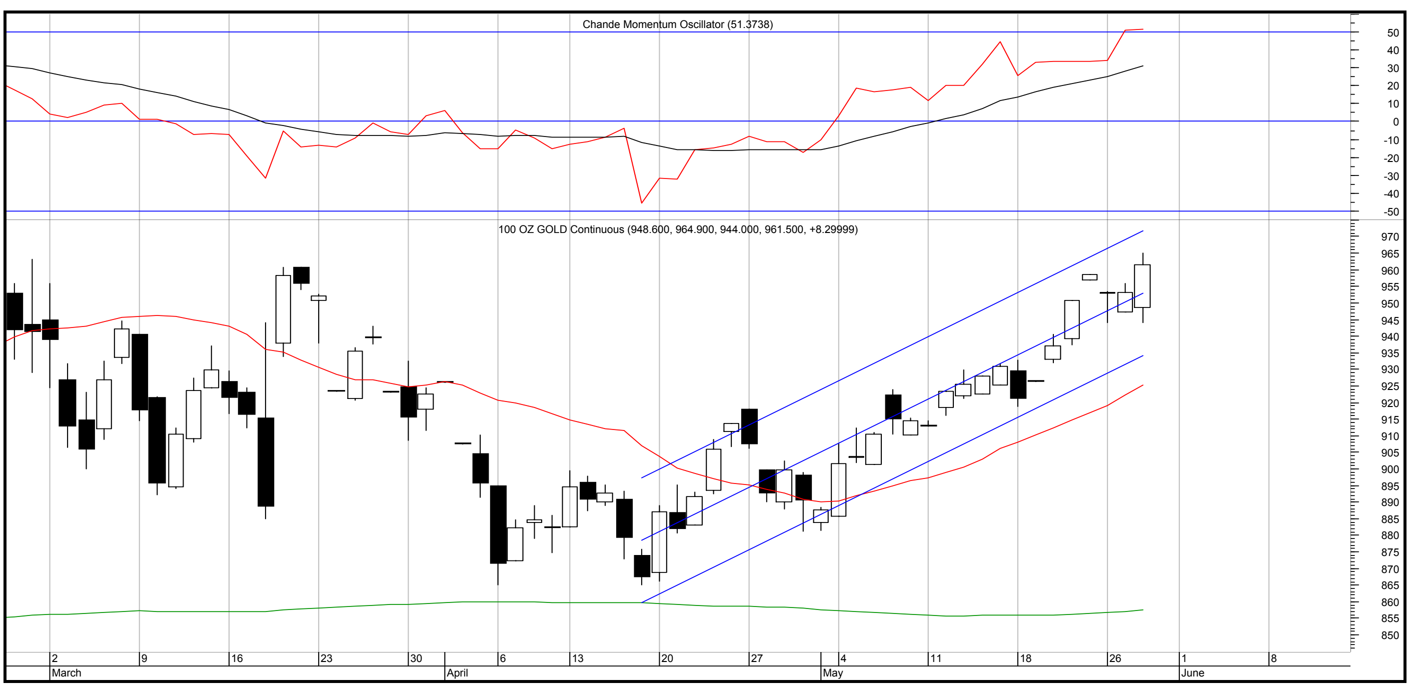
10-Year Note Index

The index closed down at 3.465% from 3.672% from 3.493% and is reversing from an overbought level.

NYMEX Light Crude Oil (Continuous Futures Contract)

Oil closed up at $66.31 from $65.08 and is overbought.

Gold Continuous Futures Contract



Gold closed higher at $978.80 from $961.50 and is getting ovrbought.

S&P 500

The index is near the channel bottom but over the red 20-day moving average.

CRB Commodities Index

The commodity index is nearing the green 200-day moving average.

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