



	SPOT	CURRENT POSITION	SIGNAL STRENGTH	OPEN DATE	OPEN RATE	POSITION GAIN/LOSS
USD/JPY	92.95	SHORT USD/JPY	STRONG	08/18/09	95.03	2.24%
GBP/USD	1.6198	LONG GBP/USD	WEAK	03/23/09	1.4538	11.42%
EURO/USD	1.4291	LONG EURO/USD	WEAK	04/30/09	1.3308	7.39%
EURO/JPY	132.85	SHORT EUR/JPY	WEAK	08/18/09	134.24	1.04%
EURO/GBP	0.8821	LONG EUR/GBP	WEAK	08/18/09	0.8590	2.69%
GBP/JPY	150.56	SHORT GBP/JPY	STRONG	08/18/09	156.26	3.65%
USD/CHF	1.0610	SHORT USD/CHF	WEAK	04/30/09	1.1338	6.86%
USD/CAD	1.0993	SHORT USD/CAD	WEAK	08/25/09	1.0783	-1.91%
AUD/USD	0.8392	LONG AUD/USD	WEAK	07/23/09	0.8188	2.49%
AUD/JPY	78.01	LONG AUD/JPY	WEAK	07/01/09	72.84	7.10%
USD/MXN	13.2519	LONG USD/MXN	WEAK	08/28/09	13.1917	0.45%

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.**

Summary: The dollar is down against the yen, up against sterling and flat against the euro. It is a holiday in London today and a holiday starts in the US on Friday through the following Tuesday (although the US bond market has stopped closing early on the Friday before a Monday holiday). We have a fair amount of news this week, including non-farm payrolls on Friday and preparations for the G-20 meeting ahead of the summit later in September. Overnight the Shanghai stock index fell dramatically and that may trigger a global correction or at least cause second thoughts about risk appetite. Perception of conditions becoming riskier tends to support the dollar, but we wouldn't count on it.

What's Happening This Morning: The euro slipped in the US afternoon on Friday, closing around 1.4297 from an opening level around 1.4369 and thus losing nearly all the gains from last week at 1.4410. The euro had followed US stocks up in the morning and followed them down in the afternoon. We can say the euro failed to match and hold the 1.4400 level, suggesting a retracement before it makes another try. We will get worried about the euro uptrend only if we see a low that is lower than 1.4200 from last Wednesday. Many traders are eyeing the 62% retracement level of 1.4183, which is also the midpoint of the upside breakout bar two weeks ago. We could also name support at the bottom of the linreg channel on the hourly chart at about 1.4150.

Japanese Election: The DPJ won the election in a landslide, 308 seats of 480. The dollar/yen slid from 93.59 to 92.52 or 100 points, not a lot in the grand scheme of things but a lot for a political event. On the whole, elections in Japan do not affect the dollar/yen by much or for long. In 1993, when the ruling LDP lost the majority in the lower house, the yen continued on an uptrend that had begun in 1990 and didn't end until 1995. This time is unlikely to be different, although it's the first loss of power for the LDP since 1955, meaning the Democratic Party of Japan gets to name the prime minister and cabinet. It's not so much that the DPJ won as that the LDP lost—keeping only 119 seats from 300. This was “throw the bums out.”

The DPJ campaigned on “change,” which historically comes to Japan at a glacial pace. The yen's gain, however, is a two-edged sword. For one thing, it tends to drive down the Nikkei stock index and that did



happen today, too—the dollar/yen retraced about 50% of the post-election loss by the European open, although the giant loss by 6.7% in the Shanghai Composite had something to do it it, too.

Financial Crisis: The Dow slipped 0.38% and the S&P fell 0.20% on Friday amid a slew of reality-checking stories questioning whether a 50%+ rise since March is justified on the economy and earnings outlooks. Overnight, the Shanghai Composite crashed 6.7% after a bank reported bad earnings and a metals company announced a big initial public offering (at a time when liquidity may be drying up). The WSJ says the market was also heeding “reports that new yuan loans made by Chinese lenders in August were likely to fall below 300 billion yuan, from 356 billion yuan in July and 1.53 trillion yuan in June.”

In the US, the WSJ is feeding the fear machine with yet another scare story about commercial real estate, saying the July delinquency rate rose to 3.14% or more than six times the level a year earlier. “The other kind of hurt is coming from the inability of property owners to refinance loans bundled into CMBS when these loans mature. By the end of 2012, some \$153 billion in loans that make up CMBS are coming due, and close to \$100 billion of that will face difficulty getting refinanced, according to Deutsche Bank. Even though the cash flows of these properties are enough to pay interest and principal on the debt, their values have fallen so far that borrowers won't be able to extend existing mortgages or replace them with new debt. That means losses not only to the property owners but also to those who bought CMBS -- including hedge funds, pension funds, mutual funds and other financial institutions -- thus exacerbating the economic downturn.”

Economic Events

In the US, Friday's data included the final August University of Michigan consumer sentiment index at 65.7 from the preliminary reading of 63.2 and down a bit from July at 66. Weirdly, expectations rose to 65 from 62.1. One-year inflation expectations held steady at 2.8%. Maybe the new cheeriness accounts for personal spending up 0.2% despite personal income being flat. Core PCE prices are up 0.1% for 1.4% y/y. The real leader was the Cash for Clunkers program, although spending on non-auto durables did well, too. Well, when you need a new refrigerator, you need a new refrigerator.

The Main Event: The yield on the 10-year Treasury note slipped a bit to 3.451% from 3.462% the day before but see the chart—it may have bottomed.

Other Markets: The oil futures contract gained on a little on Friday, to \$72.74 from \$72.49 the day before, but overnight, the drop in the Shanghai index pushed oil back down to \$71.72 by 6 am ET.

G-20 Meeting: The finance ministers of G-20 meet in London next week (Sept 4-5) to prepare for the summit Sept 24-25 in Pittsburgh, of all places. Some leaders are speaking out ahead of time. Canada's FinMin Flaherty, for example, praised the Canadian banking system (that didn't engage in bad mortgage practices and didn't need a bailout), saying it is too soon to exit the stimulus mode and regulatory change still needs to be implemented. This is the key point—everyone thinks it's a coordinated exit from crisis mode, but we think Flaherty hit the nail on the head—we need to ensure regulatory reform before conditions get so good that central banks can raise rates and the same foxes come drifting back to the henhouse.

German FinMin Steinbrueck made somewhat mysterious comments reported in the WSJ today. “In a letter to the G-20 finance ministers and central bank governors dated Aug. 27 and seen by Dow Jones Newswires on Monday, Mr. Steinbrueck said the personal responsibility of top bank management must be increased and banking supervision authorities need more power to demand banks raise their capital requirements.”

He called for coordinated controls on compensation but more importantly, "It is...of central importance that we arrive at a fair distribution of the burdens arising from the crisis and, in particular, that we enlist those who triggered the crisis in the financing of these burdens as well. I would like to discuss with you



how we can bring the financial markets to make a greater, internationally coordinated contribution to financing the immense burdens of the crisis."

He also wrote that G-20 needs to devise internationally coordinated exit strategies to avoid "possible inflationary effects in the next upswing and to reduce government involvement in the financial markets as quickly and as responsibly as possible."

Whew. What does he mean about a "fair distribution" of the costs of the crisis? Ideas are easy to find—perhaps a global FDIC financed by fees from all the big banks? A penalty charged the US? Realistically, the crisis was caused by bad mortgage banking practices in the US plus unregulated gambling in credit default swaps. This was how Goldman was able to continue selling mortgage backed securities to its customers while betting against the sector in CDS, not to mention collecting from AIG with taxpayer dollars. European and other banks bought the paper and bought the swaps, too, but surely the US is not to blame for Iceland's banks overleveraging and going bust—is it? So, if we want to put credit default swaps on a regulated market and have some regulatory agency act as bookie, why do we then wish for government to withdraw as quickly as possible? Steingbrueck's letter is not as clear as it could be. Obviously he wants government out of the business of owning and "managing" banks but we'd like to see a better definition of the regulatory role. As for the wish for a global regulatory agreement, dream on. The anti-regulatory mood in the US remains a key idea despite its obvious failures, and besides, the US resents any leadership other than its own.

Outlook: We need to worry about central banks getting hawkish before the crisis is well and truly over and a new regulatory infrastructure is put in place, something that has not happened anywhere yet (except maybe the UK). Today the central bank of Israel was the first to raise rates, even if Israel is not a G-20 member. Tomorrow's Reserve Bank of Australia meeting is doubly important because the RBA is likely to be the first major bank to raise rates, in Nov or Dec (or even Oct, as some think). Australia avoided the worst of the financial sector woes and managed to avoid recession, in part on capital spending and investment arising from Chinese demand for its commodities. Unemployment barely dipped. A hawkish RBA statement tomorrow could set off a race for forecasts on who is going to raise rates next (as well as being wildly positive for the A\$ against the US dollar and Japanese yen, now showing a curious softness).

Also tomorrow we get the newly important Chinese purchasing managers index, and whatever the Shanghai index is doing, the economy is thought to be humming along. Watch oil move in lockstep with the PMI. At the same time, we get the US manufacturing ISM. Signs of recovery in both China and the US at the same time is actually a bad thing for the world—we will hear nothing but talk of "exit strategies" when it should be perfectly clear that the major economies, including the US, are not ready and neither are their central banks.

Reuters reports that a G7 source said "G-20 policymakers will likely pledge to maintain accommodative policies for as long as is needed, like they said [*sic*] in the communiqué after the April meeting. But some central banks will come under pressure to shift gears to contain inflationary pressures...." As noted, Australia is the immediate focus but analysts could jump that gun for the US and the Fed.

Or maybe sanity will keep a grip ahead of payrolls on Friday. Market News is the only place offering a number so far, and it's a loss of 200,000 jobs. The forecast range is 365,000 to 115,000 with the unemployment rate expected to rise to 9.6% from 9.4%. We know that these are bad numbers, not exactly rigged but not accurate, either. It's hard to be worried about unemployment when what we really want to know is whether the Shanghai index has the power to lead the rest of the world's stock markets. Realistically, one reason for good sentiment indicators like the University of Michigan version is that stocks are up and even those not actively involved in the stock market hear it on the news several times per day. Everyone believes the stock market is a leading indicator of the real economy and never mind that the P/E is already at about 20, or over the historical average (The Economist magazine says the Chinese P/E is at about 30). In a way, the frothy stock markets are a tribute to the optimism gene in the human heart and that's nice. We are not willing to say it's stupid or doomed to disappointment. For all we know, stocks



can continue up all fall, meaning the dollar can continue down. All reports indicate a bearish sentiment toward the dollar and it will take a Shock to cause that to change.



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) . .

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

9-day moving average in Dark Blue.

20-day moving average in Red

55-day moving average in Teal.

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. Futures data courtesy of Reuters. Charts prepared in Metastock.

S&P 500 (Black) and Shanghai Composite—Daily



The two markets continue to diverge.



EURO/USD



The euro put in an inside day with the close under the open.

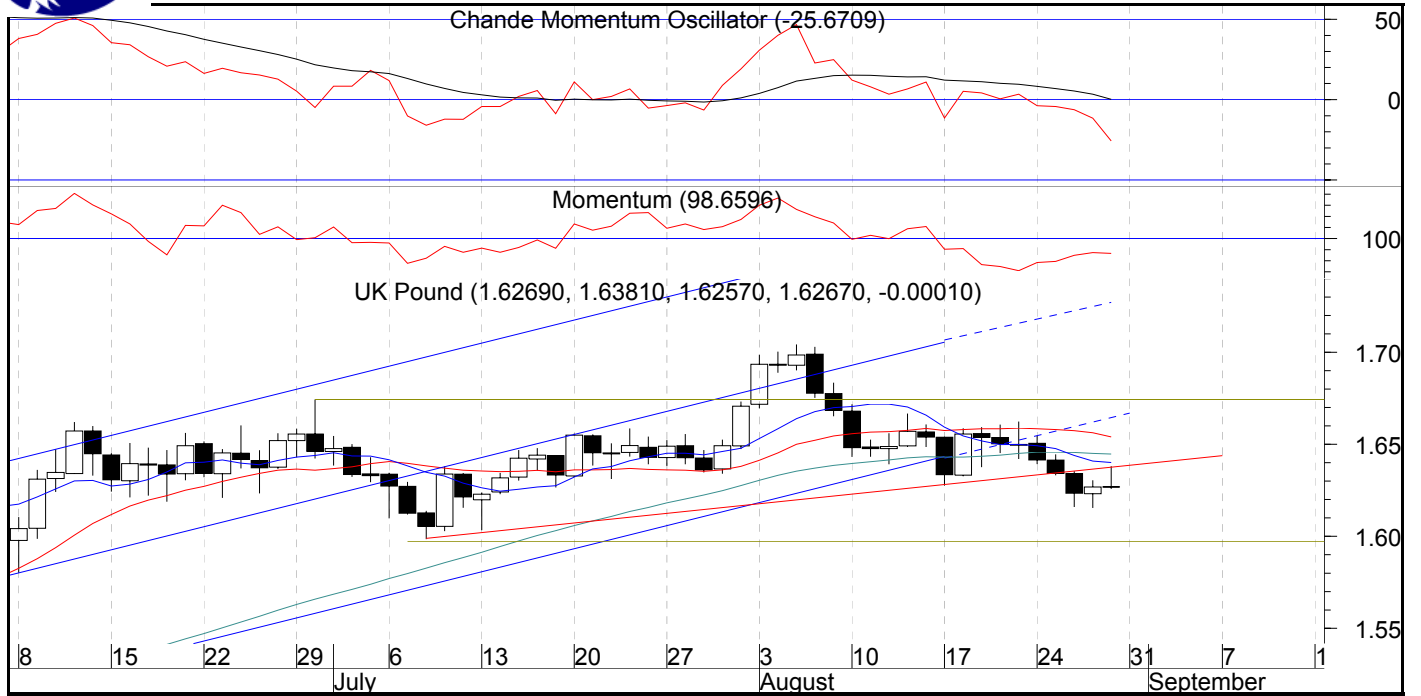
USD/SWISS FRANC



The dollar did not match or surpass the low of the day before and closed over the open.



UK POUND



The pound made a strong recovery although it closed at the open and not at the high. The only reason we are long sterling is the time of year—this looks like a sell signal.

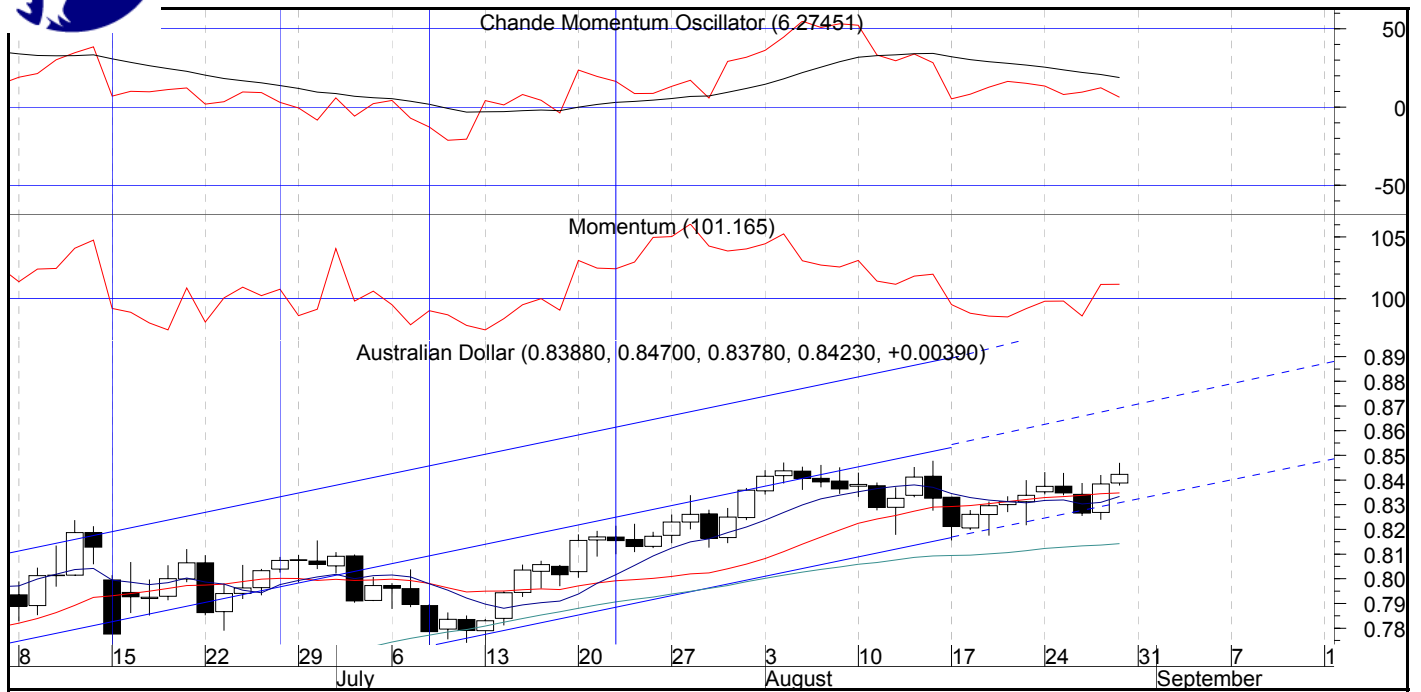
USD/JAPANESE YEN



The dollar did not make a lower low on Friday.

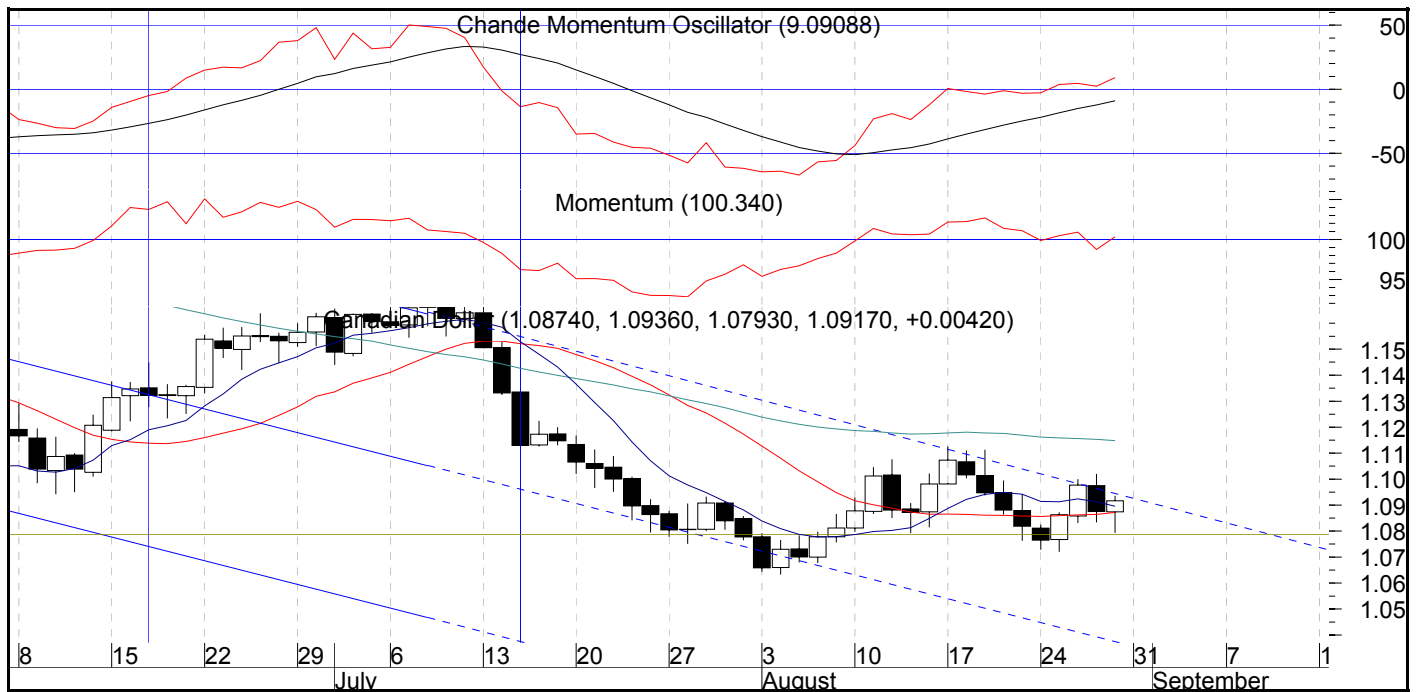


AUSTRALIAN DOLLAR/USD



The A\$ put in another higher high and while the close could be better, this is the direction we expect.

USD/CANADIAN DOLLAR



The dollar made a lower low but a good close. See relative strength in the top window—it is warning of a stronger USD.



EURO/YEN



The euro/yen made a new high but a lousy close. Go look at the AUD/JPY chart—it looks the same.

EURO/POUND



The euro didn't make a higher high or a close over open for the first time in over a week. It is within sight of the green 200-day at 8872.

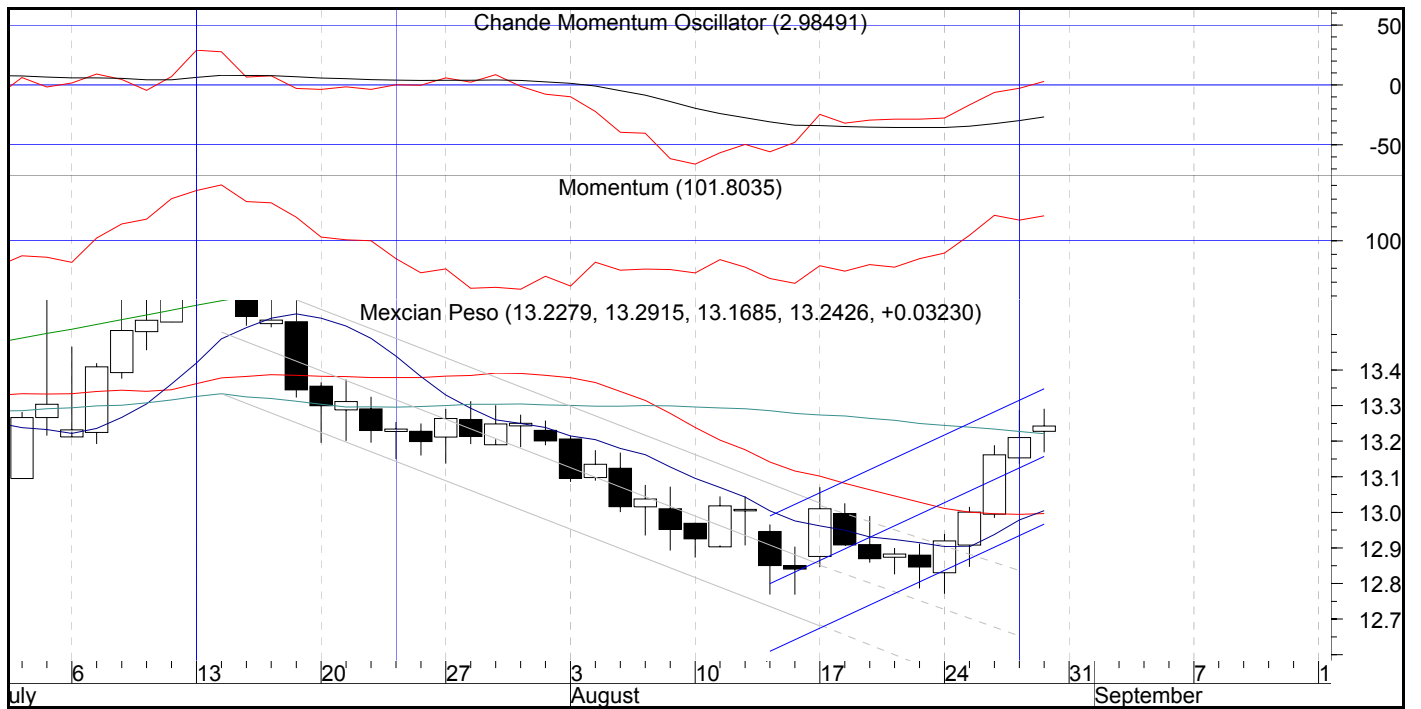


GBP/JPY



The pound/yen took a breather with a higher high but a bad close.

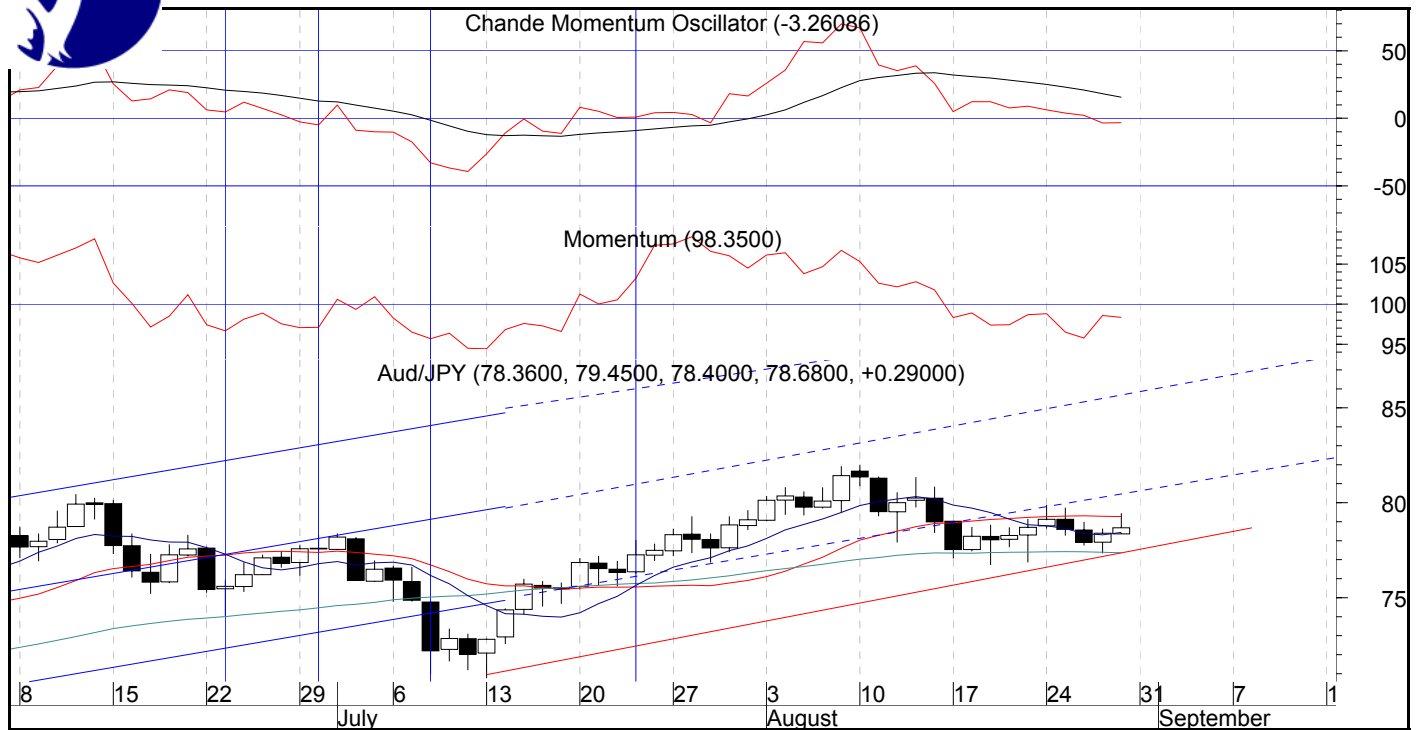
MEXICAN PESO



The dollar closed higher and a little over the teal 55-day moving average.



AUD/JPY



The AUD/JPY made a higher high but overall is barely clinging to secondary support.

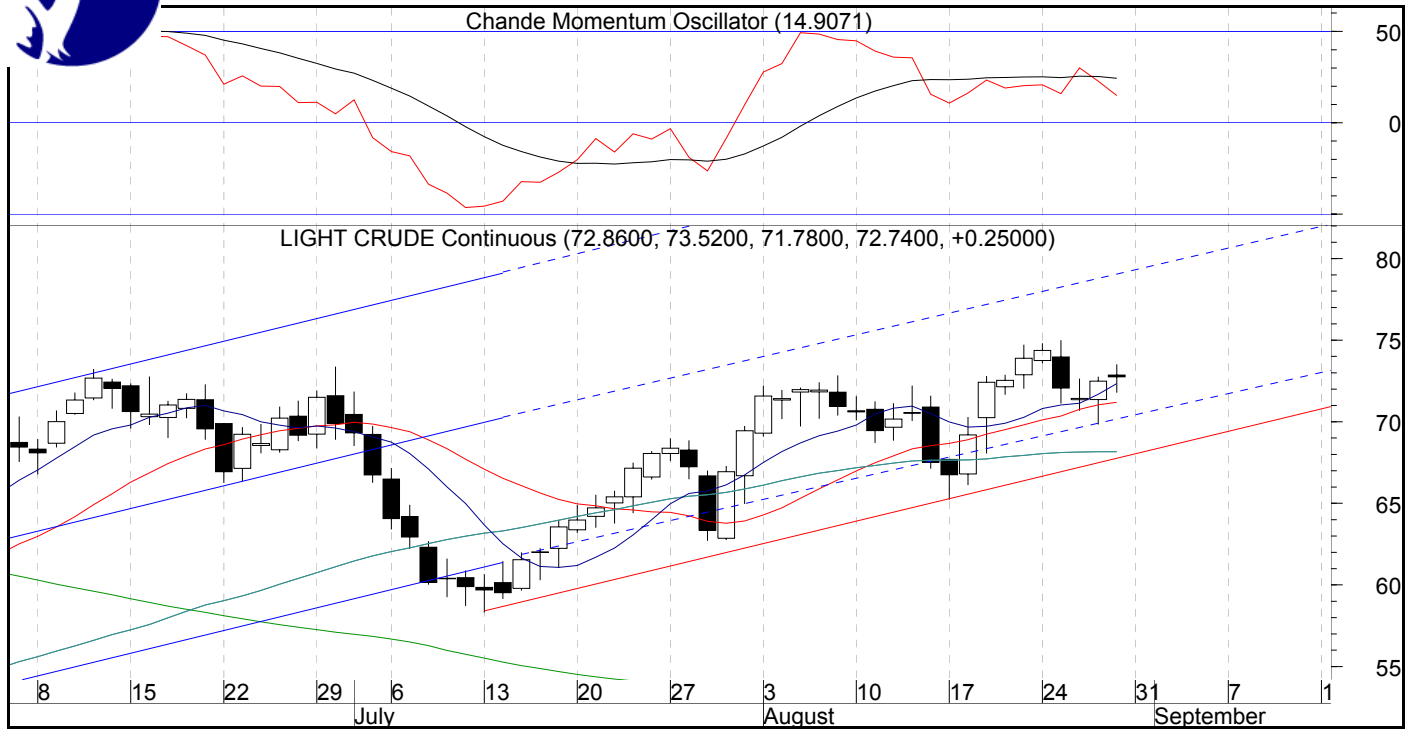
10-Year Note Index



The index made a higher high but a lower close at 3.451% from 3.462%. We think the uptrending channel is justified and higher rates are coming.

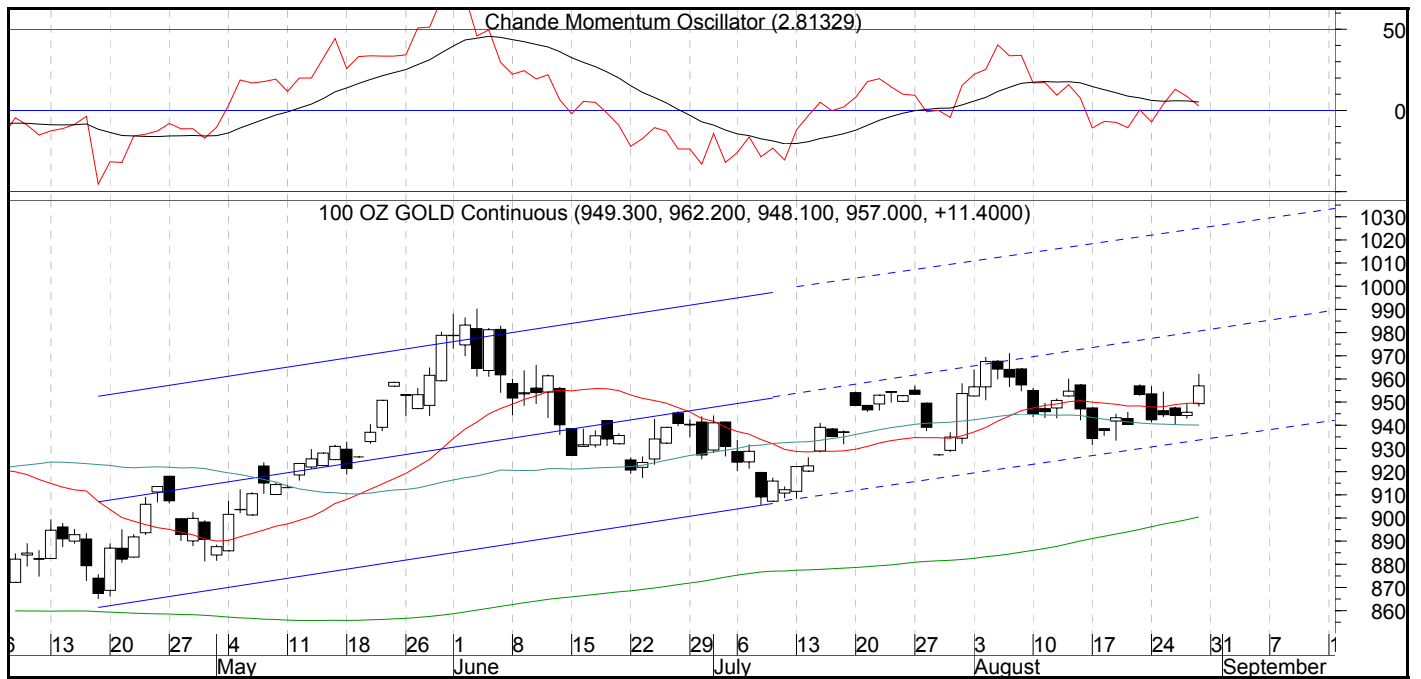


NYMEX Light Crude Oil (Continuous Futures Contract)



Oil made a higher high and closed higher at \$72.74 from \$72.49.

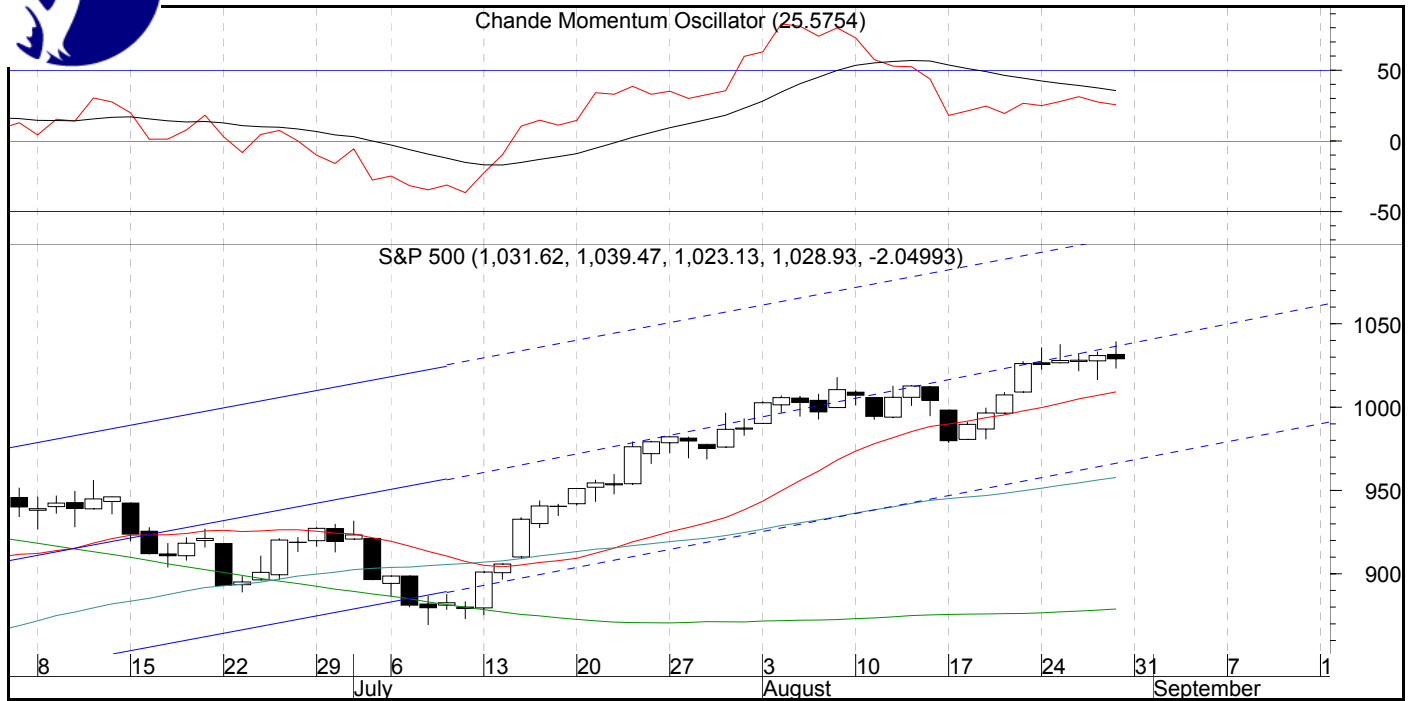
Gold Continuous Futures Contract



Gold closed higher at \$957.00 from \$940.12 and passed above the 20-day moving average.

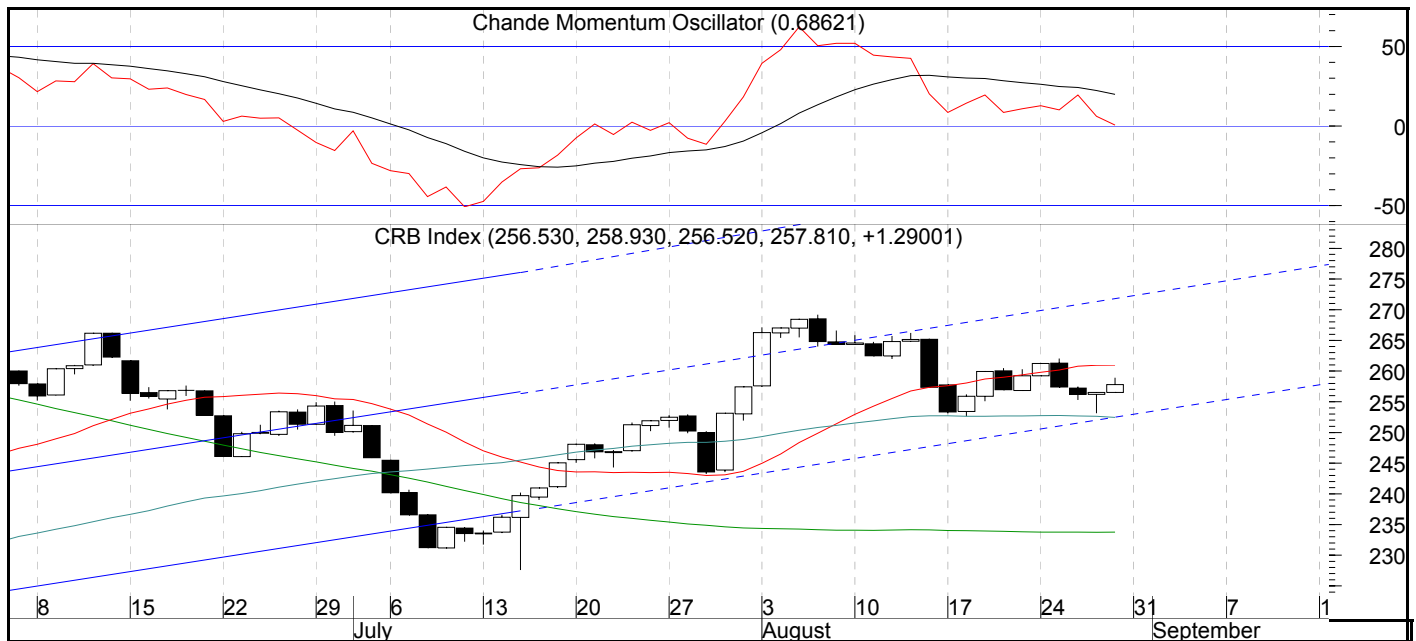


S&P 500



The index closed a hair lower at 1028.93 from 1030.98. Real bodies of late (spread between open and close) has been tiny, denoting lack of heavy interest. The index is flat near the linear regression, too.

CRB Commodities Index



The index closed higher at 257.81 from 256.52.