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ROHR ALERT!! Curiously Creaky in a Constructive Environment

1 message

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Dear Subscribers,

US equities struggled to hold gains on what was overall positive economic data. Stalling since early the previous week (on Closings) at no better than the middle of the recent significant range (more below) was a curious development. Yet as noted from the age-old market axiom once again many times of late, "*The market (which is to say the equities) is a creature of expectations.*" And on that front there was much to be concerned about in the overall US COVID-19 situation.

This is why Friday's 'Bank Stress Test Joy' Alert!! title was a tongue-in-cheek acknowledgement that Thursday's late release of this unmitigated good news was not going to make any difference to the overall economic concerns. As noted on Friday morning, it was very similar to the first early March emergency 50 basis point rate cut, which we deemed as 'meaningless' in the context of the broader early COVID-19 pandemic contagion. And expansion of the COVID-19 infection rates at present is a renewed concern into the attempted US economic reopening.

The question now is whether the 'creaky' weakening in the face of that otherwise positive economic data turns into more of a full-blown 'crack' in the recent heavy 'Normalcy Bias' psychology (for more on that please see our various analyses since last Tuesday's "Sustainable Strength or More 'Normalcy Bias'?" ALERT!!) And as we often suggest, the best resource for that answer is the market itself based on whether the September S&P 500 future either holds or cracks the lower support at the historically critical 3,030-2,970 area it has held on recent pullbacks.

That said, in the context of last week's positive fundamental news, the price weakness is a bit of a case of "Curiouser and Curiouser." (Thanks to Lewis Carroll for that.) That included everything from Tuesday's firm global Advance PMIs to Wednesday's German IFO to Thursday's undershoot on US Initial Weekly Jobless Claims and firm KC Fed into those healthy bank stress test results and relatively firm US numbers (even if a bit weaker than expected) on Friday.

Yet the various knee-jerk responses to this good news did not see the September S&P 500 future hold rallies above the interim 3,100-30 congestion (in the middle of the major ranges.) And as much as the market "*is a creature of expectations*", there is the Rohr axiom regarding successful traders needing to figure out what expectations the markets will need to 'discount' next: "*Successful traders (and analysts and investors) are creatures of anticipation.*" So what's next?

Well, it appears that the optimists who were promoting the upbeat outlook on which the recent 'Normalcy Bias' was based are being refuted by the numbers on the recent surge of COVID-19 infections, and more importantly hospitalizations.

Whether this is an extension of the coronavirus Wave I or a much-dreaded Wave II is moot. The extent of the spread in areas which were previously far less affected actually supports the Wave I extension advocates. Yet it is bad enough to cause a reversion to more restrictive commercial constraints on key entertainment, dining and hospitality businesses, which is a key concern for the economic revival.

While we will have more to say on this soon, we have been strong advocates of looking past the current levels of consumer spending and confidence to what the 'stabilized' situation will look like once the recent government support programs lapse at the end of next month. The estimable Mohamed El Erian (chief economic adviser at Allianz who warned of the COVID-19 threat at the end of January) said two interesting things of late. The first was his comment on the northeast states' travel restrictions, which effectively place an extra burden on their businesses.

Yet just this morning he had another, possibly even more telling, observation on those government support efforts. In a CNBC interview (<https://cnb.cx/3gcJZ5t>) he notes that the US equities have already seen three main rally drivers lapse. From 00:30 he summarizes this and points to the importance of 'policy' as the only driver left which might be able to resurrect a bullish psychology. He goes on to note more largesse from the Fed is going to be 'hard to by', and (from 01:40) the big question is whether Congress can wake up to the pressing need.

However in that regard he notes just what we have been highlighting for some time: the reticence by Republican lawmakers to push more spending despite a still troubling outlook. To wit, *"One of the problems with the good jobs report that covered May is that it created complacency, it divided Congress, and suddenly we see very little momentum; and a lot of the relief measures are going to run out in the next few weeks. So my hope is ...that our lawmakers get the message that this economy is still facing considerable headwinds, and we can't face another downward trend. We don't want to lose the Q3 GDP bounce. Well said.*

To put a personal face on what is being repeated in millions of cases across the US, we found this morning's Reuters 'cash cliff' article (<https://reut.rs/2BOuba9>) article as compelling economically as it was personally depressing. It is about the fate of workers who have benefitted quite a bit from the expanded US government unemployment benefits, yet are going to be in dire straits once they terminate at the end of July. Some analysts have made a big deal out of how high the savings rate has gone despite the pandemic's economic impact. Yet as the article points out, in many cases this is by folks who are scared about what comes next.

As we have been highlighting for a couple of months, the temporary assistance provided by those higher benefits and the Paycheck Protection Program and others cannot be sustained indefinitely. As such, even if the 'extended pandemic Wave I' folks are correct, it isn't going to mean much to all of the people who will be laid off from business reductions and closures later this summer. Even airlines who have received significant federal support are pre-signaling (as required by law) about major layoffs, and offering early retirement to many employees.

So we return to the 'sustainable' level of business later this summer (let alone the more troubling potential into the colder months later this year), and the problems overall economic activity will suffer. That was amply highlighted in our review of what the OECD and Fed had to say three weeks ago, reinforced by the IMF World Economic Outlook (<https://bit.ly/2ViyCRc>) last Wednesday along with all of the COVID-19 spread information in

that very good Vox article (<https://bit.ly/2VhjPpT>) on how few US states actually are meeting White House reopening guidelines.

Therefore, 'anticipation' of the next market 'expectations' leaves the US equities recovering a bit this morning from last week's ostensible COVID-19 pressure. It is likely the case that there are some upbeat thoughts on what Treasury Secretary Mnuchin and Chair Powell might say in their Congressional testimony tomorrow.

That takes on extra significance due to what El Erian had to say about 'policy' being the only bullish driver left for the US equities. So will there be new policy initiatives announced, and will the Senate Republicans show any affinity for pursuing them? If so, US equities might find new life after last week's creaky performance on otherwise positive economic data and sentiment indications.

However, if not, then any pronouncements by Mnuchin that only cover what has been done and commitments by Powell to act on some newly expanded programs only if things get worse may be met with the same sort of disappointment to those same sorts of indications after Powell's June 10th FOMC press conference. And it must be allowed that Powell was very specific that more fiscal action is what is needed (i.e. not just Fed balance sheet expansion.) As El Erian noted, this leaves the ball squarely back in Congress' court. We shall see later this week.

In the meantime, the global govies reflected the return of a nominal 'risk off' psychology last week with nominal gains on top of their recent rallies. Those have not been reversed by the partial US equities bounce this morning.

And the emerging currencies remain under overall pressure since they peaked three weeks ago on the disappointing communication from the Fed in the wake of the OECD's downbeat economic view. They are also remaining weak this morning despite the US equities bounce. As a reference for just how far they rallied on the previous 'risk on' psychology (from late May) and scope of the current reversal, see the weekly chart of USD/ZAR (<https://bit.ly/3dGawGE> through last Friday's Close; inverse indication of overall SA rand strength.) It's going to be interesting.

This is the critical consideration

COVID-19 virus spread caused US equities intermediate-term bull psychology to 'crack'. Early March already saw front month S&P 500 future back below key congestion around the mid-2019 3,030-00 previous all-time high congestion. That was below support from the push above the multi-year topping line at 3,070 as well, and left a late-February intermediate-term up channel 2,970 DOWN Break.

The subsequent DOWN Break below the front month S&P 500 future 2,600 area major up channel seemed to indicate more of a near-term failure. That was from the early 2016 low (<https://bit.ly/2Vt5QxD> updated through last Friday.) That was the key higher resistance it had violated on its mid-April push above its 2,675 trading high Tolerance from prior to the DOWN Break (including monthly MA-48.)

As such, it is reasonable the front month S&P 500 future will now treat the low 2,600 area (with a Tolerance to the mid-2,500 area) as support, with interim levels at 2,850 and 2,750 that were important in the recent up trend. And the front month S&P 500 future pushed out of the broad higher range top in the 3,030-2,970 area in early June and sustained it, with the 3,200 area the next higher meaningful resistance that has a 3,230 Tolerance. That is

obviously what the market knew once it exceeded the 3,030 area, as it also rallied directly to 3,200 in early June.

It stalled all three days early the following week up against that 3,230 Tolerance with no sign it was going to push further. After the following Wednesday's friendly Fed communication yet with no additional stimulus announcement into a still weak economic situation (see that Thursday's ALERT!!), the US equities were extremely disappointed. In the context of recent hypervolatility, this opened the potential to retest that more prominent confluence of technical factors in the 2,970-3,030 range, which it vigorously tested early week into mid-June.

That congestion is reinforced by the manner in which the market churned up against the low end into May. It was recently churning into the 3,100-30 middle of those major ranges pending clarification of the future 'macro' factor psychology. As that was remaining weak on COVID-19 concerns, it dropped back once again.

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