



Alan Rohrbach <ar.rohr.intl@gmail.com>

ROHR ALERT!! On the Yellen Yin-Yang... Again

1 message

ROHR Alert <rohralert@gmail.com>
Bcc: ar.rohr.intl@gmail.com

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Dear Subscribers,

First of all, apologies for our Wednesday technical issues preventing publication of our research. That said, everything was still very consistent with Tuesday's 'Split Personality into Trend Test' ALERT!! on the overall combined factors which drove the rapid US equities selloff and subsequent recovery. Yet in addition, that was obviously triggered by a specific influence: the inflation and interest rate musings of Treasury Secretary Janet Yellen... as we have often seen before.

We share much more on that below, yet will first briefly revisit the influences from Tuesday that likely set the stage for the current US equities vulnerability. As we have often noted, it is unlikely a single factor causes a selloff in any generally resilient US equities bull trend, or for that matter reversal of a well-established 'risk-on' psychology. As noted Tuesday, even though the US equities saw their first sharp downside volatility in a while, the other indications were still 'risk-on'.

However, as opposed to the rampantly bullish anticipation of the benefits of more US government spending (infrastructure and social support) in early-mid April (notes in Monday's 'Non-Anticipatory Fed Boom and Problem' ALERT!!), the problem is with the Biden administration's two-edged infrastructure and social support plan. To wit, *"While the spending is of course welcomed by the US equities as a driver of near-term strength in an already recovering economy, concerns over the higher taxation is finally a more real concern."*

That is also on the high input costs to companies that have shown such strong Q1 earnings in the current reporting cycle. That is also consistent with the Fed possibly allowing more inflation than will be healthy. On the recent international indications, the ECB and BoJ remain consistent in their support of the Fed's still aggressive accommodation, even if the Bank of Canada very slightly tapered their QE program two weeks ago. And the next shoe to fall was this morning's Bank of England holding steady at £895 billion of asset purchases, even if there was an 'operational shift' to lower weekly purchases. It's 4-1 in favor of the Fed approach.

There was also discussion of why the current supply disruption inflation is likely temporary (versus the far more pernicious 'demand-pull' inflation) both in the Monetary Policy Report (<https://bit.ly/3toaACJ>) and press conference. The latter can be accessed near the bottom of the Monetary Policy Report summary page.

In addition to the other stresses on the US equities at present, the highly volatile whipsaw on Tuesday was also due to the return of the 'Yellen Yin-Yang'. That is very reminiscent of the messaging and Fed interest rate decision during Yellen's tenure as the Fed Chair. While current market and economic conditions are much different than 2015, the communication on a prospective basis then not actually doing anything in reality is consistent with the Fed's 'normalcy bias' back then.

Before we explore that further, there is also the classical matter of US Treasury Secretaries eschewing any opinion on interest rates, just as the Fed demurs on questions of the value of the US dollar that is more so Treasury's bailiwick. It is also very much contrary to Fed Chair Powell's commitment to wait for more so full employment prior to considering any tightening monetary policy. We can only imagine what Powell thought about Yellen's comment. Possibly something on the order of, "*Janet, please stay in your lane*" (...or a potentially ruder iteration.)

Yet Yellen expressing opinions which influence markets that do not amount to definitive activity is an old story. For those who were not involved at the time (or have not thought about it lately), this was extensively the case for the Yellen Fed in 2015. Maybe it was the degree to which the Fed's major QE program was not providing as much economic growth and inflation as many had hoped.

Along with that the Fed might have been feeling some pressure to show that improvement due to the risk the QE program would come under more criticism. Of course, this was silly, as tax and fiscal policy were always more responsible for the business community 'animal spirits' at the heart of the matter. Yet after the Fed 'rescued' the world into early 2009 (and even that was as much the FASB ruling on valuing illiquid assets on bank balance sheets), many folks ascribed superpowers to the Fed that in fact do not really exist. Hence the pressure.

And in the event, Yellen and her minions (especially Deputy Chair Fischer) were keen to project confidence, repeatedly cautioning from January 2015 onward that due to solid projections they would need to raise rates 'soon'. In a clear case of a market PTL (Perverse Trend Logic), that threat/promise to raise rates was seen as a sign of potentially accelerating economic strength, and bullish for US equities.

That is obviously contrary to the classical broad 'received wisdom' that the Fed increasing the base rate is NOT good for US equities. However, not in 2015, when the investor class was hungry for confirmation the previously sluggish recovery was gaining momentum. And so it was the Fed minions 'Normalcy Bias' cautions on a potential rate increase inspiring the US equities to rally into their meetings. Once anticipated Fed hikes did NOT materialize, the US equities would weaken.

Whatever one may think of the classical wisdom, that was clearly perverse, and can be seen in our annotated historic weekly chart (<https://bit.ly/3f1NOLN>.) Yet it was the case that anyone who understood the message of the first 2015 instance of this phenomenon in March was able to take advantage of the situation into all of the ensuing meetings that year. It feels the same at present. Any sentiment on higher rates sooner than Chair Powell has signaled may well create selloffs in the US equities (and weakening of other assets enjoying the 'risk-on' psychology.)

However, as long as Powell remains steadfast in his accommodative stance, it is likely that the central bank stance will be a bullish factor. The other edge of that sword will of course be just how much the markets organic assessment of the higher input costs affects the overall 'risk-on' psychology. Now that US COVID-19 pandemic trends are constructive, the other main 'two-edged sword' is the fate of the Biden infrastructure plan, and especially the associated taxation plans.

That 'Split Personality' (i.e. now two-way trade) after the manic early April bullish psychology was also extensively explored in Tuesday's ALERT!!, and we suggest a read for anyone who has not done so already. The bottom line is that while US equities might not

like any reduction in the spending, if that also comes with a bit less taxation (especially NOT a 28% corporate rate) it will likely be constructive; even more so than the rote plan, especially on any bipartisan cooperation.

To illustrate the critical near-term US equities tendencies (likely also a bellwether for overall 'risk-on' psychology), note the daily chart (from the US opening today) short-term Head & Shoulders Top potential (<https://bit.ly/2QZKbhd>.) While June S&P 500 future quickly recovered Tuesday on Yellen's moderation of her rate hike comments, stalling back around the 4,183.50 April 16th Left Shoulder high leaves the possible formation of a Right Shoulder in place. That allows another selloff into the low 4,100 area, whether to the current 'Neckline' in the 4,130 area, or to set a bit of a more gradual 'Neckline' back into the 4,115-10 late-April lows.

There are two keys here: the first is that there should not be any resumption of the rally much above that 4,183.50 high in the very near term. The second is our consistent admonition that just because there is a DOWN Break out of a top does not in and of itself mean the trend has reversed. As always, this is more so an indication of a particular price and point in time from which the actual decision will evolve. In this case it would seem only a failure below the 4,100 'big penny' would indicate the chance for a sustained selloff, with the 4,021-15 Runaway Gap the next important support... but only if any DOWN Break actually maintains.

The indication from the other asset classes is also still supportive of the overall 'risk-on' psychology. Note that even on the US equities sharp Tuesday selloff and subsequent stall into the 4,180 area (also daily MA-9) the emerging currencies only continued to test support. Even the less buoyant developed currencies have held their recent selloff as the US Dollar Index stalled into its 91.00-.30 area (also reflected in EUR/USD holding the low end of the 1.2100-1.2000 range.)

This is the critical consideration

Aside from the sheer magnitude of the selloff in the first week of September, it was also a technical pattern top. That is clear on the front month S&P 500 future weekly chart (<https://bit.ly/3ufmjVb> updated through Friday.) Such a significant rally above the previous week's 3,504.50 Close and drop well below it established a major DOWN Closing Price Reversal (CPR) with a 3,510 Tolerance.

While that might have been a sustained top, the December S&P 500 future posting weekly Closes above first 3,505-10 and ultimately the 3,550 area was indeed again 'Risk On' Forever. This is confirmation of our estimation the US election would be a win-win for US equities, along with key accelerated bullish influence from the serial positive vaccine announcements since early November.

The near-term question was whether it could hold support at the early-September 3,587 trading high and 3,582 early November Close, with a Tolerance to the 3,575 congestion? Even though it slid below them in early-mid November on US election concerns, those issues clearing up reinstated the 'risk on' psychology.

Above that range since late November left minor congestion resistance in the 3,625-35 range. Also above that pointed to the recent 3,668 all-time high that was exceeded into the beginning of December with a 3,700 new all-time high. While it traded slightly above that into early December, the lack of a Trump signature on the COVID-19 relief package sent it back down to a very temporary late-December test of the 3,600 area. Finally more fully out

above the low 3,700 area on a belated 'Santa Claus Rally' saw it up near and ultimately above the 3,750-3,800 resistance.

On recent form, the March S&P 500 future stalled into the old high, and then US equities struggled to sustain activity above the 3,959.25 previous all-time high by more than \$10 (both a natural rule of thumb and key weekly Oscillator level) through all of that week. This was the further indication that Negation of the 3,931-35 dual resistance might be more of a 'failure swing' than full bullish signal.

There was even atypical weakness into the FOMC announcements and Chair Powell's press conference. Even the March S&P 500 future push back above the old 3,960 area high, saw various factors conspire to drop it back to 3,960 area. June S&P 500 future (front month since March 19th) also fell sharply below the previous week's 3,942 weekly Close. That was important insofar as it established a 3,942 weekly DOWN Closing Price Reversal (CPR), nominally a real top.

Of note that had a Tolerance at the previous week's high, most interestingly 3,958.50, right near 3,960 again. However, after overrunning that the previous Friday, a strong US Employment report pushed it up into higher 4,010 and 4,035 resistances. The following Monday there was a 4,015-21 UP Runaway Gap, where the Objectives are 4,193 with a higher one not until 4,316. As such, whether a push generally above 4,200 can be maintained is a key indication on that front.

It is also the case there is a weekly Oscillator threshold into 4,210 this week on the back of a \$25/week rise in weekly MA-41. It appears the market anticipated this last week by leaving a 4,211 new all-time trading high last week. Of course, this makes that level that much more critical a technical threshold on any attempt to extend the rally this week. Along with that the next threshold rises to 4,240 this week that was also set at last December's high end Closes. However, if the market makes it that far, it would also represent fully overrunning the 4,200 area, with the higher UP Runaway Gap Objective not until that 4,316 level.

Yet the current selloff below the 4,140-50 interim congestion suggested a test of the more prominent congestion into the low 4,100 area (mid-April pullback lows.) As noted above, that is now evolving into a short-term Head & Shoulders Top. While the overall fate of the near-term trend is yet to be decided, with the general trend still favors the bulls. However, if there is a general failure below the 4,100 area, next major support is not until the early April 4,021-15 UP Runaway Gap (post-US Employment report.) That's due to the straight line early April rally.

Thanks for your interest.

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