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ROHR ALERT!! A Whiff of Risk-Off

1 message

ROHR Alert <rohralert@gmail.com> Thu, Jun 17, 2021 at 10:59 AM
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Dear Subscribers,
Well, the movement of a couple of the dots into a marginally earlier FOMC rate hike in the infamous projections 'dot plot' raised concerns over the Fed's commitment to continued accommodation. Access to Fed Chair Powell's press conference along with the FOMC Statement and updated Economic Projections are all available in one easy link: https://bit.ly/3gvAIbB. The main point from the press conference is Powell's admission inflation may be stronger than expected.

That said, he also delivered chapter and verse on how some inflation inputs are seeming to self-correct from very elevated levels… like lumber prices. Despite the housing market strength, lumber was the poster child for price escalation being due to processing constraints (lack of milling capacity) while there were plenty of trees out there waiting to be turned into usable construction materials.

The used car price escalation was similarly driven by supply constraints on new vehicles due to computer chip shortages. When automobile demand is high, the lack of new cars and trucks translated into more demand for used vehicles. It is also the case that this sort of chip shortage will take some time to correct, as you cannot just snap your fingers to create a new high tech chip production facility.

All of this points to the degree to which the inflation is indeed likely to continue for a while, with the operative question being what is the definition of 'transitory'? That is for the public at large, yet even more so for the central bank. And that raises the issue of if and when the public becomes so conditioned to higher prices to a degree that affects the consideration of wages. As consistently noted in all analysis, the greater inflation threat is 'inflation expectations' as applied to wage related price increases… the rightfully dreaded 'demand-pull' inflation.

In fact, Powell did an excellent job early in the press conference (14:45-17:00) of folding the current 'supply disruption' likely temporary (even if a bit extended) inflation situation into the employment situation. The latter will need to be something the Fed needs to keep an eye on not just for the return to 'full employment' (whatever that means in the current post-pandemic recovery), yet also for the implications for wages and spending which are strong at present.

We like to remain as independent as possible in our views, yet also appreciate it when any source we respect reinforces them. Along with other well-regarded observers, it is much as we said in Wednesday morning's "Waitin' on the Fed ...Again' ALERT!! To wit, "*On balance, the situation still appears 'risk-on' overall, and it is going to be interesting to see how markets respond to the likely mention from the FOMC and Chair Powell that the Fed is indeed "talking about talking about" a future taper. However, as much as the financial press wants to characterize that as a big deal, it is merely a continuation of what we know since the May 19th minutes release.*" And there were no surprises on that front.

The shift of two FOMC members to the first rate hikes coming in 2022 versus 2023 just doesn't seem such a big deal. Also in Wednesday's assessment, "...*the Fed and Powell must signal they are watching inflation closely while not signaling any imminent plan to taper Quantitative Easing program monthly bond purchases. While much of the financial press and certain analysts are looking for 'new news' from today's meeting, we doubt it*." And indeed Powell stuck with the script.

While markets have reacted somewhat surprisingly sharply (more below on the implied shift to a 'risk-off' psychology), it was as expected on the slight shift in FOMC's overall psychology in the context of the 'macro' influences. In a brief CNBC interview this morning (https://cnb.cx/3vyJKsw), nobody less than the estimable ex-Dallas Fed President Fisher said that "*this was no news… fully to be expected*", and the dot plots "*are just guesstimates*". He also noted that based on that, "*I was surprised there was any market reaction whatsoever*.

Yet there was a rather interesting market reaction, which hinted at the possible reversal of the recent grudging, grinding 'risk-on' psychology into 'risk-off'. September S&P 500 future (front month as of Friday morning) has sagged well below the first lower support at 4,200 after the June S&P 500 future failed to remain out above the old 4,238 early May all-time. Yet at least so far the lowest that the June contract dropped was back to the old lower 4,021-15 UP Runaway Gap 4,193 Objective (only finally exceeded a week ago after the mid-May selloffs.)

Now it will be up to the September S&P 500 future at its $10 discount to the June contract to re-establish upside momentum back above the 4,200 area from its 4,183 overnight trading low into this morning (Tolerance 4,175.) It seems to be doing that presently, which leaves the entire short-term FOMC response feeling like another of those typical 'knee-jerk' reactions which can recover very quickly.

Yet it is not quite that simple for other 'risk-on' psychology indications, especially in foreign exchange. The developed currencies that had been holding up well against the US dollar in a continuation of the global reopening 'risk-on' sentiment are back under pressure. That is reflected in the US Dollar Index surging back above the 90.50-91.00 range, with next significant resistance not until back in the 92.00-.30 area (including a failed September 2020 UP CPR.) This is also reflected in EUR/USD back below the 1.2100-1.2000 range, and GBP/USD below 1.4000.

The recently stronger emerging currencies have also taken a significant hit on the concerns over the potentially accelerated Fed tightening. USD/ZAR has ratcheted back up from below 13.80 to somewhat above 14.00. While the next interim resistance is as nearby as recent 14.20 congestion, the more major levels remain up into the 14.40-.50 area. Similarly, yet starting prior to FOMC, USD/MXN has come up from below 19.80 to well above 20.00 and even 20.30 to nearer to the more major 20.60-.60 area. All of that will need to be closely watched.

The recently buoyant global govvies are also reflecting the renewed higher yield expectations, which is especially important in the US. June T-note future that has dropped back more than a full point from the recent test of the prominent 134-00 area expires on Monday. With the September T-note future at a typical full point discount, it is trading below the historically important 132-00 area once again. Unless it can stabilize and push back up at least above that area into early next week, it will be vulnerable to further weakness. This higher yield indication will not just be bad for the other global govvies, but possibly other markets as well.

This is the critical consideration
On previous form, the March S&P 500 future stalled into its old all-time 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. That is clear on the front month S&P 500 future weekly chart (https://bit.ly/2RTca2F updated through Friday.)

There was even atypical weakness into the mid-March FOMC announcements and Chair Powell's press conference. Even a 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 an early-April weekly Oscillator threshold into 4,230 on the back of a $25/week rise in weekly MA-41. It appears the market anticipated this previous by leaving a 4,211 new all-time trading high the previous week (when that was going to be the Oscillator threshold into early April.) This made that level that much more critical a technical threshold on any attempt to extend the rally, and it was overrun despite the weak April Employment report.

A really interesting part of the overall equation is whether generally overrunning the 4,200 area (including that lower 4,193 Objective), just means a likely test of the higher (weekly Chart) 4,316 Runaway Gap Objective? Yet on the recent sharp selloff it revolved around the degree to which the June S&P 500 future could hold the 4,100 Tolerance of the 4,120-10 support, or needed more of a correction.

Much below the 4,100 area the overall up trend corrected back near the early April 4,021-15 weekly UP Runaway Gap, as expected. While that was a significant further slide, it was actually very reasonable based on the straight up surge from the gap into the upper-4,100 area prior to stalling in mid-April. Yet the inflation concerns which triggered the mid-April selloffs have been addressed.

As such, June S&P 500 future pushing back above the previously tested lower early April UP Runaway Gap 4,193 (daily chart) Objective would seem to speak of it maybe being ready to extend the rally to a higher 4,316 (weekly chart) Objective. Yet that push above the 4,193 (daily chart) Objective at this point is also in line with this week's 4,215-4,240 weekly Oscillator thresholds (MA-41 rising $20/week.) 4,193 down to 4,175 should still be viewed as key near-term congestion support.

Repeatedly holding that support left the door open to exceeding the early May 4,238.25 all-time high, as has now transpired. This is in the context of the higher Oscillator levels set up at the strong weekly Closes back in December rising to the (wait for it) ...4,235 and 4,260 this week. The extended levels set up at the highest weekly Closes back in December rise to the 4,330 and 4,360 levels this week with both still rising $20 per week.

Yet the bigger question on the current downside reaction is whether September S&P 500 future (front month as of Friday morning) at its $10 discount to the June contract can re-establish upside momentum back above the 4,200 area from its 4,183 overnight trading low into this morning (with overall Tolerance still 4,175.)

Thanks for your interest.

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