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ROHR ALERT!! The Curious Dollar 'Haven' Bid

1 message

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Dear Subscribers,
As extensively explored in Wednesday's 'Rationale Retread' ALERT!! (repeated below with a suggestion of review if you've not done so), the market psychology shift from 'risk-on' last Thursday into Friday and 'risk-off' this week is nothing less than a major whipsaw; and that was with some aspects that made no sense.

As we had noted since Monday's 'The Biden Bipartisan Bonanza?' ALERT!!, the idea accommodative central banks could extend such a major rally in the overall bearish govvies at the same time 'risk-on' global sentiment toward significant economic improvement could support a further rally in US equities and non-US dollar currencies seemed more than a bit far-fetched. And that came home to roost in the wake of Wednesday's much higher than expected US inflation.

The improvement in the US equities along with a more sustained rally in non-US dollar currencies was still suspect despite any near-term improvement, due to key 'macro' factors not supporting it into the near-term future. As we revisited as recently as in our October 20th 'Mixed Inflation Indications' ALERT!!, "...*it takes three different headwinds to reverse any sustained 'risk-on' psychology in US equities… and that still seems to be the case at present, which makes sustained improvement somewhat problematic*." In fact some of those had deteriorated further despite last week's knee-jerk reaction to a slightly less hawkish BoE.

Inflation has obviously risen in a manner that can no longer be considered 'transitory' (as central bankers are belatedly admitting.) When we noted that this might not only eat into recently strong corporate profits yet would also depress consumer spending power, we had not as yet reviewed Wednesday's US Bureau of Labor Statistics 'Real Earnings' release (https://bit.ly/3oo2ucV.) It is striking in its indications that over the past two months US workers had already suffered.

Part of the deferral of any inflation concerns have been that 'the US consumer is in good shape' due to savings built up during the pandemic. Yet spending down savings only goes so far before spending requires robust real earnings growth. And at present that is already not the case based on current (and likely to be sustained) levels of inflation. From the BLS report, "*Real average hourly earnings for all employees decreased 0.5 percent from September to October…"*

***"Real average weekly earnings decreased 0.9 percent over the month due to the change in real average hourly earnings combined with a decrease of 0.3% in the average workweek*." Interesting that so many folks are still looking for record holiday season purchases, especially with higher energy prices. We shall see.**

The second risk factor is a further significant weakening of the Chinese economy, especially if there are more pronounced problems at their beleaguered property developers

(more on that below includes the Fed now being concerned.) It is the case today however that Evergrande may be just barely avoiding official default after the 30-day 'grace period' on its $148 million dollar-bond payment lapsed.

According to today's Bloomberg article on that topic, "*It would be quite a surprise if the funds do not flow to the trustee in the requisite timeframe given the immediate cross-default and ripple effect on suppliers and the wider People's Republic of China real estate market,*" according to a knowledgeable source. Especially note the contagion potential, which we have cited for some time.

The final headwind (also explored at length on Wednesday) is the seemingly less than credible ubiquitous perspective that somehow the world is either into, or has indeed already entered, a 'post-pandemic' phase. Check out the link to the CDC graph of New US COVID-19 Cases (https://bit.ly/3BYKtGB), which have ranged back between 70,000 and 140,000 daily and a 7-Day Average now trending back above the recently tested 65,000-70,000 area (more on that from Wednesday.)

Also consider that this is also with more aggressive surges in quite a few other global locales, even those which are highly vaccinated. It will be very important to see what transpires in the US over the next two weeks, after which it will be into the Thanksgiving holiday travel crunch. Maybe those new cases will drop again, creating a more tolerable situation. Yet if they rise from here… well, we'll see.

However, all of that still leaves the question, "*Why would the US dollar attract a haven bid at this time, which has driven the US Dollar Index out above its 94.74 16-month trading high, with the next Evolutionary Trend View (ETV) resistance not until the upper-95.00 to mid-96.00 area?*" The US has some of the worst inflation that is looking to deteriorate further, political disarray even within the current majority party, a resurgent COVID-19 pandemic from still elevated levels (see above) despite improved vaccination rates, and some of the worst supply chain problems of any country due to the congestion at the West Coast ports.

Well, it's a bit of a reach to shift into a slightly longer-term view, but maybe it's the 'least bad' of alternatives on looming Winter 'macro' factors… especially energy. While 'haven' bid has ostensibly meant 'flight to quality' in the past, in present stressed global circumstances it would seem to include a 'shift to the least bad'.

For the film buffs out there, here's a Nicholson quote as private investigator Jake Gettes in the 1990 'The Two Jakes' (sequel to the renowned 'Chinatown') on his standing in that less than 'reputable' professions (not suitable for print here.) This seems an apt metaphor for the relative US dollar psychology at present in its being the 'least undesirable' (https://www.youtube.com/watch?v=py6IpUx4eWs.)

Considering the natural vulnerability of emerging currencies to their economies' pressure from rising inflation, especially unavoidable energy expense, it is no surprise they should have shifted back to extensive weakness on Wednesday. However, into this Winter various aspects of the shift to 'green' energy have conspired to leave China, Europe and UK also threatened by energy shortages in coming months. There is heavy reliance on hydro power with recent extensive droughts that are affecting that power generation… especially in China.

There was also the German decision in the wake of the 2011 Fukushima nuclear disaster in Japan to dismantle all of its nuclear power plants, leaving it dependent on recently less than adequate wind power, and natural gas from Russia. We are sure they are not relishing

that dependency on the tender mercies of Mr. Putin this Winter. The UK also moved to more dependence on currently less than adequate wind power. With only the most modest natural gas storage capacity, both it and Europe have seen major increases in their bulk natural gas prices.

And the United States? Perversely enough, it has massive natural gas reserves in the ground, which are mostly accessible via current production… even if that has lagged a bit after the lack of 2020 investment due to the pandemic-driven energy price collapse. Yet in the broader perspective the US production has led the world (with Russia a close second), and based on current production it has been called 'the Saudi Arabia of natural gas'. Certainly the far and away leader in the West.

Compare the Americans griping about their natural gas prices doubling over the past year to the situation elsewhere. German natural gas prices have sextupled from previous average prices, and are up 20 times from their May 2020 low. However, even more troubling is the UK price increase. While they have backed off substantially from their early October high, they are also still up 20 times from their May 2020 low… and due to pricing boards that control the consumer price, quite a few smaller gas companies have collapsed right into Winter's onset.

The glib phrase for the extreme higher energy expense on top of food inflation is that quite a few UK residents will need to "*choose between heating and eating*." That's more than sad for a developed economy, yet most starkly illustrates the challenges elsewhere that are not quite as bad in a US still experiencing some significant stresses. So here we are, with a 'haven' bid in a US dollar that seems ready to continue on the basis of not much more than it being the 'least bad'.

Courtesy Repeat of Wednesday's 'Rationale Retread' ALERT!!
First of all, apologies for the lack of a research update, as our ISP had a significant problem with all internet and cable TV signals down. Yet as we have noted since the beginning of the week, today was going to be the more important horizon on both major inflation data and a key economic outlook (more below.)

As noted since the end of last week, there seemed to be a 'buy everything' market rationale in the wake of combined positive influence of the deft performances of the Fed and BoE, US Employment, the high efficacy announcement for the Pfizer COVID-19 therapeutic pill, and even some anticipation of the US House finally passing an already Senate-approved bipartisan infrastructure bill. There was quite a bit of 'good news', yet a question over the euphoric market response.

As we noted in Monday's 'The Biden Bipartisan Bonanza?' ALERT!! (repeated below for your ease of access), the improvement in the US equities and non-US dollar currencies was understandable. However, if all of the news was pointing to a much stronger US and global economy, what were the global govvies doing extending an already significant rally? It was clear 'something's gotta give'.

And that became more apparent on the subsequent influences which returned to our recent revisit to the way in which only tripartite negative influences are sufficient to deliver any sort of weakness in a strong US equities market. And there was especially a question over whether the US equities were the true indication for the extended trend, or was it the signal from the global govvies?

In market terms that had at least been partially resolved by the December S&P 500 future stalling this week into the higher of the near-term weekly Oscillator thresholds at 4,710; where it also stalled into new all-time highs late last week. That has led to at least temporary slippage below the lower near-term Oscillator threshold at 4,685 (both still rising $25 per week.) Even if this develops into a more extensive selloff, the overrun 4,621 major 'swing count' Objective will loom large a the lower area critical for any more extensive selloff to continue.

The three items on which we have recently focused for any 'risk-on' psychology problem are inflation, the chance of a COVID-19 pandemic resurgence, and risks to the Chinese economy from its highly over-leveraged property developers. However much many observers would like to downplay those influences, they are recently more prominent and posing a greater threat to US equities and both the developed currencies and emerging currencies. And while there is some pressure on global govvies today from the surprisingly high US CPI, it is of note the Bund is weakening much less than the T-note, with the Gilt somewhere in between.

Those only work hand-in-glove if not just the US but also prospects for the global economy appear to be dimming. Let's begin with the US CPI that saw an already still elevated 0.5% monthly rise come in at 0.9%; with an annual figure of 6.2% versus a 5.3% estimate. While early recovery inflation can be viewed as a positive sign, we are now into worries about ingrained inflation. As noted previous, while companies have passed along materials price increases, that may not continue.

Then there is the threat from the over-extended Chinese property developers, and whether they can continue to make payments on their loans; especially offshore debt that cannot be easily stretched out. According to a Tuesday Reuters article updated just this morning (https://reut.rs/2YzmGPX), "*Some bondholders of cash-strapped China Evergrande Group have not received coupon payments by the end of 30-day grace periods at the close of Asia business on Wednesday*", which was for a $148 million. This threatens contagion into other hard-pressed property developers. The concern is that this will affect the Chinese economy.

Up to this point there has been a sense that the financial press can often be in a somewhat self-serving hyper-excitable mode… the old adage is, "*You can't sell newspapers* (or online clicks) *with the headline 'The House Is NOT Burning*'." This is fair enough, except for the fact that it is becoming more of a reasonable concern that any weakness spreading from developer layoffs on project failures will have an outsized impact on broader Chinese economic activity, as well as the broader Chinese financial markets through investors turning risk averse.

And lo and behold, who should now weigh in on that potential and its possible spillover to at least some degree for the global economy: none other than the US Federal Reserve. In Monday's extensive semiannual Financial Stability Report (https://bit.ly/3wC0NMG for our very lightly marked-up version) notes, "*Financial stresses in China could strain global financial markets through a deterioration of risk sentiment, pose risks to global growth, and affect the United States*." It is something that many had previously played down, yet now here's the Fed.

That is from page 60 in the "Near-Term Risks to the Financial System' section that begins on the previous page. We suggest a read of that highlighted section, yet note that the Fed indication is that, "*Given the size of China's economy and financial system as well as its extensive trade linkages with the rest of the world, financial stresses in China could strain global financial markets through a deterioration of risk sentiment, pose risks to global*

***economic growth, and affect the United States*" ...along with the rest of the global economy we have noted.**

Yet beyond a now heightened risk from a weaker Chinese economy that might be exacerbated by its property developers woes and inflation that might crimp consumer sentiment and corporate profits, there is the threat from the resurgent COVID-19 pandemic. In a somewhat surprising development, that is even for well-vaccinated countries. While the surging case numbers in an unvaccinated Eastern Europe are not that much of a surprise, the fact Germany is experiencing a real problem again highlights the resilience of the virus and pandemic.

Even allowing regional under-vaccination in the US, the latest new case counts are very troubling. That this could still be an issue though many were playing it down has been highlighted since our October 28th 'Post-WHAT?' ALERT!! It was the case that the psychology had been co-opted by ubiquitous 'post-pandemic' communication from both the regular and financial press. There were a lot of assumptions that the recent improvement from what were once again horrific levels of new US cases meant it was alright to anticipate the end of the pandemic. Yet the real statistics were always refuting that overly optimistic assumption.

As we have done from time to time, once again take a look at the CDC New US COVID-19 Cases graph (https://bit.ly/3BYKtGB.) As we have noted previous, the key is the 7-Day Average so far only dropping back to the 65,000-70,000 area. During the course of the pandemic in the US it is the key level at which new cases stalled on the way up in July 2020 prior to easing off before a massive Fall-Winter surge; it was also where the temporary case increase stalled in April 2021 on the way down to more constructive levels. Yet having atypically surged to major levels again over the Summer, that it is no lower than that level is troubling.

So there we have the three part concern for the 'risk-on' psychology. There is the worsening inflation that can be a direct threat to both consumer activity and corporate profits at this point (as opposed to earlier in the recovery.) There is now also a prominent risk of exacerbation of recent Chinese economic weakness in the wake of problems at their property developers. Just to be clear, it is not just Evergrande that is the poster child for problems of debt service and overall performance that is endemic in many other developers with offshore debt.

And now we have the resurgence of the COVID-19 pandemic that was supposed to be tamed in the 'post-pandemic' world. It is also striking that this is occurring in the early Fall on the way into what is presumed to be a worsening of conditions once again. It must be allowed the seasonal tendency did not act as expected this Summer, and possibly there will be a milder than expected Winter surprise.

Yet in the context of the normal pattern, this is quite a bit of 'hope over reason'. We allow that pandemic progressions cannot be tracked and predicted with the same assumptions that assist in predicting market price movements. That said, consider that the latest new case count on Monday is back up to 134,072, and unless something changes quickly the prognosis is not good. We must also allow that new cases may not be as troubling in a vaccinated environment.

That said, for whatever reasons that are not extensively discussed in any of their releases of these analyses, the Organization for Economic Opportunity and Development (OECD) released their latest monthly Composite Leading Indicators (CLI https://bit.ly/3bZRYCM.) As

its "OECD Composite Leading Indicators Suggest Economic Growth Approaching Post-Pandemic Peak" title notes, there is a better chance than not the global economy will weaken from the already weakening tendencies highlighted in the previous month's release. [Keep in mind this is a net 4-month forward view based on a 2-month delay of a 6-month outlook.)

It specifically notes, "*Signs of a possible upcoming peak in the growth of economic activity have emerged in the United States, Japan, Germany and the United Kingdom*." And it also cautions at the bottom of its statement, "*Despite the gradual lifting of COVID-19 containment measures in some countries and the progress of vaccination campaigns, persisting uncertainties may result in higher than usual fluctuations*." Uncertainties indeed, and note that 'post-pandemic' term turns up here as well despite the warnings about unusual fluctuations.

Here we are into lunchtime in the US with global govvies back under pressure, yet not on indications of being driven by global growth. It is more so a manifestation of the inflation fears. Similarly, both the developed currencies and emerging currencies are back under pressure after a recent attempt to strengthen against the US dollar. That the US Dollar Index is up against recent highs near the 94.74 16-month trading high is a sign of a renewed 'haven' bid. Next resistance if that is violated is not until the upper-95.00 to mid-96.00 area. And it is much the same for emerging currencies that are no less than getting 'trashed' after their recent rally.

Courtesy Repeat of Monday's 'The Biden Bipartisan Bonanza?' ALERT!!
In Friday's 'Synergistic Breakthroughs' ALERT!! (repeated below for your ease of access), we explored the synergistic nature of the Pfizer announcement on its high efficacy COVID-19 self-administered therapeutic pill even prior to the strong US Employment report. See below for the full review. In the event, the US equities were already up into a new all-time high prior to the release of a US report that was better than already elevated estimates... complementary 'risk-on' forces.

However, even all of that might have been influenced by the degree to which the US House was very likely to finally pass the bipartisan infrastructure bill, which had already passed the Senate back on August 10th. While it did not pass until after markets closed on Friday, we suspect anticipation made this the third leg of a 'risk-on' stool which boosted 'risk-on' market sentiment during the day.

Many questions remain over why the Progressives in the House did not see the advantage in passing this additional $550 billion of spending over the next 10 years sooner, despite wanting their 'social infrastructure' bill to be passed at the same time. The 'received wisdom' is that some of them saw the degree to which the Democratic Party bickering was weighing on their electoral prospects, as was already reflected in much weaker liberal voter turnout in recent off-year elections.

Whatever the case may be, some components of that bipartisan bill may be contributing to the US equities sense of euphoria. That is because there is now a sense that the worst effects of the COVID-19 pandemic will be suppressed in the future, which may solve the conundrum of major employee resistance to the current vaccine mandates (much more on that Friday as well.) At the same time, the US economy may be seeing more sustainable near-term earnings potential.

This is a major '*good news is* (indeed) *good news*' for a change. Yet the fly in the proverbial ointment is the question over why the global govvies should have seen such a sharp rally if

indeed the other 'synergistic' factors are creating so much stronger an economy in an already inflationary environment? As noted on Friday, there seems only one way to view it in the context of that "...*should be weighing on global govvies. The only squaring of that circle might be that the therapeutic developments might assist in clearing the supply chain congestion, due to more workers being available once the COVID-19 concerns are more fully addressed*."

The Pfizer therapeutic (and potentially others to follow) eliminating much more of the workplace or schoolroom risk of COVID-19 may free up more of the workforce, which could buffer some of the current upward pressure on wages. However, the greater inflationary influence over recent months has been the very significant port congestion. That will not be solved by the additional tonnage coming on line in 2022 Madame Lagarde mentioned at the ECB press conference.

The US bipartisan infrastructure bill's major spending also does not provide any near-term inflation relief. The bill expends $42 billion on airports, waterways and port infrastructure, and invests $110 billion in roads and bridges. Yet that does not occur by magic wand, as it takes quite a bit of time to deploy federal funding.

So with neither immediate inflation relief from the employment aspect of the Pfizer therapeutic nor the extended spending on the ports, roads and bridges (as also noted Friday), "*It is counterintuitive, to say the least, that the December T-note future is back up near the 132-00 area, with the Gilt well above 126.00 and Bund above 169.50-170.00*." It would seem those who are hopeful on the US bipartisan bill being counter-inflationary have the cart out in front of the horse.

In the first instance is it adding fiscal largesse just as central bank largesse is being reduced, which is sensible in the broader picture. Yet it will not weigh on an economy which is already recovering nicely from the recent pandemic dip on the Delta variant impact over the Summer. Possibly the weekend has given the global govvies a chance to reconsider their wild end of week rally. The December T-note future is a half point back below the 132-00 area. While the Gilt and Bund have not weakened as much, that may be due to the current European COVID-19 surge.

As far as what to look for next in US equities, this was also noted at the end of last week regarding the higher front month S&P 500 future Oscillator thresholds. Those stand as the outlook into any further rally. We have updated them for this week based on weekly MA-41 now rising $25/week once again. The next (ultimate) thresholds this week are from back near the top of the rally in December 2020, at 4,755 and 4,785. As such any sustained escape above the 4,685 and 4,710 area current thresholds at the end of this week points to 3,780 and 3,810 this week.

Of note, along the way is the major 'topping' line from the 3,587 August 2020 high across the 4,232 May 2021 high and the 4,550 August 2021 high into the 4,740 area this week. That is a 'delimiter' on any attempt to escape the low 4,700 area..

Similarly in foreign exchange, the US Dollar Index is maintaining its recent bid without having retested (much less failed below) its key 93.70 area. This is a reflection of weakness in the other developed currencies, and most especially the euro that may also be related to the recent European COVID-19 resurgence.

It is also the case that emerging currencies have only reacted back up somewhat modestly from their recent selloffs. That has been most impressive on the South African rand seeing

USD/ZAR dropping back below 15.00 after its recent test of the 15.40-.50 area. That will need to be closely watched after the December WTI Crude Oil future recovered from a brief dip below 80.00 to the 82.00 area again.

Courtesy Repeat of last Wednesday's critical consideration (updated chart)
[Brief current comments above; to be updated Friday morning]
After the early July downside reaction the recovery back above the 4,300 area violated support left the higher resistance into the previous week's 4,360 DOWN Closing Price Reversal with a Tolerance to 4,364. That is clear on the S&P 500 future weekly chart (https://bit.ly/3BUQCDY updated through Friday.) It is of note September S&P 500 future had managed to retest that area right into the ECB press conference prior to weakening again the following Thursday morning.

And the September S&P 500 future subsequently sustaining activity above the 4,425 and 4,450 weekly Oscillator thresholds was a sign of continued strength as they were still rising $25 per week. As such, the Oscillator indications remained important after what was the 'lackluster jailbreak' after the previous outstanding US Employment report. With the market dropping back below the 4,450 level (on weekly MA-41 up $25), there seemed to finally be some real risk.

Yet even below the key lower interim levels into the recent 4,425 area congestion and 4,380-65 area bottom of that, it also held key lower support in mid-August looking forward into the following week. That bigger level was 4,340 on weekly MA-13 (loosely held on all sharp reactions) at that time, and the significant aggressive weekly UP Channel from the major 2,174 March 2020 cycle low.

In the event, the recent late week recovery back above the 4,425 area pointed to the strength of the psychological recovery as well as exceeding the key technical resistance areas. That led to the recent new all-time highs above the previous week 's 4,476.50 trading high (prior to the temporary selloff.) That again left the near-term Oscillator thresholds into 4,515 and 4,540 areas (on the rising MA-41), which it failed to maintain in early September, fomenting the reaction.

This led to the violation of the 4,492 interim daily chart congestion after trading around it previous, with the more prominent 4.462 area also being violated three weeks ago. And while it subsequently traded back above that as well, recent softening below it spoke of an ability to trend lower in the near term. That left the more major 4,420-10 area as next support on both weekly MA-13 as well as that significant aggressive weekly UP Channel from the major March 2020 low.

Having tested that area into the mid-September Close and violating it from the beginning of the following week was a fresh 4,410 DOWN Break. That fed further weakness which was already anticipated from the negative influence flowing out of China. As usual there was a Tolerance below that (as seen on selloffs in both June and July) down to 4,350 area lower congestion developed during the temporary July topping activity, and retested on the mid-August sharp temporary reaction to a 4,347.75 trading low. While that seemed a broad berth, on past form only below the 4,350 area does it signal a full trend reversal.

Yet as always with these matters, the weekly Close was more important than temporary trading weakness below it. And the December S&P 500 future held against interim low-4,300 support, and ended the week back above the low 4,400 area. The extent of the temporary selloff means that it needed to be treated as a 4,410 weekly up channel DOWN Break. Yet that also means the Close back above it established it as a Negated DOWN Break, and therefore a support area. That is also consistent with weekly MA-13 moving up to the 4,430 area this week.

That said, the 4,348 area had reverted to the key support again on the then renewed pressure. And much like previous, it was temporarily violated. The difference is that the daily 'trend flow' was quite a bit different with the rally back above the low-4,400 area. Holding above the 4,430 area Tolerance of the 4,400-10 resistance for a weekly Close also above the at that time weekly MA-9 and MA-13 in the 4,435-45 area looking more bullish again.

The next higher resistance was at the 4,472 late September trading high from which it previously dropped to the 4,300 area. That being exceeded last week was a further strong sign, which has not surprisingly led to the December S&P 500 future also pushing above the next minor early-September congestion in the 4,510 area. That only left the early September 4,549.50 front month S&P 500 future all-time high as resistance. Now that it has been exceeded, the 4,621 major 'swing count' is the next key threshold, with the next key weekly Oscillator thresholds up into the 4,660-85 area this week (rising $30 per week.)

Thanks for your interest.

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