ROHR ALERT!! Like Charming a Cobra

1 message

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Dear Subscribers,
After all of the important releases earlier this week (including Wednesday's ECB Financial Stability Review), there was not much more of any consequence today other than the pleasant surprise of Euro-zone CPI coming as expected. While still at an elevated level, that is a constructive change from some recent individual European countries' hotter inflation indications, which is also the case elsewhere.

Along with the downside correction back below 80.00 in WTI Crude Oil prices, that is likely responsible for the nominal bid in global govvies today. Yet it is curious that the direct influence of lower energy prices, along with its importance for overall inflation, is not assisting emerging currencies at all. In fact, they are under more extensive pressure now even than their recent return to weakness since their mid-October rally highs. That is a sign of the degree to which a 'risk-off' psychology is continuing to expand beyond the inflation consideration.

As noted in Wednesday's 'ECB Financial Stability Review and More' ALERT!! (repeated below for your ease of access), with China temporarily sidelined as a major negative influence, it comes back around to the impact of the now resurgent COVID-19 pandemic. Check out the latest CDC New US Cases graph there for the indication that is also apparent in the UK and much of Europe outside of France. US cases surging back up to 150,000 on Monday is a distinctly bad sign right in front of the Thanksgiving weekend major travel and gathering beginning in the middle of next week. While the daily new cases dropped back to 96,000 on Tuesday, only numbers consistently below 65,000 are constructive.

That concern over the potential impact on the global economy might also be contributing to the bid in the global govvies. Yet they have been very hard to read under the prevailing cross currents, where inflation remains high and well above the current risk-free yield levels. It has been like trying to stare down a cobra to watch them in current narrow ranges after the major September-October selloffs. Even weak sister December Gilt future has recovered back above the 126.00 area.

And if it is evolving into more of a COVID-19 resurgence 'risk-off' environment, the same can be said for the US equities. Since the December S&P 500 future exhausted its rally into the low 4,700 area Oscillator resistance late week two weeks ago, it has been stuck up against it; yet mostly only reacting down to no lower than the 4,650 area. When do the next more substantial price moves commence again? That's anybody's guess with strong corporate earnings.

However, in general the now pronounced weakness of emerging currencies tends to reinforce our recent sustained view that the entire 'post-pandemic' psychology so prominent in the general and financial press a month ago was a 'triumph of hope over reason' for anyone considering the broader macro influences… especially the COVID-19 pandemic resurgence that is a global development.

As noted on Wednesday, there is still an analytic choice to be made on whether the extensive higher new cases will bring as extensive a negative economic impact as last year. We suggest a read of Wednesday's analysis for a full review.

Repeat of Wednesday's 'ECB Financial Stability Review and More' ALERT!!
We noted in Tuesday's 'Critical Cross Current Choices' ALERT!! that we were only going to update the Evolutionary Trend View after this morning's (08:00 GMT) ECB Financial Stability Review

(https://bit.ly/2YUAnsW.) That is after the recent significant short-term impact of the BoE Monetary Policy Report and press conference two weeks ago, and last Monday's Federal Reserve Financial Stability Report, which highlighted some of the risks from China's property developers.

It is of note that the ECB seems so sanguine about the risks from what it sees as a waning COVID-19 pandemic, and is even highlighting the recovery since the depths of the early phase quarantines and general public fears. Yet we continue to ask the same questions repeated in Tuesday's analysis that we have been looking at for some time: Is the pandemic really waning? And will the impact of any resurgence really be as benign as many observers would like to believe?

We will revisit that shortly, but first we suggest a quick review of what the ECB had to say by scrolling down to 'presentation slides' for a look past the better tendencies the ECB has highlighted. In the initial bullet points on the outlook it notes, "*Supply disruptions and energy prices pose risks to inflation and growth*." As we have highlighted for both Europe and the UK, that energy price component of the general sustained inflation picture is of particular concern into the Winter.

On a more subtle note regarding market valuations, the "Deviation of a basket of global financial assets from long-term average" graph (page 7) is very interesting. It illustrates the degree to which general asset prices have become inflated to the same degree as they were depressed during the Credit and Housing Bust in 2009.

Of course, these tendencies are hard to quantify for any definitive market view. However, the recent explanations of why corporate earnings can remain strong despite the ongoing inflation likely eating into consumer discretionary spending, especially in the UK and Europe, are suspect. Even in a US where savings remain robust after the spread of government relief package largesse, the recently cited BLS Real Earnings report (see last Friday's ALERT!! for the full details) showed that US workers are losing ground to inflation despite the recent wage gains.

With the China risk factor temporarily suspended due to encouraging Retail Sales and Industrial Production data early this week, the remaining risk is the COVID-19 pandemic resurgence. That is underway in quite a few areas, especially Eastern Europe and now Western Europe as well (France excepted) and the UK, where it surged as far back as July and has remained high. Yet the poster child for how bad it might become on a near-term assessment and outlook is still the US.

As we have noted in recent analysis, and committed to updating on a regular basis, the US was the main source of the 'post-pandemic' quip on just how far new cases had fallen. That was with an expectation case counts would collapse further into a benign limited spread in the future. This was despite the still low overall US full vaccination (around 60%) and rejection of suppression measures.

However, as we have emphasized since our October 20th 'Post-WHAT?' ALERT!!, that sanguine extrapolation of the near-term trend was folly without any credible exploration of the 'macro' factors that would support that sort of optimistic view. And lo and behold, that 'post-pandemic' designation has disappeared from the general and financial press vernacular in a heartbeat in the face of the renewed spread of the pandemic. While Asia has seen an uptick in cases that is troubling due to its more draconian responses, those have proved effective in the past.

And the real risk for a major COVID-19 resurgence that could lead to extensive government restrictions to curb it is in the US. As we have been at pains to point out previous, the real impact of the pandemic on economic activity is twofold. The first is outright government (whether local, regional or federal) restrictions that weigh on economic activity. Yet there is also a broader psychological force which has a real impact beyond any government action: public aversion to activity in the 'gathering' economy, including dining, travel and hospitality.

On the back of greater vaccination confidence, each of those areas has recently seen a major rebound after waning in Q2 on surging COVID-19 new case counts. However, that recent new case improvement is now significantly reversing in the wake of the more sanguine public attitudes. Again as we have highlighted and committed to regularly updating, here is the latest CDC New US COVID-19

Cases graph (https://bit.ly/3DpHyIH.) After the typical lighter reporting over the weekend, US new cases as of Monday have surged strongly, up to every bit of 150,000.

Along with the recent consistent push to new cases above 100,000 since late October, the 7-Day Average (that did not even drop back below the consistently highlighted, key 65,000-70,000 area) is trending in the wrong direction again. However hopeful the optimists would like to be, this is also into what is expected to be a return to major US Thanksgiving travel and gatherings a week from today.

Might it really be that this will bring a reduction of new cases despite those rising prior to this higher risk time? Might it also be that US vaccination progress (that is less than Europe and the UK) will bring a period where the economic impact is going to be very limited? Possibly. Yet we recommend keeping an eye on that potential general public reticence regarding the 'gathering' economy. It is an even more powerful indication for future US economic performance in a world where the pandemic is once again resurgent, and might even inform our view beyond any government action… it might also extend to influencing the public elsewhere.

While sustained inflation and especially its impact into UK and European energy prices this Winter will be a forward consideration, and China is on hold for now, the COVID-19 impact that many had hoped would be in the rearview mirror by now is once again a key consideration. The cross currents on that noted above form the critical choices the markets and their participants will need to make.

Courtesy Repeat of Tuesday's 'Critical Cross Current Choices' ALERT!!
The markets have arrived at a juncture where there is both current good news and bad news along with positive and negative anticipation. While that is always the case to some degree, it is particularly pronounced at present due to some of the key factors we have highlighted previous. While this is very evident in the 'country' tendencies in foreign exchange, it is also still the case in the resilient 'risk-on' psychology in US equities while the global govvies are also holding up.

While that general perspective deserves more definitive articulation, first we will provide additional background on how each area is playing out in general. In the first instance is inflation, which remains a major negative that was reflected in this morning's over the top French and Italian CPI and US Import/Export prices after last week's also much higher than expected US CPI. Just to put an emphasis on it, this is also with strong overall economic numbers all of this week so far, like Chinese Retail Sales and Industrial Production and today's US Retail Sales.

As such, inflation is looking to remain a sustained problem. Yet as has been the case, retailers are showing an ability to pass along enough of the elevated costs to the consumer to also maintain healthy corporate earnings. This is true of all of them from Walmart to Home Depot, which will continue to support elevated US equities valuations in the near-term with an emphasis on watching turnover.

The risks to the Chinese economy have been a recent concern, especially as it might be impacted by any additional acute problems with its major property development companies. The issue is not the direct financial harm from any outright defaults, but rather the 'ripple effect' out into the Chinese economy if any major developer (like Evergrande) or developers should cancel projects. It is similar to the risk seen when the US Housing Bubble collapsed in 2008.

In both construction employment and the smaller businesses which depend on spending of those workers the net impact for the economy might be quite large. As last Thursday's Reuters article (https://reut.rs/30vNEZh) notes, "*Investors are worried about wider contagion from the property sector which has seen a string of missed offshore debt payments*…" While it is always possible that the central government might step in to avoid any broader economic fallout, at least so far… "*There are absolutely no fundamental changes or relaxations on the property lending caps*…" This leaves ongoing lack of financing risks out there for now.

Last, yet by no means least, is unexpectedly (at least by some folks) heightened concerns over a resurgent COVID-19 pandemic after so many (present advisor excluded) had been noting imminent

arrival of a 'post-pandemic' environment. Due to this having been extensively explored in Friday's 'What A Week' ALERT!! (repeated below for your ease of access), we will be brief today.

As previously noted, while the drop in US cases has been impressive, that was from the surge back to daunting levels through all of August and September. In essence, the 'improvement was only to 'less bad' rather than any great degree of elimination of the overall pandemic on average in the US (or elsewhere as well.)

Also as already highlighted previous, the current CDC US New COVID-19 Cases graph (https://bit.ly/3oCDM8w) shows a sharp increase back to the 125,000 level not seen since late September. The 7-Day Average is also trending up again from its recent probing of the key 65,000-70,000 area. That is important as July 2020 peak, above which the pandemic exploded into last Winter, and the April 2021 level on the way back down at twitch the new cases stalled prior to atypically surging again into this Summer. This all becomes more telling again over the next week as the level from which the US enters its key Thanksgiving travel.

Yet, here as well, there is a choice for the markets to make on whether any COVID-19 resurgence will weigh heavily on the economies where that occurs. Given the now quite high levels of vaccination in many countries (outside of a US that is languishing around 60% fully vaccinated), might there be much less of an impact on the global economy? Possibly. Yet that will depend in good measure on whether local outbreaks cause national or local officials to impose restrictions or quarantines once again that affect the economy. It is going to be a fluid situation.

Yet, getting back to the impact of the general costs from inflation, it appears that in addition to any COVID-19 impact Europe and the UK are going to see quite a bit of pressure on consumer spending from much higher energy bills this Winter. However much government agencies may try to ease the burden, the alarmist view in the UK is that many of its citizens will need to "...choose between heating and eating." (See Thursday's ALERT!! also repeated below for more on that.)

That higher energy cost drain on household income will likely also affect the 'discretionary spending' habits of Europeans affected by similarly higher energy costs this Winter. Even as better off as the US may be, Thursday's ALERT!! also highlighted the US Bureau of Labor Statistics 'Real Earnings' release that showed the labor force had fallen well behind inflation during September-October.

It is most interesting that Thursday's title had also alluded to how 'curious' it was that with all of the US problems (extending into the political sphere as well) that the US dollar should have developed a 'haven' bid, with the US Dollar Index up to a new 16-month high above its 94.74 September 2020 trading high. Yet that is substantial on the back of weakness in the inflation and COVID-19 plagued (literally) UK and Europe. The Australian dollar that had seen the worst of its major COVID-19 surge over its just ended Winter has been holding up well.

Where this leaves the markets is in a more balanced state than the 'whipsaw' back from late last week's heavy temporary 'risk-off' activity. It is likely the US equities can be more of a two-way trading market after the December S&P 500 future neared and rebounded from the 4,621 major 'swing count' Objective that leaves it back up closer to low 4,700 resistance (with a 4,730 Oscillator level.)

The global govvies still need to be concerned about the elevated inflation levels, which are both expected to continue and are well above the current yields on all of the government (i.e. 'risk free yield') instruments. Yet the degree to which the economic situation deteriorates on the factors we have noted likely means they will also be more of a two-way street for a while compared to September-October.

This is the critical consideration
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/3HsfCX2 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. After that was exceeded, a 4,621 major 'swing count' was the next key threshold, with the next key weekly Oscillator thresholds up into 4,705 and 4,730 this week (still rising $20 per week.) After stalling into the lower one two weeks ago, there was finally a reaction... yet only down to near 4,621.

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