Our Guides - the **Technical Trader's Guide** and the **Macro Trader's Guide** both deal with these and many other markets in much more detail over multiple time- frames. **Key Trades Bulletins** subscribers receive a detailed report on every trade we enter for our Key Trades Portfolio. More details about all these products: CLICK HERE

Market Update 26th March 2009

Whither the Dollar? ("Yours!")

The Macro Trader's view:

After a period of strength which began in October, albeit with a serious correction in December, the Dollar once again looks in danger of suffering a fresh bear market.

The reasons for the Dollar's strength which originally began in July 08, can largely be put down to the realization among traders that the Euro zone and other leading economies were going to suffer at least as much as the US, and in some cases more.

The Euro zone, for instance, had initially been seen as the economy most likely to emerge from the global crisis relatively unscathed. So too was Japan. But it became brutally clear that neither were as well insulated as first thought.

Indeed, both the Euro zone and Japan have suffered sizable declines in industrial output, with Japan seeing exports collapse at a record rate. This realization and the wave of euphoria that surrounded the election of the new US President, gave the Dollar a bull impetus that on two occasions has looked like the start of a great fight back by the Dollar towards levels not seen in several years.

However, there has been a clear change of sentiment. President Obama sent congress a budget with a US$1.8T deficit which began to ring loud alarm bells: could the US sustain such large deficits and who was going to buy all this new bond issuance?

For a while these fears were largely quelled by the argument that the surplus economies had little choice but to keep on buying US IOU's or else see the value of their holdings collapse.
While that may hold true in the short and medium term, the Chinese recently voiced their concern over the security of their Dollar assets, seeking a guarantee from the US over their value. This week those concerns intensified. China called for the Dollar to be replaced as the

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World's reserve currency, urging a debate about the IMF's SDR's being beefed up to fill that role.

In addition, Russia (another large surplus economy with in excess of US$400.B in reserves) has also called for a new global currency to be created. This cannot happen overnight, but is the world starting to lose confidence in the US Dollar and more importantly, US economic policy which largely underwrites its value?

If global confidence in the Dollar were to ebb sufficiently, it could be the start of a long bear market.

The consequences are serious as currently there is no viable alternative. But the likes of China, India and Russia, not to mention the Middle East oil exporters who also hold vast Dollar reserves, are sounding serious, and they might just now have enough economic clout to bring about a serious debate, which would not be Dollar friendly.

Add to this the fact that the US fiscal stance is, in the words of the Congressional budget office, 'set on an unsustainable path' and the Dollar could suffer a more immediate sell-off as a result of the administration suffering severe difficulty funding the massive budget deficit.

Only yesterday a 5 Year note auction failed to attract its expected interest.

We judge the writing is written clearly on the wall: be careful of the Dollar.

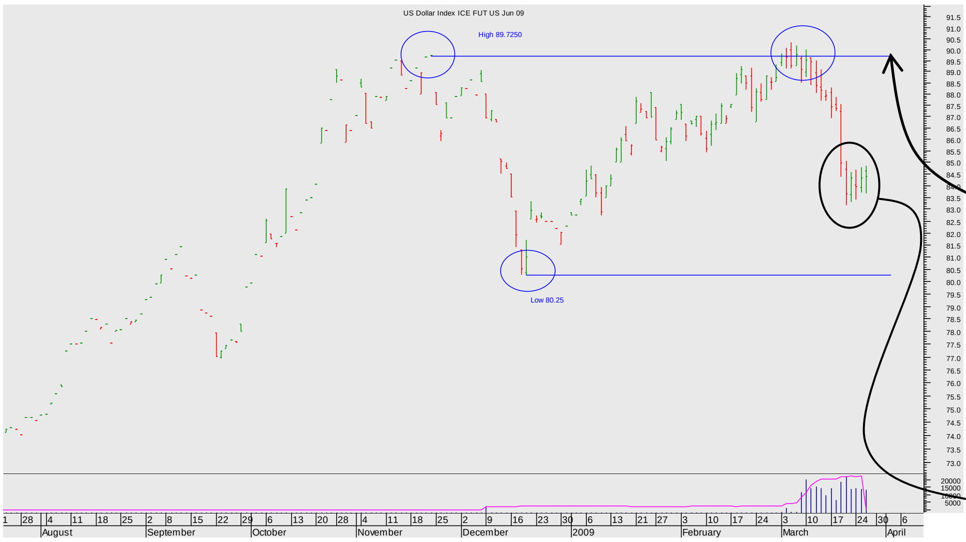
The Technical Trader's view:

DAILY CHART

The US Dollar Index broke a powerful and well-established down trend in the autumn of 2008.

But the strengthening since then seems to have stalled.

Look closer.



DAILY CHART

Here's that pause in more detail.

The double failure at 89.7250 is important.

The pull back from that has come halfway towards the critical low at 80.25.

It certainly looks like a Pennant formation.

And if Pennants complete then they tend to move the same distance as the fast prior move.

Implying a break of 80.25 (which would, of course, complete a powerful bear Double Top)

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DAILY CHART

An equivalent possible reversal pattern can be found in the Dollar Euro.

The Double Bottom is clearly a long way from completion – requiring a break up through the High at 1.4716.

But if the falling diagonal broke (currently 1.3850) that would be small additional bear Dollar evidence…

… and near term, the last few weeks' trading look very like a bear flag (for the Dollar).

Mark Sturdy

John Lewis

Seven Days Ahead

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