



9th February 2012

Market Update:

Oil is reacting at last but is it a buy?

UPDATE
Technical
Fundamental





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WEEKLY CHART

The market has rallied hard from the \$40 lows in early 2009.

The 2011 sell-off found good support at the 50% Fibonacci retracement at \$74.

Bouncing twice from \$74, the market has stagnated around \$100.

Now look closer.

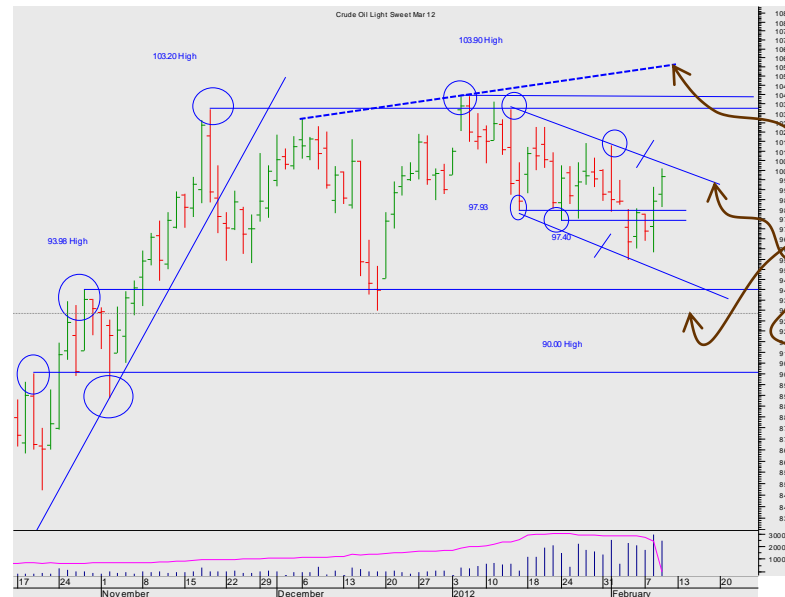
DAILY CHART

The stagnation in the week chart can now be seen at a trading range bounded by the 104 Highs and the 93 7/4 Prior high and Fibonacci supports.

There are 3 latent possibilities in the price action within the range:

1. A Double Top possibly, which would be competed on a breakdown through \$93.
2. A bear channel (but which is akin to a bull parallel flag surely) which would be completed on a break up through 100.25.
3. Might there also be a continuation Head and Shoulders on a break up through the possible Neckline at 105.50?

Note the good volume on the recent rally. On a break of the \$100 diagonal, expect a test of the Pivotal Highs band at 103.20-90.



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More



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FUNDAMENTALS:

Apart from being an almost indispensable resource globally, oil also acts as a bell-weather in two ways:

1. The rise and fall of geopolitical tensions generally has a direct impact on the oil price especially when linked to oil producing regions, and
2. The oil price will rise or fall in reaction to the health of the global economy due to the impact that has on energy demand.

After a sell-off throughout much of last year, driven by concerns about the health of the US and global economies together with the deepening Euro zone debt crisis, oil began a rally that started early in November 2011.

This was driven by a run of strengthening US data releases that pointed to a pick up in the US economic recovery. Although the Fed continued to voice its concerns about the fragility of the recovery and was concerned the Euro zone sovereign debt crisis held the potential to tip the US and global recovery back into recession, traders responded to the expected impact a stronger US economy would have on energy demand **by taking the oil price higher.**

At the same time, the long running stand-off between the major powers and Iran over Iran's nuclear program moved back to centre stage as estimates about how long it would take Iran to develop a nuclear weapon were cut.

Iran also stoked the tension by test-firing longer-range missiles that could potentially carry a nuclear warhead, prompting the US and her allies to enact stronger sanctions in the hope the Iranian regime would enter into serious negotiations.



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FUNDAMENTALS: CONTINUED

Alarmed by the prospect of a nuclear armed Iran, which is openly hostile to Israel, rumours started circulating once again about Israel planning a unilateral strike on Iran's nuclear facilities. But, despite all of this tension, and the on-going improvement of US economic data, the oil price has failed to build on those early gains.

Over recent weeks the market appears stuck in a sideways trading range, and may actually have lost its bullish momentum, **but surely a sell-off in oil now would run counter to the forces supposedly underpinning it, or would it?**

The US economy is printing stronger data. Only last week Non-Farm Payroll reported a healthy jobs gain with a drop in the unemployment rate and the ISM non-manufacturing survey came in much stronger than expected.

The Euro zone crisis hasn't gone away, but recent data releases there seem to show the chances of recession have receded with the German economy still performing strongly.

And the geopolitical scene hasn't changed much either, the US and EU have implemented strong economic sanctions that basically prevents the purchase of Iranian oil and the regime remains defiant about its right to pursue a nuclear program that they claim is for electricity generation.

But what about oil demand. The IEA has recently revised down its forecast for global oil consumption, and revised up its estimates for oil production. Additionally, the US is developing various domestic sources of energy reducing her reliance on imports. So where now for oil? **We judge the standoff with Iran would have to turn hostile to send oil prices higher in the short/medium term meaning more frustration for the Bulls is likely.**

But given the risks would you go short?



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