

SevendaysAhead

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The Macro Trader's guide To Major Markets

23rd – 29th November 2004

Short Sterling hangs on.

Dollar remains under pressure.

Gold makes new highs as Oil bounces back.

John Lewis

SevendaysAhead

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About John Lewis

John Lewis has worked in the London financial markets for 27 years. He joined Standard Chartered Bank London in 1976 trading the Sterling money markets.

He then trained as a floor trader with Holco Trading on the London Commodity Exchange specialising in cocoa and oil futures.

He began to trade off the floor with Drexel Burnham Lambert becoming Deputy Manager of their Money Desk in Europe responsible for all funding, money market trading and FX hedging for the European operation.

He rose to become Deputy Global Head of Proprietary Trading with Skandinaviska Enskilda Banken and thence Head of Proprietary trading Svenska Handelsbanken London.

After 1998 he moved into the hedge fund business as a senior fund manager of Weavering Capital UK.

Now in association with *SevendaysAhead* he works with a wide variety of financial institutions and independent traders, utilizing his long experience and successful trading record.

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UK MARKETS

SHORT STERLING

WHAT HAPPENED LAST WEEK

	Week of 15 th November
Monday	
Tuesday	RICS House price balance. -40 WEAKER THAN EXPECTED CPI 0.3m, 1.2y. AS EXPECTED RPI-X 0.2m, 2.1y. HIGHER THAN EXPECTED
Wednesday	MPC minutes 9/0. AS EXPECTED Unempoyment +900, WORSE THAN. rate 2.7%. AS EXP Avg earnings 3.7%. LOWER THAN EXPECTED
Thursday	PSNCR -1.4B. LESS THAN EXPECTED PSNB 0.8B. LESS THAN EXPECTED Retail sales -0.4m, 6.0y. WEAKER THAN EXPECTED
Friday	

Last weeks calendar, as above.

Last week the data continued to paint a picture of a slowing economy; the RICS house price survey continued to decline, unemployment increased slightly, inflation remained near the lower half of the mandated target and retail sales fell on the month. The minutes of the earlier MPC meeting were as expected; 9/0 and apparently they didn't even discuss tightening policy. An assertion made by the Governor of the BoE earlier that

falling house prices wouldn't lead to falling consumer demand does not hold water since with wage increases having been well contained for a long period most people's sense of increasing wealth had come via the housing market. The markets reaction to this was clouded as a report from the Nationwide claiming House prices would grow in 2005 sent the market lower.

JUNE 05 SHORT STERLING



See how the market reacted to the Nationwide report on house prices claiming they would grow next year.

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THE WEEK AHEAD IN SHORT STERLING

	Week of 22 nd November
Monday 9.30am	
Tuesday 9.30am	
Wednesday 9.30am	
Thursday 9.30am	BBA Mortgage lending n/f CBI Monthly trends survey/Quarterly forecast n/f
Friday 9.30am	GDP 3 rd Q 2 nd 0.4% m, 3.0% y.

This week's calendar, as above.

This week there is very little in the way of data to sift through. Friday's GDP data provides the only heavy weight release and as this is the second showing, unless much different to the first; it will have little impact on the

market. In the absence of much fresh data it will be interesting to observe how the market trades. Bull markets move quietly higher when left to them selves.

MY TRADING STANCE: BULLISH.

Last time I was bullish of June 05.

This week I remain bullish of June 05.

Although the market closed lower on the week I maintain my bullish view. After the Bank of England clearly stated in its latest Inflation report that house prices are expected to decline from current levels, Barclays Bank, which owns the Woolwich, has written in a statement intended for the stock exchange, its view that house prices will decline by 20% over the next 2 years.

BULLS should hold their positions, markets never move in straight lines. **BEARS** wait and watch. Even if rates do eventually move high by a further

No doubt we will see more such reports emerge now this view is becoming mainstream thinking as economists are pack animals by instinct. If they are right, and I think they will be, it is inconceivable to me that consumers will continue to spend with alacrity whilst they watch their single largest asset diminish in value.

25bp that will be seen as the peak and the next move as a cut so there is little mileage to the down side.

THE GILT

MY TRADING STANCE: NEUTRAL.

Last time I was neutral.

DECEMBER 04 GILT



This week I remain neutral.

Much the same as Short sterling, the Gilt traded lower on the week even as domestic data painted a picture of a cooling economy. Across the Ocean the US was showing a rather unpleasant uptick in both Producer prices and consumer prices and this had the effect of pushing bond markets including the Gilt lower over the course of the week. As I have often said and am happy to repeat, I prefer to steer clear of this market since Government finances are

coming slightly off the rails and with a General election possibly only as little as 6 months away, investors will have to begin focussing on how policy will evolve around this period. Spending cuts are off the agenda and although taxes will rise after the election the Government will want to give a different perception to the electorate as Labour has had its hands in our pockets ever since they came to power in 1997.

BULLS remain square.

BEARS stay square, last weeks data offered no comfort and the market will

trade short term on the slowing domestic economy.

THE POUND STERLING

MY TRADING STANCE: BULLISH.

Last time I was bullish the currency.

THE CABLE CHART



Note how the Pound consolidated the previous weeks rally. Only on Friday did it look willing to push higher.

THE STERLING/EURO CHART



Against the Euro, the Pound is clearly in a bear channel, slowly weakening along with the US Dollar.

This week I remain bullish of Sterling/Dollar.

The pound maintained its bullish tone largely consolidating its recent rally. The struggle between higher inflation in the US and a cooling economy here in the UK left the Pound unable to push any further a head. This will prove temporary as the US Dollar has further

to go on the down side. Indeed Alan Greenspan himself set the scene for further weakness when he stated on Friday that the US budget deficit needs to be reduced as does the current account deficit. Traders will conclude a weaker Dollar will be tolerated.

BULLS stay long of Cable we will see US\$2.00 against the pound over the coming months.

BEARS should stay square.

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US MARKETS

EURO DOLLARS

WHAT HAPPENED LAST WEEK

	Week of 15 th November
Monday	Empire Mfg 19.8. WEAKER THAN EXPECTED
Tuesday	PPI 1.7m, ex-F & E 0.3m. HIGHER THAN EXPECTED
Wednesday	Build'g permits 1984k, LESS , Starts 2027k HIGHER THAN EXP CPI 0.6m, ex-F & E 0.2m. HIGHER THAN EXPECTED Cap use 77.7, Ind prod 0.7. HIGHER THAN EXPECTED
Thursday	Jobless claims 334k. HIGHER THAN EXPECTED Philli Fed 20.7. WEAKER THAN EXPECTED
Friday	Greenspan speaks on Euro & economy. US NEEDS TO SHRINK DEFICIT.

Last weeks calendar as above.

Last week's data showed a mix of higher inflation, both producer and consumer coupled with stronger industrial production and capacity utilization numbers suggesting that, together with the very strong non-farm payroll data at the beginning of the month, the Fed will carry on tightening policy at each of its regular meetings well into next year. Fed chairman Alan Greenspan on Friday, added to the

debate when he said the US budget deficit in Dollar terms was too large and had to be reduced before foreign investors demanded higher rates of return and also to facilitate a reduction in the current account deficit. His view was this would be the best way of bringing about the needed correction rather than the Fed induce a recession through much tighter policy. The market responded by selling off.

JUNE 05 EURO DOLLARS



See how the market added to losses after strong PPI and CPI inflation data.

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THE WEEK AHEAD IN EURO DOLLARS

	Week of 22 nd November
Monday	
Tuesday pm	Existing Home sales 6.75M.
Wednesday pm	Durable goods 0.5%, Ex-Transport -0.2% Jobless claims 335k Uni of Michigan Confidence 96.0. New home sales 1200k
Thursday pm	Thanks giving day; - US MARKET HOLIDAY.
Friday	

This week's calendar as above.

This week the main focus will be the thanksgiving holiday on Thursday and traders will be reluctant to take any new positions especially since the calendar this week is very light with only

Wednesday offering any meaningful data; of this Durable goods is a very volatile number and with the market closed the next day, unlikely to force much trading activity.

MY TRADING STANCE: NEUTRAL.

Last week I was neutral of June 05.

This week I remain neutral.

Although the market has a distinct tone of bearishness about it, this is primarily due to the non-farm payroll report earlier in the month and last weeks inflation data which was largely driven by higher energy costs. Before I conclude the soft spot is passed and the economy is once again firing on all cylinders I want to see another payroll report. If that too shows strength then I will join the camp of the bears, until

then I remain sidelined. The Fed will undoubtedly continue increasing interest rates at the current pace but at which level will they stop. Neutrality is difficult to judge; dependent largely on the current growth and inflation rate, which is roughly 5%. However the fed argues that in the current environment it is more like circa 4% because of continuing spare capacity and labour market slack.

BULLS for the time being remain square.

BEARS who are short should proceed with caution.

THE US TREASURY NOTE (10 yr)

MY TRADING STANCE: BEARISH.

Last week I was neutral.

US 10yr NOTE DECEMBER 04



This week I am bearish.

Last week I said again I expected to see the market try to regain some of the ground lost as a result of the very strong non-farm payroll report at the beginning of the month and it did, but as I also expected, the market failed and pushed back down towards the recent lows. This was mainly due to comments made by Fed chairman Alan Greenspan on Friday when he was talking about currencies. He said the US budget deficit was much too large and should be reduced before investors demanded higher real returns. Although he said foreign investors were still willing to

buy US debt, they may not want to continue amassing US IOU'S indefinitely. This is a theme I have aired several times over recent months. Indeed the Government of India announced only 3 or 4 weeks ago that they would divert a portion of their foreign currency reserves away from US debt and use it to finance infrastructure projects in their own country. If more semi developed countries with large foreign exchange reserves adopt this tactic the US will be in trouble. Greenspan recognises this and wants action a head of such an event.

BULLS stay square, if not already.

BEARS run small short positions. I expect the market to push lower.

THE DOLLAR

MY TRADING STANCE: BEARISH.

Last week I was bearish the Dollar.

EURO/DOLLAR CHART



This week I remain bearish of the Dollar.

Last week the Dollar continued to weaken, pausing briefly on Thursday as stronger CPI, capacity utilization and industrial production numbers lent some support. However this was brushed aside by Alan Greenspan and his comments regarding the unsustainable US budget deficit. Currency traders took these comments as a green light to continue selling the Dollar especially as he stated that a smaller Government deficit would help bring the current

account deficit under control as it would free up domestic resources currently being swallowed up by the Federal Government. This is akin to the situation that existed during the cold war era. Big deficits used to fund big military which was domestically resourced and served to drive up inflation as defence suppliers knew the US Government did not want to be reliant on foreign defence industries.

BULLS stay square.

BEARS stay short and continue to use any pull back to add on.

EURO 12 MARKETS

EURIBOR

WHAT HAPPENED LAST WEEK

Week of 15 th November	<u>German</u>	<u>French</u>	<u>Italian</u>
Monday		Investment survey 5% WEAKER THAN EXP	CPI 0.0m, 2.0y. AS EXPECTED
Tuesday			
Wednesday		Unemploy'm't 0.1%. AS EXPECTED	Trade bal -921m Trade bal EU -141m WORSE THAN EXP
Thursday	PPI 0.9m, 3.3y. WORSE THAN EXP	Current a/c -158m. LESS THAN EXP	
Friday		GDP 3qtr 0.1q, 2.0y. WORSE THAN EXP CPI 0.3, 2.1y. AS EXPECTED	Ind orders -0.1m, 5.3%y. HIGHER THAN EXP Ind sales -1.0m, 4.8y. HIGHER THAN EXP

Last week's calendar; as above.

Last weeks data showed Producer inflation worsening, GDP to be disappointing and Trade data worse than expected. The Euro zone economy continues much as before and it was external data which seemed to drive the

Euribor market last week. Worse than expected US inflation data weighed on the market and in spite of continued Euro strength against the US Dollar the market moved lower.

JUNE 05 EURIBOR



See how the market is unable to advance even though the economy continues to perform badly. Instead it is led lower from abroad.

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THE WEEK AHEAD IN EURIBOR

Week Of 22 nd November	<u>German</u>	<u>French</u>	<u>Italian</u>
Monday			
Tuesday	GDP 3Q 2 0.1%q, 1.3%y		Trade Bal 1000M
Wednesday			Consumer Conf 105.7 Retail sales 0.2m, -0.5y.
Thursday	Import prices 0.7m, 3.6y. IFO 94.6		Business Conf 90.5
Friday	Consumer Conf n/f	PPI 0.5m, 3.5y.	

This week's calendar as above.

This week sees a light weight calendar. German GDP on Tuesday is a second look at the 3rd quarter, Italian retail sales on Wednesday will likely confirm what we already know; the Italians aren't

spending and German IFO on Thursday will give an insight into that country's business climate. In all a week when in the absence of any lead the market will drift sideways.

MY TRADING STANCE: NEUTRAL.

Last week I was neutral.

This week I remain neutral.

I still see little potential over all in this market and would advise those who are bullish to trade Short Sterling and bears to trade Eurodollars. If it is the Euro

zone one wishes to trade then the Bund still looks inviting but not Euribor. At least until something happens to knock the ECB out of its current torpor.

BULLS stay square and watch
BEARS do likewise.

THE BUND

MY TRADING STANCE: BULLISH.

Last week I was bullish of the bund.

THE BUND DECEMBER 04



Note the mainly side ways price action which is in distinct contrast to the US and UK bond markets.

This week I remain bullish of the Bund.

The Bund largely consolidated its gains from the previous week, ending just a little lower. The overall performance was impressive for the bulls as unlike the US Treasury market and the UK Gilt, both of which traded lower, the bund maintained its bullish feel supported by the continuing strength of the Euro against an increasingly beleaguered looking US Dollar. Indeed after Alan Greenspan's comments

regarding the sustainability or otherwise of the now record US budget deficit, the Bund would be a natural alternative to the US Treasury market for all those large holdings of foreign currency reserves which countries like; India, China and the rest of South East Asia currently hold. Naturally if this switch were to take place, even in part, the demise of the US Dollar would be hastened.

BULLS stay long and run a stop at 117.17. With the economy underperforming and the currency over

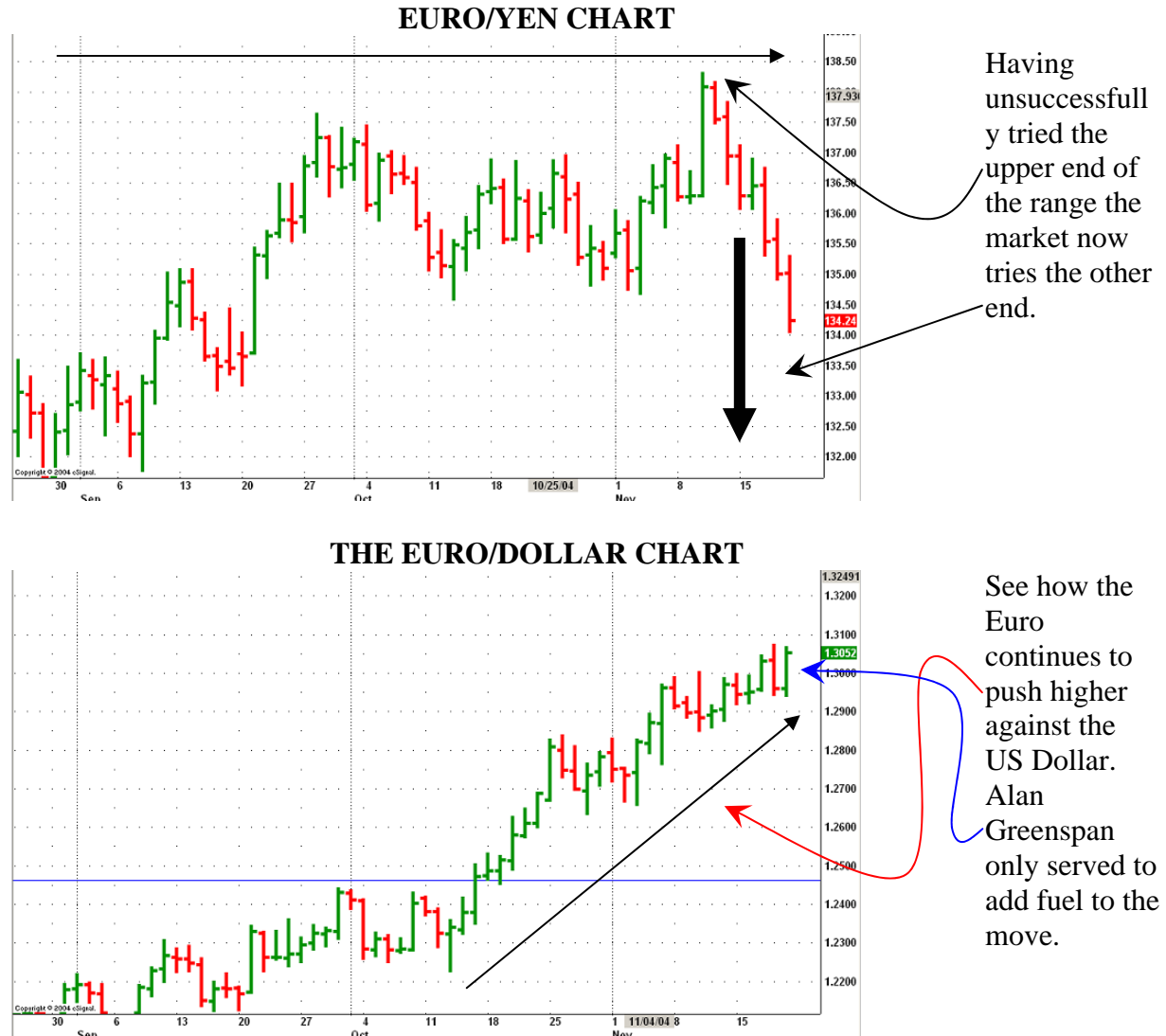
performing; as they say in the theatre, "this one can run and run".

BEARS stay square while the market trades above 115.90.

THE EURO

MY TRADING STANCE: BULLISH.

Last time I was bullish the Euro.



This week I remain bullish.

The Euro has remained at the high's against the US currency and there is no sign this move is near to completion; to the contrary with Fed chairman Greenspan sounding strong warning signals over the record US budget deficit and equally unsustainable US current account deficit, the move has further to run. US consumers for the time being appear to have absorbed

most of the energy price rises and carried on importing; albeit at a slightly reduced pace but not by enough to correct the now massive trade imbalance with the rest of the world. It would increasingly appear that any correction will only come about with a large currency adjustment, meaning a much lower US Dollar.

BULLS hold positions. The rally has much further to go 1.35-1.40 medium term.

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BEARS stay square.

COMMODITIES

GOLD

MY TRADING STANCE: BULLISH

Last week I was bullish of gold.

THE GOLD CHART



See how the tone in the currency market turned increasingly negative towards the US Dollar Gold continues to rally.

This week I remain bullish.

Last week the market continued the now familiar upwards march with US\$450.00 an ounce in its sights. This is made possible because as I have constantly said, the worlds major currencies represent struggling economies and investors not wedded to the foreign exchanges are turning increasingly to Gold. This trend will continue for so long as the Dollar is seen in need of downward realignment

BULLS stay long but run a stop at US\$440.00 an ounce. I expect Gold to move up to US\$450.00 an ounce as the Dollar eventually moves through 1.30 and on up to 1.40 against the Euro.

and the other trading blocks around the world; mainly the EU and Japan, are unable to take up the baton and generate sufficient economic growth themselves thereby bringing about the much needed rebalancing of the World economy, so that the whole burden of generating World growth and wealth doesn't fall solely on the shoulders of the US, as is currently the situation as evidenced by the massive US current account deficit.

BEARS Stay square until the market breaks US\$390.00 an ounce. Which isn't likely for the moment?

OIL

MY TRADING STANCE: BULLISH.

Last time I was neutral of oil.

THE CRUDE OIL CHART



See how the oil price pushed back up on Friday as traders once again started worrying about stocks for the upcoming northern hemisphere winter.

This week I am **bullish** of oil.

The market rallied strongly last Friday as fears surfaced over stocks being sufficient to meet demand during the fast approaching northern hemisphere winter. With the geopolitical situation in the Middle East little changed after one of the Palestinian leaders only narrowly escaping death at the hands of gunmen from the Palestinian side, the whole situation is little better than before Arafat's death. Although Iran professes to have stopped producing highly

enriched weapons grade Uranium, there are many stories circulating in diplomatic circles that Iran has a secret facility which it continues to operate. Further other stories claim it has or is on the verge of developing the capability to place a nuclear warhead on one of its own home produced missiles. A terrifying development given the support Iran is known to have given and still gives to terrorist organisations such as Hezbollah.

BULLS go long but run a stop at US\$48.00 a barrel.

BEARS square up and wait.