Short Sterling bounces at last.

Dollar finds renewed strength.

Oil remains a long term buy, Gold pauses.

WEEK 12 22nd – 28th MARCH 2005

THE MACRO TRADER'S GUIDE TO MAJOR MARKETS

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ABOUT SEVEN DAYS AHEAD

Seven Days Ahead publishes a variety of trading guides suitable for experienced market operators.

ABOUT THIS GUIDE

John Lewis's unique contribution is to bridge the gap between the trader and the economist by being acutely sensitive to the interplay of real world economic data with market expectations. Using his successful trading experience of 29 years, he studies the evidence in minute detail but tries never to lose sight of the big picture, or the day-to-day problems of running a position.
Each week the Macro Trader's Guide identifies the key economic releases of the previous week and explains why the markets reacted as they did. Then it anticipates the week ahead, emphasising the critical releases and predicts the likely market outcomes.
The Guide reveals money-making trading opportunities but includes a candid assessment of loss-making situations that can arise from trend less or too-volatile markets.

ABOUT JOHN LEWIS

John Lewis has worked in the London financial markets for 28 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 Handlesbanken London.

After 1998 he moved into the hedge fund business as a senior fund manager of Weavering Capital UK.
Now in association with Sevendays*Ahead* 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 14th March
Monday	PPI Output SA ex-FBTP 0.3m 2.6y. HIGHER THAN EXPECTED ODPM House Prices 10.0% LOWER THAN EXPECTED
Tuesday	
Wednesday	Unemployment rate 2.6 AS Change -800 LESS Avge earnings 4.4 AS THAN EXPECTED
Thursday	Retail Sales 0.2m, 3.6y. 3 mth/3mth -0.6 WEAKER THAN EXPECTED
Friday	Net mortgage lndg +4.8B HIGHER Feb PSNB -81M WEAKER Feb PSNCR 616M WORSE M4 Lending £10.9B HIGHER THAN EXPECTED

Last week's calendar.

Last week the market was driven by a steady stream of interesting data, on Monday; core PPI was a little above consensus but was eclipsed by the weaker than expected ODPM house price report, on Wednesday; employment data painted a benign picture; average earnings was in line while unemployment fell by less than expected although the ILO measure of unemployment rose by 22K, on Thursday; retail sales were weaker than consensus both on a year/year view and a three month/three month view, then on Friday; housing market data was surprisingly stronger with the net mortgage lending figure above consensus, M4 Sterling lending was also stronger than expected, but the Governments borrowing measures disappointed and were both worse than expected. The market reacted to all of this by focussing on the bullish data and steadily rallied throughout the week; ending seven ticks higher and forming what looks like the basis for a steady bull move over the coming weeks.

SEPTEMBER 05 SHORT STERLING

See how the market rallied on all the bullish releases as the week progressed.

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SHORT STERLING

THE WEEK AHEAD

	Week of 21st March
Monday 9.30am	
Tuesday 9.30am	CPI 0.3m, 1.7y. RPI-X 0.4m, 2.1y.
Wednesday 9.30am	Q4 GDP F 0.7q/q, C/A Q4 -8.0B MPC MINUTES 7/2 CBI Ind Trends -8
Thursday 9.30am	
Friday 9.30am	MARKET HOLIDAY GOOD FRIDAY

This week's calendar.
This week the calendar is light and it is a short trading week due to Easter, on Tuesday; CPI is released, which is expected to have crept up a little, this would not be a surprise since the recent cold weather must have pushed up the price of fresh food, mainly vegetables, also the Oil price has been climbing over the last few weeks and although prices at the petrol pump do not yet reflect the move, if it is sustained I am sure it will be and as we move into the summer holiday season, no doubt air lines will be trying to pass on these additional costs. On Wednesday; the final version of Q4 GDP and Q4 C/A data; if the C/A data is worse than consensus it will likely have an impact on the GDP report. The "main event", is the MPC minutes; these *will* set the tone for the market; I expect the lone dissenter from February to have again voted for a hike, since nothing much has happened to change his mind, but has any one joined him, retail sales were stronger in February on a monthly read so maybe that has been taken as excessive demand?

MY TRADING STANCE: BULLISH.

Last time I was bullish of September 05.
This week I remain bullish of September 05

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Last week I remained bullish of the market and it rallied steadily throughout the week, as traders focussed on the more bullish data. Regular readers will know I have held this view for some time, since I have considered the recent protracted retreat as over done, Retail sales has clearly cooled and the housing market continues to give mixed signals. On some measures house prices are indeed declining on others; slowing and until last week, this was largely reflected in the lending data. My own assessment of the economy is it is cooling, but just that. The housing market will be the key to activity over the next six months; if it bounces so will retail sales, but I don't think it will and for this reason I expect retail sales to remain subdued. Inflation will be a tricky call; with a slowing economy retailers will continue to discount, but the Oil market is on a strong bull run and I see nothing that will materially change that. The MPC will have to see through the noise of higher energy costs and focus on the core economy; although Mervin King is an arch inflation Hawk, he is also an astute political operator and for this reason I think his view will prevail and rates will stay on hold for several months yet. Just as well because I have little confidence in the ability of several members on the current committee.

BULLS stay long but remain wary of CPI and the minutes, I think the market will cope with a 7/2 vote but no closer, anything less, e.g., 8/1 and it will rally.
BEARS stay square unless the vote is closer than 7/2, or CPI unexpectedly spikes.

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THE GILT

MY TRADING STANCE: NEUTRAL.

Last time I was neutral.

GILT JUNE 05

See how the Gilt market mirrored that of cable. When weaker retail sales were released on Thursday; both markets moved lower.

This week I remain neutral.

Last week I adopted a neutral position as I felt there was too much uncertainty for a clear view of the market, I continue to believe that to be the case. After last week's budget the Governments finances are back under the spot light, and although the chancellor's attempted bribes were modest, they will not help the overall fiscal position, which will require attention once the expected election is out of the way. Together with slightly disappointing borrowing data on Friday; questions are again being asked as to whether Brown will meet his Golden rule, especially since his growth forecasts seem to preclude any notion of a slow down.
If inflation jumps by more than consensus when the CPI report is released on Tuesday, the Gilt will come under renewed selling pressure, however I believe that will be limited as the Pound would gain support from such an out come and this would, to a degree, spill over into the bond market and there is much talk about the expected 50 year Gilt issue which is expected to attract strong interest.

BULLS remain square, much uncertainty remains in this market and I see very little to recommend it. If Oil prices continue to rally as I expect, Bond traders will fret about inflation.
BEARS stay square until Tuesday's CPI and Wednesday's MPC minutes. If the vote is closer than 7/2 traders will sell into the market as they will again speculate the next move from the MPC is an increase; not my view.

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THE POUND STERLING

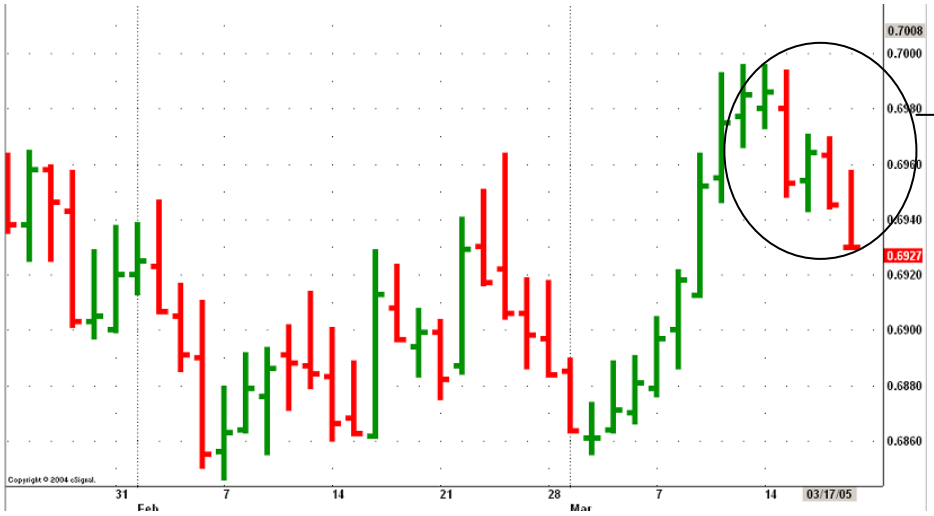
MY TRADING STANCE: BULLISH.

Last time I was bullish the currency.

THE CABLE CHART

See how the Pound moved side ways over the week with the two big swings on Tuesday and Wednesday due to conflicting US data releases.

THE STERLING/EURO CHART



Against the Euro the Pound faired better as the Euro endured the same fate against the Dollar as the Pound, but with much talk concerning the renegotiation of the Euro zone stability pact, the Euro was hit a little harder.

This week I remain bullish of Sterling.

Last week I urged traders to remain bullish of Sterling as I said I expected it to spend the week mainly consolidating the recent rally before making further gains. In the main that it is what happened. The Pound was unable to add to the rally for several reasons, these being; the softer house price data from the UK Government on Monday, then on Tuesday; the US released a near record high for net foreign securities purchases; which was Dollar supportive, then on Thursday; weaker than expected UK retail sales, which will make it harder for the MPC to justify an increase in interest rates in the near term. Even though the US reported a larger than expected Q4 C/A deficit on Wednesday, it was insufficient to sap the Dollar's renewed strength. For the Pound to regain its momentum and rally further the market will need a reintroduction of uncertainty concerning the MPC'S next policy move; this may come from CPI on Tuesday and the MPC minutes on Wednesday.

BULLS stay long, but if the CPI unexpectedly drops and/or the MPC minutes show a return to unanimity; square up as the Pound will lose ground to the Dollar which will receive a short term boost from this week's FOMC meeting. Bulls should run a stop at 1.9000 to protect against such an outcome.
BEARS stay square unless CPI or the minutes are supportive.

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US MARKETS

EURO DOLLARS

WHAT HAPPENED LAST WEEK?

	Week of 14th March
Monday	
Tuesday	Retail sales 0.5 WEAKER THAN EXP Less Autos 0.4 WEAKER THAN EXP Net foreign security purchases $91.5B MUCH STRONGER THAN EXPECTED
Wednesday	C/A Balance Q4 -US$187.9B HIGHER Housing starts 2200K STRONGER Permits 2070K STRONGER Industrial production 0.3 WEAKER Capacity Utilization 79.4 HIGHER THAN EXPECTED
Thursday	Jobless claims 318K HIGHER THAN EXPECTED Philly Fed 11.4 MUCH WEAKER THAN EXPECTED
Friday	Import prices 0.8m, 6.1y.HIGHER Export prices 0.2m AS U Michigan cons conf 92.9 WEAKER THAN EXPECTED

Last week's calendar.

Last week's calendar painted a mixed picture; on Tuesday; retail sales was weaker than consensus, on Wednesday; Industrial production was weaker than expected, on Thursday; the Philly Fed was materially weaker than consensus and on Friday; University of Michigan consumer confidence was also below expectations, however, Tuesday also saw the release of the 2nd highest ever level of net foreign securities purchases, on Wednesday; Q4 C/A deficit was larger than expected and capacity utilization was higher than consensus. On Friday; import prices increased by more than expected, raising inflationary concerns once more and so close to the up coming FOMC meeting. The market reacted in a volatile manner and although closed the week unchanged, there were some sizeable intra-day swings for traders to contend with, which given the profile of the data as above, was hardly surprising.

SEPTEMBER 05 EURO DOLLARS

See how the data whipped the market around all week eventually leading it back to where it closed the previous Friday. The continued volatility in the Oil market added to uncertainty especially on Thursday when the Oil price traded above US$58.00 a barrel.

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EURO DOLLARS

THE WEEK AHEAD

	Week of 21st March
Monday	
Tuesday	PPI 0.3 PPI Ex-F & E 0.1 FOMC Rate decision +25bp
Wednesday	CPI 0.3 CPI Ex- F & E 0.2
Thursday	Durable goods 0.8 Durables Ex Autos n/f Jobless claims 315K
Friday	MARKET HOLIDAY GOOD FRIDAY

This week's calendar.

This week the focus will be the FOMC meeting on Tuesday. From speeches and comments made recently expectations are for another 25bp increase. Also released on Tuesday is PPI which may have been adversely affected by the spike in Oil prices, on Wednesday; CPI is released, it is probably too soon for that effect to be registered here although Gas prices have been pushing up to record levels over the last couple of weeks. On Thursday; durable goods are released, this number has a history of volatility and the data is often significantly revised later in the month, so unless very far away from consensus, it will have a limited impact, especially with the Easter holidays looming large, traders will wont to go home square.

MY TRADING STANCE: BEARISH.

Last week I was bearish of September 05.
This week I remain bearish of September 05.

Last week I remained bearish, of the market and although it failed to add to the recent bear move, traders showed no real appetite to take the market higher. Although last week's data was uneven and offered support for bulls and bears, the underlying message is still; the economy continues to expand at a satisfactory rate and the labour market continues to improve with weekly Jobless claims data firmly anchored in the low 300k neighbourhood which is consistent with a healthily expanding economy. Even though the Fed has said on many occasions it views rising Oil prices as a tax on growth and is concerned by that affect more than inflationary implications, with the price of oil now at such a high level and still threatening to rally further at a time when there is little spare capacity amongst suppliers and the Chinese economy is such a voracious consumer of energy and commodities in general, the Fed may have to tweak its view and regard the spike in Oil prices as more of an inflationary threat than usual. This may cause it eventually to up the pace of its policy actions. While I expect policy to be tightened by 25bp this time; watch the accompanying statement for any heightened concerns over Oil induced inflation; if the wording does indeed take such a course the market will react negatively and price in a greater degree of tightening than hither to; the market currently prices interest rates at 41/2% by September 2006, that is to sanguine a view and the market could be at least 50 basis points out on its thinking.

BULLS remain square.
BEARS hold positions and add on if the Feds statement on Tuesday shows a heightened worry over inflation due to Oil prices.

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THE US TREASURY NOTE (10 yr)

MY TRADING STANCE: BEARISH.

Last week I was bearish.

US 10yr NOTE JUNE 05

See how the market tried to bounce from the lows on Monday, after the combination of the strong capital inflow report and weak retail sales on Tuesday and worse Q4 C/A deficit on Wednesday, but with Oil prices surging the market lost traction.

This week I remain bearish.

Last week I held to my bearish view and although the market failed to sell off, the rally was limited and lacked conviction. While Tuesday's net foreign purchases data was good news for the US economy because it showed foreign investors had lost none of their appetite for US assets which is essential for the funding of the record twin deficits, Wednesdays Q4 current account deficit reminded traders that such an inflow is required every month, after recent rumblings from Asian Central Banks hinting at a desire to diversify their foreign reserve holdings, the market cannot afford to be complacent just because they didn't repeat the statement again last week. With the economy continuing to grow at satisfactory levels and the US experiencing strong competition for natural resources from the Chinese, traders need to be aware that the likely consequence of the current spike in Oil prices; which increasingly appears structural, will be a re-emergence of inflation; something bond markets definitely dislike. Alan Greenspan himself said only two weeks ago that the current account deficit would be corrected by rising import prices. While at the time, I interpreted that to mean a weaker Dollar and still do, higher Oil prices will definitely play a part in bringing about such an outcome.

BULLS stay square.
BEARS remain short and look for selling opportunities.

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THE DOLLAR

MY TRADING STANCE: BEARISH.

Last week I was bearish of the Dollar.

EURO/DOLLAR CHART

This week I remain bearish of the Dollar.

Last week I held to my bearish view of the US currency, but in spite of weak retail sales, worse than expected Q4 C/A data, a weak Philly Fed and softer University of Michigan consumer confidence; the Dollar rallied, deriving its strength from the net foreign securities purchases report released on Tuesday. Despite all of the rhetoric and concerns about Asian Central Banks diversifying their foreign reserve holdings away from the Dollar; they bought US assets at near record volumes last month, traders took this as a bullish signal and the Dollar regained some lost ground. As welcome for the Americans as it is, that foreign investors are still willing to accumulate ever increasing quantities of US IOU'S, such purchases, if sustained, would undermine Greenspan's view that the market will correct the US C/A deficit via higher import prices achieved through a weaker Dollar. This may force the Fed to eventually resort to a more aggressive stance in its delivery of monetary policy, because if the Dollar and the bond markets are supported by such massive foreign inflows, the Feds current pace of tightening is a bit like running fast just to stand still; a lot of energy exerted but no ground covered. At this Tuesday's meeting I expect a 25bp tightening and this may disappoint traders to the extent that the Dollar losses momentum, however if they express concern over the inflationary implications of the recent and ongoing spike in Oil prices, the Dollar will remain supported as a more aggressive Fed will be anticipated in the future.

BULLS stay square until the FOMC statement is known; if it flags concern over Oil induced inflation then buy Dollars.
BEARS stay short; the US has still to tackle the two record deficits and if the FOMC statement reads unchanged Dollar bulls will be disappointed. Realistically, last Tuesday's report showing a near record inflow of foreign capital is unlikely to continue at such a pace.

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EURO 12 MARKETS

EURIBOR

WHAT HAPPENED LAST WEEK?

	Week of 14th March
Monday	
Tuesday	FR CPI 0.5m, 1.6y. AS EXPECTED DM ZEW 36.3 HIGHER THAN EXPECTED
Wednesday	IT C/A Deficit -4.350B WORSE THAN EXPECTED IT FEB CPI 0.3m, 1.9y AS EXPECTED
Thursday	FR C/A -3.911B WORSE THAN EXPECTED
Friday	IT Trade Bal -1.982M BETTER THAN EXPECTED DM PPI 0.4m, 4.2y. AS EXPECTED

Last week's calendar.

Last week the market had a relatively thin calendar to digest, on Tuesday; French CPI came in as expected and Germany's ZEW survey was stronger than consensus, on Wednesday; Italy released its Current Account data which was worse than expected and its CPI report which was in line, on Thursday; France released its Current Account data and it to showed a much worse deficit than expected. Then on Friday; Italy released its trade a/c data which was better than feared and German PPI was released which was in line with consensus. The markets reaction was curious; the Inflation measures were all in line and yet the market traded lower, why? The main reason was the various utterances by ECB President Trichet when he said he would not hesitate to tighten policy if necessary as a response to high Oil prices affecting inflation. Since Oil traded above US$58.00 a barrel last week; traders fretted over the course of policy.

SEPTEMBER 05 EURIBOR

See how the market was affected by Trichet's talk of higher rates.

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EURIBOR

THE WEEK AHEAD

	Week of 21st March
Monday	
Tuesday	FR Consumer conf -0.2
Wednesday	DM IFO 94.8 IT Retail sales 0.2
Thursday	DM CPI 0.2m, 1.7y.
Friday	MARKETS CLOSED GOOD FRIDAY

This week's calendar.

This week's calendar is again light and the market is closed on Friday for Easter. On Tuesday; a look at French consumer confidence; weak considering France is one of the Euro zones better performing economies, on Wednesday; German IFO; this has shown some stronger readings over the last few months but the real economy hasn't produced a performance to match, Italian retail sales are also due but these have been weak for some while. On Thursday; German CPI is released but unlikely to cause the ECB concern.
Sadly these numbers are unlikely to have any material impact on the market, that accolade will go to the ECB'S response to the softening of the stability pact due later today.

MY TRADING STANCE: NEUTRAL.

Last week I was neutral of September 05.
This week I remain neutral September 05.

Last week Euribor had a mixed week; it started off promisingly as the market added to yet another fledgling rally which was aborted when ECB President Trichet sounded alarm bells over inflation potentially being derived from rising Oil prices and how the ECB would not hesitate to react by raising interest rates. This neatly sums up the dichotomy in the Euribor market right now; traders want to take the market higher as they see the economy underperforming with the EU'S largest economy; Germany, teetering on the brink of recession and the others exhibiting, at best, patchy performances, but the ECB does not see it that way. In their eyes the Euro zone is more likely to suffer a bout of higher inflation than face economic contraction and they obviously see little or no risk to the already anaemic growth rate by threatening, let alone actually increasing, interest rates.

BULLS stay square, the fundamentals argue in favour of a rally, but the ECB has the market capped.
BEARS remain square; there is no bear case to trade off of. Although with the Oil price showing no sign of falling back, even after OPEC made an increase to its production ceiling, the ECB may engineer one by raising interest rates; LUNACY.

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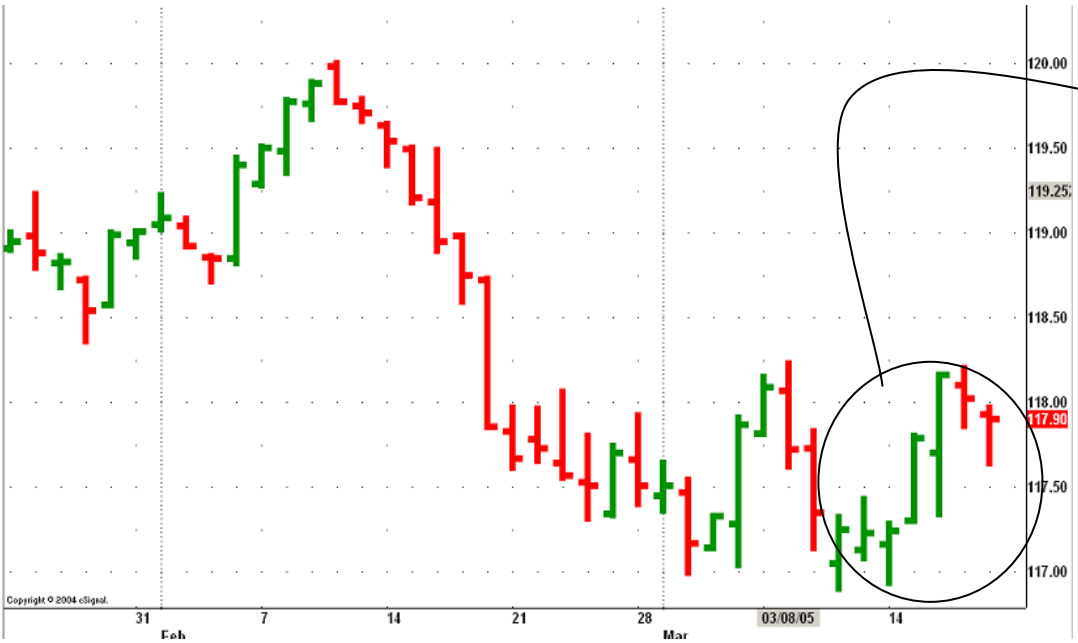
THE BUND

MY TRADING STANCE: NEUTRAL.

Last week I was neutral of the bund.

THE BUND JUNE 05



This week I remain neutral of the Bund.

Last week I was neutral of the Bund, being the long term bull of this market that I am, I was unwilling to join in what I saw as a correction and trade against my fundamental view of the market. I argued it was best to stand aside until the market turned bullish again and then buy into the rally. For a while last week it seemed the strategy was working and I was anticipating going long. As the week matured it again seemed wise to remain neutral and now the EU 12 politicians have agreed to relax the stability pact with the ECB announcing it will deliver its own assessment of the relaxation later today, it seems best to remain sidelined. The ECB has used its reticence over short term interest rates as a stick to beat the politicians into enacting much needed economic reforms; it placed much importance on the stability pact as a boundary to stop the politicians running ever larger deficits in an attempt to skirt around the ECB'S reluctance to lower short term rates. Even though several member states; Germany and France, not to mention Italy, were running deficits which breached the limits that pact imposed and had been for several years. The ECB took solace from the pacts provision that ultimately if the offending states did not eventually comply they would face fines; this it felt would stop them expanding their deficits. Now the pact appears to have been relaxed the ECB has lost its security blanket what will be its response? It could threaten to tighten policy if the politicians further expand their deficits, thereby engineering a much stronger currency, although paradoxically at the expense of higher bond yields which may force the politicians eventually to clean up their act. In this environment I will stand aside from this market and gauge the ECB'S response.

BULLS should for now, stand aside.
BEARS remain square until the ECB makes its views on the stability pact known.

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THE EURO

MY TRADING STANCE: BULLISH.

Last time I was bullish the Euro.

EURO/YEN CHART

See how the Euro moved side ways against the yen as the Dollar enjoyed a bounce.

THE EURO/DOLLAR CHART

See how the Dollar bounced against the Euro after news of strong capital inflows and higher Capacity utilization.

This week I remain bullish.

Last week I remained bullish of the Euro, saying minor swings were to be tolerated in order to stay involved in a market I expect to rally further. In the event the market eased back from the previous weeks highs as traders digested the massive monthly inflow of foreign capital into the US markets. As the Euro has largely benefited from investors selling Dollars as a result of the record US twin deficits, the dynamics in the market are clearly Dollar driven as no one would usually be an aggressive buyer of a currency whose economy so consistently underperforms as does the Euros'. However now that the EU 12 politicians have agreed to relax the terms of their stability pact, by crucially allowing "costs associated with the unification of Europe" to remain out side of the pacts terms, the way seems clear for some EU 12 countries to increase Government spending in an attempt to boost their hither to anaemic growth rates. This may eventually force the ECB to tighten monetary policy as it will probably view such moves as potentially inflationary; if this is the case the Euro will have gained two new sources of support; potentially better growth prospects from more public spending and higher interest rates. Good for the Euro, but not the Bund.

BULLS stay long and watch the US FOMC.
BEARS stay square and watch the ECB.

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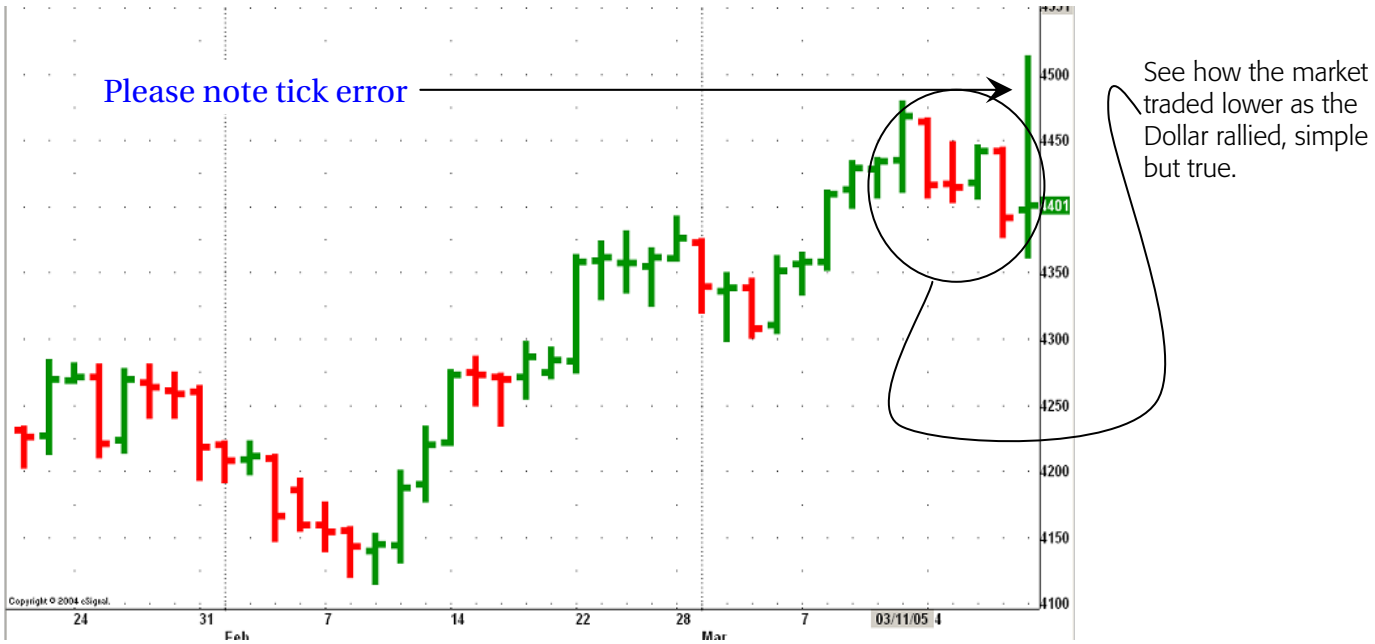
COMMODITIES

GOLD

MY TRADING STANCE: NEUTRAL.

Last week I was bullish of gold.

THE GOLD CHART



This week I am neutral.

Last week I remained bullish of Gold expecting it to continue with the rally, I opted for a stop at US$440.00 in case the rally suffered a set back; well it did and I was stopped out. Although the market did close back above US$440.00 an ounce the same day, I was unwilling to re-enter the market so close to where I was stopped out so quickly. The market sold off on the back of the Dollar rally which began after the US released much stronger than expected net foreign securities purchases data and lasted much of the week ignoring the larger than expected Q4 C/A deficit. Since the relationship between the Dollar and Gold has been very tight over the last year or so, it was unsurprising that Gold reacted as it did.

With the US Dollar rallying as I write, in anticipation of Fed policy action due from the FOMC on Tuesday evening, the Gold market will remain under pressure. The FOMC is expected to increase interest rates by 25 basis points to 2.75%, if this is, as I expect, all they do and leave the statement unaltered, the Dollar will suffer a relapse allowing the Gold market to recover and push on to higher levels.

BULLS square up and await the FOMC.
BEARS Stay square until the market breaks US$390.00 an ounce; which isn't likely anytime soon.

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OIL

MY TRADING STANCE: BULLISH.

Last time I was bullish of oil.

THE CRUDE OIL CHART

See how the Oil price rallied on Wednesday after the Chinese announced strong growth in yr/yr industrial production, even though OPEC increased its out put ceiling, which at 500,000bpd was quickly deemed insufficient.

This week I remain bullish of oil.

Last week I remained committed to the rally in the Oil market as concerns lingered over the long term supply/demand relationship. When on Monday OPEC announced they were considering increasing their production quota the market briefly dipped, and even when the Saudi Arabian Oil minister voiced his view that Oil prices were unjustifiably high and asked OPEC to increase production, which they did, the market snapped back and rallied further, this was fuelled in part by news from China of a 16.9% increase in its year/year industrial output. Since China has emerged as a large consumer of commodities, especially Oil, the market was reminded of recent reports highlighting the expected growth in world demand for energy and the insufficient response from supply. This propelled the Oil price to above US$58.00 a barrel and although it did ease back, the stage is now set for a further leg to the recent strong rally, which I suggested only two weeks ago may reach US$60.00 a barrel; that now looks less fanciful as the market in its current mood, driven by worries over supply at a time when not only the US economy is expanding, but also those of China and other Asian economies, placing a strain on known reserves, could push on eventually to US$70.00 a barrel.

BULLS stay long with a close stop at US$55.00 a barrel, the market is being driven by the realization that not enough new reserves are being found to cover increases in Asian led demand and although I fully expect the market to go higher it has come along way and profit taking may push it down short term; hence the stop.
BEARS stay square.

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