



Black Swan Currency Strategist

WEEKLY SUMMARY & OUTLOOK 6.23.2009

A Currency Strategist supplement geared towards intermediate- and long-term players

US Dollar Index (DXC)					
Last Price:		8018			
1-Wk Chg:		-0.8%			
	Last	Trend	RES	SUP	Comment
Monthly	8018	UP	8962	7131	---
Weekly	"	DOWN	8263	7768	Wave -4- correction complete?
Daily	"	UP	8263	7833	8000-level proving strong resistance
Key Intermarket Prices					
Weekly View					
		Trend	RES	SUP	Comment
S&P 500	890.5	UP	957	875	Wave -4- complete?
10-yr Notes	115	DOWN	120^18	114^10	Slipped below trendline support!
Gold	923.9	UP	1,004	865	Continuing to rollover
Oil	68.16	UP	76.57	43.8	Can global demand support this price?
EM Stocks	32.61	UP	35	26	Too much optimism it seems!
<i>RES= Resistance; SUP= Support; Blue = Chg since last week; Blue Bold = Chg of trend since last week</i>					
Recommended cash holding:		US dollar (No change)			

Key Changes/Summary from last week:

- No trend changes to key inter-market assets, but notable is 10-year T-Notes testing key support—again. Gold prices continuing to rollover, surprising the dollar doom crowd; oil and emerging markets could be due for a swift pull-back on a quick change in sentiment.
- The Intermarket moves: lower oil, lower emerging stocks and lower gold is significant for the dollar in two ways: 1) Suggest inflation expectation fears triggered by US dollar debt may be residing, and 2) Losing some safe haven status as fears over US currency reserve status prove overblown.
- Key Risk to US dollar Here: Treasury Bonds. Despite the correlated inter-market price moves referenced above, **if confidence is lost on the US's ability to handle its debt burden, and it's believed there is an implicit policy of dollar neglect, this would become a primary driver despite what the other asset classes are doing.**

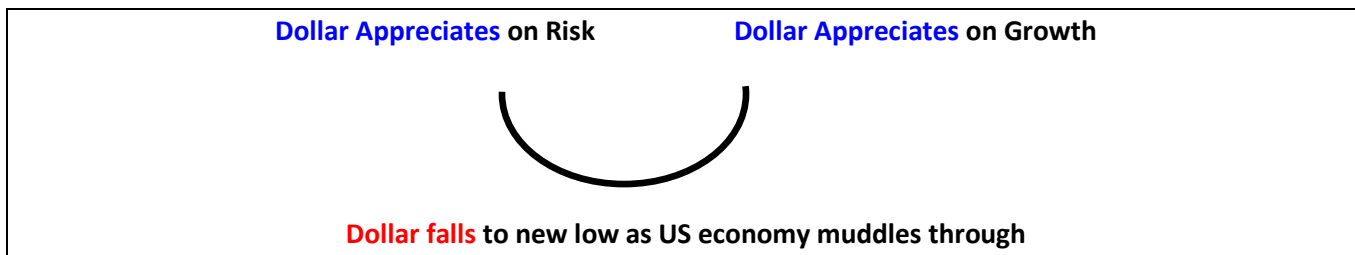
There is substantial risk of loss in forex, futures, and options trading. Past results are no guarantee of future performance.

- Seven day sideways chopping block has been eating us up of late; which suggests the tug-o-war between competing global macro themes. No change in \$ trend view since last issue: US dollar daily trend is up; weekly trend is down; monthly is up.
- The Dollar Smile (page 2) – It’s a simple theoretical construct that defines the major themes well.
- Last week we said: “Commodity currencies vulnerable to gold turning over and any correction in oil!” We are still waiting for a major breakdown here to support the green shoots morphing to brown weeds theme.

Dollar Smile & Themes

Where is the dollar going? ‘We don’t know’ is the short answer. But we place our bet based on themes—and price action of course. An excellent way to both visualize and better understand the competing themes in the market is by considering the Dollar Smile -- a concept created by former Morgan Stanley currency analyst Stephen Jen. And right now, the scenarios for divergent paths for the dollar are summed up well by the dollar smile.

Three scenarios gleaned from the dollar smile



Three major scenarios portrayed by the Dollar Smile.

- 1) **Left side of the smile reflects an appreciating dollar as global risk comes back into the financial system.** This is the risk aversion trade we have seen in a big way; it rocketed the dollar in July of last year as traders rushed to de-leverage, brought money home from risky asset investments offshore and hid in US treasuries.

We continue to see mini-bouts of risk aversion on the competing global macro views on growth—green shoots or not? Most believe risk aversion, as it benefits the dollar, was a one-off event ... and we won’t be seeing that again soon as the worst is behind us. However, if we consider industrialized nations may experience significant subpar growth on the rebalancing of the global economy—reduction of Western demand and Eastern production—this will lower profitability everywhere; thus reducing the margin of error and leading to a sustained risk averse period that would be dollar supportive.

- 2) **The middle of the smile reflects dollar depreciation against the major currencies as the US economy muddles through.** Implicit in this view is ongoing weakness in the US economy led by a consumer who continues to save, instead of spend. But inherent in this view is there may be growth elsewhere and the US government would be happy to fund that growth through increasing amounts of US dollar-based credit being thrown out into the world in two forms: 1) As a signal the Fed will not hike interest rates for a long time; and 2) Increasing amounts of debt buying, i.e. quantitative easing.

This sets the stage for significant dollar weakness and is very similar to the implicit weak dollar policy from the US that drove the dollar down from 2001 to March of 2008. And now, given the extremely low interest rates in the US, and overall dollar neglect by policy choice, it's not hard to consider the US dollar could become the new carry trade currency as US growth muddles through.

- 3) **The right side of the smile reflects an appreciation in the dollar on the back of a US growth surprise.** Now this would be a surprise to many, but it is plausible given the trouble in Europe. And keep in mind this currency game is all relative.

The scenario runs something like this: Despite the many warts in the US economy, the stimulus gains some traction and the Fed makes it clear it's time to start cleaning up the liquidity dumped into the market. This would imply not only that the US would be recovering faster well before Europe (we've always believed they were behind us in terms of the cycle), but it would also say the Fed will be hiking first, improving the negative yield gap on the dollar.

This scenario, if played out, would mean the US gets foreign direct investment flow (as players position for growth) and some hot money flow to achieve higher yields—both are highly self-reinforcing for a currency.

No doubt there are plenty of other plausible scenarios we could think of that might determine the path of the US dollar. But I think the three scenarios gleaned from the dollar smile provide usable analytical perspective.

What are we positioned for at the moment:

A big disappointment to the green shoots story of growth optimism and the dollar catches a multi-week risk aversion bid (left side of the smile)

...then we evaluate underlying fundamentals from there to see if the US is (or is perceived to be) growing faster than Europe and will emerge first, possibly along with China. If so, we shift to the right side of the dollar smile on relative growth—dollar rally continues.

However....

...the Muddle-Through and Implicit Weak Dollar Policy scenario is clearly in play; Treasury keeps selling debt and the Fed keeps monetizing and expecting the dollar to play the global stimulus role boosting asset markets. This policy could be very dangerous for the dollar, as the players would see it as the new carry trade currency and likely dump it accordingly for much better capital gain opportunities offshore.

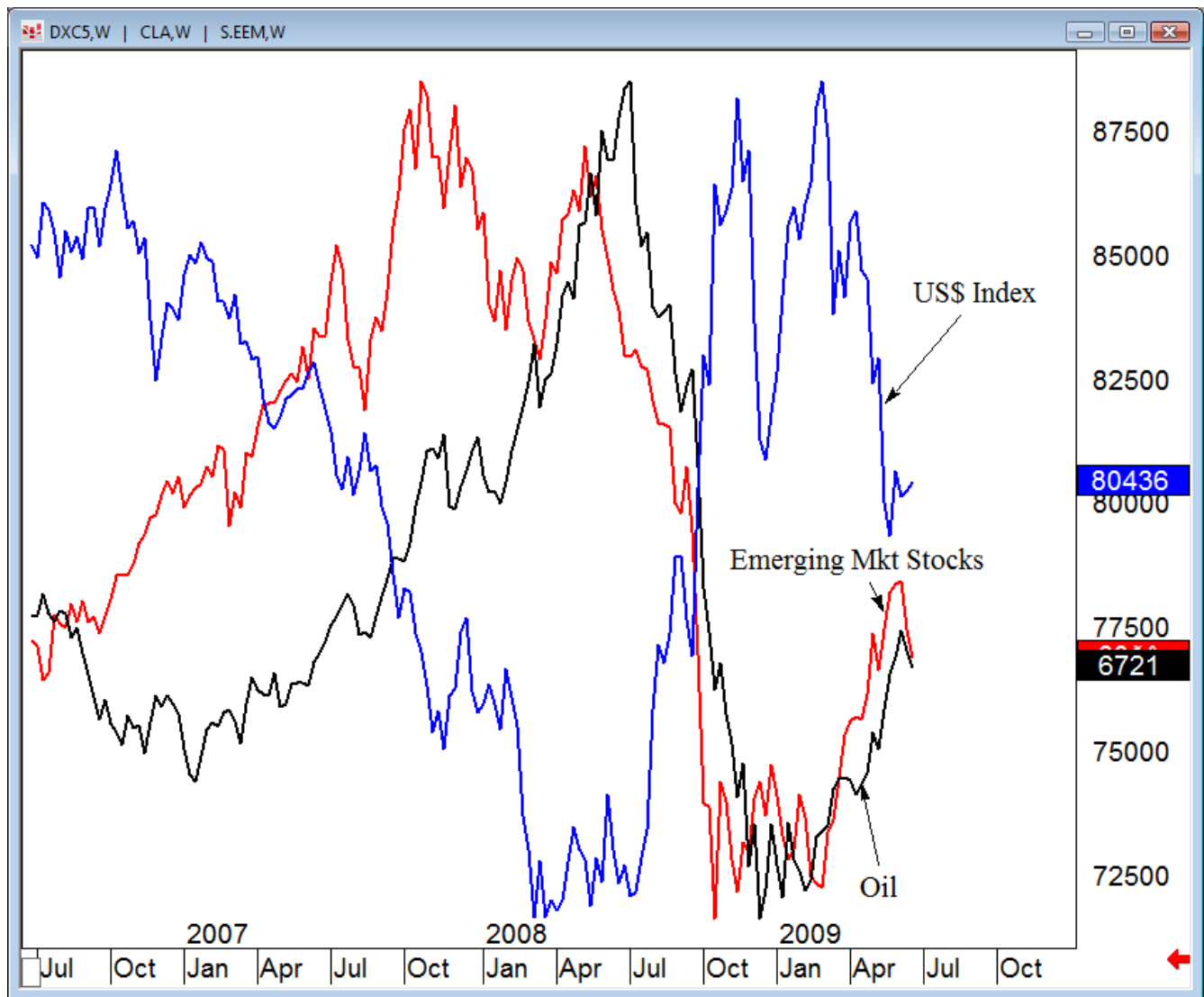
The Federal Reserve Open Market Committee meeting is today and tomorrow. Stay tuned.

Chart View

US Dollar Index Weekly: Still leaning toward the view the dollar correction is complete (Wave -4- correction in the chart below), but there are plausible competing stories on both sides.



US Dollar vs. Emerging Market Stocks vs. Oil Weekly: This correlation continues to play out—oil and emerging stocks up, dollar down, and vice versa.



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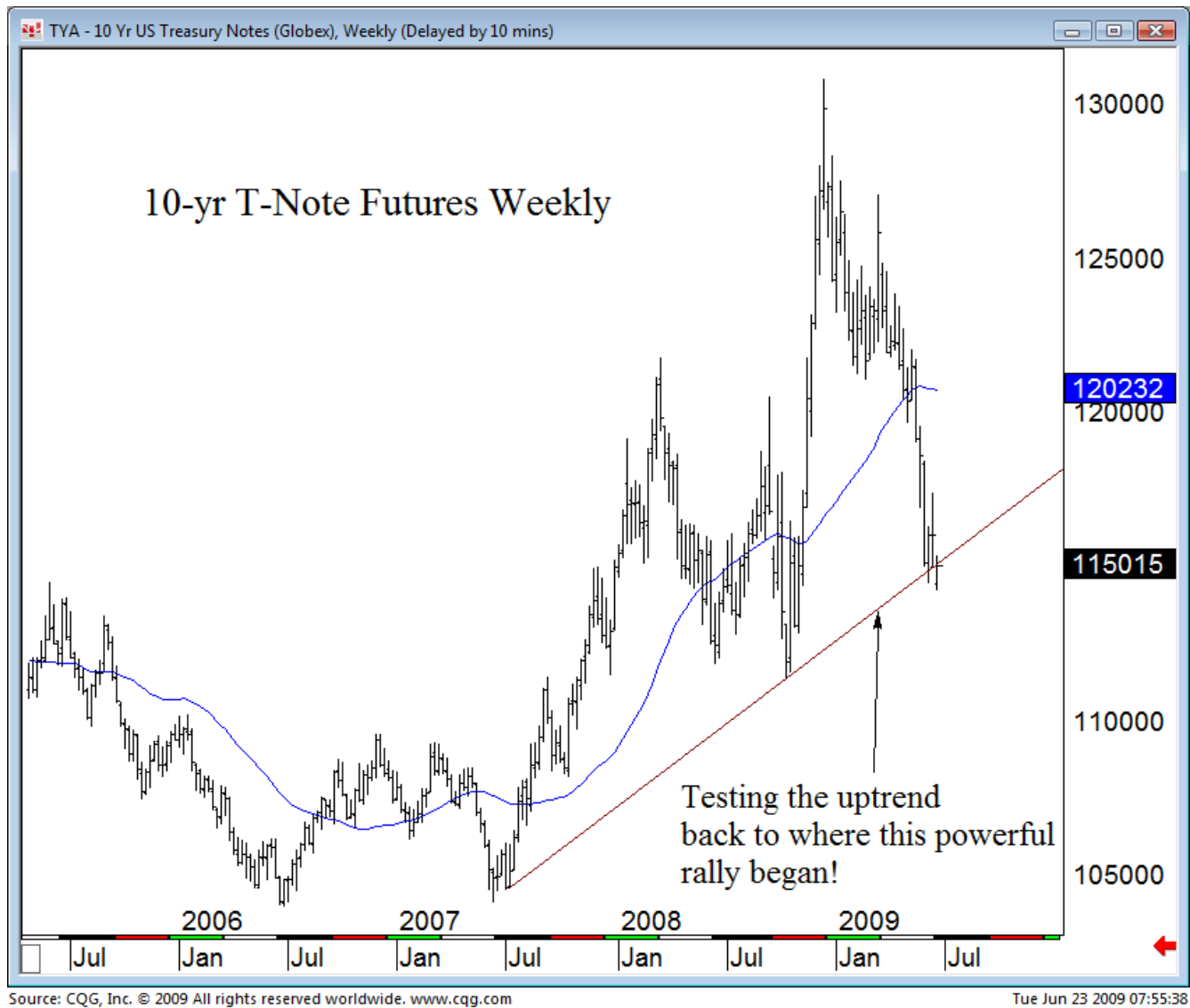
S&P 500 Index Weekly: Turned on key retracement resistance (38.2%); next support is 875, then 848.



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10-yr Note Futures: Testing key support at 114^10...



Positioning:

Despite the hit to emerging stocks on increased pessimism overnight, the commodity currencies are bidding higher this morning and the euro is sharply higher on mixed news. No changes for now.

EXISTING OPEN POSITIONS AS OF				23-Jun-09				
Spot FX								
Entry Date	Pair	Symbol	Long/ Short	Entry Price	Stop Loss	Last Price	% Chg	PT
6/22/2009	USD - Polish Zloty	USDPLN	Long	3.2800	3.1900	3.2775	-0.1%	3.5100
6/22/2009	NZ\$ - USD	NZDUSD	Short	6300	6410	6365	-1.0%	5900
Futures								
Entry Date	Currency	Symbol	Long/ Short	Entry Price	Stop Loss	Last Price	% Chg	PT
6/22/2009	NZ\$ - USD	NEU9	Short	6266	6376	6330	-1.0%	5863
Options (ISE)								
Entry Date	Curr/Mo. /Stk	Symbol	Put/ Call	Long/ Short	Entry Price	Last Price	% Chg	
4/8/2009	Yen, Sep, 101	UZOIB	Call	Long	3.75	1.60	-57.3%	
6/4/2009	Aussie, Aug, 127	JCKHN	Call	Long	5.00	4.65	-7.0%	
6/4/2009	Euro, Sep, 72	EUHIE	Call	Long	1.80	2.00	11.1%	
Options (CME)								
Entry Date	Curr/Mo. /Stk	Symbol	Put/ Call	Long/ Short	Entry Price	Last Price	% Chg	
3/20/2009	Yen, Sep, 100	JYU9P 10000	Put	Long	2.50	1.79	-28.4%	
4/8/2009	Yen, Sep, 99	JYU9P 9900	Put	Long	3.05	1.38	-54.8%	
6/3/2009	Aussie, Aug, 79	ADQ9P 7900	Put	Long	2.51	2.36	-6.0%	
6/4/2009	Euro, Sep, 137	ECU9P 13700	Put	Long	2.47	2.67	8.1%	
ETFs								
Entry Date	Currency ETF	Symbol	Long/ Short	Entry Price	Stop Loss	Last Price	% Chg	
4/1/2009	Yen UltraShort	YCS	Long	25.15	-----	23.23	-7.63%	

Black Swan Currency Strategist is published each trading day. The subscription cost of the letter is \$89 per month recurring billing or \$995 per year. To subscribe, simply go to our website at www.blackswantrading.com or call 866-846-2672.

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