



Black Swan Capital

Currency Currents

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Key News

[China Fixed-Asset Investment Surges 32.9%, Countering Record Export Slump](#)
(Bloomberg)

[Australian Employers Fired Fewer-Than-Expected Workers, Adding to Recovery](#)
(Bloomberg)

[New Zealand Leaves Rate Unchanged at 2.5% Amid Signs of Economic Recovery](#)
(Bloomberg)

Quotable

“How I wish that somewhere there existed an island for those who are wise and of goodwill! In such a place even I would be an ardent patriot.”

Albert Einstein

FX Trading – Imagiflation Takes It

Imagination inflation – a.k.a. imagiflation -- is what’s needed in order to understand price action these days.

Deflationary trends remain; no concrete evidence of inflation just yet. China yesterday posted a notable drop in its May Consumer Price Index. Of course, this bolsters China recovery efforts, according to news sources. Sure, in one sense it does, I guess.

But would the picture be any different if inflationists weren’t in control of the market right now? I think so.

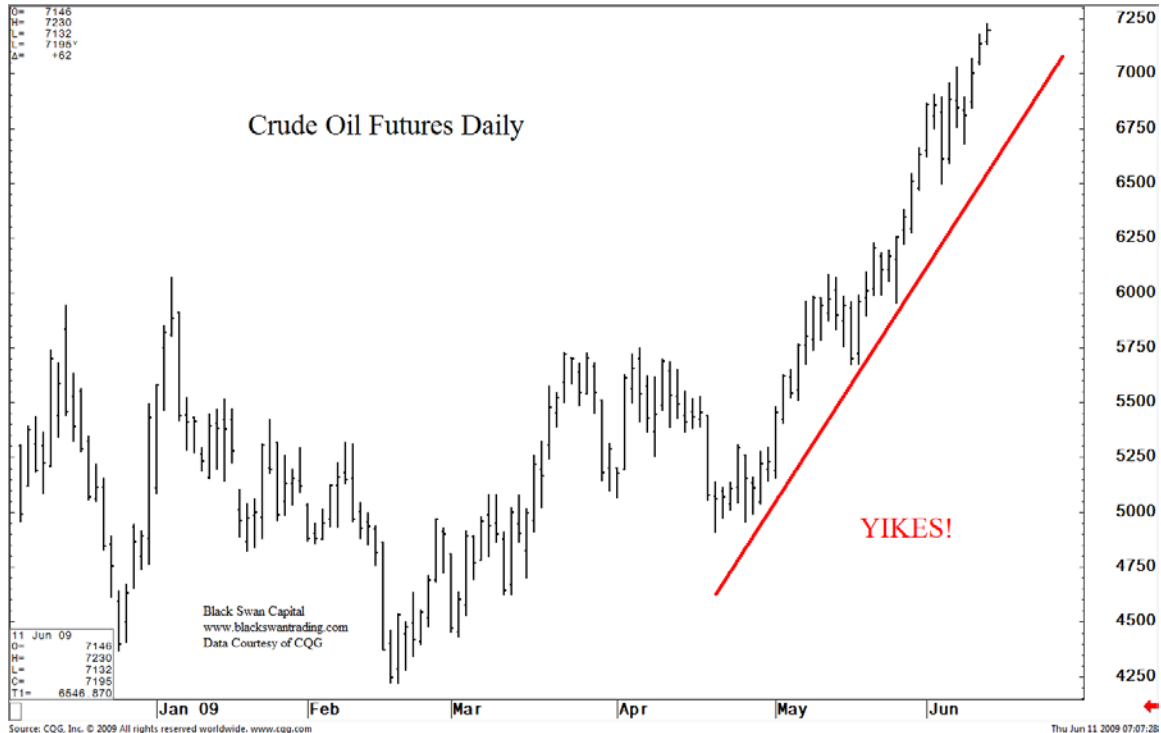
We all know China is stock piling commodities (most notably iron ore and crude oil.) And we know they’re fortifying their gold reserves (heaven forbid we fail to acknowledge that fact.) These maneuvers simply amount to a big bet that the global economy will soon return to business as usual.

Business as usual means growth ... which means global demand ... which means inflation. If we get inflation then the Chinese will look like geniuses buying up their much needed natural resources et al when prices were relatively low. (In case you were wondering, [Chinese exports plunged again in the month of May](#) at a faster rate than April which too was a faster rate of decline than the month before.)

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Their decision hasn't come under much scrutiny just yet even in the face of deflation. That's because inflation expectations are dominating markets, leaving prices of commodities high, keeping the value of China's purchases from rolling over.

Let's look at crude – a fairly precise gauge of commodity prices lately ... and, of course, the “anti-dollar”.



Crude oil is DOWN a whopping 47% since this day in June last year when prices started getting ridiculously overextended. (Just wanted to point that out even though that's not what this chart is trying to show!)

The above chart does show crude oil's recent parabolic rise – up roughly 69% from its February lows. What's the driver?

- Surging demand?** No, total world consumption has actually fallen since February.
- Depleted supply?** No, total world production has actually ticked higher since February.
- OPEC rhetoric?** No, the cartel notes high oil stockpiles and declining demand growth.
- Government rebates for gas guzzlers?** Ahhhhh yes, maybe we're on to something now.

Congress is sifting through a plan to offer a \$4,500 rebate, plus or minus, for trading in fuel-hungry trucks and SUVs in exchange for fuel-efficient cars. So as this plan takes hold we should see demand for gasoline drop considerably (at least that's the hope) and crude oil prices skyrocket.

Sound a bit counterintuitive? What doesn't sound counterintuitive these days when it comes to government ideas?

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The estimated cost is \$4 billion. Sounds like chump change in these days of hundred-billion-dollar bailouts. But the point is, it's another couple BILLION dollars being spent that doesn't make any sense.

Here is not the place to argue the potential effectiveness of this program, but it goes to the reason crude oil prices are higher – inflation expectations. With all this spending by our government, we'll never be able to avoid inflation ... whenever it gets here.

The tight negative correlation between the US dollar and crude oil got thrown out of whack a little bit last week, but the expectations of inflation seem to be the common driver here. And if inflation weren't enough, then whatever is being riled up against the buck these days is eventually becoming supportive for crude oil based on this heavily-watched correlation.

Let's beat up the dollar and send oil and commodity prices through the roof – the government wouldn't have it any other way.

Regards,

John Ross Crooks, III
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