



Black Swan Capital
Currency Currents

Thursday 16 July 2009

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Key News

- [Verleger Says Oil to Collapse to \\$20 This Year on 'Devastating' Crude Glut](#) (Bloomberg) [Editor note: Perhaps this is simply a search for a sound-bite or headline-maker, but we wouldn't be completely surprised if crude falls to \$20 a barrel. Demand is not there and neither is peak oil.]
- [China's Economic Growth Quickens to 7.9% on Record Loan Growth, Investment](#) (Bloomberg)
- [China's \\$2 Trillion Reserves Help Sustain Obama Borrowing, Shore Up Dollar](#) (Bloomberg)
- [Geithner promises to defend dollar](#) (Financial Times) Tim Geithner, US treasury secretary, sought to assure Gulf nations on Tuesday about their holdings of treasury bills when he told Saudi business leaders that his country "has a special responsibility to play" in defending the value of the dollar.

Key Reports Due (WSJ):

8:30 a.m. Initial Jobless Claims For July 11 Week: Expected: -60K. Previous: -52K.

9:00 a.m. May Tsy International Capital: Previous: -\$53.2B.

10:00 a.m. DJ-BTMU Business Barometer For July 3: Previous: +0.8%.

10:30 a.m. Jul 3 EIA Natl Gas Inventories, in billion cubic feet

1:00 p.m. July NAHB Housing Index: Previous: 15.

Live Black Swan and ISE Event today

We will be doing a webinar regarding the use of intermarket analysis in currency trading in conjunction with the ISE today. Please follow [the following link](#) if you are interested in attending. Hope to see you there. Thank you.

Quotable

"This is a government of the people, by the people and for the people no longer. It is a government of corporations, by corporations, and for corporations."

Rutherford B. Hayes

FX Trading – Reconcile This!

The word of the day is: **reconcile**.

Merriam-Webster is gracious enough to define it for us as:

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rec·on·cile

1 a: to restore to friendship or harmony <*reconciled* the factions> **b:** **settle, resolve** <*reconcile* differences>

2: to make consistent or congruous <*reconcile* an ideal with reality>

3: to cause to submit to or accept something unpleasant <*was reconciled* to hardship>

4 a: to check (a financial account) against another for accuracy **b:** to account for

Can we really reconcile the expectations flooding the market this week with key fundamental data we've got our hands on? I sure can't. Can you?

It's early in second-quarter earnings season – I mentioned that briefly on Tuesday. This week has so far been a testament to the fact that investors are more than willing to jump all over better (and less-bad) than expected earnings numbers; they're loving on growth projections for the second half of 2009 too.

Sure, the quarterly earnings expose is far from over ... and the mood can certainly change quickly ... or not change at all. But as things stand now, I can't seem to reconcile the nascent optimism – whether it is over earnings, China, or whatever -- with the underlying economic developments.

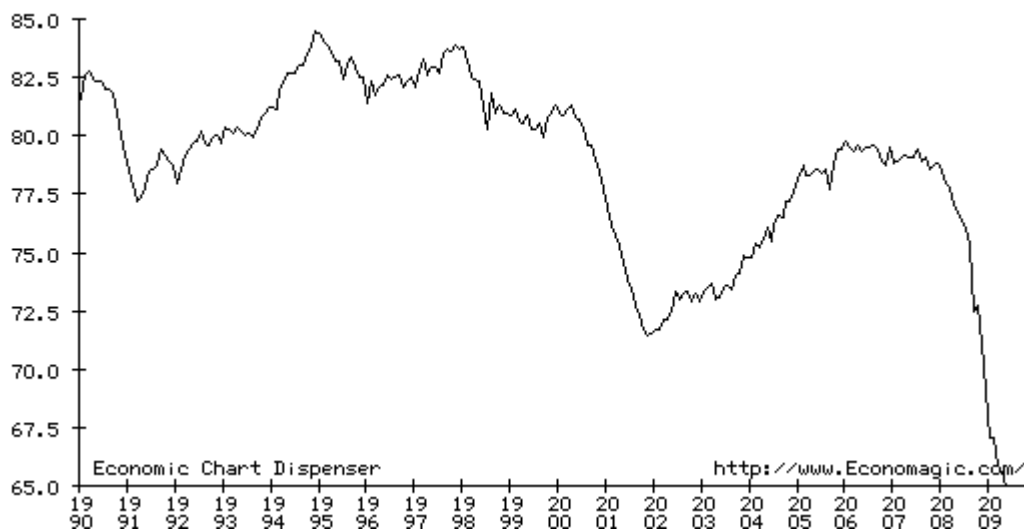
The job market is in the tank. Many analysts are starting to feel unemployment's 'lagging indicator' characteristic is a bunch of baloney at a time like this. And rightly so -- estimates call for joblessness to surpass 10% in the US. The picture ain't much prettier everywhere else you look either. (Yes, unemployment is an issue even in China!)

Past and future unemployment numbers alone should leave investors with a discomfoting feeling. But if need be, reach for some other reason for caution and you'll probably find it. Oh, let's say ... capacity utilization.

Yeah, capacity utilization – everyone's favorite statistic. Ok, I admit – capacity utilization is not everyone's favorite statistics. I think the US deficit is everyone's favorite statistic – at least everyone in the currency market anyway. (By the way, TIC data for the month of May is scheduled to be released today in the New York session. This simply reveals investment capital flows into and out of the US. Expectations have it coming in much improved from the previous month's read, meaning the US is demanding fewer foreign assets than foreigners are demanding of US assets.)

Ok, sorry – back to capacity utilization. Have a look at the following chart:

U.S. Manufacturing Capacity Utilization: SA, Percent



Like so many pieces of data recently, we've seen quite a sharp drop-off since financial crisis shook the economy. Capacity utilization tells us whether a country is meeting its output potential based on available productive capacity. Clearly we're well below potential right now.

And the US isn't alone in this area. Developed and emerging markets alike are seeing notable draw-downs in capacity utilization. A key factor here is the absence of demand. A return of demand does not appear to be anywhere in sight as global consumers continue to battle their own financial headwinds. Therefore, thus, it follows, that it will be unlikely we see a recovery in capacity utilizations rates anytime soon.

It is believe that at a certain rate of capacity usage – roughly 85% -- an increase in the rate of inflation will occur. Does then the current excess capacity not mean that inflation is not currently a threat and that perhaps inflation fears are overblown?

-----Announcing BSCM Managed Money Program-----

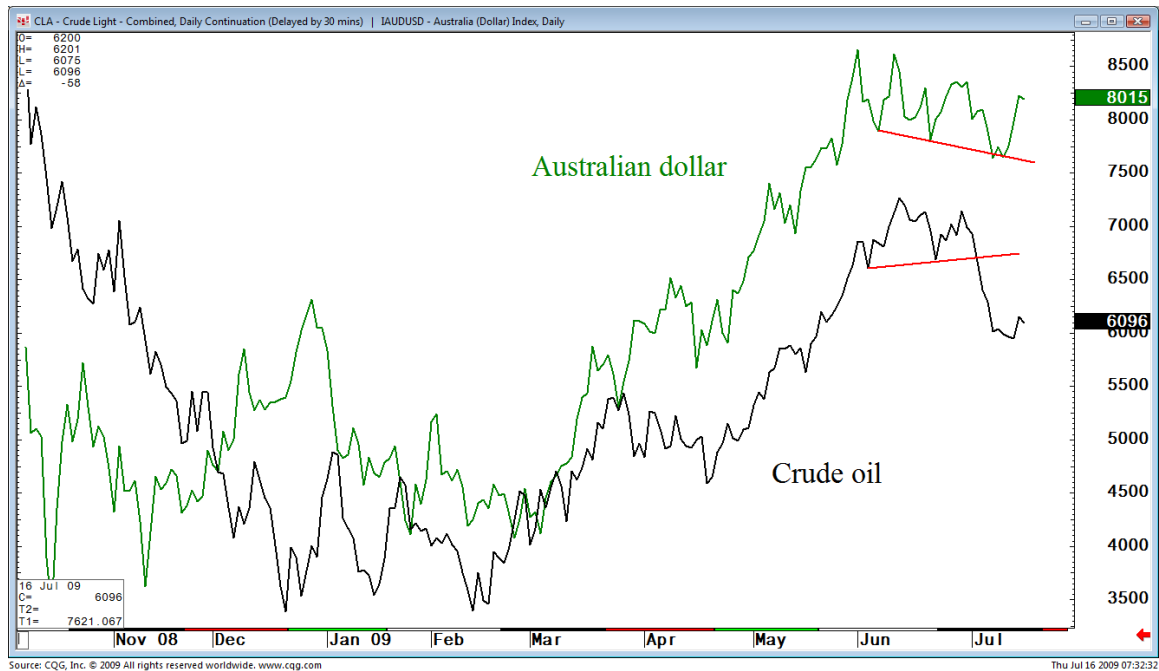
Black Swan Capital Management Managed Currency Program: Black Swan Capital Management is a registered CTA and Member of the National Futures Association. If you would like information regarding our Managed Currency Program, you can find it at the [following link](#).

Available also are the **hypothetical performance results based on 10.5 years of back-tested** daily data for the trend following model we will be utilizing to manage client funds. Please contact us directly at info@blackswantrading.com or phone us at 866-846-2672 and we will send it along for your review.

It appears the biggest threat remains deflation. And it's tough to reconcile the prospects of deflation with the potential for a better-than-expect second quarter and second half.

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Early this week and last week in our *Currency Strategist* newsletter we pointed out a price divergence in two highly correlated assets. The chart below shows crude oil (black) and the Australian dollar (green):



The breakdown in crude oil came on the realization that prices had become far detached from rather soft supply/demand fundamentals. The Australian dollar has remained resilient, however, on sustained risk appetite.

If you want another look at that point, check out crude oil (black) and the Shanghai stock index (red):



Is risk appetite being sustained because the globe is on the cusp of recovery? Or because so many out there think (and hope) the globe is on the cusp of recovery? It seems to me that critical pieces of economic data are not yet hinting at recovery, much less renewed prosperity. (Of course this excludes China – did you hear about their stimulus efforts?? Just checking!)

World leaders have their work cut out for them while they try to keep the confidence train rolling on fiscal and mental stimulus.

Fingers crossed.

John Ross Crooks III
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