



Weekly Market Update December 17, 2009

Bottom-Line: We reiterate our bullish stance on the dollar and we argue that this is just the beginning of a major intermediate move higher that will last for several months. We maintain our long dollar and short euro positions, while adding a new short position on the Yen. We believe that the dollar and the equities market can rally together in the short-term. We are also getting long gold for a short-term move for reasons discussed in our report. With regards to equities, we maintain our overall neutral stance on the markets, while arguing for one final move/leg higher into year-end/early 2010 – our upside target remains 1160-1170. Our current strategy is to play for this last leg higher through select sector plays that we expect to outperform. Last week, we went long utilities and we are now adding a new long position in semis.

The “Short-Term Trading Ideas” section can be found at the end of this report and summarizes all of our positions.

Equities: We have been arguing for the past few weeks that the market has started the “topping” process for an intermediate top, and has become increasingly defensive with outperformance seen in Healthcare and Utilities. Nevertheless, we continue to argue that despite not boding well for the sustainability of the rally, it does not preclude the markets from going higher into year end/early 2010 and we expect a final move higher.

We initiated several shorts on Nov 18th, with the intention of covering those shorts and getting long at approximately 1060 to play for the last surge higher. The market managed to hold the support level of 1085 (bottom of range) and we never got our opportunity to get long. Our current strategy is to play for this last leg higher through select sector plays that we expect to outperform, while keeping our short on the S&P as a hedge given the deterioration in market internals. For example, we like the risk/reward in semis vis-à-vis the S&P. We are also maintaining our long position on Utilities (see updated Charts 1-3).

See Charts 4 and 5. We like semis for a short-term trade for the following reasons: (1) SOX Index broke above a critical long-term pivot level, and has consolidated above this level for the last few days, usually a bullish sign (2) the risk-reward is attractive given that we can place stops below the recent tight consolidation range, and (3) several of the individual names that make up the index have exhibited constructive bullish price action with breakout gaps on heavy volume, breakouts above important resistance levels et cetera. Semis as a group have also relatively outperformed the broader market since the beginning of November (see Chart 6), and we see no signs of this slowing down over the next few weeks. For aggressive accounts, we recommend an outright long in Semis but if you want to be more conservative, we recommend going long Semis versus short the S&P due to expected continued outperformance over the short-term.

New long position: SOX (Semis) – short term target of 370, stops at 330.

Technical Analysis & Strategy

Foreign Exchange Markets: We reinitiated our long position in the Dollar (we initially went long at the end of September) and our short on the Euro after getting stopped out of our initial position with a brief break below the 75 support level in the DXY. We are confident that the dollar can continue its ascent higher over the next few months, and that in the short-term, equities and the dollar can rally together. See updated Charts 7-9.

We continue to monitor the Aussie Dollar, since the AUD is a large beneficiary of the dollar carry trade - borrowing in dollars and buying Aussie bonds has been a popular trade. We pointed out last week several bearish divergences, RSI breaking below support (RSI has a tendency to lead price), and that price would confirm with a break below 0.9 which occurred today. The Aussie Dollar is currently testing the 100 day sma so we will wait for a bounce/retracement to initiate a position.

In our last weekly update, we also discussed several reasons why betting on the continued depreciation of the Japanese Yen makes sense. Besides being in the best interest of the Japanese Government to intervene in the currency markets to help their struggling export industries, there is also evidence that the total money supply in Japan is expanding, which will also help depreciate the currency. Furthermore, if the Yen carry trade regains focus as people move away from the dollar that could be another contributing factor.

Technically, there is a major divergence with the oscillators on the weekly chart, which suggests that the intermediate trend could be in the process of changing. We also had a failed “breakdown” below a key level. Please see Charts 10 and 11.

New short position: JPYUSD (Yen) – short term target of 100, stops at 87.

Gold: We are initiating a new long position in Gold, given that our technical structures indicate that we have at least one more new high before we have a much larger intermediate correction. We also continue to believe that the main driver is the expansion of the monetary base, and as this expands, the nominal price of gold should continue to rise. We see little evidence that the Fed and the Treasury have any other choice but to continue to follow inflationary policies to counter the deflationary credit bust that we have just experienced. Lastly, there is little technical evidence to counter the notion that Gold remains in a bull market and has decoupled from other commodities. As we discussed in October, we believe that the breakout above the consolidation that took place over approximately 18 months has implications to the 1300 level.

New long position: Gold – short term target of 1250, stops at 1068.

Technical Analysis & Strategy

BKX (Financials) – Consolidating in a sideways fashion after breaking below uptrend, and has broken below short term support ~43. The 100 day sma has recently proven to be resistance, and the 50 day sma has crossed below the 100 day sma. Financials have underperformed the S&P since the end of August.

XOI (Energy) – Has fallen below support at the 50 day sma after finding resistance at the 38.2% Fibonacci retracement level of ~1100. Currently finding support from the 100 day sma. Oscillators broken below equilibrium level, suggesting weakness. Outperformed the S&P from August to early November, but has since underperformed.

OSX (Oil Services) – Throwback rally is currently testing the trendline from the March lows that was broken a few weeks ago. Has underperformed since late October.

IXI (Industrials) – Currently finding resistance from the 50% Fibonacci retracement from the highs in '07. Relative performance versus S&P has been neutral overall since May.

IXR (Consumer Staples) – Breaking below the trendline from the March lows. Bearish divergence with RSI. Has been underperforming the broader market since March.

IXB (Materials) – Consolidating in a sideways fashion. Uptrend since March remains intact. RSI currently testing the 50 level. Has outperformed since end of October, but neutral performance overall since August.

DRG (Pharmaceuticals) – Remains in its March uptrend. Overall since summer of '08 has been outperforming, and longer-term we expect this trend to continue.

BTK (Biotech) – Found support at the intersection of the 50 day sma and the 100 day sma. RSI has broken out of its downward trend, and MACD continues to hover above the zero level. Overall, entered into a period of massive out-performance in the summer of '08 and we expect that to continue longer-term. Relative strength has broken out of its September downtrend.

DJR (Real Estate) – Continues to find resistance in the 175-180 area. Maintaining March uptrend. Broadly speaking, has been underperforming since early '07. Relative strength is once again testing the '07 pivot low and December '08 resistance, where it failed in September.

NDX (Tech) – Bounced off of the 50 day sma, continues to find resistance ~1815. Broadly speaking, began a period of longer-term out-performance in 2007 and we expect that to continue in the longer term.

SOX (Semiconductors) – Broken above resistance ~340, now finding support at that level. RSI confirms the move, having broken its September downtrend. Relative strength has rebounded sharply since breaking below its late-2008 uptrend, and has been outperforming since the beginning of November.

UTY (Utilities) – Continues upward since breaking resistance ~410 and completing a bullish pennant pattern. RSI has broken above the ceiling that has bound it since late 2008, confirming strength. Relative strength has broken its 2009 downtrend, and looks poised to continue to outperform over the next few weeks.

IRH (Retail) – Currently testing the uptrend from the March lows. Bearish divergence with RSI. Overall, has outperformed the market since the beginning of the year.

Active Short-Term Trading Ideas

Short SPX (S&P 500) with short-term target of 1060. Stops at 1116.

Long UTY (Utilities) with a short-term target of 450. Stops at 402.

Long SOX (Semis) with a short-term target of 370. Stops at 330.

Long DXY (Dollar) with a short-term target of 81-82 and an intermediate target of 86-88. Stops at 74.

Short EURUSD (Euro) with a short-term target of 1.38-1.4 and an intermediate target of 1.3-1.32. Stops at 1.52.

Long USDJPY (Short Yen) with a short-term target of 100. Stops at 87.

Long GOLDS (Gold) with a short-term target of 1250. Stops at 1068.

Closed Short-Term Trading Ideas

Short IBOV (Brazil) had stop elected at the 65,500 level.

Long DXY (Dollar) had stop elected at 75 level.

Short EURUSD (Euro) had stop elected at 1.505 level.

Short UTY (Utilities) had stop elected at 412 level.

Short MID (S&P 400) had stop elected at 712 level.

Short RTY (Russell 2000) had stop elected at 608 level.

*Stops on a closing basis

Technical Analysis & Strategy

Chart 1: UTY Daily with RSI



Chart 2: UTY Daily with Volume



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Chart 3: UTY Relative Strength with RSI



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Chart 4: SOX Daily with RSI



Chart 5: SOX Weekly with MACD



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Chart 6: SOX Relative Strength



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Chart 7: DXY Daily with RSI



Chart 8: DXY Weekly with RSI & MACD



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Chart 9: EUR Daily with RSI

EUR ↑ 1.4524 - .0014 BGN 1.4523/1.4525 BGN CurncyG
 At 15:45 Op 1.4538 Hi 1.4591 Lo 1.4506 Close 1.4538 Value 12/18/09



Chart 10: USDJPY Weekly with RSI & MACD

USDJPY ↑ 89.77 + .16 BGN 89.76/89.78 BGN CurncyG
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Technical Analysis & Strategy

Chart 11: USDJPY Daily with RSI



Technical Analysis & Strategy

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