CURRENCY CURRENTS

A free global-macro & market newsletter

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Quotable

"There are as many styles of beauty as there are visions of happiness."

--Stendhal (aka Marie-Henri Beyle)

Commentary & Analysis

Path of the dollar = Path of commodities?

It's not easy trying to forecast future prices from chart patterns; nor is it any easier to do so no matter how much fundamental information you possess, or believe you possess (see Frédéric Bastiat's famous essay: "What is seen and what is not seen"). Said forecasting difficulties prove the axiom, so succinctly stated by the late great Mark Douglas: "Every moment in the market is unique."

That being said, because decision-making and forecasting skills of the average human have not changed much since the beginning of time; i.e. we continue to see similar reactions across a fractal time frame which shows up as price patterns; albeit some differences which may be the result of high frequency trading a la algos. (*As an aside, it seems despite individual's attaining no better skill in forecasting, they have attained much higher confidence-levels. We can thank the dramatic increase in access to technology—producing vast amounts of data—for the spike in confidence levels. But, arguably, this fact has led to even less critical thought across the body of players who make up this thing called a market. And it may be a contributing factor for the next major market debacle.*)

From that summary, I share one premise and two thoughts about market price action derived from chart patterns I watch day in and day out:

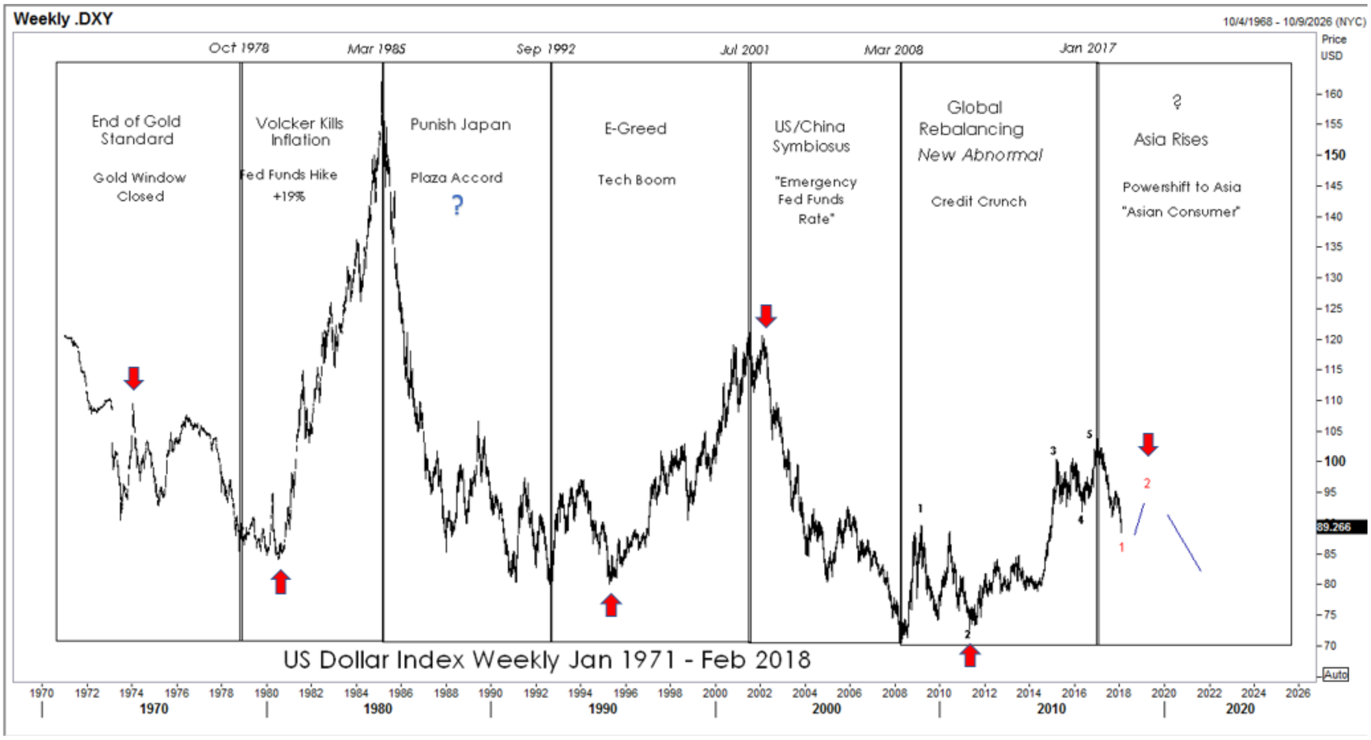
- Given a certain level of mastery with chart patterns (defined by watching, thinking, and acting on price action over several years in real markets using real money), **they *do* provide an edge which if applied judicially will increase the probability of success** (albeit, the same argument may be applied to fundamental mastery). The degree to which chart patterns increase one's probability will vary dramatically and can change dramatically as the market environment itself changes. So. I think it best to use the phrase: "Over time one can gain a *slight* edge using chart patterns as a forecasting tool."

  Keep in mind, it is that *slight* edge which builds and nourishes casino's and race tracks.

The dollar path and the correlated commodities path.

1. **I suspect the dollar has entered a long-term bear market cycle** (first chart below). This decline will be measured in years (approximately seven to eight years) and should carry the dollar to fresh lows. But in the process of this long-term downtrend we will likely see a major multi-month rally in the dollar (second chart below) before we enter the big one; defined as the third wave down (past dollar cycles are usually not straight lines and consists of what is known as "tests" of the trend to wrong-foot market players.

Weekly Dollar Index: Cycles (global macro era's defined)..the red arrows on the chart represent "tests" of the new trend. Note: We didn't get a test during the "Punish Japan" era as defined (the [Plaza Accord]() worked); and the last red arrow is a forecast. So far, no test since the fall in the US dollar began back in January 2017.



2. **There seems a tight negative correlation has developed between the US dollar index and commodities index** (Thomson/Reuters). I have again noted the macro environment during this negatively correlated trend moves in the dollar and commodities. Thus, if one expects the US dollar to stage a rally before dropping to new lows, one should also expect we will see a better long-term buying opportunity in commodities.

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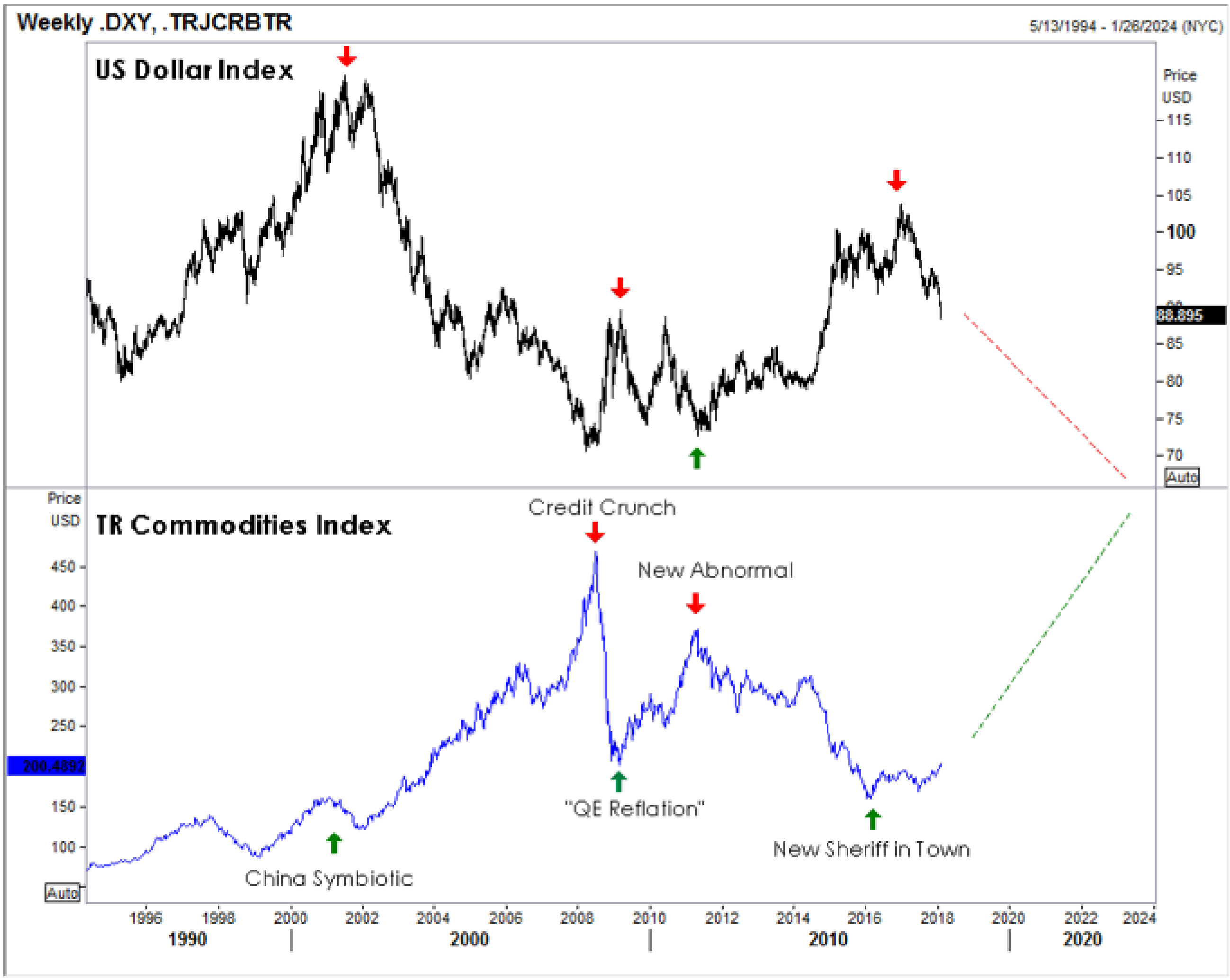
US Dollar Index vs Thomson/Reuters Commodities Index Weekly: Note the tight negative correlation; i.e. as the dollar falls commodities rise, and vice versa. I have noted four macro environments where this correlation seems tight:

1) China Symbiotic period 2000-2007;
2) Credit Crunch 2007-2008/9;
3) QE Reflation 2009-2011 (*a false start as the real economy never responded*);
4) New Sheriff in Town aka President Trump most likely wants a weak dollar.



So, if the dollar is now in another bear market cycle, commodities should do very well indeed. Long-term buy and hold players will likely be quite happy in a few years owning things like wheat, soybeans, and platinum. The question is, from a trading time-frame perspective: Will there be yet another better opportunity to buy commodities? I think so.

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