

Strategies, analysis, and news for FX traders

CURRENCY TRADER

July 2010

Volume 7, No. 7



COMMODITY

currency outlook p. 6

THREE-BAR INTRADAY

forex scalp strategy p. 18

THE CHINA REVALUATION DEBATE:

p. 10 and p. 14

GIVING A STRATEGY

a test run p. 34

THE ROBIN HOOD CARRY TRADE:

Using the Chinese yuan as a funding
currency p. 22





| | | | |
|---|-----------|--|-----------|
| Contributors | 4 | Currency Futures Snapshot | 27 |
| Global Markets | | International Markets | |
| Risk on, risk off: Aussie and Canada | 6 | Numbers from the global forex, stock, and interest-rate markets. | |
| Continued gains in the “commodity currencies” depends on whether the global economy can keep rolling. | | Global Economic Calendar | 31 |
| <i>By Currency Trader Staff</i> | | Important dates for currency traders. | |
| On the Money | | Events | 32 |
| Hail the China float | 10 | Conferences, seminars, and other events. | |
| Review the ramifications of China’s decision to allow to yuan to revalue on a limited basis. | | Key Concepts | 32 |
| <i>By Barbara Rockefeller</i> | | New Products | 33 |
| The yuan revaluation situation | 14 | Forex Journal | 34 |
| Forecasts about the impact of a semi-floating yuan are missing the economic mark. | | Testing out a scalp setup. | |
| <i>By Yinghua Zhu and Marc Chander</i> | | | |
| Trading Strategies | | | |
| Five-minute forex scalp | 18 | | |
| High winning percentage, modest goals, and favorable entry points help scalp pattern capture profits. | | | |
| <i>By Currency Trader Staff</i> | | | |
| Advanced Strategies | | | |
| The Robin Hood carry: | | | |
| The yuan as a funding currency | 22 | | |
| The yuan carry trade that started last year triggered a stock and bond bull market around the world. | | | |
| <i>By Howard L. Simons</i> | | | |

Looking for an advertiser?

Click on the company name for a direct link to the ad in this month’s issue.

[dbFX](#)

[eSignal](#)

[FXCM](#)

[The Futures & Forex Expo](#)

[Your FX Trading Room](#)

Questions or comments?

Submit editorial queries or comments to
webmaster@currencytradermag.com.

Trade Forex Anywhere and Anytime with FXCM*

Introducing our New Mobile Trading Products



- Monitor streaming prices • Place market and entry orders
- View account balances • Check real-time news and charts • Get breaking news alerts directly to your phone

Free Practice Account at www.fxcm.com/mobile



www.fxcm.com/mobile

Forex Capital Markets, Financial Square, 32 Old Slip, 10th Floor, New York, NY 10005 USA • 1-866-497-3926 (FXCM)

Risk Warning: Trading foreign exchange on margin carries a high level of risk and may not be suitable for all investors. Before deciding to trade foreign exchange, you should carefully consider your monetary objectives, level of experience, and risk appetite. The possibility exists that you could sustain a loss of some or all of your deposited funds, and, therefore, you should not speculate with capital that you cannot afford to lose.

*Subject to available liquidity, the trading desk is open from 5:15 p.m. (ET) Sunday afternoon through 4 p.m. (ET) Friday afternoon.

CURRENCY TRADER

A publication of Active Trader®

For all subscriber services:

www.currencytradermag.com

Editor-in-chief: Mark Etzkorn

metzkorn@currencytradermag.com

Managing editor: Molly Goad

mgoad@currencytradermag.com

Contributing editor:

Howard Simons

Contributing writers:

Barbara Rockefeller, Marc Chandler,

Chris Peters

Editorial assistant and

webmaster: Kesha Green

kgreen@currencytradermag.com

President: Phil Dorman

pdorman@currencytradermag.com

Publisher, ad sales:

Bob Dorman

bdorman@currencytradermag.com

Classified ad sales: Mark Seger

seger@currencytradermag.com

Volume 7, Issue 7. Currency Trader is published monthly by TechInfo, Inc., 161 N. Clark St., Suite 4915, Chicago, IL 60601. Copyright © 2010 TechInfo, Inc. All rights reserved. Information in this publication may not be stored or reproduced in any form without written permission from the publisher.

The information in Currency Trader magazine is intended for educational purposes only. It is not meant to recommend, promote or in any way imply the effectiveness of any trading system, strategy or approach. Traders are advised to do their own research and testing to determine the validity of a trading idea. Trading and investing carry a high level of risk. Past performance does not guarantee future results.



▼ **Howard Simons** is president of Rosewood Trading Inc. and a strategist for Bianco Research. He writes and speaks frequently on a wide range of economic and financial market issues.

▼ **Barbara Rockefeller** (www.rts-forex.com) is an international economist with a focus on foreign exchange. She has worked as a forecaster, trader, and consultant at Citibank and other financial institutions, and currently publishes two daily reports on foreign exchange. Rockefeller is the author of *Technical Analysis for Dummies* (For Dummies, 2004), *24/7 Trading Around the Clock, Around the World* (John Wiley & Sons, 2000), *The Global Trader* (John Wiley & Sons, 2001), and *How to Invest Internationally*, published in Japan in 1999. A book tentatively titled *How to Trade FX* is in the works. Rockefeller is on the board of directors of a large European hedge fund.

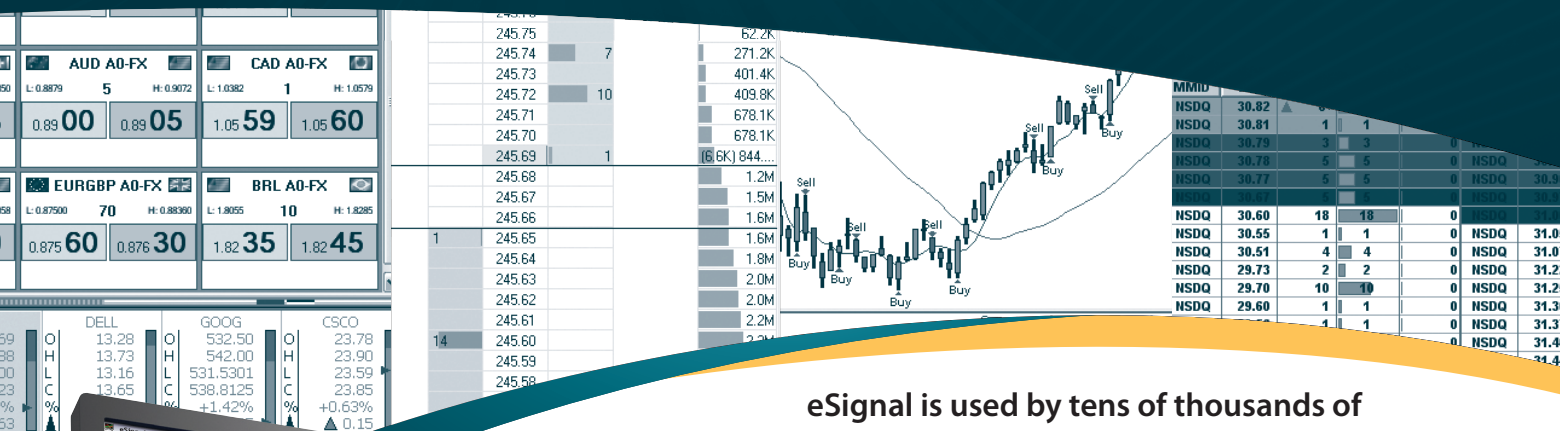


▼ **Marc Chandler** (marc@terrak.com) is the head of global foreign exchange strategies at Brown Brothers Harriman and an associate professor at New York University's School of Continuing and Professional Studies. Chandler has spent more than 20 years analyzing, writing, and speaking about global capital markets. He has worked for several consulting firms and banks as well as a hedge fund in the early 1990s. Chandler appears regularly on CNBC and Bloomberg Television. He is the author of *Making Sense of the Dollar: Exposing Dangerous Myths about Trade and Foreign Exchange* (Bloomberg Press, 2009).



▼ **Yinghua Zhu** is a financial research analyst specializing in commodity and emerging-market investment at a New York-based money management firm. She is a graduate of the University of Chicago, where she received a master's degree in statistics.

Which Tools Are Used by More Successful Traders Worldwide?



Tens of thousands of individual traders prefer to use the professional, feature-rich tools found only in eSignal.



eSignal
Voted Best for More Than 15 Years!
Stocks & Commodities Readers' Choice Award
Best Real-Time/Delayed Data



eSignal
Trade2Win Members' Choice
5 Years in a Row!
Best Real-Time Data Feed



eSignal
Voted Best
Real-Time Data Feed
World Finance

eSignal is used by tens of thousands of traders and is voted #1 by organizations worldwide. Why?

eSignal gives you access to the same **reliable data and predictive tools** professionals use — so you'll know exactly when to get in...and out of your trades.

eSignal gives you what you need for **consistent market success:**

- **Real-time stock, futures, options and Forex quotes** plus news that can change the direction of the market
- **Advanced charting with EFS**, so you can create your own strategies or modify 100s of existing free strategies
- **Market scanners** to quickly and easily find the best trading opportunities of the day
- **Free online education** to help you gain skill in the art and science of trading
- **Free software** and free integrated trading with your choice of broker

Find out for yourself how easy it is to get started. Call now and we'll have you up and running right away. **Get your 30-day, risk-free trial** of eSignal today and start trading for yourself.

eSignal

Start your 30-day trial* today and ask about our "2nd-month-free" special

800.215.7202
www.eSignal.com/offer/ct



Risk on, risk off: Aussie and Canada

Enthusiasm for “commodity currencies” dependent on sustained global economic recovery.

BY CURRENCY TRADER STAFF

“Risk on, risk off” may be the mantra for the darlings of the FX world in recent months — the Australian dollar (AUD) and the Canadian dollar (CAD). Bolstered by solid underlying economic growth fundamentals, higher interest rates in Australia, and a new tightening cycle in Canada, these country’s currencies have been favorites among forex traders. Both Canada and Australia are major commodity exporters which has adds to their luster because of expectations (however shaky) of continued global economic recovery.

However, since late April when U.S. equities topped out, both the Aussie and Canadian dollar, or “loonie” have

posted overall losses. From April 23 through June 24 the U.S. dollar gained 6.91 percent vs. the Aussie dollar and 4.48 percent vs. the Canadian dollar (Figure 1). That data “shows how excessively badly these currencies perform against others when risk is ‘off,’” says Brian Dolan, chief currency strategist at Forex.com.

However, the early June rebound in stocks helped flick risk switch back to the on position. “The Aussie dollar has recovered quite smartly from its slide in May, with investors snapping it up before a test of .8000,” says Sean Callow, senior currency strategist at Westpac Institutional Bank in Sydney. “Global risk appetite has improved, most

importantly in equities. The daily correlation of percentage changes between AUD/USD and the S&P 500 was a solid 0.70 in the first quarter 2010 but rose to a very tight 0.84 in the second quarter. So Wall Street is vital for the Australia dollar at the moment.”

Let’s shift away from forex action for a moment and examine the underlying fundamentals of the Australian and Canadian economies, which are the basis for the attractiveness of their currencies during times of global financial risk appetite.

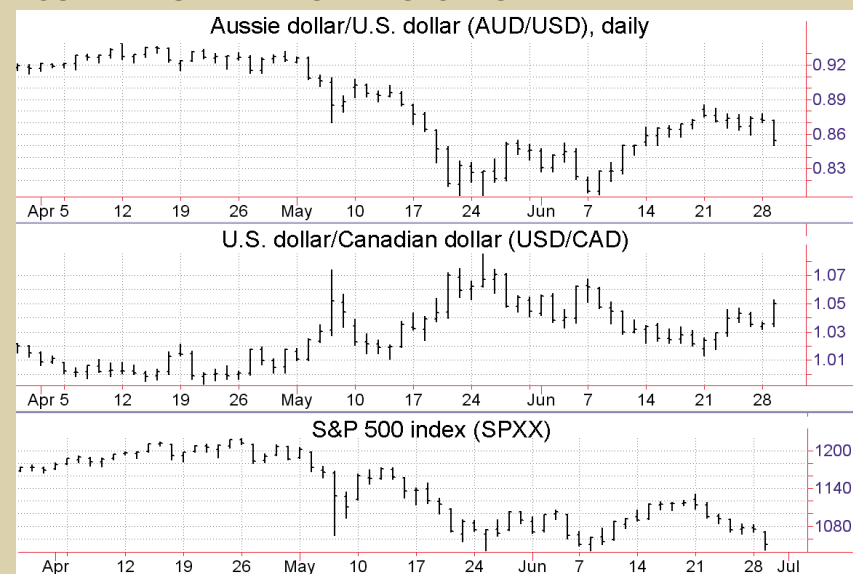
Up down under

Bottom line, the Aussie economy is in better shape than most other developed nations.

“I see GDP growth accelerating to 3.0 percent in 2010 from 1.3 percent in 2009,” says Stephen Roberts, chief economist Australia at Nomura Australia.

Matt Robinson, senior economist at

FIGURE 1: CURRENCIES AND STOCKS



From April 23 through June 24 the U.S. dollar gained 6.91 percent vs. the Aussie dollar (top) and 4.48 percent vs. the Canadian dollar (middle).

Moody's Analytics Australia has a similar outlook, targeting Australia's 2010 GDP growth at 2.7 percent.

"The Australian economy has outperformed most of its industrialized country peers over the past two years," he says. "Buoyed by a mix of policy stimulus, solid fundamentals, emerging market export demand, and surprisingly resilient confidence, Australia avoided recession and quickly returned towards its trend growth rate."

A key factor behind this strength is Australia's export picture. "We expect a major acceleration in export growth over the next 12 months mostly because of the strong growth recoveries in Australia's major export markets in Asia," Roberts says.

Australia exports several important raw commodities, including coal, iron ore, gold, crude oil, natural gas, aluminium, beef, and wheat.

"Commodity export volumes are growing at the moment after a cooling during the global recession," says Gavin Stacey, fixed income strategist at Barclay's Capital. "Even more important is the fact that the price of Australia's commodities are going up rapidly. This gives Australia a massive income boost, which in turn spurs growth elsewhere in the economy."

Australia's strong ties to Asia — arguably the fastest-growing economic region in the world — are pivotal to its growth outlook.

"More than 70 percent of Australia's exports are destined for Asia, 55 percent to just four markets — China, Japan, South Korea and India," Roberts notes. "The two biggest exports to Asia are coal and iron ore, but an increasingly big export item is liquefied natural gas."

Buttressing a robust commodity export position is Australia's solid fiscal condition. "Australia has a relatively enviable fiscal situation; modest budget deficit and minimal net debt," Moody's Robinson notes.

In stark contrast to the U.S., UK, and some other Western countries, Australia managed to avoid digging itself into too big a hole during the financial crisis.

"Until 2008-09 Australia had run budget surpluses for a decade and had run net government debt down to zero," Roberts says. "Post global financial crisis fiscal spending has pushed the budget position into a relatively small deficit, and the worst is already over. The budget position is expected to return to surplus within three years and net government debt is likely to peak on our forecasts around 7 percent of GDP, before declining back to zero before 2020."

Barclay's Capital's Stacey has an even more optimistic view on the Aussie budget. "Australia has a very low government net debt level," he says, noting the "balance is forecast to return to surplus in 2012-13. Once again strong

commodity prices lie at the heart of the strong fiscal position. In essence, strong commodity prices boost mining profits, which lifts government revenues."

Aussie rate advantage

Another factor supporting the Aussie in the FX arena is high interest rates. With an official central bank lending rate of 4.5 percent, the Aussie dollar boasts bullish rate differentials vs. New Zealand dollar (2.75 percent), the British pound (0.5 percent), Canadian dollar (0.5 percent), Euro (1 percent), and the U.S. dollar (0.25 percent).

While the Reserve Bank of Australia (RBA) is currently assumed to be taking a break from its recent tightening moves, analysts see additional rate hikes not to far in the future.

"I expect another set of three 25-basis-point rate hikes between November 2010 and February 2011," Nomura's Roberts says.

Moody's Robinson sees the possibility of a rate hike at the August RBA meeting but thinks November is more likely, adding that Moody's Analytics expects the official rate to move to 5.25 percent by mid 2011.

Canada keeps its bearings

Although it posted a 2.6-percent GDP decline in 2009, Moody's Economy.com forecasts a strong +3.5-percent GDP reading for 2010.

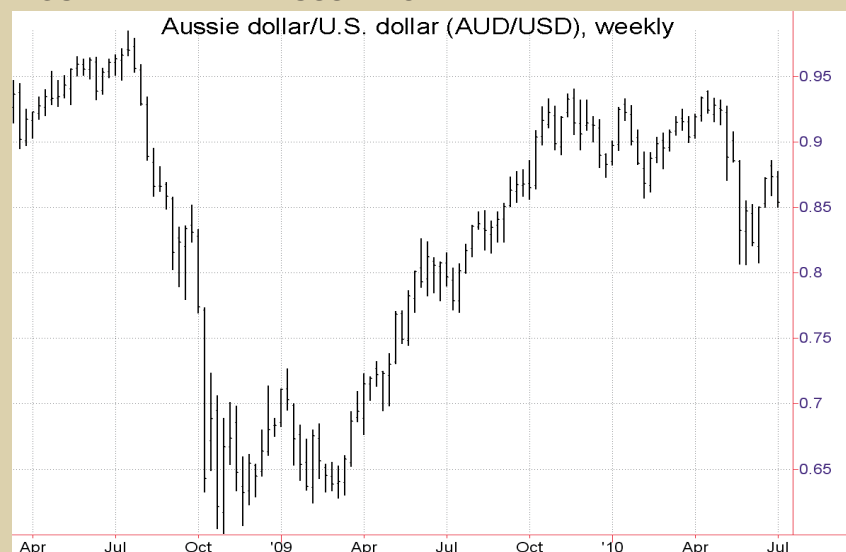
"The Canadian economy looks good," says Nick Bennenbroek, head of currency strategy at Wells Fargo. "The economy is growing and getting steady job growth each and every month. They don't have the same budget problems the U.S., U.K., or Europe have."

The absence of a housing bubble and bust and sustained consumer strength have helped keep Canada on an even keel.

"Consumer spending has been very hot," says Jimmy Jean, economist at Moody's Economy.com, who refers to Canada as one of the better-performing developed nations. "They haven't had the pressures on household wealth and consumer credit, which are still prevalent here in the U.S. Canada is well positioned and is ahead of the pack, especially with Europe looking at the possibility of another recession."

Jean also says strong banking positions have helped support Canada's rebound. "Banks in Canada haven't been affected by the recession," he explains. "They remain well funded and they didn't restrict credit to consumers."

Home buying and consumer spending related to new homes has bolstered growth. First quarter 2010 data shows consumer spending grew by 4.5 percent, which is "very strong" according to Jean.

**FIGURE 2: WEEKLY AUSSIE DOLLAR**

The 2009 rally took the AUD/USD pair close to its July 2008 all-time high of .9849, but that level might be out of reach for the foreseeable future, according to some analysts.

FIGURE 3: LONG-TERM LOONIE

Despite its losses vs. the U.S. dollar during the financial crisis, the Canadian dollar is currently closer to its November 2007 generational high than its March 2009 crisis low.

Overall, by sidestepping the roots of the global recession, Canada was able to rebound faster than the U.S.

"Domestically, they never had much of a housing bubble and their banks weren't really exposed to sub-prime loans," explains Jay Bryson, global economist at Wells Fargo. "Going forward we see relatively strong growth at 3.5 percent GDP in 2010."

Also, Canada, like Australia, is a major commodity exporter, including crude oil, iron ore, aluminum, and gold.

However, the destination of Canada's exports is different. "75 to 80 percent of Canadian exports go to the U.S.,"

Jean explains. And the U.S. simply isn't growing as strongly as the Asian region soaking up the majority of Australian exports.

"We have seen higher [Canadian] exports of commodities, especially since the beginning of 2010, but it hasn't been the primary driver of recovery," Jean says. "Nearly all those exports are absorbed by the U.S. and it hasn't been a big bonanza."

Another similarity to Australia is Canada's moderate debt situation. Although Canada fell into a deficit in 2008 and 2009 because of stimulus spending, that deficit came "after 12 years of fiscal surplus," notes Moody's Jean. Generally known as a government focused on fiscal prudence, Canada "came out with a budget in February to close the deficit by 2015," Jean adds.

"No one is looking for their debt to become unsustainable anytime soon," Bryson says.

BOC rate hikes

An exceptionally strong a 6.1-percent GDP growth rate in the first quarter of 2010 was one of the factors behind the Bank of Canada's (BOC) decision to initiate a rate-hike cycle in early June. The BOC bumped up its central bank lending rate by 0.25 percent to 0.50 percent.

"It shows the economy is heading toward self-sustaining growth so they are starting to remove unconventional policy measures" Jean says of the strong first quarter growth. He forecasts additional rate hikes this year that could "drive the rate to 1.50 percent by year-end."

Wells Fargo's Bryson agrees with that forecast. "We see another 100 basis points [in rate hikes] this year to take the rate to 1.50 percent," he says.

Looking out toward the end of 2011, Bryson sees additional Canadian tightening that will eventually bring the benchmark rate up to 3.50 percent.

"Obviously, rate hikes will be supportive to the Canadian dollar," he adds.

Currency action

The daily chart of Aussie/U.S. dollar pair reveals that after a hefty sell-off from mid-April into mid-June, the Aussie dollar has begun to strengthen again.

Figure 2 shows the AUD/USD rally in late 2009 took the pair within spitting distance of the July 2008 high of 0.9849.

That was the highest level for the Aussie dollar vs. the buck since it began floating in December 1983, says David Forrester, vice president global FX strategy at Barclay's.

However, Forrester says his firm does not expect a test of that high, for two reasons.

"We expect a stronger U.S. dollar going forward as U.S. economic data surprise to the upside and eventually lead the Fed to start raising rates in the first half of 2011," he says. "This will help erode the AUD's interest-rate advantage and also withdraw some of the global liquidity underwriting all risky assets, including the AUD."

The second reason is related to an expected cool-down in Asia.

"We expect emerging-market Asia to continue to gradually tighten policy this year, which again will withdraw some of the global liquidity underwriting the AUD and prevent the high global inflation that led to AUD moving to a post-float high in 2008 given its attraction as an inflation hedge" Forrester says.

Westpac's Callow sees an outright shorting opportunity in the Aussie. "The RBA is in an extended pause in its tightening cycle, and given the risks to Chinese growth, too much good news seems to be priced into AUD/USD in the .8700-.8800 area," he says. "We would look to go short in this region, with a stop loss around 0.8900, targeting 0.77 over the third quarter."

Turning to the Canadian dollar, Wells Fargo's Bennenbroek saw upside potential for the Canadian loonie based on interest-rate differentials. "We see the Fed steady and the ECB steady, and we think the BOC will be raising rates before the end of the year," he says.

The USD/CAD pair, which in April fell to its lowest level in nearly a year before rebounding to around 1.08 in May, was again turning back toward parity (1.00) in late June (Figure 4).

Bennenbroek targeted gains in the Canadian dollar/U.S. dollar to "parity, but there is potential to go beyond that," he says.

Be wary

Dolan points to the potential for the global recovery to falter in the months ahead, and notes the dampening effect this would have on the "commodity currencies."

"People are bullish on these [currencies], because people are bullish on the global recovery view," he says. "The global recovery is likely to be stalling. These are higher-beta currencies for the risk. When risk is on and the outlook is positive, these currencies will tend to appreciate to a greater extent than other non-dollar currencies." On the flip side, however, when risk appetite decreases these currencies can rack up outsized losses relative to the dollar, he adds.

Overall, Dolan admits "there are a lot of reasons to buy" these two currencies but underscores that they "are all dependent on the view for global recovery."

"I think we are at the tipping point into the end of July," he says. "Things are likely to only become more negative. I think the global recovery is extremely imperiled and the markets have only begun to start repricing that. Everybody's bullish on these currencies, which is another reason that downside might be underestimated," Dolan concludes. ☐



Your
fx trading
Room

Proud Independent Distributor of Your Trading Room

**5 Day FREE Trial to sit alongside
our Professional Traders
Experience the Your FX Trading
Room difference today**



Hail the China float

China's decision to allow to yuan to float on a limited basis has implications for the FX market and the global economy.

BY BARBARA ROCKEFELLER

Is China running the global macro show these days? The evidence is strong China has more influence than it's getting credit for, and it's not doing a bad job, either. But we can barely stand to think of the idea of China running the show because the Chinese approach is one of judgment, management, and top-down control rather than free-market principles.

Just ahead of the G20 summit in Toronto in late June, China announced it would allow a more flexible yuan exchange rate from the dollar peg instituted in July 2008. Before that, from August 2005 to July 2008, the yuan was in a managed float that resulted in a 20-percent appreciation against the dollar (Figure 1).

As with all artificially set rates, a chart like this is of no

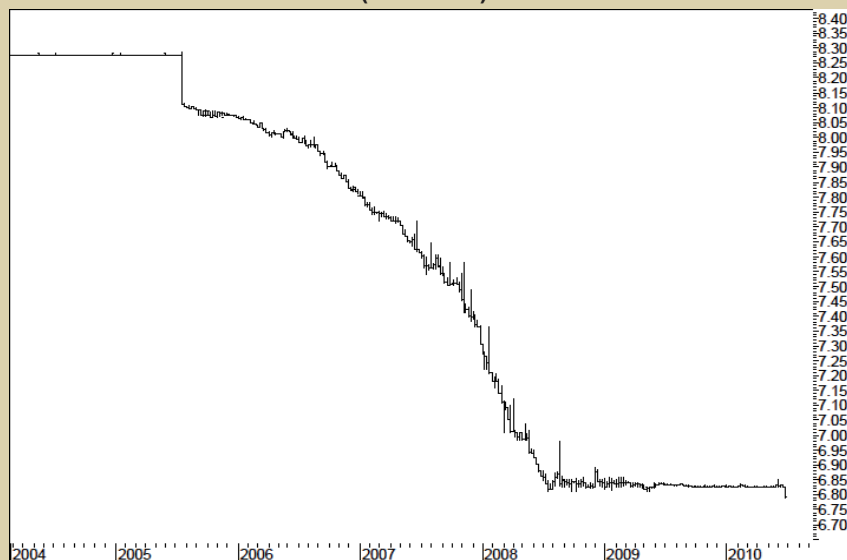
use to a technical analyst. We might suggest the scope of the first revaluation is likely to be repeated, but such an assertion would have to be a matter of faith rather than evidence. Conditions are different now than in 2005. Not only are conditions different within China, the entire world of international finance has been transformed — by everything from the Bear Stearns and Lehman Brothers failures to the sub-prime and European sovereign-debt crises.

And therein lies the explanation for the Chinese abandoning the managed float and returning to a fixed-dollar peg: as 2008 progressed, they lost confidence in the soundness of Western and particularly American institutions to deal effectively and quickly with crisis. Figure 2 shows the yuan/dollar from March 2008, when Bear Stearns failed, to the July restoration of the dollar peg.

We need to revisit this ancient history to understand what is happening today in the FX and other markets. On the surface, the Chinese appear to be caving in to Western demands for a revaluation to reduce trade imbalances. Despite their repeated warnings that they accept no outside interference and will act only on their own timetable, China was concerned about the threat of a face-losing unfavorable mention at the G20 meeting, not to mention a U.S. Senate tariff bill.

But the decision to re-float the yuan is actually a vote of confidence in Western governments and financial institutions. That it signals a spirit of cooperativeness and suits domestic Chinese priorities (such as promoting consumption and tempering hot-money flows) is secondary. The decision has far-reach-

FIGURE 1: CHINESE YUAN (WEEKLY)



During its "managed float" from August 2005 to July 2008, the yuan appreciated 20 percent vs. the dollar.

ing consequences for intermarket analysis and for the dollar.

To see how events might unfold, we need to go back to 2008 again. The Fed had already cut rates (by 50 basis points) in September 2007 and November 2007 (by 25 bp), but on January 22, 2008 and again on March 18, 2008, it cut rates by an “emergency” 75 bp for a total of 2.25 percent. In April it cut again by the more usual 25 bp. This series of rate cuts was taken by the markets as a signal the Fed was willing to throw the dollar under the bus in order to keep the financial sector liquid and functioning, and thus fend off recession.

This was the period when hedge funds and other supposedly sophisticated investors decided oil was a hedge against the falling dollar. This never made much sense from an economic perspective; if the U.S. was heading into recession, surely demand for oil would fall and prices should follow suit. The dollar index was crashing during 2006-2007, and oil started to move inversely, with more momentum near end-2007 (Figure 3). This strange correlation was halted and reversed, for a while, around the same time as China re-pegged the yuan in July 2008. Speculators, including banks, lost a lot of money when oil failed to keep rallying to \$200/barrel, as forecast, and instead stopped at a high of \$147.27 on Sept. 11, 2008.

In fact, the yuan peg coincided with the end of the stock market free-fall and drop in 10-year Treasury yields, as well as the end of the oil bubble (Figure 4). We don’t usually attribute all these events to the single act of the Chinese re-pegging the yuan, but the Chinese assert their decision was for the greater good of the global financial system, and we cannot say they are wrong.

Fast forward to summer 2010
China’s decision to re-engage in a man-

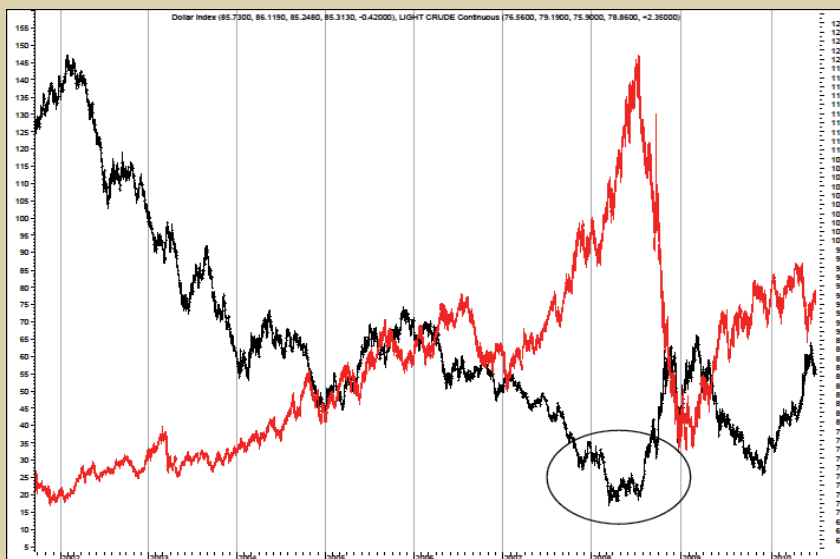
aged float saw the heavy hand of the state from Day 1 (June 21). First there was a big move, then on Day 2, instead of the morning fixing at a set percentage change from the previous day’s fix price, the central banks set the rate at the previous day’s close. The day after that, Chinese banks became heavy dollar buyers, presumably as a form of hidden state intervention, to prove the managed float

FIGURE 2: CHINESE YUAN 2008



The July 2008 restoration of the dollar peg halted the yuan’s continued appreciation.

FIGURE 3: DOLLAR INDEX VS. OIL



The inverse relation between oil (red) and the dollar (black) halted and reversed (for a while) around the same time as China re-pegged the yuan in July 2008.



was not a one-way street. On any day the yuan may vary as much as 0.05 percent, but not every day. Speculators are on notice not only of a two-way street, but also that the government is market-savvy and can change its practices at will.

Manipulating your currency via a managed float is a very different thing from manipulating other markets with a diverse set of players, such as Euro/dollar, oil and gold. And yet, on the first trading day after the weekend announcement of the float, the Euro/dollar opened higher

but closed near its low, and proceeded to fall for the next two days — in the midst of a corrective up move (Figure 5). Commentators for the most part noted China's announcement of the resumption of the float was Euro-negative, as though this was the most natural and logical thing in the world.

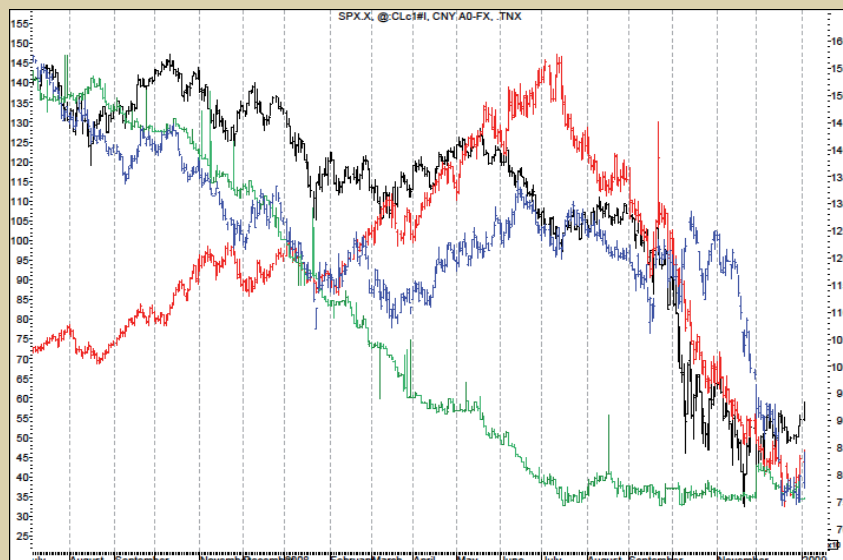
But it's not natural and logical. Why should the Euro automatically fall? By the time of the 2008 yuan peg to the dollar, the yuan had already appreciated against the Euro by about 15 percent. Perhaps analysts assumed the yuan would be an equilibrating agent — and yet the sums that go through the tightly controlled yuan market are tiny compared to the overall size of the Euro/dollar trade.

Nobody knows how much the yuan will rise against the currency basket, which does indeed include the Euro as well as the dollar, but current thinking is that it will be less than the 2005-2008 move and possibly as little as the non-deliverable forwards suggest, or 2-3 percent per year. All the work is not yet in, but even if it's a reasonable 10 percent, that's not going to change the global imbalance by much. But maybe it doesn't need to be changed by much; a change at the margin can be critical.

The other effect of the China float is the encouragement of risk appetite, which has the perverse effect of raising the price of oil and other commodities, surely not a goal of the Chinese. Equities, as of the week ending after the announcement, are not embracing the Chinese move as an "all-clear," but they can be a bit slow to see the forest for the trees.

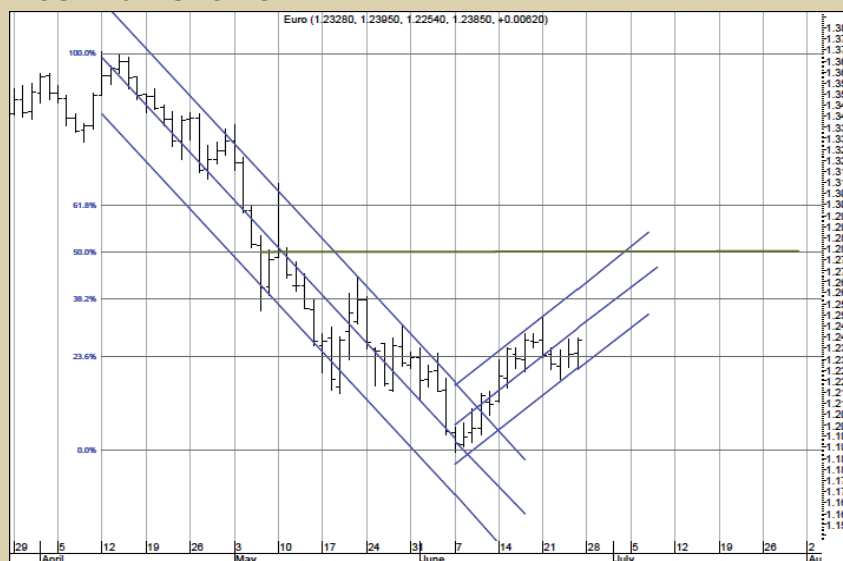
Right now the forest looks gloomy. The U.S. continues to show signs of persistent recessionary tendencies, including housing sales down despite the lowest mortgage rates in 60 years, a distinct lack of inflationary pressure

FIGURE 4: 2008 COMPARISON



The yuan (green) peg coincided with the end of the stock market free-fall (black), a drop in 10-year Treasury yields (blue), and the end of the oil bubble (red).

FIGURE 5: EURO/DOLLAR



On the first trading day after the announcement of the float, the Euro/dollar pair opened higher but closed near its low, and fell for the next two days — in the midst of a corrective up move.

and, as of the Federal Open Market Committee meeting in late June, U.S. rates on hold for an indefinite “extended period.” First-quarter GDP was reported at only 2.7 percent in the final estimate, down more than expected from the first estimate and down a lot from Q4 at 5.6 percent, if a whole lot better than -6.4 percent in Q1 the year before.

Deleveraging is still taking place slowly and banks are still not lending, preferring instead to borrow at nearly no cost and park the money in safe, if low-yielding, government paper while they re-build capital.

Net-net, the China float does the U.S. three favors, not only by the vote of confidence and some trade equilibration that will push exports and export-industry jobs, but also optimism that global change is possible and a rise in risk appetite. As timing goes, the Chinese picked a really good point in the cycle to demonstrate confidence in the West and promote risk appetite — with little risk of being accused of starting a forest fire. By normalizing conditions and reducing uncertainty about the currency component, if a managed float can be called “normal,” they also are setting the stage for a recovery in their own stock index, beset by numerous structural problems and down in bear-market territory that may be just leveling near the end of June (Figure 6).

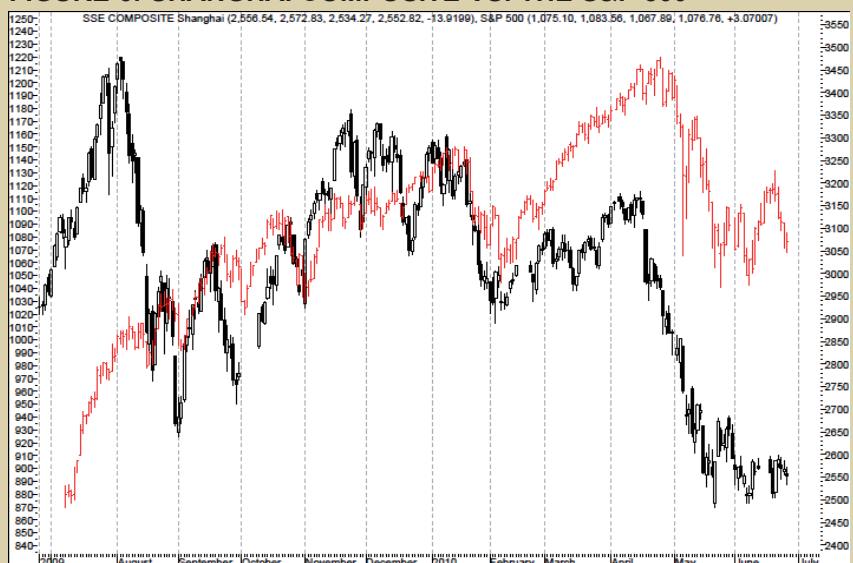
The currency effect

The near-term effect of the China float on the dollar should be relatively negative. With U.S. interest rates so low, the dollar is a funding currency for [carry trades](#) into more risky and glamorous assets, including BRIC equities.

Longer-term, to the degree trade does become less unbalanced, the ugly U.S. deficit may become less of a millstone around the dollar’s neck. The question then becomes when the Fed will raise rates. After the downbeat June policy meeting, forecasters pushed out their first-hike date to end 2011 and some even to 2012. Relative interest rates are not the only factor determining exchange rates these days, but they are still a powerful one. That implies a weak dollar for a very long time, but it also implies low bond yields, with the 10-year yield breaking the 3-percent “floor,” but the bright side of that is lowered funding costs at a time when bond vigilantes are complaining about the nearly Grecian level of U.S. government debt.

What if revived risk appetite takes oil back to \$140, or some other unintended consequence develops? China has more than one ace — the pegging ace — up its sleeve. As

FIGURE 6: SHANGHAI COMPOSITE VS. THE S&P 500



Chinese stocks (black) have sold off significantly over the past several months.

the world’s second largest consumer of oil (and vast stock-piles), China can potentially have a big effect on day-to-day demand. As the world’s largest gold producer, it can influence the price of gold if it starts heading for \$1,500 and \$2,000, signifying fear. And as the second-largest holder of U.S. government paper it can, as we have already seen several times, influence yield simply by repeating it will continue to hold and to buy, even if the reason is not particularly pro-U.S. (It has no choice — the U.S. has the only large bond market.)

It’s not that China will or should manipulate global markets, but make no mistake, it could if it wanted to. China has a mistrust of the free market and prefers control. The mistrust is defensible. History shows whole generations can lose their savings and trust in government, a very big risk for what is essentially a new regime. The communist regime may date back to 1949 but the partial embrace of free markets, dating from 1979 but accelerating after 2002, is relatively new. It has paid off handsomely, too. Why risk it?

A new era may be about to begin in which prices are a lot less free, whether from the heavy hand of regulation or state interference. The interesting thing about such a trend, if it develops, is that artificially set rates are not sustainable once the market decides against the false levels. The most famous case is the UK, where Britain saw its artificially pegged currency get thrown out of European Exchange Rate Mechanism (ERM) in 1992 after extreme pressure from speculators, including Mr. Soros, with great financial and economic dislocations both before and after. The question becomes whether a government that likes control can demonstrate restraint.📌

For information on the author, see p. 4.



The yuan revaluation situation

Economic realities in China make the much-debated yuan exchange rate less of an issue than many traders think.

BY YINGHUA ZHU AND MARC CHANDLER

The Russian despot Vladimir Lenin was a big fan of Frederick Taylor, an American whose scientific management principles revolutionized the labor process by boosting output, albeit often at the cost of worker dehumanization. Taylorism is not about capitalism per se, it is about efficiency, and apparently good communists can respect that.

As Taylorism was adopted by the Soviet Union, so too, it appears, "Fordism" may be coming to China. Fordism refers to a type of political economy that recognizes, despite great disparities in power between workers and owners/management, workers need to earn high enough wages to purchase the goods that are being created in order to complete the production cycle.

The financial impact of the Euro's decline over the past six months has prompted European officials to dial back their calls for Chinese yuan appreciation (Figure 1). While the U.S. Treasury appears to be embracing a multilateral effort (e.g., via the IMF and G20), many in the U.S. congress are preparing to escalate their case for yuan appreciation, perhaps (if it is not too cynical) as the November mid-term elections approach.

Unfortunately, the focus on bilateral exchange rates makes for poor economics and poor policy and investment strategy, even if it plays well in Peoria. The large U.S. trade deficit with China (and its larger trade deficit with the rest of the world) is not simply a function of exchange rates, but is rather a result of investment, savings, consumption patterns, and corporate strategies, which include the division of labor brought about by globalization.

Wages, not exchange rates

Although many pundits refer to China as "factory of the world," it might better described as the "assembler of the world." While last year China was the world's biggest exporter, it was also one of the world's biggest importers. China does not simply import raw materials and commodities; it also imports parts and semi-finished goods, which it then assembles.

Those imported raw materials and commodities are largely invoiced in U.S. dollars, as are the parts and semi-finished goods. The cost of these inputs is estimated to be about 25 percent of the price of the finished good. Another quarter of the price can come from the value-added in the assembly work, which is the only part that is sensitive to the value

FIGURE 1: EURO/YUAN



In addition to falling hard against the dollar, the Euro has declined significantly vs. the Chinese yuan over the past six months. European officials have dialed down their calls for Chinese yuan appreciation in light of the Euro's decline.
Source: ADVFN

of the yuan.

The other 50 percent of the price is incurred locally in the U.S. for storage, shipping, and marketing. Of course, each of those middlemen also earns a profit. The fact that only a small part of the price of the Chinese-made goods is impacted by the value of the yuan means that nearly any reasonable currency appreciation will be insufficient to balance the accounts.

Some U.S. politicians like to cite extreme estimates that the yuan is undervalued by as much as 40 percent vs. the dollar. But the discrepancy between U.S. and Chinese manufacturing wages represents an even more profound gap. Chinese manufacturing wages are about 3 percent of manufacturing wages in the U.S.

The impact of a 40-percent appreciation of the yuan on the price of a Chinese good would be limited to the increased cost of the value-added component of that good—that is, the wages of the Chinese manufacturing worker. Everything else being equal, it would raise the price of a Chinese-made good by 10 percent. However, Chinese manufacturing wages would still be only 4.2 percent of U.S. wages, and the imbalance would remain. A sharp appreciation of the yuan would also reduce import prices, and therefore likely offset the impact on wages.

Experiences in other countries, such as Japan and Germany in 1970s, suggest a strengthening currency will make the life of many low-cost manufacturers difficult, and in these circumstances whether a country can upgrade its value-added would be a key factor to determine its future competitiveness.

Lessons of the 2005 yuan revaluation

Commodities that rely on Chinese demand will ultimately benefit from eventual yuan revaluation. The 21-percent of appreciation in the yuan from July 2005 to July 2008 provides clues to how commodities may be affected this time around (Figure 2). Like then, the move will probably be gradual and take place over months and years rather than days.

Commodity prices were somewhat encouraged by the moderately stronger yuan, but the primary driver of the 100-percent upward movement during that period was a Chinese economy firing on both domestic and export cylinders. This time around, exports may play a smaller role in the economy and domestic consumption may have a larger role. Chinese domestic consumption is also commodity intensive (i.e., products such as automobiles and white goods). A revalued yuan will only enhance domestic purchasing power.

There was a speculation in 2005 that Chinese purchases of U.S. Treasuries would dwindle as its need to intervene decreased. However, net Treasury purchases actually rose between 2005 and 2008. Trade surpluses

It's all about choosing the right tools to succeed.

Power, precision and control – the drivers to successful FX trading.

Use dbFX's innovative FX tools including Advanced Real Time Charts to:

- Analyse Trends
- Track Positions
- Trade directly from Currency Charts

Plus trading with Deutsche Bank, the largest FX liquidity provider, offers dbFX customers fair and transparent pricing from 1.5 Pips.

Passion to Perform



For a FREE trial of the platform:
Visit: dbfx.com/CT
Call: 866 550 3239



The above information has been approved and/or communicated by Deutsche Bank AG London in accordance with appropriate local legislation and regulation. Deutsche Bank AG London is regulated for the conduct of investment business in the UK by the Financial Services Authority. Trading in margin foreign exchange can be risky. The use of leverage in foreign exchange trading can lead to large losses as well as large gains. Markets referred to in this publication can be highly volatile. For general information regarding the nature and risks of the proposed transaction and types of financial instruments please go to www.globalmarkets.db.com/riskdisclosures. This product may not be appropriate for all investors. Before entering into this product you should take steps to ensure that you understand and have made an independent assessment of the appropriateness of the product.

**FIGURE 2: DOLLAR/YUAN**

The dollar/yuan pair shifted slightly out of its straitjacket after China announced in mid-June it planned to let the yuan resume floating in a limited range.

Source: ADVFN

also rose dramatically during this window, which might have been the primary catalyst for the increased Treasury purchases.

Revaluation may be a positive for the Chinese A-share market (the country's domestic-only equity market) because it makes stock valuations appear more attractive in foreign currency terms and will aid Chinese companies by boosting domestic purchasing power. Raw material importers, airlines, and paper producers benefited the

China says it will loosen reins

In late June China's central bank signaled it would make the yuan more flexible. Although the move was universally embraced, what the U.S. (and many others) mean by flexible is different than what China means. The U.S. means the Chinese government should stop depressing the yuan so the currency can appreciate accordingly. China seems to mean two-way movement within a relatively narrow band. The 0.5-percent band that China allows the yuan to fluctuate vs. the dollar's reference rate is not being changed.

China's move succeeded in stealing some of the thunder from its critics at the Toronto G20 meeting the weekend of June 25, but the resulting pace and magnitude of the yuan's appreciation is far from clear. The 12-month non-deliverable forward market implies a little more than 2-percent appreciation over the next year which, if roughly accurate, is not very meaningful in terms of trade and capital flows.

most in the domestic A-share market after China's July 2005 yuan revaluation, because the move reduced the cost of raw materials such as fuel oil and pulp, and increased the ability of domestic consumers to take on higher costs. Companies with dollar-denominated debt also benefited after the 2005 revaluation.

Since the yuan's first appreciation against the USD that year, there have been three major periods of currency movement: 1) July 2005-May 2006, when the yuan appreciated slightly and the MSCI China index rose about 2.7 percent annually; 2) June 2006-July 2008, when yuan appreciation accelerated and the MSCI China index rose 2.3-percent per month on average; and 3) August 2008 to mid-June 2010, when yuan appreciation stopped and the MSCI

China index was flat. It appears yuan appreciation may have some positive impact on Chinese equities, perhaps attracting even more hot money.

Revaluation will also support the currencies of Emerging Asia and Australia, economies that are closely linked to China. Forty-nine percent of China's imports came from Emerging Asia, followed by Japan, with 13 percent. China has been Emerging Asia's biggest trading partner over the past few years and a gradual yuan appreciation will further boost the country's purchasing power. China is South Korea's largest trade partner, accounting for a much larger portion of Korean imports and exports than the U.S., Europe, or Japan. China is not only the biggest source of Malaysia's imports but also one of the major destinations for its exports, behind only the U.S., the EU, Japan, and Singapore. In addition, China is Argentina's second-largest trade partner, topped only by Brazil.

More flexible yuan policy could also mean the yuan could fall. Most people have assumed a non-dollar-pegged yuan would mean a higher yuan, which, all else being equal, would reduce the Chinese trade surplus with the U.S. (and is what the Americans want). On the other hand, if China enters a period of more consistent trade deficits, it would not be surprising if the yuan actually falls. Much to the surprise of many observers and economists, China did import more than it exported in March 2010. ■

For information on the authors, see p. 4. To read an extended version of this article, which analyzes China's labor situation and the implications of a revalued yuan, see the September issue of Active Trader magazine, available in August.

Join Thousands of Futures and Forex Traders in Las Vegas This Fall...



THE Futures & Forex EXPOSM

SEPTEMBER 23-25, 2010
CAESARS PALACE • LAS VEGAS

- **Discover** tools and strategies relevant to the futures and forex markets that you trade
- **Learn** proven techniques from industry leaders that you can implement for profit immediately
- **Gain** the advantage and knowledge successful traders need to stay ahead of today's futures and forex markets



Rob Booker



John Carter



John Forman



Todd Gordon

...and many more!

Register FREE at
www.FuturesandForexExpo.com
or call 800/970-4355.
Mention priority code 019171.

GOLD SPONSORS



MEDIA PARTNER



a Production of



Githler Center • 1258 North Palm Avenue
Sarasota, FL 34236



Five-minute forex scalp

Favorable winning percentage and aggressive entry points
help scalp pattern capture modest profits.

BY CURRENCY TRADER STAFF

Although intraday trading lures many market players who are reluctant to make long-term trade commitments, it's not an easy path to profits. For starters, traders must overcome the high commission and slippage costs of active trading, they can't make big mistakes that will wipe out multiple small gains, and they also have to be able to sit in front of the screen all day or have an automated execution setup. And they're often competing with highly sophisticated and well-funded algorithmic trading firms.

This all might lead one to wonder whether there are any scalping opportunities left in the markets for retail traders. There might be, but traders should be realistic about what they can accomplish. The following analysis of a short-side scalping setup offers some potential insights into the issues traders will confront regarding trade entry and timing on a very short-term time frame.

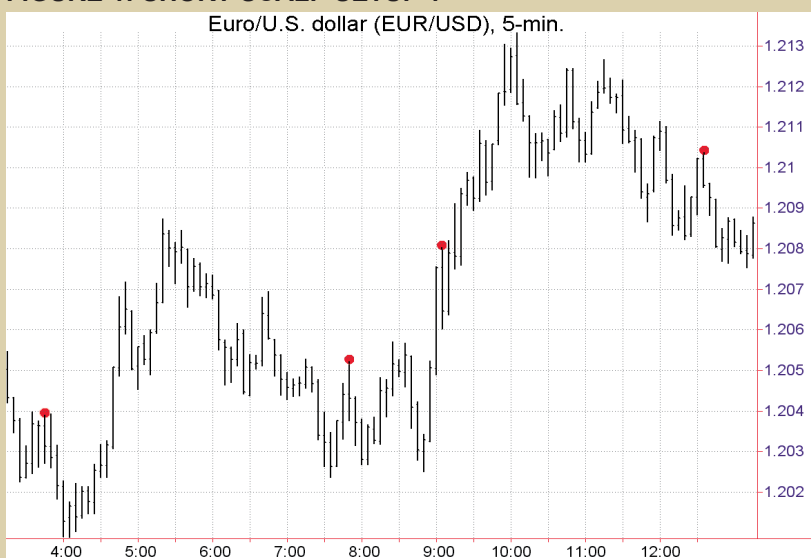
Intraday setup

Figure 1 highlights four examples of a three-bar pattern based on five-minute bars in the Euro/USD pair (EUR/USD): two consecutive bars that close in the upper 25-percent of the bar's range followed by a bar that makes a high at least .0004 higher than the previous bar but closes in the lower half of the bar's range and below the previous close:

1. $(\text{close}[1] - \text{low}[1]) / (\text{high}[1] - \text{low}[1]) \geq .75$
2. $(\text{close}[2] - \text{low}[2]) / (\text{high}[2] - \text{low}[2]) \geq .75$
3. $\text{High}[0] - \text{High}[1] \geq .0004$
4. $\text{close}[0] < \text{close}[1]$
5. $(\text{close}[0] - \text{low}[0]) / (\text{high}[0] - \text{low}[0]) \leq .5$

Where 0, 1, and 2 refer to the most recent bar, one bar ago, and two bars ago, respectively.

FIGURE 1: SHORT SCALP SETUP 1



The pattern goes short after two five-minute bars close strongly, and are then followed by a bar that trades higher but closes weakly.

Source: TradeStation

The various parameters can certainly be modified or optimized, although none of the ones used here are; they are simply based on observation of five-minute bars from June 3 to June 24. Figure 1 shows price dropped at least modestly for several bars after each highlighted bar, with the exception of the one that occurred around 9:10 a.m. Also, no research was conducted to test this pattern or a similar formation on the long side of the market.

Table 1 shows the EUR/USD's average performance from the close of the final bar of the pattern to the closes of the subsequent 12 five-minute bars for the June 3-June 24 period. Two results are shown for each bar interval: one for all 82 patterns, and another for patterns that occurred between midnight and 5 p.m. ET ("00-17 ET"), which encompasses the London and New York trading sessions (59 total). This was done simply to see if there was a notable difference between performance in peak and non-peak trading

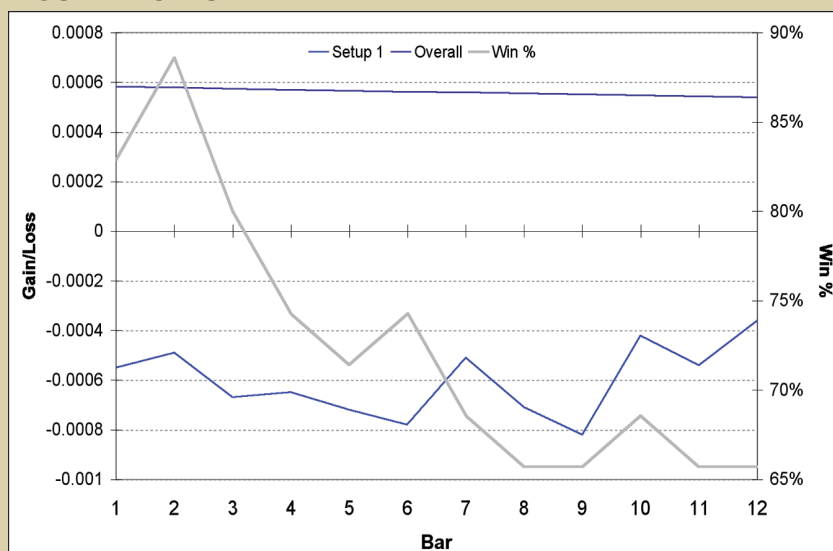
hours for this currency pair. The table also shows the total profit (sum) that would have been captured by exiting the trades at each given bar, and the overall performance for all one- to 12-bar close-to-close moves for the analysis period. Figure 2 graphs the pattern's bar-to-bar performance, and highlights its high winning percentage, especially in the first few bars.

Considering it is unoptimized and provides no context — no information about the immediately preceding price action or the prevailing trend, for example — the pattern shows evidence it was able to identify intraday weakness in the EUR/USD pair. Although an average -1 or -2 pip move might seem hardly worth the effort, it is more noteworthy in light of the EUR/USD pair's upside bias during the period (most five-minute intervals had an average close-to-close gain of five or six pips). The cumulative gains show exiting the trades automatically at each bar's close was profitable, not accounting for commissions. (The figures in the sum row are negative because they represent short trades and price declines.)

Also, the subset of trades in the midnight to 5 p.m. ET period were more profitable, on average, than all trades combined — which is what we'd expect given this period encompasses the

native trading sessions of both components of the EUR/USD pair. Table 2 shows the ratio of the cumulative gains for all trades and the midnight-5-p.m. trades, with both groups being adjusted for their number of trades. A number above 1 means the "all trades" group was more profitable per-entry than the midnight-5 p.m. group; a number below 1 means the opposite. After bar 3, the midnight-5

FIGURE 2: SETUP 1 BAR-BY-BAR



The setup's winning percentage, which was especially high in the first few bars, never fell below 65 percent.

TABLE 1: SCALP SETUP 1 ANALYSIS

| Bar | 1 | | 2 | | 3 | | 4 | | 5 | | 6 | |
|---------|---------|----------|---------|----------|---------|----------|---------|----------|---------|----------|---------|----------|
| | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET |
| Avg. | 0.0000 | 0.0000 | -0.0001 | -0.0001 | -0.0001 | 0.0000 | -0.0002 | -0.0002 | -0.0002 | -0.0002 | -0.0001 | -0.0002 |
| Sum | -0.0025 | -0.0008 | -0.0091 | -0.0064 | -0.0045 | -0.0024 | -0.0135 | -0.0116 | -0.0157 | -0.0131 | -0.0104 | -0.0088 |
| Overall | 0.0006 | | 0.0006 | | 0.0006 | | 0.0006 | | 0.0006 | | 0.0006 | |
| Bar | 7 | | 8 | | 9 | | 10 | | 11 | | 12 | |
| | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET |
| Avg. | -0.0001 | -0.0001 | -0.0002 | -0.0002 | -0.0002 | -0.0002 | -0.0002 | -0.0002 | -0.0002 | -0.0001 | -0.0002 | -0.0002 |
| Sum | -0.0044 | -0.0032 | -0.0124 | -0.0104 | -0.0151 | -0.0111 | -0.0183 | -0.0108 | -0.0136 | -0.0071 | -0.0131 | -0.0131 |
| Overall | 0.0006 | | 0.0006 | | 0.0006 | | 0.0005 | | 0.0005 | | 0.0005 | |

The moves were small, but the setup bucked the EUR/USD's bullish bias during the analysis period.



TABLE 2: PRIME-TIME ADVANTAGE?

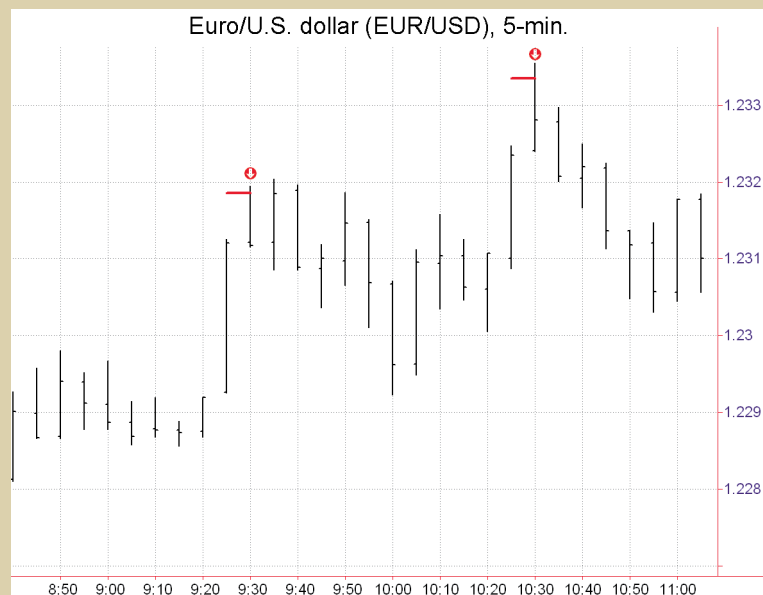
| | |
|--------|------|
| Bar 1 | 2.33 |
| Bar 2 | 1.02 |
| Bar 3 | 1.33 |
| Bar 4 | 0.84 |
| Bar 5 | 0.86 |
| Bar 6 | 0.85 |
| Bar 7 | 0.98 |
| Bar 8 | 0.86 |
| Bar 9 | 0.98 |
| Bar 10 | 1.22 |
| Bar 11 | 1.38 |
| Bar 12 | 0.96 |

From bar 4 to bar 12 trades executed between midnight and 5 p.m. ET had a relative advantage over all trades for all intervals bars 10 and 11.

p.m. group was more productive than the all trades group, with the exception of bars 10 and 11. (The lower cumulative profits for the midnight-5 p.m. group at each interval are simply a function of its smaller number of trades.)

Overall, though, it might be wise to question the practicality of this setup, given the maximum accumulated profit was 183 pips (exiting on the close of bar 10), before commissions. Let's see if there's any way to extract more potential from the pattern.

FIGURE 3: SHORT SCALP SETUP 2



The second short setup enters .0006 above the high of the second consecutive bar that closes in the upper 25 percent of the bar's range. In both cases the entry points were higher than the third bar's close. Source: TradeStation

Selling into strength

Like many patterns of this type, execution is triggered by evidence of the reversal of the recent price momentum. In this case, the upside momentum of two bars that close strongly is reversed by a third bar that closes weakly.

It might be psychologically comfortable to wait for the confirmation of the third bar's weak close, but doing so

means the market has already moved lower by the time the trade is executed. Although this might be relatively unimportant to a pattern triggering a trade that might last several days or weeks (or even hours), it can mean the difference between winning and losing when attempting to scalp the market to extract a handful of ticks. It would be

TABLE 3: SCALP SETUP 2 ANALYSIS

| Bar | 1 | | 2 | | 3 | | 4 | | 5 | | 6 | |
|---------|---------|----------|---------|----------|---------|----------|---------|----------|---------|----------|---------|----------|
| | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET |
| Setup 2 | -0.0003 | -0.0006 | -0.0006 | -0.0006 | -0.0009 | -0.0009 | -0.0007 | -0.0007 | -0.0010 | -0.0011 | -0.0008 | -0.0010 |
| Overall | 0.0006 | | 0.0006 | | 0.0006 | | 0.0006 | | 0.0006 | | 0.0006 | |
| Win % | 74.07% | 69.57% | 85.19% | 82.61% | 81.48% | 78.26% | 77.78% | 78.26% | 74.07% | 73.91% | 70.37% | 69.57% |
| Bar | 7 | | 8 | | 9 | | 10 | | 11 | | 12 | |
| | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET | All | 00-17 ET |
| Setup 2 | -0.0007 | -0.0009 | -0.0008 | -0.0010 | -0.0009 | -0.0009 | -0.0007 | -0.0008 | -0.0006 | -0.0009 | -0.0009 | -0.0009 |
| Overall | 0.0006 | | 0.0006 | | 0.0006 | | 0.0005 | | 0.0005 | | 0.0005 | |
| Win % | 70.37% | 65.22% | 66.67% | 65.22% | 66.67% | 60.87% | 66.67% | 65.22% | 59.26% | 60.87% | 62.96% | 56.52% |

The second scalp setup was much more profitable than the first on a net basis, despite triggering only 33 percent as often.

much more advantageous to enter when the market is still rising.

Further analysis showed the lower-close component — which was the result of visual chart inspection — was more or less superfluous. In fact, by requiring the second and third bar's to exceed their preceding bars' highs by a certain amount, it was possible to enter a certain amount above the second bar's high — rather than at the third bar's close — and enhance the pattern's profitability (in the context of a modest scalp approach, of course) without sacrificing much of its reliability. The modified pattern rules are:

1. $(\text{close}[1] - \text{low}[1]) / (\text{high}[1] - \text{low}[1]) \geq .75$
2. $(\text{close}[2] - \text{low}[2]) / (\text{high}[2] - \text{low}[2]) \geq .75$
3. $\text{High}[0] - \text{High}[1] \geq 0.0006$
4. $\text{High}[1] > \text{High}[2] + 0.0004$,

This variation removes the current bar's close from the picture, and instead requires the current bar's high to be at least .0006 above the previous bar's high, and that bar's high must be more than .0004 above the preceding high. Again, these parameters are unoptimized; no effort was made to find better-performing settings. Figure 3 shows two representative trades. Notice the dashes marking the entry points on the left sides of these bars are well above the closing prices. The first setup, which also triggered a trade at the 9:30 a.m. bar, would have entered seven ticks lower on the close and would have been in the red for most of the next 10 minutes.

By entering short at the current bar .0006 above the previous bar's high ($\text{High}[1]$), this scalp pattern sells into strength as it still unfolding rather than entering lower on a "confirming" lower close. Although this pattern triggered only 27 times during the analysis window, Table 3 shows it was much more profitable than the initial setup, both on an average-trade basis and cumulatively. Figure 4 graphs the pattern's performance. Again, the winning percentage was very high (above 70 percent through bar 7), and the median trade profit peaked at bar 5.

Adjusted for the number of trades, the difference in performance is even more noticeable. This setup was cumulatively more profitable than the first despite far fewer trades. The ratio the second pattern's trade-adjusted profitability was five to 31 times larger than the initial pattern's from bars 1 to 3, after which it tapered off to the 3 to 4 range. (It was smaller only at bars 11 and 12.)

Finally, Table 4 shows there was little difference between the midnight-5 p.m. trades and all trades — mostly because 23 of the 27 trades occurred

in the "prime time" period. The ratio of trade-adjusted cumulative profits flitted above and below 1.00, with the midnight-5 p.m. results operating at a slight advantage through bar 6 and a slight disadvantage after. (The negative result at bar 12 is the result of the cumulative net gain posted by the second pattern at this interval.)


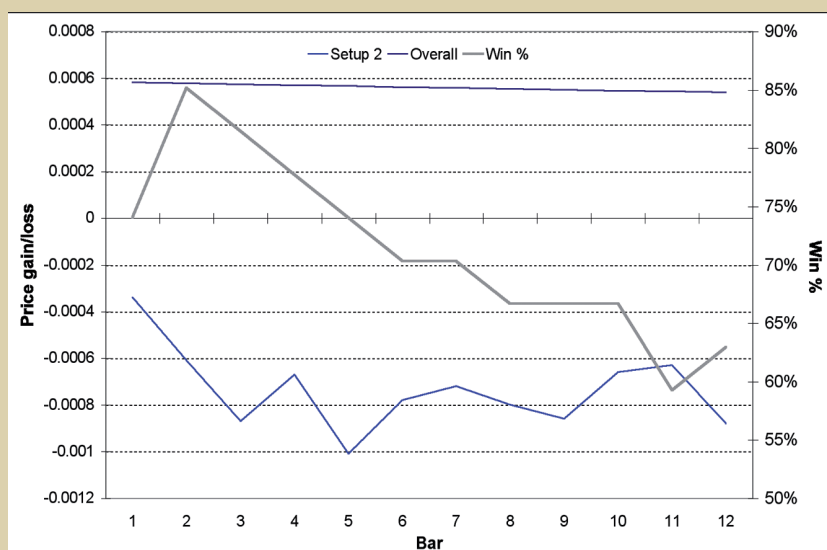
There's not a lot of room for error in any short-term intraday trading technique. Large losses must be avoided and a relatively high winning percentage must be maintained to keep profits flowing. Also, traders do not have the luxury of waiting for a confirming move before entering position; more often than not, doing so will mean the move is over before you can capitalize on it. Most of all, traders must reconcile themselves to trading large position sizes to make the small point gains of such setups worthwhile (see the [Forex Trade Journal](#), for example). Selling into strength or buying weakness that is still in effect increases the odds of capturing more of a correction or reversal. 

TABLE 4: PEAK AND OFF-PEAK

| | |
|--------|-------|
| Bar 1 | 0.94 |
| Bar 2 | 0.97 |
| Bar 3 | 1.00 |
| Bar 4 | 1.16 |
| Bar 5 | 0.98 |
| Bar 6 | 0.91 |
| Bar 7 | 1.07 |
| Bar 8 | 0.90 |
| Bar 9 | 1.07 |
| Bar 10 | 1.05 |
| Bar 11 | 2.19 |
| Bar 12 | -0.52 |

There was little difference between the midnight-5 p.m. trades and all trades — mostly because 23 of the 27 trades occurred in the "prime time" period.

FIGURE 4: SETUP 2 BAR-BY-BAR



The second scalp pattern's winning percentage was very high, especially at bars 1-3, which were all 80 percent or higher.



The Robin Hood carry: The yuan as a funding currency

The opening of the yuan carry trade after June 2009 led to a liquidity-fueled global stock and bond bull market.

BY HOWARD L. SIMONS

Carry trades have been part of the global financial and economic landscape for the entirety of the floating exchange-rate era. As long as one country's interest rates are less than another country's interest rates, the temptation to borrow in the former and lend in the latter will be there. It is no more remarkable than water flowing downhill.

What is unusual about the topic at hand is we are accustomed to thinking of the funding currency, the one with the low interest rates, as being in economic trouble. This certainly was the case for the long-running yen carry trade, and later for the Swiss franc and U.S. dollar carry trades

(see "Looking at the carry trade," "The short, awful life of the dollar carry trade," and "Franc-ly my dear, I don't give a carry," June 2007, August 2008, and September 2008, respectively). What happens when the funding country is the world's largest holder of foreign reserves, the world's largest creditor to the United States, and the owner of the highest average annual economic growth rate for the last decade?

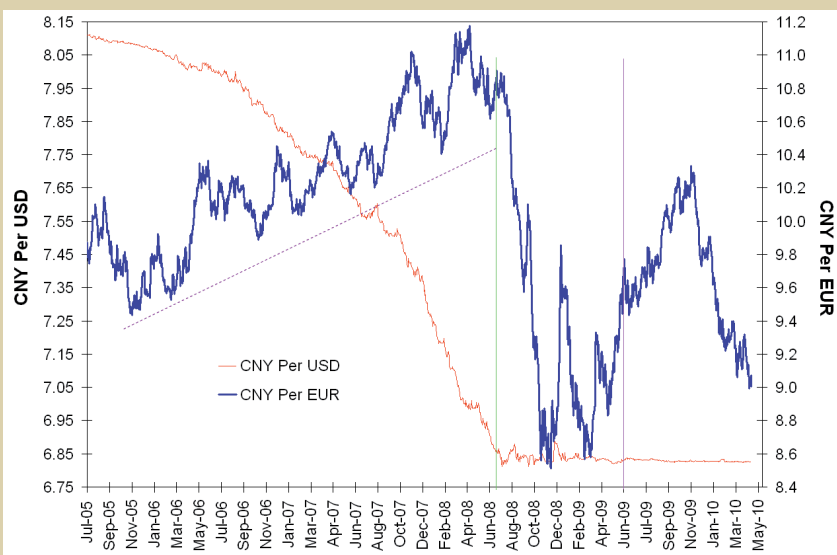
We are speaking, of course, about China. The Chinese yuan (CNY) has gone through three distinct periods over the past decade. First, it was pegged, much to the consternation of U.S. protectionists, to the

USD until July 21, 2005. It then began a gradual and controlled revaluation until, without public notice, it was re-pegged to the USD over the weekend of July 12-13, 2008—apparently part of a deal to maintain China as an investor in U.S. agency securities. This date will be noted with a green vertical line on all accompanying charts.

The third period, noted with a magenta vertical line on all charts, came during mid-June 2009. This was when the total carry return of the USD into the CNY stopped rising. As the currency was pegged, we can infer the interest spread converged to zero at this time. The Chinese had to adopt U.S. interest rates to maintain the peg of the CNY

This started to end on May 25, 2010 with a significant flattening of the Chinese money market curve; six-month CNY rose relative to nine-month CNY. After the close of business on June 18,

FIGURE 1: TWO YUAN SPOT RATES



Before July 2008, the CNY consistently strengthened vs. the USD (declining red line) while the CNY weakened against the EUR (blue line), which means the USD was weakening significantly against the EUR during this period.

2010, the Peoples' Bank of China announced it would allow for a gradual revaluation of the CNY.

Greenbacks and Euros and yuan, oh my

We can illustrate the yuan carry trade with two currency pairs, the USD/CNY and the CNY/EUR. First, let's take a look at them as spot rates only. Figure 1 illustrates the previously discussed history; prior to July 2008, the consistent strengthening of the CNY against the USD is quite visible (declining red line). The CNY weakened against the EUR as part of an erratic trend (blue line); by the transitive property of relationships, we can deduce the USD was weakening against the EUR significantly over this period.

The effects of the July 2008 re-pegging of the CNY are obvious, especially in light of the rather pronounced volatility of the CNY per EUR rate. Once interest-rate convergence was achieved in June 2009, the CNY began to weaken against the EUR until the latter currency started to feel the ill effects of its various sovereign-credit crises at the end of November 2009.

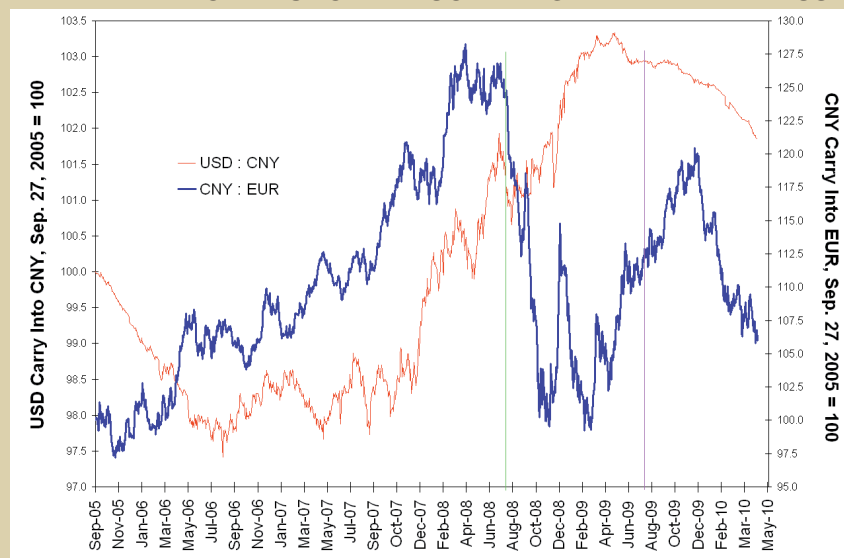
Now let's restate the two exchange rates not in terms of spot values, but rather in terms of a carry index beginning in September 2005. For simplicity's sake, the dollar carry into the yuan and the yuan carry into the Euro will be designated as USD:CNY and CNY:EUR. The carry indices combine interest-rate spread returns as well as spot rate gains and losses.

The key feature for the USD:CNY is how it flattens after interest-rate convergence (Figure 2). The key feature for the CNY:EUR is how profitable it became between June and November 2009 to borrow the CNY and lend in the EUR. This profitability and a similar profitability for the USD:CNY prior to July 2008 coincided with global bull markets in equities and other risky assets. After both carry trades started to weaken, global markets for risky assets remained stalled until irrefutable evidence the world was not headed back into recession emerged in February 2010.

Equity market effects

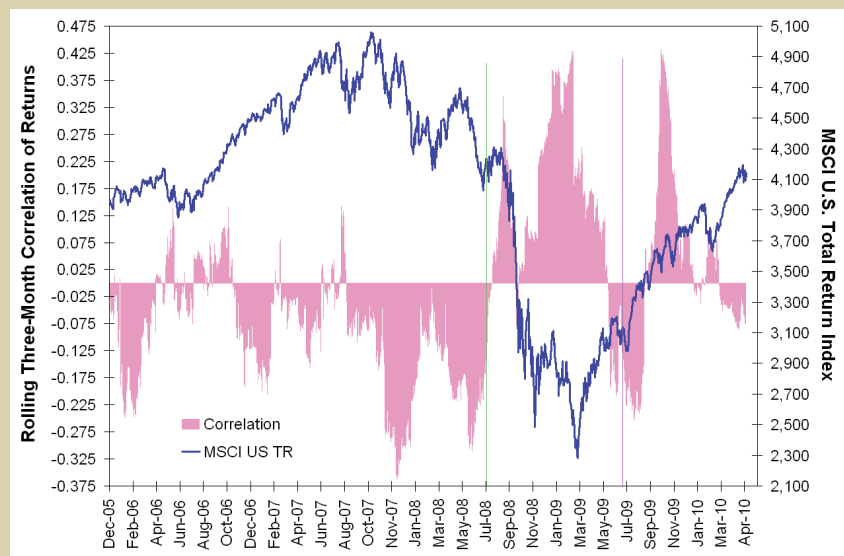
Let's demonstrate these relationships by mapping the MSCI total return index for the U.S. against a three-month rolling correlation of returns for this series against those

FIGURE 2: CHINA COULD LEND PROFITABLY IN EUROZONE BEFORE EUROPEAN SOVEREIGN-DEBT WEAKNESS



The profitability of borrowing the CNY and lending in the EUR between June and November 2009, and a similar profitability for the USD:CNY prior to July 2008, coincided with global bull markets in equities and other risky assets.

FIGURE 3: THE USD:CNY CARRY AND U.S. STOCKS



Prior to July 2008, the correlation between USD:CNY carry returns and U.S. stock return was mostly negative. During the late-2008 financial crisis the correlation of returns turned positive as global money fled into the dollar, but by 2010 the overall correlation was weak and unstable once again.



of the USD:CNY (Figure 3). The answer does not jump out at us immediately when we view the chart; prior to July 2008, the correlation of returns is mostly negative. As

American stocks rose (fell), the USD:CNY generally fell (rose). During the financial crisis of late 2008, the correlation of returns turned positive as global money fled into the dollar. By 2010, the overall correlation was weak and unstable once again.

It was only after August 24, 2009 that the impact of the USD:CNY became apparent, and here the cause was external. Three-month USD LIBOR fell below three-month JPY LIBOR; it was now cheaper for anyone involved in global carry trades to borrow the USD than to borrow the JPY. This unexpected switch in global funding rates would remain intact until March 2010. As the global supply of USD is much larger than that of JPY, and because the \$2.273 trillion foreign exchange reserves of China were linked to USD rates, a sudden source of cheap funding became available for global financial speculation. Global equity markets scarcely experienced a downtick over the next two months.

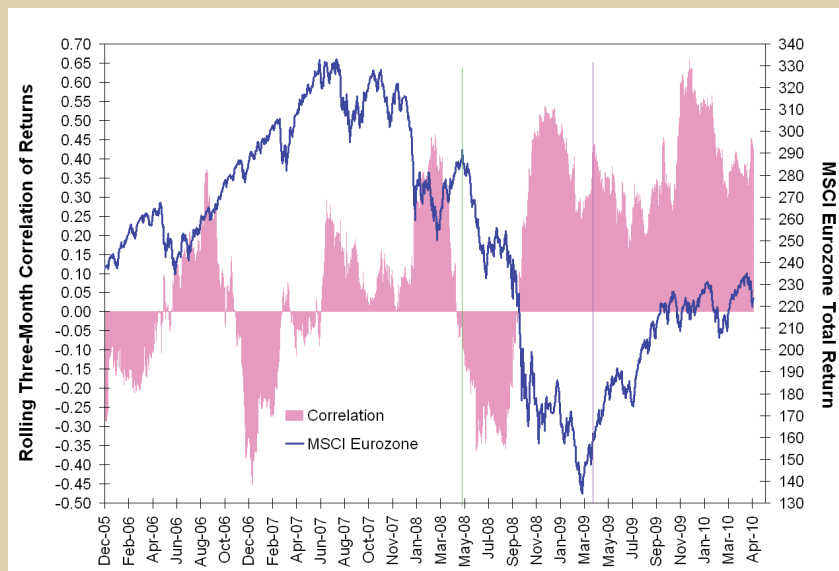
It is in the EUR, however, where the effects of the carry trades really become evident (Figure 4). Shortly after the July 2008 re-pegging, the three-month rolling correlation of returns between the MSCI Eurozone index and the CNY:EUR turned and remained strongly positive regardless of what European equities were doing. USD rates were well below EUR rates throughout this period, and as China moved toward interest-rate convergence with the U.S., both currencies became funding sources for European (and other) markets.

Fixed-income effects

If the yuan carry trade affects equities, it should affect fixed-income markets as well. Let's use the Merrill Lynch total return series for the U.S. and Pan-European bonds for government bond returns and the ML U.S. Corporate & High-Yield Master and Eurozone 7-10 Year Corporate index for corporate bonds.

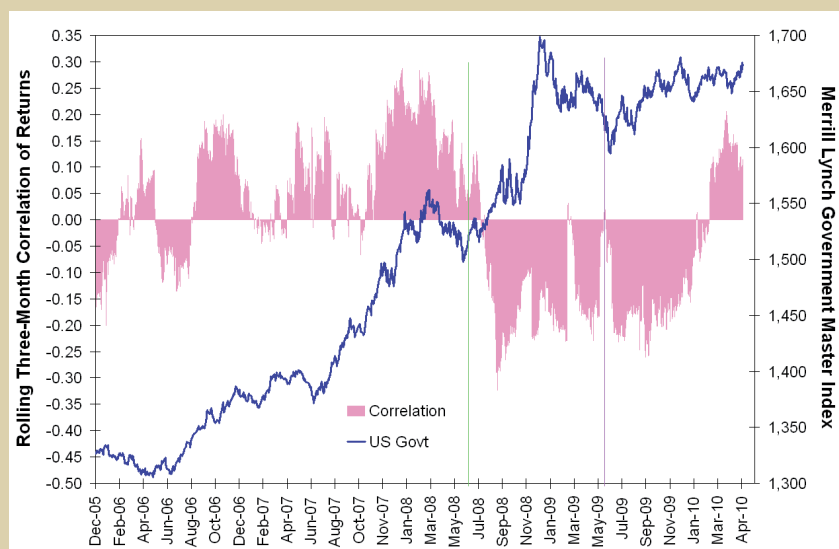
First, the three-month rolling correlation of returns between the USD:CNY and U.S. government bonds turned negative after the July 2008 re-pegging of the CNY, and it remained negative until

FIGURE 4: THE CNY:EUR CARRY AND EUROZONE STOCKS NOW STRONGLY POSITIVELY CORRELATED



Shortly after the July 2008 re-pegging of the yuan to the dollar, correlation of returns between the MSCI Eurozone index and the CNY:EUR turned and remained strongly positive regardless of what European equities were doing.

FIGURE 5: THE USD:CNY CARRY AND U.S. GOVERNMENT BONDS



The correlation of returns between the USD:CNY and U.S. government bonds turned negative after the July 2008 re-pegging of the CNY, and it remained so until February 2010.

February 2010 (Figure 5).

The picture is different for the U.S. corporate bonds (Figure 6). As investors dumped these bonds during the 2008 financial panic, the correlation turned sharply negative. Once the returns on the USD:CNY started to flatten and investors moved back into corporate bonds in 2009, the correlation again turned negative until February 2010.

Figure 7 shows much less negative correlation of returns between the CNY:EUR and Pan-European government bonds. The wider carry allowed funds to flow into the European government bonds and support a huge rally during 2009.

That diminished negative and weakly positive correlation of returns is even more apparent when we look at the European corporate bonds (Figure 8). Investors were able to pile into these bonds at a very wide carry, especially after the June 2009 convergence of interest rates.

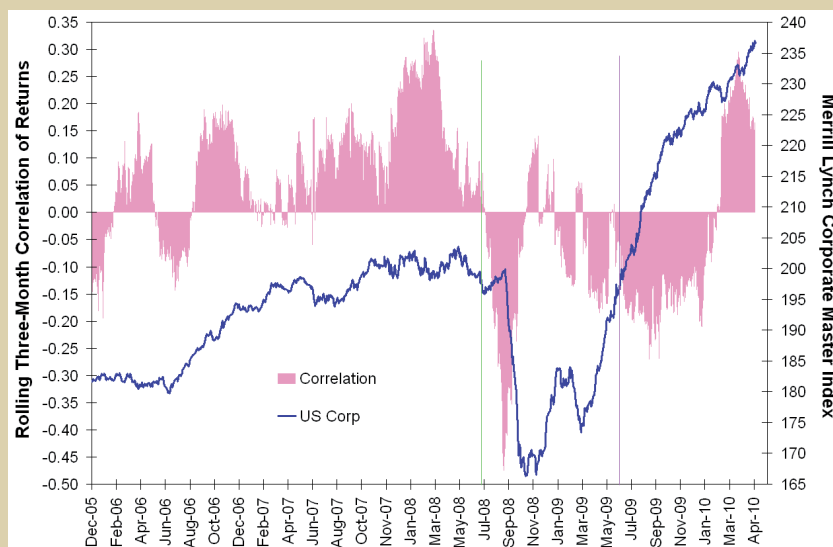
How significant were the shift dates of July 2008 and June 2009 in assessing the impact of the carry trades on fixed-income markets? If we run a series of regressions across the three different periods of the form $\ln(\text{bond}) = f(\ln(\text{carry}))$ and capture the residuals of each, the results become quite apparent. In Figure 8, each residual set is displayed with the pre-July 2008 period in turquoise, the revaluation period in green and the post-June 2009 period in magenta. The shift in regime did not exert a significant change on the relationship between the USD:CNY and U.S. government bonds. We can be confident the third period, the interest rate convergence period, was different from the combined previous two periods and the second period at 5.6 percent and 0.8-percent confidence only. The answer is markedly different for the U.S. corporate bonds; here the respective confidence levels are 99.8 percent and 95.4 percent. We can conclude the convergence of interest rates for the yuan carry trade affected risk-taking behavior positively and risk-averting behavior not at all.

Now let's shift to the CNY:EUR cases (Figure 9). Here the impact of interest-rate convergence for the third period with respect to the combined previous two periods was a highly significant 95.2

percent, and the impact between the third and second periods was 28.5 percent. The wide carry made European government bonds attractive.

What about the European corporate bonds? Here we should expect the very wide carry to produce highly sig-

FIGURE 6: THE USD:CNY CARRY AND U.S. CORPORATE BONDS



As investors dumped U.S. corporate bonds during the 2008 financial panic, the correlation turned sharply negative. When the returns on the USD:CNY started to flatten and investors moved back into corporate bonds in 2009, the correlation again turned negative until February 2010.

FIGURE 7: THE CNY:EUR CARRY AND PAN-EUROPEAN GOVERNMENT BONDS

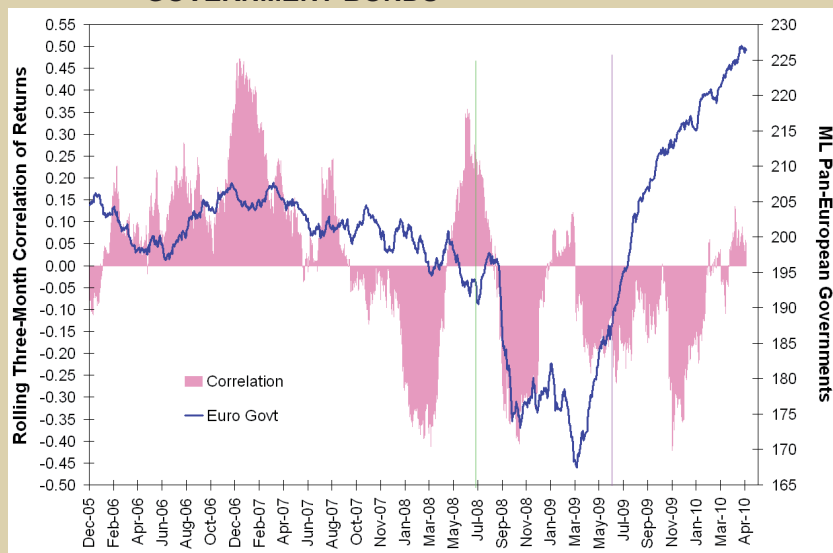
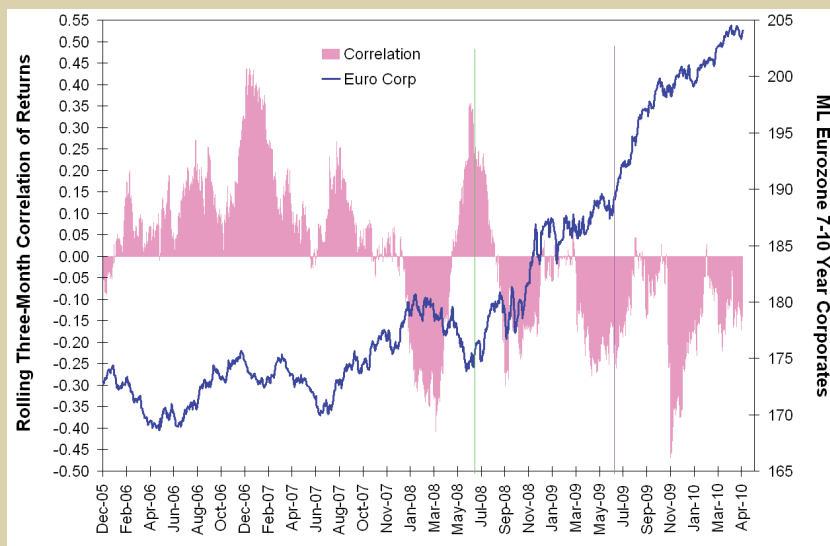


Figure 7 shows much less negative correlation of returns between the CNY:EUR and Pan-European government bonds than between the USD:CNY carry and U.S. government bonds.



FIGURE 8: THE CNY:EUR CARRY AND EUROZONE 7-10 YEAR CORPORATE BONDS



The diminished negative and weakly positive correlation of returns from Figure 7 is even more pronounced in the case of European corporate bonds.

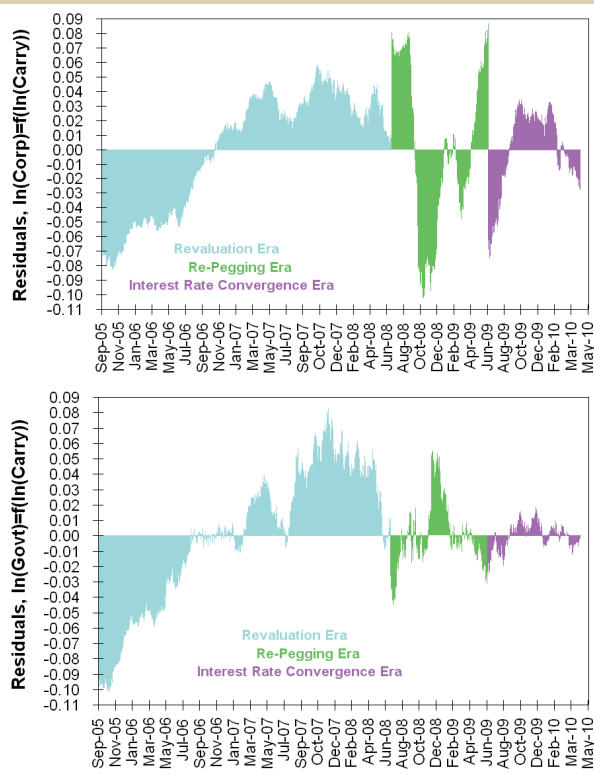
nificant changes in behavior, and this is exactly the case. The third period is different from both the combined first two periods and the second period alone at near-100 percent confidence.

We have to conclude on both the stock and the bond cases that the opening of the yuan carry trade after interest-rate convergence in June 2009 led to a liquidity-fueled bull market around the world.

Of course, liquidity, like tides, can flow out as well as in, and any ending of the interest-rate convergence accompanied by an increase in U.S. short-term interest rates (note to younger traders: U.S. short-term interest rates can and do rise) will pose an extreme threat to the global financial markets. ☹

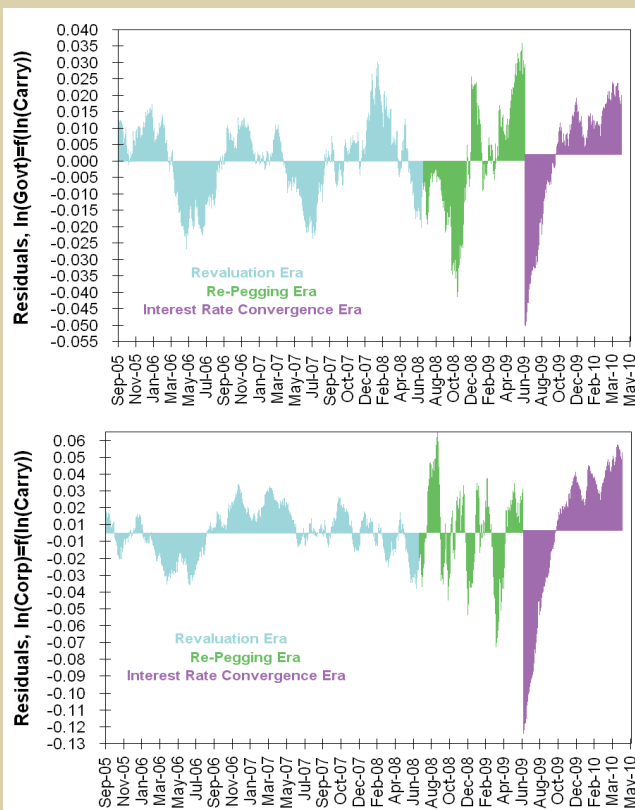
For information on the author, see p. 4.

FIGURE 9: U.S. CORPORATE AND GOVERNMENT BONDS



The shift in regime did not exert a significant change on the relationship between the USD:CNY and U.S. government bonds (bottom), but in the case of U.S. corporate bonds (top), the convergence of interest rates for the yuan carry trade affected risk-taking behavior positively and risk-averting behavior not at all.

FIGURE 10: EUROZONE CORPORATE AND GOVERNMENT BONDS



A wide carry made European government bonds (top) attractive, and produced highly significant changes in behavior in the case of European corporate bonds (bottom).



The information does NOT constitute trade signals. It is intended only to provide a brief synopsis of each market's liquidity, direction, and levels of momentum and volatility. See the legend for explanations of the different fields. Note: Average volume and open interest data includes both pit and side-by-side electronic contracts (where applicable).

| Market | Sym | Exch | Vol | OI | 10-day move / rank | 20-day move / rank | 60-day move / rank | Volatility ratio / rank |
|-------------------|-----|------|-------|-------|--------------------|--------------------|--------------------|-------------------------|
| EUR/USD | EC | CME | 377.4 | 241.4 | 0.33% / 10% | -0.26% / 2% | -8.85% / 78% | .06 / 0% |
| JPY/USD | JY | CME | 143.0 | 111.8 | 2.38% / 92% | 1.67% / 50% | 6.01% / 100% | .48 / 62% |
| AUD/USD | AD | CME | 125.2 | 82.8 | 1.53% / 31% | 2.45% / 75% | -5.15% / 64% | .14 / 0% |
| GBP/USD | BP | CME | 125.1 | 128.3 | 2.27% / 75% | 4.28% / 100% | -0.52% / 3% | .31 / 72% |
| CAD/USD | CD | CME | 95.7 | 94.3 | -0.41% / 0% | 1.56% / 45% | -2.37% / 73% | .33 / 35% |
| CHF/USD | SF | CME | 51.7 | 44.9 | 4.86% / 93% | 6.46% / 100% | -2.09% / 20% | .38 / 55% |
| MXN/USD | MP | CME | 26.5 | 68.7 | 0.13% / 6% | 1.00% / 22% | -3.13% / 97% | .19 / 13% |
| U.S. dollar index | DX | ICE | 23.8 | 31.0 | -1.01% / 30% | -0.86% / 58% | 5.74% / 58% | .09 / 0% |
| NZD/USD | NE | CME | 9.0 | 14.7 | 1.73% / 21% | 4.12% / 80% | 0.37% / 21% | .40 / 33% |
| E-Mini EUR/USD | ZE | CME | 6.3 | 4.9 | 0.33% / 10% | -0.26% / 2% | -8.85% / 78% | .06 / 0% |

Note: Average volume and open interest data includes both pit and side-by-side electronic contracts (where applicable). Price activity is based on pit-traded contracts.

LEGEND:

Volume: 30-day average daily volume, in thousands.

OI: 30-day open interest, in thousands.

10-day move: The percentage price move from the close 10 days ago to today's close.

20-day move: The percentage price move from the close 20 days ago to today's close.

60-day move: The percentage price move from the close 60 days ago to today's close.

The "% rank" fields for each time window (10-day moves, 20-day moves, etc.) show the percentile rank of the most recent move to a certain number of the previous moves of the same size and in the same direction. For example, the % rank for the 10-day move shows how the most recent 10-day move compares to the past twenty 10-day moves; for the 20-day move, it shows how the most recent 20-day move compares to the past sixty 20-day moves; for the 60-day move, it shows how the most recent 60-day move compares to the past one-hundred-twenty 60-day moves. A reading of 100% means the current reading is larger than all the past readings, while a reading of 0% means the current reading is smaller than the previous readings.

Volatility ratio/% rank: The ratio is the short-term volatility (10-day standard deviation of prices) divided by the long-term volatility (100-day standard deviation of prices). The % rank is the percentile rank of the volatility ratio over the past 60 days.

BarclayHedge Rankings for May 2010

**Top 10 currency traders managing more than \$10 million
as of 05/31/10, ranked by May 2010 return**

| | Trading Advisor | May Return | 2010 YTD Return | \$ Under Mgmt. (Millions) |
|-----|-----------------------------------|------------|-----------------|---------------------------|
| 1. | Dacharan Capital (High Exposure) | 26.81% | 42.49% | 10.0 |
| 2. | INSCH Capital Mgmt (Kintillo X3) | 12.81% | 3.59% | 54.3 |
| 3. | Friedberg Comm. Mgmt. (Curr.) | 11.91% | 33.41% | 78.7 |
| 4. | 24FX Management Ltd | 11.67% | 16.51% | 28.4 |
| 5. | Hathersage (Long Term Currency) | 9.67% | 6.23% | 425.0 |
| 6. | First Quadrant (Managed Currency) | 9.62% | 11.47% | 517.0 |
| 7. | Richmond Group (Gl. Currency) | 8.49% | 1.36% | 37.0 |
| 8. | IPM Global Currency Fund (C) | 7.89% | 8.75% | 168.0 |
| 9. | IKOS FX Fund | 6.82% | 17.43% | 684.0 |
| 10. | Hathersage (Daily Currency) | 4.11% | 5.10% | 100.0 |

**Top 10 currency traders managing less than \$10M & more than \$1M
as of 05/31/10, ranked by May 2010 return**

| | | | | |
|-----|--------------------------------------|--------|---------|-----|
| 1. | D2W Capital Mgmt (Radical Wealth) | 14.80% | 48.68% | 1.8 |
| 2. | Vaskas Capital Mgmt (Global FX) | 10.06% | -10.52% | 3.3 |
| 3. | Aurora Futures Corp (FX) | 5.20% | 3.88% | 2.5 |
| 4. | Blue Fin Capital (Managed Currency) | 3.38% | 3.29% | 3.4 |
| 5. | Capricorn Advisory Mgmt (FXG10) | 2.37% | 3.80% | 8.6 |
| 6. | Millennium Global Currency (USD) | 2.05% | -0.97% | 2.4 |
| 7. | Analytic Invest. Mgmt (ASC Enhanced) | 1.29% | 0.81% | 4.9 |
| 8. | M2 Global Mgmt (2.5X) | 0.62% | 3.54% | 2.5 |
| 9. | Quant Trading (FX Quant 11) | 0.58% | -3.00% | 4.5 |
| 10. | Trident Asset Mgmt. (Gl. Currency) | 0.38% | 0.60% | 7.0 |

*Based on estimates of the composite of all accounts or the fully funded subset method.
Does not reflect the performance of any single account.*

PAST RESULTS ARE NOT NECESSARILY INDICATIVE OF FUTURE PERFORMANCE.



CURRENCIES (vs. U.S. DOLLAR)

| Rank | Currency | June 25 price vs. U.S. dollar | 1-month gain/loss | 3-month gain/loss | 6-month gain/loss | 52-week high | 52-week low | Previous |
|------|--------------------|-------------------------------|-------------------|-------------------|-------------------|--------------|-------------|----------|
| 1 | New Zealand dollar | 0.708365 | 5.12% | 0.83% | 1.05% | 0.7635 | 0.6194 | 13 |
| 2 | Swiss franc | 0.90633 | 4.83% | -3.17% | -5.25% | 1.0087 | 0.853 | 14 |
| 3 | Australian dollar | 0.86945 | 4.71% | -4.63% | -0.89% | 0.9405 | 0.7723 | 17 |
| 4 | British pound | 1.49667 | 3.69% | 0.25% | -6.21% | 1.7042 | 1.4235 | 10 |
| 5 | Brazilian real | 0.5595 | 3.68% | -0.06% | -0.80% | 0.5882 | 0.4844 | 7 |
| 6 | South African rand | 0.13175 | 3.20% | -2.90% | 1.21% | 0.1389 | 0.12 | 9 |
| 7 | Canadian dollar | 0.960185 | 1.67% | -1.85% | 1.17% | 1.0068 | 0.8527 | 11 |
| 8 | Swedish krona | 0.12871 | 1.19% | -6.66% | -5.92% | 0.148 | 0.1227 | 16 |
| 9 | Singapore dollar | 0.71888 | 1.11% | 0.98% | 1.34% | 0.7326 | 0.6817 | 6 |
| 10 | Japanese yen | 0.01117 | 0.90% | 2.24% | 2.38% | 0.01179 | 0.01023 | 1 |
| 11 | Indian rupee | 0.02155 | 0.89% | -2.13% | 1.08% | 0.02263 | 0.01988 | 8 |
| 12 | Chinese yuan | 0.14699 | 0.38% | 0.35% | 0.37% | 0.14760 | 0.1458 | 2 |
| 13 | Hong Kong dollar | 0.128565 | 0.30% | -0.22% | -0.30% | 0.129 | 0.1281 | 3 |
| 14 | Thai baht | 0.030875 | 0.18% | 0.05% | 2.88% | 0.03157 | 0.0289 | 4 |
| 15 | Taiwanese dollar | 0.031215 | 0.18% | -0.59% | 1.02% | 0.03201 | 0.03007 | 5 |
| 16 | Russian ruble | 0.03219 | -0.12% | -4.54% | -2.38% | 0.03497 | 0.03007 | 12 |
| 17 | Euro | 1.231785 | -0.82% | -7.83% | -13.73% | 1.5144 | 1.1891 | 15 |

GLOBAL CENTRAL BANK LENDING RATES

| Country | Interest Rate | Rate | Last change | Dec-09 | Jun-09 |
|---------------|------------------------|--------|-----------------|--------|--------|
| United States | Fed funds rate | 0-0.25 | 0.5 (Dec. 08) | 0-0.25 | 0-0.25 |
| Japan | Overnight call rate | 0.1 | 0.2 (Dec. 08) | 0.1 | 0.1 |
| Eurozone | Refi rate | 1 | 0.25 (May 09) | 1 | 1 |
| England | Repo rate | 0.5 | 0.5 (March 09) | 0.5 | 0.5 |
| Canada | Overnight funding rate | 0.5 | 0.25 (June 10) | 0.25 | 0.25 |
| Switzerland | 3-month Swiss Libor | 0.25 | 0.25 (March 09) | 0.25 | 0.25 |
| Australia | Cash rate | 4.5 | 0.25 (May 10) | 3.75 | 3 |
| New Zealand | Cash rate | 2.75 | 0.25 (June 10) | 2.5 | 2.5 |
| Brazil | Selic rate | 9.5 | 0.75 (April 10) | 8.75 | 9.25 |
| Korea | Overnight call rate | 2 | 0.5 (Feb. 09) | 2 | 2 |
| Taiwan | Discount rate | 1.25 | 0.25 (Feb. 09) | 1.25 | 1.25 |
| India | Repo rate | 5 | 0.25 (April 10) | 4.75 | 4.75 |
| South Africa | Repurchase rate | 6.5 | 0.5 (Mar. 10) | 7 | 7.5 |

GLOBAL STOCK INDICES

| | Country | Index | June 25 | 1-month gain/loss | 3-month gain/loss | 6-month gain loss | 52-week high | 52-week low | Previous |
|----|--------------|--------------------|-----------|-------------------|-------------------|-------------------|--------------|-------------|----------|
| 1 | India | BSE 30 | 17,574.53 | 9.69% | 0.09% | 1.23% | 18,047.90 | 13,220.00 | 3 |
| 2 | Brazil | Bovespa | 64,824.00 | 9.53% | -5.29% | -4.53% | 71,989.00 | 48,262.00 | 12 |
| 3 | Hong Kong | Hang Seng | 20,690.79 | 8.98% | -0.42% | -3.84% | 23,099.60 | 17,186.00 | 8 |
| 4 | Italy | FTSE MIB | 19,961.74 | 8.59% | -13.34% | -14.34% | 24,559 | 17,626 | 15 |
| 5 | Singapore | Straits Times | 2,851.64 | 7.58% | -1.27% | 0.49% | 3,037.97 | 2,226.10 | 7 |
| 6 | Germany | Xetra Dax | 6,070.60 | 7.06% | -1.02% | 1.13% | 6,341.52 | 4,524.01 | 5 |
| 7 | Mexico | IPC | 32,607.13 | 6.44% | -1.68% | 0.18% | 34,223.90 | 23,033.90 | 2 |
| 8 | France | CAC 40 | 3,519.73 | 5.66% | -12.02% | -10.04% | 4,088.18 | 2,957.83 | 14 |
| 9 | South Africa | FTSE/JSE All Share | 27,258.07 | 4.12% | -4.54% | -1.17% | 29,565.10 | 21,665.90 | 4 |
| 10 | Australia | All ordinaries | 4,439.40 | 3.57% | -9.33% | -7.58% | 5,048.60 | 3,710.10 | 9 |
| 11 | Switzerland | Swiss Market | 6,275.40 | 3.02% | -8.98% | -4.63% | 6,990.70 | 5,204.80 | 6 |
| 12 | Japan | Nikkei 225 | 9,737.48 | 2.93% | -10.08% | -7.59% | 11,408.20 | 9,050.33 | 13 |
| 13 | UK | FTSE 100 | 5,046.50 | 2.14% | -11.89% | -6.59% | 5,833.70 | 4,096.10 | 11 |
| 14 | Canada | S&P/TSX composite | 11,707.85 | 1.65% | -2.09% | -0.40% | 12,321.80 | 9,535.50 | 1 |
| 15 | U.S. | S&P 500 | 1,076.76 | 0.00% | -7.63% | -4.41% | 1,219.80 | 869.32 | 10 |

NON-U.S. DOLLAR FOREX CROSS RATES

| Rank | Currency pair | Symbol | June 25 | 1-month gain/loss | 3-month gain/loss | 6-month gain loss | 52-week high | 52-week low | Previous |
|------|-------------------------|---------|----------|-------------------|-------------------|-------------------|--------------|-------------|----------|
| 1 | New Zeal \$ / Yen | NZD/JPY | 63.425 | 4.21% | -1.38% | -1.32% | 69.5573 | 58.1679 | 18 |
| 2 | Franco / Yen | CHF/JPY | 81.15 | 3.94% | -5.28% | -7.47% | 91.549 | 76.36 | 19 |
| 3 | Aussie \$ / Yen | AUD/JPY | 77.85 | 3.81% | -6.69% | -3.21% | 88.048 | 46.508 | 21 |
| 4 | Franco / Canada \$ | CHF/CAD | 0.943915 | 3.12% | -1.34% | -6.35% | 1.0724 | 0.8989 | 6 |
| 5 | Aussie \$ / Canada \$ | AUD/CAD | 0.90551 | 2.99% | -2.83% | -2.04% | 0.9895 | 0.8643 | 14 |
| 6 | Pound / Yen | GBP/JPY | 134.05 | 2.81% | -1.87% | -8.39% | 163.057 | 127.065 | 16 |
| 7 | Pound / Canada \$ | GBP/CAD | 1.558735 | 1.99% | 2.14% | -7.30% | 1.9173 | 1.4894 | 5 |
| 8 | Aussie \$ / Real | AUD/BRL | 1.55399 | 0.96% | -4.58% | -0.09% | 1.6978 | 1.5256 | 15 |
| 9 | Canada \$ / Yen | CAD/JPY | 85.97 | 0.79% | -4.00% | -1.21% | 94.1955 | 79.6163 | 17 |
| 10 | Aussie \$ / Franco | AUD/CHF | 0.959315 | -0.12% | -1.51% | 4.60% | 1.0079 | 0.8457 | 12 |
| 11 | Aussie \$ / New Zeal \$ | AUD/NZD | 1.22737 | -0.39% | -5.41% | -1.93% | 1.3233 | 1.1931 | 13 |
| 12 | Pound / Aussie \$ | GBP/AUD | 1.721395 | -0.97% | 5.12% | -5.37% | 2.0859 | 1.6328 | 2 |
| 13 | Pound / Franco | GBP/CHF | 1.65136 | -1.09% | 3.52% | -1.01% | 1.8112 | 1.5778 | 4 |
| 14 | Euro / Yen | EUR/JPY | 110.29 | -1.67% | -9.84% | -15.75% | 138.715 | 108.31 | 20 |
| 15 | Canada \$ / Yen | CAD/BRL | 1.716155 | -1.98% | -1.79% | 1.98% | 1.8244 | 1.6003 | 8 |
| 16 | Euro / Canada \$ | EUR/CAD | 1.282865 | -2.45% | -6.09% | -14.73% | 1.63 | 1.2502 | 9 |
| 17 | Yen / Real | JPY/BRL | 0.01996 | -2.75% | 2.28% | 3.23% | 0.02227 | 0.01838 | 1 |
| 18 | Euro / Pound | EUR/GBP | 0.823015 | -4.35% | -8.05% | -8.02% | 0.9411 | 0.8179 | 10 |
| 19 | Euro / Real | EUR/BRL | 2.201595 | -4.38% | -7.77% | -13.04% | 2.8724 | 2.1772 | 11 |
| 20 | Euro / Aussie \$ | EUR/AUD | 1.41675 | -5.29% | -3.35% | -12.96% | 1.8005 | 1.377 | 3 |
| 21 | Euro / Franco | EUR/CHF | 1.359095 | -5.40% | -4.81% | -8.95% | 1.5383 | 1.3542 | 7 |

ACCOUNT BALANCE

| Rank | Country | 2008 | Ratio* | 2007 | 2009+ |
|------|--------------------------|----------|--------|----------|----------|
| 1 | Singapore | 36.188 | 19.222 | 47.311 | 33.838 |
| 2 | Norway | 83.825 | 18.59 | 54.678 | 52.901 |
| 3 | Hong Kong SAR | 29.296 | 13.618 | 25.529 | 23.373 |
| 4 | Sweden | 37.279 | 7.783 | 39.054 | 25.781 |
| 5 | Germany | 245.722 | 6.69 | 253.756 | 160.627 |
| 6 | Taiwan Province of China | 25.122 | 6.239 | 32.975 | 42.572 |
| 7 | Netherlands | 41.978 | 4.787 | 67.589 | 41.652 |
| 8 | Japan | 157.079 | 3.214 | 210.967 | 141.656 |
| 9 | Switzerland | 11.947 | 2.388 | 43.531 | 43.102 |
| 10 | Canada | 7.606 | 0.507 | 14.53 | -36.132 |
| 11 | Korea | -5.776 | -0.62 | 5.876 | 42.668 |
| 12 | United Kingdom | -40.725 | -1.517 | -75.483 | -28.838 |
| 13 | Belgium | -12.855 | -2.539 | 9.956 | -1.254 |
| 14 | Czech Republic | -6.669 | -3.086 | -5.483 | -1.942 |
| 15 | Italy | -78.874 | -3.418 | -51.691 | -71.27 |
| 16 | Australia | -46.683 | -4.406 | -57.552 | -40.941 |
| 17 | United States | -706.068 | -4.889 | -726.572 | -417.999 |
| 18 | Ireland | -13.886 | -5.189 | -13.876 | -6.705 |
| 19 | Spain | -153.665 | -9.592 | -144.435 | -74.136 |

Totals in billions of U.S. dollars

*Account balance as percent of GDP
+Estimate

Source: *International Monetary Fund, World Economic Outlook Database*, April 2010.

GLOBAL BOND RATES

| Rank | Country | Rate | June 25 | 1 month | 3 months | 6 months | High | Low | Previous |
|------|-----------|-----------------|---------|---------|----------|----------|--------|--------|----------|
| 1 | U.S. | 10-year T-note | 121.48 | 4.20% | 3.33% | 4.98% | 122.56 | 114.78 | 3 |
| 2 | Germany | BUND | 128.98 | 3.97% | 4.97% | 5.82% | 129.93 | 119.85 | 1 |
| 3 | Japan | Government Bond | 141.08 | 0.11% | 1.89% | 0.94% | 143.28 | 136.94 | 5 |
| 4 | Australia | 10-year bonds | 94.73 | -0.01% | 0.54% | 0.45% | 94.87 | 94.09 | 4 |
| 5 | UK | Short sterling | 99.16 | -0.06% | -0.14% | -0.15% | 99.52 | 98.90 | 2 |



| Unemployment | | Period | Release date | Rate | Change | 1-year change | Next release |
|---------------------|-----------|------------|--------------|------|--------|---------------|--------------|
| AMERICAS | Argentina | Q1 | 5/21 | 8.3% | -0.1% | -0.1% | 8/23 |
| | Brazil | May | 6/24 | 7.5% | 0.2% | -1.3% | 7/22 |
| | Canada | May | 6/4 | 8.1% | 0.0% | -0.4% | 7/9 |
| EUROPE | France | Q1 | 6/3 | 9.5% | 0.0% | 0.8% | 9/2 |
| | Germany | May | 6/30 | 7.0% | -0.1% | -0.6% | 7/29 |
| | UK | Feb.-April | 6/16 | 7.9% | 0.1% | 2.6% | 7/14 |
| ASIA and S. PACIFIC | Australia | May | 6/16 | 5.3% | 0.1% | -0.2% | 7/8 |
| | Hong Kong | March-May | 6/17 | 4.6% | 0.2% | -0.7% | 7/20 |
| | India | May | 6/29 | 5.2% | 0.1% | 0.1% | 7/30 |
| | Japan | Q1 | 4/30 | 2.2% | -0.1% | -1.0% | 7/30 |
| | Singapore | Q1 | 4/30 | 2.2% | -0.1% | -0.1% | 7/30 |

| GDP | | Period | Release date | Change | 1-year change | Next release |
|---------------------|-----------|--------|--------------|--------|---------------|--------------|
| AMERICAS | Argentina | Q1 | 6/18 | -0.6% | 14.8% | 9/17 |
| | Brazil | Q1 | 6/8 | -2.7% | 15.2% | 9/3 |
| | Canada | Q1 | 5/31 | 2.5% | 5.6% | 8/31 |
| EUROPE | France | Q1 | 5/12 | 0.4% | 0.7% | 8/13 |
| | Germany | Q1 | 5/12 | 0.6% | 3.2% | 8/13 |
| | UK | Q4 | 3/30 | 1.2% | -1.7% | 7/12 |
| AFRICA | S. Africa | Q1 | 5/24 | 2.2% | -4.7% | 8/24 |
| ASIA and S. PACIFIC | Australia | Q1 | 6/2 | 0.6% | 2.7% | 9/1 |
| | Hong Kong | Q1 | 5/14 | -6.5% | 9.2% | 8/13 |
| | India | Q1 | 5/31 | 19.1% | 12.2% | 8/31 |
| | Japan | Q1 | 5/20 | 1.2% | 4.9% | 8/16 |
| | Singapore | Q1 | 5/21 | 4.1% | 15.5% | NLT 8/27 |

| CPI | | Period | Release date | Change | 1-year change | Next release |
|---------------------|-----------|--------|--------------|--------|---------------|--------------|
| AMERICAS | Argentina | May | 6/11 | -0.8% | 10.7% | 7/14 |
| | Brazil | May | 6/9 | 0.4% | 5.2% | 7/7 |
| | Canada | May | 6/22 | 0.3% | 1.4% | 7/23 |
| EUROPE | France | May | 6/11 | 0.1% | 1.6% | 7/13 |
| | Germany | May | 6/10 | 0.1% | 1.2% | 7/9 |
| | UK | May | 6/15 | 0.2% | 3.4% | 7/13 |
| AFRICA | S. Africa | May | 6/23 | 0.2% | 4.6% | 7/28 |
| ASIA and S. PACIFIC | Australia | Q1 | 4/28 | 0.9% | 2.9% | 7/28 |
| | Hong Kong | May | 6/22 | 0.3% | 2.5% | 7/22 |
| | India | May | 6/30 | 1.2% | 13.9% | 7/30 |
| | Japan | May | 6/25 | 0.1% | -0.9% | 7/30 |
| | Singapore | May | 6/23 | 0.6% | 3.2% | 7/23 |

| PPI | | Period | Release date | Change | 1-year change | Next release |
|---------------------|-----------|--------|--------------|--------|---------------|--------------|
| AMERICAS | Argentina | May | 6/11 | 1.0% | 15.2% | 9/3 |
| | Brazil | May | 6/9 | 2.2% | 0.5% | 7/7 |
| | Canada | May | 6/29 | 0.3% | 1.4% | 7/29 |
| EUROPE | France | May | 7/1 | 0.1% | 3.8% | 7/30 |
| | Germany | May | 6/24 | 0.3% | 0.9% | 7/20 |
| | UK | May | 6/11 | 0.3% | 5.7% | 7/9 |
| AFRICA | S. Africa | May | 6/24 | 0.1% | 6.8% | 7/29 |
| ASIA and S. PACIFIC | Australia | Q1 | 4/27 | 1.0% | -0.1% | 7/26 |
| | Hong Kong | Q2 | 6/14 | 1.7% | 4.0% | 9/13 |
| | India | May | 6/10 | 1.7% | 10.2% | 7/14 |
| | Japan | May | 6/10 | 0.1% | 0.4% | 7/12 |
| | Singapore | May | 6/29 | -2.0% | 7.9% | 7/29 |

As of June, 30 2010 LEGEND: Change: Change from previous report release. NLT: No later than. Rate: Unemployment rate.



GLOBAL ECONOMIC CALENDAR: JULY

CPI: Consumer price index
 ECB: European Central Bank
 FDD (first delivery day): The first day on which delivery of a commodity in fulfillment of a futures contract can take place.
 FND (first notice day): Also known as first intent day, this is the first day on which a clearinghouse can give notice to a buyer of a futures contract that it intends to deliver a commodity in fulfillment of a futures contract. The clearinghouse also informs the seller.
 FOMC: Federal Open Market Committee
 GDP: Gross domestic product
 ISM: Institute for supply management
 LTD (last trading day): The final day trading can take place in a futures or options contract.
 PMI: Purchasing managers index
 PPI: Producer price index

| Economic release (U.S.) | Release time (ET) |
|-------------------------|-------------------|
| GDP | 8:30 a.m. |
| CPI | 8:30 a.m. |
| ECI | 8:30 a.m. |
| PPI | 8:30 a.m. |
| ISM | 10:00 a.m. |
| Unemployment | 8:30 a.m. |
| Personal income | 8:30 a.m. |
| Durable goods | 8:30 a.m. |
| Retail sales | 8:30 a.m. |
| Trade balance | 8:30 a.m. |
| Leading indicators | 10:00 a.m. |

July 2010

| | | | | | | |
|----|----|----|----|----|----|----|
| 30 | 31 | 1 | 2 | 3 | 4 | 5 |
| 6 | 7 | 8 | 9 | 10 | 11 | 12 |
| 13 | 14 | 15 | 16 | 17 | 18 | 19 |
| 20 | 21 | 22 | 23 | 24 | 25 | 26 |
| 27 | 28 | 29 | 30 | 31 | 1 | 2 |

The information on this page is subject to change. Currency Trader is not responsible for the accuracy of calendar dates beyond press time.

July

- 1** France: May PPI
- 2** U.S.: June employment report
- 3**
- 4**
- 5**
- 6** U.S.: June ISM report
- 7** Brazil: June CPI and PPI
- 8** Australia: June employment report
Mexico: June 30 CPI and June PPI
UK: Bank of England interest-rate announcement
ECB: Governing council interest-rate announcement
- 9** Canada: June employment report-
Germany: June CPI
UK: June PPI
- 10**
- 11**
- 12** Japan: June PPI
- 13** U.S.: May trade balance
France: June CPI
UK: June CPI
- 14** U.S.: June retail sales
India: June PPI
Japan: Bank of Japan interest-rate announcement
UK: May employment report
- 15** U.S.: June PPI
- 16** U.S.: June CPI
- 17**
- 18**
- 19**
- 20** U.S.: June housing starts
Canada: Bank of Canada interest-rate announcement
Germany: June PPI
Hong Kong: April-June employment report

21

- 22** U.S.: June leading indicators
Brazil: June employment report
Hong Kong: June CPI
Mexico: July 15 CPI
- 23** Canada: June CPI
Mexico: June employment report
- 24**
- 25**
- 26** Australia: Q2 PPI
- 27**
- 28** U.S.: Fed beige book and June durable orders
Australia: Q2 CPI
South Africa: June CPI
- 29** Canada: June PPI
France: June PPI
Germany: June employment report
South Africa: June PPI
- 30** U.S.: Q2 GDP (advance) and ECI
Japan: June employment report and CPI
- 31**

August

- 1**
- 2** U.S.: July ISM report
- 3** U.S.: June personal income
- 4**
- 5** UK: Bank of England interest-rate announcement
ECB: Governing council interest-rate announcement
- 6** U.S.: July employment report
UK: July PPI



EVENTS

Event: The MoneyShow San Francisco 2010

Show focus: Green investing

Date: Aug. 19-21

Location: San Francisco Marriott

For more information: Go to www.moneyshow.com

and click on Events > The World MoneyShows

Event: The CBOE Options Intensive

Dates: Aug. 26, Oct. 21

Location: Chicago

For more information: Go to www.cboe.com and click on Education > Seminars

Event: Fifth annual free Paris Trading Show

Date: Sept. 17-18

Location: Paris

For more information: www.salonAT.com

Event: Security Traders Association 77th annual conference and business meeting

Date: Sept. 22-25

Location: Washington D.C.

For more information: www.securitytraders.org

Event: CBOE Real Trading with Dan Sheridan

Date: Sept. 23

Location: Chicago

For more information: Go to www.cboe.com and click on Education > Seminars

Event: The Forex, Futures & ETFs Expo Las Vegas 2010

Date: Sept. 23-25

Location: Caesars Palace, Las Vegas

For more information: Go to www.moneyshow.com

Event: SEC Customer Protection Rule one-day seminar

Date: Sept. 29

Location: Bayards, New York City

For more information: www.fmwonline.com

Event: The Third Kuwait Traders Expo

Date: Oct. 13-14

Location: J.W. Marriott, Kuwait City

For more information: www.metradersexpo.com

Event: The First Qatar Traders Expo

Date: Oct. 17-18

Location: J.W. Marriott, Qatar

For more information: www.metradersexpo.com

Event: CME Group's Global Financial Leadership Conference

Date: Oct. 18-20

Location: Ritz-Carlton Beach Resort, Naples, Fla.

For more information: www.gflc.com

Event: FXstreet.com International Traders Conference

Date: Oct. 20-22

Location: Barcelona, Spain

For more information: www.traders-conference.com

Event: 2010 Sydney Trading & Investing Seminars & Expo

Date: Oct. 29-30

Location: Sydney

For more information: www.tradingandinvestingexpo.com.au

Event: Las Vegas Traders Expo

Date: Nov. 17-20

Location: Caesars Palace, Las Vegas

For more information: Go to www.moneyshow.com



KEY CONCEPTS

Carry trades involve buying (or lending) a currency with a high interest rate and selling (or borrowing) a currency with a low interest rate. Traders looking to “earn carry” will buy a high-yielding currency while simultaneously selling a low-yielding currency.📌



Interactive Brokers (www.interactivebrokers.com) has **enhanced its ScaleTrader algorithm to include pairs trading**, enabling clients to trade the spread between any two securities. Investors typically buy the shares of one company and sell those in another when the distance between the two prices moves towards an extreme value and away from an observed relationship. The Interactive Brokers ScaleTrader algorithm allows clients to create conditions under which a long position in one stock is built while simultaneously creating an offsetting short position in the other. The ScaleTrader is named because investors can “scale-in” to market weakness by setting orders to buy as the market moves lower. Similarly, sell orders can be “scaled” into when a market is rising. The ScaleTrader algorithm can be programmed to buy the spread and subsequently take profit by selling the spread if the difference reaches predetermined levels set by the user. Orders can be entered using net share price differences or by using credit or debit ratios. Investors can set their own parameters to determine the starting number of shares and maximum size of the position they wish to create, and must determine the distance between each incremental buying price. In addition the user may vary the increment over time. The ScaleTrader Pair Trading algorithm is available to all Interactive Brokers customers through its Trader Workstation trading software at no additional charge.

E*TRADE Securities has launched an **open application programming interface (“Open API”)** for third-party and independent software developers to integrate seamlessly with E*TRADE’s investing platform. Through the new Open API, customers will have access to technical information and documentation, reference guides, and other resources to help integrate external applications and programs with E*TRADE’s investing platform. E*TRADE also announced plans to integrate with third-party vendors, including CoolTrade and AbleSys, offering investors seamless integration between E*TRADE’s trading technology, and the market research and stock trading tools of external programs.

CQG, Inc. (www.cqg.com) has **expanded its fixed-income news coverage** by adding a new product, MNI Fixed Income Select, from real-time news agency Market News International (MNI). MNI Fixed Income Select will offer original running commentary on global fixed-income markets, presented in bullet-point format. MNI’s reporting and commentary includes live coverage from Chicago’s futures exchanges.

The **Bollinger on Bollinger Bands Web site** (www.BollingerOnBollingerBands.com) finished a **complete upgrade in late June**. New features include John Bollinger’s latest work and Bollinger Band tools unique to the Web site: BB Impulse, which measures price moves as a function of the width of the Bollinger Bands; Percent

Bandwidth, which is a normalized and more intuitive view of BandWidth; Bandwidth Delta, which charts the rate of change in BandWidth. Also included are three indicators developed by Jim Alpher: Alpher Conviction, which is a divergence indicator that compares the count of plus and minus days vs. actual gains; Alpher Expectation, which is a supply-demand chart with specific buy and sell rules; Alpher Psychology, which is the central component of the Alpher Expectation chart that is more sensitive and shorter-term in outlook. New Chart Overlays include: the Price Magnet, which is an overly that plots a series of points in and around the price structure that provide an indication of potential price movement; Bollinger Envelopes, which are a variation on Bollinger Bands that focus on the extremes of price action. Bollinger Bands are centered on a moving average (usually of the closing price), while Bollinger Envelopes are anchored by the extremes (highs and the lows).

Worden Brothers Inc., (www.wordenbrothers.com) provider of stock-market analysis tools, including FreeStockCharts.com, announced its technological suite of real-time charts was chosen by QUODD Financial Information Services to be used in its full-featured platform. Worden’s Web-based widgets deliver streaming, real-time stock data to any browser and can be crafted to fit into many applications. Worden’s retail products include TeleChart, StockFinder, and FreeStockCharts.com, as well as educational materials published in books, newsletters, videos and live nationwide training classes.

The Active Trader Magazine Group (www.activetradermag.com) has launched a new digital magazine, *Managed Futures Today*, dedicated to the professionally managed futures industry. This free magazine, which will initially be published quarterly, covers investing and trading concepts, risk management, and industry news for investment advisors and individual investors seeking to integrate managed futures into their long-term, diversified investment portfolios. To see the current issue, go to www.managedfuturestodaymag.com.

Alpari (US), a leading provider of online forex trading services and technology, has announced the launch of a free live audio market commentary service for its clients, launched in conjunction with Alpari (UK) and its subsidiaries. “Alpari Squawk” is a dedicated audio stream that covers major market-moving stories throughout the trading day, including coverage of economic news and figures as they are released, such as fixed-income, interest rates, equities, FX and commodities. First Call, a team of professional market analysts, manages the service. Alpari clients are able to access Squawk via the Alpari Web site: <https://my.alpari-us.com/en/squawk/> from 7:15 a.m.-4:15 p.m. ET, Monday through Friday. ☎



Testing out a scalp setup.

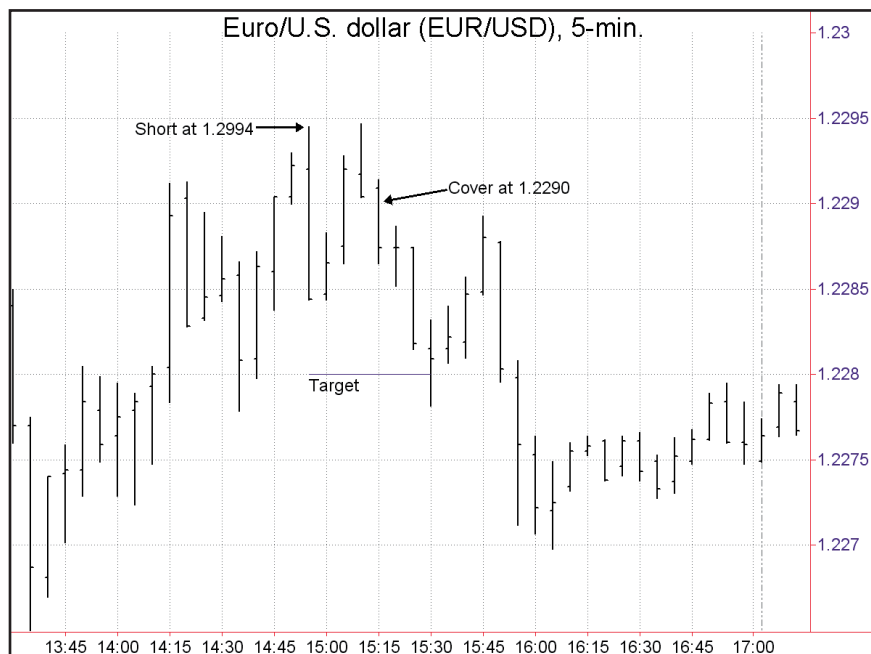
TRADE

Date: Monday, June 28, 2010 (1:50 p.m.).**Entry:** Short the Euro/U.S. dollar pair (EUR/USD) at 1.2294.

Reason for trade/setup: The trade was based on one of the signals from “Five-minute forex scalp.” Monitoring different variations of the two setups presented a short opportunity around 1:50 p.m. CT. After two consecutive five-minute bars that closed in the upper 25 percent of their ranges, a limit order was entered .0004 above the high of the second bar. The next five-minute bar extended only 3 pips higher, so the trade was executed at the next bar. We look for a quick 10-pip profit, and will risk 10 pips to the upside.

Initial stop: 1.2304.**Initial target:** 1.2280.

RESULT

Exit: 1.2290.**Profit/loss:** .0004

Source: TradeStation

Outcome: After an initial drop to 1.2285, the market rebounded to the entry price over the next 15 minutes. We simply decided to cover at 1.2290 because this was an “exploratory” trade designed to test out the pattern setup, and the more favorable patterns we analyzed often appeared to hit their targets within the first few bars (maxing out around six or seven bars after entry).

Price dropped to the target three bars later and, after one more upside bounce, fell another 10 pips by 3 p.m. Despite not capitalizing fully on the trade, it was gratifying to see this pattern perform as expected in real-time, as did two more setups the next morning. 📌

Note: Initial trade targets are typically based on things such as the historical performance of a price pattern or a trading system signal. However, because individual trades are dictated by immediate circumstances, price targets are flexible and are often used as points at which to liquidate a portion of a trade to reduce exposure. As a result, initial (pre-trade) reward-risk ratios are conjectural by nature.

Trade Summary

| Date | Currency pair | Entry price | Initial stop | Initial target | IRR | Exit | Date | P/L | | LOP | LOL | Trade length |
|---------|---------------|-------------|--------------|----------------|------|--------|---------|-------|---|-------|-----|--------------|
| | | | | | | | | point | % | | | |
| 6/28/10 | EUR/USD | 1.2294 | 1.2304 | 1.2280 | 1.00 | 1.2288 | 6/28/10 | .0004 | - | .0010 | - | 25 min |

Legend: IRR: initial reward/risk ratio (initial target amount/initial stop amount). LOP: largest open profit (maximum available profit during lifetime of trade). LOL: largest open loss (maximum potential loss during life of trade).