Currency traders prepare for wild ride

Derivatives
John Wasiliev

Foreign exchange traders will be keeping a close eye on the Australian dollar against the US currency today after the greenback gained ground because of encouraging news on the United States employment front.

While commentators are still suggesting the Australian dollar can reach parity against the US dollar over the next six months, traders will need to watch for bouts of volatility.

As some traders risk $US1000 ($1090) on every US1¢ currency move, volatile currency trading needs to be carefully managed.

Although contracts for difference traders have been shorting the US dollar for much of this year, encouraging American economic news last week made some go long in the US currency against not just the Australian dollar, but other major currencies as well.

CFD provider GFT currency strategist Kathy Lien said there were signs the Australian dollar, which had been the global currency market's high flier for much of this year, was starting to lose steam.

Ms Lien said that given most currency trading was driven by technical indicators, traders would be closely watching to see if the dollar could hold above its 50-day moving average of US91.2¢ this week.

It closed just above this average at US91.47¢ last week, nearly US2¢ below the week's high of US93.22¢, but higher than the US91.08¢ low.

Ms Lien said if the dollar breaches the 50-day support level, traders would watch for another move that would test the US90¢ level. A rally above last week's US93.22¢ high would be seen as a positive move. Although a lot of currency action is technically driven, traders also watch for the reaction to any fundamental news, such as the better than expected US employment report. This week a report on US consumer credit activity and November retail sales news could influence the market.

In other derivatives action, CFD provider AxisODL noted reduced interest in Australian share index trading among its clients, which spokesman Quinn Perrott attributed to jitters related to the debt problems in Dubai.

Many traders took profits last week from positions held in leading resource and banking shares.

But CMC Markets believes traders are still positive about the Australian market. Its clients were maintaining long CFD positions in the S&P/ASX 200 Index while at the same time holding short positions in the Japanese, American and UK markets.

In commodity CFD trading, Mr Perrott said gold traders took profits late last week on expectations the current gold rally could be over. More falls were suggested by an absence of gold derivative buying orders until the price fell back to the $US1050 to $US1100 range.

Solid base missing in stock rallies

David Coe

Critical warning signs lurk beneath the seemingly unstoppable rallies in the Australian and US stockmarkets.

As the major indices climb, the base on which they are climbing is narrowing. Fewer and fewer stocks are making new highs, which in turn makes the rises less sustainable, according to some technical analysts.

Steven Hochberg, editor of the US-based *Elliott Wave Financial Forecast*, told his subscribers this week: ''The bluest of blue chips are holding up while entire sectors of the market lag.''

In Australia, only the materials sector is substantially above highs hit in October and that is dominated by just three stocks — BHP Billiton, Rio Tinto and Newcrest, which account for 69 per cent of the sector.

Of the other sectors, companies that sell consumer staple goods are only nudging the October highs. All the rest are well below those highs.

The benchmark S&P/ASX 200 Index hit a high for the year of 4859.90 points on October 15, but has since eased back on concerns that the stockmarket has outpaced prospects for the economy and company earnings.

The S&P/ASX 200 has rallied close to 50 per cent since March and is set to post a calendar year gain of more than 25 per cent.

> **The Santa rally is early and it won't last.**
> David Hunt, technical analyst

Equally worrying for stockmarket bears is the bullishness of small traders, who as a group tend to be the last into bull markets. Often, when their positive sentiment reaches a peak, it is an early warning sign for turns in the market.

Figures compiled daily by trade-futures.com show that about 80 per cent of small traders are bullish — about the same as when markets topped in November 2007.

Similar extremes are also being seen among options players and financial advisers but the fuel that drives rallies — volume of trades and the number of advancing stocks — has been drying up.

David Hunt, a technical analyst and principal of Adest, which advises on market strategies, expects the fragility of the US and Australian rallies to show itself soon.

''The Santa rally is early and it won't last,'' he said. ''Normally, there is a good move up to Christmas but this year there will be a top on the 14th or 15th that will surprise everyone.''

Mr Hunt said professional investors usually took advantage of low trading volumes in the lead-up to Christmas to drive the market higher, but added this was unlikely to be the case this year.

''Fund managers won't be able to manipulate the market for their year-end bonuses. Normally, they push prices up amid the light volume in December so their positions look good — but they won't be able to this year.''

Still, Mr Hunt's target for the S&P/ASX 200 Index is higher than the benchmark's close on Friday of 4702.2 points.

''I have a target for the S&P/ASX 200 of 4986 after one more leg up,'' he said.