



## Weekly Commentary

For May 26<sup>th</sup> – 30<sup>th</sup> 2008

By: Matthew Bradbard

Is Michael Masters for real? For those of you who are not aware, he is one of the gentlemen that presented to the CFTC about the impact that new money coming into the commodity sector has had with the recent price appreciation in commodities, most specifically in food and energy. His belief is that deep-pocketed investors such as corporate government pension funds, sovereign wealth funds, university endowments and kindred institutions are responsible for the phenomenal run higher in prices. This, to a very small extent, may be true, but we feel that it is more supply and demand. Recognize that we are experiencing two simultaneous industrial revolutions and the unparalleled growth of emerging markets coinciding with slack demand in a variety of commodities. Unfortunately, we feel the markets are looking for a scapegoat, as opposed to thinking logically and rationalizing that this may be as easy as ECON 101; we may, in fact, have a macro issue and, who knows, maybe inflation. The question may not be *why* but rather *how*; this is how to take advantage of price appreciation.

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Records are made to be broken as crude continues to push higher with July gaining over \$6 on the week. Oil was up 5% last week alone and without a significant retracement this week we could be up as much as 15-20% just in the month of May. As we have voiced in recent weeks, the trend remains up but at these levels you are playing with fire; tread lightly and do not fall asleep at the wheel. An untimely bathroom break in this environment could be extremely costly. Technically we are overbought but we have been so for the last \$10-15 advance, so that alone means very little. Resistance comes in at the contract high of last week, just above \$135 with support at \$130 followed by \$126 on July.

The U.S. Department of Energy said that underground supplies of natural gas were up 85 billion cubic feet last week to 1.614 trillion cubic feet. Supplies are down 16% from a year ago and slightly below the five-year average. July natural gas ended up 71 cents at \$11.98 on the week making a new contract high

trading above \$12. The recent correction was not enough to entice us to initiate a long in futures for clients but we continue to price out call spreads remaining bullish, for now have no exposure. We expect that to change in the near futures as we will initiate some type of long for clients if not by month's end then early in June.

Gasoline and heating oil prices continue to ratchet higher; however, as opposed to grumble about rising prices we suggest you recognize the opportunity and take advantage of their appreciation and accept that in all likelihood, prices have not peaked. Yeah we are overbought and seasonal tendencies do not support this movement; prices are too high; they have never been here before...yadda, yadda, yadda; the trend is up and until that changes, which could happen on a dime, continue to play the long side. Resistance in July heating oil comes immediately above 4.03 with support just below 3.96. July XRBOB has resistance at 3.43 with the first significant support at 3.30. It would not be unlikely to see 10 cent trading ranges so be prepared for volatility and make certain you have suitable margin to endure large swings.



After the close Friday, the USDA estimated beef production at 548.4 million pounds, up 3.9% from a year ago. August live cattle closed up 1.45 on Friday at a new contract high of 101.30. On the week prices advanced 2.80, with recent action we have abandoned our bearish sentiment and expect prices to continue moving north. Feeder cattle in August also gained on the week, picking up almost 2 ½ cents, finishing above 1.15 for the first time. Live and feeder cattle have advanced 11% since late March, with more gains to come the way we see it. Although we do expect higher prices, being that exports have picked up and demand remains robust, do not load up as the worst Junes have generally followed May strength. We expect to see 106 in August, live cattle with support at 99.55; the 9 day moving average. We are looking for 118.00 in August feeders with support between 114.25/114.75, which were the previous highs and served as a resistance level.

Pork production was estimated at 420.4 million pounds, up 5.0% from a year ago. August lean hogs were up 1.40 to 78.30 last week bouncing off the 40 day moving average. With the recent earthquakes that moved through China and the loss of hogs due to natural disaster, the demand should pick up in our exports and we expect that to be reflected in prices. We are forecasting a move to and through the contract highs and to levels not seen since '97. The premium of the deferred contracts are telling the story of market sentiment as prices out into mid '09 hold almost a 20% premium to the front month. Pork bellies remain on our no interest list but it appears a move back to 70 in July is in the cards and we will take a closer look this.

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## Financials



**Stocks:** Following a week of light economic data the stock market seemed to trade off oil more than anything else. So with oil moving to new highs it made sense that securities traded down. In fact stocks suffered their biggest weekly loss since early February with the Dow falling over 500 points or 3.9% to 12480. The S&P gave up nearly 50 or 3.5% to 1376. The NASDAQ fell 84 points or 3.3% to 2445. As we indicated last week, without a convincing move through the 200 day moving average it was likely that the S&P would lead stocks lower. The good news is that its descent stopped just short of the 50 day moving average at 1374, the 61.8% Fibonacci retracement comes in at 1368 which should also serve as mild support. On a breach of those levels, expect a trade below 1350. The Dow sliced through 12700 which we felt would serve as support and it appears will take a run at 12378 to fill a gap from mid-April. On new highs in oil we could see a trade down to 12150 where institutional buying would emerge. Volumes have been anemic and for a turn to happen we would need to see some more participants. Remember the adage sell in May and go away.

**Bonds:** June bonds and notes are being sold on rallies as we run into the trend resistance line. As we forecasted last week, June bonds should not trade above 118; last week's high was 117'13.5 and notes should stay contained under 117; last week's high was 116'02.0. We would expect this to be the trade this week as well so continue to sell rallies. When Bill Gross, Pimco founder and one of the foremost authorities on bonds advises investors to avoid treasuries in favor of commodity backed assets and foreign equities, debt is most likely moving down. Based on the release of the Fed minutes last week it appears they are starting to take inflation more seriously.

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## Currencies



The U.K.'s Office for National Statistics confirmed again that real GDP was up .4% in the first quarter and up 2.5% from a year ago, as expected. That was down from a .6% gain in the fourth quarter of 2007. The June British pound closed higher on the week as we had forecasted, as we are still looking to re-establish shorts for our customers expecting an attempt at 1.9900 this week.

We recommended waiting for a bounce in the Euro which we got last week as prices bounced off support and registered a gain of just over 2 cents on the week. We should encounter resistance at last week's high, just beneath 1.5800 and will start selling at those levels for clients willing to risk up to 1.6000 looking for prices to roll over from overbought levels. We would only suggest a light short as inflation expectations and the idea of future rate increases may prevent a failure shorter term.

If you got long the Swissie last week based on our recommendation we would advise trailing a stop to protect profits just under .9700 on June. In fact aggressive traders can reverse their longs and get short with a stop just above last week's highs roughly .9800. On a failure to make new highs early in the week we would expect prices to drift south back to the 20 day moving average of .9580.

The trend is up in the Aussie and we do expect parity in 08' but more than likely with the September contract and not the June. Last week we ran into resistance just above .9600 and we would suggest waiting for a pullback to .9250/.9300 before establishing a long position. We advise treating this trade as a position trade if we get our entry looking to hold for a move to par as opposed to a quick scalp. Patience is a virtue!

The yen has bounced off .9500 as we had predicted, but we had hoped for more action being that the stock market came under pressure. June should be supported at the 100 day moving average at .9635 for now and we maintain our feeling that we will make a run at .9850 or higher by month's end. We would advocate scaling into longs while paying close attention to equities.

If there was a currency that you wanted to be short on from current levels, it would be the Canadian dollar as most technical indicators support a move lower. We should have trouble penetrating above last week's high of 1.0180 on June, and on a move lower in energies or metals the Loonie could find its way back below par relatively quickly.

The dollar index lost just over 1.0% last week, closing below 72.00 for the lowest close since April 22<sup>nd</sup>. We will continue to stay clear of trading this instrument unless we get an opportunity to sell near 74.50 in June, but we will continue to follow the movement as many commodities continue to trade off the dollar.



**Corn:** Weekly export sales showed 507 t.m.t. of corn was sold last week. Corn planting on crop progress report should be over 90% complete from 73% last week, essentially meaning weather's impact on planting turns to weather's impact on growing as the spotlight shifts to emergence and crop conditions. With historically low ending stocks for next year, there is little margin for error in the growing season, so temperatures and precipitation will be closely monitored. A price rally taking corn to new record highs could occur rapidly as weather in June and into July will dictate yield development with this year's late plantings. We continue to advise using corrections to get long December '08. It is our opinion that without ideal growing conditions from here on out yields will be affected and a weather /risk premium is not fully reflected in current prices. Downside risk this week on month end profit taking by the funds in agriculture, a sharp retraction in oil or any significant rally in the dollar. Support on December corn is 6.18; the 40 day moving average followed by the psychological 6.00 level

**Beans:** Weekly export sales showed 382 t.m.t. of beans were sold last week. With the majority of corn in the ground, weather now will play a larger role in bean planting progress. The Argentine farm strike remains on the mind of traders and day to day can cause a 30-50 cent move just on rumors. As with corn, beans, too, will look for guidance from outside markets and may succumb to movement from oil, the dollar or month end position squaring. Use breaks back to support near 13.25 as a long term buy for November '08. November has support at 13.25 then 13.09; the 61.8% Fibonacci retracement level. On a move out of the recent trading channel above 13.75 no real resistance emerges until 14.35.

**Wheat:** Weekly export sales showed 492 t.m.t. of wheat sold last week between old and new crop. After a 60 cent rally, prices struggled to get much above the 200 day moving average, running into resistance at 8.10 for July CBOT. The story reads the same on KCBOT as a 50 cent rally failed to hold as prices were unable to stay above the 8.00 level. The charts remain bearish and we would continue to advise selling rallies anticipating that prices may get to 7.00 which have not been seen since around Thanksgiving. Harvest is just around the corner with farmer bins empty domestically and abroad we have to expect supplies to fill immediate needs with tight inventories to continue until next crop. It is still possible for a demand rally but from what price level? We still prefer trading beans and corn as opposed to picking a bottom in wheat until we get a close above resistance; July CBOT above 8.20 and KCBOT on July above 8.60. It may seem like you are missing the bottom waiting for those levels, but conversely a trade there should confirm a short term bottom has been made.



With the Brazilian coffee harvest beginning, a growing supply together with consumption slowing in the northern hemisphere, we expect lower prices. September coffee ran into resistance at the 100 day moving average and traded 4 cents lower on the week. We are pricing out 15-20 cent bear put spreads for clients in September.

Of late, in sugar if you were long you were wrong, which we have been with our clients, as prices hit the lowest levels in 7 months. This market has been pressured by fund and speculative long liquidation. The good news for the most part is that we are holding position into late 08' or into 09'. Although prices have come off 25% from the February highs, in dollar terms this reflects only a \$4500 move per contract, and being that we are friendly to sugar, expecting a major push higher as the fundamentals are starting to shift from bearish to bullish, we have advised clients to hold on. It boils down to holding onto what we believe to be a winning trade if patience is exercised. It is frustrating when other markets are making new highs to stay positioned in sugar, but at 20 cents/lb we believe our vigilance will be rewarded.

Cocoa grinded lower last week running into resistance at 2700 on July ending the week at 2577 down \$89 on the week. Support comes in just above 2500 at the 100 day moving average but there is still no clear

direction and we will continue to monitor the dollar hoping to get a feel for direction. Prices tend to move lower into June because of the growing cycle so do not be quick to establish a long until you get a clearer picture.

With mixed signals still coming from the housing market we would only suggest a light long in the lumber as we have discussed in previous commentaries. July gained about \$5 on the week and stayed contained within the recent trading range continuing to base out.

September FCOJ finished 180 points lower on the week but we are betting that we are going to get a 10-15 cent move higher from these levels as prices have exaggerated the move lower. On a continuation chart we bounced off support and being that we are extremely oversold a move to 120-125 seems attainable; we initiated a bullish option play for customers. Inquire for exact details.

Cotton came within 1 tick of the 200 day moving average on Friday before bouncing 1 ½ cents finishing at 78.01 on December. As we have said in previous commentaries we are bullish December and hold bullish options spreads for clients and have advised getting long futures as close to the 200 day moving average as possible thinking it will serve as the line in the sand. 90 cents remains our target but cotton continues to play follow the leader so closely monitor the happening in outside markets.



Gold was able to penetrate the \$920 level on June as we had anticipated but we did not see much follow through as prices didn't drift away from the 100 day moving average that currently comes in at \$923. This level should serve as support with the next target being the 50% Fibonacci level at \$943. We are at overbought levels but for now it appears the momentum still remains up. We would not rule out back and fill action but looking further out using the weekly charts as guidance we remain friendly. That being said we would advise holding your December calls for the next leg up and use pullbacks to start exploring long June and August futures for clients.

July silver finally pushed through the \$17.25 consolidation area we have been speaking to in recent weeks. This was quickly followed by a move back above \$18 as we had forecasted as silver traded \$1.22 or 7% higher on the week and is back at levels not seen since mid-April. We would suggest scaling into long futures trailing your stop on prior entries and will start to explore rolling out of July option spreads for clients. On daily charts we are currently overbought but like gold looking at a longer time frame we could be starting the next leg up; we would like to see a move over \$18.90 to confirm. Make sure you have an exit strategy in place on signs of weakness because June is historically weak for silver; from 1982-2006 September silver futures have declined 18 years during June or over 70% of the time. Furthermore,

weakness in June tends to follow strength in May as the last 14 May advances in September silver have been followed by 11 declines in June. Past performance is not indicative of future results.

*If a portion of your portfolio is not already in gold or silver we highly suggest you diversify into these metals as we expect to see much higher prices in coming months due to inflationary concerns.*

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Risk Disclosure: The risk of loss in trading commodity futures and options can be substantial. Before trading MB Wealth recommends that you should carefully consider your financial position to determine if commodity trading is appropriate for you. All funds committed should be purely risk capital. Past performance is no guarantee of future trading results. There are no guarantees of market outcome stated, everything stated above are our opinions. Calculations of profit and loss have not factored in commissions and fees.