The Hightower Report
Futures Analysis & Forecasting

Weekly Market Summary
Monday September 13, 2010

BONDS

Treasury prices have made a fresh downside breakout and are starting the new trading week on the defensive. They have already fallen to their lowest levels since mid-August. A noted GOP Congressman indicating he would be in favor of a middle class tax cut extension over the weekend. That seems to have given the US equity market an additional economic lift and in turn may be another element serving to weigh on Treasury prices early during the week. The Basel III banking regulation plans are serving to keep down flight to quality fears, as the markets are seeing the new guidelines more as a positive more than a big negative for European banks. Many see the markets looking for some direction from scheduled data during the coming trading sessions. With the market in some respect upgrading the economy, or becoming less concerned about the start of a double dip recession, expectations for upcoming scheduled US data may be raised slightly. It would appear that the potential for a US tax cut agreement (on middle class tax cuts) is being seen as a fresh macroeconomic positive, and may have initially improved sentiment and in turn applied fresh pressure to Treasury prices. At least to start the week, the trade seems to be in a position to seek risk and move away from the flight to quality markets, as fears of slowing and fears of Euro zone debt contagion appear to be diminishing.

CURRENCIES

The Dollar has come under broad-based pressure to start the week, as a rally in global equity markets has helped to send prices back down to last week's lows. Positive news from several regions overnight has dampened risk concerns throughout the markets, while the rise in longer-term US yields has only provided a small measure of support for the Dollar. While it may be a bit premature to suggest that a sea-change has occurred with the Dollar, the positive tone from global markets may act to keep prices on the defensive during the course of this week’s trading. The December Yen has been able to recover from an erosion of safe-haven support that has moved prices well away from the recent highs. A leadership vote for the current ruling party in Japan may keep trading relatively subdued early in the week, as the challenger to the current Prime Minister has been very vocal in his opposition to the recent strength in the Yen. While the December Yen has been able to hold these price levels in the face of global equity strength, a retest of the highs would likely need some fresh negative news to reignite risk concerns in the markets. The December Euro has been able to rally outside of the recent trading range, supported by a 2010 Euro zone growth estimate from the EU Commission that almost doubled from earlier in the year. That number has followed a series of positive global news stories over the weekend, and that has helped to lift the December Euro back up towards last week's highs. The Dec Canadian was able to regain upward momentum over the weekend, as lower market risk concern has provided solid support this morning. The recent rally remains intact, and further strength in global equity markets could see a new high for this move during the course of this week’s trading. In spite of lower market risk concerns to start out the week, the December Swiss has been able to grind out a gain today. Although the recovery from Friday’s lows has been impressive, it remains to be seen whether a move to new highs can be undertaken without the benefit of safe-haven support. The December Pound has benefited from the rebound in global equities, but has only moved back to the middle of the recent trading range. There will need to be more in the way of decent UK economic data flow before a move above this recent trading rang will occur.

STOCKS

Equity markets have started out the week with sizable gains, as they clearly like developments from the Euro zone, but more than likely the prospect of a middle class tax cut extension is the main catalyst behind the huge range up gap that seemed to be in place Monday morning. With US economic data last week that was not as bad as expected giving the bulls a leg up, weekend developments seem to have allowed the market to speculate on slightly improved conditions ahead. With merger and buyout activity expected to increase over the next several months, there are ideas that Washington may finally "doing something" to alter the slowing track in the economy. However, financial issues may also contributing to the rally this week, as Basel III banking guidelines agreed upon over the weekend were seen as a positive, instead of just a signal that more European banks would need additional capital.

GOLD, SILVER AND PLATINUM

With overnight international gold markets marking time instead of exhibiting a definitive direction on Monday morning, it seemed like gold was mostly unmoved by the weekend events. However, it does seem as if the markets are viewing the Basel III requirements as something that is good for the global economy in the long run. With very strong range up action in US equity market indicators, it also seems as if economic and investor sentiment is improved because of the prospect of an extension in US middle class tax cuts. At least in the early action this week, it also seems like gold is trying to track positively with the equity markets or perhaps gold is attempting to track positively with physical commodity markets. The Commitments of Traders Futures and Options report as of September 7th for gold showed non-commercial traders were net long 264,633 contracts, an increase of 3,720 contracts. Non-commercial and nonreportable traders combined held a net long position of 313,912 contracts. This represents an increase of 5,160 contracts in the net long position held by these traders.

COPPER

The copper market has started off this week with strong gains from what appears to be widespread macroeconomic optimism. The markets saw the Basel III banking regulation developments, along with the prospects of a US middle class tax cut extension, as positives for future copper demand, as copper prices have now regained 75% of the value they lost during last Thursday’s large selloff. The copper market did not appear to be pressured by news of a strong jump higher in Chinese August copper production, even though that could prove to reduce the need to import copper into China. Chinese copper production news may have been partially offset by a decline in production from Kazakhstan over the first 9 months of 2010. Chile's Codelco has indicated that their copper production for the first half of 2010 will be above last year’s levels by 16,000 tons.

ENERGY COMPLEX

October crude oil prices began the week near their highest levels since August 12th, helped by easier capital rules for Euro zone banks from the Basel III and better than expected Chinese Industrial Production figures. The positive industrial output also seemed to be a factor that boosted China's implied oil demand by 7.4% in August from year ago levels. Additional support for October crude oil prices in the U.S. comes after the closure of a key Canadian pipeline responsible for around 7% of crude flows to the Midwest. The supply uncertainty poses a threat to inventory levels in Cushing Oklahoma, and that remains a key driver behind the rally in nearby crude oil contracts. The Commitments of Traders Futures and Options report as of September 7th for crude oil showed non-commercial traders were net long 103,550 contracts, an increase of 2,851. Non-Commercial and nonreportable traders combined held a net long position of 119,126 contracts, an increase of 3,372 in the net long position held by these traders. Traders indicate that October crude oil has potential upside targets above at the August 12th gap of $78.40-$78.50, which also corresponds with upside retracement targets of the $13 August decline at $78.60. October RBOB prices have also managed to break out into new four week highs in response further supply concerns resulting in the Enbrige pipeline shutdown. Last week, cash gasoline differentials in Chicago surged by nearly $0.20 during Friday's session. Meanwhile, the non-reportable net short position in RBOB has reached a new record level at 5,513 contracts. October heating oil prices also seem to benefit from weekend data from China that indicated that the combined inventories of gasoline, diesel and kerosene were down 6.4% in August compared to the previous month, and that continues the six month trend in monthly inventory draws. October natural gas continues to digest Baker Hughes data released last Friday that pegged the natural gas rig count at 980, up three in the latest week. Horizontal rigs also touched a new record high of 911. However, there does to appear to be some weather support with category 4 Hurricane Igor in the Atlantic and Tropical Storm Julia off of Cape Verde.

BEANS

Trade focus seems to be on the corn market, but soybeans may also be influenced by spreading versus corn as harvest advances and more yield results come in. A record high yield and a record high production forecast from the USDA on Friday sparked a lower close of 15 cents on the day and down 4 cents for the week. Weather seems to be turning a little too wet for harvest this week, especially Iowa and the central Plains. Traders remain concerned with dryness in Brazil and Argentina ahead of their planting season, and the USDA still assumes an 8.5 million tonnes decline in production from these two countries combined for the crop which will be harvested early next year. Even with this lower production, world ending stocks are pegged at a record high. China's import demand was revised higher by 3 million tonnes to a record 55 million tonnes compared with 50 million this year and 41.1 million tonnes last year. US soybean production rose to a new record high at 3.483 billion bushels versus trade expectations near 3.400 billion and last month's USDA estimate of 3.433 billion. Ending stocks for 2010/11 were lowered by just 10 million bushels to 350 million from 360 million last month. Traders see the potential for higher production in future reports due to the large pod count, if we see favorable finishing weather. Solid economic numbers from China to start the week helped support many markets in which China is an importer. The Commitments of Traders report as of September 7th showed non-commercial traders were net long

139,490 contracts, up 7,015 contracts for the week. The buying trend of the funds is seen as a positive short-term force, but many traders see the high level of fund longs in the market as an overbought condition.

CORN

December corn pushed above the January 6th, 2009 high at 480 3/4 to start the week. This followed similar push through the June 2009 highs last week, and the result is that the trade may be getting increasingly bullish in corn. Support also came from a lower dollar to start the week along with last week's larger than expected decline in the corn yield on the USDA's September Crop Production report. Last week's weather brought moderate to heavy rains in Missouri with lesser totals in western and central Illinois and along the Iowa-Minnesota border, but conditions dried into the weekend in most areas to the south of the Great Lakes. Mostly dry weather is expected to persist into mid week with the exception of moderate to heavy rains in the east central Plains and parts of western Iowa. Last week's Crop Progress report showed harvest at 6% complete versus the 10-year average of 4%, and traders are expecting to see that total rise to 10-15% complete this week. The Commitments of Traders report for the week ending September 7th showed strong buying by funds. Trend-following (managed) funds were net buyers of 33,560 contracts to increase their net long position to a record large 333,214. Index funds were net buyers of 4,298 contracts, and their (long) position of over 495,000 contracts sits just shy of its all-time high. The USDA lowered the average US corn yield to 162.5 bushels per acre from 165 bushels in August. Production was lowered to 13.160 billion bushels from 13.365 billion with ending stocks dropping to 1.116 billion bushels, not far from trade expectations near 1.110 billion. Last month's ending stocks were 1.312 billion bushels. US stocks/usage dropped to 8.3%. This only the third time stocks/usage has been below 10% since 1973 this and the lowest stocks/usage since 1995. World corn ending stocks were revised down by about 3.6 million tonnes from last month to 135.56 million tonnes. China production was left unchanged at 166 million tonnes. US Corn exports were revised higher by 50 million bushels to 2.1 billion bushels from 2.05 billion last month. Some traders see the possibility of further increases in corn exports on future reports. Feed usage was revised down by 100 million bushels to 5.25 billion. Last week's exports were considered somewhat disappointing at 680,200 tonnes. Sales need to average 730,000 tonnes each week to reach the USDA forecast.

WHEAT

December wheat moved past last week's high to its highest level since August 13th to start the week. This followed the building of a minor upward bias during last week’s holiday-shortened action. Support is coming from a very strong demand outlook with last week’s export sales total running at the highest level in three years. Strength in the dollar and signs of possible renewed buying interest on the part of managed funds is also lending support. These factors are outweighing a somewhat disappointing supply and demand report from the USDA on Friday. The USDA left all-wheat domestic numbers unchanged with the exception of a 50 million bushel increase in exports and a corresponding 50 million bushel decrease in 2010/11 ending stocks to 902 million bushels. This is still well up from 306 million in the 2007/08 season. World numbers were viewed as negative with 2010/11 beginning stocks up by 2 million tonnes and overall production down by just 2.72 million tonnes to 643.01 million. This drop was smaller than traders expected, but it marked the 4th month in row that the USDA has lowered its world production total. Total world usage was lowered by about 1 1/2 million tonnes and this resulted in an unexpected increase in world ending stocks to 177.79 million tonnes from 174.76 in August. Russian production was lowered by another 2 1/2 million tonnes to 42.5 million while Ukraine and Kazakhstan were left unchanged. Canada was raised by 2 million tonnes to 22.5 million and the EU was lowered to 135.13 from 137.51 last month due to lower production in Germany.

Last week's export sales totaled a very strong 953,400 tonnes for the current marketing year and 660,000 for next year for a combined total of 1,613,400. The biggest individual sales were for hard red winter wheat to an unknown destination and to Egypt. The Commitments of Traders report for the week ending September 7th showed that trend-following (managed) funds were net buyers of 3,961 contracts to shift back to a small net long position of 505 contracts. Index funds were net buyers of 7,071 contracts. Lebanon bought 25,000 tonnes of US wheat on its latest tender, indicating a minor push by the US into the big import market in the Mediterranean Basin. Traders report that two Black Sea feed wheat export sales to the Philippines have been cancelled. The sales were said to total 123,000 tonnes. Strong export sales and very little competition for the US other than France should keep importers on the buy side. Importers would probably balk at paying near the summer’s highs in wheat, but they appear to find current levels very attractive, and that advantage would only increase if the dollar moves lower.

HOGS

The market is likely to see some pressure from increasing supply into the fall, but weekly slaughter levels continue to come in well below expectations from the last USDA Hogs and Pigs report. The USDA lowered pork production in the September 10 supply/demand report 35 million pounds. For the month of July. Pork exports slipped to 327.7 million pounds, as compared with 365.2 million in June and down 6.3% from last year. There have been only 5 months of lower exports since late 2007. The CME Lean Hog Index as of September 8th came in at 81.86, down from 83.01 the week before. Packer margins are still in the black but were pinched last week with declining pork prices but firm cash markets. The estimated hog slaughter came in at 1.917 million head last week, down from 2.113 million head the previous week and down 6.4% from last year. Production for the week was down 7.6%. Pork cutout values ended last week at $89.85, down from $92.38 the previous week. This was the lowest pork price since August 12th. The Commitments of Traders reports as of September 7th showed non-Commercial traders were net long 50,513 contracts, up 434 contracts for the week. The market acted tired last Friday and the reversals for the 2011 contracts show some sign of a near-term top. However, until the slaughter pace picks up versus last year, the market is likely to continue to receive good support on corrective breaks.

CATTLE

December live cattle finished last week down 67 points as they struggled with overbought conditions along with the possibility that poor economic news could spark a significant wave of in long liquidation selling from fund traders. The USDA raised 2010 beef exports by 70 million pounds to 2.263 billion pounds in the month supply/demand report, and imports were lowered. Monthly beef exports for July reached 204.8 million pounds, up slightly from June and up from 166.5 million pounds for the same period last year. U.S. beef export sales for the week ending September 2nd came in at 10,100 metric tonnes, compared with the prior 4-week average of 11,325 tonnes. Cumulative sales for 2010 have reached 470,400 metric tonnes, up 29.8% from last year's pace. The estimated cattle slaughter for last week came in at 583,000 head, down from 672,000 head the previous week but up 3.7% from last year. However, beef production for the week was up just 0.8% due to lighter weights. There remains some trepidation after the recent runup in corn prices helped support deferred contracts in cattle, as there may be less of an incentive to move cattle into feedlots. Boxed beef cutout values ended last week $159.42, which was down from $162.91 the prior week and was the lowest they had been since August 18th. The Commitments of Traders reports as of September 7th showed non-commercial traders were net long a new record high 143,587, an increase of 876 for the week. Commodity index traders held a net long position of 132,087 contracts, up 256 contracts in their net long position. The buying trend from the fund traders is a positive short term force, but the market is extremely overbought and vulnerable to increased selling from speculators if support levels are violated.

COCOA

The cocoa market continues to see aggressive selling from fund traders who are building a large net short position ahead of the main crop harvests in West Africa. Prospects for large upcoming crops from several producing nations in West Africa continue to weigh on the market, as prices have now reached their lowest levels in nearly 14 months. With the heavy losses, the cocoa market has fallen over $500 in a little over 5 weeks of trading. Additionally, traders see the September London futures trading at a discount to the December into expiration as a negative force, and that provides less concern for short-term cash tightness. However, the weather looks a little too wet in the Ivory Coast growing areas, which might help provide some underlying support soon. Recent wet weather in the Ivory Coast has affected cocoa bean quality from that nation but has not lowered crop expectations for the upcoming 2010/11 season. The Commitments of Traders Futures and Options report as of September 7th for cocoa showed non-commercial traders were net short 8,709 contracts, an increase of 3,511 for the week. Trend-following funds (non-commercial without index traders) increased their net short position by near 3,400 contracts for the week to 18,883. Records have been kept for this group of traders since 2006, and this is a record large net short position. Non-commercial and nonreportable traders combined held a net short position of 8,987 contracts, which is an increase of 2,727 for the week.

COFFEE

The coffee market seems a bit too overbought given the supply increases expected on the world market in coming months and after December coffee closed 285 points higher last week to a 13-year high. Traders remain fearful that next year's coffee harvest in Brazil could be negatively impacted if the weather stays too dry into flowering in the next few months. Last week the Brazilian government made a slight upward revision to their forecast for 2010/11 coffee production, lifting their estimate up to 47.2 million bags as compared with 39.5 million last year. While a 20% increase over last season, the figure remains well below trade estimates which are at 50-55 million bags. Additionally, there are concerns that there was too much rain in Colombia in August which will slow harvest progress and could impact production in 2011 as well. However, recent precipitation in Vietnam has improved the prospects for this season's coffee crop, which might be a limiting factor for the upside in London. Meanwhile, India's crop production estimates are slipping due to poor weather. The Commitments of Traders reports as of September 7th showed non-commercial traders were net long 42,347 contracts, an increase of

3,298 for the week. The buying trend is seen as a short-term positive force. Non-commercial and nonreportable traders combined held a net long position of 43,074 contracts, up 3,148 for the week, and that leaves the market in an overbought condition but not at an extreme. The net long position from this group reached a record high near 69,000 net long in February of 2008. ICE exchange stocks were up 1,920 bags Friday to 2.012 million with 1,850 bags pending review.

COTTON

December cotton posted its highest close for the move last Friday, following the release of a neutral to supportive US and world supply and demand update, and a lower dollar helped to push prices higher to start this week. However, last week's Export Sales report may have raised a caution flag for bulls. For the first time in several weeks, cotton sales fell to well below the weekly average needed to reach the USDA's current export projection. Net sales for cotton came in at 97,100 running bales for the current marketing year and 42,000 for the next marketing year for a total of 139,100. This compares to last week's total of 245,800 bales for 2010/11 alone. As of September 2, cumulative cotton sales still stand at a very strong 47.0% of the USDA forecast for 2010/2011 versus a 5-year average of 32.0%. Sales need to average 162,000 running bales each week to reach the USDA forecast. The USDA's supply and demand report raised the US export forecast for 2010/11 by 500,000 bales on Friday versus last month's total of 15.00 million. It also raised US domestic usage by 200,000 bales. Planted and harvested acreage and yield were all raised fractionally, but the increased usage resulted in a decline in ending stocks to 2.7 million bales from 3.2 million in August. Traders were looking for reductions in Pakistan and China production, but Pakistan was only lowered by 200,000 bales from last month to 9.3 million while China was lowered by 500,000 bales to 32.5 million. Overall world production was left about unchanged and ending stocks were lowered slightly to 45.44 million from 45.61 million in August. Texas received moderate to very heavy rains last week but has seen widespread drying since. Dry weather is expected to prevail from Texas through the Delta, Deep South and SE into mid week, which is welcome as bolls are open or opening in many areas and harvest approaches. Far southern areas of the North China Plain are expected to see thunderstorms in the next few days. This is unwelcome as bolls are open in many fields there and recent localized flooding in the broader region has already trimmed production. Most areas of India and Pakistan have received ongoing showers and thunderstorms that has soil moisture levels at adequate to surplus levels. However, flooding remains a danger in some location. The Commitments of Traders report for the week ending September 7th showed mixed activity by funds. Trend-following (managed) funds were net buyers of 4,324 contracts to increase their net long position to its highest level since early 2008 at 71,730 contracts.

SUGAR

The sugar market does not appear to have any significant tightness over the near-term, but there is some concern over production next year in Brazil. Some traders said that the recent rally has "priced-in" a general tone that the projected surpluses for the world market for 2010/11 have been revised down to near zero. October sugar prices surged 213 points higher last week to new six-month highs with active fund and speculator buying noted. Traders pointed to continued concerns with dry weather conditions in Brazil and lower than expected production out of Europe as supportive factors behind the 33% rally in prices off the August 10th lows. Dry weather in Brazil is keeping this year's harvest very active, but the trade remains concerned with next year’s crop. Near term weather forecasts call for a few showers in southern Brazil growing areas in coming days but not enough to ease concerns for next year’s crop potential. The Commitments of Traders reports as of September 7th showed non-commercial traders were net long 147,501 contracts, an increase of 14,242 for the week, and that buying trend is seen as a short term positive force. Non-commercial and nonreportable traders combined held a net long position of 182,228 contracts, up 15,861 for the week. This indicates that the market is in an overbought condition is a bit vulnerable to selling if the trend turns down, but the combined position is still not near an extreme. The combined spec net long reached near 303,000 contracts in February of 2008. Meanwhile, the USDA’s monthly supply/demand report on Friday forecasted a further decline in U.S. ending stocks to just 1.084 million tonnes from 1.258 million last month and 1.510 million last year. The stocks/usage ratio is down to 9.8% from 13.7% last year and 14.3% the previous year. The USDA seems to prefer a ratio near 15%, and traders indicate that a drop to near 5% can spark increased imports.