

Market Research

Crude Oil vs. US Dollar Index

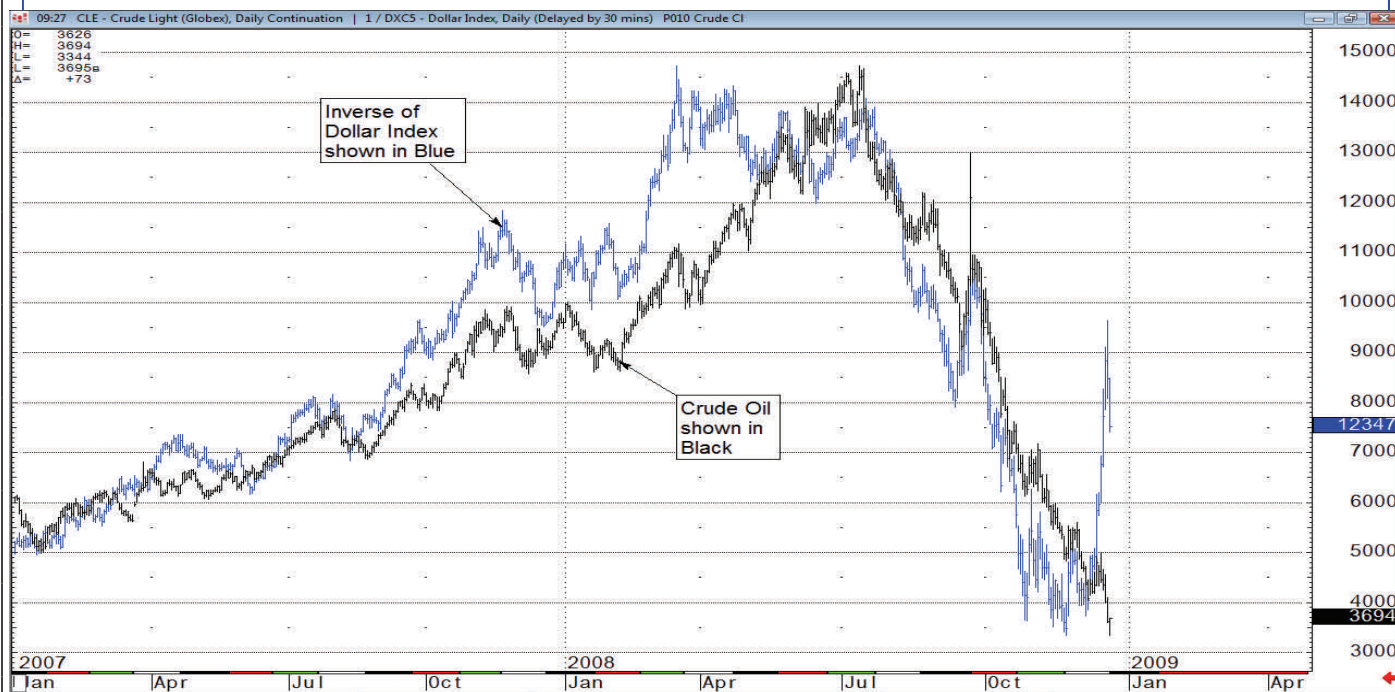
Over the last year, much debate surrounded the relationship between crude oil price and the relative value of the US Dollar. On the one hand, there was a belief that erosion of the value of the US Dollar resulted in higher crude oil prices. On the other hand, it was argued the two markets have unique fundamental aspects and any correlation (actually, inverse correlation) was expected to be a temporary phenomena. In our Mar08 Market Research, Capstone argued the two markets have unique fundamentals and the strong inverse correlation would eventually breakdown. To review that article, visit our website at http://capstonetrading.sitestreet.org/8/Energy_Analysis.html.

The chart below displays the correlation between NYMEX Prompt Month Crude Oil (black) and the inverse of the US Dollar Index (blue).

As Helicopter Ben continues his strategy of “Quantitative Easing”, flooding the market with newly minted US Dollars, the relative value of the US Dollar has re-engaged its path of decent. Remember, the chart below reflects the inverse of the US Dollar Index. Estimates of US only monetary stimulus are now estimated at over \$8 trillion US Dollars.

The relationship depicted below may be an early indicator of future global economic health. That is, are we headed for recovery or a more intense recession? Capstone believes continuance of the inverse relationship will suggest global economic recovery, while breakdown of the inverse relationship will suggest a more intense recession. In other words, if crude oil price fails to recover and the US Dollar continues to lose relative value, the economic outlook could be quite dire.

Although very recent price action suggests a breakdown of the inverse relationship may be underway, there is yet insufficient time and data to draw such a conclusion. This relationship deserves review in the first quarter of 2009. Capstone believes the extent of economic stimulus is so massive, that economic recovery is forthcoming, the price of which is unprecedented resource based inflation.



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