Sweet Spot, Overbought?

Beyondbond

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Record low oil prices, calm inflation data, and a most likely full-stop interest rate weaved a strong safety net for the markets at the five-year anniversary of 9/11. For the week, the Dow gained 1.5%, the S&P 500 added 1.6%, and the Nasdaq increased 3.2%. Both the Dow and the S&P 500 nearly reached May's high. Crude oil dropped to $63.33 per barrel, the lowest prices since March, after an estimated cut in global consumption by International Energy Agency. Slightly touching above 4.80% during the week, the 10-year Treasury note yielded at $4.78%, a very small change from last week as the buyers stepped in.

Weak numbers from the Energy/Commodities sector and the Labor Department were the major lifts behind this rally. In addition to the fall on demand, oil prices have plunged 19% since July due to high inventories, temporary peaceful geopolitics, and a quiet hurricane season. The high-profile inflation indicator, CPI and the core index, which excludes energy and food price, rose 0.2% in August. The second consecutive month of benign consumer price data reassured investors to bet on a steady interest rate from the Fed. On top of this, better-than-expected earning reports from Goldman Sachs(GS), Lehman Brothers(LEH), and Bear Stearns(BSC) also helped heat up the markets.

Complementing all of these timely catalysts, Wall Street thrived for another week of September and was not affected by Friday's quadruple witching event. Fifteen out of eighteen years in the past, the markets suffered from the volatility spells cast quarterly by the simultaneous expiration of four contracts, stock index futures, stock index options, stock options, and single stock futures, referred to as quadruple witching. In spite of standing at a sweet spot, the markets are short term overbought. Before the Fed's decision and earning warnings coming out next week, the markets remain in trading range. It is better not to commit and chase the markets during this waiting period. Active traders and investors should continue to secure the profits when they can.

Due to the low oil prices, anticipation on the Transportation sector lead to an overbought market. The Dow Jones Transportation Average soared 2.8%. It is looking bright in the long run but investors should be aware that a correction in the short term might occur.

The short term overbought happened in the Retail sector as well. Prices may drop due to the end of back-to-school season. Nevertheless, investors probably can target their positions at a longer outlook as the Christmas shopping season approaches.

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In the long run, housing market remains bearish but it is oversold in the short term. Although some upsides might be observed, short term traders might enjoy a better ride than the others.

The other big news over the week would be the G7 meeting that was held in Singapore. While the theme of the meeting was to push greater exchange rate flexibility and strengthen Asian currencies, the Yen still dropped to a five-month low against the dollar at 117.55 yen. Countries such as Australia, New Zealand, and Canada with major mining exports tied in their dollars all suffered drops in their currencies due to the shaky commodity demands. Investors can let US dollar continue to rise and use ETF to buy Euro when it drops.