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## U.S. stock market closely tracking moves of dollar

Some analysts believe relationship will persist until Fed raises rates

By Kate Gibson, MarketWatch

**NEW YORK (MarketWatch) --** The U.S. stock market is paying more attention than usual to the movements of the U.S. dollar, with the greenback's newfound status as a funding currency leaving its moves highly correlated to equities and other riskier assets.

Since the S&P 500 (INDEX:SPX) hit a low in early March, the index of large-cap stocks has jumped nearly 60%. The U.S. dollar has moved in the opposite direction, falling 15%.

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Dean Curnutt, Macro Risk Advisors

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"We expect the relationship between the movement in the dollar and stock prices to continue for several more months until the Fed actually steps in and begins to lift short-term interest rates," said Fred Dickson, chief market strategist at Davidson Companies.

The greenback's status as both the world's reserve and funding currency means the Federal Reserve "still has the luxury of imposing its monetary policy on the global markets," said Dean Curnutt, president of Macro Risk Advisors LLC.

In essence, as Curnutt sees it, the central bank is managing "the most giant carry trade of all time," which has U.S. equities rising as the dollar weakens.

With short-term interest rates very low, global traders have turned to borrowing funds cheaply in the U.S. and then reinvesting the proceeds in equities and commodities, looking to lock in higher returns and benefiting from further erosion in the dollar.

The so-called carry trade has helped to further weaken the dollar this year.

The dollar index (INDEX:DXY), which measures the U.S. unit against half a dozen currency rivals, hit a high of 89.08 in early March, within days of the S&P 500 Index falling to a low of 667. On Tuesday the dollar index traded at 76.22, while the S&P 500 ended at 1,063.41. Read Currencies.

"Nervous global investors, not wanting a repeat of massive Japanese carry-trade-financed global investments experienced a year ago, appear to have a hair trigger on the sell-side, reacting to very small movements in the dollar by selling commodities, financials, commodity-related metals and crude oil when the dollar shows even the slightest of gains," Dickson said.

### Rally over?

U.S. policy makers are contending with a dilemma much as Japan did in the last decade, when the country wanted to keep interest rates low to bolster asset prices and encourage growth, yet at the same time worried about creating too much liquidity, said Bill Gross, a founder and co-chief investment officer at Pacific Investment Management Co., in commentary on PIMCO's web site.

**SPX** 1,061, +18.79, +1.80%

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**DXY** 75.92, -0.51, -0.66%



“Investors must admit that without the policy guarantees of the Fed, Treasury, and FDIC, as well as the continuation of punitive 0% short-term rates that force investors to buy something, anything, with their cash, that risk spreads may widen again, not stabilize,” Gross wrote. Read Gross.

He said the six-month rally in risk assets “is likely at its pinnacle.”

In recent earnings reports, some companies cited the weaker dollar for improving financial pictures.

Bemis Co. Inc. (NYSE:BMS) , a supplier of flexible packing materials for food and consumer products companies, on Tuesday listed the weakened greenback in raising its profit outlook for the second time this year. Read more.

“These days, it all goes back to the dollar. The investment community tends to focus on something from time to time, right now it’s the dollar,” said Yu-Dee Chang, principal at ACE Investment Strategists LLC.

On Tuesday, consumer discretionary shares fell the most as Wall Street finished mostly lower after a two-day drop that had the Dow Jones Industrial Average (INDEX:INDU) losing more than 200 points. The Dow industrials gained 14.21 points, or 0.1%, to 9,882.17.

The S&P 500 fell 3.53 points, or 0.3%, to 1,063.41.

The Nasdaq Composite Index (NASDAQ:COMP) fell 25.76 points, or 1.2%, to 2,116.09

Past performance is not indicative of future results. The risk of loss exists in futures trading.