

The Rally May Be Running Out of Momentum

I hope everyone had a good Holiday Season. Wheat has posted a nice move higher since my last article. While the reasons for the move higher are numerous, the fundamentals of the wheat market were not a key factor. The Chicago March contract failed to trade above the 200 day moving average of 568 for the second day in a row.

Speculation pertaining to index fund position rebalancing has provided support to the wheat market. The market is expecting this process to commence on Friday. It appears to me that the process will result in index funds buying 15,000 to 20,000 Chicago wheat contracts. They would also be buyers in KC. If this two month old story materializes, do not expect them to make big waves in Mpls. In fact, I am not sure they will make big waves in any of the markets. It appears they have 5 days to complete the process. How this process affects the markets will depend heavily on order flow. These markets are deep enough to handle orders spaced out over a few days, but I do expect volatility to increase during this process. Do not rule out the possibility of a majority of the trade taking place very late in the session. Time will tell how it goes, but it will be nice to get it over. The expectations related to this process may ultimately be a bigger market mover than the actual process.

Trend following funds will continue to be a factor. As of Dec 29th, The Commitments of Traders Report indicates that large spec traders are net short 39,000 contracts in Chicago, net long 500 contracts in KC and remain net long 5,400 contracts in Mpls. Momentum to the upside would result in more buying in Chicago. For this to happen, however, the market is going to have to establish trade above the 200 day moving average. I do not believe purchasing wheat near these levels is a sound practice, but I cannot rule out further upside movement. If wheat can find upside momentum from these levels, I expect most commodities to find upside movement from these levels, as well.

If you are holding long positions, keep a close eye on the next few sessions for areas to exit at least a portion of the positions. Currently, I am looking for areas to get short these markets. Initially, I will do so via the purchase of puts or put spreads. I want to be certain the fund community is done buying these markets prior to establishing new short futures positions. Ultimately, the market will come under the weight of huge domestic and global supplies, disappointing export activity and perhaps a dollar that continues to strengthen.

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