

26th September 2006

British Pound vs U.S. Dollar – Long Term Outlook

The long term chart is not an easy one to read and as we move forward there will need to be constant assessment of the potential wave structures that may appear. The problem we face is that on a multi-year basis we simply do not have enough data history to judge just what is happening.

The favored two scenarios are a long term sideways correction or possibly a three wave rally that could rise to as high as 2.3500-2.4500 before corrections which will probably last well into our retirements... This second scenario is such a large call that I prefer to place this as secondary but keep it in the back of my mind.

The pictures that appears to be developing from the weekly and daily charts appear to be a little more consistent, and quite frankly, relevant to our time horizons. Cycles are most certainly looking to reach highs, and the earlier of these should occur quite soon – and we may have possibly seen it already. In fact this is one clue of which we can take note. If the 1.9144 high remains intact then we have around 10 weeks of decline. A breach of the 1.8550-1.8600 pivot level will be critical for this point. While it holds there is still one chance of a move back towards the 1.9548 high.

The difference between the two is more relevant for the longer term. Should 1.9144 hold the larger pattern would seem to favor a large triangle pattern from the 1.9548 high and thus any decline will remain well above the 1.7046 low. Alternatively, a retest of the 1.9548 high would suggest a flat correction and thus an eventual test of 1.7046.

We need therefore to remain flexible an open to moves in either direction but watch for evidence of which scenario is correct. For now we have downward daily cycles for 2-3 weeks and where this ends will be important. If this remains above 1.8550-60 then the scenario calling for a retest of 1.9548 is still open. A break below 1.8550 would then favor a larger triangle and what is likely to be a return to some tight range trading and breaks which could prove to be frustrating.

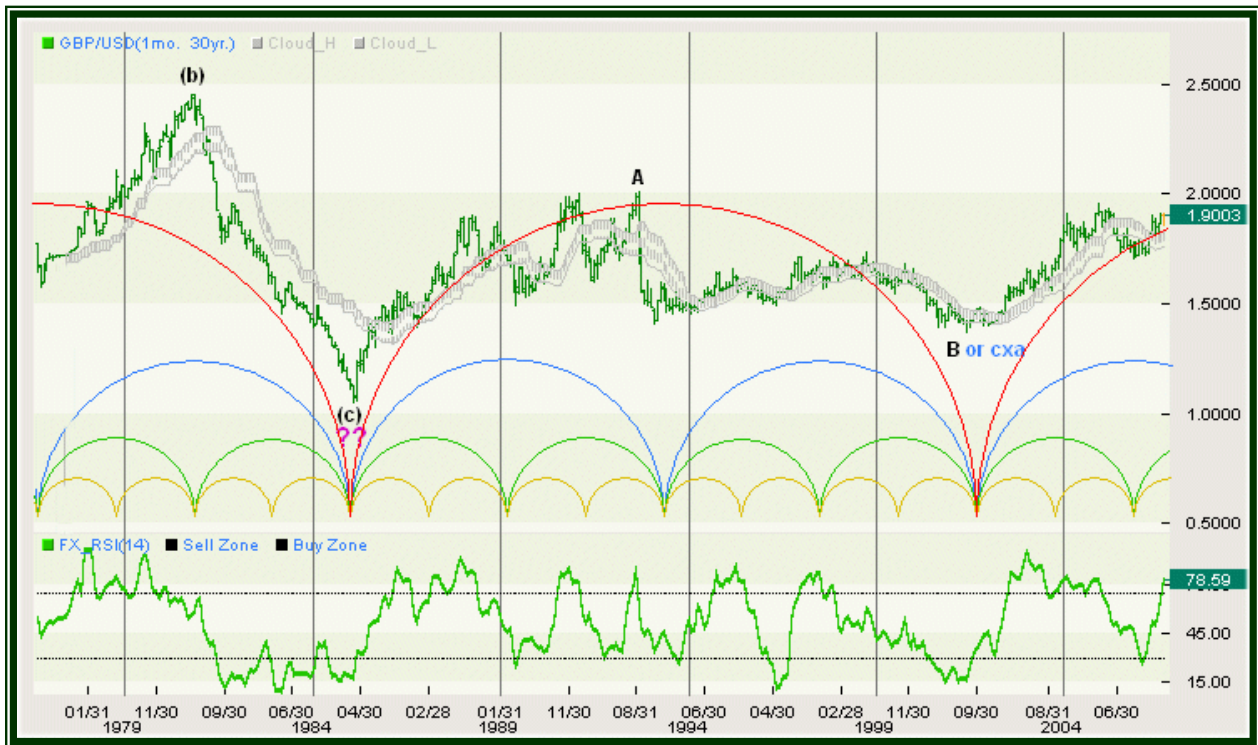
I shall update as the price pattern develops.

Ian Copsey

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Monthly Chart



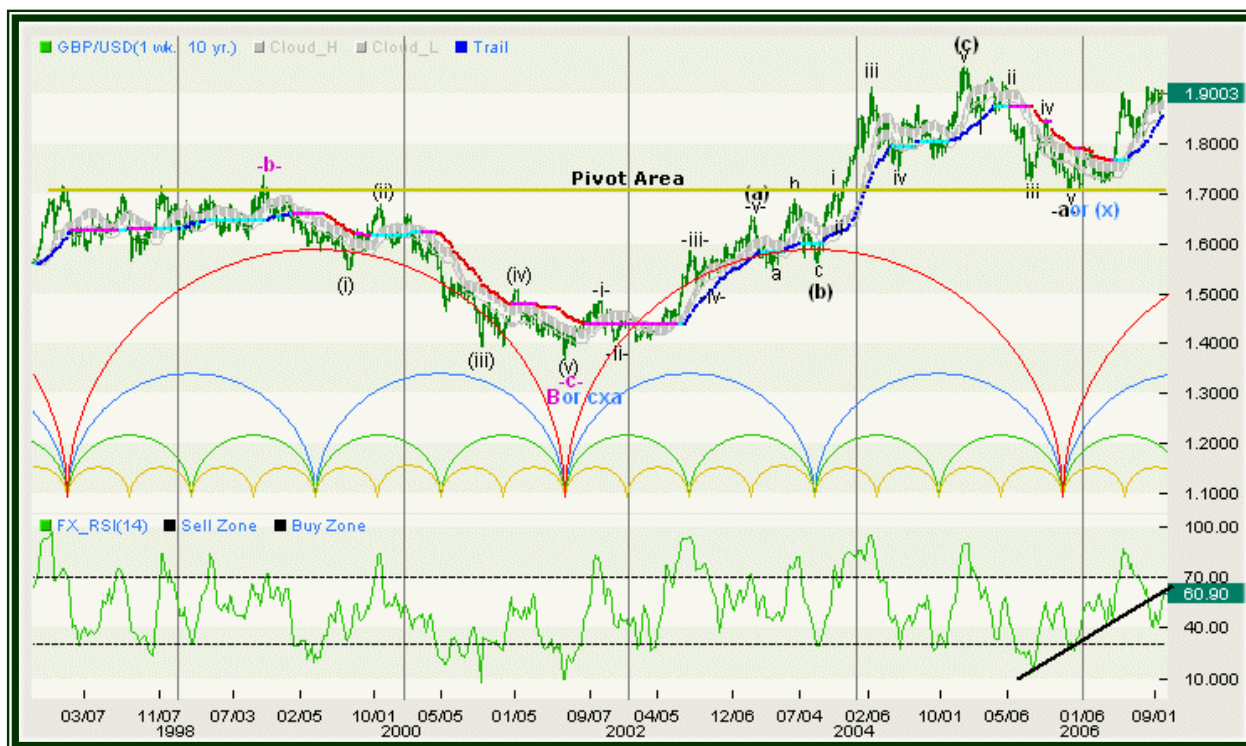
Points to note on the monthly chart:

- The wave structure can be interpreted in several ways.
- It is most likely that a major multi-year low was seen at 1.0370
- The first peak following the 1.0370 low at 2.0100 looks to be a Wave A
- Tentatively the corrective low at 1.3682 is therefore Wave B or Wave a of a complex correction
- Monthly cycles appear to be bullish with the most recent low at 1.7046
- The monthly blue cycle has begun to decline
- The next combined low of blue, green and yellow cycles is not due until 2010
- FXS-RSI Does look to have a possible bearish divergence

To summarize the monthly chart, it is rather difficult to recognize the wave structure and thus to generate upside projected targets. The two most favored patterns would be a straight ABC pattern higher with Wave A at 2.0100, Wave B at 1.3682 and thus we may be in Wave C higher. Alternatively this may be a large complex correction. Thus we need watch the shorter time frame charts to judge when moves are coming to an end.

At some point we can expect a larger decline since in approximately four years time we can expect a major cycle low of blue, green and yellow cycles. This tends to suggest a greater risk of a complex correction which will end at that time. The alternative of seeing Wave C complete to generate a correction to the ABC pattern from 1.0370 seems unlikely since the time to see the correction appears too short, although it could allow an initial Wave (a) decline in a further multi-year correction in Wave (x).

Weekly Chart



Points to note on the weekly chart:

- We appear to have seen a three wave move from 1.3682 to 1.9548
- The correction to this three wave move appears to be fairly short in duration
- While red & blue cycles are bullish, the green and yellow cycles are bearish
- There is around 10 weeks left to the next green & yellow cycle lows
- FXS-RSI has broken below a support line and is currently retesting this line
- Price is above the Pivot Cloud and Trailing Stop
- There is a strong pivot support area around 1.7000

To summarize the weekly chart we are getting some early messages of the upside beginning to run out of steam with the green and yellow cycles now looking to decline for the next 10 weeks. However, following that we can expect the upside to come under renewed pressure. It is interesting that a support line in FXS-RSI has been broken and now retested and this tends to confirm the conjecture that there is beginning to be some downward pressure beginning to build up.

Given the relative short duration of the correction to the 1.3682 -1.9548 rally it would tend to imply that we are still within a complex correction. Given the stage of the cycles this would appear more likely to be either a flat correction (which would imply a test of 1.9548) or a triangle (which would imply a peak has already been seen.) Note the pivot support around 1.7000. This would lend support to the possibility of a complex correction in the two patterns suggested since both would imply that the pivot support would remain intact.

We should be watching for the next break of the Pivot Cloud on the downside as an early signal of further losses.

Daily Chart



Points to note on the daily chart:

- The cycles appear to be turning lower
- The blue cycle is still rising while the red is declining but still quite high and this could allow one final new high
- There is around 2-3 weeks until the next yellow cycle low
- If a new high is seen there is a larger risk of a bearish divergence forming
- There is a pivot support area around 1.8550-1.8600
- There is a Wave (b) at 1.8090 that would be retested on any reversal lower
- Price is oscillating around the Pivot Cloud and thus any break lower must be matched by the weekly Pivot Cloud

To summarize the daily chart, it appears that we are still possibly in the middle of a move higher. There is no clear reversal signal as of now although with the blue cycle coming to a high soon and the green and yellow cycles already declining for a further 2-3 weeks that any recovery (if seen at all) would be short lived and would also probably cause a bearish divergence to form. We should also not rule out a direct move lower. We should observe any test of the 1.8550-1.8600 pivot support – breach would imply a move down to the 1.8090 Wave (b) low once again.

Should we by any chance see an earlier move higher we may consider a possible expanded flat correction of the original decline from 1.9025 to 1.8090. Resistance points implied by this will be at the 23.6% expansion at 1.9246 and at the 38.2% expansion at 1.9382.