

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE
THAT WAS THE WEEK THAT WAS



Monday, April 19TH

The New York-based Conference Board's index of U.S. leading economic indicators rose by 1.4% in March, following a revised increase of 0.4% in February

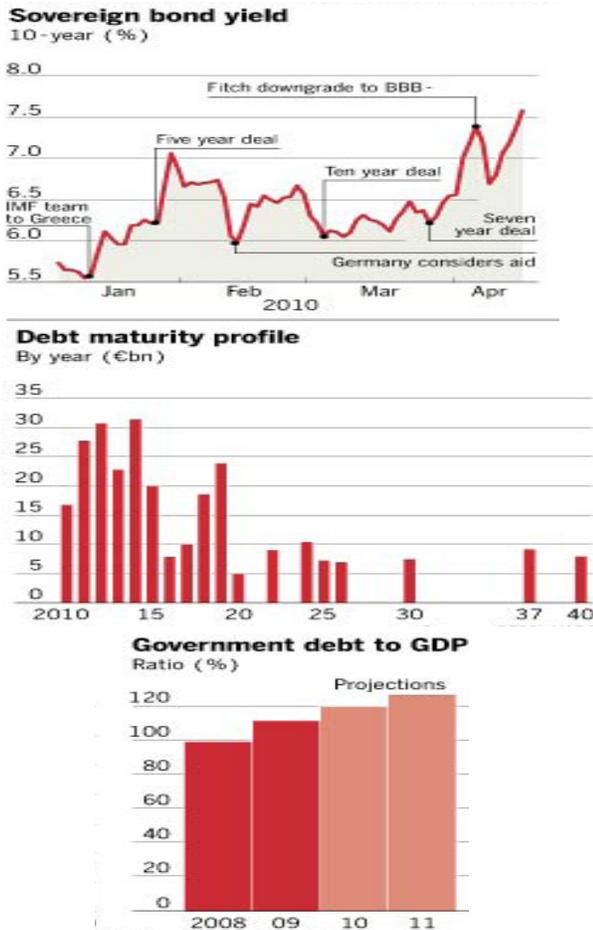
MONDAY, APRIL 19TH

- In June 2009, the U.S. Securities and Exchange Commission (SEC) filed a civil suit in Los Angeles federal court against Countrywide Financial longtime chief executive, Angelo Mozilo. According to the Wall Street Journal, the pending SEC lawsuit alleges that Mr. Mozilo defrauded investors by falsely claiming that Countrywide underwrote low-risk mortgages, at a time when the company was entering increasingly risky areas of the lending business, including "subprime" mortgages. In addition, the SEC accuses Mr. Mozilo of insider trading of Countrywide stock. The lawsuit is seeking monetary and other penalties, including repayment from Mr. Mozilo of \$139 million (U.S.) in alleged stock trading profits. A trial in the case is scheduled for October. (See also, Winter Warning, October 20, 2008 – The Wolves of Avarice)
- Two U.S. prison management companies, the Geo Group and Cornell Companies, agree to merge, as budget constraints among state and local governments increasingly prompt authorities to consider outsourcing correctional and detention facilities. The Geo Group will remit \$385 million (U.S.) to Cornell in cash and stock, as well as assume \$300 million (U.S.) of Cornell debt. George Zoley, chairman and chief executive officer of Geo commented: "This merger represents a compelling strategic fit for both of our companies and positions us well to meet the increasing demand for correctional, detention and residential treatment facilities and services."
- Fabrice Tourre (self-dubbed the 'Fabulous Fab') the Goldman Sachs employee at the center of the U.S. Securities and Exchange Commission lawsuit alleging securities fraud, decides to take some "paid leave with no end date." Perhaps, a little humility therapy could be carved into our vacation plans!
- New York-based Citigroup reports a net income of \$4.43 billion (U.S.) in the 1st. quarter, following a loss of \$7.58 billion (U.S.) in the 4th. quarter of 2009, citing a 16% decline in loan losses to \$8.37 billion (U.S.)
- Goldman Sachs is under pressure on four fronts, as it fights to limit the fallout from the fraud charges laid by the Securities and Exchange Commission on Friday. According to the Times of London, clients protested about the bank's behavior, British and German regulators launched investigations into its activities and American lawyers attempted to solicit investor interest in class action suits. Moreover, Goldman faces the loss of lucrative British Government work, including a host of planned privatizations, after Prime Minister Gordon Brown described the bank as "morally bankrupt."

TUESDAY, APRIL 20TH

- The Reserve Bank of India raises two benchmark short-term interest rates by 25 basis points: the repo rate at which it lends to commercial banks to 5.25%; and the reverse repo rate for which it pays banks for deposits to 3.75%

- The Bank of Canada leaves the Bank Rate unchanged at 0.25%, as Governor Mark Carney commented: “Despite recent (economic) progress (in Canada), considerable uncertainty remains about the durability of the global (economic) recovery. The persistent strength of the Canadian dollar, Canada’s meager gains in labour productivity and weak (economic) demand from the crucial U.S. market, will continue to act as significant drags on the (Canadian) economy. The extent and timing of (any administered) interest rate hikes will depend upon the outlook for (the country’s economic) growth and (the) inflation (rate).”
 - A report by the Securities and Exchange Commission’s inspector-general reveals that Spencer Barasch, a lawyer and former SEC director of enforcement in Fort Worth, Texas, repeatedly blocked investigations of Allen Stanford, the financier charged with defrauding investors of \$7 billion (U.S.), before leaving the SEC in 2005 to work for Mr. Stanford. The report found that the SEC’s Fort Worth examination group conducted investigations of Mr. Stanford in 1997, 1998, 2002 and 2004, concluding in each case that he was likely to be operating a ponzi scheme. Mr. Stanford was not charged until 2009.
 - Goldman Sachs Group reports a net profit of \$3.3 billion (U.S.) in the 1st. quarter, compared with a net income of \$1.66 billion (U.S.) in the same period a year ago. In a separate news release, as a result of the securities fraud charge against Goldman, the Financial Services Authority (FSA) announces that it will undertake a formal review of Goldman’s London-based units, to determine whether a full investigation into the operations of the bank is warranted.
 - The International Monetary Fund (IMF) Global Financial Stability Report warns: “The (economic) crisis has led to a deteriorating trajectory for debt burdens and sharply higher sovereign risk. Vulnerabilities now increasingly emanate from concerns over the sustainability of governments’ balance sheets. The recent turmoil in the euro zone has demonstrated how weak fiscal fundamentals coupled with underlying vulnerabilities can manifest themselves as short-term financing strains. Countries with outsized deficits and an unsustainable debt trajectory” that rely upon foreign bond investors, can experience a quick expiration of financing timelines. The report stated there was a risk of financing “standoffs, as bond investors demand higher yields” from defiant states. This could invite “an unresolved solvency crisis,” a veiled warning that some rich countries may also default. (See also Winter Warning, January 11, 2010 – It’s The Debt, Stupid)
 - In testimony before the House Committee on Financial Services, Securities and Exchange Commission Chairwoman Mary Shapiro states the SEC is examining whether any of the 19 largest U.S. banks are using an accounting maneuver, known as Repo 105, that banking examiner Anton Valukas determined, led to the collapse of Lehman Brothers in September, 2008. The committee is probing the bankruptcy examiner’s report that revealed Lehman hid \$50 billion (U.S.) in debt.
 - Goldman Sachs deregisters the U.K. securities license of Fabrice Tourre, the “fabulous one,” under the jurisdiction of the Financial Services Authority in London. Mr. Tourre, currently on an extended holiday, was recently named at the center of an SEC lawsuit accusing Goldman Sachs of securities fraud.
- ### WEDNESDAY, APRIL 21ST
- According to Bloomberg News, Goldman Sachs Chief Executive Officer Lloyd Blankfein and Executive Director Fabrice Tourre, the “fabulous one”, will testify before the Senate Permanent Sub-Committee on Investigations on Tuesday, April 27th. at a hearing which will focus on the role of investment banks during the financial crisis
 - UK unemployment hits 2.5 million mark, which is 8% of the workforce and a 16 year high.
 - In its most recent World Economic Outlook report, the International Monetary Fund lowers its GDP growth forecast for the United Kingdom to 2.5% for 2011 from a previously forecast rate of 2.7% citing: “In the United Kingdom, the (economic) recovery is projected to continue at a moderate pace, with previous sterling depreciation bolstering net exports, even as domestic demand likely remains subdued.”
 - In Athens, the Greek government commences two weeks of talks with European Union officials, the European Central Bank and the International Monetary Fund, focusing on additional deficit cutting measures Greece must accept as a condition to access emergency loans. Greece’s finance minister, George Papaconstantinou, hints that Greece could activate a 45 billion euro (\$60 billion U.S.) emergency aid package before meetings regarding conditions for the loans conclude. Meanwhile, the yield on outstanding Greek 10-year bonds has soared to 8.25%, representing a spread of 555 basis points over comparable German bunds.



Sources: OECD; HSBC; High Frequency Economics; Thomson Reuters

- German public sector bank Landesbank Bayern LB severs its business ties with Goldman Sachs, citing the Securities and Exchange Commission's allegation that the dominant Wall Street bank committed securities fraud

THURSDAY, APRIL 22ND

- Moody's Investors Service downgrades Greece's sovereign debt rating to A3 from A2, citing "a significant risk that debt may only stabilize at a higher and more costly level than previously expected". Rival agencies rate Greece significantly lower, with Standard & Poors having cut its rating to 'BBB' (High) in December and Fitch to 'BBB' (Low) on April 9th. Moody's senior analyst for Greece, Sarah Carlson, stated: "It is unlikely that the (sovereign debt) rating will remain at A3, unless the government's actions can restore confidence in the markets and counteract the prevailing headwinds of high interest rates and low growth that could ultimately undermine the government's ability to sustainably cut debt levels."

- The National Association of Realtors reports U.S. home sales rose by 6.8% to a seasonally adjusted annual rate of 5.35 million units in March. Sales in February were downwardly revised to 5.01 million units.
- Amazon.com Inc. reports earnings of \$299 million (U.S.) in the 1st. quarter ended March 31st. compared to a profit of \$177 million in the 1st. quarter of 2009
- Eurostat, the European Union's statistics agency, increases its estimate of Greece's 2009 budget deficit to 13.6% of its gross domestic product (GDP), somewhat higher than the Greek government's recent estimate of 12.9%. In the meantime, Greek bond yields continued to soar, with the 2-year bond yield climbing to 11.60% and the 10-year maturity reaching 9.14%.
- Microsoft Corp. reports a net profit of \$4 billion (U.S.) in its 3rd. fiscal quarter ended March 31st. compared to a profit of \$3 billion (U.S.) in the same period a year ago, citing strong sales of its Windows 7 software

FRIDAY, APRIL 23RD

- The Commerce Department reports U.S. durable goods orders, excluding transportation, increased by 2.8% in March, citing higher demand for computers, machinery, metals, electrical equipment and automobiles
- Greek Prime Minister George Papandreou formally asks for the activation of a European Union (EU) / International Monetary Fund (IMF) aid package totaling upwards of 40 billion euros by May 19th., basically, admitting that Greece can no longer afford to market debt issues on its own accord. In the secondary market, the yield on outstanding 2-year Greek bonds declined to 10%. Complicating the situation however, is a report from Reuters News Agency that Germany's main opposition Social Democratic party (SPD) does not want to hasten any legislation that might result in Germany issuing guarantees for billions of euros worth of aid. SPD budget spokesman, Carsten Schneider commented: "We won't go along with this. First the government can't decide what they want to do and now they want to put us under pressure with the legislative process."
- The Commerce Department reports new home sales in the U.S. rose by 26.9% (411,000 units annualized) in March, compared with a revised decline of 4.1% (324,000 units annualized) in February, as buyers sought to beat the expiration of the first-time home buyer tax credit of \$8,000 (U.S.) on April 30th.

- The Federal Deposit Insurance Corporation (FDIC) closes seven banks in the State of Illinois, bringing the number of U.S. bank failures to 57 so far this year
- Canadian retail sales rose by 0.5% in February compared to January
- According to the Wall Street Journal, Goldman Sachs' strategy for winning business in Germany is being rejected by German officials, corporations and banks. Goldman's most recent battle is a dispute with the City of Berlin, which has accused Goldman of trying to intimidate it with legal threats, in order to make more profit from a municipal housing underwriting. After months of negotiations over Goldman's proposal to underwrite an initial public offering for a company that owns municipal housing, Mr. Ulrich Nussbaum, Berlin's chief financial officer, stated: "I would not deal with this bank again unless I couldn't (possibly) avoid it." So, now we see Goldman bullying and intimidating government underwriting clients in the pursuit of profit. Is there no limit to the depths this bank will stoop for the love of money?
- Statistics Canada reports the consumer price index declined slightly in March to an annual rate of 1.4%, compared to 1.6% recorded in February. Core inflation, which excludes food and energy, declined by 0.4% to an annual rate of 1.7%.
- In testimony before the Senate Permanent Sub-Committee on Investigations, former executives at Moody's and Standard & Poors confirmed that competitive pressures and conflicts of interest were enabled to obdurate accurate, fair and unbiased ratings of complex investment securities that Wall Street firms marketed to investors. Eric Kolchinsky, a former managing director at Moody's, who in 2007 oversaw the ratings of collateralized debt obligations (CDOs), commented: "The incentives in the market for rating agency services favoured, and still favour, short-term profits over credit quality. It was an unspoken understanding that loss of market share would cause a manager to lose his or her job." Mr. Kolchinsky was suspended, after warning in September 2007, that a selection of securities "being hyper-aggressively pushed by the bankers" had been given a rating that was too high because it was based upon a 2006 ratings model that was about to be downgraded. Mr. Kolchinsky further stated: "I believe that to assign new ratings based on assumptions which I knew to be wrong would constitute securities fraud." Staff at Moody's and Standard & Poors described a tense relationship with investment banks, which put pressure on the rating agencies to deliver 'AAA' ratings. Most lawsuits against rating agencies in the U.S. have failed because the courts have deemed their ratings are an "opinion" and therefore, are protected as free speech. At Longwave Analytics, we believe this could be about to change, however, as the truth is uncovered that in many cases, U.S. rating agencies assigned premeditated higher ratings on various investment products than warranted, due to pressure from investment banks. Therefore, many ratings allocated to securitized products in the past were merely "stated false opinions" and not the agencies' "true opinions."

Big Banks

Investment banking revenue in Germany, 2009, in millions

| | |
|--------------------|---------|
| Deutsche Bank* | \$352.4 |
| Goldman Sachs | 196.3 |
| Commerzbank Group* | 161.4 |
| Credit Suisse | 159.0 |
| J.P. Morgan | 158.1 |
| Morgan Stanley | 141.2 |
| UBS | 122.8 |
| UniCredit Group | 110.7 |
| RBS | 105.1 |
| BNP Paribas | 99.0 |

*Banks with German headquarters

Source: Dealogic

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"Those who cannot remember the past are condemned to repeat it." Santayana