

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

# THAT WAS THE WEEK THAT WAS



## Monday, May 31ST

The Commerce Department reports U.S. consumer spending was flat in April, citing the weakest level in seven months; as personal income rose by 0.4% and the personal savings rate increased to 3.6% from 3.1% in March

### MONDAY, MAY 31ST

Memorial Day - U.S. Holiday

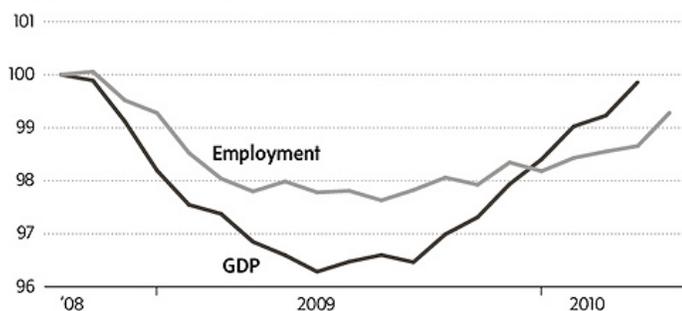
- Fitch Ratings downgrades Spain's sovereign debt rating to 'AA' (High) from 'AAA' citing the country's economic recovery would be more muted than the government's forecast, due to strict austerity measures passed last week. The downgrade applies more pressure on the Spanish government, which is struggling to reassure the fixed income market that its fiscal, political and social problems will not result in another European Central Bank / International Monetary Fund financial rescue package.
- The Ministry of Economy, Trade and Industry (METI) reports Japanese industrial output rose by a seasonally adjusted 1.3% in April from March. Manufacturers polled by METI expect their orders to climb by 0.4% in May and a 0.3% in June.
- Spain's financially stressed savings banks, under pressure from the central bank for resisting rationalization, are hastening to announce mergers and cooperation agreements, before the government's offer of consolidation assistance expires on June 30th. Caja Madrid, the second largest of Spain's unlisted savings banks (cajas de ahorros), is in talks with five small cajas from different parts of Spain, regarding a "cold fusion deal." By creating a Sistema Institucional de Proteccion, the six would merge treasury operations and some specific central functions, but would retain their own brands and local structures.
- In comments to Parisian television stations, France's budget minister Francois Baroin, admitted that while maintaining the country's 'AAA' sovereign debt rating would be a "stretch," the government is committed to this "demanding" target
- In a weekend newspaper interview, Greece's Finance Minister George Papaconstantinou confirmed the country has no plans to restructure its massive sovereign debt and perceives no necessity to adopt new austerity measures to meet its budget targets. Mr. Papaconstantinou postulated: "A renegotiation (of our national debt) would be catastrophic for the credibility of Greece. It would lead to the effective marginalization of the country from the markets. It would require even bigger spending cuts and a very deep recession."
- Canada's Department of Finance reports in its Fiscal Monitor that the federal budget deficit for the year ended March 31, 2010 totaled \$47 billion (CAD), about \$6.8 billion (CAD) less than the \$53.6 billion (CAD) forecast in the budget of last March. The Department estimates "\$19 billion (CAD) of the \$47 billion (CAD) deficit was attributable to actions taken under Canada's Economic Action Plan."
- Statistics Canada (Statscan) reports the country's seasonally adjusted deficit in current transactions with other countries narrowed to \$7.8 billion (CAD) from \$10.2 billion (CAD) in the 4th. quarter of 2009, citing an increased "trade in goods" surplus and a reduced deficit in international travel. Statscan noted: "Cross-border (U.S.) financial transactions generated continued inflows of foreign funds to the Canadian economy, although less than the previous quarter, but were again led by purchases of Canadian (investment) securities. Non-residents have made large acquisitions of Canadian (investment) securities since the outset of 2009, mainly (in the form of) longer-term debt instruments."

- Statistics Canada reports the country's gross domestic product (GDP) rose by 6.1% in the 1st. quarter, following a revised growth rate of 4.9% in the 4th. quarter of 2009, citing a buoyant housing market, a rebounding manufacturing sector, improving personal incomes and a stronger level of business hiring.

### Canadian employment and output

**The Canadian economy was just 0.4 per cent below its pre-recession levels in the first quarter, signalling GDP is on the brink of expansion, though employment levels still have further to go.**

INDEX SEPTEMBER 2008=100



THE GLOBE AND MAIL | SOURCE: STATISTICS CANADA

- Canadian Finance Minister Jim Flaherty unveils the federal government's proposed legislation for a national securities regulator, empowering the Canadian Securities Regulatory Authority (CSRA) to investigate securities-related crimes. The CSRA would be a crown corporation governed by a board of directors appointed by the federal cabinet. It would be comprised of two divisions accountable to Parliament through the minister of finance. One would be a regulatory division led by the chief regulator who would be its chief executive officer. The second division would be a separate Canadian Securities Tribunal, led by a chief adjudicator, which would conduct hearings of enforcement cases before the commission. Despite the voluntary membership structure of the CSRA, the Provinces of Quebec and Alberta have repeated their determination to legally contest the federal government in its effort to secure a Supreme Court ruling that it has the constitutional authority to adopt the new securities regulator legislation.

### TUESDAY, JUNE 1ST

- Eurostat reports the unemployment rate in the 16-nation euro zone rose to 10.1% in April from 10% in March, citing 25,000 additional people were seeking work in April compared to March; and 1.27 million jobs have disappeared over the last year

- In a regulatory filing, Hewlett-Packard Co., the world's largest personal computer manufacturer, announces 3,000 job layoffs costing \$1 billion (U.S.) and to be implemented before its fiscal year 2013
- The Bank of Canada raises its Bank Rate by 25 basis points to 0.50%, citing the country's recent economic growth rate and inflation rate have been "largely as expected" while the global economic recovery "is increasingly uneven." In a prepared statement, central bank Governor Mark Carney commented: "Given the considerable amount of uncertainty surrounding the (economic) outlook, any further reduction of monetary stimulus would have to be weighed carefully against domestic and global economic developments."
- The Bank of Nova Scotia reports a net profit of \$1.1 billion (CAD) in the 2nd. fiscal quarter ended April 30th. citing higher returns from residential mortgages and record earnings from its Canadian retail banking sector. In a statement, Scotiabank chief executive officer Rick Waugh commented: "Our (earnings) results reflect strong contributions from personal and commercial banking and wealth management; as well as the excellent performance of our whole business."
- The Institute for Supply Management (ISM) reports its U.S. manufacturing index declined to a reading of 59.7 in May from a level of 60.4 in April
- The Commerce Department reports U.S. construction spending rose by 2.7% in April to a seasonally adjusted annual rate of \$869.09 billion (U.S.) compared to March
- The purchasing managers' index (PMI) published by China's logistics federation declined to a reading of 53.7 in May from a level of 53.9 in April; while the PMI published by the Hong Kong and Shanghai Bank (HSBC) fell to a revised reading of 52.7 in May from a revised level of 55.2 in April
- The commercial arm of Dubai Holding, the conglomerate owned by Sheikh Mohammed bin Rashid Al Maktoum (the emirate's ruler) reports a net loss of \$6.2 billion (U.S.) for 2009, citing declining real estate sales and project delays; as the group holds talks with banks to refinance a \$555 million (U.S.) loan due in July
- The Reserve Bank of Australia (RBA) leaves its key lending rate unchanged at 4.5%

## WEDNESDAY, JUNE 2ND

- The German government widens the ban on speculative trades, by expanding restrictions on naked short selling to include all shares. The planned legislation, which must pass both houses of parliament, adds to regulations established in May, in an initiative of Angela Merkel's government to curtail financial speculation, which it blames for intensifying the euro zone debt crisis.
- Every major automaker, except Toyota Motor, reports an increase in new vehicle sales in the U.S. of at least 17.5% in May. In contrast, Toyota's sales rose by only 6.7%, a sign that the company was still struggling to overcome its recalls of more than eight million vehicles, to resolve a problem regarding unintended car acceleration. In a conference call briefing, Steve Carlisle, General Motors Vice President of U.S. sales operations, noted: "We're a much leaner and more nimble company that can take advantage of these shifts in consumer tastes as they occur. We've moved from our back foot to our front foot in terms of competitiveness, and have started to play some pretty good offense."
- Appearing before a U.S. Financial Crisis Inquiry Commission (FCIC) hearing on credit ratings in New York, Moody's Corp. chief executive officer Raymond McDaniel stated: "The performance of our credit ratings for U.S. residential mortgage-backed securities and related collateralized debt obligations (CDOs) over the past several years, has been deeply disappointing. Moody's is certainly not satisfied with the performance of these ratings." FCIC Chairman, Phil Angelides remarked: "To be blunt, the picture is not pretty. (While) Moody's did very well; the investors who relied upon Moody's ratings did not do so well." Citing Moody's assignation of 'AAA' ratings to 42,625 residential mortgage-backed securities between 2000 and 2007, Chairman Angelides stated: "In 2006 alone, Moody's gave 9,029 mortgage-backed securities a 'AAA' rating. To put that in perspective, Moody's currently bestows its 'AAA' rating on just four American corporations." Eric Kolchinsky, a former Moody's employee, has accused the company of violating securities laws by knowingly providing "incorrect" ratings; but Moody's has denied his claim. Moody's awarding 'AAA' credit ratings to 42,625 residential mortgage backed securities when only four U. S. companies have this rating, is the ultimate rating absurdity.
- The partially-nationalized Royal Bank of Scotland announces 500 job layoffs over the next three years in its wealth management division of Coutts and Adam & Co. – the banker to Her Majesty the Queen
- London-based BP PLC (formerly British Petroleum), the world's fourth largest public corporation has already suffered a stunning 40% loss of market capitalization, since the April 20th. deep water well blowout in the Gulf of Mexico. Following a tour of the oil-stained coastline of Louisiana, U.S. Attorney General Eric Holder announces he has opened civil and criminal investigations into the well blowout, which could result in years of court battles and crippling fines for BP. According to Credit Suisse, BP's final cost for the continuing oil leak disaster could reach a staggering \$37 billion (U.S.).
- The National Association of Realtors' reports its index for pending U.S. sales of used homes rose by 6% to a reading of 110.9 in April, as first-time home buyers raced to beat the April 30th. deadline for the expiration of the \$8,000 (U.S.) tax credit.
- Japanese Prime Minister Yukio Hatoyama resigns his post, under pressure from colleagues within his party. Mr. Hatoyama's brief term was tainted by failed campaign pledges and a scandal over election (scheduled for July) fundraising.
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## THURSDAY, JUNE 3RD

- Recent statements from the U.S. Internal Revenue Service (IRS) have cast doubt regarding a federal government subsidy of 35% for interest costs (coupon rates) for municipal issuers of Build America Bonds (BABs). Under this U.S. Government stimulus program, these bond issues were designed to encourage construction and infrastructure projects and create jobs. The BABs program has been popular since its introduction in April 2009, accounting for almost a third of all municipal bonds that have been issued. However, the IRS is concerned that many BABs issues were wrongly priced, citing it has opened audits on 10 issues.

- The Bank of Nova Scotia issues \$1 billion (CAD) of 7-year bonds at a 102 basis point yield spread over comparable Government of Canada bonds; while the Province of Quebec raises \$500 million (CAD) by re-opening a 10-year note issue bearing a 4.5% coupon

FRIDAY, JUNE 4TH

- The EEF manufacturing organization reports the U.K. Index of manufacturing output rose to a reading of 30 at the end of May from a level of 5 in March, citing a sharp upturn in domestic orders, as well as exports
- Hungarian Prime Minister Viktor Orban's press aide comments that the country is experiencing a debt crisis similar to that being experienced by Greece, reigniting concerns that Europe's financial problems, not only, are far from contained, but also, are pressuring the euro lower in value versus the U.S. dollar



- Mike Neal, chief executive officer of GE Capital, announces the company plans a 50% reduction to \$40 billion (U.S.) in its commercial real estate holdings, such as office and apartment buildings, and shift its portfolio composition more toward real estate loans (mortgages) and away from direct ownership stakes
- In a Wall Street Journal op/ed, Arthur Laffer, Chairman of Laffer Associates, states: "On or about January 1, 2011, federal, state and local taxes are scheduled to rise quite sharply, as former President George W. Bush's tax cuts expire, meaning that the highest federal personal income tax rate will rise from 35% to 39.6%; the highest federal dividend tax rate jumps from 15% to 39.6%; the capital gains tax rate increases by a third from 15% to 20% and the estate tax rate is introduced at 55%. Tax rate increases next year are everywhere and my best guess is that the train goes off the tracks and we get our worst nightmare of a severe 'double dip' recession. The economy will collapse in 2011 and if you thought that deficits and unemployment have been bad lately, you ain't seen nothing yet." At Long Wave Analytics, we agree with Mr. Laffer's short-term economic outlook for America. For our mid-term to long-term economic outlook, see Winter Warning, January 11, 2010 – It's the Debt, Stupid.
- The Department of Labor reports U.S. non-farm payrolls, net of temporary census hirings, increased by only 41,000 in May. According to Shadow Government Statistics, "increasingly, at work here will be an intensifying economic downturn, as well as some likely catch-up from distortions created by bad quality seasonal factors. The unemployment rate declined to 9.7% in May from 9.9% in April, but to the extent the unemployment rate is moderated by census hires, such too, would reverse in the months ahead, beginning with a sharp reversal in June."

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