

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



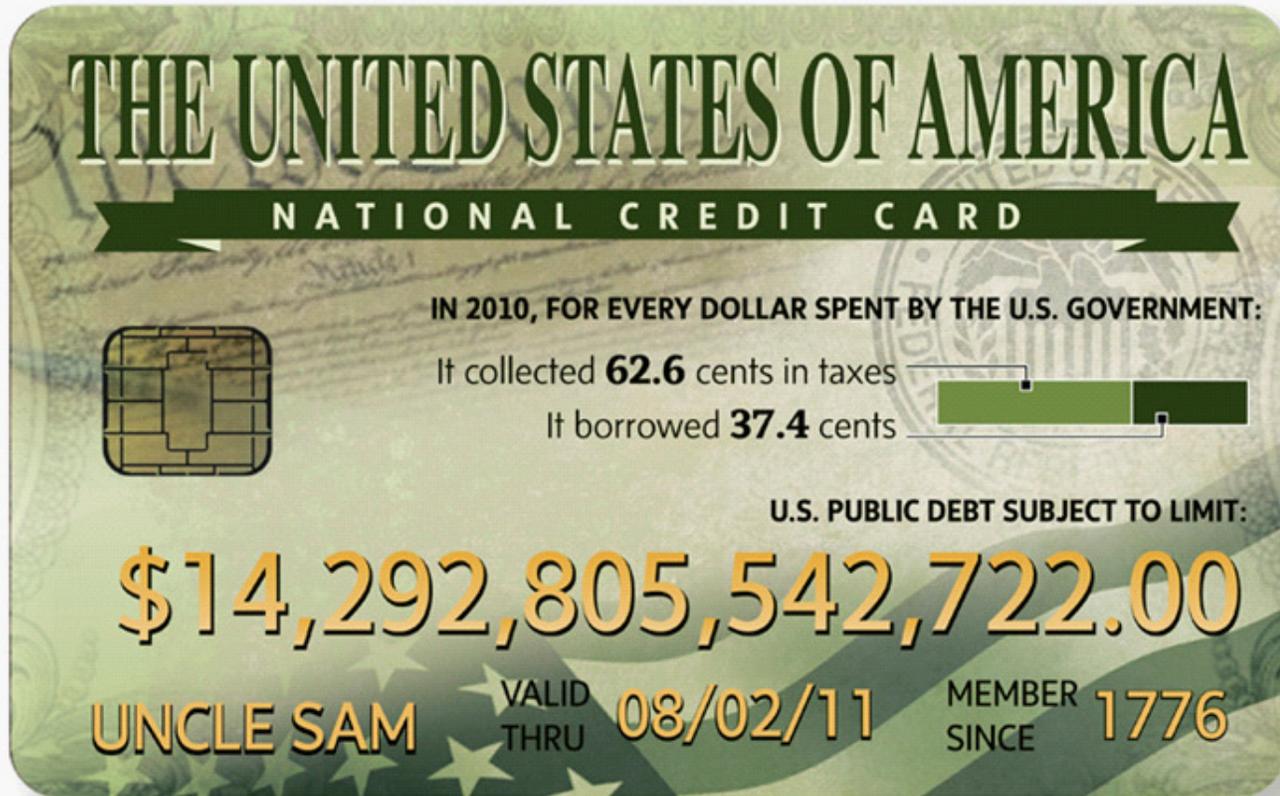
Monday, July 25th

Research in Motion (RIM) announces 2,000 job layoffs, 10.5% of its work force, reacting to the declining popularity of the Blackberry line of smartphones. RIM also announced the retirement of Don Morrison as Chief Operating Officer.

MONDAY, JULY 25TH

- Moody's Investors Service downgrades Greece's sovereign debt credit rating to 'Ca' – one level above what it considers to be a default rating, following last week's unveiling of a second European Union (EU) bailout package, citing "substantial losses ('haircuts') implied for private creditors (bondholders). While a Greek debt default is virtually 100% (assured) ... the package of measures could lead to downgrades of creditor countries not rated 'AAA' because of the precedent of future bailouts. For creditors of such countries (Ireland, Portugal), the negatives will outweigh the positives and weigh on (credit) ratings in the future."
- In a prime time national address, American President Barack Obama delivers a statement regarding the political stalemate in the raising of the U.S. statutory debt limit: "If we stay on the current path, our growing debt could cost us jobs and do serious damage to the economy. More of our tax dollars will go toward paying off the interest on our loans. Businesses will be less likely to open up shop and hire workers in a country that can't balance its books. Interest rates could climb for everyone who borrows money: the homeowner with a mortgage, the student with a college loan, the corner store which wants to expand. (Moreover), we won't have enough money to make job-creating investments in things like education and infrastructure, or pay for vital programs like Medicare and Medicaid ... Neither (political) party is blameless for the decisions that led to this problem, (but) both parties have a responsibility to solve it."
- House of Representatives Speaker John Boehner (R.- Ohio) responds to President Obama's statement: "President Obama came to Congress in January and requested business as usual – yet another routine increase in the national debt limit – we in the House said: "Not so fast." Here was the President, asking for the largest debt increase in American history, on the heels of the largest spending binge in American history. Here's what we got for that spending binge: a massive health care bill that most Americans never requested; a stimulus bill that was more effective in producing material for late-night comedians than it was in producing jobs and a national debt that has gotten so out of hand it has sparked a crisis without precedent in my lifetime or yours. The United States cannot default on its debt obligations. The jobs and savings of too many Americans are at stake. What we told the President in January was this: the American people will not accept an increase in the debt limit without significant spending cuts and reforms. Over the last six months, we've done our best to convince the President to partner with us to do something dramatic to change the fiscal trajectory of our country, something that will boost confidence in our economy."

# Put it on the plastic



Debt figure as of 5:30 p.m. Monday

## U.S. FEDERAL SPENDING

Fiscal year 2010 (in billions of U.S. dollars)

**TOTAL:**  
**\$3.456-TRILLION**



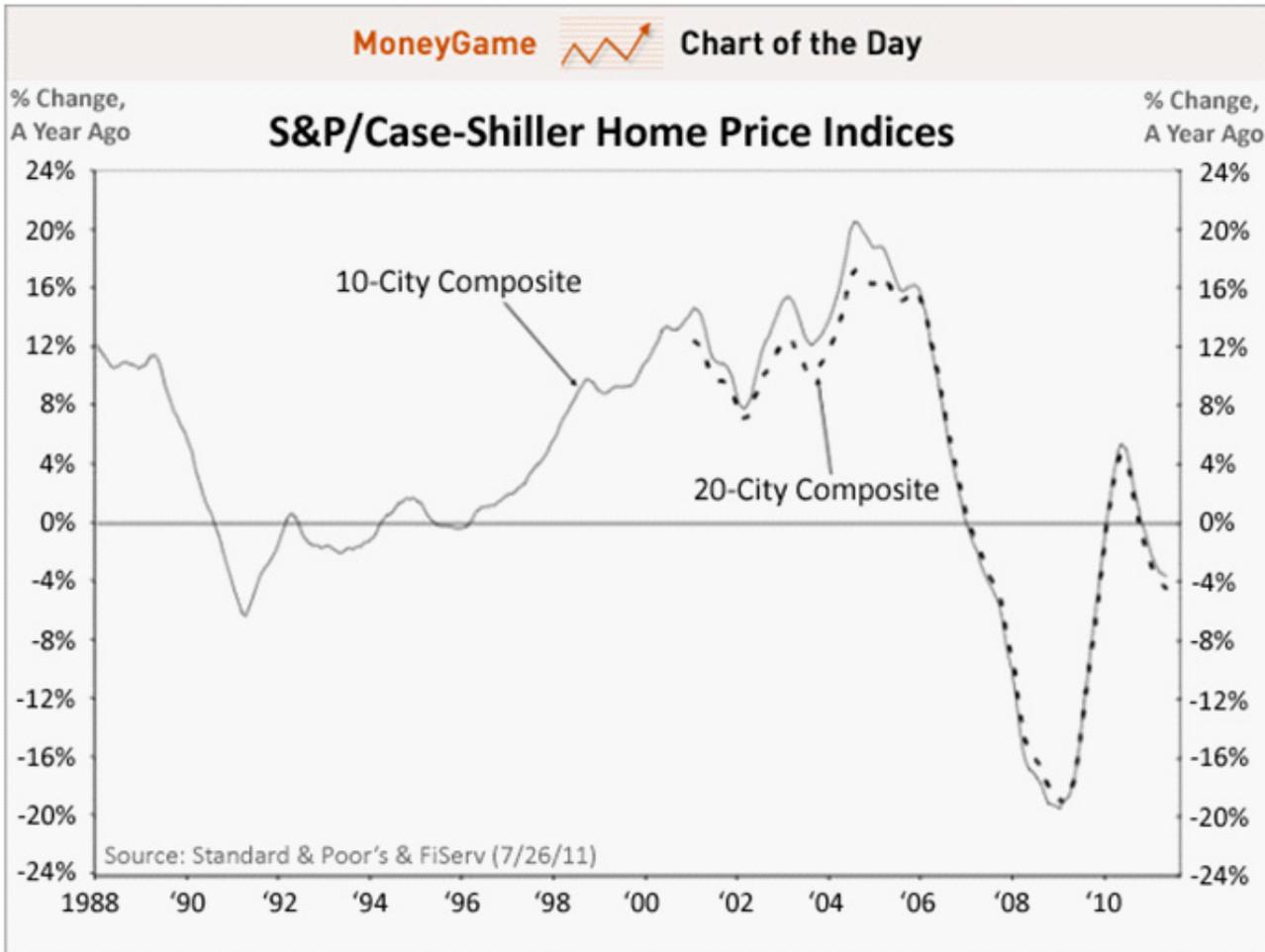
## U.S. TAX RECEIPTS

Fiscal year 2010 (in billions of U.S. dollars)

**TOTAL:**  
**\$2.162-TRILLION**



TUESDAY, JULY 26TH



- The Standard & Poors/Case-Shiller U.S. home price index rose by 1% in May, reflecting price increases in 16 of 20 major cities monitored. The index compares home prices with those of a January 2000 base and then provides a 3-month average. Boston posted the biggest monthly increase, followed closely by Minneapolis and Washington. However, 19 of the 20 cities have registered price declines on a year-over-year basis.
- The Commerce Department reports new U.S. single-family home sales declined by 1% in June to a seasonally adjusted 312,000 annual rate, following a downwardly revised sales pace of 315,000 in May, previously reported as 319,000
- As reported in the Financial Times, U.S. President Barack Obama has urged congressional leaders to reach a “fair compromise” over the next few days to avoid a U.S. debt default and attacked a new Republican plan to increase the country’s statutory debt limit in two steps as “no way to run the greatest country on earth.” President Obama stated the Republican approach might still lead to a downgrade of the country’s ‘AAA’ sovereign debt credit rating. “It would not solve the problem of the country’s rising debt levels and would force a repetition of the brinkmanship that has unfolded over the past few months ... We can’t allow the American people to become collateral damage to Washington’s political warfare.”

## Policy Changes Under Two Presidents FIGURES IN BILLIONS

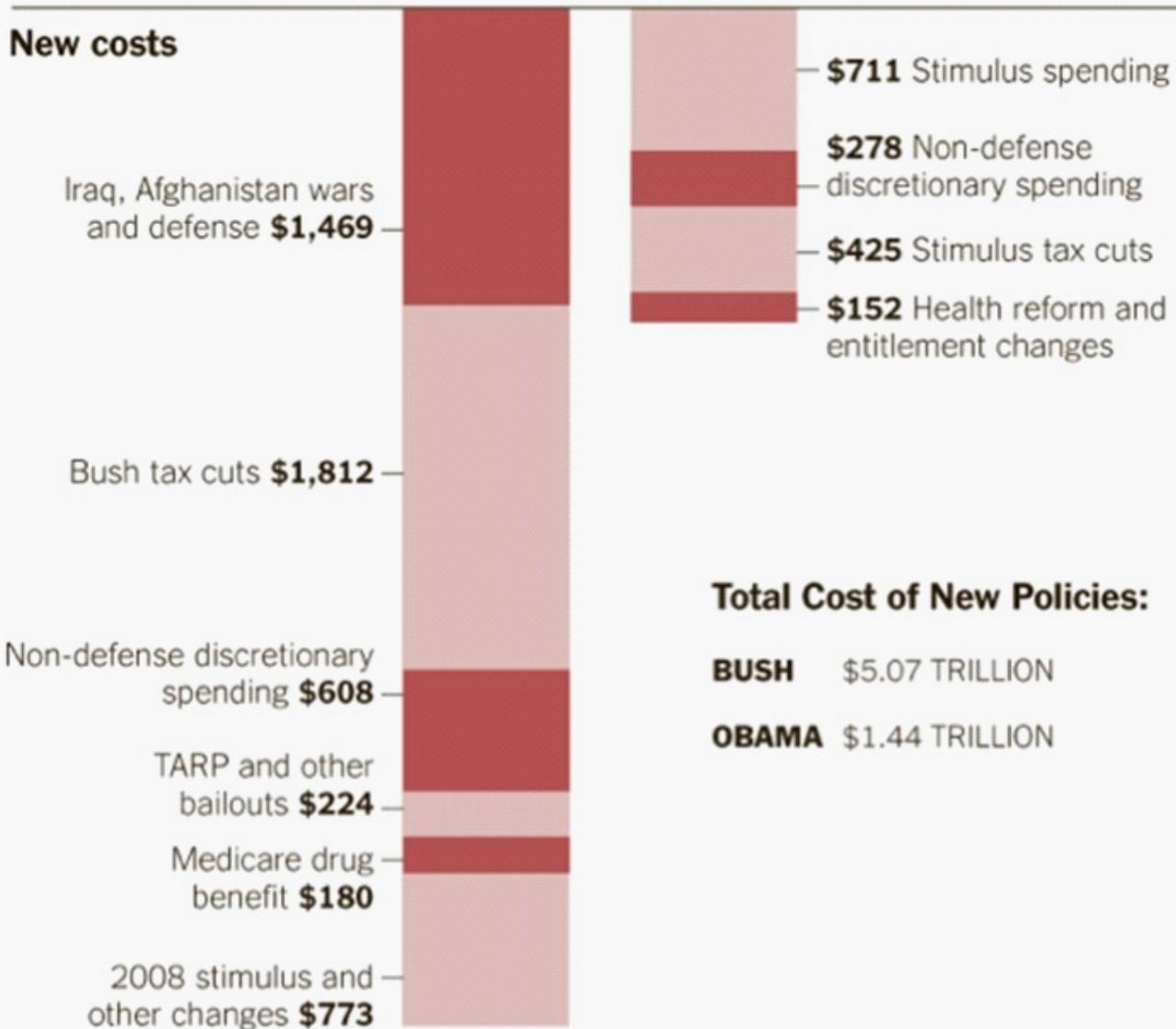
### Savings

**\$126** Defense

**BUSH**  
F.Y. 2002-09

**OBAMA**  
F.Y. 2009-17  
(incl. projections)

### New costs



### WEDNESDAY, JULY 27TH

- The Federal Reserve's Beige Book, based upon economic information compiled prior to July 15th, reports: "Economic growth has slowed in a majority of districts, particularly those nearest the Atlantic seaboard, with the Minneapolis district hurt by the now concluded state government shutdown." This represents a slightly worse result than the June 8th. Beige Book when seven districts reported economic growth at a steady pace.
- The Commerce Department reports U.S. durable goods (meant to last at least 3 years) orders declined by 2.1% in June, following a 1.9% increase in May, citing reduced demand for business equipment, including machinery and computers
- Standard & Poors (S&P) downgrades Greece's sovereign debt credit rating from 'CCC' to 'CC' with a negative outlook, citing the European Union's (EU) proposed debt restructuring as a "distressed exchange" that would place Greece into a "selective default ... In our opinion, the terms of both the exchange and rollover options appear unfavourable to investors. Under our criteria, we characterize a distressed borrower as one that would – in the absence of debt relief – fail to pay its debt on time and in full. The probability of a future default on any new securities is likely to remain high ... We anticipate that we would assign a low speculative-grade credit rating to Greece, given our view that Greece will likely to be burdened by high debt to gross domestic product (GDP) of just under 130% at the end of 2011 and uncertain (economic) growth prospects even after the debt restructuring is concluded."

### THURSDAY, JULY 28TH

- Moody's Investors Service affirms Canada's 'AAA' sovereign debt credit rating citing: "Ottawa and the provinces are on a track of fiscal consolidation and their debt loads will improve over the next few years. Since the provinces also enjoy high credit ratings, the risk they pose to Ottawa's budget is deemed low, even though their (individual) debt loads are relatively large ... (One of) the main risks to Canada's (economic) outlook is the share of residential mortgages backed by Ottawa through the (crown corporation) Canada Mortgage and Housing Corp. (CMHC). A major downturn in home prices could hurt the federal government's balance sheet ... As a large and diversified economy with a stable political system and strong regulatory framework, Canada has a low susceptibility to event risk. Natural resource industries, a competitive manufacturing sector, a well-developed and well-regulated financial market and Canadians' high per-capita income also support the country's resiliency."

- The Labor Department reports U.S. initial claims for state unemployment benefits declined by 24,000 to 398,000 in the week ended July 23rd. from an upwardly revised 422,000, previously reported as 418,000. The number of continuing unemployment benefit claims – those drawn by workers for more than a week – fell by about 17,000 to 3,703,000 in the week ended July 16th.
- Credit Suisse Group announces 2,000 job layoffs, 4% of its work force, citing a 50% decline in 2nd. quarter profits, a strong Swiss franc and lower trading revenues
- Italy successfully issues 2.7 billion euros of 10-year bonds at an average yield of 5.77%, up 83 basis points from the previous auction a month ago. Analysts at Forex.com commented: "Contagion is well and truly in the air. Both Italian and Spanish bond yields have risen sharply and are close to the highs reached last week, which suggests upon reflection, that the credit markets are not convinced with the EU's latest deal."
- According to the Health Affairs journal, the U.S. Medicare Office of the Actuary reports the nation's health care bill is on track to reach \$4.6 trillion (U.S.) by 2020. Including government and private money, health care spending will average \$13,710 (U.S.) for every man, woman and child ... Government, which already has a dominant presence because of Medicare and Medicaid, will become increasingly important. By 2020, federal, state and local government health care spending will account for about half the total bill, up from the current 45%. The report stated: "As the health care law's coverage expansion takes effect, health care financing is expected to further shift towards governments."

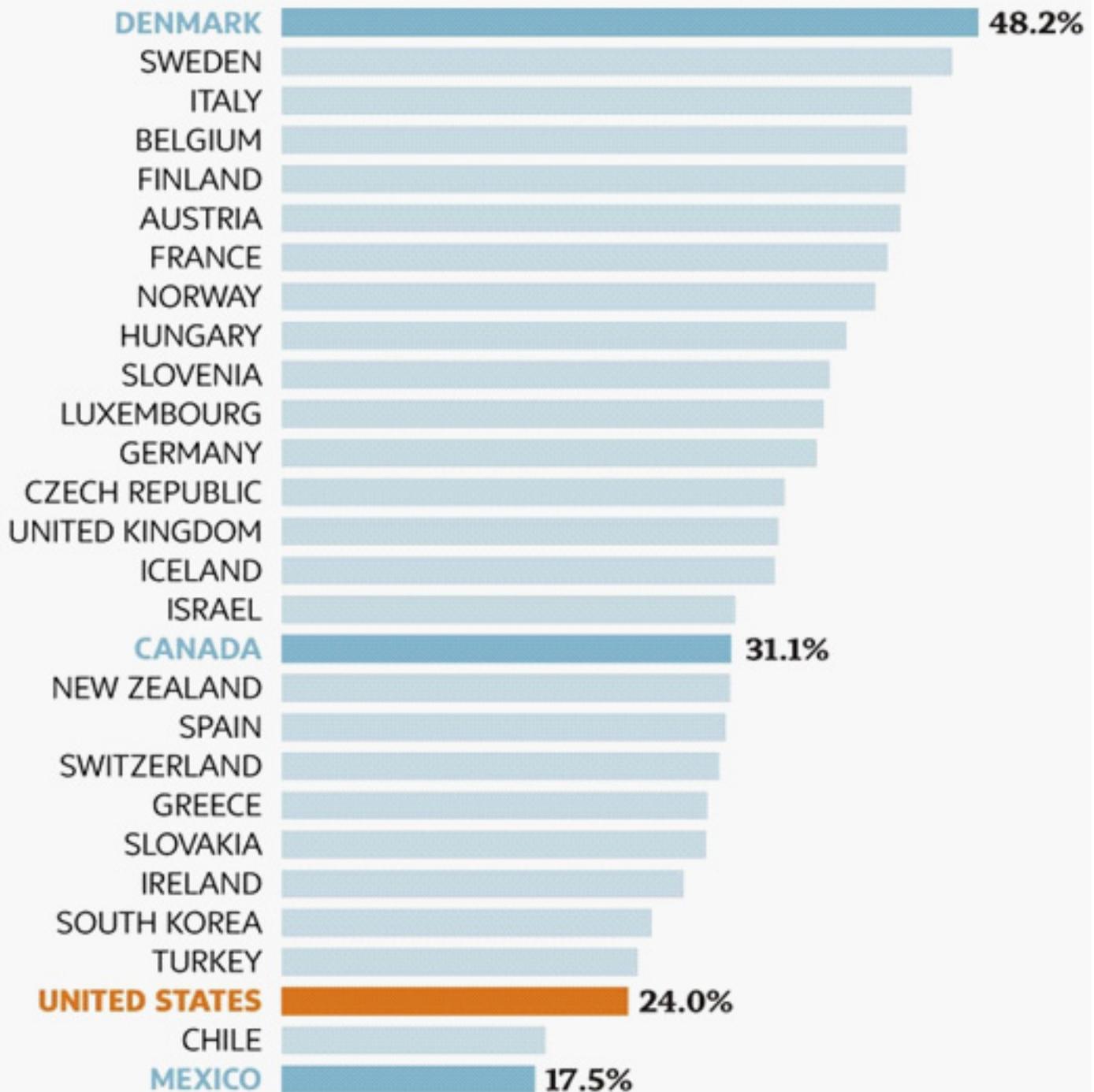
### FRIDAY, JULY 29TH

- Moody's Investors Service places Spain's 'Aa2' sovereign debt credit rating on credit watch for possible downgrade, citing weak economic growth and funding pressures. Moody's observed: "Funding costs will remain high for the Spanish government in the wake of the Greek (bailout) package which signaled a clear shift in risk for bondholders. That package set a precedent for private sector participation in future sovereign debt restructurings in the euro area. Moody's notes that challenges to long-term budget balance remain, due to Spain's subdued economic growth and fiscal slippage within parts of its regional and local government sector."
- The Federal Statistics Office reports German retail sales rose by 6.3% in June

## FAR BELOW AVERAGE

Americans pay among the lowest taxes in the developed world.

Tax revenue as a percentage of GDP, 2009



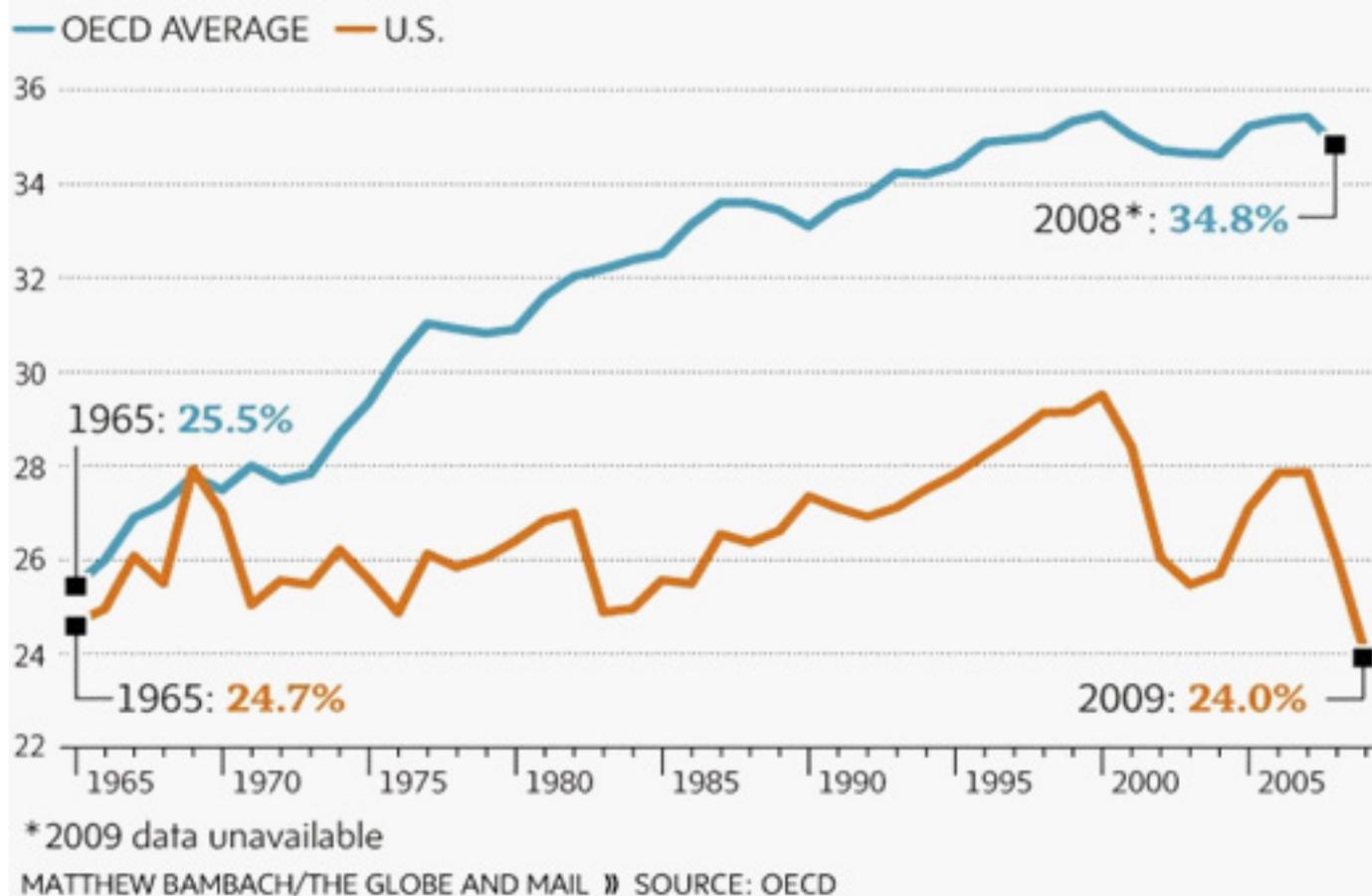
\* 2009 data unavailable

MATTHEW BAMBACH/THE GLOBE AND MAIL » SOURCE: OECD

## BURDEN IN DECLINE

Americans' total tax burden, as a percentage of gross domestic product, is lower than it was in 1965.

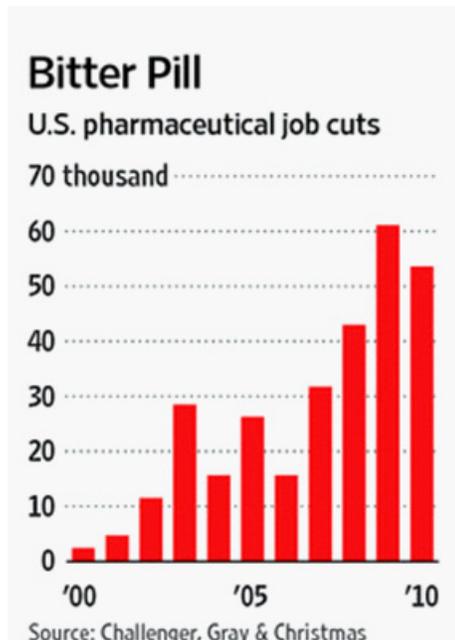
### Tax revenue as a percentage of GDP, 1965-present



- In our Winter Warning of February 14, 2011 – It's Still The Debt, Stupid, in our Summation we warned: "It would appear that many (U.S.) state and local governments with deficit issues have a preference for cutting spending, passing the problem down the line, downsizing their administrations, or, all of the above. Their consummate belief is that economic growth will return in abundance and bail them out of their debt and unemployment problems. We believe this is purely wishful thinking, basically, a pipe-dream. Nowhere in America is there any meaningful support for higher taxes in any form." Now, in a cover story in the Globe and Mail, reporter Barrie McKenna observes: "Tax has become a dirty word in the U.S. (statutory) debt crisis debate. But almost unanimously, experts agree that raising taxes, perhaps

significantly, is key to the country's long-term (financial) salvation ... Contrary to what most Americans believe the United States is one of the least taxed countries in the developed world. (In fact,) they pay much lower taxes than any other G7 country. Among wealthy OECD (Organization for Co-operation and Development) countries, only Chile and Mexico tax their people and companies less ... What foreign investors don't see is the deep-seated opposition of many Americans to tax increases, even at the risk of jeopardizing the country's economic well-being."

- Giant pharmaceutical firm Merck & Co. announces 13,000 job layoffs, about 14% of its work force, in addition to 17,000 job cuts already planned; as well as spending cuts of an additional \$1.3 billion (U.S.) by the end of 2015. The closings of unspecified offices and manufacturing plants are also contributing to the cost savings.
- The Commerce Department reports U.S. gross domestic product (GDP) rose by a 1.3% annual rate in the 2nd. quarter, following a downwardly revised growth rate in the 1st. quarter of 0.4%, previously reported as 1.9%



CLOSING LEVELS FOR JULY 29TH.

WEEKLY CHANGE

Dow Jones Industrial Average	12,143.24	- 537.92 points
Spot Gold Bullion (August)	\$1,628.30 (U.S.)	+ \$26.80 per oz.
S&P / TSX Composite	1,292.28	- 52.74 points
10-Year U.S. Treasury Yield	2.80%	- 16 basis points
Canadian Dollar	104.66 cents (U.S.)	- 0.70 cent
U.S. Dollar Index Future (Spot Price)	73.745 cents	- 0.412 cent
WTI Crude Oil (August)	\$95.70 (U.S.)	- \$ 4.17 per barrel

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