

Weekly Market Commentary

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Overview Another slightly scary week where the US dollar lost ground initially but then clawed its way back to where it started. Cable managed a high at \$1.6664 before being slapped down by politics, the Euro \$1.4339, and best performer the Brazilian real at just 1.9180 per greenback. Eastern European, Baltic states and Scandinavian markets were under a certain amount of pressure, rumours regarding a devaluation of the Latvian currency swirling. FX moves helped many commodities trade higher, most managing to hold on to their gains. Silver led the metals, up at \$16.22 per ounce, closely followed by LME Copper (3-month at \$5140 per tonne), Palladium (263.50 per ounce) and Platinum (\$1293.00). Among foodstuffs Oats, Cocoa and Coffee did best, while Nymex Crude Oil traded up to \$69.60 per barrel and Gasoline \$1.9850 per gallon. Baltic Dry Freight and Capesize indices soared, to 4093 and 7561 respectively and have now retraced 38% of the calamitous declines of the last twelve months. However, ship owners meeting in Athens this week painted a gloomy picture of massive overcapacity, approximately 35% of current bulk tonnage due in new deliveries within the next three years. Note: most of the ships are being built in China, Japan and South Korea, usually with massive government subsidies. Treasury yields backed up further, benchmark US ten-year hit 3.90% and two-year to a new high for this year at 1.215%. This dragged money market futures prices a little lower.

Political and Economic Developments Indonesia trimmed its key interest rate 25 basis points to 7.00%, hinting more were to come. Denmark cut another 20 bp to 1.45%. The eagerly awaited US May employment data caused havoc, lower than expected non-farm payrolls of -345K and the slowest loss of jobs since September, offset by soaring claimant count of 9.4% one of the highest since records began in 1948 (10.8% in November 1982). Eurozone Unemployment surged to 9.2%, almost as high as the record 9.4% of 1999, France's up from 8.0% to 9.1% in just 30 days. Japanese April wages were down 2.5% Y/Y, in negative territory again as they have been for most of the past decade, overtime pay down a whopping -18.8%. Also in negative territory was Taiwan CPI, -0.8% Y/Y and UK Output PPI -0.3% Y/Y, a rare occurrence matching that of June 2002. On a brighter note UK May Nationwide Consumer Confidence at 53 and Services PMI at 51.7 were both above the 50 point which marks the difference between gloom and optimism.

Underlying Themes Bank 'stress tests' carried out by the US Treasury assumed 8.9% Unemployment in 2009 and 10.3% in 2010, so possibly we are already too close for comfort. The US authorities this week are said to have insisted that JPMorgan Chase and American Express raise equity before repaying TARP funds. UK FSA's stress tests assume unemployment at 12.0%, no economic growth until 2011, that house prices halve from the 2007 peak, and commercial property drops 60%; they did not publish their results. Carrying out a similar exercise for the Eurozone is possibly too daunting a task for many, and too embarrassing for some.

What to watch for next week Oh to be a fly on the wall in Orlando Sunday where the American Bankers Association Regulatory Compliance Conference takes place. Monday Eurogroup finance ministers' meeting in Luxembourg, German April Factory Orders, Japan Trade Balance, May Money Supply, Bankruptcies, Economy Watchers' Survey and EZ16 June Sentix Confidence. Tuesday Japan April Leading and Coincident Indices, German Trade Balance and Industrial Production, US Wholesale Inventories, UK DCLG House Prices, May RICS House Price Balance, BRC Retail Sales and Japan Machine Tool Orders. Wednesday Japan April Machine Orders and May Domestic CGPI, UK April Trade Balance and Industrial Production, German WPI, US Trade Balance and May Budget Statement, then late in the day the Fed's Beige Book of economic conditions and the Reserve Bank of New Zealand decides on rates (from unchanged to -50 bp cut from the current 2.50%). Thursday Corpus Christi holidays for a few, Japan final Q1 GDP, US April Business Inventories, May Retail Sales and UK NIESR GDP. Friday (and Saturday) G8 finance ministers meet in Lecce, Italy and a Presidential election in Iran. Eurozone April Industrial Production, Japan May Consumer Confidence, US Import Price Index and June University of Michigan Confidence Survey. Parliamentary election in Lithuania Sunday the 14th.

Positioning and Technical Analysis Volatility, both implied and observed, should increase as markets become more of a two-way street. Generalised US dollar weakness this month will probably be punctured by sharp reversals, these getting bigger as currencies trade higher. The Yen will continue in a world of its own though follow-through to rallies in Yen crosses is certainly not a given, so be very careful with these. Eastern Europe will remain Europe's Achilles heel where unhelpful comments and gross generalisations must be avoided. Slash and burn in the Treasury markets as the back-up in yields continues further and for longer than any had anticipated. The blood-letting must stop, and soon, before it infects other important financial instruments. Have a nice weekend!