

## Weekly Market Commentary

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**Overview** For a change markets didn't bother waiting for today's US Non-Farm Payroll (-20K and Unemployment lurched down to 9.7% in January from 10.0% the previous month); there were bigger fish to fry (see below). To sum up, a good dose of the jitters as we contemplate the scale of the mess we are in and the fact that governments are planning to take back last year's largesse. Again investors rushed into top-rated Treasuries, taking two-year Schatz to a new record low yield of 0.986% (below the ECB's target rate which was kept at 1.00%) and, despite the Bank of England announcing an end to Quantitative Easing, ten-year Gilt yields dipped from 3.960% to 3.842% and the three-year Swap hit a new record low at 2.184%. All commodities traded lower as the US dollar strengthened and allegedly people moved away from so-called 'risky' assets. Interestingly front month CME Lumber soared to \$281.90 per 1,000 board feet, its best since August 2007 and a surprise amid continuing housing woes.

**Political and Economic Developments** Individuals, companies and countries that mis-manage their finances can and will (eventually) be punished by investors. There are many ways to do this and there is probably more to come. First the cost of insurance goes up, so that five-year Credit Default Swaps on Greek, Portuguese and Spanish sovereign bonds all set new records at 444, 238 and 182 basis points respectively. Yield premia over quality (read German) ten-year government bonds widened this week, Greece just under the record high at 368 basis points, Spain at 100 just 25 basis points shy of the peak in Q1 2009, Portugal matching it at 163. Next currencies get sold, this week the Euro losing ground against many (low \$1.3650), but also Eastern European ones hit a little as well as those that had been last year's darlings, among them the Australian dollar (\$0.8620), Brazilian real (1.8910) and Chilean peso (550). Winning hands down has been the Yen (88.55) and to a lesser extent the Swiss franc which at 1.4550 to the Euro is at levels where the Swiss National Bank intervened in March 2009. All of the above is then rounded off by selling stocks, hardest hit Spain's Ibox index (-16% year-to-date), Athens Composite -14% and Italy's MIB -10%. Needless to say those which rallied most last year have potentially the furthest to slip, explaining the Hang Seng's -10%, Mumbai's and Bovespa's -7%.

**Underlying Themes** GMAC, now US government-owned, managed to rack up a \$5B loss in Q4 alone mainly on mortgages going sour. Bank of America's ex-CEO Ken Lewis, who accepted \$20B of TARP money weeks before unveiling \$16B Q4 2008 losses at Merrill Lynch, is being sued for fraud by New York's Sate attorney along with CFO Joe Price. Government Sponsored Enterprises (and government owned for over a year) Fannie Mae and Freddie Mac, at the epicentre of the sub-prime mortgage mess, are 'a huge issue that we're being silent on right now which I think is a very big mistake' said Bob Corker of the Senate Finance Committee. So far and still counting these two have sucked \$111B from the Treasury. Do we really want more government initiatives for banking?

**What to watch for next week** Monday Japan December Trade Balance, January Money Supply and Bank Lending, Bankruptcies and Economy Watchers' Survey, plus EZ16 February Sentix Investor Confidence. Tuesday UK January RICS House Price Balance, BRC Retail Sales Monitor, Japan Machine Tool Orders, German and UK December Trade Balances, then US Wholesale Inventories. Wednesday Japan December Machine Orders, January Domestic CGPI, UK December Industrial Production, US Trade Balance, January Monthly Budget Statement and the Bank of England's Quarterly Inflation Report followed by NIESR January GDP. Thursday Japan National Foundation Day holiday while Taiwan gets two days off with just US December Business Inventories and January Retail Sales due. Friday Japan January Consumer Confidence, German and EZ16 Q4 GDP, Eurozone December Industrial Production and US February University of Michigan Confidence Survey. Sunday the 14<sup>th</sup>, Valentine's Day, is the start of the Chinese Lunar New Year (which means up to a week of holidays for some), while Monday the 15<sup>th</sup> kicks off a three-day Carnival holiday for others.

**Positioning and Technical Analysis** Stock markets will probably gather downside momentum, particularly if this week's potential 'shooting star' candles hold. This will exacerbate worries surrounding the financial system generally, and the banking system in particular. Expect more sheltering in top quality Treasuries, with yield curves flattening as short dates move towards zero. While we cannot rule out another big push for the US dollar, we feel its strengthening bout is almost over and we shall be looking for reversal patterns, preferably a dramatic one in the Euro. Other currencies must confirm allowing commodities to start trying to form interim bases.

Have a nice weekend!