Weekly Market Commentary

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Overview A week spent speculating which banks might fail their 'stress tests', and whether these were worth doing at all, indices alternating between fairly large up and down days to end the week in positive territory. Jakarta, Mumbai and Thailand set new highs for 2010. The Japanese stock market closed near the lowest levels in two years, pressured by a strong yen (86.27) and dragged down by the banks index. The US dollar has lost ground against all major currencies this week, the Australian dollar leading at $0.8972 (a ten-week high) and the Swiss franc at 1.0400, best this year. The Hungarian forint weakened to 292.00 per Euro because of new PM Viktor Orban's refusal to implement IMF-suggested austerity measures. Top-quality Treasuries remain well bid, those of weaker Eurozone countries still all too close to their records over Bunds. US asset-backed securities the first casualty of new financial regulation, so the SEC has had to allow a 6-month grace period for implementation. [Rating agencies can now be sued for fraud and reckless behaviour so they are not allowing their ratings to be published in prospectuses]. ICE Sugar rallied to 18.66 cents per pound, its most expensive since March though a fraction of February's unsustainable 30.40 peak. Most Baltic Freight rates are at their lowest in a year or more.

Political and Economic Developments The Bank of Canada raised it key rate by 25 basis points to 0.75%; Brazil raised its Selic rate 50 basis points to 10.75%, slightly less than expected on negative inflation in June.
UK Q2 GDP came in a better than expected +1.1% Q/Q taking Y/Y growth to +1.6%, helped in part by June Retail Sales which rose by 1.0% M/M and +3.1% Y/Y excluding auto-fuel. No doubt the football World Cup had an effect, but this keeps it at the average of the last decade. With June Core CPI also running at +3.1% Y/Y (RPI +5.0% Y/Y and among the highest in two decades) yet Gilts maturing within 9 years yielding under 3.00%, real interest rates are decidedly negative. Pity then that National Savings and Investments was forced to withdraw its index-linked securities (RPI +1.00% per annum) to all new investors, the first time in their 35-year history, because of huge inflows. Hometrack has annual house prices rising by under 3.00% or shrinking since December 2007, Rightmove suggests +3.7% Y/Y, though the Halifax and Nationwide calculate 6.3% and 8.7% respectively. Gains on main homes tax free.
German and Eurozone Purchasing Managers' Indices, IFO and Consumer Confidence Surveys all upbeat versus June's.

Underlying Themes For several weeks now politicians and central bankers have been suggesting we shouldn't be so gloomy, that in fact the economy was growing and banks were sound, many giving lengthy TV interviews on these subjects. Mercifully chairman Bernanke in his semi-annual testimony to the Senate Banking Committee spared us the usual drivel. Saying the number one concern for small businesses was a lack of demand not access to credit and that funding was not a constraint on large firms, that state and local governments were under fiscal stress, plus the worrisome structural problems of high unemployment, were all drags on economic recovery; above all the 'economic outlook remains unusually uncertain'. Perhaps they have at last grasped the enormity of the problem; perhaps they now know there are no more tools in the box; perhaps they now understand that deleveraging and rebuilding overstretched balance sheets takes a **very** long time. Perhaps the Bank of England's MPC is also adopting a more realistic approach. After predicting UK CPI would be back at target by the end of this year (their usual mañana mentality) chief economist Spencer Dale suggested this might now not happen until the end of 2011, and that the country would not get back to normal 'for an awfully long time'.

What to watch for next week Monday Japan June Trade Balance, German Import Prices due from this day, US New Home Sales and UK July Hometrack Survey. Tuesday Japan June Corporate Service Prices, EZ16 M3 Money Supply, UK CBI July Distributive Trades, US Consumer Confidence, German August GfK Consumer Confidence and US May CaseShiller House Prices. Wednesday Japan July Small Business Confidence, ECB Bank Lending Survey, July CPI for the various German states due and US June Durable Goods Orders. Thursday Japan June Retail Trade, Large Retailers' Sales, UK Net Consumer Credit, Mortgage Approvals, German July Business Confidence, Unemployment, EZ16 Business Climate and Confidence and the Fed's Beige Book. Friday Japan June Unemployment, Household Spending, CPI, Industrial and Vehicle Production, Housing Starts, Construction Orders and Tokyo July CPI. Then EZ16 June Unemployment, CPI, US Q2 GDP, July Chicago Purchasing Managers and final University of Michigan Confidence Survey. Monday 2nd August holidays in Canada and Iceland.

Positioning and Technical Analysis The last week of another thin summer month and many markets are tottering at fairly pivotal levels. August will probably see trends develop and more chaotic conditions predominate. Watch FX weekly closes for important breaks; another round of generalised US dollar selling is due, something which should prop up commodity prices. Top-notch Treasuries and Corporate bonds should remain well bid maintaining the pressure on credit spreads. Stock markets will probably be subject to increasingly violent intra-day swings.

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