

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



Monday, October 12th

Scott Pattison, Executive Director of the National Association of State Budget Officers, reports that states' tax revenue shortfalls continue to be "close to unprecedented" as many states continue to see no end in sight to significantly lower income tax revenues.

MONDAY, OCTOBER 12TH

Moreover, sales tax collections continue to decline in Georgia, Texas and New York State. (See also Winter Warning, December 1 /08 – In One Hell of a State).

- California State Controller, John Chiang, reports that State revenue in the 1st. quarter of fiscal 2010 ended September 30th. was 5.3% less than assumed in the State's \$85 billion annual budget. Since California's unemployment rate climbed to 12.2% in August, lower income tax revenues represented a sizeable portion of the revenue shortfall. (See also Winter Warning, June 8 /09 – The Golden State at the Brink of Collapse).
- According to Reuters, new accounting rules to be introduced in 2010 by the Financial Accounting Standards Board (FASB), will eliminate the concept of a "qualifying special purpose entity" forcing banks to restore securitized debt to their balance sheets, thereby, retaining exposure to the risks related to transferred financial assets. In turn, these accounting changes could constrain the amount of credit available to consumers for mortgages and credit cards.
- According to a recent report by Pricewaterhouse Coopers, on the average within 15 years, American public pension funds will have less than half the money they require to pay pension benefits. Collectively, after losing about \$1 trillion (U.S.) in their investment portfolios, U.S. state and local government pension funds are facing a devilish decision: either reduce retirement benefits, or seek out high risk investments in the hope of higher rates of return. (See also Winter Warning, July 6 /09 – America's Albatross – Unfunded Government Pension Liabilities).

TUESDAY, OCTOBER 13TH

- The Mannheim-based ZEW research institute reports that its economic sentiment index declined by 1.7 points to 56.0 points in October
- The U.K. consumer price index declined to a 5-year low to 1.1% in September, due to moderating utility and food costs
- In a new economic report, the Economic and Social Research Institute, Ireland's leading independent think-tank, comments that Ireland will have to borrow the equivalent of almost 13% of its gross domestic product (GDP) to finance its 2010 fiscal deficit. The Institute states that the 4 billion euro budget savings will only stabilize, rather than reduce the deficit.
- In a Financial Times interview, former Clinton and Carter administration Treasury official, Roger Altman commented that "more poor economic data have put Washington in a nearly impossible fiscal position. The U.S. economy requires more stimulus than provided by the original package passed in March. But the dismal deficit outlook poses a huge longer term threat. Indeed, it is just a matter of time before global financial markets reject this fiscal trajectory. That could lead to a punishing dollar crisis. To avoid it, America's leaders should commit now and in detail to implement deficit reduction plan ... vague promises will not work. (See also Winter Warning, September 28, 2009 – The American Greenback Will Be Cast into the Hazard and The Deteriorating U.S. Debt Dilemma).

WEDNESDAY, OCTOBER 14TH

- In its monthly economic survey, Britain's Office of National Statistics states that "The U.K. risks a double-dip recession" because the forces now sustaining an attempt at recovery are likely to prove fragile. The ONS analysis cites that economic prospects are muted by consumers, businesses and governments all struggling to pay down debts, a rising unemployment rate and continuing reluctance by the banks to lend.
- JP Morgan Chase reports a \$3.6 billion (U.S.) net profit in the 3rd. fiscal quarter ended September 30th. compared with a profit of \$527 million (U.S.) in the same period a year ago, citing strong revenues in investment banking, fixed income trading and other trading divisions.
- The U.K. unemployment rate remains unchanged at 7.9% in August
- U.S. retail sales declined by 1.5% in September, following the end of the popular "cash for clunkers" car subsidy program
- The California Public Employees' Retirement System (Calpers – America's largest public pension fund) announced it is launching a "special review" into payments made by money managers (including billionaire Leon Black's Apollo Management LP) to placement agency firms including Arvco Financial Ventures LLC. Arvco's founder and owner is Al Villalobos who served on Calpers' board of directors from 1993 to 1995. Calpers revealed that Mr. Villalobos had reaped more than \$50 million (U.S.) in fees for recommending the hiring of money managers whose investment advice cost the pension fund \$50 billion (U.S.), shrinking its assets by more than 23% to June 30 /09. Calpers' spokesperson, Patricia Macht, stated that "We are gathering the facts to confirm that the \$50 million (U.S.) in fees received by Arvco did not come at our expense."
- While the Dow Jones Industrial Average (DJIA) has recovered to the 10,000 level, or by 50% from its March low, the National Federation of Independent Business Index (NFIB) which represents 350,000 small firms, is at a reading of 88.8 up only 10% from March

THURSDAY, OCTOBER 15TH

- The Labor Department reports the U.S. consumer price index (CPI) rose by 0.2% in September, citing higher prices for automobiles, energy and medical care. Over the past 12 months, the CPI has declined by 1.3% while the core rate (ex-food and energy) has risen by 1.5%.
- Goldman Sachs reports a net profit of \$3.19 billion (U.S.) in the 3rd. fiscal quarter compared to a profit of \$810 million in the same period a year ago, citing near record profits in bond and currency trading. Indeed, principal trading profits on investments totaled \$10 billion (U.S.) representing 80.6% of its \$12.4 billion (U.S.) total revenue
- The Federal Reserve Bank of Philadelphia reports its index of general business conditions declined to a reading of 11.5 in October from 14.1 in September
- Citigroup Inc. reports a loss of 27 cents (U.S.) per share on revenue of \$20.39 billion (U.S.) in the 3rd. fiscal quarter, citing charges of \$8 billion (U.S.) in net credit losses and \$802 million (U.S.) in loan loss reserve provisions
- Spain's house prices declined by 7.8% in the 3rd. quarter on a year-over-year basis and with its unemployment rate of 19%, further declines are expected
- Canadian factory orders declined by 2.1% in August, amid falling sales in the aerospace and automotive industries
- The Canadian Real Estate Association reports 135,182 homes were sold from July to September, representing an 18% increase from the same period a year ago and the most ever sold in the 3rd. quarter. Average prices gained 11% to \$327,736 as the number of new listings declined significantly. Meanwhile, earlier this week, several major Canadian banks raised their 5-year mortgage rates by 35 basis points to 5.85%.
- New York State's Governor David Paterson proposes billions of dollars in spending cuts as the Empire State faces a deficit of nearly \$50 billion (U.S.) over the next 3 1/2 years. The Governor's plan, which seeks to close a deficit for this fiscal year ending March 31 /10 projected to be \$3 billion (U.S.), includes sizeable cuts to the Department of Education, Medicaid and the Metropolitan Transportation Authority, as well as other areas.

Evidently, Governor Paterson and State lawmakers in Albany used federal stimulus money to continue New York's heady spending increases in the budget passed in the spring of this year, leaving the State with unprecedented projected deficits over the next five years.

FRIDAY, OCTOBER 16TH

- Sir Howard Davies, former head of the Financial Services Authority (FSA) and now Director of the London School of Economics (LSE), tells a group of HSBC clients in London that Britain faces a dangerous acceleration in the levels of public debt and "it is very clear that something dramatic has to happen to control spending (so) the next six months are going to be extremely delicate in the U.K." Even university professors are "planning to go on strike for an 8% pay raise ... people are miles away from understanding what's needed" to fight this economic crisis. Sir Howard said the reality is that the U.K. government has to date revealed only "half of the fiscal consolidation necessary over the next five years, merely to stabilize the debt problem. By 2014, we will be among the Big Four of global profligates." We couldn't be more in agreement, Sir Howard!
- Germany's leading institutes warn that the pace of the country's economic recovery is "unsustainable" and that banks may confront a fresh crisis in 2010 as bad debts continue to surface. A five-man panel dubbed "The Wise Men" which advises the German government states in a joint report that "There is still a significant risk of further shocks to the international financial system, since credit to non-financial firms has clearly been declining. Financial conditions are likely to worsen further because banks are, (not only) facing large write-offs on toxic debt, (but also) a rising toll of company insolvencies."
- Eurostat, the European Union's statistical office, reports that Eurozone exports declined by 5.8% in August, compared to a 4.7% increase in July.
- Rating agency Moody's Investor's Service reports that Spanish banks face "severe asset quality deterioration" and have yet to make provisions for write downs of over half of the 108 billion euros of likely loan losses over the next five years. Under Moody's "stress scenario" loan losses could reach 225 billion euros, if the Spanish economic downturn continues unabated.
- According to a report from Ernst & Young Item Club, the U.K. budget deficit will cause the pound to be stuck at near-parity against the euro until at least 2014. Professor Peter Spencer, Ernst & Young's chief economic advisor, states that as a result of consumers emphasizing savings, the value of the pound will be depressed for a long time. Professor Spencer also forecasts the U.K. economy will continue weak for an extended period and "interest rates will (remain) pinned to the floor."
- RealtyTrac Inc. reports that U.S. residential property foreclosure filings rose by 5% during the July – September quarter, affecting a record 938,000 properties. Foreclosure related filings are now on a pace to reach about 3.5 million in 2009, compared to 2.3 million in 2008. With the U.S. unemployment rate at a 26-year high of 9.8%, it is easy to see why more and more homeowners are delinquent in their mortgage payments.
- The Bank of America posts a \$2.24 billion (U.S.) loss in the 3rd. fiscal quarter, citing rising mortgage defaults, soaring credit card losses and increased reserve provisions for loan losses. B of A Chief Executive Officer, Ken Lewis, is retiring on December 31st. uncompensated for all of 2009, at the urging of President Obama's executive compensation czar, Kenneth Feinberg. Mr. Lewis, no doubt you will enjoy your hard-earned \$56 million(U.S.) retirement package. (See also, Winter Warning, February 2 /09 – The Clash of Cultures).