

Insight Financial Services Presents Monthly Economic Update for June, 2009



Quote of the month. “I don’t know any other way to lead but by example.” – Don Shula

The month in brief. While economists gathered around the water cooler to discuss whether or not a recovery was really underway, stocks soared, consumer confidence grew, and home sales rose. The broad commodities market had a positive month; the dollar didn’t. Meanwhile, the government found that 10 out of 19 stress-tested banks needed more capital. One U.S. automaker went into Chapter 11 bankruptcy, and another prepared for it.

Domestic economic health. What would the government find out about the banks? Would GM and Chrysler go BK? Those were the media preoccupations for May, and while many investors worried plenty about them as well, Wall Street as a whole rode through the attached fears and crises admirably.

The results of the stress tests administered by the Federal Reserve were publicized in the second week of May. Bank of America, Citigroup, Wells Fargo and GMAC were instructed to raise more capital; BofA was told to go get a whopping \$34 billion. Some other banks (notably American Express, Capital One, Goldman Sachs, JPMorgan Chase and MetLife) were judged well capitalized to face the government’s worst-case scenario.¹

Speaking of worst-case scenarios ... as May ended, General Motors was poised to follow Chrysler into bankruptcy. (The official filing came June 1). There were indications that the bankruptcy process might be unusually swift. After only a month in bankruptcy proceedings, Chrysler got permission on May 31 to sell

most of its assets to a group led by Fiat and emerge from court protection. Perhaps GM would do something similar. In the bankruptcy plan, the U.S. government will own 60% of GM, the UAW 17.5%, the Canadian government 12% and GM bondholders 10%.²

And now, the other notable news items. Consumer confidence rose: the Conference Board’s May survey recorded its best one-month gain in six years, and the Reuters/University of Michigan index climbed to 68.7, the highest mark since September.³⁻⁴ Unemployment, of course, also climbed: the Labor Department figure for April was 8.9%, although the pace of layoffs declined from March.⁵

Deflation fears were calmed a bit with the release of the April Consumer Price Index. Yes, consumer prices were flat for April, and yes, CPI fell by 0.7% over the 12 months ending in April - the first year-over-year drop since 1955. However, core CPI had gone up 1.9% across the same 12 months.⁶ Durable goods orders also increased in April by 1.9%.⁷

May consumer spending was down by just 0.1%, the Commerce Department reported, better than expected; personal income for May was flat rather than negative.⁸

The Obama administration got tough with credit card firms. It issued new rules forcing card issuers to notify cardholders of rate hikes 45 days in advance and curb retroactive rate increases. It also made collegians and teenagers less attractive targets for these companies by tightening credit limits for them.⁹

Global economic health. In Asia, it seemed inflation was easing notably in May. In Indonesia, it was 6.04%, the lowest level since June 2007. In South Korea, it was 2.7%, a 20-month low. In Thailand, May consumer prices were 3.3% below levels of a year before.¹⁰ The outlook for China’s economy was better, with manufacturing activity increasing for the third month in a row in May after contracting from October to February.¹¹ Japan? Well,

after a -15.2% GDP in the first quarter, there was room for improvement.¹² The Japanese government did raise its economic outlook in May for the first time since 2006.¹³

Turning to Europe ... we learned that the economies of the 16-country Eurozone collectively contracted 4.6% in 1Q 2009. The economies of England and Germany had respectively contracted by 4.1% and 6.9% in the quarter.¹⁴ The European Central Bank had set its key interest rate at 1% (a new low) and the EU May manufacturing PMI rose to its highest level in seven months, a sign of stabilization.¹⁵

World financial markets. May was as positive as April – that is to say, an amazing month for many stock indices worldwide. India’s Sensex gained – are you ready for this? – 28.3% last month. Meanwhile, the Russian RTSI shot up 21.7% and the Singapore Straits Times index gained 21.3%. So how about the MSCI Emerging Markets Index? It followed a 16.3% gain for April with a 16.7% gain in May. The MSCI World Index didn’t do too badly either, rising 8.6% for the month.¹⁶

Among Asian indices, the Australian All Ordinaries rose +1.8% in May, but that was nothing; the Hang Seng was up +17.1%, the Shanghai Composite +6.3% and the Nikkei 225 +7.9%. In Europe, the CAC 40 gained 3.7% in May, the DAX 3.6% and the FTSE 100 4.1%. Just north of us, Canada’s S&P/TSX Composite rose 11.2% in May.¹⁶

Commodities markets. Oil had a great month – in fact, the whole energy sector did. Oil futures went up 29.71% in May. Gasoline futures did even better, soaring 31.74%. Diesel fuel? Up +22.66% for the month. Heating oil futures rose 22.82% and natural gas futures gained 4.89%. Silver left gold in the dust: it rose 26.65% in May, enjoying its best month since April 1987. Gold didn’t perform too shabbily either, gaining 9.83%. It was a fine month for other metals, as these May gains demonstrate: platinum, +8.08%; palladium, +8.18%; copper, +7.33%. But the greenback didn’t fare so well: the U.S. Dollar Index dropped 6.29% in May.¹⁷

How about crops? Well, it was spring, and most ag futures were in the plus column. Oats futures gained 23.65% in May. Other big gains: wheat (+18.78%), soybean meal (+15.73%), orange juice (+12.61%) and

soybeans (+12.23%). Rice futures lost 5.76% for the month.¹⁷

Housing & interest rates. Spring is homebuying season, right? So were the buyers out, encouraged by low prices? The April indicators we received seemed relatively positive: new home sales rose 0.3%, existing home sales rose by 2.9%. Of course, median prices for new and used homes were respectively 15.0% and 15.4% below last April’s figures. While the inventory of existing homes for sale saw no decrease, the number of new homes on the market was at its lowest level in eight years.^{18,19}

Mortgage rates were still low at the end of May ... but with bond yields rising, how long could that last? At the end of last month, Freddie Mac had 30-year FRMs averaging 4.91%, as opposed to 4.78% at the end of April. As for other types of mortgages, 5-year ARMs ticked up to 4.82%, 1-year ARMs fell to 4.69%, and averages on 15-year FRMs crept up to 4.53%.²⁰

Major indexes. For the third straight month, the market behaved as if the recession had become a memory. The Dow gained 20.39% across March, April and May, representing its best three months since September-November 1998.²¹

% Change	1-Month	Y-T-D
DJIA	+4.07	-3.15
NASDAQ	+3.32	+12.51
S&P 500	+5.31	+1.76

Source: cnbc.com, 5/29/09²¹

Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly. These returns do not include dividends.

June outlook. The major stock market indices have entered a notable upswing in the last three months – there’s still a long way to go, but stocks have shown some resilience. If we are on the second downward leg of a potential W-shaped recovery, the market is paying no attention to that reality. Let’s hope we are watching a U-shaped or even V-shaped recovery instead. Some confidence may have returned to consumers and investors – when General Motors announces bankruptcy and the market posts a triple-digit rally on the same day, that’s saying something.²²

The important economic releases for the rest of June: April factory orders and the May ISM services index

(6/3), May unemployment (6/5), April wholesale inventories (6/9), May retail sales and April business inventories (6/11), preliminary June consumer sentiment (6/12), May PPI, core PPI, industrial production and housing starts (6/16), May CPI and core CPI (6/17), May existing home sales and durable goods orders (6/23), May new home sales (6/24), May personal spending and personal income (6/26), and the Conference Board's June survey of consumer confidence (6/30).

Riddle of the month. What is the significance of the following: The year is 1978, thirty-four minutes past noon on May 6th.

(Contact my office or see next month's Update for the answer.)

Last month's riddle. What is no sooner spoken than broken?

Answer: Silence.

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