Key Trades Round-up for this week:
18th August 2009

Open Positions

We have no open positions.

The Macro Trader's view:

It is no secret we have found the markets challenging this year, as too many of our positions have ended by being stopped out, even though they initially went into profit. But our style of trading isn't short-term, it is more medium and longer-term, and therein lies our current difficulty.

Our underlying view has been that the US and UK economies are gradually emerging from recession, with the Euro zone and Japan a little way behind, although recent Q2 GDP data from France, Germany and Japan has shown these three to be already out of recession, but our basic analysis still holds: without a robust recovery in the US these three export-oriented economies will struggle to consolidate their recovery.

However, given the nature of the recession and its cause - an almost complete financial sector meltdown, requiring unprecedented intervention from the political and monetary authorities, recovery was always going to be a somewhat torturous affair. In most post-war recessions the Banking sector has been able to provide adequate credit to feed the recovery, this time, the Banks themselves are the recipients of intensive care.

But even so there have been clear signs that the worst of the recession is in the past:

- In the US the housing market has begun to show signs of recovery and the pace of job destruction has slowed dramatically in recent months, with both ISM surveys having moved away from their early lows.
- In the UK the signs of recovery are even better, the housing market has shown clear signs of stabilizing, both PMI surveys have recovered to above the 50.0 level, inflation hasn't turned to deflation, at least as measured by CPI and retail sales are holding up well.
- In the Euro zone, there is optimism that recovery will feed through here too after France and Germany posted positive Q2 GDP data, with Japan also reporting growth in its Q2 GDP data.

So, why the hesitancy in the markets?

SEVEN DAYS AHEAD 124 REGENTS PARK ROADLONDON NW18XL
TEL +44 (0) 7849 922573 E-MAIL MSTURDY@SEVENDAYSAHEAD.COM JLEWIS@SEVENDAYSAHEAD.COM WWW.SEVENDAYSAHEAD.COM

The US, while improving, still reports falling prices as measured by CPI indeed they are falling at their fastest in 60 years reawakening fears of deflation. This has led the Fed to report in its recent FOMC policy statement that while there are signs of improvement, with economic activity leveling out, household spending remains constrained by job losses, sluggish income growth and tight credit, meaning policy will remain at exceptionally low levels for an extended period.

In the UK the Bank of England continues to do its best to play down recovery signs and has warned any recovery will be weak, leading policy makers to extend their QE program beyond previously announced levels, surprising traders and wrong-footing the markets.

So although a head of steam had begun to build for recovery to take hold later this year, traders have suddenly abandoned their optimism and become worried about a protracted recession with lingering deflationary risks in the US and a false recovery in the UK.

Which has also meant that the better data released by France, Germany and Japan has been taken with a pinch of salt.

What this means for the markets is that there is every chance that the current period of featureless trading will continue a while longer as markets remain bound in largish ranges. This to us looks especially true for short-term interest rate markets, bonds and currencies.

The one exception seems to be stocks. Although a correction has occurred there over recent days, we judge the positive Q2 earnings reporting season was good enough to place a floor under the market and allow the improving data releases that we expect to see send equities higher.

In conclusion: these are frustrating times, but market conditions such as these do not persist indefinitely. Eventually a clear economic scenario emerges and markets begin to trade in line with fundamentals rather than anxiety and fear. We look forward to the markets emerging from the current unprecedented uncertainties.

The Technical Trader's view:

Mark Sturdy is away.

John Lewis

Seven Days Ahead