



# Market Weekly

Commodities, Forex, Futures and Options

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## HEADLINE OF THE WEEK: "Dow Hits Bear-Market Territory" (The Wall Street Journal, 6/28/2008)

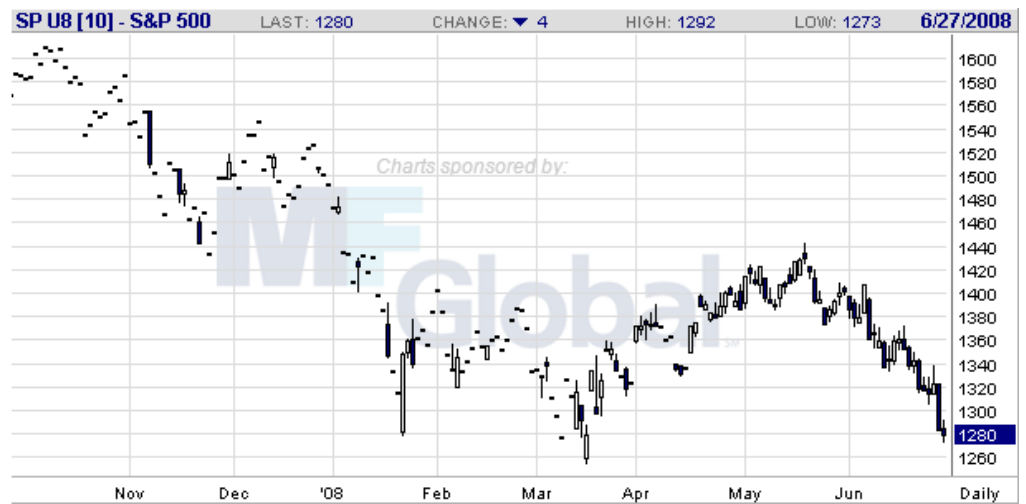
Compiled by Mack Frankfurter, Chief Investment Strategist

### WEEKLY RECAP

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*"...the challenges confronting investors are starting to look like a redux of the 1970s."*

The stock market is reeling with global equities heading for their worst first-half performance in 26 years after a week in which oil surged to a record. The Dow Jones Industrial Average (DJIA) closed down 19.9% from its October record on Friday, just shy of the so-called 20% decline mark of a bear market. The S&P 500 fared little better. Technical analysts are warning that if the index breaks through its March lows it could retest its 2006 lows at 1,219 points. Yet as stocks suffer, the surge in oil and other commodities during 2008 has the Reuters-Jefferies CRB spot index on track for its largest gain in 35 years. With oil setting a new record just shy of \$143 a barrel yesterday, the challenges confronting investors are starting to look like a redux of the 1970s. According to investment icon Warren Buffet, the U.S. economy suffers from stagflation that's going to get worse and may not end this year or even next. Federal Reserve Chairman Ben Bernanke is vowing to prevent that from happening, insisting the Fed is on the case; but few Fed watchers count on him to back up that talk with action anytime soon. The VIX rose to only 23.9 indicating that stocks may have further to fall. The index reached 32.2 on March 17 when the S&P 500 traded at its lowest level of 2008, the day after the Federal Reserve led a bailout of Bear Stearns.



The September S&P 500 futures contract reflects a steady breakdown to the Bear Stearns March low.

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## Headlines from page 1

For all the brouhaha regarding the debate on speculation in the futures markets, soaring energy prices is having a fundamental impact by forcing Proctor & Gamble, the world's biggest consumer goods company, to rethink how it distributes products. According to Keith Harrison, head of global supply at P&G, "A lot of our supply chain design work was really developed and implemented in the 1980s and 1990s, when our capital spending was fairly high as a cost of capacity and oil was ten bucks a barrel." Meanwhile, the Russian state-controlled energy company Gazprom belittled Opec this week, saying the oil producers' cartel had in effect lost control of the market. In a sign of increasingly internationalized trade, Gazprom hopes to serve the North American market from 2014 with liquefied natural gas from its proposed Shtokman project off Russia's north coast. While these ideas are being bandied about, Royal Dutch Shell said it will delay drilling in offshore Alaska for another year owing to an ongoing court challenge by environmentalists who say regulators should not have approved the project because of possible risks to whales and other marine animals. Given the court delays Shell said it would shift focus to other opportunities, given the very tight market for labor at a time when the oil and gas industry was rushing to capitalize on rising oil prices.

*"...soaring energy prices is having a fundamental impact by forcing Proctor & Gamble to rethink how it distributes products."*



*While the steelmakers cartel has negotiated an almost 100% price rise, copper prices have stayed in a range.*

Global inflation fears deepened this week as Chinese steelmakers agreed to a record increase in annual iron ore prices in a move likely to boost the cost of cars, machinery and other products. Chinese millers agreed to pay Anglo-Australian miner Rio Tinto up to 96.5% more for their ore supplies this year, the biggest ever annual increase and well above the 9.5% increase paid last year. The spectre of inflation is haunting the global economy as companies ranging from Dow Chemical to South Korea's Posco unveiled sharp price rises to combat the soaring costs of energy and raw materials. The general price pressure was exacerbated when BHP Billiton, the mining company, said the 96.5% record increase in iron ore announced by Rio Tinto was not enough, signaling it could ask for a rise of 100% from its steelmaker customers. The sustained rise in the price of oil and commodities has hammered industries such as airlines and carmakers, and deepened fears of a global inflationary spiral as producers pass on higher costs to manufacturers and consumers. Price rises has already provoked riots across Asia.

*"...the 96.5% record increase in iron ore announced by Rio Tinto was not enough..."*

## ECONOMIC REVIEW

European Central Bank council member Yves Mersch said the bank will do whatever is needed to contain inflation in the 15-nation euro region. "We will do whatever we need to do to be faithful to our primary objective that is inflation. Our mandate is fixed by the European treaty, and that clearly states that our primary objective is price stability." ECB President Jean-Claude Trichet has said the bank may raise its benchmark interest rate by a quarter-point to 4.25 percent in July after inflation accelerated to the fastest pace in 16 years. Investors are betting the ECB will increase the key rate to 4.5 percent by the end of the year. The ECB aims to keep the inflation rate below 2 percent.

Meanwhile, confidence among U.S. consumers fell in June to the lowest level in 28 years as record-high gasoline and rising joblessness rattled Americans. The Reuters/Univ. of Michigan final index of consumer sentiment dropped to 56.4, the weakest level since May 1980, from 59.8 the prior month. The measure averaged 85.6 in 2007. Gasoline at over \$4 a gallon and rising costs for food are pinching household budgets, just as mounting job losses and falling home values raise stress levels. The report showed the inflation rate that Americans expect over the coming five years held at 3.4 percent for a second month, the highest

since 1995. Nevertheless, U.S. consumer spending rose more than forecast in May as tax rebates drove the biggest gain in incomes in almost three years, enabling households to at least temporarily overcome soaring fuel bills. Economists had forecast spending would rise 0.7 percent, according to the median of 72 estimates in a Bloomberg News survey. The spending estimate for April was revised up to 0.4 percent from an originally reported 0.2 percent increase.

In Asia, Japan's household spending slumped in May, the ratio of jobs available fell to a three-year low and the inflation rate almost doubled, signaling that the economy's longest postwar expansion may be over. Household spending declined 3.2 percent, the most since September 2006, the statistics bureau said today. Core consumer prices, which exclude fruit, fish and vegetables, rose 1.5 percent from a year earlier after climbing 0.9 percent in April. The Nikkei 225 Stock Average slid to a two-month low on concern global demand for Japanese-made cars and TVs is being curbed by record crude prices. Bonds gained because the risk of a recession may prevent the Bank of Japan from raising its key interest rate from 0.5 percent even as inflation accelerates.

## Next Week's Economic Calendar

Will the tax rebates permeate into the numbers for auto and truck sales, factory orders and ISM services? Maybe...

Date	Time (ET)	Statistic	For Period	Briefing Forecast	Market Expects	Prior
30-Jun	9:45 AM	Chicago PMI	Jun	49.0	48.5	49.1
30-Jun	10:00 AM	Mich Sentiment-Rev.	Jun	56.7	56.7	56.7
1-Jul	12:00 AM	Auto Sales	Jun	NA	NA	5.3M
1-Jul	12:00 AM	Truck Sales	Jun	NA	NA	5.1M
1-Jul	10:00 AM	Construction Spending	May	-0.5%	-0.6%	-0.4%
1-Jul	10:00 AM	ISM Index	Jun	49.6	NA	49.6
2-Jul	8:15 AM	ADP Employment	Jun	-	28K	40K
2-Jul	10:00 AM	Factory Orders	May	0.0%	0.6%	1.1%
2-Jul	10:30 AM	Crude Inventories	28-Jun	NA	NA	830K
3-Jul	8:30 AM	Average Workweek	Jun	33.8	33.7	33.7
3-Jul	8:30 AM	Hourly Earnings	Jun	0.3%	0.3%	0.3%
3-Jul	8:30 AM	Initial Claims	28-Jun	375K	NA	384K
3-Jul	8:30 AM	Nonfarm Payrolls	Jun	-50K	-50K	-49K
3-Jul	8:30 AM	Unemployment Rate	Jun	5.4%	5.4%	5.5%
3-Jul	10:00 AM	ISM Services	Jun	52.0	51.5	51.7

*Data is provided for informational purposes only, and is not intended for trading purposes.*

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### MANAGED FUTURES NEWS

On June 23, 2008, FIA along with the CME Group, NYMEX and MFA filed a joint comment letter with the Federal Trade Commission which addressed the FTC's implementation of section 811 of the Energy Independence and Security Act of 2007. Section 811 gives the FTC anti-manipulation authority over wholesale purchases and sales in crude oil, gasoline and petroleum distillates. The FTC must adopt rules prohibiting certain misconduct to implement its authority. The letter urged the FTC to respect CFTC exclusive jurisdiction over futures markets and to coordinate its anti-manipulation rules and enforcement efforts in the wholesale cash markets with those of the CFTC.

The House of Representatives yesterday approved legislation that directs the Commodity Futures Trading Commission (CFTC) overseeing commodity trading to use its emergency authority to investigate and rein in speculators who lawmakers blame for the run-up in oil prices. The CFTC has not yet taken such action, arguing that oil prices are rising simply because supply cannot keep up with demand. But lawmakers who authored the bill say recent congressional hearings have shown that investors such as hedge funds, pension funds and big financial firms are flooding into commodity trading and causing oil prices to soar. The measure immediately allows the agency to use its most dramatic powers, such as imposing temporary limits on traders or halting trading altogether when oil prices swing wildly. The legislation, which passed by a 402 to 19 vote, is a sign of Congress's growing impatience with the CFTC's response to the oil crisis, lawmakers said.

As oil prices heat up and stock prices stagnate, more investors are interested in jumping on the "speculation" bandwagon. Direxion Funds of Newton, Mass., is capitalizing on that trend with Commodity Trends Strategy Fund, which was started June 10 under ticker DXCTX. The open-ended commodity mutual fund is benchmarked and pegged to the Standard & Poor's Commodity Trends Indicator. The fund actually holds commodity futures, unlike other mutual funds that invest in corporate stocks exposed to the commodities market.

Senate Republicans unveiled an ambitious energy bill Thursday expected to establish a unified message on soaring gas prices leading up to the November elections. The bill, supported by nearly every member of the GOP Conference, essentially calls for more oil drilling while promoting less use and embracing some conservation measures. That strategy sharply contrasts with that of Democrats, who oppose expanded drilling and instead propose reining in oil companies and speculators, and are promoting conservation and renewable energy.

As a light sprinkle of rain fell across his 3,000 acres of corn and soybean fields early on Thursday, Missouri farmer Jim Collins knew it was too late to replant flooded fields, and too late to hope for better weather. Flooding up and down the Mississippi and other waterways, deemed the worst in 15 years, has either drowned or damaged millions of acres of corn and soybeans throughout several states in the U.S. Midwest this month, leaving farmers like Collins with dwindling options. Some farmers worked earlier this week to replant still-saturated fields with new seed, hoping still to grow a good crop and capitalize on record-high grain prices.

The heads of two of the world's biggest steel companies gave the New York Mercantile Exchange (NYMEX) a thumbs-down for its plan to launch steel futures trading this year. Dan DiMicco, chairman of Nucor Corp, told a steel conference on Wednesday that futures trading was "phony baloney" that encouraged "unethical and illegal activity." And ArcelorMittal chief executive officer of Lakshmi Mittal said he saw no positive impact from a move that benefits only traders.

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