



Market Weekly

Commodities, Forex, Futures and Options

August 22, 2008
Quarter 3, Issue 06

Managed Account Research, Inc. 929 Santa Barbara Street, Santa Barbara, CA 93101
www.ma-research.com research@ma-research.com 800.308.1495

HEADLINE OF THE WEEK: "Risky Business in Russia" (TIME Inc., 8/22/2008)

Compiled by Mack Frankfurter, Chief Investment Strategist

WEEKLY RECAP

- 1 Headline of the Week
- 2 Headlines Continued
- 3 Economic Review and Next Week's Calendar
- 4 Managed Futures News

In front of a badly damaged government building, a Russian orchestra this week performed pieces by Tchaikovsky and Shostakovich as 1,000 or so residents held up candles and the flags of Russia and South Ossetia, the catalyst in this month's conflict between Russia and Georgia. In the meantime, investors are pulling their money out of Russia in the wake of the conflict at the fastest rate since the 1998 ruble crisis. As a result, Russian debt and equity markets have suffered sharp falls since the conflict erupted on August 8, with yields on domestic ruble bonds increasing by up to 150 basis points in the past month. Up until the escalation of hostilities, the attractions of resource-rich Russia, a net foreign creditor with sustainable trade and fiscal surpluses and the world's third-largest foreign exchange reserves, has boosted the ruble. However, the events in Georgia prompted a change of attitude towards the currency as nervous investors demanded a greater risk premium for investing in Russia, pushing the ruble down to its lowest level this year. Although not officially confirmed, traders say the Russian central bank intervened in the market to support the currency and damp volatility, the reverse of its previous policy. All this has policy implications for Russia it probably did not foresee.

"Russian debt and equity markets have suffered sharp falls since the conflict erupted on August 8th."



The Russian ruble futures contract is lightly traded; nonetheless, the chart shows the impact of war.

Copyright © 2008 Managed Account Research, Inc. – All rights reserved.

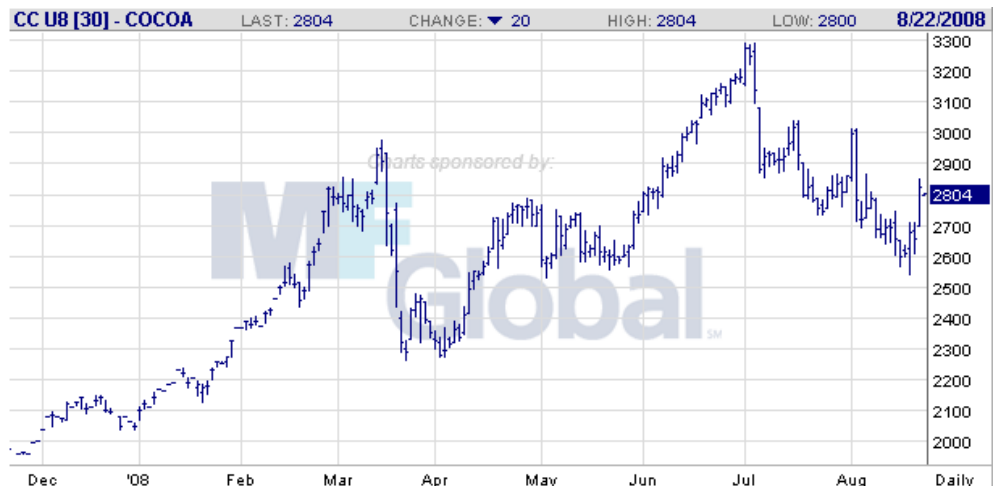
Compiled by Mack Frankfurter, Chief Investment Strategist. Commodities, forex, futures and options trading involve substantial risk. In no event should the content of this newsletter be construed as an express or an implied promise or guarantee that you will profit or that losses can or will be limited in any manner whatsoever. Past performance is not necessarily indicative of future results. Information provided in this correspondence is intended solely for informative purposes and is obtained from sources believed to be reliable. The risk of loss in trading commodities can be substantial. You should carefully consider whether such trading is suitable for you in light of your personal circumstances and financial resources.



Headlines from page 1

“Other companies caught out by soaring commodity prices include Hershey’s competitor Cadbury...”

Food companies were once a little blasé about the price they paid for the ingredients that went into their corn flakes, chocolate bars and yoghurts because in the 1980s and 1990s, prices of agricultural commodities were falling. While many food companies took precaution by hedging some of their key ingredients—Mars, the owner of Snickers bars, has been hedging cocoa since the 1960s—they did not have to worry too much about being caught out by unexpectedly big price jumps. Today, that luxury has vanished. Soaring global demand for commodities has driven prices of all kinds of food ingredients, from corn to cocoa to coffee, to new highs, and more than a few food companies have been unpleasantly surprised. Hershey, the US chocolate group, became the latest in a long line of food companies to warn that its commodity costs, which include sugar and peanuts as well as cocoa and are up as much as 45 percent since the start of the year, were rising faster than expected. Other companies caught out by soaring commodity prices include Hershey’s competitor Cadbury, which found rising raw material prices “a stronger challenge” than it had previously anticipated. Companies have been trying to counter higher costs by raising the wholesale prices for their products. But companies are starting to find that consumers are reluctant to pay more for groceries as inflation rises and disposable incomes fall, and many price increases are being followed by drops in sales volumes.



Cocoa futures price outlook medium-term was well-supported due to worries over the quality of beans.

“The shutdown of the BTC pipeline was followed three days later by Russia’s invasion of Georgia, which further disrupted Caspian fuel shipments.”

Crude oil fell more than \$6 a barrel on Friday, the biggest drop since December 2004, as the U.S. dollar strengthened and BP Plc restored shipments on a Caspian Sea pipeline through Turkey. Energy futures fell as the rising dollar eased demand for commodities as an inflation hedge. The Baku-Tbilisi-Ceyhan pipeline, which moves oil from Azerbaijan through Georgia to Turkey’s Mediterranean coast, resumed normal flows today after a fire shut it earlier this month, a Turkish official said. The shutdown of the BTC pipeline was followed three days later by Russia’s invasion of Georgia, which further disrupted Caspian fuel shipments. Oil prices have also fallen on reduced demand in the U.S., the country responsible for almost a quarter of global oil use. Crude oil may tumble to \$80 a barrel within 12 months on increasing supplies of alternative energy. Pump prices haven’t increased since July 19, according to AAA, the nation’s largest motorist organization.

ECONOMIC REVIEW

U.S. wholesale prices rose twice as fast as expected by economists and recorded their biggest annual increase in 27 years last month, as inflation fears continue to haunt the American economy in spite of the recent drop in crude oil values. The producer price index for finished goods, which was forecast by economists to jump by 0.6 percent in July from a month earlier, instead gained 1.2 percent, government data showed yesterday. Compared with July 2007, wholesale prices were up by 9.8 percent, the highest rate since 1981. At the core level, which excludes food and energy, producer prices for goods jumped three times more rapidly than forecast, a sign that wholesalers are passing on higher input costs to their customers. The surge in producer prices mirrored the release of the consumer price index last week, which also increased much faster than expected by economists at the headline and core levels. Both sets of data were measured too early in July to take into account the decline in the price of crude oil and many economists and policymakers hope that inflationary pressures will rapidly ease, removing one of the key threats to the health of the US economy. However, the readings for last month suggest this may take longer than expected.

Mainland China overtook the U.S. as Japan's largest export destination for the first time last month, underlining the growing importance of Chinese demand to the world's second-largest economy. Exports to China, which have risen in each of the past 38 months, expanded by 16.8 per cent in July to their highest level since the Japanese government began compiling statistics in 1950. At the same time, exports to the U.S. declined by 11.5 percent, marking the 11th consecutive monthly drop. Japanese companies such as Toyota, Honda Motor and Komatsu have recently identified an increasing reliance on China and other emerging markets for sales growth as the U.S. economy slows. Honda last month announced double-digit increases in the volume of China sales in the three months to June, compared with a 5 per cent fall in the U.S. However, the export growth will provide little cheer to policymakers, faced with rising input costs and an uncertain outlook in the economies of Japan's main trading partners. Many analysts expect exports to fall again in coming months as the slowdown in western economies begins to have an impact on demand in emerging economies such as China.

Next Week's Economic Calendar

Must of this week's risk aversion stemmed from renewed worries about Fannie Mae and Freddie Mac...

Date	Time (ET)	Statistic	For Period	Briefing Forecast	Market Expects	Prior
25-Aug	10:00 AM	Existing Home Sales	Jul	4.95M	4.90M	4.86M
26-Aug	10:00 AM	Consumer Confidence	Aug	53.0	53.0	51.9
26-Aug	10:00 AM	New Home Sales	Jul	535K	523K	530K
26-Aug	2:00 PM	FOMC Minutes	5-Aug	-	-	-
27-Aug	8:30 AM	Durable Orders	Jul	0.5%	0.1%	0.8%
27-Aug	10:35 AM	Crude Inventories	23-Aug	NA	NA	9390K
28-Aug	8:30 AM	Chain Deflator-Prel.	Q2	1.1%	NA	1.1%
28-Aug	8:30 AM	GDP-Prel.	Q2	2.8%	2.7%	1.9%
28-Aug	8:30 AM	Initial Claims	23-Aug	NA	NA	432K
29-Aug	8:30 AM	Personal Income	Jul	-0.3%	-0.1%	0.1%
29-Aug	8:30 AM	Personal Spending	Jul	0.3%	0.3%	0.6%
29-Aug	9:45 AM	Chicago PMI	Aug	50.5	49.9	50.8
29-Aug	10:00 AM	Mich Sentiment-Rev.	Aug	63.0	62.3	NA

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

Copyright © 2008 Managed Account Research, Inc. – All rights reserved.

Compiled by Mack Frankfurter, Chief Investment Strategist. Commodities, forex, futures and options trading involve substantial risk. In no event should the content of this newsletter be construed as an express or an implied promise or guarantee that you will profit or that losses can or will be limited in any manner whatsoever. Past performance is not necessarily indicative of future results. Information provided in this correspondence is intended solely for informative purposes and is obtained from sources believed to be reliable. The risk of loss in trading commodities can be substantial. You should carefully consider whether such trading is suitable for you in light of your personal circumstances and financial resources.



MANAGED FUTURES NEWS

The Philadelphia Stock Exchange, Chicago Board of Trade and International Securities Exchange all have been digested by larger players. Now it is the New York Mercantile Exchange's turn. CME, the world's largest derivatives exchange, won shareholder approval this week for the acquisition, thanks in large part to a pledge of \$60 million in cost savings. The Chicago exchange has been coy on what that means for the nearly 400 staff at NYMEX, but CME Chief Executive Craig Donohue told Reuters last month he expects "head count reductions, because there will be some redundancies between the two companies."

Transatlantic exchange Nyse Euronext is to launch a new US futures exchange in September after the Commodity and Futures Trading Commission (CFTC) approved its application to become a designated contract market (DCM). At launch, Nyse Liffe will move some gold and silver futures contracts from the Chicago Board of Trade (CBOT) to the new trading platform. Nyse Euronext acquired CBOT's precious-metals business from CME Group in March this year.

A U.S. District Court in Pennsylvania has ordered former hedge fund trader Paul Eustace to pay more than \$291 million to settle charges that he defrauded commodity pool participants. Mr. Eustace was ordered to pay more than \$279 million in restitution and a \$12 million civil penalty. In July 2007, he was charged with solicitation and regulation violations for operating the pools and for concealing losses by issuing false account statements.

With speculation over U.S. vice presidential picks at a boil, prediction markets this week judged Democrat Joseph Biden and Republicans Mitt Romney and Tim Pawlenty most likely to get the nod. Traders on the Dublin-based Intrade market gave Biden, a U.S. senator and former presidential candidate from Delaware, a 38.5 percent chance of being named as Democratic candidate Barack Obama's running mate in the November 4 election. Biden's prospects increased sharply over the past week as he visited war-torn Georgia. Virginia Gov. Tim Kaine was given a 21 percent chance to be picked by Obama, while Indiana Sen. Evan Bayh and Kansas Gov. Kathleen Sebelius were each given a 15 percent chance. Traders gave Obama a 62 percent chance of winning the November election, versus 39 percent for McCain.

When U.S. futures regulators recently reclassified one of the largest traders in the oil market as a speculator, they didn't identify the firm. But people familiar with the matter now say the company whose activities helped change perceptions about the escalating pace of oil speculation is Vitol Group, a large commodity-trading company with headquarters in Europe. A probe into commodity market manipulation by the Commodity Futures Trading Commission (CFTC) has identified Vitol Group as having controlled as much as 11% of oil contracts on the NYMEX, implying the Swiss firm may have manipulated oil prices. The CFTC asked Vitol Group to provide information on its oil futures activities last month. The Swiss organization is supposedly in business to help industry purchase oil, but instead, the Commodity watchdog found it was more profiting from futures trading instead.

The Abu Dhabi Securities Exchange (ADX), will start derivatives trading next year in an effort to keep pace with rival bourses competing for a greater share of regional capital, an official said. ADX wants to compete with Gulf rivals such as the Dubai Financial Market and the Dubai International Financial Exchange for access to the global futures market that is estimated to be worth about \$81tn, according to the Bank of International Settlements.

Market Weekly is a newsletter publication of Managed Account Research, Inc. Its purpose is to provide weekly commentary on the commodity, forex, futures and options markets, as well as economic news impacting your managed futures investments. To subscribe or unsubscribe, contact us at 800.308.1495 or email: research@ma-research.com.

Managed Account Research, Inc. 929 Santa Barbara Street, Santa Barbara, CA 93101
www.ma-research.com research@ma-research.com 800.308.1495

Copyright © 2008 Managed Account Research, Inc. – All rights reserved.

Compiled by Mack Frankfurter, Chief Investment Strategist. Commodities, forex, futures and options trading involve substantial risk. In no event should the content of this newsletter be construed as an express or an implied promise or guarantee that you will profit or that losses can or will be limited in any manner whatsoever. Past performance is not necessarily indicative of future results. Information provided in this correspondence is intended solely for informative purposes and is obtained from sources believed to be reliable. The risk of loss in trading commodities can be substantial. You should carefully consider whether such trading is suitable for you in light of your personal circumstances and financial resources.
