

August 16, 2010

LME Prices (3-mos.ask)	Last Friday's Close	Last Week's Averages
NASAAC	\$2,095.0 = 95.03 cts.	\$2,122.90 = 96.29 cts.
Aluminum Alloy	\$2,110.0 = 95.71	\$2,151.50 = 97.59
Aluminum	\$2,110.0 = 95.71	\$2,160.65 = 98.01
Copper	\$7,156.0 = 324.59	\$7,270.20 = 329.77
Nickel	\$21,275.0 = 965.02	\$21,849.00 = 991.06
Zinc	\$2,047.0 = 92.85	\$2,081.90 = 94.43
Lead	\$2,057.0 = 93.30	\$2,111.30 = 95.77
Tin	\$20,800.0 = 943.47	\$20,625.00 = 935.54

Monday's LME 3-mos. Officials (3-mos ask)

NASAAC	\$2,110.0 = 95.71 cts.
Al Alloy	\$2,130.0 = 96.62
Aluminum	\$2,119.0 = 96.12
Copper	\$7,220.0 = 327.49
Nickel	\$21,525.0 = 976.36
Zinc	\$2,080.0 = 94.35
Lead	\$2,068.0 = 93.80
Tin	\$20,750.0 = 941.21

Monday's LME Inventories

	148,260 -
	67,140 -
	4,377,975 -
	406,700 -
	117,012 +
	616,625 -
	189,975 -
	13,940 +

For the week beginning **Monday, August 16th**

A tough last week that saw global commodities and equities fall hard, traced to a host of unsettling data and central-bank messages out of the U.S., Asia and Europe. LME metals were lower all around, Comex Sept copper lost some 10 cents last week, and on Wall Street, stocks fell for the fourth day with Dow ending the week back in negative territory for the year at 10,303. It was not good, boys and girls...

This week's LME is off to firmer start reflecting the usual suspects in the absence of fresh macro news: dollar weakness, bargain hunting, short covering, and the latest LME inventory drawdowns. Overall market sentiment, however, remain cautious and conservative.

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A relatively light-weight week as far as major economic indicators go, but we do get a look at July housing numbers, wholesale inflation, and the closely watched IP figures for July. The markets could sure use a lift given the potential for some positive news below...

Date	Time	Release	Period	Consensus	Prior
August 16	08:30	NY Fed - Empire Mfg.	August	8.00	5.08
August 17	08:30	Housing Starts	July	560,000	549,000
August 17	08:30	Building Permits	July	580,000	583,000
August 17	08:30	PPI	July	0.2%	-0.5%
August 17	08:30	Core PPI	July	0.1%	0.1%
August 17	09:15	Industrial Production	July	0.5%	0.1%
August 17	09:15	Capacity Utilization	July	74.6%	74.1%
August 19	08:30	Initial Claims	08/14	476,000	484,000
August 19	08:30	Continuing Claims	08/07	4.50 mln.	4.452 mln.
August 19	10:00	Leading Indicators	July	0.1%	-0.2%
August 19	10:00	Philadelphia Fed. Survey	August	7.00	5.10

Weekly Retail On-Highway Diesel Prices - Average All Types (Dollars per gallon, including all taxes)					
Region	07/26/10	08/02/10	08/09/10	Change from week ago	Change from year ago
U.S.	2.919	2.928	2.991	0.063	0.366
East Coast	2.928	2.934	3.000	0.066	0.335
New England	3.014	3.009	3.027	0.018	0.326
Central Atlantic	3.020	3.020	3.086	0.066	0.331
Lower Atlantic	2.880	2.890	2.962	0.072	0.338
Midwest	2.891	2.900	2.966	0.066	0.365
Gulf Coast	2.875	2.887	2.947	0.060	0.366
Rocky Mountain	2.920	2.937	2.991	0.054	0.418
West Coast	3.060	3.071	3.124	0.053	0.424
California	3.125	3.132	3.183	0.051	0.341

Guest Contributor:

Lynn Reaser, Ph.D., Chief Economist
Fermanian Business & Economic Institute
Point Loma Nazarene University
lynnreaser@pointloma.edu
<http://www.pointloma.edu/FBEI>
Blog: fbei.wordpress.com
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The Fed and Unintended Consequences

Last week, Federal Reserve policymakers voted to leave their primary monetary policy lever, the federal funds rate, in a target range of 0 to 1/4 percent and suggested that this target will be maintained for an “extended period.” With unemployment still high and inflation low, most of the policy officials are probably not contemplating an interest rate hike until perhaps the latter part of 2011 or beyond.

More importantly, with only one dissent, the policy-setting body voted to hold the size of its balance sheet constant by not allowing any of its \$2.1 trillion of securities to run off. The Federal Reserve now holds about \$0.8 trillion of Treasury bills, notes, and bonds and \$1.3 trillion of debt either issued or guaranteed by government agencies (Fannie Mae and Freddie Mac). Prior to its massive relief effort launched as the financial crisis escalated in fall, 2008, Federal Reserve security holdings totaled less than \$500 billion with holdings limited strictly to Treasuries.

The intent of last week’s policy announcement was to prevent monetary policy from becoming more restrictive through a shrinkage of its balance sheet, which would otherwise take place as various securities matured. The proceeds will now be reinvested in Treasury notes with maturities of two to ten years.

Federal Reserve policymakers might have hoped that financial markets would interpret this as a “pro-growth,” strategy. Instead, the dominant reaction was a new sense of concern over economic prospects. If the Federal Reserve had now turned much more bearish on the economy’s outlook, why should investors think differently? In response, stock prices dropped substantially, interest rates fell, and the dollar rallied as a “safe haven.”

The attempt of policymakers to avoid tightening in a period of economic slowing might be justified, although it is not clear how serious or prolonged this slowing might be. In any case, the decline in stock prices and rise in the dollar’s value may have cancelled the stimulative effort. Lower stock prices represent a tightening in financial conditions by raising the cost of equity capital while also reducing household wealth. A stronger dollar could reduce U.S. export potential.

The new balance sheet strategy could also have an adverse longer term impact. First, it represents a monetization of the federal debt, which could delay some of the pressure to address our fiscal imbalance. Second, it could spawn a new wave of excessive risk taking, such as help drive much of the last financial crisis. Already the “junk” or high-yield bond market has seen a resurgence of activity. Third, it could make the eventual “exit strategy” by the Federal Reserve from an aggressive support and intervention into credit markets even more difficult.

Monday Musings: Sometimes it's not how big the steps are, simply just the direction in which the steps are going.

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