

EMPYREAN

FUNDING AND MANAGEMENT

Two Trillion and Counting!! The Chinese government announced that its U.S Dollar and Treasury holdings exceeded Two Trillion Dollars in the 2nd quarter of 2009 exceeding all expectations. This massive increase has worried many economists and politicians as Chinas massive trade surplus continues to grow at an alarming rate giving the Chinese tremendous leverage over the U.S. economy. Servicing this Two Trillion Dollar surplus will haunt us for years to come as the cost of servicing this debt alone will be a massive burden on the economy. Add to it our continued deficit spending and the problem is dramatically exaggerated. If at any time, china decides to sell dollars or stops buying U.S debt, we could see a dramatic spike in interest rates across all sectors.

Add to the massive foreign holdings of U.S debt, the pace of monthly job losses accelerated in June as the U.S. economy lost 467K jobs. This marks the 18th consecutive month of payroll contraction, during which, the U.S. economy has shed 6.46 million jobs. In addition, the unemployment rate rose to (9.5%) the highest level since 1983 and the pace of losses doesn't appear to be slowing as we look to exceed the 10% unemployment mark in the very near future.

Additionally, banks and consumers continue to de-leverage balance sheets as consumer confidence slides on the heels of weaker housing figures. Increases in foreclosures, payment defaults and reduced prices keeps consumer spending down as net worth continues to drop.

There are some bright spots as banks continue to report very healthy gains in the second quarter lead by reduced borrowing costs and massive amounts of fee income and widening profit spreads over existing loans. While banks are able to borrow at close to zero cost, they continue to maintain artificial floors that are very high and are not passing the lower cost of borrowing to customers.

The housing sector reported its slowest monthly decline in over 18 months and inflation fears have subsided as consumer and producer prices continued to drop. Additionally, signs of increased activity in the debt markets show improved investor sentiment as record amounts of debt are coming to market as stronger companies continue to raise capital through the debt markets. Continued foreign investment in U.S. Treasuries is also a good sign that the world still believes in the U.S. market and continues to bet that a rebound in economic activity is around the corner.

Continued volatility and markets adjustments/corrections will continue to dominate the landscape as we maneuver through this downturn with the hope of slow-solid and steady growth going forward vs the continuous bubbles that have plagued our economy over the last decade or so. Maybe wishful thinking but I continue to remain an optimist even in these trying times.