

The Other Side of the Street November 23, 2008

Nov. 22 (Bloomberg) -- Bank of Canada Governor Mark Carney said the global financial crisis was caused in part by banking executives who thought about opera and ski trips instead of risks in their loan portfolios. Regulators and executives were “seduced” by the idea that risk was “spread thinly around the world” by packages of loans . . . Carney, 43 said he was troubled by talks he had with bank executives during the past five years. . . . “If you were having a conversation with a central banker like myself, and the chief executive drifted into opera or the ski slopes of Davos or some type of social setting, that’s an issue,” Carney told the London-based network. The credit crisis might have been prevented if other countries had regulations like Canada’s, Carney said. The country’s banks were rated the strongest by the World Economic Forum last month. “It’s like many things -- it’s excess,” Carney said in the radio interview. “Fundamentally, the ideas were sound, but they got applied too widely and ultimately by people who had forgotten about the fundamentals, or never knew the fundamentals of what they were doing.”

Comments

The foregoing is about as succinct and accurate as anything I could say. I have been astounded by the lack of “fundamental understanding” evidenced by those running hundreds of billions of dollars. The result of this lack of understanding most recently exhibited last week in the second market crash in as many months (Nov 4 high of 9711 to Nov 21 low of 7,392 a 24% drop in 13 trading days).

Thus, all the jawboning about “greatest buying opportunity of a lifetime” became yet another falling knife.

I will reiterate there will NEVER again be a time where simply plopping money into XYZ index will be a smart thing to do. Instead people who do well will do so by thinking about what they are doing and having some “fundamental understanding” of finance, economics, and trading.

Meanwhile . . . gold and silver showed some life on Friday. Crude will again some day soon. The farce that is the dollar rally will end soon as the game players will be over run by reality just as the latest stock market “rally” was.

With that said, there are now five and a half weeks to year end. This includes the abbreviated Thanksgiving week and then the December spendathon. Only the brave would be very short at this point. We instead will let the soon to be out of work try their last inning jam jobs and look forward to lots of great shorts the last week of December as the tape is manipulated.

Stock Notes

- Nov. 17, 2008 Citigroup plans to announce job cuts of up to 50,000 through attrition and layoffs as Chief Executive Vikram Pandit addresses employees in a town hall-style meeting Monday morning. Citigroup's head count would be cut to 300,000 from about 350,000 at the end of the third quarter.

Notes

- GMAC Financial Services said it submitted an application to the Federal Reserve for approval to become a bank-holding company. GMAC also said it is asking to participate in the Treasury's Troubled Asset Relief Program. [let them all eat free cheese]

Web links

Credit

- Nov. 19 (Bloomberg) -- **Credit markets from commercial mortgages to junk bonds fell to record lows as concerns grew that the slowing economy would overwhelm government efforts to stem the worst financial crisis since the Great Depression.** The average yield on high-yield, high-risk debt rose beyond 20 percent for the first time in two decades. Top-rated securities backed by subprime and commercial mortgages fell and loan prices declined as U.S. automakers lobbied Congress for government aid to stave off bankruptcy. "Everything is under a tremendous amount of pressure," said **Jamie Jackson**, who oversees government and agency debt trading at Minneapolis-based RiverSource Investments, which manages \$90 billion. Prices of leveraged loans and high-yield bonds fell as General Motors Corp., Ford Motor Co. and Chrysler LLC renewed pleas today for government aid to prevent their failure in what GM Chief Executive Officer **Rick Wagoner** said would be a "catastrophic collapse" for the economy. "Prices are in a virtual freefall," said **Martin Fridson**, chief executive officer of money management firm Fridson Investment Advisors in New York. Depression-Level Defaults? "Either the market is right and expecting a default rate considerably higher than it was in the Great Depression, or we have such profound dislocations and selling pressures going on that it really is creating extraordinary fundamental value." Commercial-mortgage securities are also plunging following reports yesterday that two borrowers with \$334 million of loans bundled into bonds were about to default. Forced selling by investment funds is causing the difference between yields on Washington-based Fannie Mae and McLean, Virginia's Freddie Mac's corporate debt to soar relative to benchmarks. The difference between yields on Fannie's two-year debt and similar-maturity Treasuries rose 19.5 basis points to a record 177.6 basis points as of 3:50 p.m. in

New York, the widest ever, according to data compiled by Bloomberg. "Risk appetite among the investor community remains more skewed towards fear rather than greed," RBS Greenwich Capital Markets analyst [Kenneth Hackel](#) wrote in a research report today. **Credit Markets Fall to Records as Confidence in Economy Wanes**
<http://www.bloomberg.com/apps/news?pid=20601087&sid=a20c1PvOLYn8&refer=home>

Commercial Real Estate

Commodities

- Nov. 18 (Bloomberg) -- **A Saudi Arabian supertanker filled with 2 million barrels of crude oil was hijacked off east Africa and is now anchored close to the Somalian coast, the U.S. Navy and its owner said.** Pirates directed the Sirius Star, the largest merchant ship ever seized, to the Eyl coastal area to the north of Somalia, navy spokesman Lieutenant [Nate Christensen](#) said by phone from Bahrain today. Saudi Arabia's state-owned shipping line, Vela International Marine Ltd., said it created negotiation teams to free the vessel and its crew of 25. "What we've seen typically in the past, the vessel will be held in anchorage off the coast in a pirate stronghold, for want of a better word," Christensen said. "We've had no communication. Sometimes it's a couple of hours, sometimes a couple of days." Ships passing close to Somalian waters carry oil from the Middle East via the Suez Canal and Asian-made goods to Europe and the U.S. Some companies including Odfjell SE, the world's largest chemicals shipping line, have said they will shun the canal because of the attacks off Somalia, threatening one of Egypt's biggest foreign-currency earners. Oil rose more than 1 percent on concerns about supplies. Frontline Ltd., the world's largest owner of supertankers, said it may divert vessels from the area though it has yet to make a final decision about sending carriers away from Somalia, Jens Martin Jensen, interim chief executive officer of the company's management unit, said by mobile phone from Singapore today. **About 11 percent of the world's seaborne petroleum passes through the Gulf of Aden en route to the Suez Canal or regional refineries.** Shipping lines should "seriously consider" sailing around Africa rather than using the Gulf of Aden, said Simon Stonehouse, a hull underwriter at Brit Syndicates Ltd., a Lloyd's of London syndicate. Insurance premiums will rise and unless the Egyptian government becomes "more actively interested" in combating piracy in the region they risk damaging the business of the Suez Canal, Stonehouse said. **Grappling Hooks** The pirates are likely to have fired grappling hooks at the supertanker, allowing them to scale the side of the ship using rope ladders, said Roger Middleton, an analyst at Chatham House, a foreign policy consultant in London. Middleton has researched Somalia for the past three years and piracy for nine months. **Somalian pirates have asked for \$1 million ransoms on average this year, he said. New supertankers cost \$148 million, according to data from Oslo-based shipbroker Astrup Fearnley. The Sirius Star is designed to carry more than 2 million barrels of crude, which at the current price would be worth about \$110 million on the New York Mercantile Exchange.** Ships are normally attacked by five or six pirates, though given the size of the supertanker as many as 15 may have been involved this time, Middleton said. Once the pirates are on board they are normally joined by others, he said. A supertanker is bigger

than the 77-story [Chrysler Building](#). The crew of the Sirius are "believed to be safe" and Vela is talking to their families, Vela said in an e-mailed statement today. The crew consists of 19 Filipinos, 2 Britons, 2 Poles, 1 Saudi and 1 Croatian. Armed Response Unlikely Saudi Arabia is unlikely to be considering an armed response to the hijacking because it may endanger the crew, according to [Nick Day](#), London-based chief executive officer of Diligence Inc., a security and intelligence group. "Once in port you've got several hundred people around there, heavily armed," said Day, a former member of the U.K.'s [Special Boat Service](#). Somali pirates are holding 250 crew hostage on board 14 merchant ships in coastal waters, according to the International Maritime Bureau, which compiles data on piracy. There have been 88 attacks against ships in the area since January, of which 36 were hijacked and 14 remain captive, [Noel Choong](#), head of the bureau's reporting center, said by phone from Kuala Lumpur today. Somali pirates seized the Faina, a Belize-flagged vessel with a crew of 17 Ukrainians, three Russians and one Latvian, on Sept. 25, the Ukrainian Foreign Ministry has said. It was carrying at least 30 Soviet-designed T-72 tanks to Kenya. The Sirius Star is anchored nearby, Puntland's Jama said. Shipping lines are increasingly forming convoys to navigate the Gulf of Aden, he said. The European Union last month joined the North Atlantic Treaty Organization, India, Malaysia and Russia in deploying vessels to combat piracy. **The capture of the Sirius Star on Nov. 15, about 420 nautical miles off Somalia, was the first seizure of a so-called very large crude carrier, the biggest vessels used to carry oil.** The vessel was last tracked on Nov. 10, leaving the Persian Gulf and bound on its original course for St. Eustatius in the Caribbean Sea, where Saudi Arabia leases oil-storage facilities from NuStar Energy LP, according to data compiled by Bloomberg. **Hijacked Oil Tanker Anchored Off 'Pirate Stronghold'**
http://www.bloomberg.com/apps/news?pid=20601207&sid=aOGqlKqx_YrE&refer=energy

- Today, the Federal Reserve is laying the groundwork for massive inflation. "Over the past year," Grant's Interest Rate Observer notes, "the central bank's balance sheet has grown by 133%. It was only yesterday when annual growth of 13% seemed aggressive, if not reckless, and certainly inflationary. Ten times that aggressive-if-not-reckless-and-certainly-inflationary rate of expansion is a fact that takes some getting used to." Over the last three months, Federal Reserve Bank credit is up 1,560%, reports Grant's. It was only in September that the Fed's balance sheet crossed \$1 trillion for the first time. On Nov. 5, it scooted past \$2 trillion. By year-end, says the president of the Federal Reserve Bank of Dallas, it could slide right on past \$3 trillion. Our Federal Reserve seems hellbent on making Argentina look like Switzerland in terms of monetary restraint. Why is this ballooning balance sheet inflationary? The Federal Reserve increases its assets by buying stuff -- financial assets of banks and others. The Federal Reserve pays for these assets by creating money that did not exist before. Of course, our government is not acting alone. Central banks across the globe are doing the same thing, if with somewhat lesser vigor, at the moment. In any event, it means paper money will buy less. We may see nominal prices -- for oil and gold and metals -- continue to fall in the short term, but long term, I think we're set up for some huge re-flation in 2009.

Currency

Diversification

Derivatives

- Nov. 18 (Bloomberg) -- The cost of protecting against default by [Warren Buffett's](#) AAA rated [Berkshire Hathaway Inc.](#) has almost tripled in two months, a sign of just how skittish investors have become amid the global financial crisis. The cost to protect against Berkshire being unable to meet its debt payments, based on credit-default swaps, is more than four times that of rival insurer [Travelers Cos.](#) At those levels, the swaps are typical of companies rated Baa3 by Moody's Investors Service, one level above junk. "If you were going to start picking companies that are going to default, you probably wouldn't put Berkshire at the top of the list, so it's totally unexpected to see them there," said [Jeff Matthews](#), author of "Pilgrimage to Warren Buffett's Omaha" and founder of Greenwich, Connecticut-based hedge fund Ram Partners LP. Of the swaps, he said: "I wouldn't buy them, and yet it's there." Standard & Poor's said Buffett's bet on the stock indexes wouldn't cause a liquidity crisis. Berkshire spokeswoman [Jackie Wilson](#) said she had passed along requests for comment to Buffett. The stock fell below \$100,000 a share for the first time in two years last week and has dropped about 33 percent this year.
Buffett's Bets The cost of protection on Berkshire [debt](#) has jumped to 415 basis points from 140 basis points two months ago, according to CMA Datavision. That translates to \$415,000 a year to protect \$10 million for five years. The median for companies rated Baa3 was 348 basis points yesterday, according to data from Moody's capital markets research group. Credit-default swaps, used to hedge against losses or to speculate on the ability of companies to repay their debt, rise as investor confidence deteriorates. The increase may be tied to a series of bets that Buffett has taken on four stock indexes across the globe, including the [Standard & Poor's 500 Index](#), according to Berkshire shareholders. Buffett sold contracts to undisclosed buyers for \$4.85 billion that protect the buyers against declines in those markets. **Under the agreements, Berkshire will pay as much as \$37 billion if, on specific dates beginning in 2019, the market indexes are below the point where they were when he made the agreements. By Sept. 30, Omaha, Nebraska-based Berkshire had written down the contracts by \$6.73 billion as the S&P declined for a fourth straight quarter.** "Greater Gains" "I believe these contracts, in aggregate, will be profitable," Buffett said in a statement in May, reiterating comments from his letter to shareholders in February. "We are always ready to trade increased volatility in reported earnings in the short run for greater gains in net worth in the long run. That is our philosophy in derivatives as well." A total of 2,450 credit-default swaps had been sold on Berkshire as of Nov. 14, protecting a net amount of \$4.7 billion, according to data from the Depository Trust & Clearing Corp., which runs a central registry for the derivatives. **Berkshire's Credit Risk Soars on \$37 Billion Bet** <http://www.bloomberg.com/apps/news?pid=20601087&sid=awMIhCcHAcXU&ref=r=home>
- Nov. 18 (Bloomberg) -- Citadel Investment Group LLC, the Chicago-based investment firm run by Kenneth Griffin, had the counterparty rating for its two biggest hedge funds cut by Standard & Poor's after posting their worst losses. The ratings were cut to BBB from BBB+ on the Kensington Global and Wellington funds, which tumbled about 40

percent this year. Further reductions are possible if the funds, which oversee \$13 billion in assets, don't improve their investment returns, S&P said today in a statement. "The downgrade reflects Kensington/Wellington's negative performance in September and October" after the bankruptcy of Lehman Brothers Holdings Inc. and the subsequent declines of stocks and bonds, Daniel Koelsch, S&P's primary credit analyst for Citadel, said in the statement. **Citadel Hedge Funds' Counterparty Rating Cut by S&P**
<http://www.bloomberg.com/apps/news?pid=20601087&sid=axLc1BT2ZXbA&refer=home>

Housing

- Nov. 17 (Bloomberg) -- **James Hardie Industries NV, the biggest seller of home siding in the U.S., scrapped its first-half dividend as earnings dropped 26 percent in the second quarter amid the worst housing slump since the Great Depression.** Net income excluding expenses on asbestos compensation and other items totaled \$36.2 million, or 8.4 cents a share, in the three months to Sept. 30, compared with \$49.2 million, or 11 cents, a year earlier, the Netherlands-based company said in a statement to the Australian stock exchange today. Full-year profit on that basis may drop 44 percent, James Hardie said. The U.S. housing market is in the third year of its worst slump since the Great Depression, with housing starts plummeting 65 percent in less than three years. The U.S. economy has slowed even as the Federal Reserve cut the benchmark interest rate in the past 14 months to 1 percent and provided more than \$1 trillion in loans to banks and other financial institutions. **"Given these current conditions, the level of uncertainty surrounding the global economy and future industry trends, and in order to conserve capital, the board has decided to omit the interim dividend for the current fiscal year,"** the company said in the statement. James Hardie fell 37 cents, or 7.8 percent, to A\$4.38 at 10:58 a.m. in Sydney trading, valuing the company at A\$1.9 billion (\$1.2 billion). The stock has dropped 32 percent this year, compared with a 44 percent decline in the S&P/ASX 200 index. **James Hardie "notes there remains significant uncertainty over the outlook for U.S. housing activity, as economic conditions and markets are severely impacting consumer and business confidence,"** according to the statement. The market for renovations and repairs has also been declining, as banks tighten lending and homeowners find it harder to justify upgrades as property values drop, James Hardie said in the statement. James Hardie said second-quarter sales fell 12 percent to \$341.9 million. Net income soared to \$153.5 million from \$19.1 million because of foreign-exchange adjustments to asbestos liabilities. **James Hardie's Earnings Decline by 26% on U.S. Slump**
<http://www.bloomberg.com/apps/news?pid=20601087&sid=aElvWIs7XJO4&refer=home>

Housing Finance

- Nov. 19 (Bloomberg) -- **Mortgage applications in the U.S. dropped last week as demand for home-purchase financing slumped to an almost eight-year low.** The

Mortgage Bankers Association's **index** of applications to purchase a home or refinance a loan fell 6.2 percent to 398.6 for the week ended Nov. 14, from 425 the prior week. The group's **purchase index** decreased 13 percent to the lowest level since December 2000. **The prospect of even bigger decreases in property values and stricter lending rules by banks may be scaring away home buyers, indicating the housing slump is likely to enter a fourth year in 2009.** The economy may be heading for the worst recession in decades as consumers and business retrench. "The intensification of economic and financial problems since September has been having a negative effect on home sales," **Abiel Reinhart**, an economist at JPMorgan Chase & Co. in New York, said in a note to clients before the report. More Refinancing The share of applicants seeking to refinance loans increased to 49.9 percent from 45.1 percent of total applications. **Confidence among U.S. homebuilders in November dropped to the lowest level since record-keeping began in 1985, according to a report yesterday from the National Association of Home Builders/Wells Fargo. The index of builder confidence decreased to 9, lower than forecast, from 14 in October. A reading less than 50 means most respondents view conditions as poor.** A Commerce Department report today is projected to show that builders in October **began work** on 780,000 homes at an annual rate, the fewest since record-keeping began in 1959, according to the median estimate in a Bloomberg survey. **Building permits** probably fell to the lowest level since 1981. Today's report also showed the average rate on a 15-year fixed mortgage decreased to 5.87 percent from 5.90 percent. The rate on a **one-year adjustable** mortgage rose to 6.80 percent from 6.77 percent the prior week. The Washington-based Mortgage Bankers Association's loan survey, compiled every week since 1990, covers about half of all U.S. retail residential mortgage originations. **U.S. MBA's Mortgage Applications Index Decreased 6.2% Last Week**
<http://www.bloomberg.com/apps/news?pid=20601213&sid=atH4rE.qc9Eo&refer=home>

Macro Economic

- Nov. 17 (Bloomberg) -- Treasury Secretary **Henry Paulson** said markets may be under stress for "months" and two of President-elect **Barack Obama's** top economic advisers agreed that further steps are needed to shore up the economy. **"There will be stress in the capital markets for a number of months,"** Paulson said at a panel discussion in Washington. He was joined at the conference by Clinton administration Treasury chiefs **Robert Rubin** and **Lawrence Summers**. "Restoring the financial system will go a long way toward helping the economy recover," Paulson said. **"There's still a good bit to be done, because the economy has turned down, housing prices are still declining."** Rubin, now a senior counselor to Citigroup Inc., predicted the crisis of confidence will abate "within a reasonable period." Summers, now at Harvard University, called for a "speedy, substantial and sustained" fiscal stimulus that seeks **to boost the economy for the next two to three years.** Paulson and Federal Reserve Chairman **Ben S. Bernanke** met earlier with House Speaker **Nancy Pelosi** and other Democratic leaders to discuss how the funds are being used and a proposal to rescue the auto industry. The Treasury

has completed about \$159 billion in preferred equity purchases of large and medium-sized banks. A total of \$250 billion of the \$700 billion has been set aside for capital injections into financial institutions. **Paulson said strains on the country's budget will require his department to sell \$1.5 trillion in Treasury debt this fiscal year, which began Oct. 1. The Treasury announced on Nov. 3 plans to borrow \$550 billion in the current quarter and \$368 billion in the January-March period.** Treasury and the Fed are working on a new plan to ease strains in the markets for car and student loans, as well as credit-card debt that "would take relatively modest amounts of TARP assets," Paulson said. "When you look at what this economy may need, it's pretty hard to believe we're going to get the kind of recovery we need with the credit markets in a number of areas still as clogged as they are." **Paulson Says Markets to Remain Stressed for `Months'** http://www.bloomberg.com/apps/news?pid=20601087&sid=a2Y_Kw_aj36E&refer=home

- Nov. 17 (Bloomberg) -- Japan's economy, the world's second largest, unexpectedly shrank in the third quarter, confirming it entered the first recession since 2001 as companies cut spending. **Gross domestic product** fell an annualized 0.4 percent in the three months ended Sept. 30, the Cabinet Office said today in Tokyo. Economists **predicted** the economy would grow 0.1 percent after contracting a revised 3.7 percent in the previous period. The slowdown that last month forced Prime Minister **Taro Aso** to propose a stimulus package is likely to worsen as export demand weakens and companies respond with investment cuts and layoffs. **Toyota Motor Corp.** and **Canon Inc.** slashed profit forecasts in the past month as U.S. consumers spend less and the yen's rise against the dollar erodes the value of sales. "It's only going to get worse," said **Masamichi Adachi**, senior economist at JPMorgan Chase & Co. in Tokyo. "Japan may be entering its deepest recession in a decade as the global financial crisis cools demand overseas." **Japan's Economy Shrinks 0.4%, Confirming Recession (Update2)** <http://www.bloomberg.com/apps/news?pid=20601087&sid=aQuULgil3JJU&refer=home>

Retail

Retirement

Risk

Savings Rate

Tech

The Fed

- Nov. 19 (Bloomberg) -- Federal Reserve policy makers last month predicted the U.S. economy will contract through the middle of 2009, with some prepared to lower interest rates further in response, a record of their meeting showed. "Some suggested that additional policy easing could well be appropriate at future meetings," the Fed said in minutes of the Oct. 28-29 Federal Open Market Committee gathering released today. "In any event, the Committee agreed to take whatever steps were necessary to support the

recovery." Fed officials cut their forecasts for inflation and growth to account for the choking off of credit to households and businesses as some of the biggest financial companies failed. Some FOMC members foresaw a risk that the inflation rate will fall below the Fed's objective of "price stability." Below Fed Target "Some saw a risk that over time inflation could fall below low levels consistent with the Federal Reserve's dual mandate of price stability and maximum employment," the minutes said. Some Fed officials felt "more aggressive easing should reduce the odds of a deflationary outcome." **Fed Chairman Ben S. Bernanke said yesterday in testimony to the House Financial Services Committee that "there are some signs that credit markets, while still quite strained, are improving." "However, overall, credit conditions are still far from normal," he said.** The U.S. economy may contract at a 3 percent annual pace this quarter, the median estimate in a Bloomberg News survey of 59 analysts this month. Economists don't expect growth to resume until the three months ending in September 2009. The U.S. economy shrank at a 0.3 percent annual rate last quarter, the most since the 2001 recession. "We are navigating the mother of all financial storms," Dallas Fed President **Richard Fisher** said Nov. 4. A recovery in the U.S. economy "will take time," Fisher said. **"I don't see any economic growth in 2009. None."** The Fed is forecast by economists to reduce the federal funds target rate to 0.75 percent by the end of December and 0.50 percent in the first quarter. The federal funds rate was last below 1 percent a half century ago, when **Dwight Eisenhower** was president. **Fed Saw Economy Shrinking Through Mid-2009 Last Month**

http://www.bloomberg.com/apps/news?pid=20601087&sid=a_slZDP2pjqs&refer=home

- Nov. 18 (Bloomberg) -- Federal Reserve Chairman **Ben S. Bernanke** said the central bank won't disclose details of the \$2 trillion in emergency loans of taxpayer funds because doing so would stigmatize banks needing the money. "Some have asked us to reveal the names of the banks that are borrowing, how much they are borrowing, what collateral they are posting," Bernanke said today to the House Financial Services Committee. "We think that's counterproductive." Bernanke and Treasury Secretary **Henry Paulson** said in September they would comply with congressional demands for transparency in a \$700 billion bank rescue plan. Two months later, as the Fed lends far more than that in separate lending programs that don't require lawmakers' approval, Bernanke said too much disclosure would harm the borrowers. **Bernanke Says Federal Reserve Won't Reveal Details on Loans**

<http://www.bloomberg.com/apps/news?pid=20601087&sid=aS1eWoJj0sKc&refer=home>

Wall Street

- Nov. 18 (Bloomberg) -- GE Capital, the lending arm of **General Electric Co.**, will cut \$2 billion in costs next year as it pares jobs, forms regional units and marks assets such as overseas home mortgages for possible sale amid a global financial crisis. The changes include a newly created chief operating officer post and take effect Jan. 1, the Fairfield, Connecticut-based company said today on its **Web site**. GE Capital will shed an unspecified number of its 75,000 jobs as the unit consolidates back offices and curbs lending in areas such as residential mortgages, Vice Chairman **Michael Neal** said in an interview. "In a world where we think liquidity is an issue and is likely to remain an issue

for a while, we're de-emphasizing in general product lines that attract a lot of debt for the amount of earnings," said Neal, who oversees GE Capital. Chief Executive Officer [Jeffrey Immelt](#) is shrinking the [finance units](#) to 40 percent of the parent's profit from about half last year as he reduces debt issued and focuses on more profitable areas. GE Capital funds its businesses using the highest-available AAA-credit rating and is betting it can continue that model without becoming a bank holding company in the U.S., Neal said. The new setup will help liquidity, he said. "They have got to protect that AAA rating," said [Bill Batcheller](#), who helps manage \$700 million in assets including GE shares at Butler Wick & Co. in Youngstown, Ohio. When the global crisis subsides, that rating "is going to be a key competitive advantage for them." GE Shares **GE Capital to Pare Jobs, Assets to Save \$2 Billion**
http://www.bloomberg.com/apps/news?pid=20601087&sid=aJd9ubB_EQSA&refer=home

- Nov. 18 (Bloomberg) -- **Bank of America Corp. will pay about \$7 billion to almost double its three-year-old stake in China Construction Bank Corp., three weeks after being awarded \$15 billion from the U.S. government to thaw frozen credit markets.** Bank of America, which is buying [Merrill Lynch & Co.](#), will boost the stake in China's No. 2 bank to 19.13 percent from 10.8 percent, the Charlotte, North Carolina-based lender said today. It will buy shares from [China SAFE Investments Ltd.](#), a state investment arm that is the Beijing-based bank's biggest stakeholder. **Bank of America isn't funding the purchase with proceeds from the government's Troubled Asset Relief Program, or TARP, said spokesman Scott Silvestri. Merrill received \$10 billion through the Treasury's \$250 billion bank-rescue package. "This is falling closely on the heels of their receiving TARP money, which was intended to spur lending in the U.S. or have bigger, stronger banks buy the failing banks," said Jaime Peters, an analyst at Morningstar Inc. in Chicago. "But neither of these things is happening."** Bank of America first invested in China Construction in June 2005, buying a \$3 billion [stake](#) before the lender was publicly listed. It invested another \$1.9 billion in June. The value of its holding almost tripled, to \$14.5 billion, as of Sept. 30, a regulatory filing showed. Bank of America plans to be "a long-term and significant strategic investor in CCB," the U.S. lender said in a statement. The new shares can't be sold until Aug. 29, 2011, without the Chinese bank's consent. The stock Bank of America bought in 2005 became eligible for sale last month, prompting analysts to suggest the U.S. lender would sell part of its stake to boost capital. Analysts and politicians should focus on how both sides can benefit from the deal, said Daniel Rosen, principal of Rhodium Group, a New York firm that advises companies on overseas investments. "People should be delighted that Bank of America is thinking long-term about its options and isn't just barricaded in their shack out in the woods," he said. "Banks have entered the political world and everything they do is going to be under the political microscope," said [Christopher Whalen](#) of Institutional Risk Analytics, a Torrance, California-based research firm. **Ken Lewis can say it's a good investment and he can probably get away with it if he doesn't have to take any more government money."** **Bank of America to Pay \$7 Billion for China Construction Stake**
<http://www.bloomberg.com/apps/news?pid=20601087&sid=ad2GOu79c.3Q&refer=home>

Don't Fight The Fed

I Disagree . . . and why

Article of the week:

- **IT WAS JOHN MAYNARD KEYNES**, a great investor as well as a great economist (the two superlatives are not always compatible, much less synonymous), who with his trademark dry humor remarked that the market inevitably managed to stay irrational longer than he could stay solvent. Since he made his fortune, as we recall, trading commodities, racy, quirky and even inexplicable market behavior was no stranger to him. All the more pity, then, try as we might, we can't seem to channel the old boy to get his acerbic fix on this year's incredible yo-yo stock market. But, whatever his precise description, we strongly suspect he wouldn't dream of accusing it of being entirely rational. **Its erratic disposition was beautifully epitomized in Thursday's wild and woolly session in which the market swung fitfully from plus to minus and minus to plus dozens of times, until when, late in the afternoon, without any visible excuse, it suddenly bolted upward, as if some mischievous prankster had given the poor confused beast a hot foot.** After being down by over 300 points, the Dow rallied with crackling esprit, topping it off with a Garrison finish that left it some 552 points higher than where it started the day. Not to be outdone, the S&P 500, which had been hammered in the early trading to the lowest level in nearly six years, bounced smartly and closed with a hardly shabby 6% gain. It was, moreover, an inclusive turnaround, with roughly three times as many stocks closing up as down. The breathtaking change of direction was rather a puzzle to simple souls like us, who tended to shrug it off as just another but scarcely the most nettlesome of life's multitude of imponderables, or merely fresh evidence, if any were needed, that emotion often tops reason as the market's motivating force. **But it drew a much different response -- something approaching jubilation -- from more than one member of that band of hardies who claim the title of market technicians.** For the uninitiated, technicians adhere to the idea that past is prologue, that all markets are cyclical and that cycles invariably repeat themselves. So they studiously consult their charts of stock-market action, sometimes stretching back to when the bids and offerings were made under the Buttonwood tree, and their copious compilations of investment history, stretching back even further, to divine what the future may hold. For all its vaguely mysterious aura, such analysis can be, we can attest, a helpful adjunct in identifying budding trends and assessing individual stocks by revealing critical nuances about strengths and weaknesses that otherwise are tough to detect. As it happens, this market has not been inordinately kind to technicians, any more than it has been to the more familiar kind of market and securities analysts. Some of the tried and true tools of the technical trade, sentiment readings are a case in point, have proved less than reliable. Sentiment is supposed to be a contrarian indicator: When the crowd is bullish big time, that's usually a sign the market's poised to take a serious dive, and, of course, vice versa. Maybe it needs to be sent to the shop for repairs, for it sure hasn't worked this way. Once the market started to crumble in earnest, sentiment measures turned bearish and got increasingly so all the way down. All the world's still anxiously waiting for a rebound that lasts more than a day or two. **As we persist in saying, this bear market is different, just as the economic storm lashing at us is different, different certainly**

from any we've suffered through for over a quarter-century. Which explains why we're so leery of the scattered exultation that gripped Wall Street after Thursday's performance (and was dampened a wee bit by Friday's droopy action). The celebrants, not a few of whom normally sneer at technical analysis as investment voodoo, nonetheless seized on the smashing snapback from the depths as proof that stocks have successfully "tested the lows" set on Oct. 10 and, they crowed, according to technical writ that means we've achieved the long sought-after but elusive bottom. Their buy-word was that the battered market had resolutely "drawn a line in the sand." (We'll forgive the anthropomorphism, if only because we occasionally indulge in it, ourselves.) But it's not the first time in the course of this year's bruising market descent that we've heard that glad cry. Trouble is, each time, it turns out, it wasn't any old sand the supposed line was drawn in, but quicksand. **FEW THINGS BUG US MORE than the notion that "stocks are cheap," which has become a kind of maniacal mantra among wounded bulls. It's not at all clear, at least to us, why the person so confidently intoning that opinion believes stocks are cheap.** That the S&P 500 index has come down nearly 40% this year does make it indisputably lower than it was on Jan. 1. But so what? For just as indisputable is that earnings have been coming down as well -- 20% in the third quarter. For the year as a whole, on a per-share basis, those earnings, according to the consensus estimates, are likely to total something like \$80-\$81. Which, if by some weird chance it is right, means the index is selling at around 11 times this year's profits. Ah, we can hear the thunderous counter, but the consensus estimate for next year is \$91-\$92 a share and, by golly, on that basis, stocks are not only cheap, they're a steal. The only problem, in our bloodshot view, with that reckoning is that with the economy growing ever more rocky by the day, logic, if it has any place in this discourse, **makes it far more likely that per-share earnings on the S&P will be \$70 or even less.** Of course, that will translate into a 12 P/E. Provided, that is, investors' funk and fury don't deepen as the global slump exacts its melancholy toll and inspires a new selling spree (which, if it's any consolation, would make stocks cheaper still). **As Morgan Stanley's Richard Berner points out in a nifty recent piece on profits, an awful lot of things on the corporate and economic scenes have turned upside down, a monumental change that somehow seems to have eluded the good old consensus.** When borrowing was no problem and times were good, Corporate America used leverage like there was no tomorrow, eagerly taking on debt for any number of louche purposes. As, for example, buying back stock to goose earnings per share and return on equity and, we might add the obvious, give a nice lift to its shares (on which management just happened to hold a bounty of options). We'd like to whisper a kind word for commodities. Not all of them, to be sure (we haven't completely lost our mind). The two we're feeling uncharacteristically kindly towards are oil and gold. Gold is a no-brainer (who was it out there who just said that automatically qualifies us to talk about it?). Our thesis is as simple as it is unoriginal: Virtually all of the civilized world and a good chunk of the uncivilized world is in a race to see who can debase its currency the fastest. The big spur here is the great global bailout and the trillions in paper money being the baling instrument of choice. We can't think of a better way to take advantage of this frenzy of financial free-fall than stowing away a few nuggets. Gold has taken its lumps along with virtually every swappable asset, hard and soft. Its current price of \$742 and change an ounce is down some \$300 from its peak. It's volatile, but so is life. You can't eat it, but it's durable and a reasonable haven. Oil, no secret, has been on the skids

ever since it set an all-time peak of \$147.27 a barrel back in July. It ended last week at a few pennies over \$57. The steepness of its decline frankly surprised us, and we don't have a decent feel for where it will be next week or next month. But OPEC, scared out of its ermine robes (a discomfort we truly enjoy watching), is slated to take another slice out of production before year's end, while the tailspin in prices may give pause to some of the more notorious cheaters in the cartel. Meanwhile, more so it seems to us than in similar fallow stretches in the past, producers have been quick to adjust to the drop in demand. And then, as our old pal Tom Petrie out in Denver puts it, the era of what he calls "Practical Peak Oil" has been delayed by the global recession. But it still looms in the not-too-distant future and promises -- or threatens -- to furnish a powerful lift to prices. <http://online.barrons.com/article/SB122670739274029945.html?mod=djemBF&page=sp>

Best of the Dog

Monday, November 10, 2008 at 11:37 CDT

Ominous

the first hours of today's action are very ugly

in particular, oil was up \$5 on the open in new york and that is now gone.

similarly the averages opened up with enthusiasm because of global government intervention and are now red.

this is very reminiscent of the action in September when the U.S. government interventions quickly were sold.

we may well be headed to another ugly move down

[Dow traded at 9200 on its way down to 7392 in the nine days after this post – the point – this is not all that difficult to see coming if in fact one wants to think for ones self instead of listen to the pumpers]