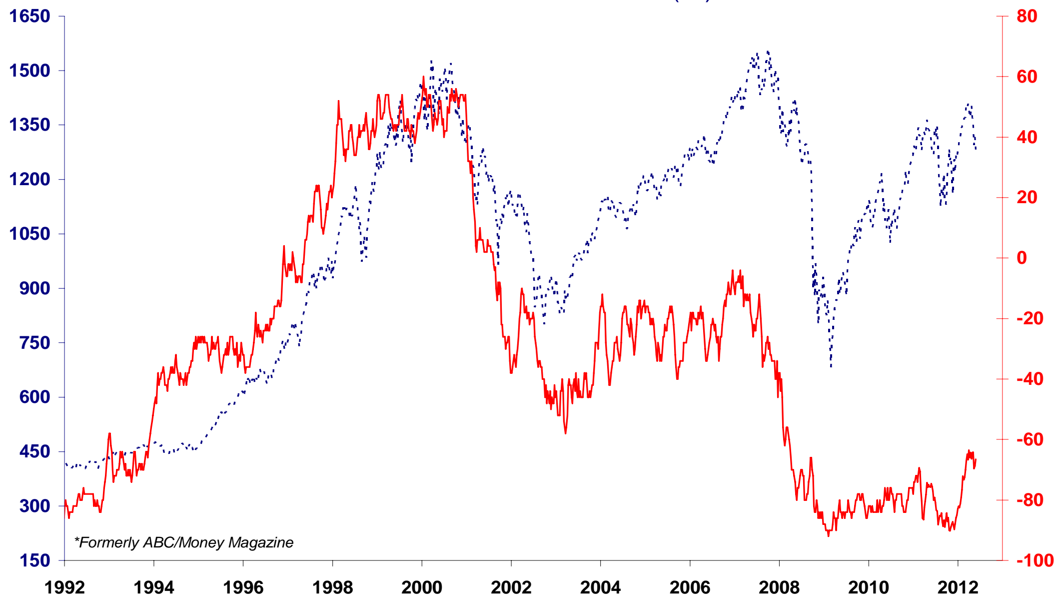
Stephanie Pomboy
212.989.3311



Third Time's A Charm?...

After watching my beloved fundamentals dragged around like Aunt Edna's dog behind the Griswold Family Truckster, I will confess some relief at the action last week. At last, **investors are beginning to acknowledge the less-than-fabulous economic reality I've been chirping about for months.** Of course, **it took a pretty good pounding to the head in the form of GDP and Payrolls. And it will doubtless take even more before they dare consider what Main Street figured out a long time ago --** ***that this whole 'recovery' has been nothing more than a paper illusion.*** Asset prices may be up in nominal terms and the economy, to which they are tied, up nominally as well. But in real terms, we've gone essentially nowhere. *(By way of reminder, 83% of the "recovery" in GDP from its pre-crisis levels has been inflation. Only 17% has been increased demand).*

Realizing that asset prices are now tilted dangerously over their skis, markets would normally get to work bringing things into a better balance. And the gap above, as it started to do on Friday, would begin to close. But in our hyper-manipulative world, that is an outcome policymakers cannot abide. **Ben will not let his single achievement be undone. It won't take too many more Dow points before the Fed is laying the groundwork for QE3.** *Indeed, I expect he will have done so in his testimony before Congress, just hours before this paper hits inboxes.*

So, here we go again. ***Right?*** **With the Fed sure to make with QE3, the fundamentals will once again be tied to the rear bumper as the markets go on another Fed-fueled joy-ride.**

Stephanie Pomboy
212.989.3311

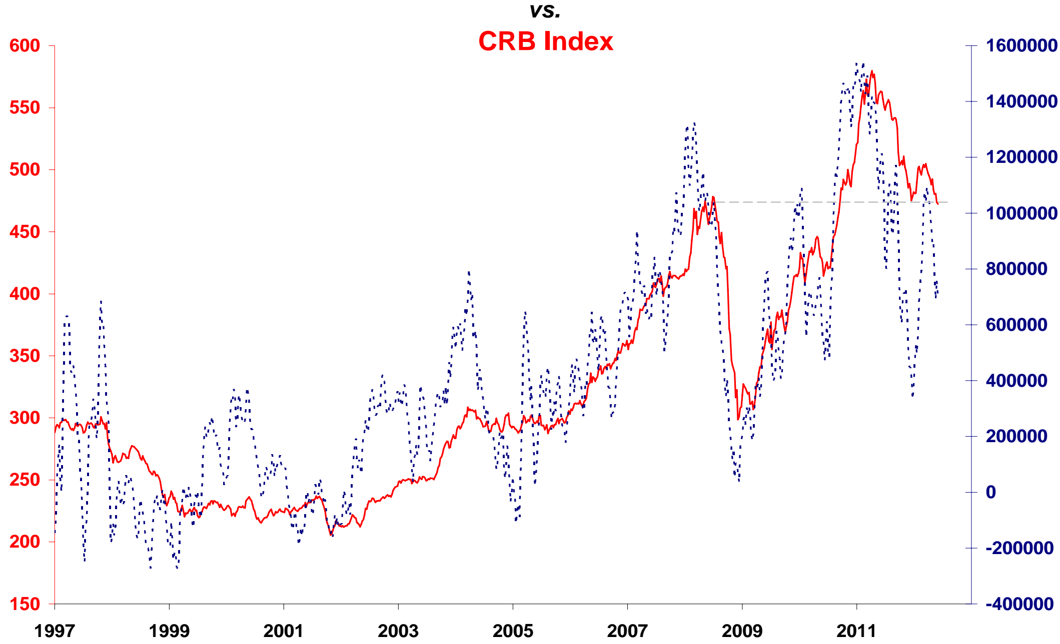
It's certainly a decent bet. **Never stand between a mother bear and her cub or the market and Fed liquidity.** ***Although…*** One can't help but note, as I have on myriad occasion, that **we are well beyond the point of diminishing marginal returns on all this QE.** As you can see above, QE2 yielded less reflationary 'oomph' than QE1, which yielded less than the conventional rate cuts before it. By the time we get to QE5 or 6, *who knows?* Maybe there will be no market fillip at all.

It would stand to reason. I mean, you have to imagine that the failure of the first two attempts has even the most hopeful characters starting to question why the third time should be any different. And while it's true that many are institutionally 'required' to dance until the music stops, it gets harder and harder to justify taking greater risk. For, **not only does each new round of QE come at lower and lower levels of confidence in the fundamental underpinnings of the US economy, but each occurs at lower and lower levels of nominal rates—*across the entire risk spectrum* – as well.**

	JUNK Yield	BAA Yield
QE1	15.17%	8.39%
QE2	8.13	5.71
Today	6.96	4.97

It's hard to imagine. But **when QE1 was initiated back in March of 2009, Junk yields were trading north of 15%!** At 6.96% **today, your average Junk investment doesn't even fulfill minimum pension fund return mandates.** Which means, if I may fill in the blanks, that those managers must resort to leverage if they mean to fill the return gap. **With Europe threatening to split apart, China slowing rapidly and the US speeding toward the fiscal cliff, do you really want to buy Junk, *WITH LEVERAGE (!!)*, right now?**

Stephanie Pomboy
212.989.3311



It's no wonder, then, that **each successive QE results in LESS financial asset inflation and MORE commodity price inflation. If you can't get the returns you need in conventional assets without taking inadvisable risk, why not explore "alternatives"?**

	EM stocks	S&P 500	Commodities	Gold
QE1	**120%**	**70%**	46%	44%
QE2	41%	33%	**50%**	**64%**
QE3	?	?	?	?

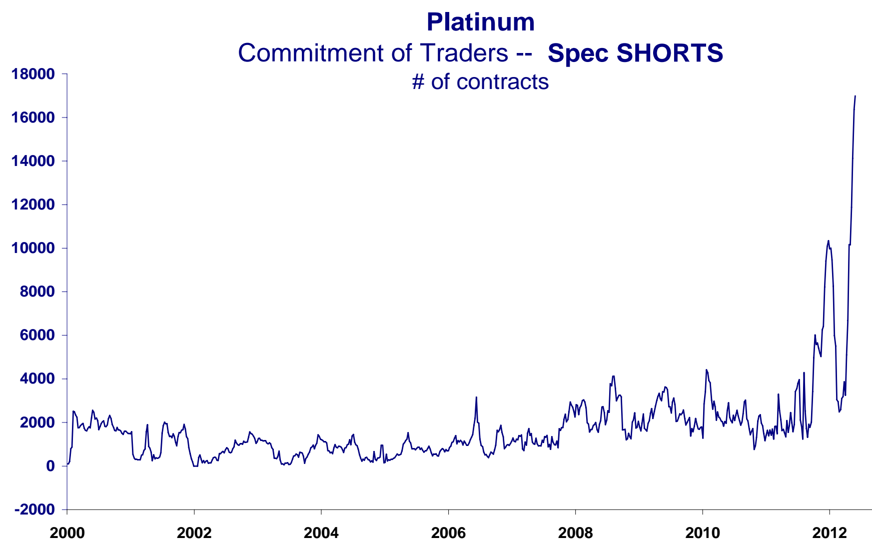
To say nothing of the rising preference for hard assets that all this dollar debasement engenders around the globe. US investors may take comfort in the idea that the dollar is 'less bad' than its major global competition. But our creditors (who are getting paid back in all this funny money) aren't the least impressed. Their loans to (and reserves held) in all of these currencies are being debased away, just at varying rates of speed. **Determined to preserve whatever value they can, they have turned increasingly to hard assets. Their steady and silent 'bid' is evident in the chart above.** Even as speculators have slashed their long exposure BY HALF on global slowdown fears, the CRB has only declined to its 2008 pre-crisis peak.

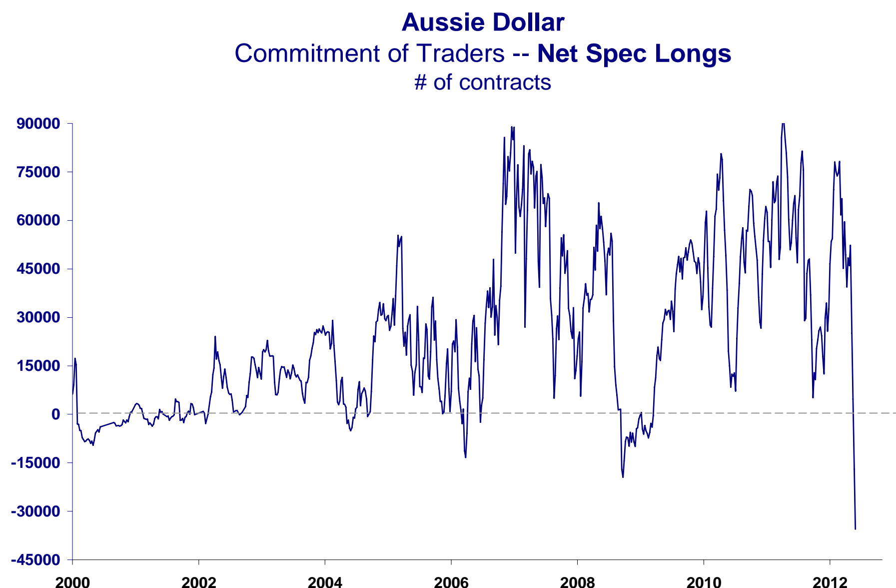
MacroMavens

Stephanie Pomboy
212.989.3311

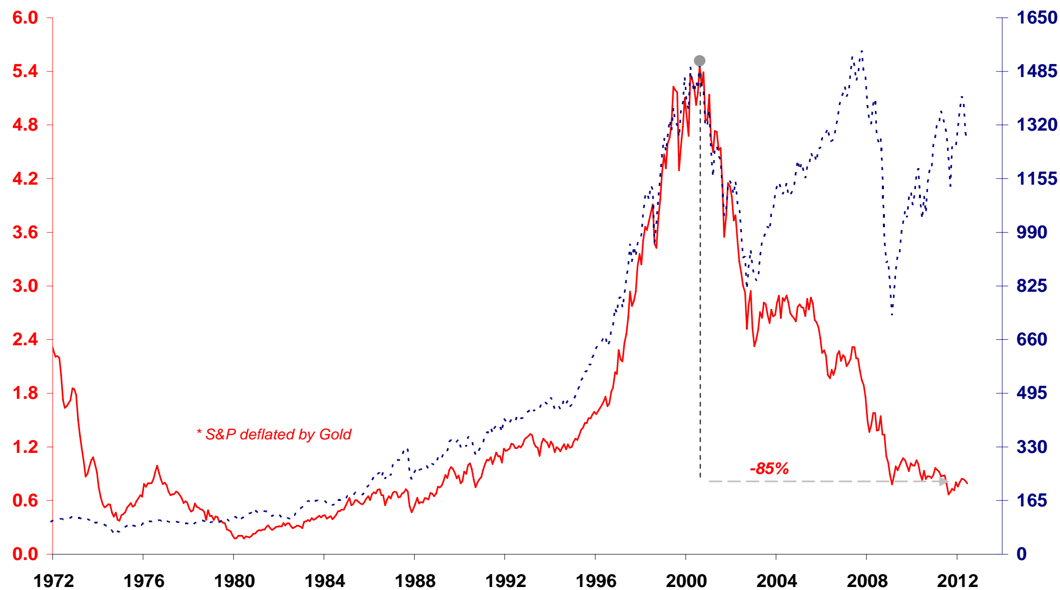
And that, my friends, is where things get interesting! **In a market notable for its well-deserved lack of conviction, there is one area in which investors are resolutely confident.** The weekly CFTC trader commitments reveal ***unprecedented*** **positions now being staked-out on the short side of many major commodities and the resource currencies tied to them.**

These aren't just your run-of-the-mill wagers on a global slowdown. As you can see below (and addenda), **we've never seen anything like this in terms of speed and magnitude.** Specs were net long 52k contracts in the Aussie Dollar at the beginning of May. Four weeks later they are net short -35k contracts! Copper shorts, have climbed 40% over the same 1 month stretch. Meanwhile smaller markets, like Palladium and Platinum have seen short positions double and quintuple, respectively, in the last TWO months!





Stephanie Pomboy
212.989.3311



That the one thing about which investors have conviction these days is that commodity prices are headed *lower* is a testament to how little progress we've made wringing an understanding of the true impact of QE. Four years in, **Wall Street still doesn't see the results of QE as purely inflationary.** Yet, to Main Street, it's plain as day (see addenda).

Even **more dangerously, investors seem to view the wanton destruction of the world's reserve currency as having no long-term consequences.** They still have their heads buried in the cozy bosom of relative performance, content to play the minute-to-minute swings in the performance of one flimsy piece of paper versus another. **Nothing could be more illustrative of their allegiance to the primacy of paper than the rush to the Yen as a safe haven in the turmoil last week?!** Here the BoJ has redoubled its efforts to coax forth inflation and, courtesy of two decades of deflation, has AMPLE room to print money. To say nothing of the fact that an aging population that must now sell JGBs to fund its retirement will increasingly "require" the BoJ to pick up the deficit-financing slack. **The fact that the BoJ has seemed less shamelessly debauched than its monetary counterparts makes the currency a 'safe haven'*??!!#$!***

Meanwhile, **the collective actions of ALL these developed-world central banks are surely speeding us toward an unpleasant reckoning.** Either the debasement of all the world's developed currencies will push global creditors to the point they say enough's enough, or the ability to print unchecked will drive commodity prices to the point they break the back of global economy. Either way, there will be consequences and they won't be pretty.

But, **even if the third time isn't the charm on wringing that acknowledgement, there is every reason to expect QE3 here in the US** (and similar action in the Eurozone) **will beget more of the same result.** The returns on financial assets will be smaller than they were the last time around. And the returns on hard assets will be greater. *And someone now shorting the heck out of platinum, palladium, copper and resource currencies is going to get spanked hard.*

MacroMavens is the exclusive trademark of MacroMavens, LLC. The commentary released under its banner may **not be forwarded**, reproduced or referenced without the express consent of **MacroMavens**. While we presume the information and data contained herein to be accurate, it is not guaranteed.

Stephanie Pomboy
212.989.3311