

The King Report

M. Ramsey King Securities, Inc.



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Today – SPMs are down 14.60 in Sunday night trading because Obama’s chief economic adviser, Larry Summers, asserted while appearing on Fox News Sunday, that the economic freefall is over but, **“I expect the economy will continue to decline... [with] sharp declines in employment for quite some time this year.”** <http://www.reuters.com/article/newsOne/idUSN2441697520090426>

BN: *“The anticipation over the white paper appears to be much ado about nothing,” said Josh Rosner... “The most significant numbers provided by the Fed in the paper appear to be the page numbers.”...*

“A lot of triple talk,” said Jim Glickenhaus... “I think they’re going to say while things are bad, the end is not at hand. Maybe.”

“The question I have, by using fourth-quarter numbers, is this skewed positively?” said Lawrence Kaplan, an attorney with Paul Hastings, who served as a senior attorney in the chief counsel’s office at the Office of Thrift Supervision. “Because January and February were pretty lousy, and as a result that’s when it hit the fan.” <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aCr3TWsU8dtg>

As most people guessed, the ‘stress test’ is an innocuous exercise based on rosy economic projections. Besides, why is a ‘stress test’ needed when there are already three agencies (Fed, FDIC, OCC) that apply metrics to measure banks’ solvency and financial condition?

Table 1
Economic Scenarios: Baseline and More Adverse Alternatives
 (Minus signs indicate negative values)

	2009	2010
Real GDP ¹		
Average Baseline	-2.0	2.1
Consensus Forecasts	-2.1	2.0
Blue Chip	-1.9	2.1
Survey of Professional Forecasters	-2.0	2.2
Alternative More Adverse	-3.3	0.5
Civilian unemployment rate ²		
Average Baseline	8.4	8.8
Consensus Forecasts	8.4	9.0
Blue Chip	8.3	8.7
Survey of Professional Forecasters	8.4	8.8
Alternative More Adverse	8.9	10.3
House prices ⁴		
Baseline	-14	-4
Alternative More Adverse	-22	-7

<http://online.wsj.com/public/resources/documents/scap2009424.pdf>

A major problem with the ‘stress test’ is it depends on modeling and it’s the precise practice responsible for much of this economic and financial mess. It’s extraordinary that so many people believe that the Fed and Treasury, after missing the financial disaster, housing debacle, recession and derivative implosion,

can now extrapolate economic conditions and resultant financial affects from its models. How did all that rocket-science modeling for subprime defaults and securitization workout? Yet many people already forget or ignore this reality.

Here's another reality that most investors are missing – banks must raise more capital. So who's the patsy in recent days that has been driving financial stocks higher? The FT: **Fed will seek bank capital increase** *Some of the country's biggest banks will be asked to raise more capital by US authorities following the completion of bank stress tests, senior Federal Reserve officials said on Friday.*

<http://www.ft.com/cms/s/0/cab07cf6-30fb-11de-8196-00144feabdc0.html>

BN: Banks May Need \$1 Trillion After U.S. Tests, KBW Says

<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aj5XjJ6xwN6Y>

What few analysts realize is that economic 'muddling', the best case scenario for the next two years, gives no relief to an economy burdened with record debt. If you lose a high paying job and you are struggling to pay your debts, you will not suddenly be able to pay your debt with a job a Wal-Mart.

What analysts should do is quantify the US private and public sector debt load and then extrapolate the needed income and GDP to service the debt. And then they should calculate how much debt will implode with little or no income and GDP growth.

The 'real budget deficit', "Treasury Gross Public Debt", is now \$1.85 Trillion (Barron's p. M70).

The most disturbing aspect of the current scheme to manipulate markets, economic data and industrial data into something benign enough to increase consumer confidence and reinflate assets is that it is the precise scheme that Easy Al and others perpetrated over many years. And it created the current mess.

Solons again are trying to inflate assets to a level that is a huge disconnect with economic reality in the misguided belief that they can paper over structural US economic problems and fostering 'confidence through asset bubbles' that will translate into economic activity. We are back to square one in 'the new economy' gambit.

And because we are back to square one in 'the new economy' of inflating assets to paper over problems, the markets are diving back into inflation mode. Commodities are soaring; bonds are struggling even with Fed support and the dollar is finally buckling.

The WSJ: **Commodities Throw a Curveball** *...the extreme steepness of the current contango, with oil a year out trading 20% above the May 2009 contract, points to a more complex situation... An upward-sloping curve is indicative of there being a surplus of oil relative to real demand. Funds buying oil futures push up forward prices, steepening the curve's upward slope... [It's inflation expectations.]*

Optimism regarding industrial metals rests on similarly fragile foundations. Bellwether copper is up 43% since late February. This head fake comes courtesy of China cannily stockpiling inventories of raw materials like copper and iron ore even as demand contracts virtually everywhere else.

Stockpiling, however, isn't consumption. The surge in Chinese imports hasn't been matched by increases in industrial production, suggesting metals are going into warehouses, not factories.

<http://online.wsj.com/article/SB124049947981448239.html>

The FT: **China reveals big rise in gold reserves** *China has quietly almost doubled its gold reserves to become the world's fifth-biggest holder of the precious metal, it emerged on Friday, in a move that signals the revival of bullion after years of fading importance...The news could spark interest in gold among other central banks. "When the largest holder of foreign exchange reserves discloses an increase*

in gold holdings, other countries may decide to think more carefully about underweight gold positions,” said John Reade, a precious metals strategist at UBS.

<http://www.ft.com/cms/s/0/1d23f80c-30aa-11de-bc38-00144feabdc0.html>

Over the past few years we have warned that when the Fed or government extends the business cycle inflation results. Stocks are now disconnected to economic reality, just like in 2007. At that time, Goldman’s CFO warned that the stock market was at the biggest disconnect with the credit market in his career. Gold, oil and commodities then soared until the bust in July 2008.



Gold, June Future – about to break out



Copper, Continuous Future Contract



Oil, Continuous Contract – about to soar

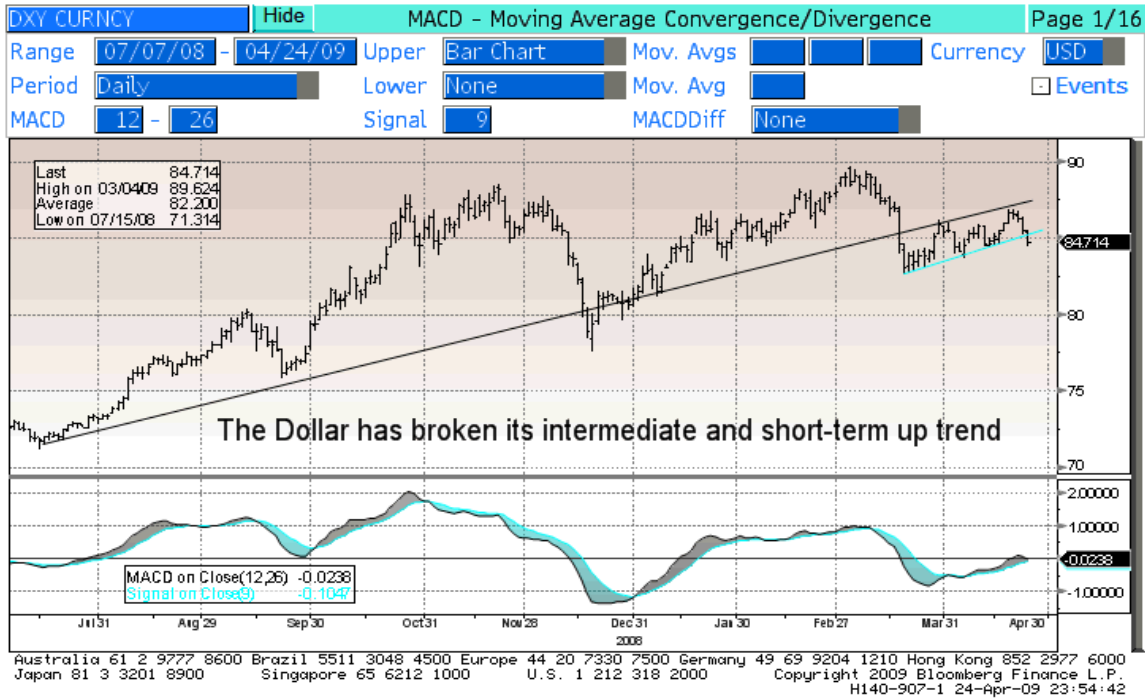


CRB Index – saucer bottom, looking to soar

We have been content to sit and watch the markets as long as the dollar was firm. But now it’s time to protect purchasing power, which is what China is doing. **China has made the empirical decision that it would rather hold commodities, real assets, instead of dollar-denominated paper.**

The Economist: **Is China souring on the dollar?** *China is America’s largest creditor... China’s government bought around one quarter of the net increase in Treasuries over the past two years. But just as Washington needs to sell record amounts of debt to fund its soaring budget deficit and to bail out its banks, there are signs that Beijing’s appetite for American debt may be shrinking.*

... China’s reserves fell in January and February. Taking the first quarter as a whole they rose by just \$8 billion, compared with \$154 billion a year earlier. Chinese officials have voiced pointed public worries about the effect of America’s massive fiscal and monetary expansion on the value of China’s dollar holdings... The combination of falling reserves and rising rhetoric has fuelled fears that China is turning its back on the greenback. http://www.economist.com/finance/displaystory.cfm?story_id=13527242



The Dollar Index with MACD, which is about to signal a sell from a dangerous level

Bonds are heading south, and unless Bernanke wants to monetize the bulk of the coming \$3 Trillion plus in US debt issuance, they will continue to decline. If Ben increases his monetization, the dollar will collapse and the real crisis will commence.

The Fed's next bond purchases are scheduled for April 27 and April 30. The Treasury said it will auction \$40B in 2s on April 27, \$35B in 5s on April 28 and \$26B in 7s on April 29...The Treasury is scheduled to announce on April 29 its issuance of 3s, 10s & 30s for the 1st week of May.

iStock Analyst: **The Fed: Our Next Troubled Bank** *The Fed now also owns more than \$355 billion of mortgage backed securities and \$61 billion in debt issued by Fannie Mae, Freddie Mac, and Ginnie Mae. Term auction credit comes to \$455.8 billion...The Fed is also holding \$238 billion in commercial paper as part of an October 2008 program to help corporations fund short-term debt obligations...*

- *The quality of the balance sheet of the U.S. central bank is deteriorating.*
- *The Fed is now heavily burdened by the same kind of crappy paper that has been hammering private U.S. banks for several quarters.*
- *And the Fed banks are holding total capital of just \$45.7 billion against the sum total of \$2.19 trillion in assets, meaning the Fed is leveraging its capital 48-to-1. That compares to only 27-to-1 two years ago...* <http://www.istockanalyst.com/article/viewarticle/articleid/3206140>

Ambrose Evans-Pritchard: *The world is running out of capital. We cannot take it for granted that the global bond markets will prove deep enough to fund the \$6 trillion or so needed for the Obama fiscal package, US-European bank bail-outs, and ballooning deficits almost everywhere.*

http://www.telegraph.co.uk/finance/comment/ambroseevans_pritchard/5220118/The-capital-well-is-running-dry-and-some-economies-will-wither.html

This is why governments are engaged in record intervention, credit creation and monetization.

The Telegraph: **Bank of Japan governor says US must tackle household debt**

<http://www.telegraph.co.uk/finance/economics/5212044/Bank-of-Japan-governor-says-US-must-tackle-household-debt.html>

The Telegraph: **Time to bail out of Britain?** *After the worst budget in memory, it may be time to leave the country. Here, our correspondents guide you through the options abroad.*

<http://www.telegraph.co.uk/finance/financetopics/budget/5209526/Time-to-bail-out-of-Britain.html>

BN: **Insider Selling Jumps to Highest Level Since '07 as Stocks Gain** *Executives and insiders at U.S. companies are taking advantage of the steepest stock market gains since 1938 to unload shares at the fastest pace since the start of the bear market...*

"Insiders from New York Stock Exchange-listed companies sold \$8.32 worth of stock for every dollar bought in the first three weeks of April, according to Washington Service... That's the fastest rate of selling since October 2007... The \$42.5 million in insider purchases through April 20 would represent the smallest amount for a full month since July 1992

<http://www.bloomberg.com/apps/news?pid=20601213&sid=au8cyqeJFifg&refer=home>

Another disturbing sign for the stock market comes from Barron's "Spring 2009 Big Money Poll". Money Managers are rapidly bullish (even though public money flows are negative per Trim Tabs).

59% of respondents are 'very bullish' or 'bullish' (54%). Only 13% are 'bearish'. But only 26% expect to be net buyers of stocks over the next six months... 84% are bearish on US Treasuries; only 3% are bullish... 32% are bullish gold; 24% are bearish. <http://online.barrons.com/article/SB124061344550254577.html>

Bulls cite the \$3.8 Trillion in money markets as fodder for further rallies but per our assertion, instead of looking at percent of cash in portfolio solely, one should also compare the cash to amount of debt... Long-term readers will recall that several years ago when bulls were heralding the enormous amount of cash on corporate balance sheets we warned that debt was growing at a multiple of that cash.

The public is withdrawing funds and the bulk of this rally has been short-covering, wise guys and banks, particularly Goldman Sachs, who now accounts for more than 50% of NYSE program trading... 56% think stocks are undervalued; only 13% say overvalued.

Bloomberg: **Goldman Sachs Boosts Risk-Taking at Fastest Pace on Wall Street** *Goldman Sachs's so-called value-at-risk, the amount the New York-based bank estimates it could lose from trading in a day, jumped 22 percent to \$240 million in the first quarter...*

Barron's Michael Santoli: **This Rally Has an Uneasy Feel** *Final-hour surges and air pockets, common lately, unnerve the methodical investor. Related to this, the upending of popular "quant" hedge-fund strategies in recent weeks has encapsulated the vexing cadence of things...*

The apparent gaming of newly popular leveraged exchange-traded funds late in the day is another wrinkle, especially pronounced in relatively new funds that deliver triple the daily return -- or triple the inverse daily return -- of indexes and sectors. Without delving too deeply, to achieve their daily return objectives, these funds always need to trade in the same direction of that day's move. Knowing this, traders attempt to quantify and front-run this action... "Is it me, or does it seem the dominant game in town is gaming ETF methodology?" asked veteran trader Adam Warner on his Daily Options Report blog last week. It's not just him. <http://online.barrons.com/article/SB124061358501154645.html>

In 1987, program trading put a 25% rally into stocks from April to August. Most everyone thought this was great. By late October, most people realized how pernicious program trading could be. But in the US, solons love manipulation and gaming when it is on the upside because it aids and abets their 'new economy' of asset bubbles to paper over declining US living standards.

But eventually the sell button is hit and all that leverage and gaming appears on the downside. And as history shows, stocks decline much faster than they rally.

Rick Bookstaber (Devil of Our Own Design): ... *the hot area now is high frequency trading. And no wonder. There are two areas that were spared in the 2008 debacle: macro and high frequency trading... Every year, people pile on to whatever strategy did well the previous year – this tendency is worth a book or two on its own – and so this year high frequency is destined to be the darling of the fund of funds.*

But I think the days for high frequency trading are numbered. For one thing, high frequency trading is capacity constrained like few other strategies. The high frequency trader is basically a stand-alone market maker; he is sitting there to provide liquidity to others. And one way he provides it is to pull in the positions that others will shortly be demanding – thus the need for speed. If the footprint for high frequency traders gets too large, they become liquidity demanders themselves, and the gig is up. The Renaissances of the strategy will make their way through, but generally we will see a lot of shooting stars.

A second reason is that high frequency trading is embroiled in an arms race. And arms races are negative sum games... <http://rick.bookstaber.com/2009/04/arms-race-in-high-frequency-trading.html>

Once again the scheme of creating better than expected economic data in the current month by revising the previous month lower occurred on Friday. Durable Goods Orders declined 0.8% in March; -1.2% was expected. But February was revised to 2% from 3.9%. And this is being spun as good news!!!

The extremely bullish sentiment is being fed by this chicanery that tries to euchre people into believing that the economy is bouncing. One month ago, people heralded the 3.9% jump in Durable Goods Orders as a sign that the economy had bottomed and was turning up. But that gain has now been cut in half.

But few people notice the February revision and focus on the modest better than expected March data.

We will again walk through the math on the scheme. If January had 1000 units of Durable Goods Orders, February was originally reported to be 1039 units. Based on this data, March was expected to be -1.5% or 1023 units. But now February has been revised to 1020 units. So March units are -0.8% or 1012.

Ergo Durable Goods Orders in reality is worse than expected in absolute units but due to economic statistical manipulation a better than expected month over month number has been manufactured so the bullish case can be presented.

New Home Sales were the opposite. February was revised higher so March is lower than expected on a month over month basis (-0.6% vs. 0%) but better than expected on a unit basis (356k vs. 337k).

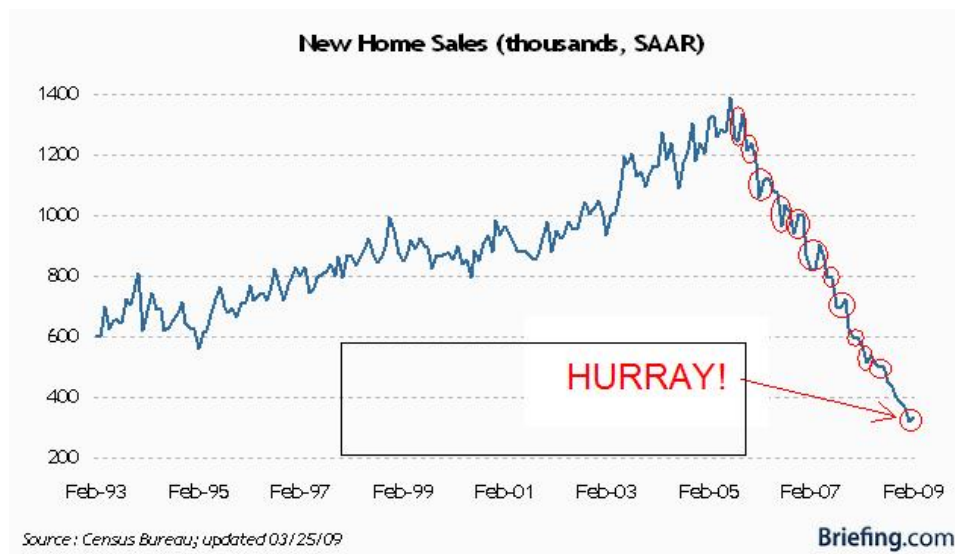


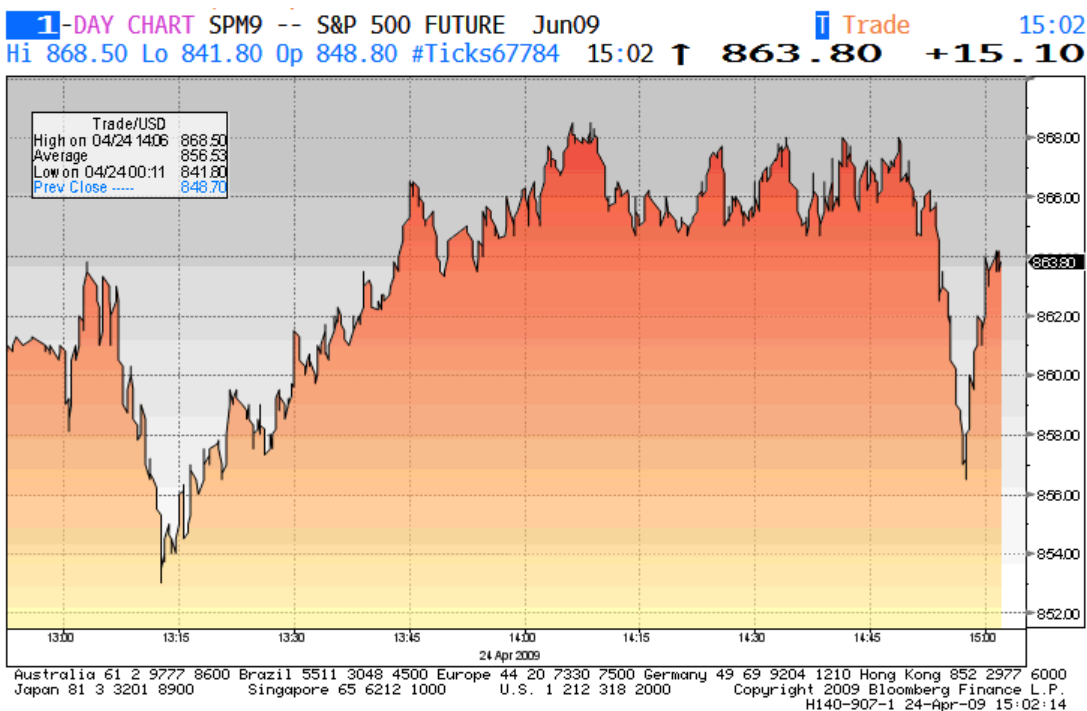
Chart courtesy of Mark Hanson

Ford's smaller than expected loss boosted stocks. Operating cash flow improved to a \$41.1m per day share drain from \$83m per day in 2008. This type of result, a slower rate of deterioration, is what is driving the 'second derivative rally'.

Hope that the slower US economic deterioration is bullish for the economy and stocks induced traders to pour back into 'the inflation trade'. Stocks, commodities and forex soared; bonds and the dollar tanked.

The 'second derivative rally' is tantamount to believing that a person is about to recover because after losing three quarters of blood very quickly, the remaining two quarts are exiting at a slower rate.

Stocks lost 50% of their rally in the waning minutes of trading on Friday as traders liquidated for the weekend. But at the close, manipulation pushed stocks back to a triple digit gain. Sanctioned deceit and manipulation has turned the markets into a rigged casino in which a handful of insiders profit.



Reuters: **U.S. mass layoffs rise to highest on record** *Large-scale U.S. layoffs rose again in March, according to Labor Department data on Thursday, as the economy struggles with what many expect will be the country's worst post-World War II recession.*

Last month witnessed 2,933 more mass layoffs, defined as affecting 50 or more workers, than February. This brought the total number of people who lost their jobs in this manner to 299,388, the highest on a record that dates back to 1995.

<http://www.reuters.com/article/newsOne/idUSTRE53M48M20090423>

Bloomberg: **Bear, AIG Dumped \$74 Billion in Subprime, CDOs on Fed; Fed's Bear Losses Dominated by Commercial Real Estate** *The Fed's losses included writing down the value of commercial-mortgage holdings by 28 percent to \$5.6 billion and residential loans by 38 percent to \$937 million as of Dec. 31, the central bank said.*

<http://www.bloomberg.com/apps/news?pid=20601109&sid=aP2XyOHiRSGL&refer=home>

American Express Co. is eliminating paper statements to potentially millions of corporate cardholders. There should be a negative hedonic adjustment for consumers.

The NY Times: **New Worries for Next Tier of Banks** *While Citigroup and Bank of America remain troubled, regional banks subject to the government's tests — including Regions Financial of Alabama, SunTrust Banks of Georgia and KeyCorp and Fifth Third of Ohio — are girding for huge losses.*
http://www.nytimes.com/2009/04/25/business/economy/25bank.html?_r=1&th&emc=th

Regional and community bank executives tell us these banks do not have the ability to dump real estate like the large banks because the hit to capital could put them in jeopardy or insolvency. **Many are sitting on foreclosures and foreclosed properties. Ergo, the hidden supply of real estate is enormous.**

AP: **Finance officials at odds over IMF funding plan** *At issue is how to supply a portion of the \$1.1 trillion increase in resources for the IMF and other lending institutions...The rich nations had hoped to get China and the other nations to commit to billions of dollars of support for that effort at these meetings. However, those countries are insisting that the IMF consider issuing bonds as a way to raise the support...* <http://apnews.myway.com/article/20090425/D97PG3JG0.html>

Auctions for Troubled Property Loans Jump to the Web
<http://www.nytimes.com/2009/04/25/business/economy/25debt.html?th&emc=th>

Rep. John Dingell (D-MI): **Nobody in This Country Realizes That Cap-and-Trade is a Tax'**
<http://www.breitbart.tv/html/325633.html>

AP: *Former House Speaker Newt Gingrich says a Democratic proposal to limit global warming pollution [cap & trade] will "punish the American people" with higher energy costs and lost jobs.*
http://www.breitbart.com/article.php?id=D97P0JM80&show_article=1

Rasmussen: **70% Say Big Government and Big Business On the Same Team**
http://www.rasmussenreports.com/public_content/business/general_business/70_say_big_government_and_big_business_on_the_same_team

Rasmussen: **53% Say Next President Likely To Be A Republican** [This is an attempt to neutralize racial bias in presidential polling, which is a new problem.]
http://www.rasmussenreports.com/public_content/politics/general_politics/53_say_next_president_likely_to_be_a_republican

Rasmussen: **Election 2010: Pennsylvania Republican Senate Primary; Pennsylvania Senate Primary: Toomey 51% Specter 30%**
http://www.rasmussenreports.com/public_content/politics/election_2010/election_2010_senate_elections/pennsylvania/election_2010_pennsylvania_republican_senate_primary

The NY Times: **Doctor Shortage Proves Obstacle to Obama Goals** [Tort reform would be a start to remedying cost and supply problems in regard to health care.]
<http://www.nytimes.com/2009/04/27/health/policy/27care.html?partner=rss&emc=rss>

The Times: **EDF strikers cut power to French homes** *It was the second time in a week that blackouts had hit the Paris region as striking gas and electricity workers adopted radical tactics to support their call for a 10 per cent pay rise and an end to outsourcing of jobs.*
<http://www.timesonline.co.uk/tol/news/world/europe/article6150447.ece>