



Black Swan Capital
Currency Currents

Friday 12 June 2009

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Key News

- [European industrial production dropped by the most on record in April](#) as the worldwide recession ravaged demand for goods. (Bloomberg)
- [German wholesale prices fell 9 percent in May from a year earlier](#), the largest decline in nearly 23 years as Europe's largest economy wallows in recession, the Federal Statistical Office reported Friday. (AP)
- [European governments have approved \\$5.3 trillion of aid](#), more than the annual gross domestic product of Germany, to support banks during the credit crunch, according to a European Union document. (Bloomberg)
- [Treasures rose for a second day](#) after Japanese Finance Minister [Kaoru Yosano](#) said his country's confidence in U.S. government debt is "unshakable." (Bloomberg)
- [China's new lending doubled in May](#). (Bloomberg)
- [Dueling Forecasts: The World Bank said Thursday](#) it expects the global economy to contract by "close to 3%," far bleaker than the bank's March estimate of a 1.7% contraction, partly because of a slowing stream of cash and investment to the developing world. But a global recovery in 2010 may expand at a 2.4% clip, according to a briefing paper by **the International Monetary Fund**, which credits the faster-than-expected rebound to stimulus spending by developed nations. (WSJ)

Key Reports Due Today (WSJ):

8:30 a.m. May Import Prices: Expected: +1.5%. Previous: +1.6%.

10:00 a.m. Mid-June Reuters/U Mich Sentiment Index: Expected: 69.8. Previous: 67.9.

Quotable

"Action is purposive conduct. It is not simply behavior, but behavior begot by judgments of value, aiming at a definite end and guided by ideas concerning the suitability or unsuitability of definite means. . . . It is conscious behavior. It is choosing. It is volition; it is a display of the will."

Ludwig von Mises

FX Trading – The \$18,100,000,000 question!

The numbers are staggering...really incomprehensible...it's the kind of stuff that if you made it up no one would believe you...I'm talking about the amount of money both the US and European Union have committed to this crisis:

- The US government and Fed spent or lent or committed **\$12.8 trillion**, an amount that approaches the value of everything produced in the country last year.
- European governments have approved **\$5.3 trillion** of aid, more than the annual gross domestic product of Germany (\$3.3 trillion).

If we break the US spending down to per person living in the US, we get:

\$12,800,000,000,000 divided by roughly 304,000,000 = \$42,105 per person

Now I know what you're thinking; if our government, in its infinite wisdom simply doled out that much money directly to every man woman and child, you can bet our crisis would be solved. Heck, in the Crooks family alone, four kids, my wife, and I would have racked up a cool \$252,630! Granted, the kids would want their pound of flesh given that all are of age, but still, we could have paid off a whole lot of debt and bought some pretty cool toys with that, deleveraging and stimulating along the way. And I bet you a dollar to a donut that I could more efficiently spend that money than some government agency that's only trying to "help" me by saving various dinosaur financial institutions and companies throughout our fair land.

Before I went off that tangent, I was going to say that what is really quite amazing is that with a total of....

\$18,100,000,000,000

...committed by the US and Europe, one wonders about a couple of things:

- 1) How in the heck can banks screw up so catastrophically? Still an open question.
- 2) Why in the heck don't we have ragging inflation by now? Still an open question.

When you consider that other governments besides the US and EU (China has been busy along with Japan, Brazil and Russia) are into the money pumping game, and we haven't seen a whole lot in the way of global traction in demand, and even more surprisingly we haven't seen any inflation per se from the "growing" countries, it has to make one very nervous.

In fact, as John Ross pointed out yesterday, we keep seeing deflation instead. Just today, as highlighted in the key news above, **German wholesale prices fell 9% in May from a year ago!** Say what? Yikes!!!!

And did anyone notice **US consumer prices went negative year-over-year for the first time since 1954!** Yikes!!!! [Highlighted below; source Economagic]

Annual Inflation Dec-Dec 1914 to 2008:

1914	01	1.000
1915	01	1.980
1916	01	12.621
1917	01	18.103
1918	01	20.438
1919	01	14.545
1920	01	2.646
1921	01	-10.825
1922	01	-2.312
1923	01	2.367
1924	01	0.000
1925	01	3.468
1926	01	-1.117
1927	01	54-2.260
1928	01	-1.156
1929	01	0.585
1930	01	-6.395
1931	01	-9.317
1932	01	-10.274
1933	01	0.763
1934	01	1.515
1935	01	2.985
1936	01	1.449
1937	01	2.857
1938	01	18-2.778
1939	01	0.000
1940	01	0.714
1941	01	9.929
1942	01	9.032
1943	01	2.959
1944	01	2.299
1945	01	2.247
1946	01	18.132
1947	01	8.884
1948	01	2.734
1949	01	-1.830
1950	01	5.803
1951	01	5.965
1952	01	0.907
1953	01	0.599
1954	01	-0.372
1955	01	0.374
1956	01	2.828
1957	01	3.040
1958	01	1.756
1959	01	1.519
1960	01	1.360
1961	01	0.671
1962	01	1.233
1963	01	1.646
1964	01	1.198
1965	01	1.920
1966	01	3.359
1967	01	3.281
1968	01	4.706
1969	01	5.899
1970	01	5.570
1971	01	3.266
1972	01	3.406
1973	01	8.941

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1974	01	12.095
1975	01	7.129
1976	01	5.036
1977	01	6.678
1978	01	8.989
1979	01	13.255
1980	01	12.354
1981	01	8.912
1982	01	3.826
1983	01	3.787
1984	01	4.043
1985	01	3.791
1986	01	1.187
1987	01	4.332
1988	01	4.412
1989	01	4.640
1990	01	6.255
1991	01	2.981
1992	01	2.967
1993	01	2.811
1994	01	2.597
1995	01	2.532
1996	01	3.379
1997	01	1.697
1998	01	1.607
1999	01	2.676
2000	01	3.436
2001	01	1.604
2002	01	2.480
2003	01	2.035
2004	01	3.342
2005	01	3.443
2006	01	2.521
2007	01	4.152
2008	01	-0.076

And Japan is getting bear hugged again by deflation despite being stimulus gurus.
Yikes!!!

This is a subject we have been harping on for a while and it goes to the point that there must be still massive amounts bad paper still on the balance sheets of a lot of institutions everywhere, not to mention private balance sheets too. This goes to the point of why this incomprehensible amount of stimulus is not getting the requisite traction, despite signs of hope and glee flowing from some of the emerging markets, which we don't deny. But for a global recovery, we still think we need places like the US, Europe, and Japan to recover, don't you?

When you look at the numbers, it's easily understandable why many expected hyperinflation once there is even a modicum of traction.

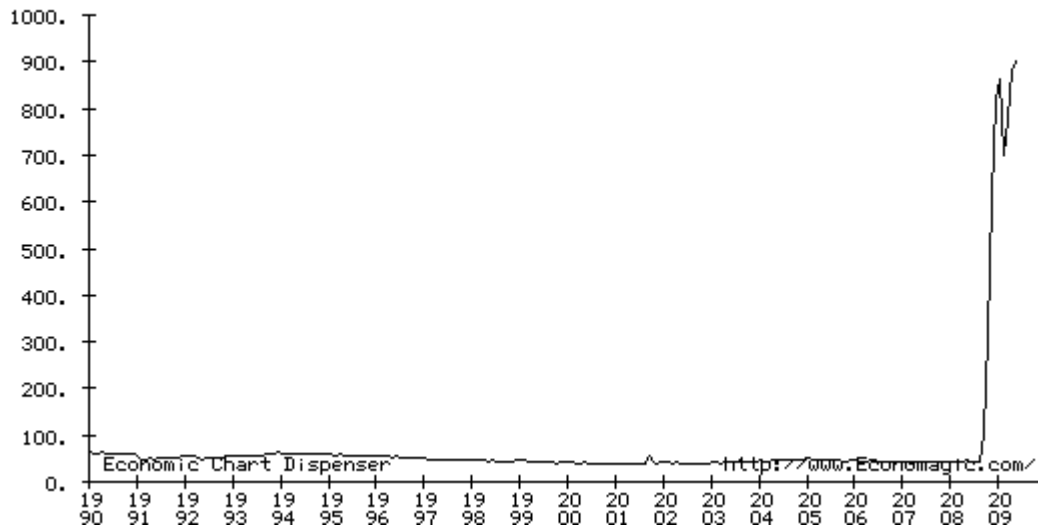
Inflation is, and always has been, the preferred route out of trouble by governments past who issued too much debt i.e. inflate away the debt problem by paying it off with

even more worthless paper. This is why you might have heard bonds referred to as, Certificates of Confiscation.

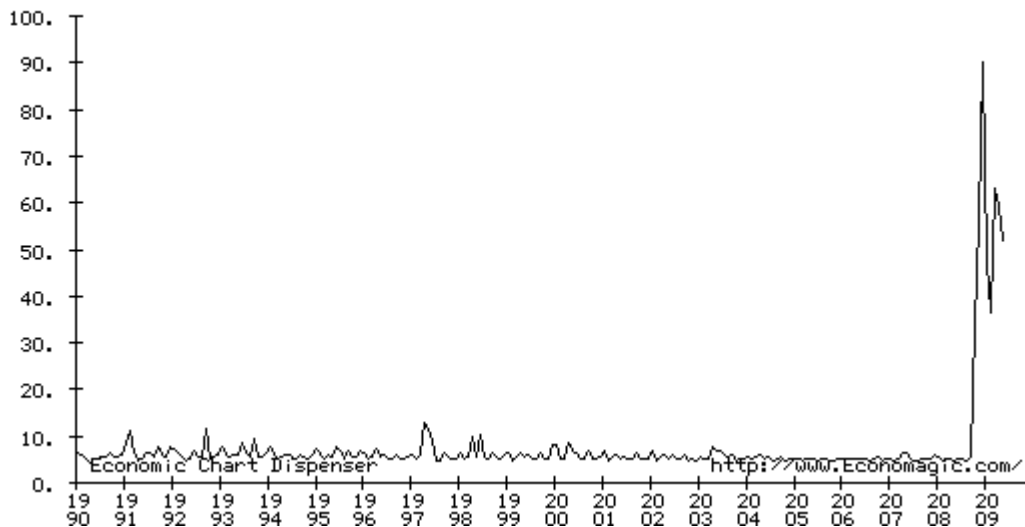
The scary part about what's going on now is that governments present are running out of trees to cut down so they can print more paper in their vain attempts to conjure up a little headline inflation; it makes them look very bad compared to their inflationist counterparts past. A pathetic performance indeed it is. Mr. Summers, put down that Diet Coke and get going buddy! We still have plenty of trees in our neighborhood, and I've even seen a few around Washington. No excuses!!! In fact, if we really cared about our country, we would each donate a tree to help out our Treasury. It is the least we could do for all they do for us.

Anyway, back to some semblance of what this missive is supposed to be about. A few charts and a little quiz:

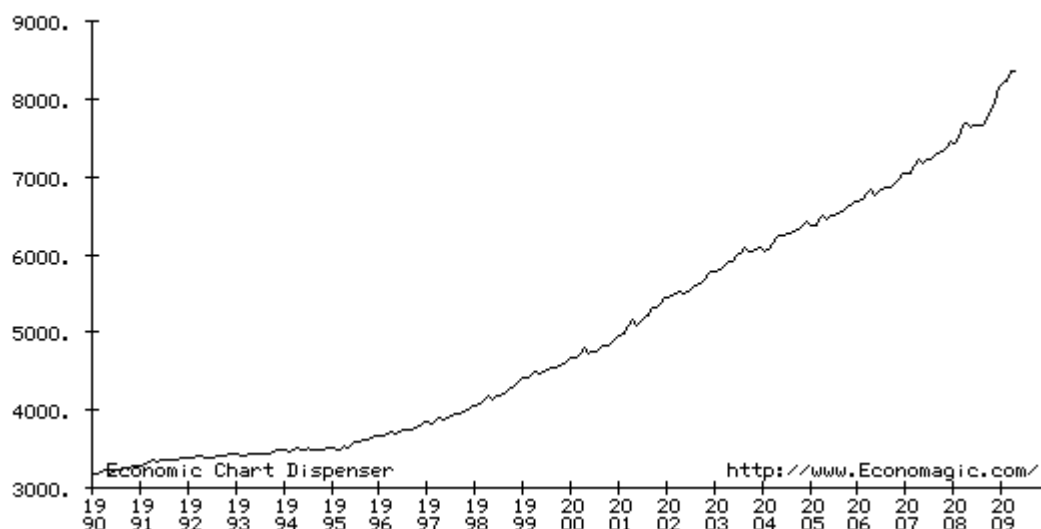
Board of Governors Total Reserves, Not Adjusted for Changes in Reser



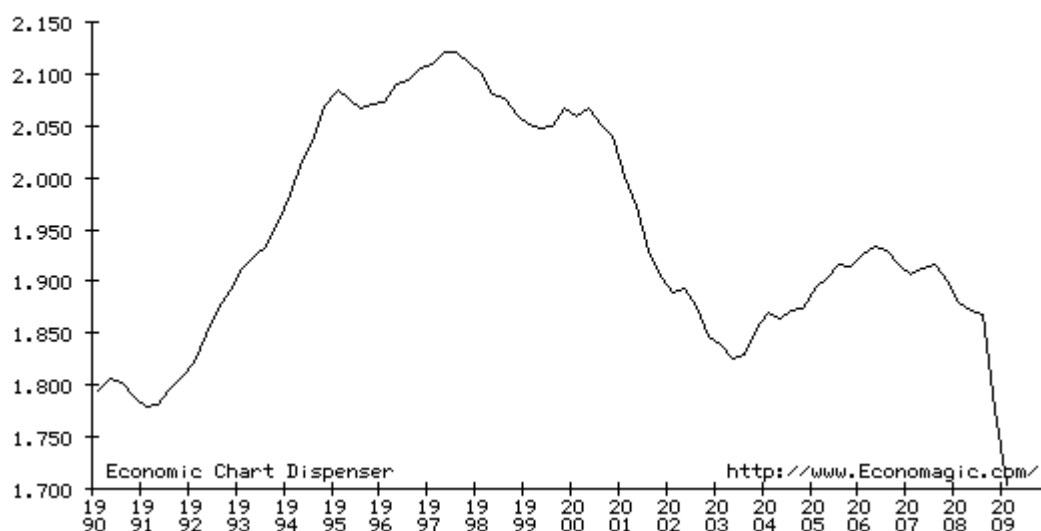
Treasury Deposits with Federal Reserve Banks: Billions of Dollars: NSA



M2 Money Stock: Billions of Dollars: NSA



Velocity of Circulation: GDP divided by M2



Do you notice which of the charts reflects why our government is having so much trouble achieving their goal of inflationism?

If you said Velocity of Circulation, you would be correct! Congrats! For those of you not versed in such arcane jargon, and be very thankful you are not, let me put it this way:

You can lead a horse to water but you can't make him drink!

If you and I are very worried about our future earnings disappearing because our companies aren't doing so well because there is little demand for its products or services, which represents most real people I know, then we are not predisposed to heading out to the store to find something shiny new to buy for us or our loved ones. Multiply this human action, which by the way is the title of the best book on economics ever written, by Ludwig von Mises, over and over and over again amongst the US population that does not either work for, or do business directly with, the US Federal

Government, the only place with booming growth, and you can see why the Velocity of Circulation of money is falling, off a cliff.

And this goes to one of the major problems, I think, for all those neo-Keynesian economists that keep flowing from the woodwork to tell us we need more spending:

Econometric models still have a little problem with human action. They have a little trouble measuring, what they would say is “irrational behavior.” But those of us that live in the real world would call it quite rational behavior. When we are nervous about the future we make a logical decision to change the way we act with a thing called money. We viciously cut waste out of our budget. We change our spending habits dramatically. Our incentive system adjusts accordingly.

And when we watch our government commit \$42,105 for every man women and child to “help” us, and eat away at the stored wealth built up by hard working Americans past, it makes us even more nervous. Thus, what the neo-Keynesians see as a rationale response, we see as incredibly irrational. And thus, we decide it’s time once again to reduce the Velocity of Circulation of our money.

Thus we end up with a self-reinforcing nasty feedback loop created by people who actually believed everything Keynes said in the *General Theory*, instead of moving on to von Mises *Human Action* and getting it right. And so it goes.

Jack Crooks
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