



Key News

- [Court Orders Federal Reserve to Disclose \\$2 Trillion Loan Program Details](#)
(Bloomberg)
- [China Stocks Decline as Premier Warns Economy Faces Many 'Uncertainties'](#)
(Bloomberg)

Quotable

“Pleasure cannot be shared; like Pain, it can only be experienced or inflicted, and when we give pleasure to our Lovers or bestow Charity upon the Needy, we do so, not to gratify the object of our Benevolence, but only ourselves. For the Truth is that we are kind for the same reason as we are cruel, in order that we may enhance the sense of our own Power.”

Aldous Huxley

FX Trading – Rehashing Two Key Points

Quickly, a brief market update before I revisit two components vital to global recovery, as we see it.

Yesterday the European currencies struggled while the commodity dollars firmed up ... that is until US stocks began rolling over late in the session to ultimately finish the day flat. The dollar strengthened.

The US dollar was stronger early this morning, giving it back now, while the British pound is the weakest of the pack. Many analysts noted the particularly dismal day that gold had yesterday after finishing last week on a strong note. Gold is trying to bounce back this morning. S&P 500 futures have pushed lower this morning but have fought back to even things out, bidding up a bit going into the open.

Overall, the price action is rather subdued thus far as we await the Case-Shiller Home Price Index at 9 am eastern ... and then consumer confidence at 10 am. Which brings me to ...

All Wet Without the Consumer

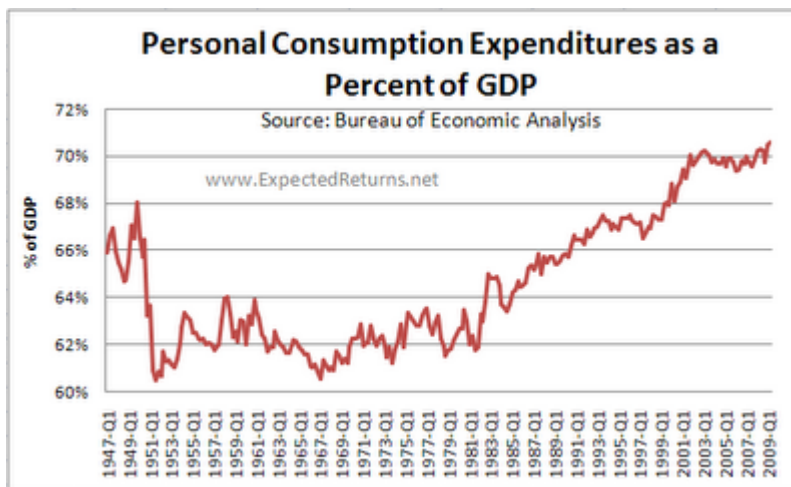
Frankly, and if you've been reading our stuff for a while you know, we've been fairly surprised at the sustained risk appetite and periods of optimism that have so steadily driven equity markets higher ... and kept the US dollar smothered. There's simply been a disconnect between our global fundamental analysis and market sentiment. Of course, varying time frames is a challenge in and of itself.

But still, we wonder how much recovery can happen without the US consumer. Consumption in the US has for some time made up an overwhelming portion of US GDP. And even though consumers have taken a hiatus, US GDP numbers are still as heavily dependent upon the consumer come out of hiding.

And there's the rub, as they say – US consumers have taken on a mindset of savings and debt reduction. Certainly, with all the better-than-expected data that seems to be surfacing throughout the economy and driving risk appetite these days, consumer statistics cannot be included in such bright-eyed indicators.

A recent blog post I came across sums up some [very key points](#) quite well. An excerpt:

An increased savings rate will put pressure on consumption, which will in turn pressure GDP. In the following chart, notice how consumption as a percent of GDP remains above historical norms. Consumption would have to contract another \$800 Billion for personal consumption expenditures as a percent of GDP to revert to historical levels.



“Everyone privately thinks this is an asset bubble driven purely by liquidity.”

The above is attributed to an executive at a Chinese investment bank. He seems to be on point. And it is likely the reason for the recent double digit percent declines in Chinese equities over the last few weeks.

This comes as no surprise to us – we've seen stimulus measures and excessive lending to be misdirected and misused. And after an extreme rise in stocks, more investors are beginning to awaken to the same idea.

What has come as sort of a surprise is the global market reaction to China's stock market. For two reasons:

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- 1) No doubt, China's market is a major indicator of risk taking, but for some reason the money flowing out of China's stocks hasn't sparked similar risk aversion in other stock markets. The US markets made new highs yesterday.
- 2) The recognition of empty price gains should beg the question: are economic growth expectations warranted considering the excess liquidity dynamic? If not, then you would think China's bearing on global trade would mean bad things for prices of natural resources and emerging market assets.

Interestingly enough, I pointed out to Jack yesterday investors' feeling that emerging markets are becoming less risky, i.e. investors are willing to put up money for smaller potential yield on their capital. From Bloomberg:

Emerging market borrowing costs dropped to a seven-day low. The extra yield investors demand to own developing nations' bonds instead of U.S. Treasuries declined 3 basis points to 3.62 percentage points, the lowest level since Aug. 12, according to JPMorgan Chase & Co.'s EMBI+ Index.

So in the face of leaking optimism over China's stock market strength and potentially over economic growth, investors in emerging markets have not blinked. It's possible that global investors are turning their heads from China and focusing on whatever green shoots they can dig up elsewhere. But I wouldn't be surprised to see global markets cave in to China if share prices don't soon stabilize.

As far as the US dollar goes, we've yet to be validated on our long-term global macro forecast; risk appetite has kept the buck suppressed. But it could pay off royally to be *open* to potentially major US dollar strength in the coming days and weeks ahead.

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