



# **Are Markets Too Fearful?**

**August 25, 2011**

**David Malpass**  
**[dmalpass@encimaglobal.com](mailto:dmalpass@encimaglobal.com)**

**212.876.4400**

Please read the important disclosure information in the Addendum section of this presentation.

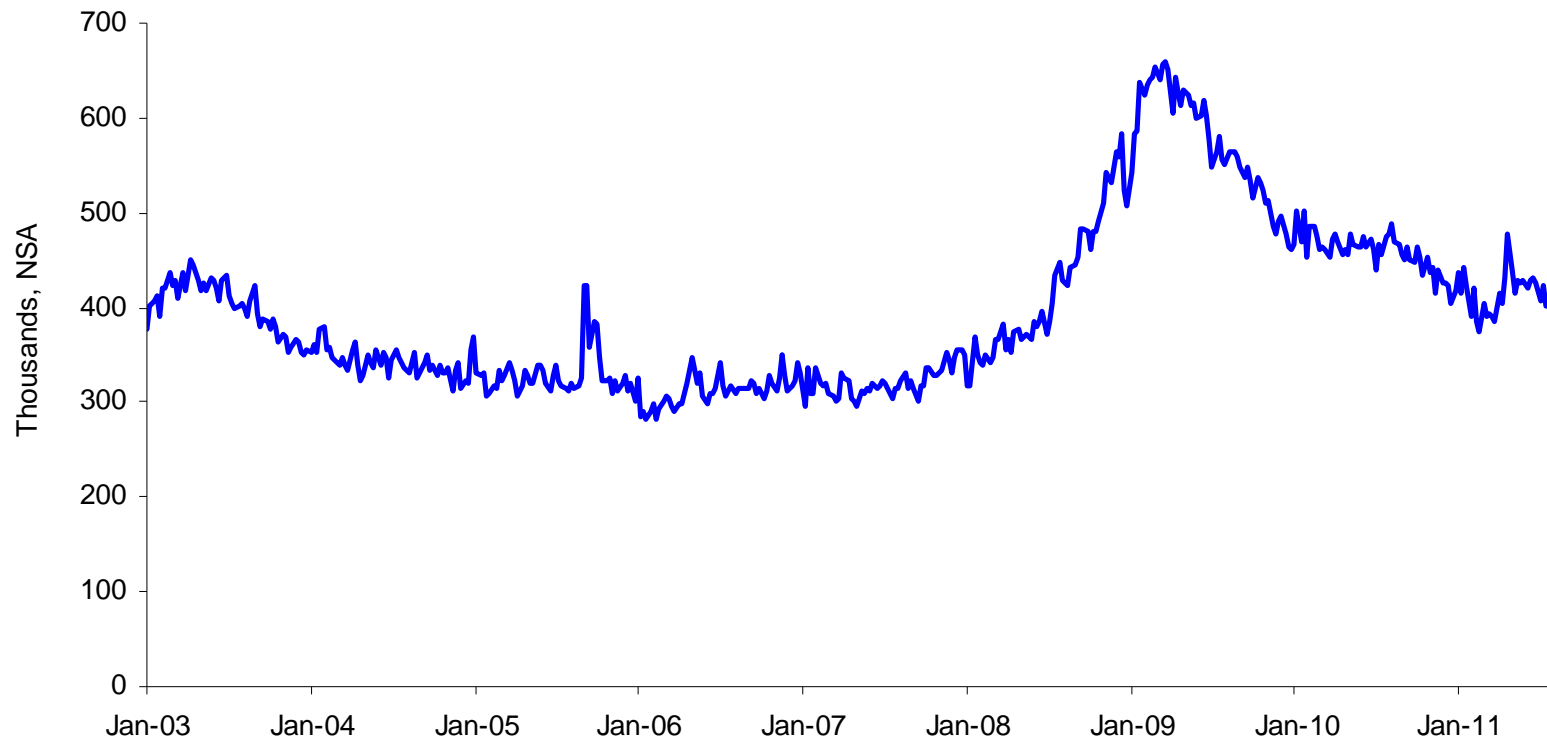
---

# Economic Outlook

- **We don't think the systemic risk is as high as the market is pricing it. Markets aren't frozen. Central banks are able to supply unlimited liquidity. We don't think the euro will break apart or major banks will declare bankruptcy. Under current policies, we expect the U.S. to suffer dissipation of its net worth but not a traumatic tipping point.**
- **Most of the economic and policy news has been negative. At 0.8%, first half growth was way below the "new norm" and the second half has started weak. We expect somewhat faster growth in the third quarter (2%) than the second (1.3% with downward revision pending) based on auto production, business investment and exports.**
- **Corporate profits have been strong and expectations for second half profits remain good based on top line growth, cost cutting and earnings abroad. China's hard landing hasn't materialized, with 9.5% growth in the second quarter despite the production crash in Japan and the U.S. weakness.**
- **Due to the Fed's weak-dollar policy, most of the world is facing inflation problems that remain serious even as GDP growth slows. China's inflation rose to 6.5% in July year-over-year, renewing the possibility of further interest rate hikes there. The U.S. itself has producer prices rising 7.2% year-over-year and the CPI remains elevated at 3.6%.**
- **We think the U.S. is set to continue ultra-loose fiscal and monetary policies at least through 2013. The U.S. publicly held federal debt-to-GDP ratio is set to rise from 65% now to 100% in 2021. We don't think the debt limit deal, fights over continuing resolutions (another is due October 1), super committees or across-the-board sequesters will be effective in slowing spending growth given divided government and the systemic bias toward more spending.**

# Initial Jobless Claims

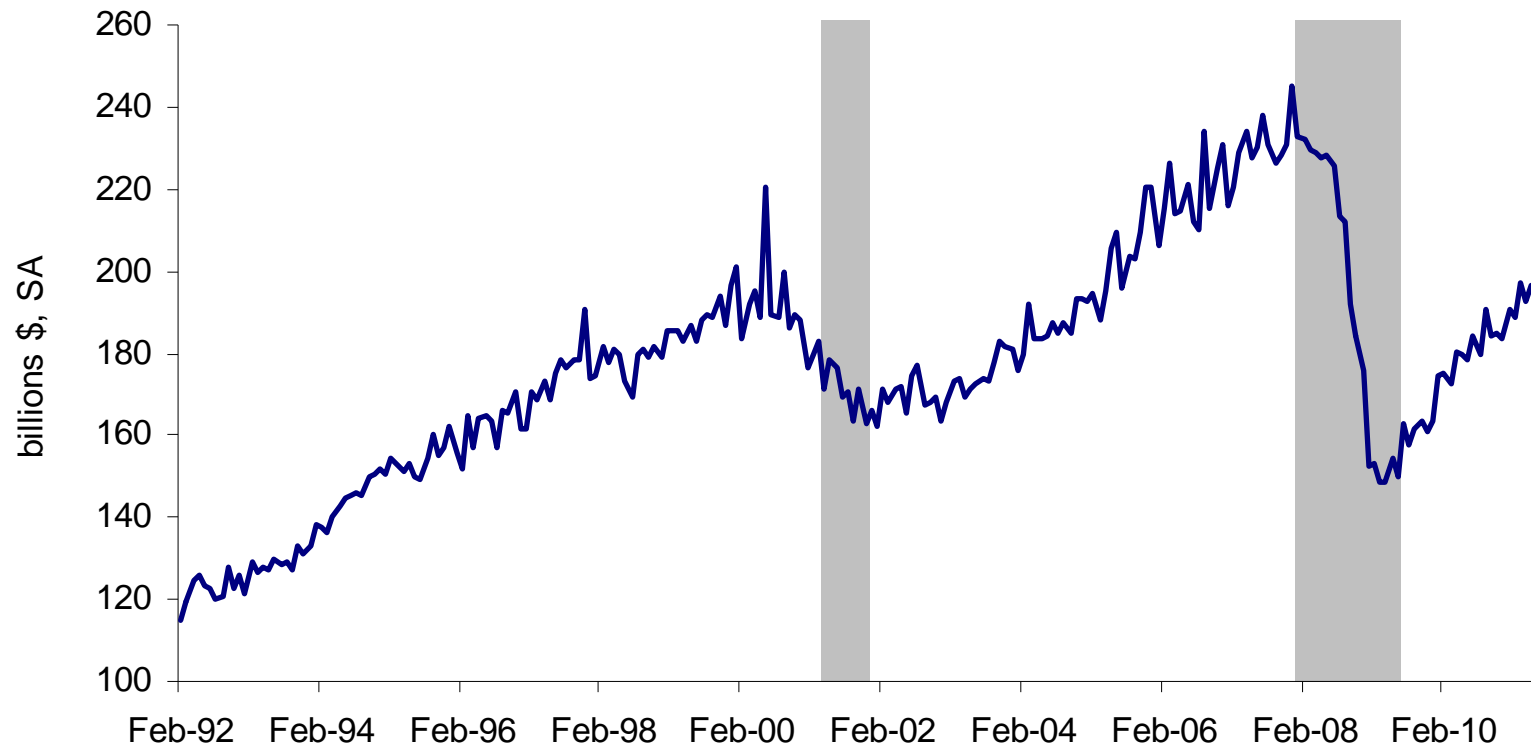
(last obs. August 20, 2011)



Source: Department of Labor: Encima Global

## Durable Goods Orders Grew 4% In July

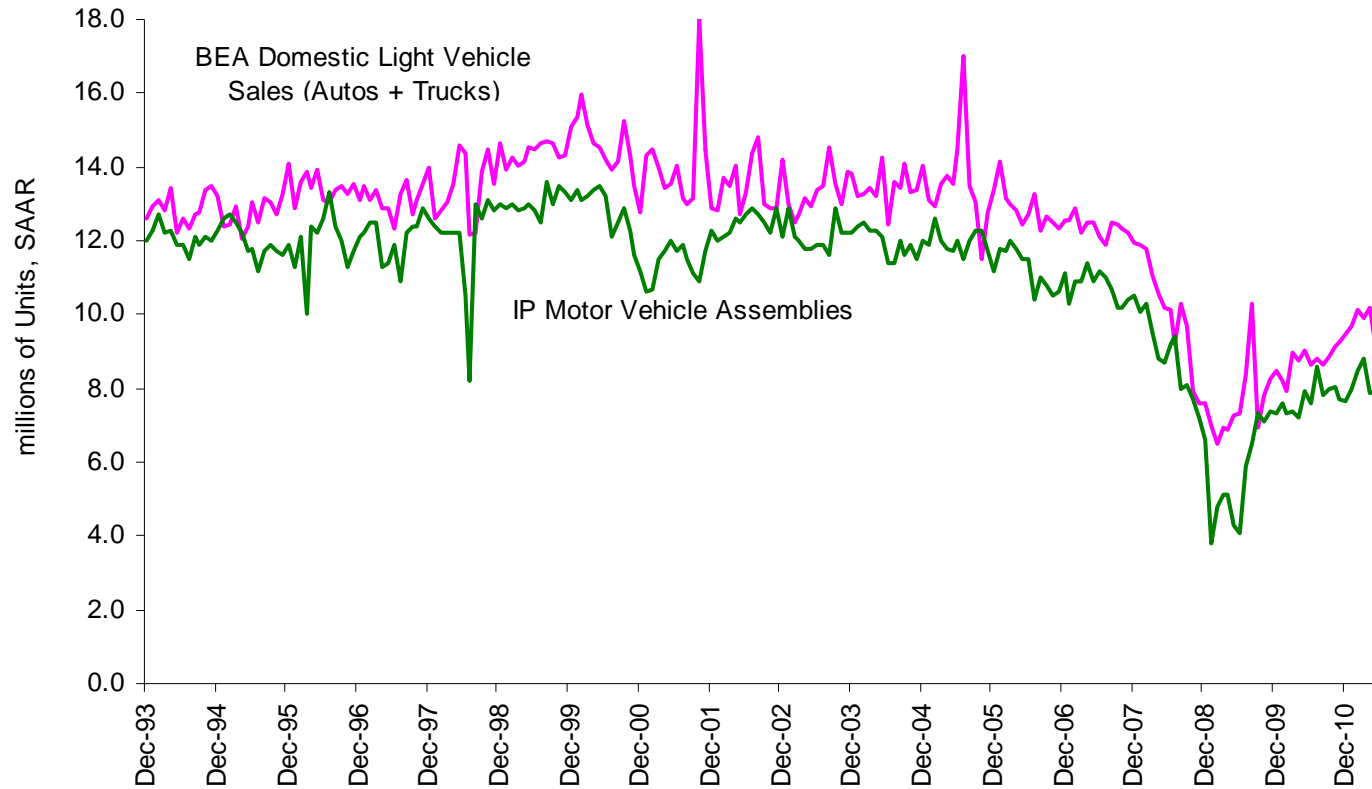
(last obs. July 2011)



Source: Bureau of Census; Encima Global

# Auto Sales and Production Rose In July

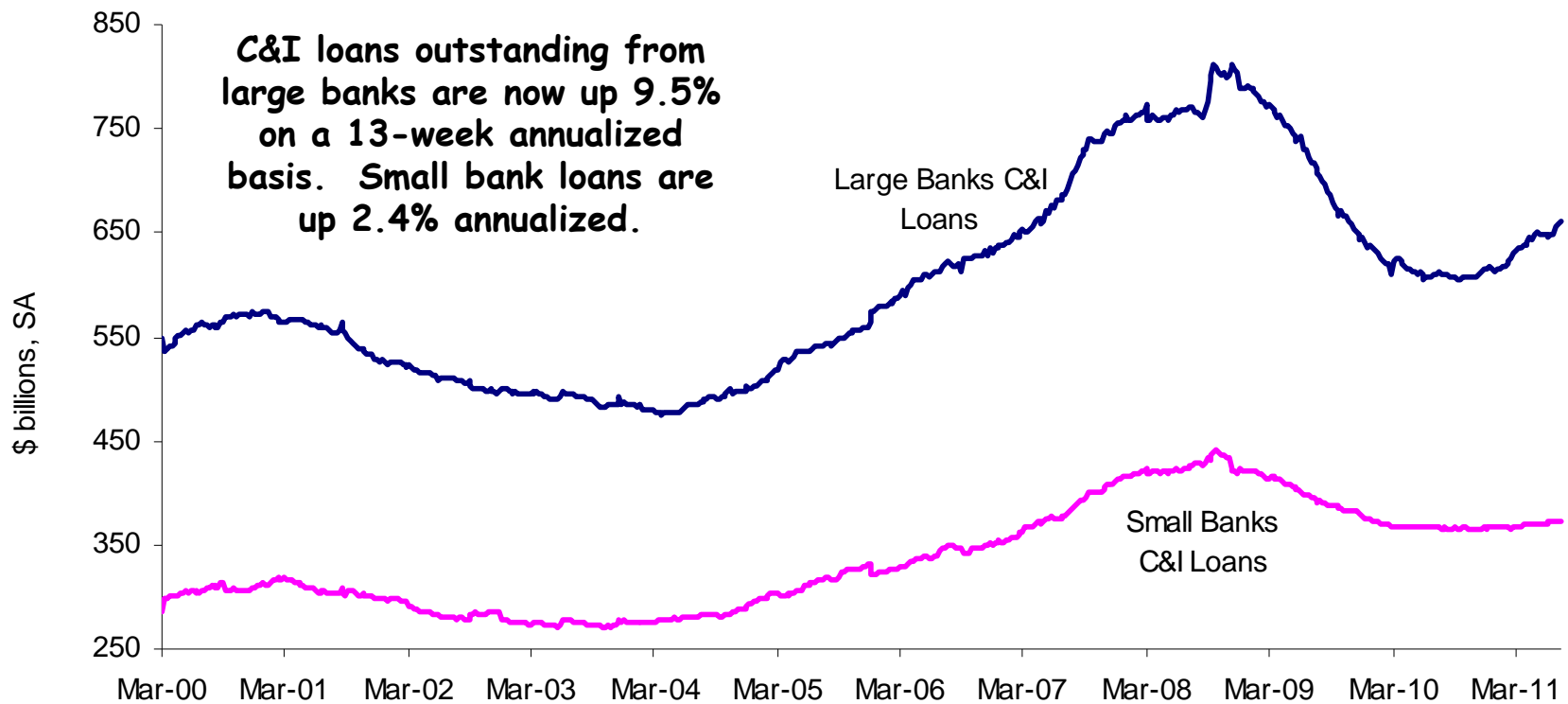
(last obs. July 2011)



Source: BEA; Federal Reserve; Encima Global

# Commercial and Industrial Loans Beginning to Rise

(last obs. August 10, 2011)



Source: Federal Reserve; Encima Global

# EURIBOR - OIS Spread Has Widened

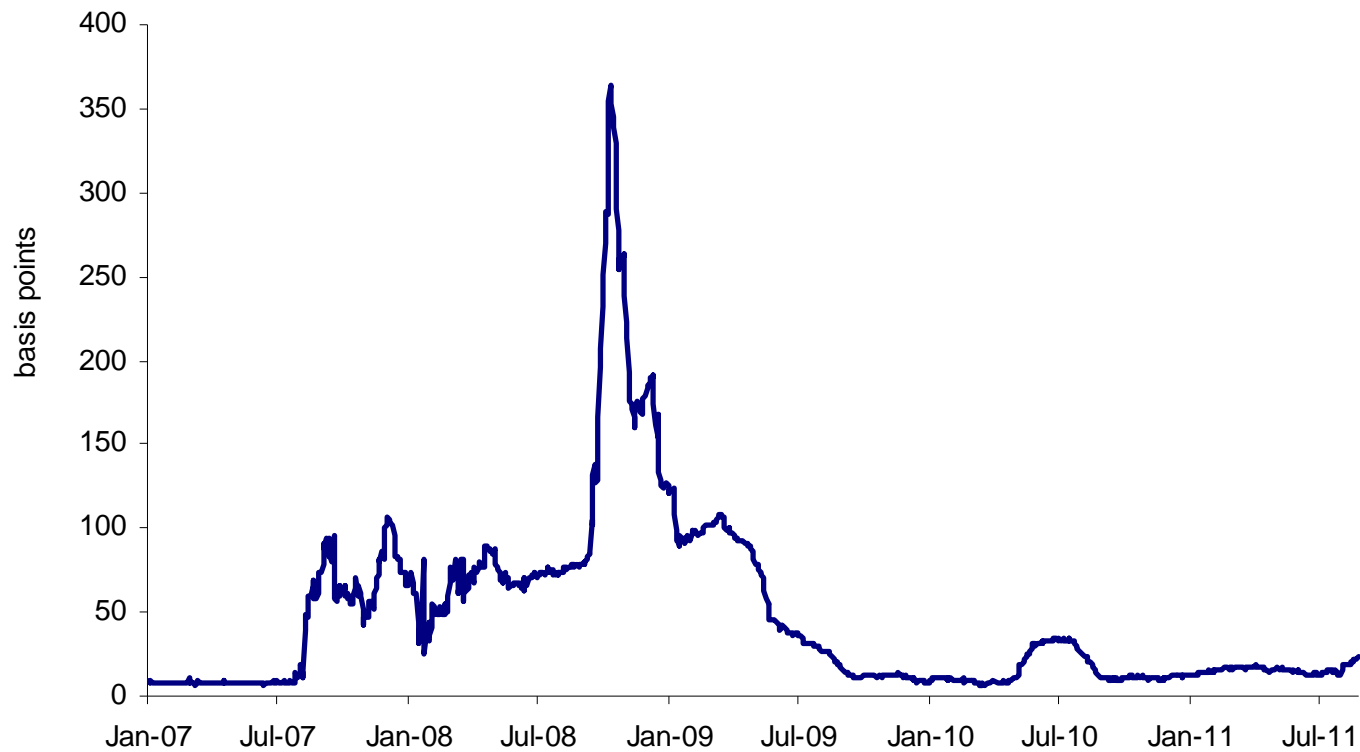
(last obs. August 25, 2011)



Source: Bloomberg; Encima Global

# LIBOR – OIS Spread Remains Calm

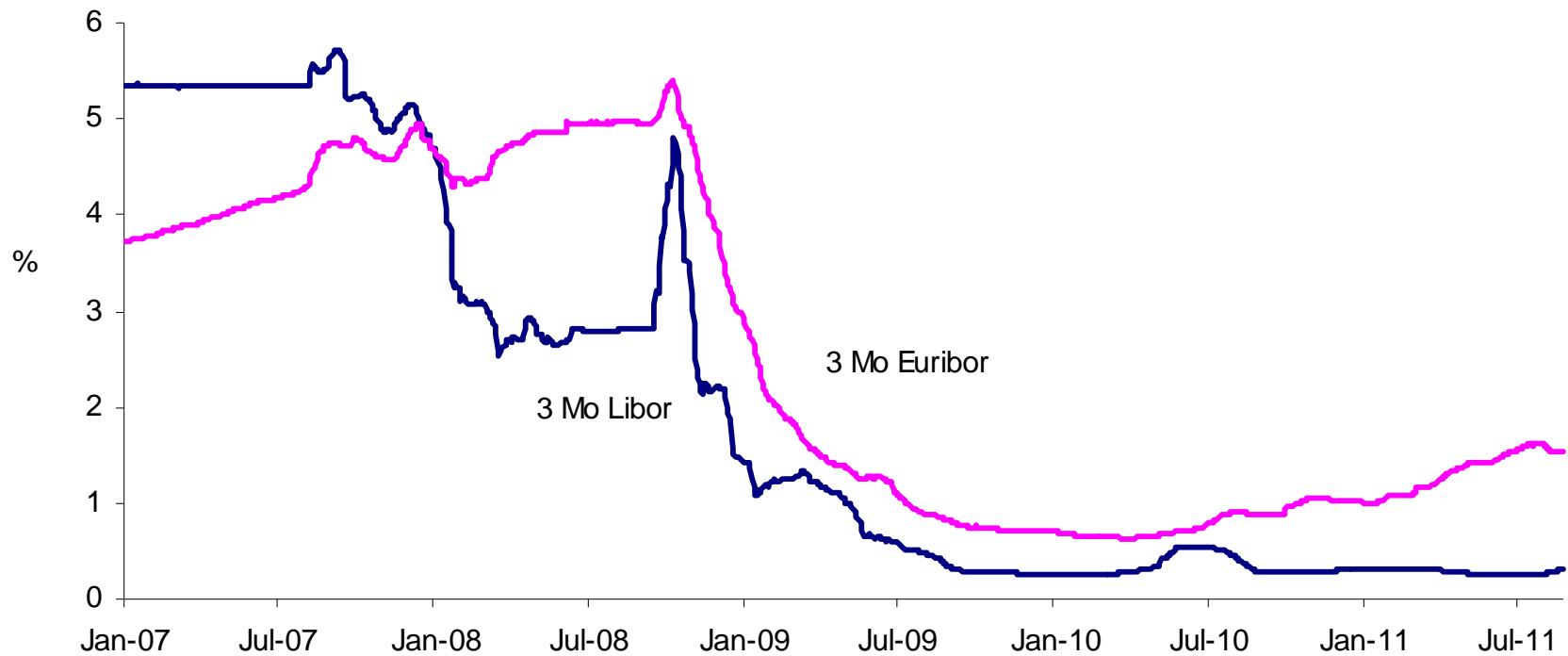
(last obs. August 25, 2011)



Source: Bloomberg; Encima Global

# Unusually Wide EURIBOR to LIBOR Spread

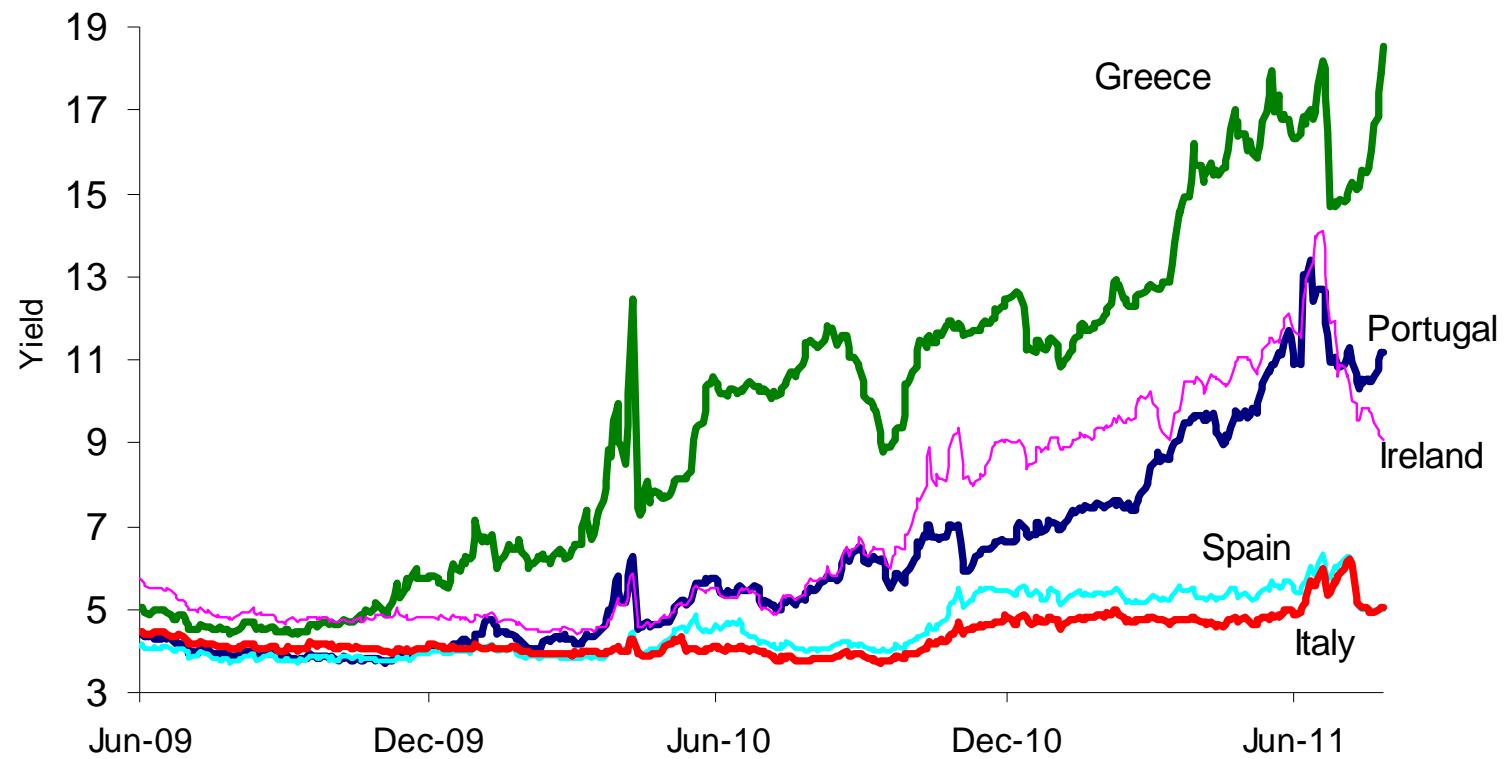
(last obs. August 25, 2011)



Source: Bloomberg; Encima Global

## Selected European 10 Yr Yields

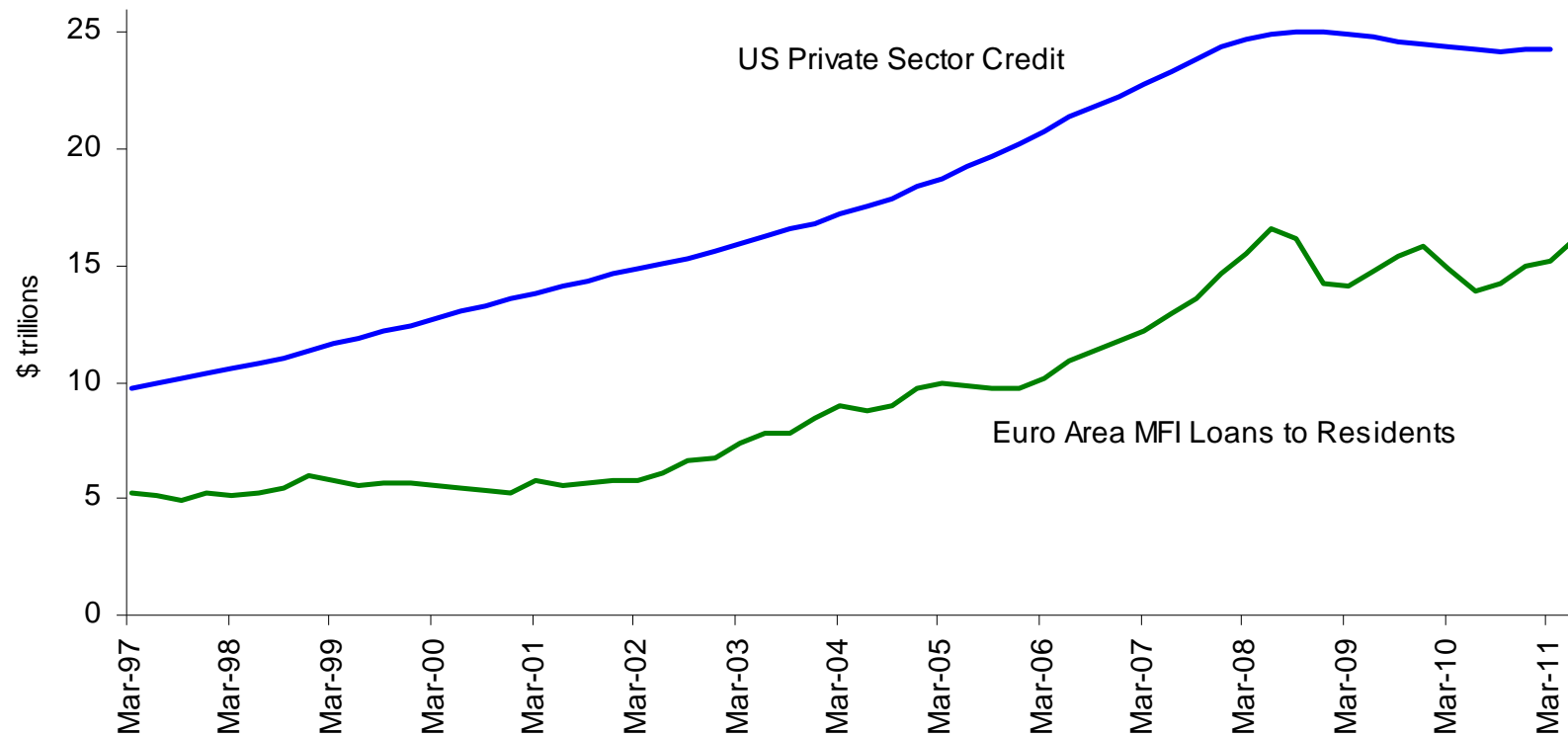
(last obs. August 25, 2011)



Source: Bloomberg; Encima Global

# US and Euro-Zone Private Sector Credit

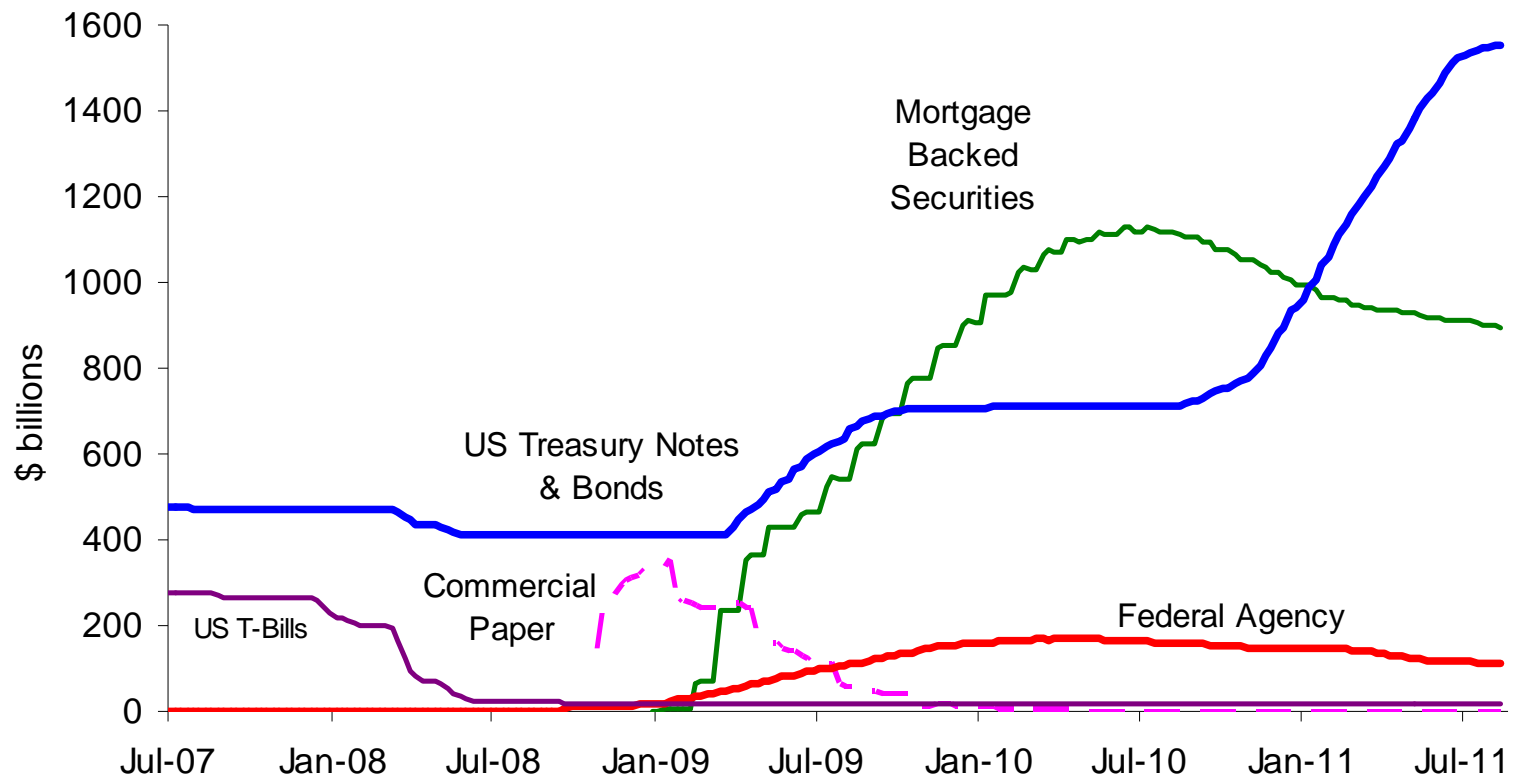
(last obs. U.S. Q1 2011, Euro area Q2, converted to dollars)



Source: Federal Reserve; ECB; Encima Global

# Fed Balance Sheet

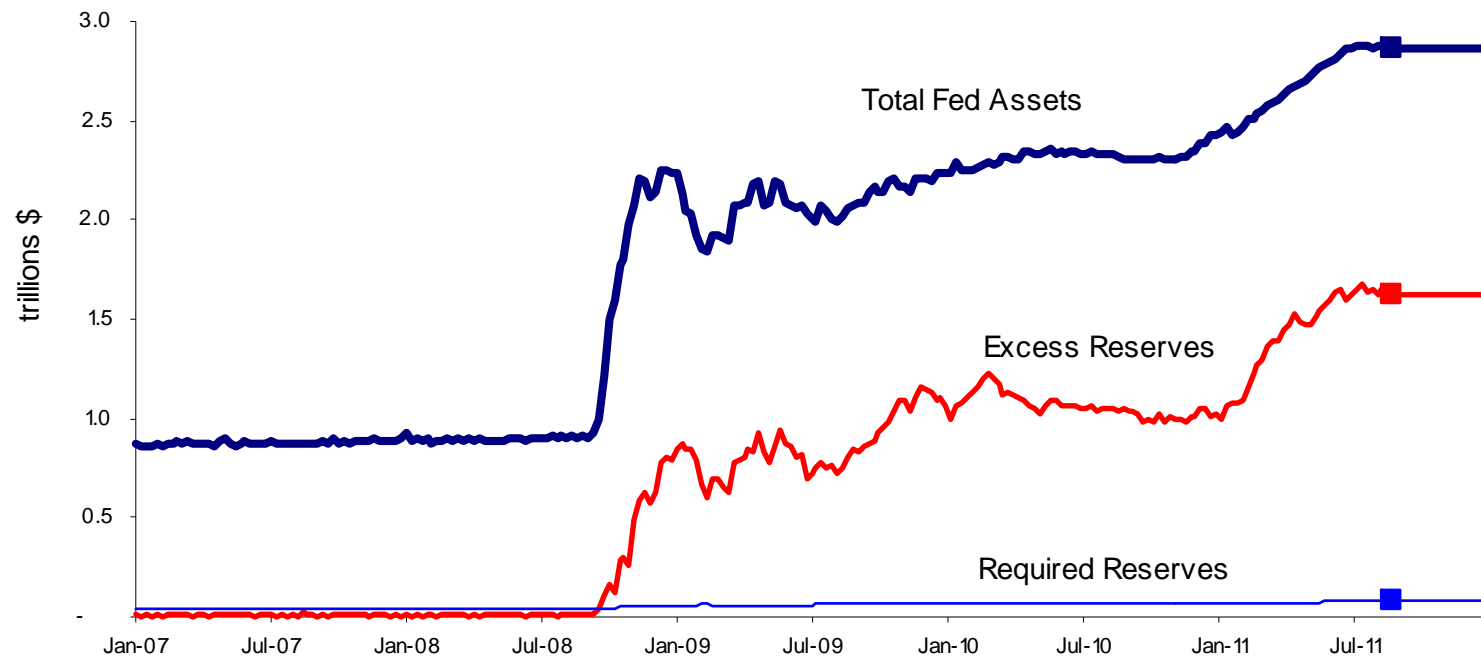
(last obs. August 17, 2011)



Source: Federal Reserve; Encima Global

# QE2 Added Excess Reserves -- ‘Pushing on a String’

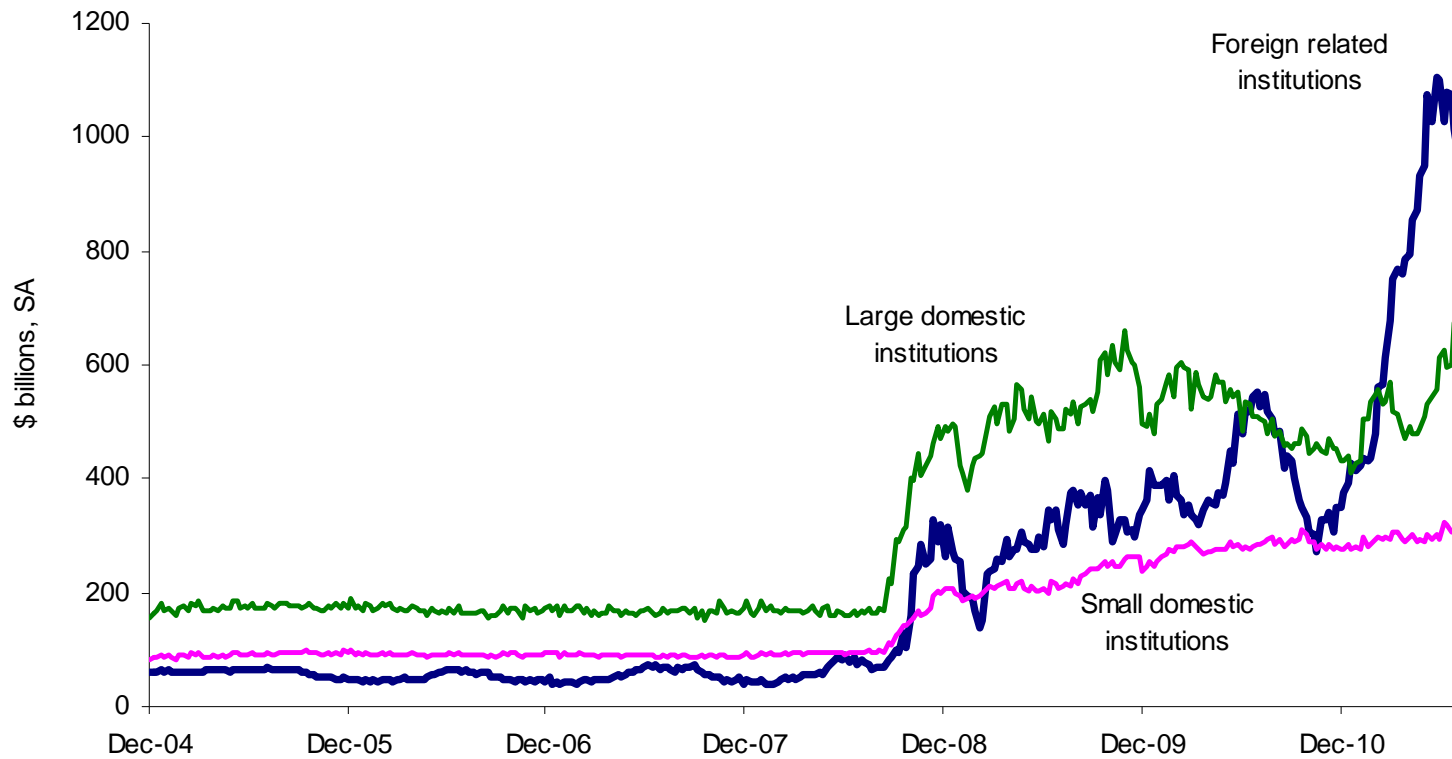
(last obs. August 17, 2011)



Source: Federal Reserve: Encima Global

# Bank Cash: Most Excess Reserves Held At Foreign Related Institutions

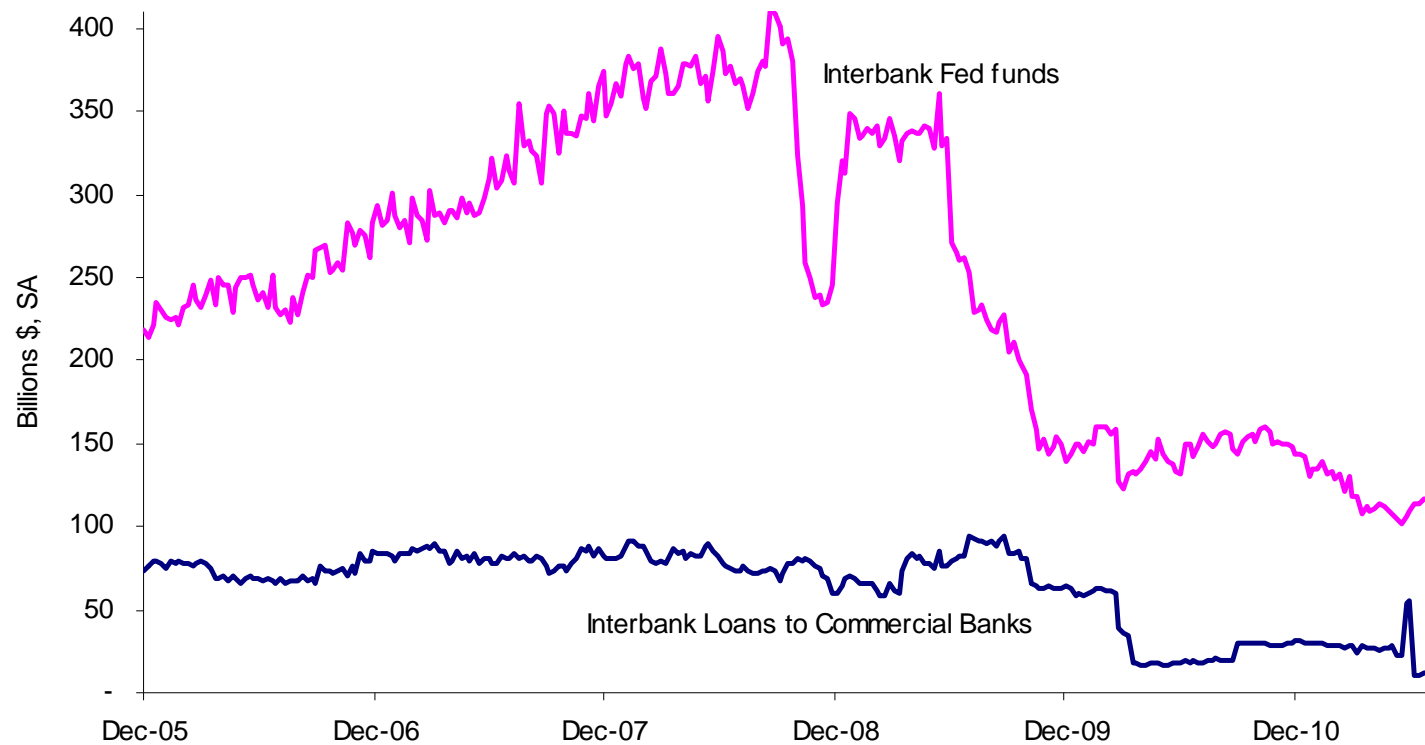
(last obs. August 10, 2011)



Source: Federal Reserve; Encima Global

# Interbank Lending Under Pressure From Zero Rates

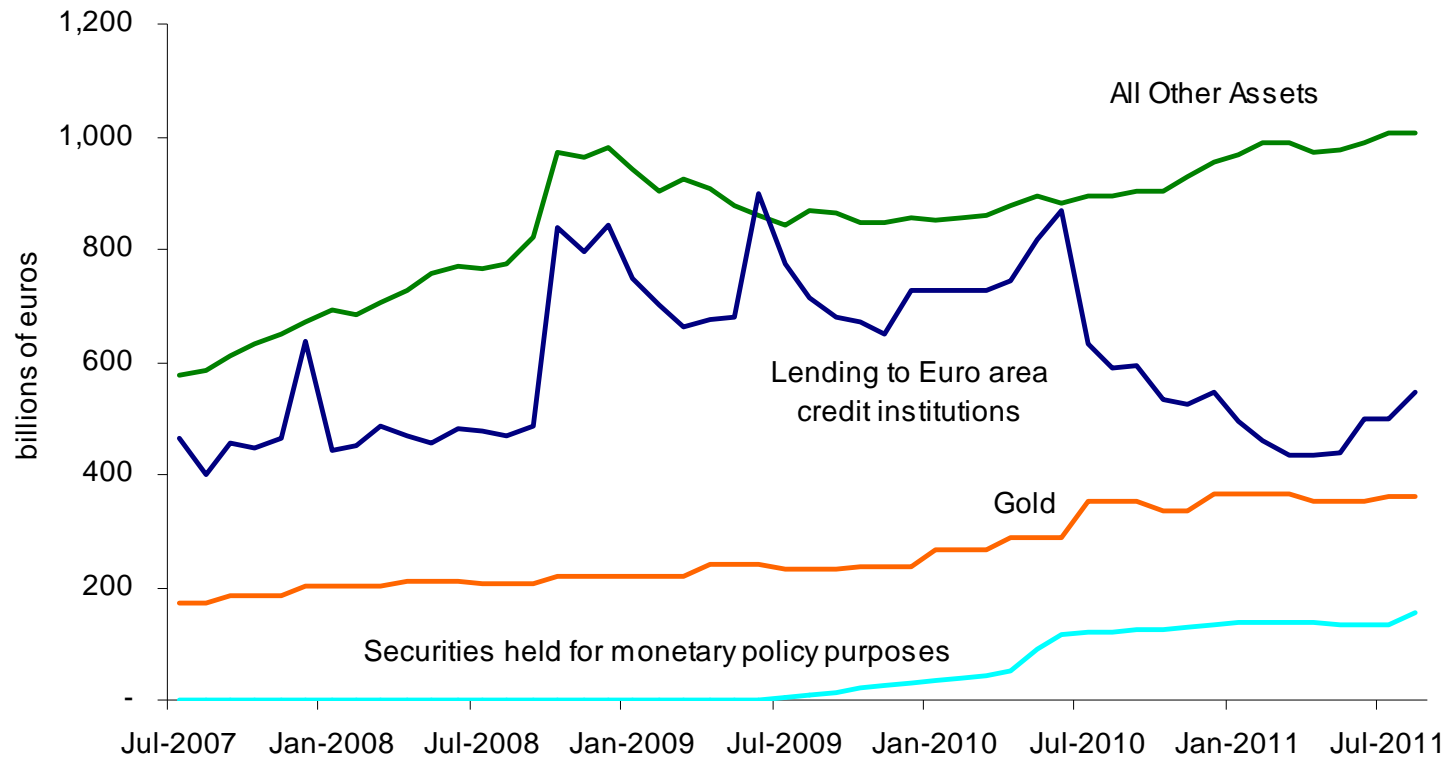
(last obs. August 10, 2011)



Source: Federal Reserve; Encima Global

# ECB Balance Sheet

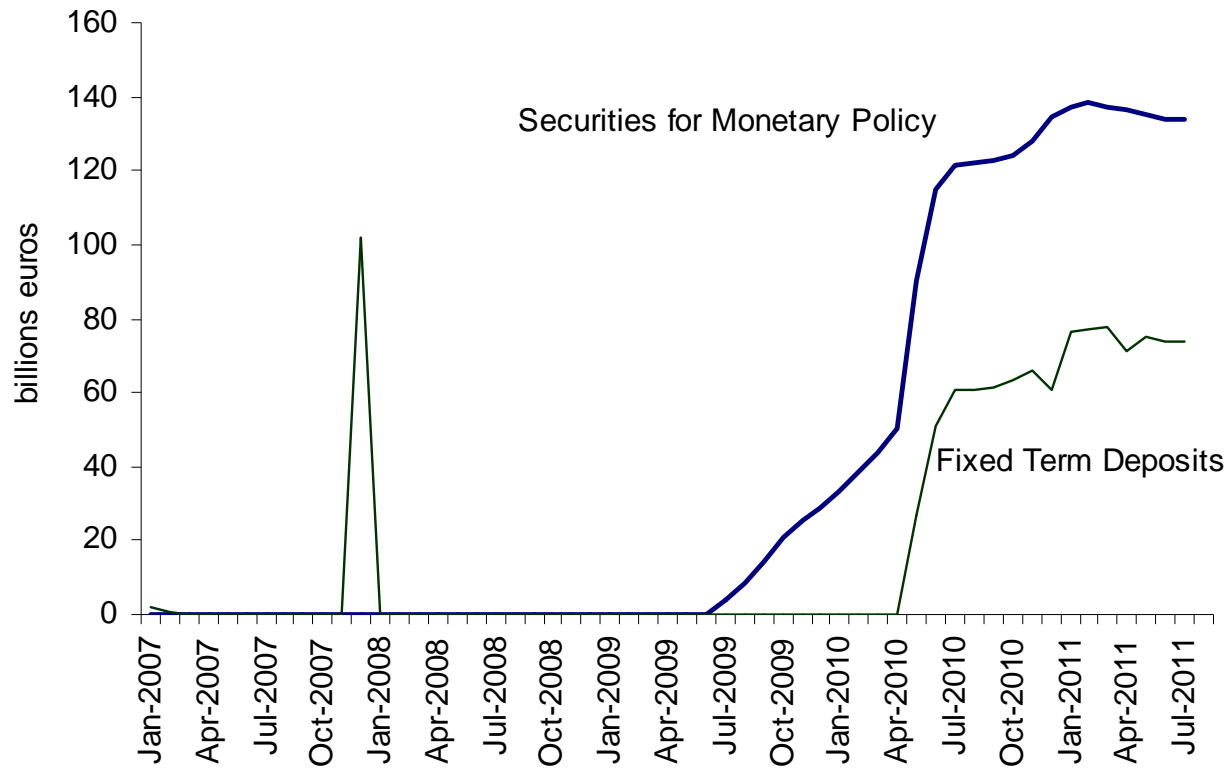
(last obs. August 12, 2011)



Source: ECB; Encima Global

# ECB Balance Sheet

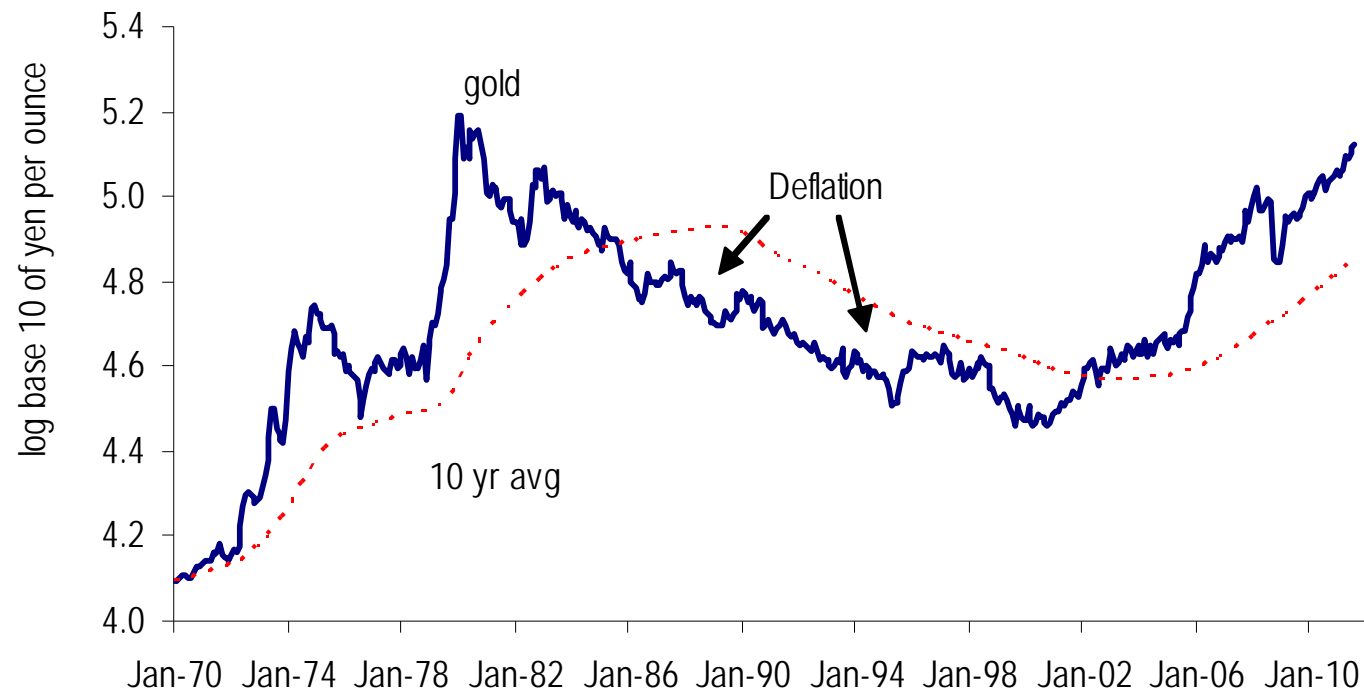
(last obs. August 12, 2011)



Source: ECB; Encima Global

# Gold in Yen

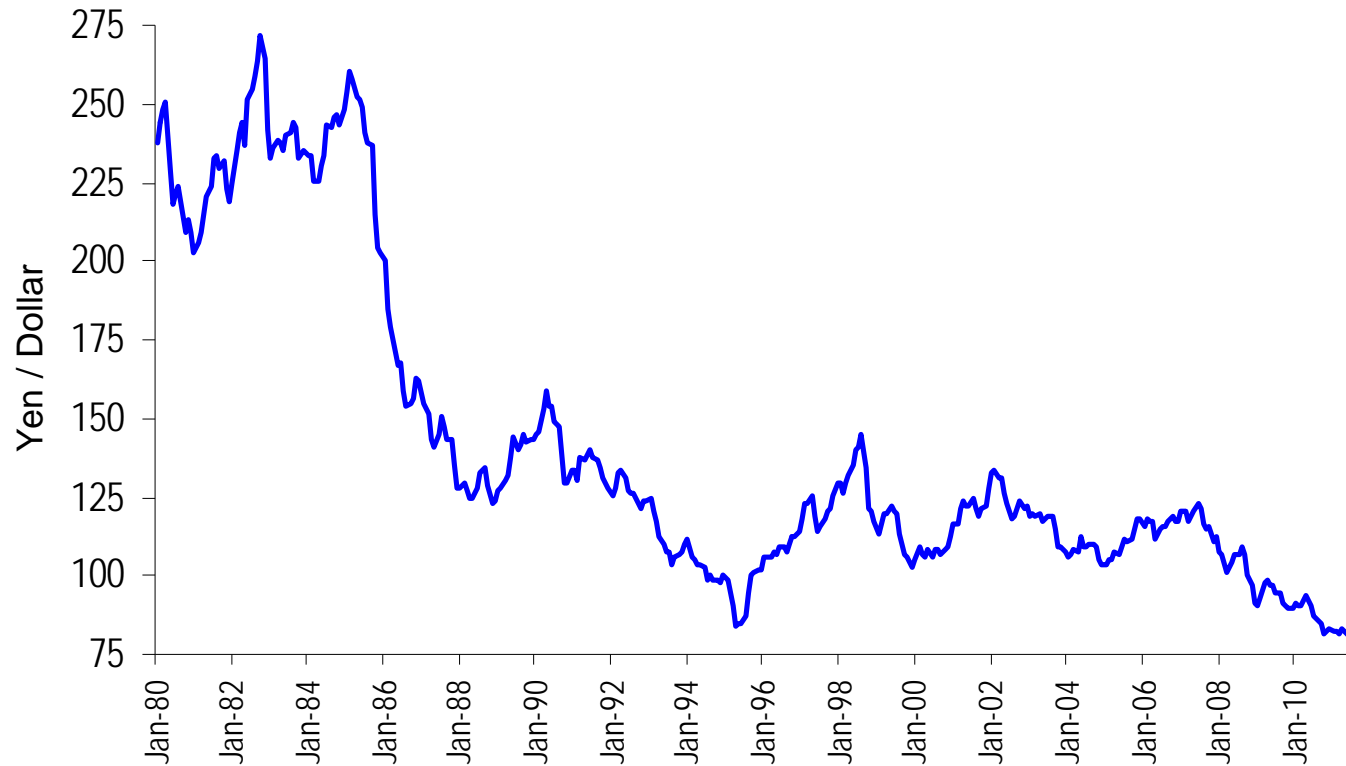
(last obs. August 24, 2011)



Source: Wall Street Journal; Federal Reserve: Encima Global

# Yen / \$ Exchange Rate

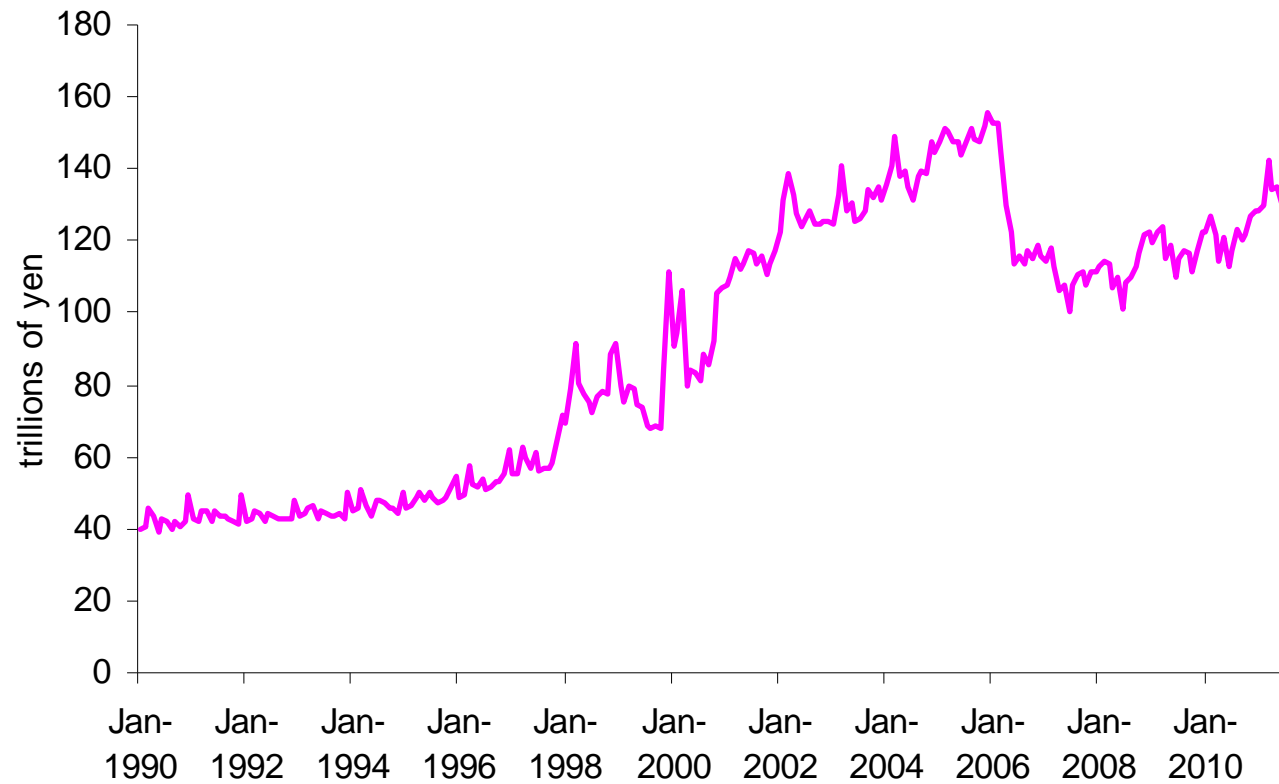
(last obs. August 24, 2011)



Source: Federal Reserve: Encima Global

# Bank of Japan Assets

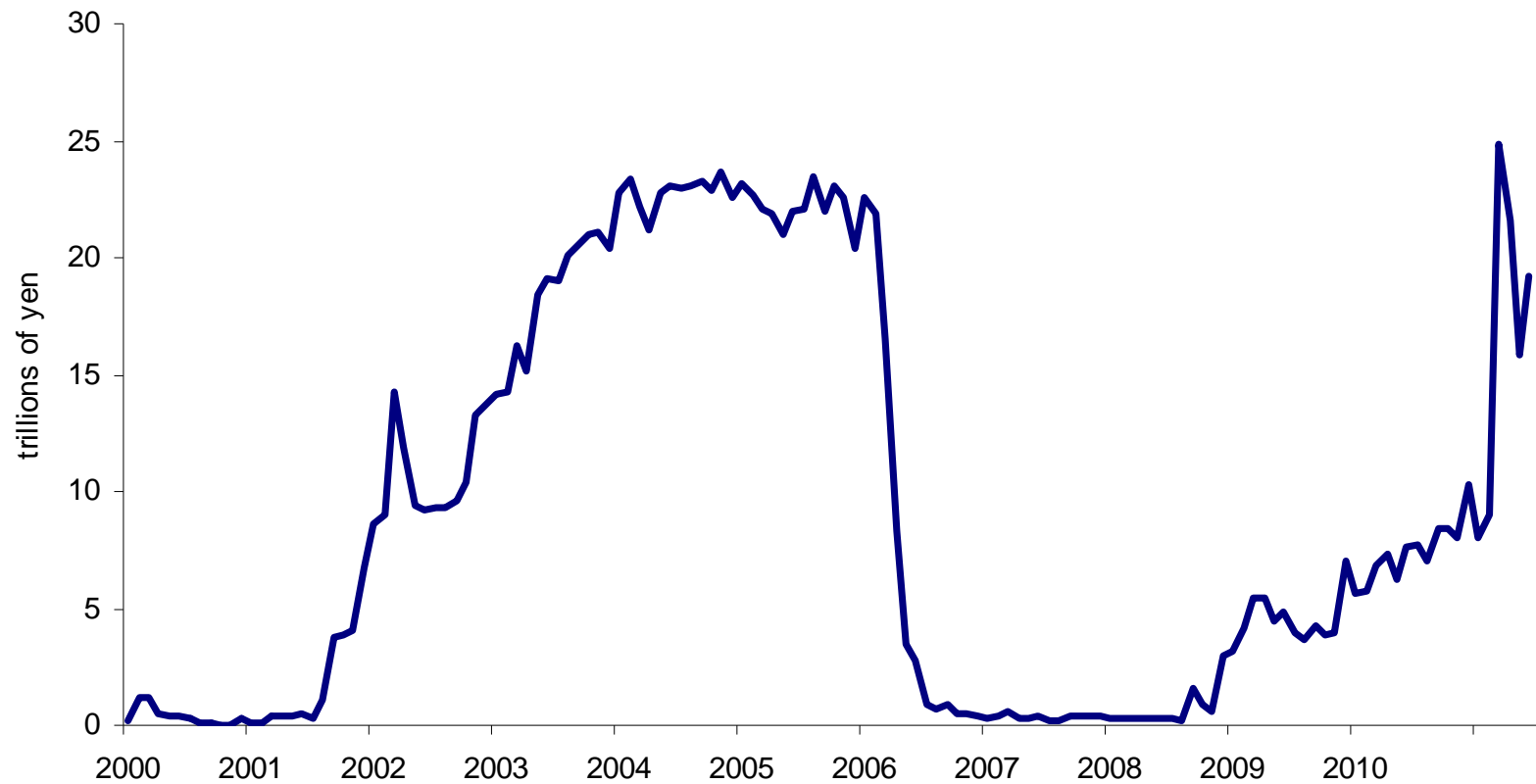
(last obs. July 2011)



Source: Bank of Japan; Encima Global

## Bank of Japan Excess Reserves

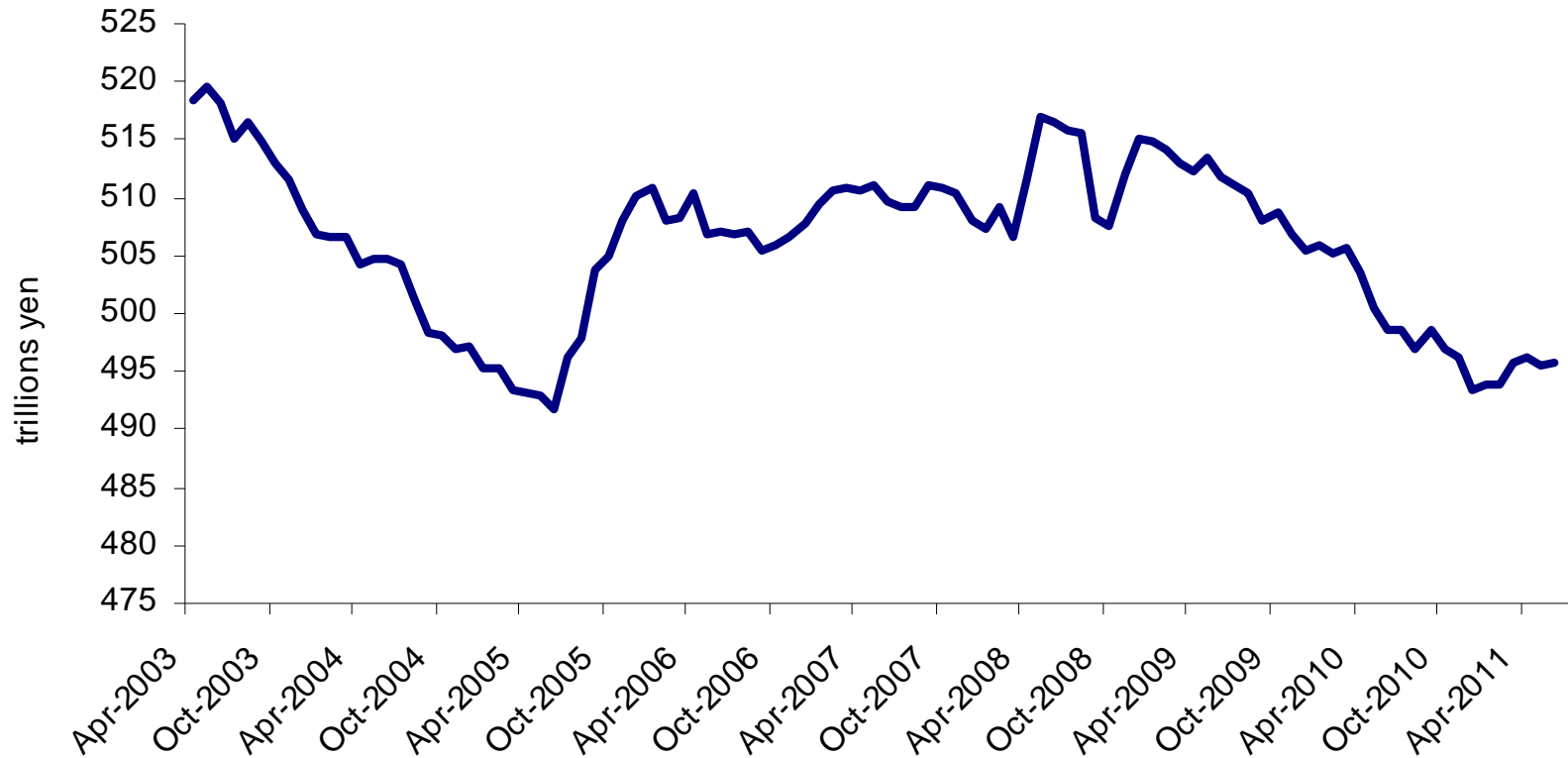
(last obs. June 2011)



Source: Bank of Japan; Encima Global

# Japan Private Sector Credit Fell During QE

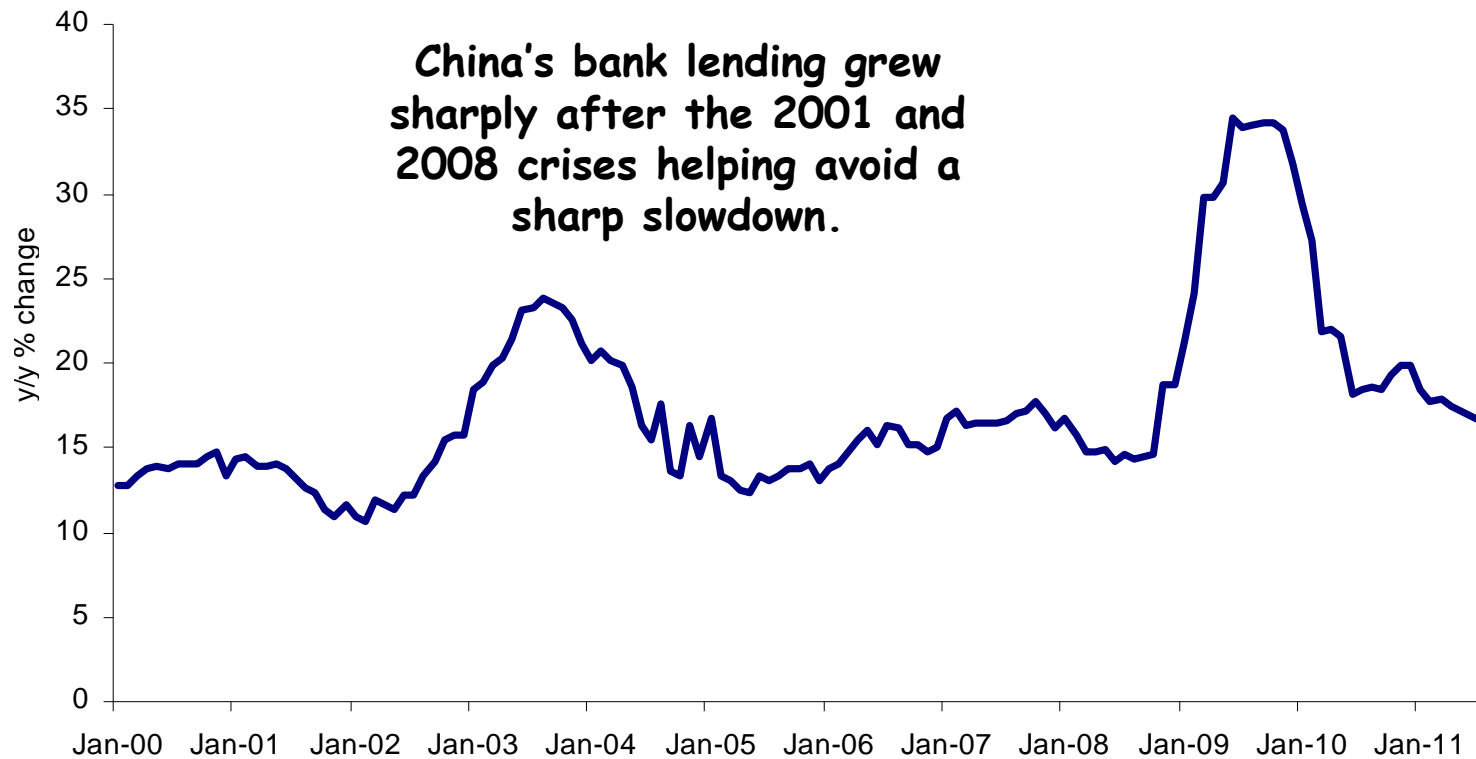
(last obs. June 2011)



Source: Bank of Japan; Encima Global

# China's Countercyclical Bank Lending Policy

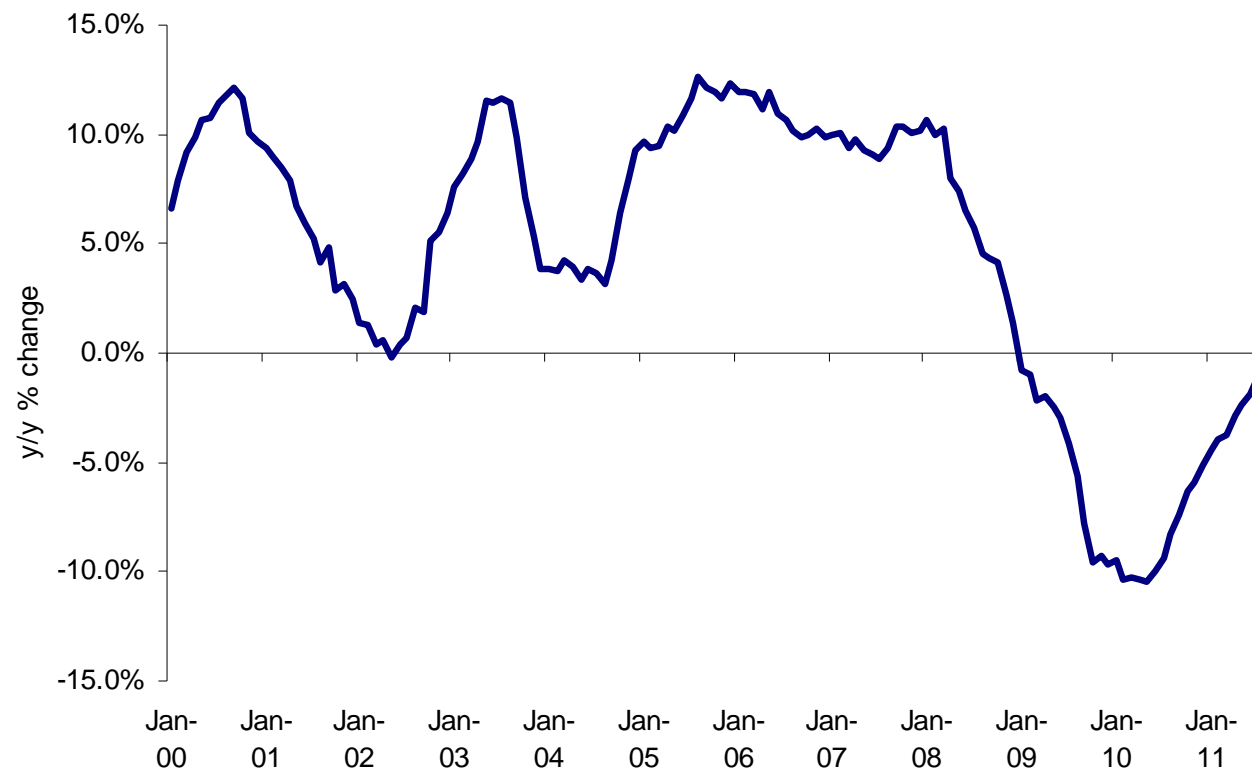
(last obs. July 2011)



Source: Bloomberg; Encima Global

# US Pro-cyclical Bank Lending Policy

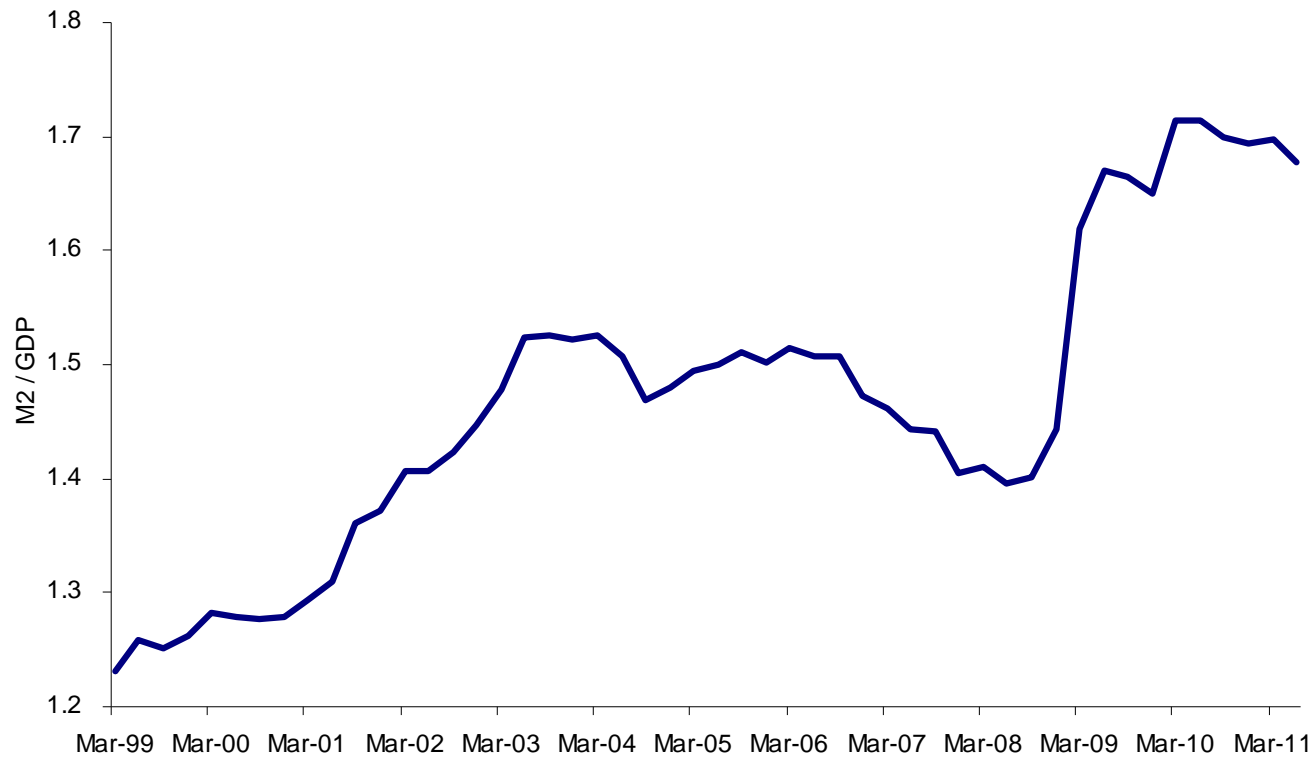
(last obs. July 2011)



Source: Federal Reserve; Encima Global

# China's M2 Grew Faster Than GDP After '08 Crisis

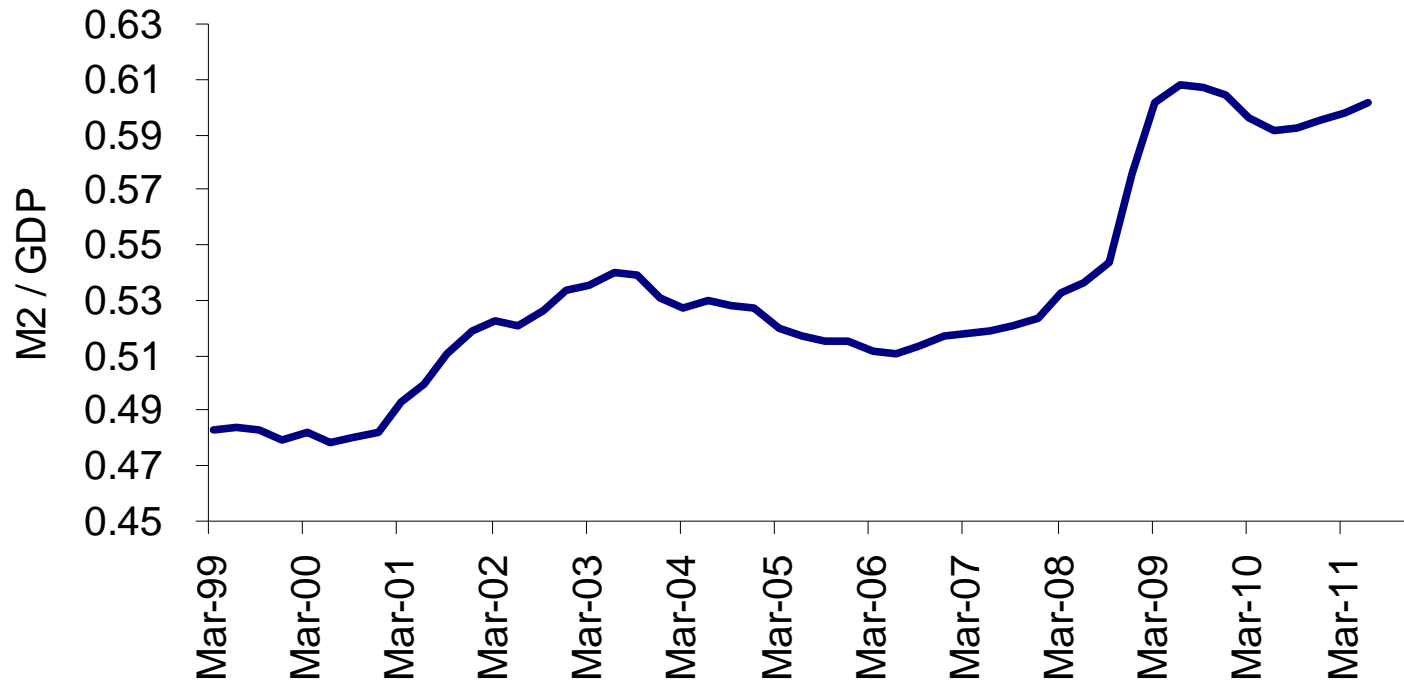
(last obs. Q2 2011)



Source: China National Bureau of Statistics; People's Bank of China; Encima Global

# Regulators Caused Decline in US M2 After '08 Crisis

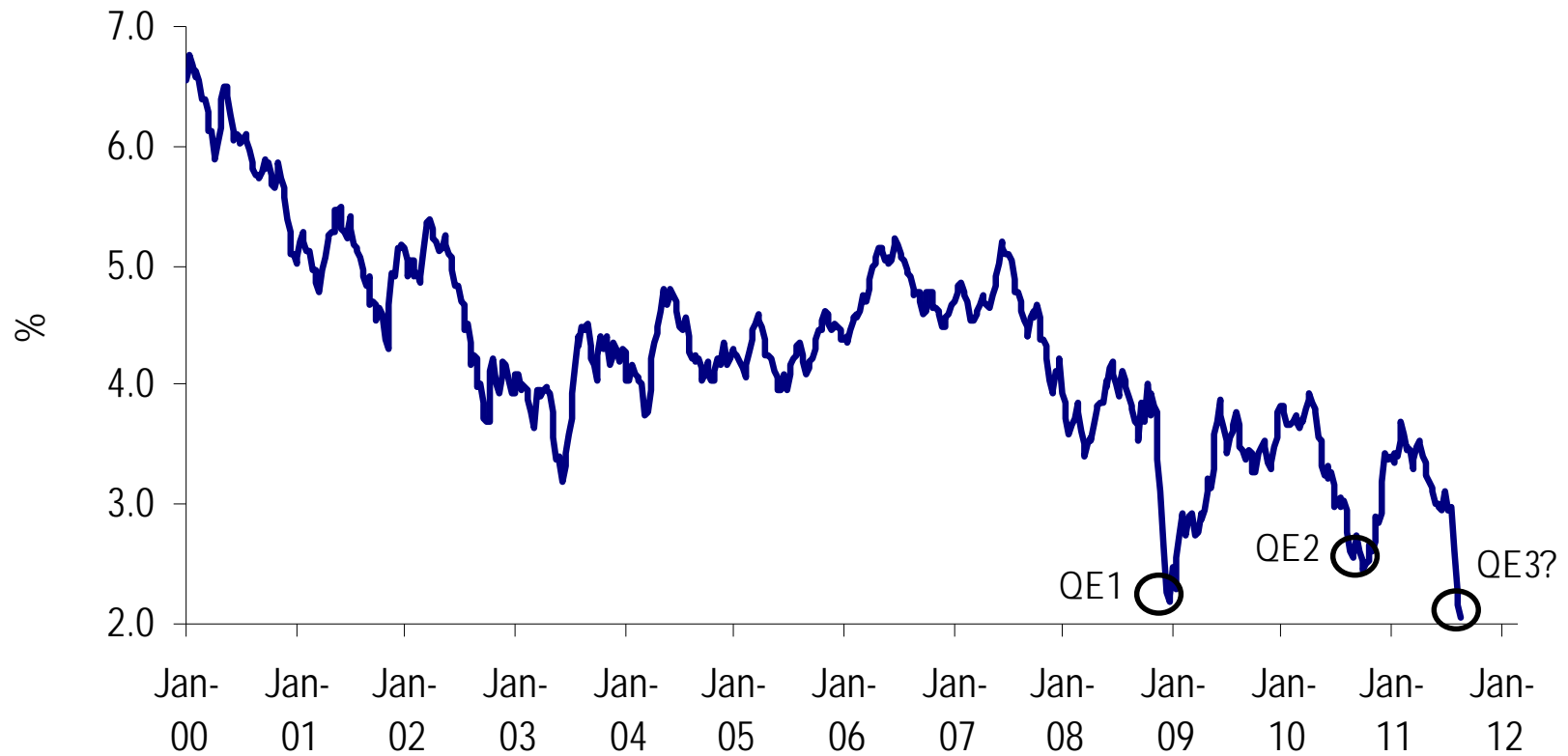
(last obs. Q2 2011)



Source: Federal Reserve; BEA; Encima Global

# 10 Year U.S. Treasury Yield Too Low

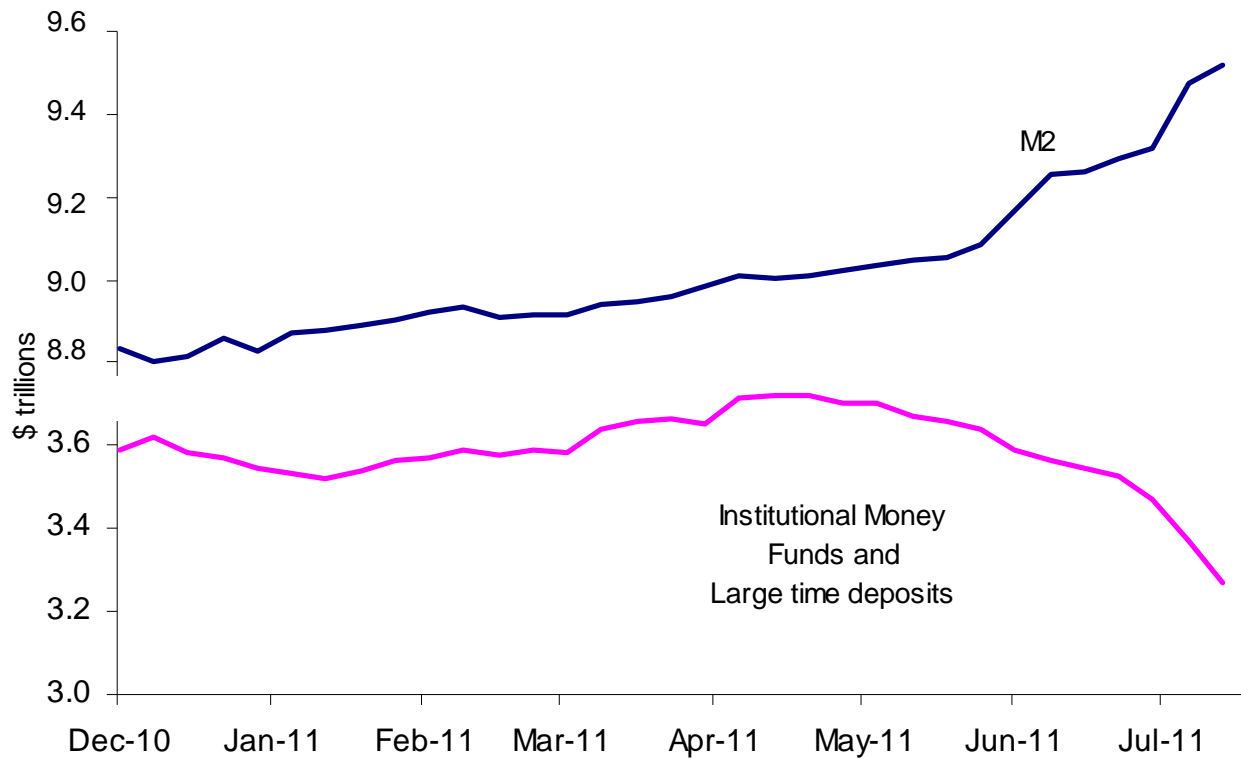
(last obs. August 23, 2011)



Source: Federal Reserve Board; Encima Global

# M2 Vs 'Institutional Money Funds' plus 'Large Time Deposits'

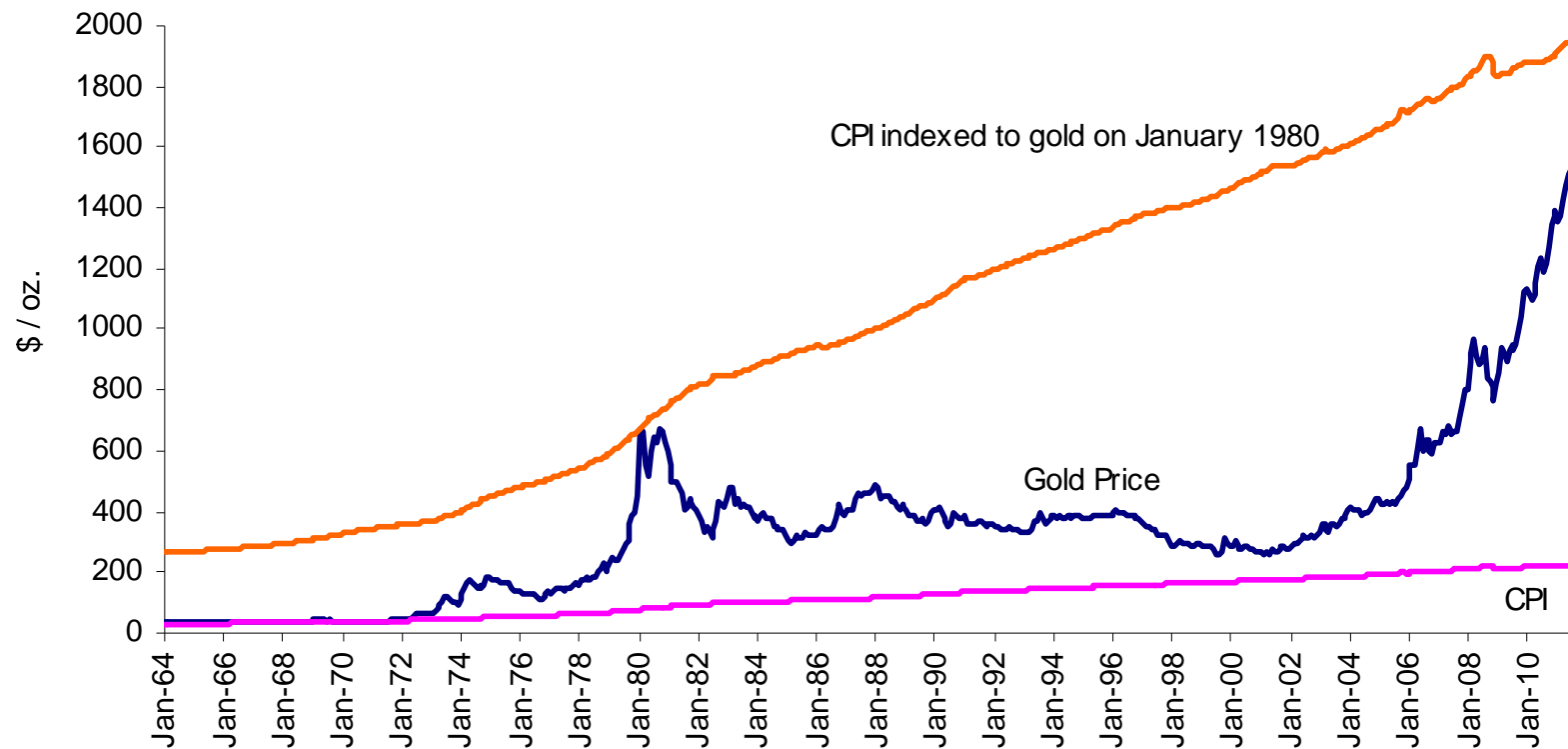
(last obs. August 10, 2011)



Source: Bloomberg; Encima Global

# Gold Prices Very High In Real Terms; Like 1980

(last obs. August 23, 2011)



Source: Wall Street Journal; Bureau of Labor Statistics; Encima Global

## Low Platinum / Gold Price Ratio

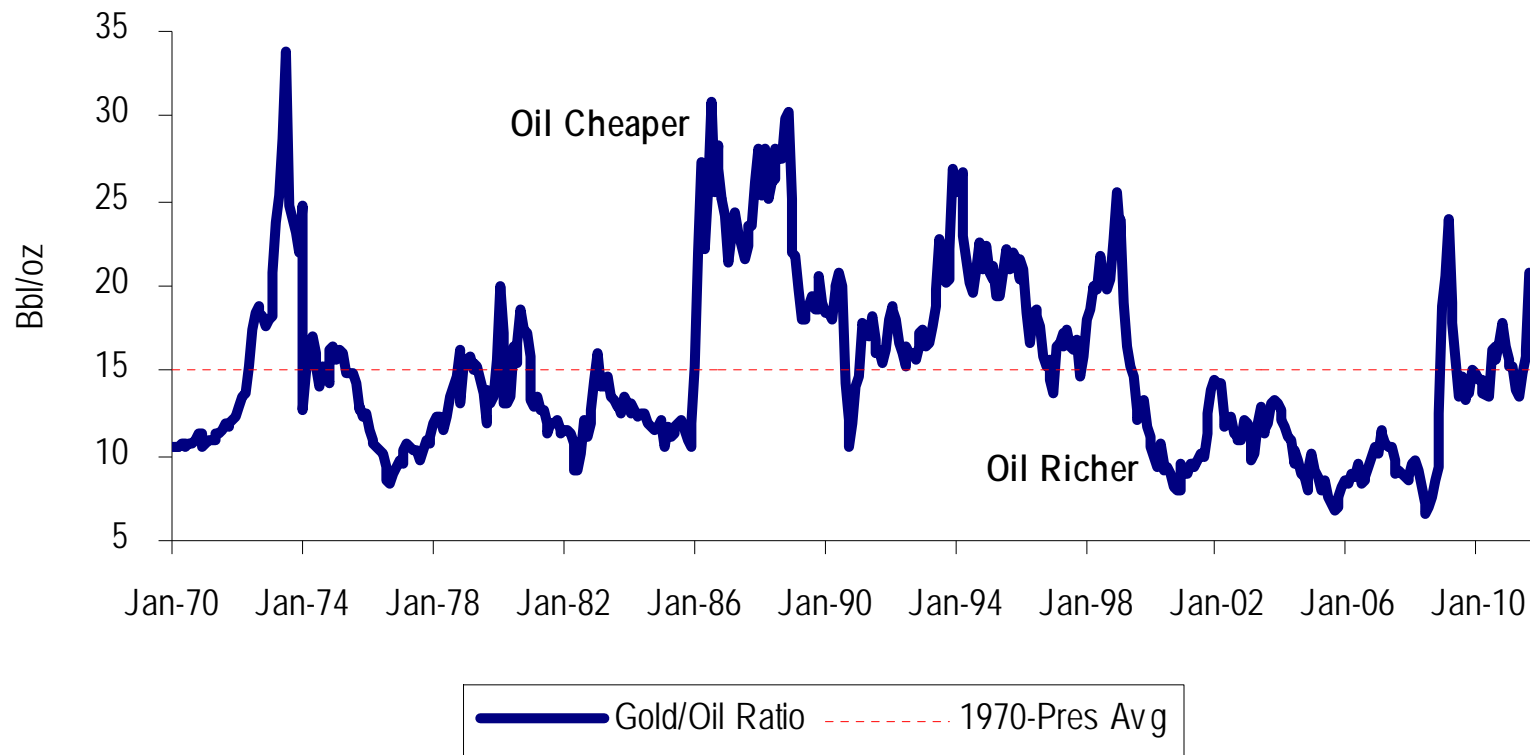
(last obs. August 24, 2011)



Source: Wall Street Journal; Encima Global

# High Gold / Oil Price Ratio

(last obs. August 24, 2011)



Source: Wall Street Journal; Encima Global



**Note: This document is confidential and intended solely for the use of the individuals to whom it is presented. Encima Global LLC does not accept liability for the content or for the consequences of any actions taken on the basis of the information provided. The information is not necessarily complete, and we make no warranty as to its accuracy.**