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Special Report

May 2008

The Latest On The Credit Crunch And Commodity Speculation

May 15, 2008 Conference Call
(This transcript has been edited)

James A. Bianco, President, Bianco Research: Good morning, everybody. This is Jim Bianco. Welcome to our monthly Conference Call.

Summary And Conclusion

"The Latest on The Credit Crunch and Commodity Speculation" is the title. So I am going to delve into two topics because I think that they are somewhat related. And they are kind of the two hot topics of the month. Let me give you a little bit of a summary up front.

The financial system losses are still outpacing the capital raised. It still means that the financial system is shrinking. We are still not out of the woods yet. Credit spreads and some measures have gotten better. But they are still at levels that would consider to be stressed. I think that credit spreads have followed the stock market higher on a hope that the worst is behind us so it is key to their performance.

Last month's call was titled "The Tradable Bounce," and we have definitely had one. We are now approaching two months from the March 18 stock market low. And I do think that it is still a rally in a bear market, and that we are very close to the end of this rally – if not at the very end of that rally. I've got some statistics to support this case.

The Federal Reserve, I have argued, has been doing what it can and not what it should. What it can do is to provide liquidity. What it should do is something that Bernanke mentioned today in his speech. He is speaking now, or wrapping up now as we start. He was strongly suggesting, imploring, begging, pleading, threatening the financial firms to keep raising capital. That is, I think, the key to this situation. We have a shrinking financial system. But the Fed can't fix that; they can only supply liquidity.

The liquidity that they are supplying has been leading, I believe, to an expectation of inflation. And I know that the Federal Reserve keeps saying that, as long as expectations for inflation don't rise, then everything is OK. But I strongly disagree with them. I think that they have been rising. They have led to higher commodity prices.

Let me be clear on this. I will talk about it in a second. It's not that the money that the Fed is providing is going straight into commodity futures contracts. It's that they are giving, if you will, to use the metaphor "wind at the back" for those that want to buy commodities. That has led to a lot of speculation in commodities.

However, I think that what is important about the speculation is that – I know the parlor game that we all want to play is "What Would the Price of Crude Oil Be If There Weren't Speculation" – nobody knows. And I'm not going to give you a guess on that number. But I want to, instead, answer what I think is a more relevant question, which is "Who are the speculators?" They are not the 25- or 30-year-old hedge fund manager in front of five computer screens screaming and barking buy-and-sell orders into the phone. In some respect, I wish that it were because I think that the market would be a lot more stable. Rather, it is the long-only commodity fund that is buying because they believe that there is a commodity bull market. And that fund is, quite frankly, you and me. It is really unlevered investors that are in endowments and in pension funds. And the public, through commodity ETFs, that I think is doing more of the speculation than the traditional speculator. And I'll talk a little bit about that and what it means at the end.

Banking Losses And Capital RaisedOK, Page 2 – let's go back to the beginning – banking losses and capital raised. Here is the update of our table that we have been running quite regularly in our *Newsclips* product. And we will continue to run it as long as it is relevant. Let me start on the right – worldwide financial

system losses and capital raised as of yesterday was at $335 billion of total losses, $246 billion of capital raised. This number does get updated every day. I think that it's about $1 billion or $2 billion higher today than it was yesterday. But the bottom line with these numbers is that, when you look at them, there is about, roughly speaking, $90 billion more in losses than in capital raised.

Total Banking System Losses & Capital Raised
As of May 13, 2008
Billions of U.S. Dollars

Firm	Loss	Capital Raised	Difference
Citigroup	40.9	44.1	3.20
UBS	38.2	28.1	(10.10)
Merrill Lynch	31.7	17.9	(13.80)
HSBC	18.3	2.0	(16.30)
Royal Bank of Scotland	15.2	23.3	8.10
Bank of America	14.8	17.0	2.20
Morgan Stanley	12.6	5.6	(7.00)
JPMorgan Chase	9.8	7.8	(2.00)
Credit Suisse	9.5	1.5	(8.00)
IKB Deutsche	8.9	13.1	4.20
Washington Mutual	8.3	10.0	1.70
Credit Agricole	8.3	0.0	(8.30)
Deutsche Bank	7.6	3.2	(4.40)
European Banks Not listed	7.1	0.0	(7.10)
Wachovia	7.0	10.5	3.50
Societe Generale	6.2	8.6	2.40
HBOS PLC	5.7	7.9	2.20
Mizuho Financial Group	5.4	0.0	(5.40)
Fortis	5.1	0.0	(5.10)
Canadian Imperial (CIBC)	4.1	2.9	(1.20)
Bayerische Landesbank	3.6	0.0	(3.60)
Other Asian banks (excluding Mizuho, Nomura)	3.5	0.0	(3.50)
Dresdner	3.4	0.0	(3.40)
Lehman Brothers	3.3	6.2	2.90
Etrade	3.3	1.8	(1.50)
Wells Fargo	3.3	0.0	(3.30)
Barclays	3.2	9.8	6.60
West LB	3.2	7.7	4.50
Bear Steams	3.2	0.0	(3.20)
National City	3.1	8.9	5.80
Goldman	3.0	0.0	(3.00)
Other Canadian banks (excluding CIBC)	2.5	0.0	(2.50)
Nomura Holdings	2.5	1.2	(1.30)
ABN Amro	2.4	0.0	(2.40)
HSH Nordbank	2.3	0.0	(2.30)
LB Baden Wuerttemberg	2.0	0.0	(2.00)
Bank of China	2.0	0.0	(2.00)
Natixis	1.9	0.8	(1.10)
BNP Paribas	1.6	0.0	(1.60)
Unicredit	1.5	0.0	(1.50)
DZ Bank	1.5	0.0	(1.50)
Lloyds TSB	1.3	0.0	(1.30)
Other US Frims	1.3	1.2	(0.10)
Commerzbank	1.3	0.0	(1.30)
Caisse d'Epargne	1.2	0.0	(1.20)
Hypo Real Estate	1.0	0.0	(1.00)
Gulf International	1.0	1.0	0.00
Sumitomo	0.9	3.1	2.20
Mitsubishi UFJ	0.9	0.0	(0.90)
21 Taiwanese banks	0.9	0.0	(0.90)
Rabobank	0.9	0.0	(0.90)
Sachsen LB	0.9	0.0	(0.90)
Sumitomo Trust	0.8	0.0	(0.80)
Alliance & Leicester	0.7	0.0	(0.70)
Aozora Bank	0.5	0.0	(0.50)
Sovereign Bancorp	0.3	1.5	1.20
Shinsei	0.2	0.0	(0.20)
Total*	**335.1**	**246.7**	(88.40)

Source: Bloomberg L.P.

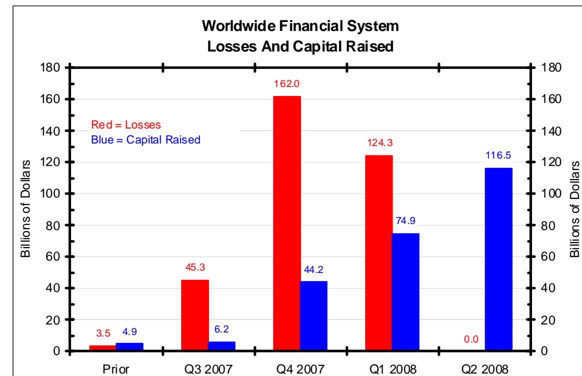
The typical financial firm is levered about 14:1. Let me just use some round numbers. That means that there is about 1.3 trillion less in credit than there was when this credit crisis started last year. There is a shortage of credit. We need the financial system to raise more capital, to cover those losses.

By the way, these losses that we are looking at here are in the financial system, which is better described as banks and brokers. And there is the list on the left of who has lost that money. This list does **not** include Fannie and Freddie, the GSEs, or the Federal Home Loan banks. It does **not** include the monoline insurers, so there is no Ambac, MBIA, Radian, or MGIC. It does **not** include insurance companies. There is no AIG on this list. Finally, it does **not** include finance companies. There is no CIT. There is GE Capital on this list.

Worldwide Financial System Losses and Capital Raised
As of May 13, 2008
In Billions of Dollars

	Total		Q2 2008		Q1 2008		Q4 2007		Q3 2007		Prior	
	Losses	Capital	Losses	Capital	Losses	Capital	Losses	Capital	Losses	Capital	Losses	Capital
America	152.6	135.1	0.0	58.7	58.6	47.9	68.5	27.7	24.8	0.8	0.7	0.0
Europe	163.9	106.3	0.0	56.0	64.5	23.5	81.3	16.5	15.3	5.4	2.8	4.9
Asia	18.6	5.3	0.0	1.8	1.2	3.5	12.2	0.0	5.2	0.0	0.0	0.0
Worldwide	335.1	246.7	0.0	116.5	124.3	74.9	162.0	44.2	45.3	6.2	3.5	4.9

Source: Bloomberg



If you added all of those firms into the list, then you would get a much bigger net loss. But I want to look, basically, at the financial intermediaries. And that is why I have kept this universe this way. Also, it becomes really unwieldy to try and scan the universe of every known company for losses related to the credit crisis, so we try to keep the sample set a little bit smaller and a little bit more manageable.

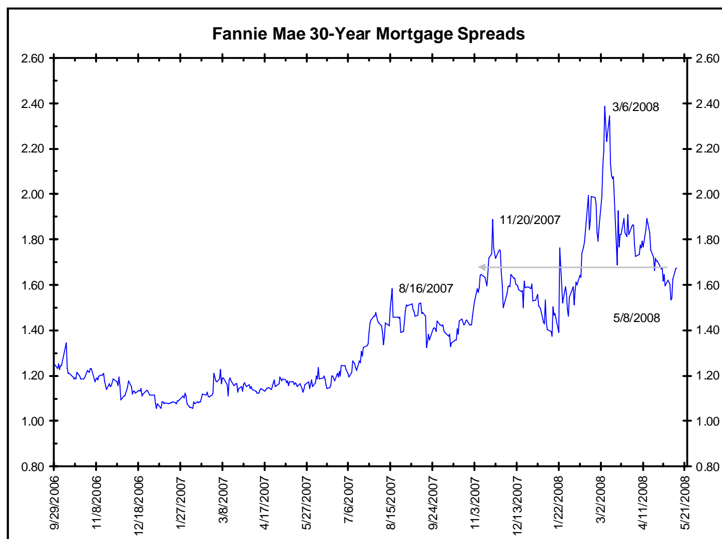
Mortgages And Munis

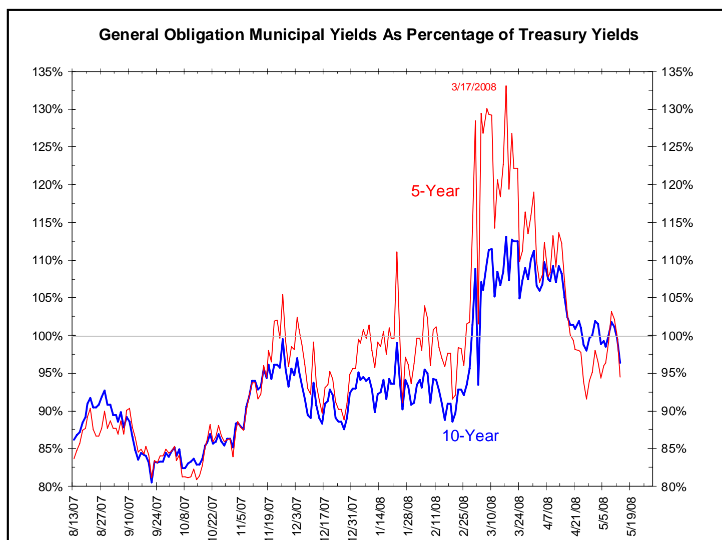
So the losses are still larger than the capital raised. That means that the financial system is still, on balance, smaller than it was a year ago. The problem – if you turn to Page 3 – has always been, then, that we don't have enough credit to go around and we have been rationing credit. And that is why we have seen, in the market, these crises bounce from one three-letter acronym to another three-letter acronym that we have never heard of, because not everybody can get credit.

In the past – the "past" being last year – when somebody wanted to borrow money, one would call up a lender or broker and say, "What is your rate?" And if you were OK with that rate, then you could borrow pretty much as much as you wanted. Today, or at least during the credit crisis, the problem was that, even though they would quote you the rate, the terms would be different, or sometimes the money was not

available. And the most recent example of that has definitely been in the Interbank Market. They have been quoting rates to each other and have been either lying on these rates, and now the British Banker's Association is trying to fix LIBOR. Or even though they may not be lying on those rates, they don't have the size that people would think.

The result of this supply constrained rationing of credit is what I have termed the "The Upside-Down Credit Crisis." In the charts on Page 3, I show munis and mortgages, two very high-quality markets. And you can see that, by early March, their spreads were the widest that we have seen. In the case of Fannie Mae spreads by March 6, that was a 22-year wide in their spreads. In the case of munis, you can see on bottom chart, that was at least a 20-year wide in munis, if not the widest ever.





What I mean by "upside-down" is that the highest-quality instruments – munis, mortgages, agencies – are **relatively** doing worse than the lower-quality instruments, say investment grade, high-yield, and even equities. Equities have yet to reach that media definition of a 20% bear market correction.

The reason that the higher-quality instruments were doing worse is that we are rationing credit. Higher-quality instruments – mortgages, munis, agencies – are not bought by investors, fully collateralized; they are bought on margin. They are bought with loans. They need credit for those markets to work. And when we had the credit crunch, the higher-quality instruments were doing relatively worse than everybody else because they could not get the lending or the leverage available in those markets

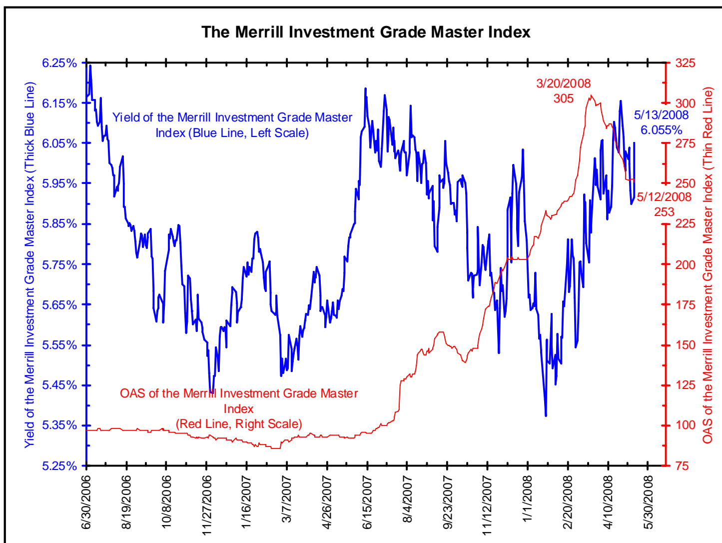
Corporate Yields And Supply

Now, if we go to Page 4, there has been some talk that the markets have been healing themselves. That is true. Even in the charts on Page 3, you could see that we're off of those mid-March wides. And, on Page 4, what I wanted to show is that there has been a lot of talk about supply in the Corporate Bond Market.

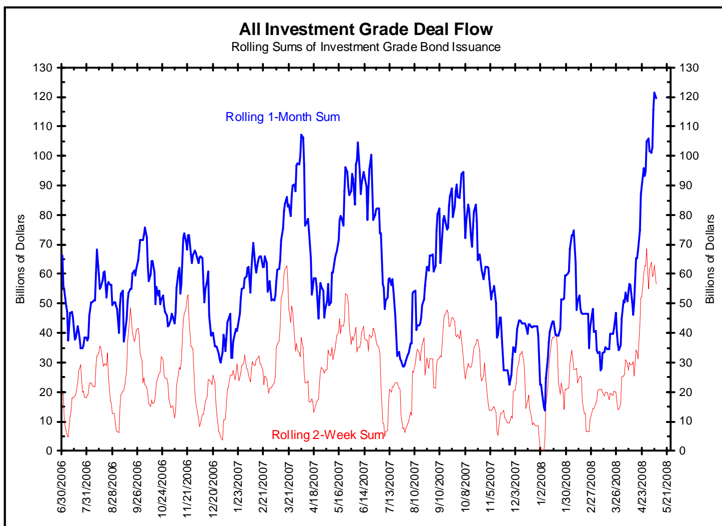
The one thing that I have always tried to emphasize with supply – my favorite line to use is the old saw in the bond market that there are no bad bonds, there are only bad prices. The fact that somebody raised money, in and of itself, is not a newsworthy event. At the right price, anybody could raise money. At the right price, I could restart Enron. You may not like the price that I would have to do it at, but it is theoretically possible. So the fact that money gets raised is not necessarily the big story. The big story is what is the price that it is being raised at. So, with that, let's take a look at the charts on the next page.

In the top chart on the upper left – Merrill Investment-Grade Master Index – the red line on the right scale shows the OAS – the option-adjusted spread. And you can see that widened out dramatically until March 20 and has been narrowing since. The blue line is the absolute yield level of this index on the left scale.

What I want to point out here is that, as of Tuesday, on the 13th, the absolute yield of the investment grade index was at 6.055%. This index was yielding 5.84% on March 20. So, the market has gotten better in terms of OAS but the overall yield is **higher** than it were when the market wasn't working.

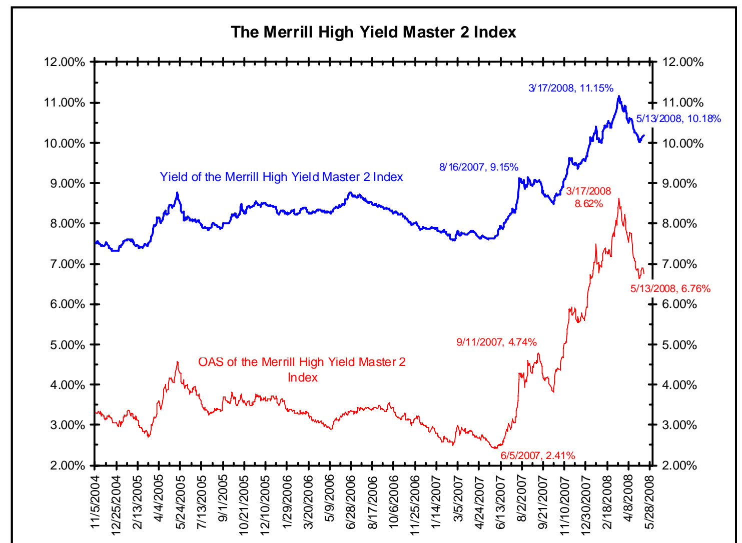


Did we all know that, really, what was needed to fix the credit crisis was higher yields? If you look at the bottom chart, it shows deal flow. The blue line, or the top line, is a rolling one-month sum of all Investment-Grade corporate bond issuance. The red line is a rolling two-week sum.

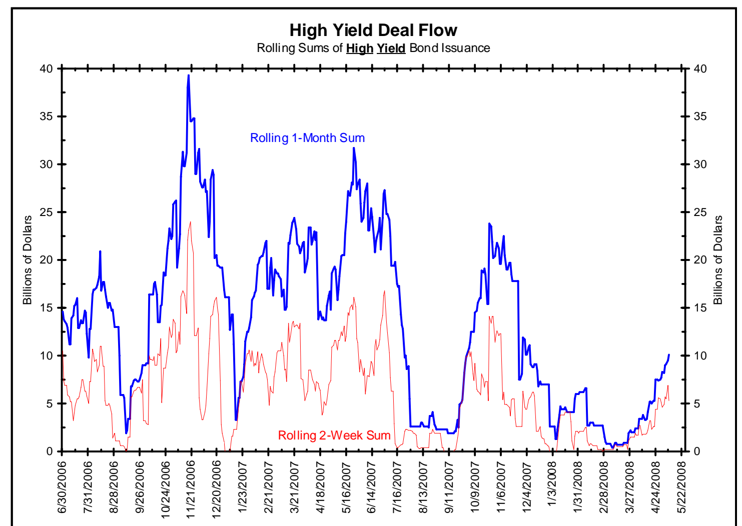


It shot out to above even the bubble era of 2006-2007. We've got more issuance in the last month in investment-grade than we did in 2007. And that is occurring at **higher** yields now than when the market was shut down in February or March.

If you look at the chart on the top right, it shows the OAS of the High-Yield Index in red and the absolute yield of the High-Yield Index on top in blue. And you can see that the absolute yield of the High-Yield Index is **lower** now than it was back in mid-March.



But if you look at the rolling sum in the chart below, of high-yield issuance, it's not anywhere near its 2007 high. So high-yield issuance has not come back as much as investment grade issuance.



We wrote a piece about this the other day. And we speculated a little bit about what this could possibly mean.

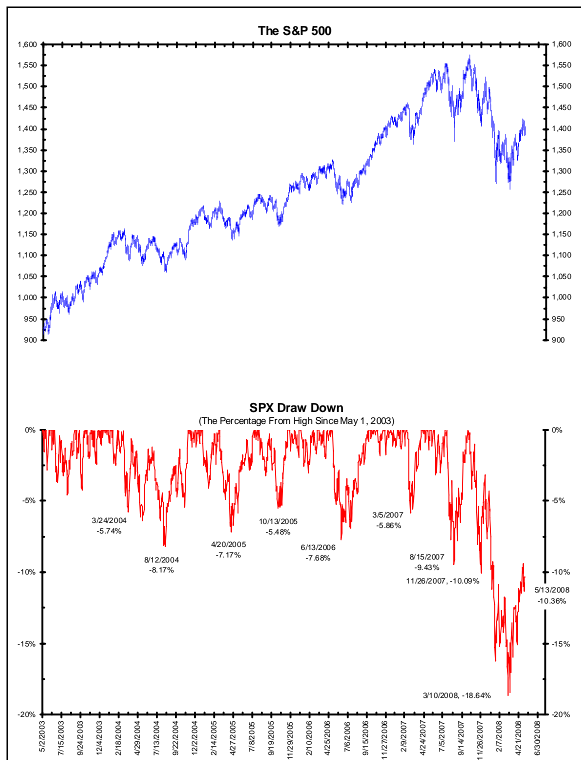
And, as we said, one of the things about trying to interpret "supply" is that it's very complicated. More supply doesn't mean that things are better, and less supply doesn't mean that things are not better. The argument that we gave was that, if the credit crisis was really passing, then the issues that depend most on credit, like high-yield, would be doing much better, and they're not. The investment-grades are getting done at higher overall yields. Why? Because Treasury yields have gone up more than the narrowing of investment-grade credit spreads.

Overall yields have been rising, I think, in part because of a fear of inflation. So it is equally as valid, I think, to look at these numbers when you break them down and just not say, “There is more issuance. That must mean that it’s over with.” To look at it and say, “It’s all coming in investment-grade.” It’s all coming in public investment-grade. It’s not even coming in Rule 144A issuance. That is still lagging quite a bit. It’s still coming into more traditional public investment issuance.

The argument could be that corporate managers are rushing out with deals higher now than they would have done a month or two months ago because they are afraid that Treasury yields are going even higher because of inflation. So it’s not at all clear that these measures are telling us that the situation is getting better. It is better now than it was in March. I still think that it’s more along the lines of a bear market rally. That leads us to the chart on Page 5.

The Stock Market

Because the stock market seems to be the risk measure that drives world finance, let’s take a look at it. The chart below, on Page 5, shows the S&P 500 on the top. And on the bottom is this contraption that we refer to as the S&P drawdown.

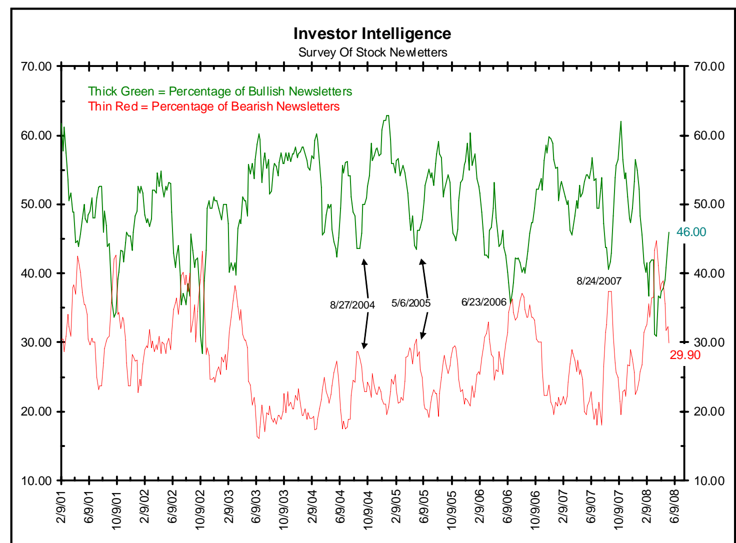


Whenever the red line in the bottom panel is at zero, that means that the S&P is at a new post May 1, 2003 high. And whatever number it is at shows you how far off that high that we are.

At its worst closing level on March 10, the S&P was 18.6% off of its all-time high that was set last October 11. Currently it is still about 10% off of that high.

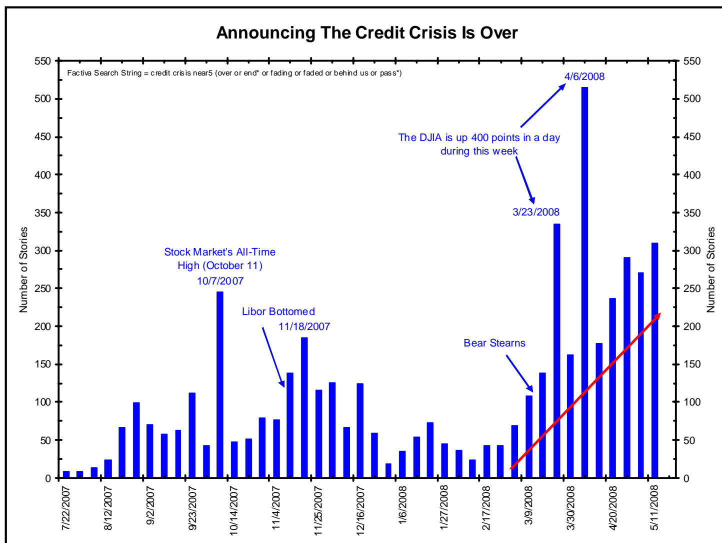
Again, remember that I was saying that this was a **relative** market. This market has not done the media definition of a 20% correction, which is a bear market. But mortgages and munis have had their worst spreads in 20 years, or 30 years in the case, possibly, of munis. Again, the better stuff, **relatively,** was doing worse than the lower-quality stuff -- at least on the credit spectrum, the lower-quality stuff.

Now, what has happened since the market has started to rebound – if you’ll look at the chart on the below – “The Investor’s Intelligence Survey” has repaired itself. We are back to 46% of the newsletter writer’s being bullish, 29% are bearish on the stock market. That’s a flip-flop of what we saw in mid-March when we had more bears than bulls.



The chart on the next page shows a measure of all of the people that have come out with mentions in the media that the credit crunch is over. We are now at the third highest week ever.

Everybody seems to want to beat a path to some kind of a reporter to say, “Put me on record as saying that the credit crunch is over. This all is happening while the stock market is retracing roughly half of its prior advance – a bear market rally.



If you were to ask me, in general, "What do you expect out of a bear market rally," I would reply, "A rally that lasts some period of time, does some kind of a major retracement, and, by the time that it's done doing the retracement, everybody has announced that whatever the previous problem was is over, and they're bullish. That seems to be exactly what we have right now.

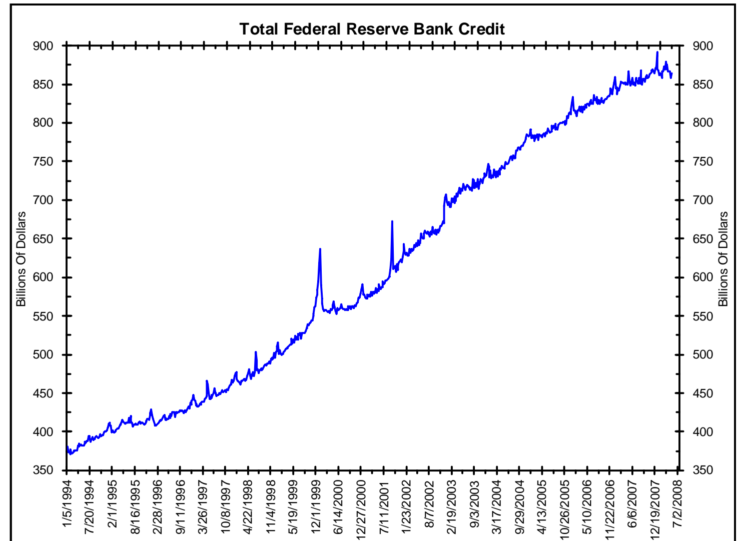
And if that is indeed the case, and the Stock Market is stalling out, and it's going to start down, then I would expect to see credit spreads start to widen out back again, and that mortgage spreads and muni spreads would start to widen. And I would even start to see – at least in terms of credit problems starting to resurface themselves or become more of an issue. It won't necessarily be the issue that we saw last year, but they could continue to start being that issue.

The Federal Reserve Page 6 – "The Federal Reserve"

The Federal Reserve has been acting in extraordinary ways to try and deal with the credit crisis. What the Federal Reserve has been doing has made a lot of us scrambling back to our old books about how the Fed works because we haven't had to think about these things for 20 to 25 years.

And I hear it all of the time and read it all of the time that a lot of people, I think, are still not quite sure what the Federal Reserve is doing. But they are hoping that it will work because they were told that it is significant. And, if nothing else, I'm not even going to bother to learn what the Fed is going to do; just don't fight the Fed. If there is a problem out there, then they are going to fix it. Just stay long risk, stay long credit, stay long stocks.

What I think that we need to do is to investigate at least a little bit of what has been happening. The top, left chart is "Total Federal Reserve Bank Credit." For those of you not familiar with the Fed, let me say this simply – the Federal Reserve is a money manager. They manage other people's accounts. I try to keep this at as simple of a level as I can. The other people's accounts that they manage are the reserve accounts of the Banking System.

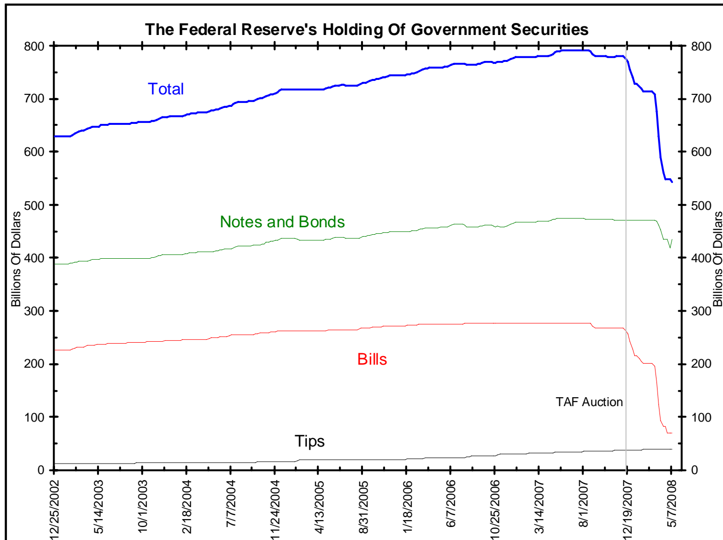


In the regulated part of the Banking System, there are roughly $11-plus trillion of assets that are supported by about $850- to $860 billion-worth of reserves, roughly around 12:1 leverage, at least on the regulated side. Then you get into LIBOR and the unregulated side, and the leverage numbers can be a little bit higher. The Federal Reserve has the ability to take the reserve accounts and add liquidity to those reserve accounts, or to drain liquidity from those reserve accounts. And banks will try to manage to their optimum level of their reserve accounts as the Fed adds and drains liquidity.

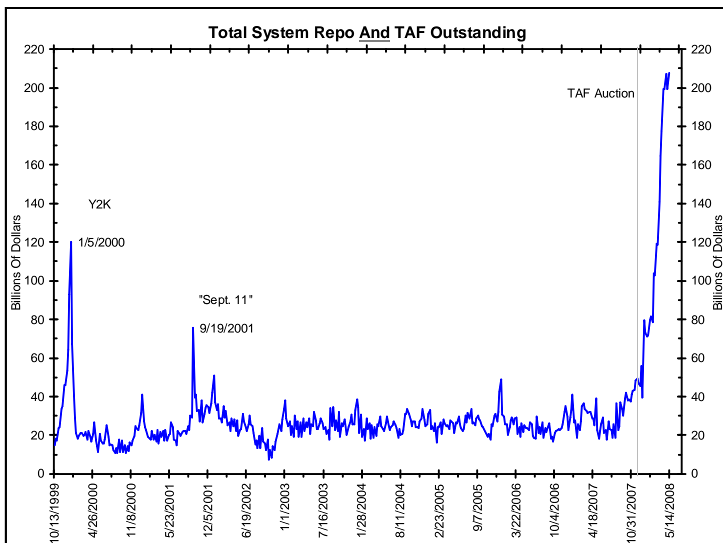
This chart on the upper left shows the total amount in reserve accounts, the total Federal Reserve Bank Credit. It's a very predictable upward-moving line. There are some seasonal spikes in it that are not very significant. And there hasn't been much change in it.

But as you look at the rest of the charts on this page, you will see that there has been change all over the place. The chart on the upper right – The Federal Reserve's Holding of Government Securities – has been collapsing as of late. It used to be before that was invented the term "Auction Facilities" and "TAF" running at a little

bit less than $800 billion. Now, it's around $550 billion. Most of that decline has come from the Fed's rolling off Treasury bills. They have, now, about $50 billion-worth of Treasury bills in those reserve accounts where they used to have about $250 billion in those reserve accounts.



What the Fed has been doing, in the fancy word, is sterilizing all of their operations. They have been increasing liquidity through system repos in the TAF Auction, and you can see that in the bottom right, to over $200 billion. They have been lending out their securities. I didn't show a chart of that, but that is still up around $150- to $200 billion, too. Now, if they did nothing else, Federal Reserve Bank credit – that chart on the upper, left – would have shot up off the top of the page. But to offset that, they have been selling or letting their bills mature – Treasuries – to the same degree so that they can keep roughly the same growth rate.

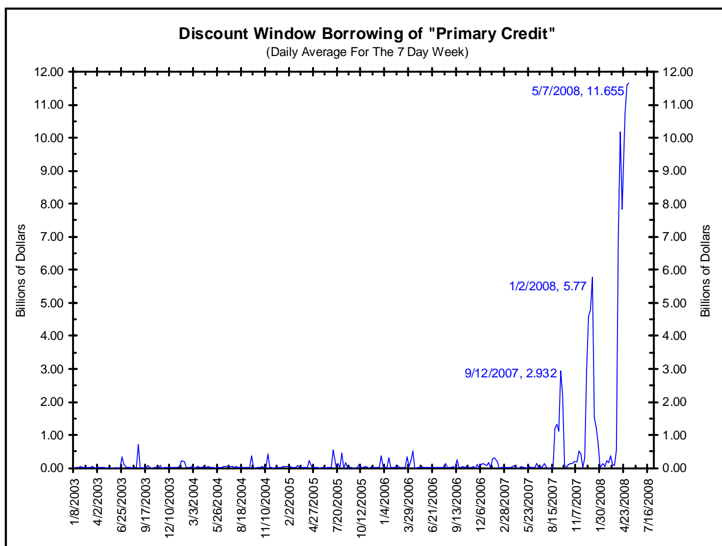


Why are they doing that? There are a couple of reasons. If the Fed over-reserves the Financial System, then that is quantitative easing, what they did in Japan. Over-reserving the Financial System means that everybody would be a seller of Fed Funds. Fed Funds are excess reserves. I sell my excess reserves. I get no interest from my reserve account. It's a zero interest rate account. So if I have access, then I will sell it to somebody who needs it and try and earn some interest on it. They over-reserve everybody, everybody is a seller, and the Funds Rate goes to zero, and it ceases to be a tool to monetary policy. The Fed doesn't want them. They want to keep the tool of monetary policy intact. So they have been sterilizing it.

Recently, the Fed has also asked for the ability to pay interest on reserves. Now, they have to ask Congress for it. Whatever profits that the Fed makes get rebated back to the Treasury. So if the Fed is going to want to make a move that is going to change the possibility of the Treasury making money, then they have to ask for Congress' permission. Congress gave them permission to start paying interest on reserves starting in the year 2011. But now they are back and formally requesting that they could move that up to right now. The idea there is that, if they start paying interest on reserves – say, two percent, which is the Funds Rate – then they can let that total Federal Reserve Bank credit number expand, and the Funds Rate would stay, roughly, at around two percent because there would be no real need to be a seller of funds because I could sell them and get two percent, or I could leave them in the account and get two percent. Why bother? It's six of one, half a dozen of the other.

I have argued, by the way, that that's a dangerous precedent that I would rather not see the Fed do. A dangerous precedent is that it's just going to lead to very easy monetary policy. The Fed could expand into infinity under that environment, and there would be no interest rate break on the Fed. At least, in the current environment, if the Fed wants to expand its balance sheet, then the sign that we know that it's too easy or too lax would be that the Funds Rate would drop or the Funds Rate would rise if they are too tight. But now they would really pretty much take that off of the table by Fiat saying, "Here's the rate that we're going to do," and then it sort of gives them carte blanche to expand or contract their balance sheet as they wish. And I think that it could increase volatility in the Market.

Finally, in the chart on the lower left, I thought that it was interesting to note that, for all of the argument that the situation is getting better, discount window borrowing of primary credit is banks only, not the brokers. The total number of discount window borrowing is $28 billion. But most of that is the brokers that have been allowed there since mid-March. The banks are at $11.655 billion as of May 7. That's the second-highest reading in history. The highest was $11.7 billion, just slightly higher than this, the day after September 11, 2001. The Banking System, for all of this talk that it's healing itself and is getting better, still has record discount window borrowings going on there, too.



Long-Only Index Funds

Now, going to Page 7, I wanted to discuss a little bit about the Commodities Market. The Credit Crisis, I think, has been enjoying a bear market rally. Ultimately, the fix, I think, is going to be that we have to raise enough capital to offset the losses, to return enough credit to this system. We are still rationing credit in the Marketplace right now. It's just a little less acute now than it was a few months ago. And we are all hoping that it's going to get better. Spreads have gotten better. But if you look at a lot of those charts on pages 3 and 4, there are still a lot that are considered crisis levels, just not the mid-March crisis levels. They are still some of the highest levels that we have seen in many years for some of those markets.

Ultimately, we have turned to the Federal Reserve and said, "Fix the problem, Ben." Ben can't fix the problem. He can't force the Banking System to go out and raise enough money to cover their losses. Although they have done a fair amount of it, they haven't covered all of them. He can supply liquidity. And that is what he has been doing. He's not doing what he should because he can't. But he's doing what he can, and that is supplying liquidity.

That liquidity, I think, has a powerful motivating effect on everybody. And I want to use the word "motivating." I don't want to make the case that there is some kind of a direct tangent to some Federal Reserve credit straight into futures contracts. You can't make that line. But what you can make the line is that all of this money breeds an expectation of inflation. The Fed is trying to pretend that it doesn't exist because they don't want to tighten. But I believe that it's there. And it's there in the belief that, since inflation is coming back, people are looking for inflation investments. And one of those inflation investments is commodities.

This chart on Page 7 talks about long-only commodities funds. They are something that did not exist about seven to 10 years ago. In fact, they did not exist to any great degree maybe even 3 to 5 years ago, and that is the Long-Only Commodity Fund.

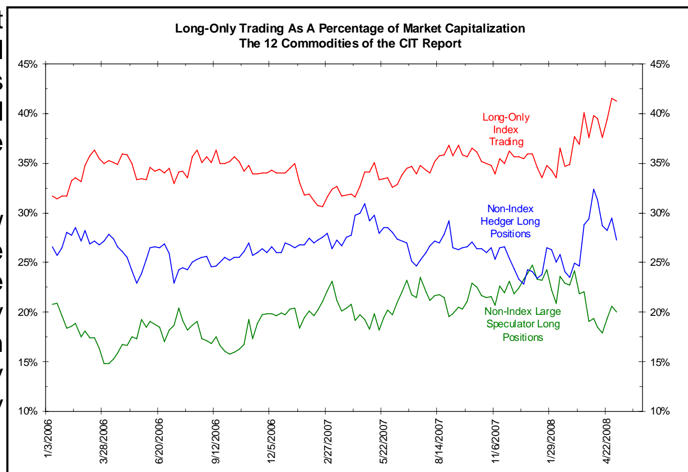
The CFTC – the Commodity Futures Trading Commission – early last year began releasing data on the Commodity Index Traders, or the CIT Report. This was taken from a recent commentary that we did. What we found is that, if you look at the long side of the Market – and I know that you've read in the paper that all of these dirty speculators and greedy hedge fund managers that are buying futures contracts, and shoving the price higher on crude oil, and people would say that it's going to be $80 or $100, or $70 if we didn't have that speculation, and I have no idea how they can make those kinds of statements. But I think that what they are doing is that they've got, conceptually, the right idea, but they are just focused on the wrong player.

The Long-Only Commodity Fund is a fully collateralized fund, meaning that they don't use leverage, so they buy $100,000-worth of crude oil with $100,000 in their account. They buy futures contracts deferred. And as they get close to expiration, they sell them and buy another deferred or roll them out. Now, initially, long-only commodity funds were sold on the idea that there was a positive carry in the roll, that if you bought these contracts and just kept rolling them every month, then you would make money on those rolls.

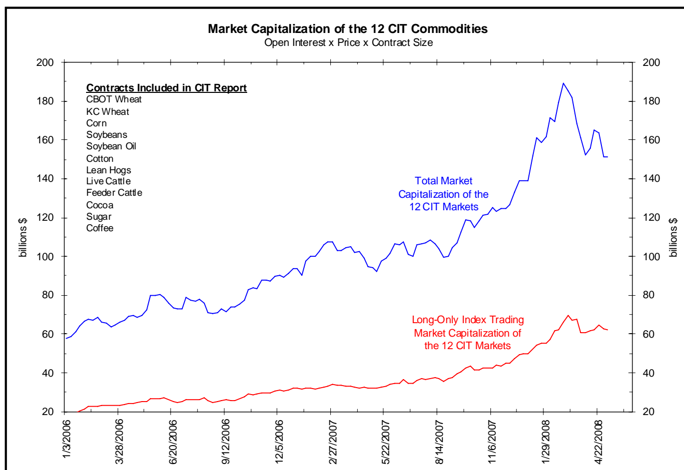
Well, what happened, I think, is that the long-only funds became so popular that they started to get rid of those rolls, that all of the forward curves in a lot of these contracts started to

become positively sloped so that, as you got close to expiration on a futures contract and went and bought the next month out, it was actually at a higher price, not a lower price. And then you started to lose money on the roll as the roll turned negative on you.

About 2 years ago, we were thinking that now that the roll is negative, and a lot of people are starting to understand this, maybe this would be the end of the long-only funds. Wrong. They continued to go, and then they turned into an object of speculation on higher commodity prices. And the charts here show how big they are.

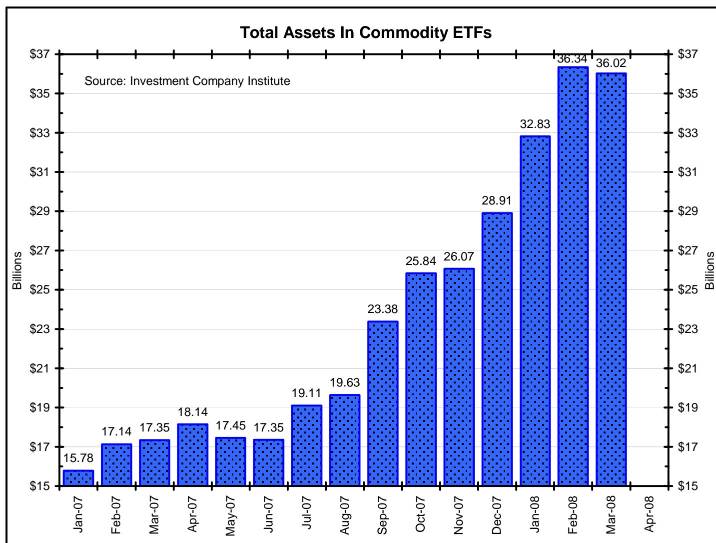


The CFTC releases hard data on 12 commodities, and those are shown on the upper chart. Notice that: energy is not on the list, gold is not on the list, gasoline is not on the list, crude oil is not on the list, and copper is not on the list. We recently asked the CFTC, and they have no plans to release anything but these 12 lesser commodities. But, nevertheless, you can see from the bottom chart that they make up over 40 percent of the open interest on the long side of the Market, where the traditional speculator that everybody wants to deride will spend half of that amount.

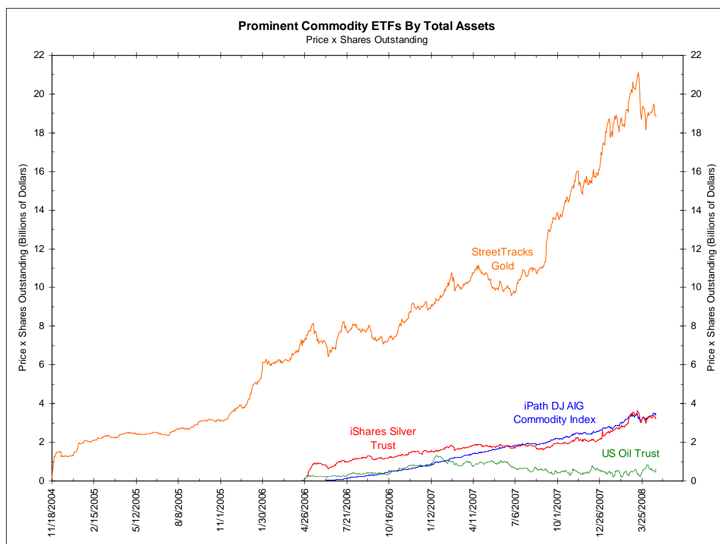


As a matter of fact, once you start stripping out the commodity index funds, the traditional speculator is net **short** these markets. What is the speculator – the 30 year-old hedge fund manager in front of a bunch of screens – doing all day long? Most likely **selling** these markets. This individual is selling these markets in hope of profiting because he believes that they are overdone and that they would start to come lower. That is why I think that a lot of people that are saying to raise margin requirements to reduce speculation – it's not going to do anything to raise margin requirements to the long-only commodity fund because they are fully collateralized. But what you could do is, if you chased the traditional speculator out of this market, then you have now removed the seller on this market. And all things being equal, you could drive prices higher.

This Is Also A Long-Only Commodity Fund Who are these long-only funds? The largest one is CALPERS. CALPER has a natural resource investment of about 5%, or about $17 billion. There are a lot of the other funds. Retirement Fund of Pennsylvania is another big player. If you go to the chart on Page 8, another player that is big in this is the public itself, through commodity ETFs. These markets have been booming as of late.



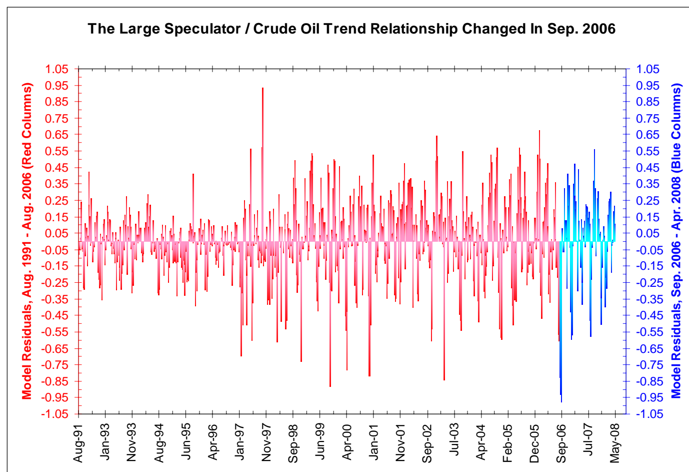
The bottom chart shows you the streetTracks ETF, which is the gold holding of ETF. This is an interesting situation. The Gold ETF is now the fourth largest owner of gold on the Planet, larger than the Bundesbank right now. It did not exist until 2004. They buy gold and stuff it in the basement of HSBC London, in their warehouse. And if you look at their glossy annual report every year, they've got pictures of palettes of gold in the basement, in the vault, saying, "Here's your gold down here."



So these are the buyers. Why are they buying. They are not buying crude oil because they are looking at charts. They are buying long-only commodity funds. Most commodity funds have somewhere between a 30%t and a 60% waiting in energy, most of them more towards the higher end, too – 40%, 50%, 60% percent waiting in energy. They are buying commodity funds because they are in an up trend. They are buying commodity funds because, I think, the Fed is inspiring them, through easy money, that there will be inflation. And if there is going to inflation, then what I want to do is to own inflation investments. And all of this money continues to flow into these investments. These investments own contracts. They push up the price of these contracts.

One of the things that I should also mention about these long-only commodity funds is that there is a hard time in understanding the way that some of these numbers and some of these data work, especially for securities people. Let me turn us to Page Nine. Yesterday, on CNBC, Dennis Neale mentioned at least half-dozen times that the Dow Jones Newswire had story about a tanker full of crude oil at New York Harbor that had no buyer and nowhere to dock, and that it was a sign that there is excess crude oil in the Marketplace, and that the Market is way over-speculated by greedy hedge funds -- that is exactly what he said – and that this was evidence that, if we were in such a shortage, then why is this tanker sitting out there? One of the problems that securities people have to understand is that we trade in fundable securities. We don't care what the serial number is on the security that we own. And we don't have to buy them in sequential order, if you want to think of it in those terms. But if you buy a cargo that is coming into New York Harbor, you're not done. Your operations department has to make sure that that cargo has a place to dock, that you can offload it, that you have a place to store it. And the industry has words for it, and it's called "distressed cargo." And that was a distressed cargo. That has happened at $10 oil. That has happened at $20 oil. That is happening at $125 oil. It's more of a sign of incompetence at a trading desk, that their operations department did not have somebody lined up or have somewhere to put that cargo. Then it was a sign that there is too much supply in the Market. So you get a lot of misinformation from them.

Regime Change In Crude Oil Commitment Data The charts on Pages 9 and 10 are taken from a recent special report that we did. We don't have commodity index trader data for crude oil. But what we did hear is that we started to try and take a look at the trend-playing abilities of the large speculators. And what we have noticed is that the relationships started to change – if you'll look at the lower right chart – in September of 2006, the reason being that the commodity index traders are embedded inside of the large speculator and the hedger accounts.



There are two types of commodity index traders, one is classified as a speculator and the other a hedger. And we did see a definite pattern between the two switch over, in that the large speculators' behavior is charted to change quite a bit since September 2006. And we think that the reason that it is that, embedded inside of that data, is the long-only guys. And the long-only guys are not the trend followers that we used to see. They just buy and just push higher. A lot of people have a hard time understanding this because a lot of people have a lot harder time understanding these markets.

Gasoline Demand

Finally, on Page 10, as far as gasoline goes, we did this little exercise. What you see on the table, on the left is the prices of gasoline as of the most current prices that we could find for 51 different countries expressed in U.S. dollars for gallon. The highest are Sierra Leone and Turkey at over $10 a gallon, all the way down to Turkmenistan and Venezuela on the bottom, at less than 20 cents a gallon.

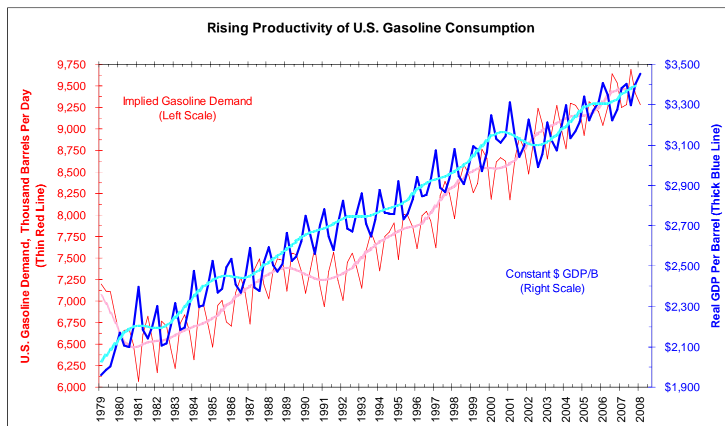
Gasoline Price ($US) and Consumption per Country

Country	US$/Gal	As of	Consumption (000's of b/d)	5 Yr Change in Consumption
Sierra Leone	$18.42	5/1/2008	8.43	6.03%
Turkey	$10.13	4/22/2008	669.40	1.59%
Norway (Oslo)	$9.87	4/14/2008	244.15	2.32%
Netherlands	$8.95	4/28/2008	987.75	-1.26%
Germany	$8.63	4/20/2008	2,467.39	-1.09%
Belgium (Brussels)	$8.44	5/12/2008	593.32	-0.16%
France	$8.25	5/5/2008	1,937.01	-0.90%
United Kingdom	$8.18	4/20/2008	1,764.34	0.97%
Denmark (Copenhagen)	$8.14	4/21/2008	190.48	-2.25%
Iceland	$8.06	3/31/2008	17.86	0.42%
Finland	$7.98	1/5/2008	238.80	2.37%
Hong Kong	$7.56	3/5/2008	293.11	3.62%
Sweden	$7.42	1/3/2008	359.64	-0.52%
Italy	$7.30	11/8/2007	1,677.95	-1.17%
Israel	$7.20	5/1/2008	232.83	-3.20%
Croatia	$6.57	3/20/2008	101.85	3.55%
Romania (Bucharest)	$6.32	4/15/2008	238.23	0.80%
Switzerland (Zurich)	$6.24	12/19/2007	252.53	0.07%
Cyprus	$6.18	3/20/2008	57.83	2.29%
Brazil (São Paulo)	$6.01	4/29/2008	2,216.84	0.10%
India (Bangalore)	$5.77	4/18/2008	2,571.90	3.33%
Japan	$5.77	4/18/2008	4,972.14	-0.89%
New Zealand	$5.42	4/20/2008	154.44	2.61%
SriLanka	$5.36	4/18/2008	86.06	3.23%
Czech Republic	$5.27	4/18/2008	207.14	3.43%
Singapore	$5.19	1/2/2008	834.64	3.36%
Australia (Melbourne)	$5.18	4/23/2008	936.62	1.03%
Kenya	$5.00	1/2/2007	65.43	4.76%
Greece	$4.93	3/13/2006	438.40	1.85%
Canada	$4.73	5/5/2008	2,348.03	1.94%
Spain	$4.55	5/5/2008	1,591.05	1.29%
Korea	$4.53	5/5/2008	2,173.79	0.39%
Ukraine	$4.43	4/18/2008	344.03	2.47%
Pakistan	$4.01	5/4/2008	344.97	-0.86%
United States	**$3.84**	**5/5/2008**	**20,697.57**	**1.04%**
Russia (Moscow)	$3.79	5/7/2008	2,180.76	1.65%
Philippines (Manila)	$3.54	9/17/2007	340.05	-0.40%
Vietnam	$2.86	1/2/2007	273.44	8.90%
Malaysia (Kuala Lumpur)	$2.75	4/18/2008	501.07	1.07%
Thailand	$2.61	1/13/2007	928.61	5.77%
China	$2.44	5/5/2007	7,201.28	7.93%
Mexico (Mexico City)	$2.36	5/5/2007	2,045.69	0.12%
UAE	$1.70	5/4/2008	381.00	3.25%
Egypt (Cairo)	$1.23	5/5/2008	652.67	3.68%
Qatar	$1.14	4/18/2008	108.85	14.84%
Kuwait (Kuwait City)	$0.78	4/13/2006	438.40	3.99%
Saudi Arabia (Riyadh)	$0.45	5/16/2007	2,139.42	5.90%
Nigeria (Lagos)	$0.38	3/13/2005	312.03	0.41%
Iran	$0.33	5/5/2007	1,685.81	5.57%
Turkmenistan	$0.29	11/25/2006	107.42	7.70%
Venezuela (Caracas)	$0.17	1/12/2008	620.13	2.64%

Also shown on the chart is the consumption that these countries will use in thousands of barrels per day, and their 5-year change in consumption. If you look at the text on the right, bottom, where it says, "Table on the left," that table shows 72 million barrels a day, or 85% of World production. The consumption rates of the countries that have gasoline prices higher than the United States is 31 million per day, and they have a growth rate of half of a percent (0.48%) a year, or they are growing at 152,000 barrels a day. The consumption rate of those countries that have gasoline prices cheaper than the United States is 19 million barrels per day, about 60% of those above. But they have a growth rate 10 times higher, 5%, or one million barrels per day.

One of the problems with gasoline, I think, is that there are a lot of emerging-market countries – and if you look toward the bottom of that list, you will see China down there, at $2.44 a gallon -- they subsidize the price of gasoline, which encourages, in high-growth countries, even greater demand. And that is why the demand of this product continues to explode. It is being

subsidized in the high-growth countries. Oh, yes, sure, it's not being subsidized in Germany, Belgium, France, and the U.K., where they are near the top of the list, among the highest prices in the World. But they are not fast-growing economies, like China is or a lot of the emerging-market countries that you will see on the bottom of the list. So demand continues to leap ahead in terms of gasoline, so it's not slowing down. And the product that we use from crude oil will continue to go higher, as well.



Finally, for all of the blather in the U.S., that there are high gas prices -- and it's the number one topic that we all talk about – if you look here at the chart, on the upper right, in red, on the red scale, this is U.S. gasoline demand, and it's near its all-time high. In fact, you could argue that, if you smooth it out over a six-month period with some of the smooth numbers that you see in there, it is at its all-time high. There is no slowdown in gasoline demand. Even though it's over $4 a gallon in most parts of the Country, when has been the highest gasoline demand?

Right now. We have **not** slowed down at all during this nine-year bull market. Now, we could talk about it being the inelasticity of demand, and that has probably got a lot to do with it. But that suggests that, $4.50, or $4.60, or $5 is not going to slow down demand.

If there is a supply-demand imbalance in this World because of too much demand and not enough supply coming online, it's being subsidized by the emerging markets. It's very inelastic in the United States. We just complain about the price and just keep paying it. And that's not fixing the supply-and-demand problem, and that continues to push the price higher.

This, along with the Federal Reserve, is inspiring everybody to say, "I have got to have an investment in the things that are going to benefit from inflation like long-only commodity funds." They plow into that, and that tide raises all of the boats in the commodities markets, which continues to push those markets ahead even more.

Questions And Answers

OK, that is what I've got for my prepared remarks. Let me stop there and thank you for joining us. I want to move onto the Question-and-Answer Period.

Remember that, in all of the questions, we do first name only. I know who you are. But we feel that first name only will encourage people to ask questions and keep it a little bit anonymous as we move forward from here.

Let me start with my first question from Christopher. It's an emailed question:

"Ten-year yields reached 3.28% on March 17. Will we retest those levels? Will we retest the June 2003 all-time lows?"

First of all, the June 2003 all-time lows were 3.07% versus 3.28% on March 17. So they were only 20 basis points difference between the two. And as we speak, the 10-year is at .3896%, so call it 3.90%.

Yes, I think that there is a chance that we could retest those lows as we move forward. This is because, if this were a bear market rally in the credit crisis, and we start back down, then I think that, by the end of the year, we could start retesting some of the lows in the stock market and maybe even some of the wides in some of the credit markets as we move forward. And if that does happen, part and parcel, that will be a bit of a flight to quality returning to the market, pushing 10-year yields down. And I could definitely see us retesting the .328 low before the end of the year.

With that, let me jump to our first live question. Mark, are you there?

Mark: Hey, Jim, yes. How are you doing? My question deals with the TIPS market from the standpoint of, if there are so many investors that are inflation-adverse and then putting money into commodity funds, then why are we seeing TIPS perform just astronomically, seeing breakevens' inflation rate increasing and widening?

Bianco: That's a good question. We have written a couple of things about this. And the answer that we have given is that the TIPS market is being distorted by the flight to quality. Remember that the inflation breakeven rate is nominal yields minus the real yield of a TIP, to give you the inflation residual. But when you get

into a credit crisis like we are in right now, and everybody is flying in the Treasuries, and the Treasury Market has been plunging in yield – and I know that we don't have short-term TIPS, but I mean, at one point, in March, you may recall that three-month bills actually got below Japanese rates, incredibly. They were down around 60 basis points at one point because of a squeeze there, too. That reverberates throughout the entire Treasury yield curve. And that has been distorting at least the breakeven measure in TIPS.

So it has been very difficult to try to separate out in the TIPS market how much inflation that you have when you still have people hiding in Treasuries because they are afraid of the riskier assets because of the credit crisis. So it is being distorted, which is, I guess, the best answer that I can give you right now.

Bianco: OK, thank you. The next question is from Kevin. Kevin, are you there?

Kevin: Jim, I'm puzzled. The level of complacency in the marketplace right now, relative to where we are either in the credit crisis or in the home market/housing crisis – and you're looking at a VIX of 17 right now – I guess that you don't fight the (inaudible).

And, as an adjunct to that, clearly, it's in the government's and the Fed's best interests to prolong the pain as long as possible to try to heal the system. So…

Bianco: Let me make sure that I got that right. You think that it's in the Fed's best interest to prolong the pain?

Kevin: Well, yes, in other words, to spread the pain out over a long period of time as opposed to **having** a market correction that could…

Bianco: Oh, OK, as opposed to having an acute let-Bear Stearns -go-and-let-everybody -pick-up-the-pieces scenario. I understand. All right.

Kevin: How do you address that with the thought that we're going to retest the most?

Bianco: I think that, in part, the best answer that I could give you is that I have a feeling that, if I back up and say, "The Fed is doing what it can, not what it should because it can't force banks to raise capital beyond minimum capital requirements." I would argue that one of the things that this credit crisis may do when all is said and done is that it is going to end the Bernanke/Greenspan put.

The belief that the government can fix problems, and that we can, therefore, speculate recklessly forever, without concern, is what I think is going to be at call here. If we go back and retest those lows, then I think that the question should be, "Why can't the Fed fix the problems," not "Why won't the Fed fix the problems?" And the answer is, "Because some things are beyond their control." And this is one of them that is beyond their control.

And I would add that part of the problem that we have had, basically, I think, dating back to the stock market crash of 1987, was this moral hazard. It's interesting that we all like to talk about the moral hazard except when we have a crisis, and then that's not the time to talk about it. We need to forget about the moral hazard, then, and need to fix the problem immediately. So I think that what you have had is a hope rally that the problem will get fixed by the Federal Reserve. I have heard a number of people say to me, "I don't know how they are going to fix it. They just are. And I just don't want to be caught short because this problem will be fixed by them, and the market will keep going." So I don't think that they can fix the problem. I think that it's up to the marketplace to fix this problem. I think that it's up to the marketplace to let this problem heal itself.

Now, as far as spreading out the pain is concerned, yes, if they want to spread out the pain, then the other thing that they are going to do is that they are going to spread out the time. If you had let Bear Stearns go down, and if you had let the chaos that ensued with Bear Stearns, then you might have focused everybody's energy – you might have had a much worse market in the middle of March. You might have focused everybody's energies on really, truly fixing the problem, and it might have been over with at that point.

By bailing out Bear Stearns and pushing the problem off to another day, you stretch out the time that the problem is there, and you don't really focus the attitude of everybody to fix the problem. One example of that is to look at what has been coming in the market in the last few days. A lot of the banks are getting together with the market, and they want to market a new ABX index of higher-quality, triple A so that they can play the Kabuki Theater of "Let's Invent a New ABX Index That's Got a Higher Mark than The Old One, So That We Can Show That Our Losses Aren't So Bad," as if everybody is going to buy that is going to fix the problem. That's not fixing the problem. That's trying to push the problem off to another day. That's trying to find a stopgap measure during the crisis that we don't have to realize these losses because,

someday, it's going to end, and then these won't be a problem anymore. And that is why I don't think that we're really trying to fix the problem. We're just trying to say, "Let the Fed fix the problem," and then are hoping that it's gone away.

I know that I'm speaking in concepts, but that is the best that I can give you, unless you wanted to follow up and narrow me down a little bit more. Does that help?

Bianco: OK, thanks. Let me jump to the next question, which is from David. David, are you there?

David: Yes, I am. I have a question for you. When I read my estimates for the fourth quarter, it strikes me that the majority of analysts are still looking for dramatic increases year over year in the range of 30%, 40%, to 50% in earnings. And…

Bianco: Overall S&P earnings are what you're talking about?

David: Yes, I'm just saying that, in terms of forecasts for general analysts' earnings estimates. And yet, to your point, when I look, credit it contracting, the balance sheets are contracting, and overall margins seem to be contracting. There seems to be a disconnect, which seems to want to set up the market, particularly when we are trading at the top end of the trading ranges here for, maybe, some disappointment.

Bianco: Oh, I definitely think that has been the case. As far as analyst estimates go, you have to be somewhat careful with those because, in some cases, they are looking at these ex-financial numbers and removing a lot of these problems. In other cases, analysts have been throwing out numbers now. They have moved onto ex-financial estimates, knowing that the financial system is going to pile up tremendous earnings losses across the board for everybody and wipe out S&P earnings. Let's not pay attention to that. Let's look at S&P ex-financial. So I think that a lot of people have been trying to do that.

And, ultimately, at the end of the day, does the financial system matter? Because if it does, then losses to this degree should affect the economy. If they don't, then the financial system can lose $330 million, but everybody who doesn't work in finance can go along just fine, then why do we even have the financial system? If financial intermediation doesn't matter that much, then we shouldn't be making as much money at doing this as we do, and we shouldn't be spending as much effort on it as we do. So, ultimately, I do think that the market is setting itself up for a lot of disappointment as we move forward. So you're right in line with me.

Did you have a follow-up to that?

David: No, I guess that I'm looking back at that when stocks go down, bonds go up, flight to quality. So it has been very interesting in watching this ride as the spreads open up. But it strikes me to your other point, that the credit crisis isn't over, but the next crisis may prove to be a refocusing on a negative GDP in the third quarter.

Bianco: Right, I definitely think that could be the case. And what is interesting about that, as far as whether or not we are going to have a recession is concerned, is that Martin Feldstein is the head of the Recession Dating Committee. And even though the Intrade markets are putting the odds of a recession now at about 25 percent this year, boy, if you listen to Martin, he's almost willing to say to you that it's already started. He just hasn't gotten quite that set of data yet where he feels that he can proclaim that it's already underway.

So there are a number of people that still look at the economy as definitely being at the point where it could still tip lower, at least in the second quarter, which is where we are now, and could prove in the next few months to be very disappointing as we move forward.

David: Is the (audio gap) ability to have a consumer recession, as opposed to an industrial/business recession? (Inaudible)

Bianco: You know, I ultimately think that you can have a consumer recession because where is the consumer benefiting here? His house is not doing anything for him. Financing is very difficult for him. His brokerage account has done nothing for him. If you look at it longer-term over the last 10 years, his brokerage account hasn't done much for him. And the economy is slowing down. Job growth is negative. You've got all of the ingredients in place right now for a consumer-led slowdown that could even be a consumer-led recession as we move forward from here.

Really, what we got bailed out by was an inventory adjustment in the first quarter numbers that we didn't show that minus number. And everybody is hoping and thinking that that is going to be the Savior.

And you remind me about one other thing, too, that I will just throw out. I attended a Federal Reserve speech a few months ago here in

Chicago. The standard line was given about the Fed's forecast. "We will avoid a recession this year by being very, very close to recession in the first half of the year, and then the economy will rebound in the second half of the year."

Just for argument's sake, let's say that that's right, and we do avoid a recession, and the economy does rebound, and the Fed said near trend growth, that we have real GDP growth from three or four percent by the end of the year. We have a two-percent Funds Rate. What is the Fed going to do with the Funds Rate under that environment? The answer is that they have to raise it hard and fast. Are they going to? They threaten that they are going to, to try and make the inflation worrywarts worry. But I think that, at the end of the day, we're going to be at a two-percent Funds Rate at the end of the year if that were to happen. And if you think that the long-only commodity inflation boom is really going now, wait until you see what happens when we have three-percent growth and still are afraid to raise the Funds Rate off of two because it could still weaken the Banking System or cause the Stock Market to go down quite a bit. We could have a full-fledged riot in the commodity markets then.

So I do think that, at this point, it almost gets to the point where it might not be any good that we avoid a recession because then we've got to start correcting a lot of interest rates and a lot of assumptions in the marketplace that we have. And the Fed is going to be the one at the front of the list, that is going to have to say, "Good. If the Recession is done, then how fast can we get the Funds Rate back to four or five, something above the real growth rate?" And the answer is, "Don't touch that because, if you do, then you could weaken the banking system, and then we've got another whole set of problems, too."

Anyway, with that, let me jump to some of the emailed questions. Boy, do I have a lot of them right now. I've gotten over 20 of them right here. I can't quite get to all of them, but let me try to take some of those.

A lot of questions are coming in about this CIT Report. "How does the $15 billion of capitalization in the CIT compare with the value of physical commodities produced annually?"

"If speculators are driving the commodity markets, then why is it that the distillate heating crack spreads are so wide, and gasoline crack spreads are so narrow, especially given the long-only index funds hold more gasoline than heating, oil?"

There are questions about the gasoline pie charts. "Looking at your gasoline pie chart, in your opinion, what price per gallon is needed to actually see demand increase? Where is the elasticity of gasoline?"

Let me try to answer these questions in general. And there are a couple of others about commodities, too. First of all, on the gasoline side of the equation, I don't know the elasticity of gasoline, what is the level that we're going to have to reach. We are at $4 per gallon right now, and it is not slowing down whatsoever. So it suggests to me that the price of gasoline has to go a lot higher before we start to see some kind of a slowdown in speculation.

Now, the price of gasoline can go higher in one of two ways. It can either go higher in the United States – a lot higher in the United States – or a lot of these countries that are subsidizing it could remove their subsidies, and that can slow down the demand. Remember that the marginal demand for gasoline is not coming from the United States. That is why you will find the gasoline argument to be so interesting, because we have been talking quite a bit about, "What can Congress do," "What can the oil companies do," as if this is solely the United States' problem; it is not.

The marginal demand for gasoline is really coming from emerging markets. The biggest thing that they could do is that, if the Chinese were to remove their subsidies –Sinopec, China's State refinery, is losing $3 billion a quarter in subsidizing the price of gasoline for Chinese consumers, buying at $120 on the spot market, refining it, and selling it at below-market rates, and taking the loss. They, in removing their subsidies, could do more than maybe $5 or maybe $6 gasoline could do in the United States.

So the price of gasoline, I think, has to go a lot higher, but not necessarily in the U.S. Now, maybe it doesn't go higher in other places in the Country. Maybe it winds up going higher in terms of the United States, or it winds up going higher in terms of the emerging markets. But I'll say it this way -- the bottom line is that, back in 2000, when the price of crude oil jumped just over $30 a barrel, *The Economist* ran a story about how high the price of crude oil was, and how there was way too much speculation, at $30 a barrel in 2000. The price of gasoline shot up over $2 a gallon for the first time ever. And most state and local governments put a holiday on their taxes to try and help relieve consumers. It was the 2000 Election. They were gnashing their teeth that we had $2.10-a-gallon gasoline.

And I can remember that a lot of states and the Federal Government put a holiday on the gasoline taxes that we had, to try and reduce and ease the pain of consumers. Today, we're seeing exactly the same thing at $4 gasoline, and at $120 per barrel.

In other words, what I want to get at is that psychologists like to say that we forget 95 to 99 percent of all sensory input after 21 days. We have been breathlessly saying that the next $3 higher in crude oil, and the next 20 cents higher in gasoline was going to be it, and that was going to kill the consumer for eight years. We have not been saying that for three weeks. We have been saying it continuously for eight years. And you can find stories all the way back to $30 per barrel, where we have been saying, "The next $3 higher, and that's it. We're done. The economy is going to collapse." But now, we're at $126, and we're saying exactly the same thing, forgetting that we have been completely wrong in that argument for eight years.

So I don't necessarily think that we're at that inflection point. Or maybe, if we are, there is no way to know. From what we have seen, especially considering the chart on the last page, with gasoline demand at an all-time high, there is no evidence that we've even begun the process of trying to reverse that. So it looks like it is going to continue to go higher. And if you add into the idea that the long-only funds think that what they are doing is very virtuous, and that they are very virtuous in what they are trying to do, they are not going to slow down their activity because they don't see it as evil speculation.

Another question related to that is, "MasterCard said on Monday that gasoline demand was down week over week, seven percent from last year."

One credit card company looking at week-over-week numbers is interesting. But there are a lot of factors that you have to take into place when it comes to MasterCard: when it comes to weather patterns versus this week for last week, what were Visa's numbers over the same period, and what were cash purchases over the same period. So I think that the MasterCard number that says that there was one week, seven-percent year-over-year change is not very relevant at this point.

A question is coming in on the earlier topics -- "Can you translate a net capital shrink of $90 billion times 14.1 leverage, 1.3 into a GDP forecast?"

No, I can't. I can't if the answer is, "Can you put together an econometric formula that says that $90 billion net capital shrink times 14.1 means how many percentage points off of GDP would that be?" I don't think that can be done. But I can just at least say that it's a headwind on the economy. It cannot not be a headwind on the economy because it is raising the cost of capital for everybody across the board. Municipalities, mortgages, everything else – it's raising the cost of capital.

Interest rates -- credit-based interest rates are higher now than they would be if we didn't have that net capital shrink. That's got to be some kind of a headwind on the economy. That's probably the best that I can give you, at least in terms of that.

I'll take two more questions here, and then I'll wrap it up because we're getting at the top of the hour. I'll try to answer all of these other questions individually. And in the transcript that we put out on Monday -- we do publish a transcript on Monday – if there are any good questions in there, then I'll include them in Monday's transcript.

"If three-month LIBOR is 30 basis too low, then it is obvious which constituency are the losers. Who is receiving?"

I think that, if LIBOR is too low – if you want to use that argument that LIBOR is too low, then the winners are definitely going to be the borrowers, and the losers are definitely going to be the lenders. And in the case of this, we tend to think that the winners of LIBOR being too low is going to be the adjustable-rate mortgage owner because most of those are tied to some kind of a LIBOR Index, be it the six-month or the three-month, or the one-year. And the losers are going to be, I think, in some cases, the banks. And that might explain one of the reasons why intrabank lending practically doesn't exist, that you can call a bank and ask, "What is your rate," and then when you ask to borrow, there is no money available to borrow at that rate, which suggests, at least, that that might be the wrong rate for a number of people.

For the final questions, I will try to throw out an answer for you. "Why does inflation feel so bad, but U.S. stats say that it is not so bad?"

"Why are the BOE and the ECB so focused on inflation when the Fed is not? Is the Fed ignoring a deeper danger?"

As far as the ECB is concerned, the ECB has a single mandate. Their single mandate is to fight inflation. The Fed has a dual mandate, which is

to promote growth and fight inflation. So the ECB can only look at the inflation equation. And they have looked at the inflation equation and decided that they have to hold the line on interest rates because of the fear of inflation. Because of the Fed's dual mandate – and the dual mandate is to promote as high of growth as possible and as little inflation as possible – is a nice way of saying that the Fed can do whatever it wants, and that it could justify it under that mandate.

The Fed has taken a completely different tact. I might add that, even though the Fed has cut interest rates over 300 basis points while the ECB has not, the relative performance of the markets between the two over the bigger picture has not been that much different, suggesting that, at least in some respects, the interest rate cuts have not been as effective as everybody makes them out to be.

Actually, what has been more effective, though not completely effective, has been the liquidity that people have been sticking into the market, that that has been more helpful from everybody. So I think that, when you look at these numbers, what you will find is that the Fed needs to worry about getting loans available rather than what the rate is. And lowering the rate or raising the rate in this environment hasn't been nearly as useful as trying to persuade the banks to raise capital and maybe providing some liquidity. The Fed is doing what it can. It does help a little bit on the margins. But changing interest rates when you can't get loans or can get loans, really, has not been as effective at all.

OK, I will try to answer some of these other questions. Again, I will include them in the transcript if there are some questions of interest. They are still streaming in. Go ahead and continue sending them, and I will do the best that I can.

Thank you, everybody, for attending the Conference Call. We will talk to you next month. Bye-bye!

END

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