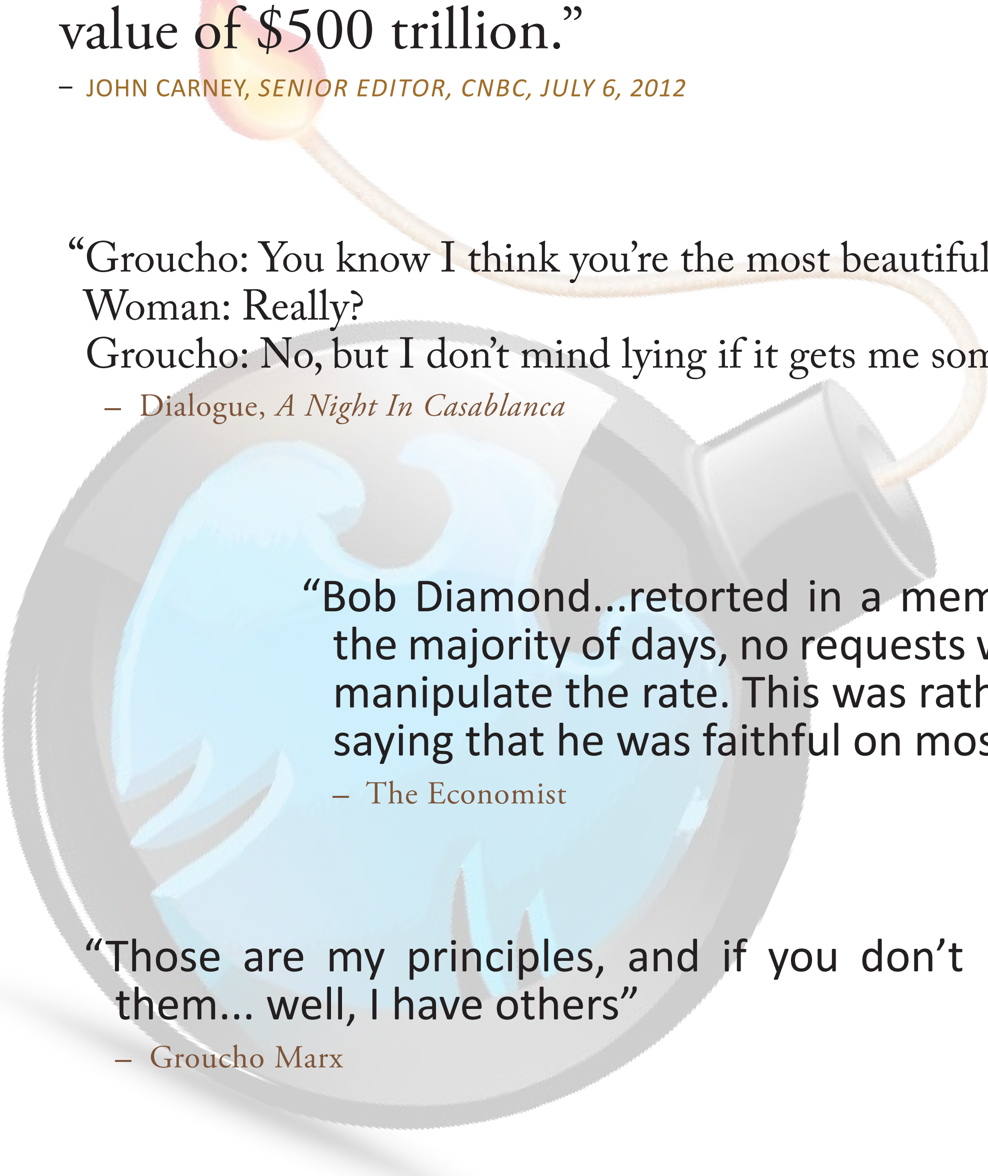
THINGS THAT MAKE YOU GO

Hmmm...

A walk around the fringes of finance



"Libor may be the most important number in the world. It is certainly the word's most important interest-rate bench mark. Regulators estimate that Libor is tied to transactions with a notional value of $500 trillion."

– JOHN CARNEY, *SENIOR EDITOR, CNBC, JULY 6, 2012*

"Groucho: You know I think you're the most beautiful woman in the world?
Woman: Really?
Groucho: No, but I don't mind lying if it gets me somewhere"

– Dialogue, *A Night In Casablanca*

"Bob Diamond...retorted in a memo to staff that "on the majority of days, no requests were made at all" to manipulate the rate. This was rather like an adulterer saying that he was faithful on most days."

– The Economist

"Those are my principles, and if you don't like them... well, I have others"

– Groucho Marx

They say it's always darkest before the dawn but in the financial world we seem to repeatedly go beyond 'dark' into pitch blackness when the periodic stumbles that are part and parcel of an ever-growing world come along.

Inevitably, when these meltdowns take place they are assigned the rather unimaginative adjective 'Black' in order to convey just how gloomy they are. Indeed, in a world such as finance, that thrives and grows in large part to hyperbole, one would think that perhaps a more evocative description could be used, but no. 'Black' it is.

In fact, one can live through a very 'Black Week' indeed just by examining the pages of history, and reliving the various episodes that have befallen the world in just the last century alone.

Such a week would begin, of course, with 'Black Monday'.

There are many still involved in the financial industry who remember vividly the events of that day when, on October 19 1987, the stock markets of the world crashed as a toxic combination of overvaluation, conflict amongst G-7 nations, problems in bond markets and the failure of portfolio insurance overwhelmed the world's bourses and led to a stunning (though ultimately short-lived) collapse in markets across the globe.

'Black Tuesday' occurred on October 29, 1929 when some 16 million shares traded on the New York Stock Exchange (a record that would stand for 40 years) as panic gripped the world. The Dow lost 12% in a day which only added to the previous day's 13% fall (a day which, funnily enough, had been called, you guessed it, 'Black Monday'). In fact, this 'Black Two-Day' saw the Dow Jones Industrial Average plummet from 298.97 to 230.07—a fall of some 23%. The following day, when the Dow bounced 12% remains sadly bereft of a snappy monicker but such is the nature of these things.

'Black Wednesday' took place on 16 September 1992 when the UK's Conservative government was forced to withdraw the Pound Sterling from the European Exchange Rate Mechanism (ERM) after their promise to keep the currency above its agreed-upon lower limit was broken—an event that famously bagged George Soros a $1bln profit—a colossal amount of money in 1992 or, as it's known today, $43 million less than the box office takings of Pirates of The Caribbean: On Stranger Tides.

'Black Thursday'? Well for that we need to return to the Wall Street Crash of 1929, specifically Thursday October 24th when, seemingly without warning (except for those issued by a few Cassandras who went unheeded) and despite the intervention of some very serious names from the financial world, panic could not be averted:

> *(Wikipedia): On October 24 ("Black Thursday"), the market lost 11% of its value at the opening bell on very heavy trading. Several leading Wall Street bankers met to find a solution to the panic and chaos on the trading floor. The meeting included Thomas W. Lamont, acting head of Morgan Bank; Albert Wiggin, head of the Chase National Bank; and Charles E. Mitchell, president of the National City Bank of New York. They chose Richard Whitney, vice president of the Exchange, to act on their behalf.*
>
> *With the bankers' financial resources behind him, Whitney placed a bid to purchase a large block of shares in U.S. Steel at a price well above the current market. As traders watched, Whitney then placed similar bids on other "blue chip" stocks. This tactic was similar to one that ended the Panic of 1907. It succeeded in halting the slide. The Dow Jones Industrial Average recovered, closing with it down only 6.38 points for the day; however, unlike 1907, the respite was only temporary.*

And so we come to 'Black Friday'.

Now, one could reasonably expect Fridays to have the potential to be the Blackest of all days in financial circles, what with traders desperate to square away positions ahead of an uncertain weekend, but, whilst the previous four days of our Black Week all involve stock markets—gripped by fear—falling precipitously, our 'Black Friday' took place on September 24, 1869 and the resultant market dislocation was due to something altogether different. Something that is uppermost in the collective psyche right now; market manipulation.

> *Incidentally, as we wend our way through the dog days of July, into August and towards September and October, it's worth bearing in mind that our 'Black Week' is constituted of two days in September and three in October. I'm just saying...*

But back to 'Black Friday'.

Unlike the other 'Black Days', this one had nothing to do with stock markets, but was, in fact, the result of an attempt by two leading financiers of the day - Jay Gould and James Fisk - to corner the gold market.

After the US Civil War, in March, 1869, Ulysses S. Grant assumed the presidency of a United States in complete disarray and with an economy on the brink of implosion. Federal debt was out of control after the conflict and hundreds of millions of dollars of 'greenbacks' had forced gold coins out of circulation. The credit rating of the country was akin to that of today's PIIGS.

Grant's very first act as President was to sign a law which promised that payment of US bonds would be made in 'gold or its equivalent' and that redemption of 'greenbacks' would be made as soon as was practicable.

The signing of this law sent the price of gold tumbling to $130 an ounce - a low not seen since Congress suspended payments in gold and silver in 1862.

Grant's Treasury Secretary, George Boutwell, rather ingeniously began selling the Treasury's surplus gold to retire 'greenbacks' and then used those very same 'greenbacks' to buy back government bonds. The strategy worked like a charm. The gold price remained low, the money supply stayed even and the National Debt was reduced (yes, folks, it is NOT a one-way ride) to $50 million - or, as we like to call it today, 25% of the payroll of the New York Yankees.

At the time, the gold market was tiny in size; $15 million in turnover, and this made it simple for the government to (in those days, *overtly*) set the price simply by selling varying amounts of gold. Gould and Fisk realized that by getting their hands on inside information as to the governments plans for gold sales, they could trade ahead of the government and make a ridiculous sum of money. Easy.

The NY Times takes up the story:

> *(NY Times): Gould convinced a brother-in-law of President Grant, Abel Corbin, to join him and Fisk in their gold-market investments. It is not certain, however, whether Corbin actually knew the real plot or was just a pawn in the high-finance game. Gould then approached the assistant treasurer in New York, Daniel Butterfield, who was in charge of gold sales. The financier gave Butterfield $10,000 (his annual salary was $8000), which the federal agent later claimed was a no-interest loan. Furthermore, Gould offered twice to invest $500,000 in gold for Grant's personal secretary, Horace Porter, who refused. Finally, Gould brazenly offered to give Grant's wife, Julia, half-interest in $250,000 worth of bonds, but she, too, declined.*
>
> *When Grant visited New York on several occasions, Corbin arranged for Gould and Fisk to be present, and the conspirators tried to persuade the president that a higher gold price (from reduced Treasury sales) would benefit the nation. As he usually did, Grant listened without comment. When Gould pointedly asked for a hint at the government's actions, the president resolutely refused. However, the financiers' visible access to Grant and*

> *those close to him enhanced the influence of Gould and Fisk in financial circles. They began buying millions of dollars worth of gold in early September 1869, initiating a rise in the market.*

So this insider trading scheme was actually a pretty poor attempt when push came to shove as the conspirators failed to actually gain any real inside information. But that didn't deter them from pressing on, undoubtedly in the assumption that, financial types being what they were, it would be assumed that, simply by the level of their association with the White House, that they HAD inside information and were using it.

There's none so blind as those that won't see.

But back to our story, and in the midst of the denouement, we see just how important correct spelling and punctuation really are:

> *(NY Times): After conferring with leading bankers in New York, Treasury Secretary Boutwell realized what the speculators were up to, and that the federal government should increase its gold sales to stabilize the market, or risk devaluing greenbacks, government bonds, and American credit. Boutwell refused to see Corbin, who then alerted Gould that something was afoot and wrote a lengthy letter to Grant urgently requesting the president to stop his treasury secretary. Grant did not reply, but the telegram to Gould stating, "Letter delivered all right," was mistranslated at the New York telegraph office as "Letter delivered. All right." Gould intensified his gold buying spree, and the price continued climbing.*

"... the telegram to Gould stating, "Letter delivered all right," was mistranslated at the New York telegraph office as "Letter delivered. All right."

> *However, the suspicious letter and Porter's admission of Gould's bribery attempt made Grant realize that he had been used as cover for the financiers to corner the gold market. The president warned Corbin to cut his ties with Gould, and allowed Boutwell to proceed with his plans to increase the government's gold sales. Corbin, though, tipped off Gould, who began selling his gold without informing Fisk. The two-week frenzy on the gold market had virtually halted the country's foreign trade, which relied on gold as the medium of exchange, and threatened to broaden into an economic panic.*

> *On Friday, September 24, 1869, the price of gold reached between $160 and $162, and Fisk, still buying, boasted that he would push it to $200. After a brief discussion with the president, Boutwell sent a telegram to Butterfield directing him to sell $4,000,000 in gold and buy the same amount in bonds. When the news reached the Gold Room, the price of the precious metal fell to $133 within a few minutes.*

And with that, 'Black Friday' was born.

Attempts to manipulate

free markets invariably end badly - after all, they are, supposedly, by their very nature, free.

From the Tulip Mania of the 1600s, to the Eerie War of the 1860s through the soybean market in 1977-78, the Hunt Brothers' ill-fated attempt to corner the silver market in 1979-80 and further attempted corners in the tin market (1981-82 and 1984-85) as well as Enron's interference with energy pricing in 1985 and various attempts to manipulate the Treasury markets, all these episodes ended badly for those perpetrating them and the battle cry of those exposing them has always been "There *ARE* no conspiracies because you can't hide manipulation".

The very fact that these episodes were brought to light is always one of the main reasons that most people inherently disbelieve in conspiracy theories, after-all, how can a manipulation of any size or scale evade the harsh light of truth?

Well, of course, they ALL do—the only vagary is the length of TIME they remain in darkness.

Over the past few weeks, the exposure of the Libor-rigging scandal has monopolized the headlines of the financial press and inveigled its way onto the front pages of every major news publication in the world through the sheer size and scale of the story.

Something as big as this just *CAN'T* be hidden from the public.

Only.....it can.

It has been. It no doubt still is to a certain extent.

I'm not going to go through all of the events of the past few weeks as you are no doubt familiar with them, but let's take a look at how Libor works:

> *(CNBC): Libor is actually not just one interest rate. It is the name for rates calculated in 15 currencies for loans of 10 different maturities, ranging from overnight to 12-months.*
>
> *The setting of Libor begins each morning between 11:00am and 11:10am (London time) when someone in one of the designated Libor panel banks enters a number into a piece of Thomson Reuters software that asks the question: "At what rate could you borrow funds, were you to do so by asking for and then accepting inter-bank offers in a reasonable market size just prior to 11am?"*
>
> *Over at a Thomson Reuters office somewhere in London—the exact location is a closely guarded secret—clerks look over the submissions for possible error. The clerks will call a bank to confirm a number that seems off for some reason. A number that greatly varies from the submission of the prior day might trigger a back-check. A number highly divergent from the submissions of other banks can also trigger a double check. Obvious typos are surprisingly frequent. The clerks are careful, however, not to reveal any other banks' submissions prior to the official publication.*
>
> *What the clerks do not do is challenge a number confirmed by the bank.*
>
> *"Our goal in the checking is to make sure we use the number the bank intended to submit," a person familiar with the matter said.*
>
> *The numbers are then entered into a "calculation engine" that ranks them in descending order and trims off the highest and lowest 25 percent of submissions. The middle 50 percent are then averaged, producing a figure that is published as that day's Libor at 11:30am. In addition, Thomson Reuters publishes the separate submission of each panel bank.*
>
> *This methodology is set by Foreign Exchange and Money Markets Committee of the British Bankers' Association, which also determines make-up of the Libor panel—the group of banks whose rates are used in the calculation—for each of the 10 currencies. The banks are supposed to be the biggest, best and most reliable in the world, selected according to their credit rating, their scale and their expertise in the relevant.*

"... What the clerks do *not* do is challenge a number confirmed by the bank"

I'm afraid it's rather obvious. Given that almost half the reported inputs that help establish the Libor rate are discarded immediately, Barclays simply *CANNOT* have manipulated the Libor rate alone. Period.

What's more, to effectively *ensure* the rate is set at the price required, you'd need to not only establish the highest and lowest 25% of prices, but then ensure the remaining 50% average out to the required rate and, based on the fact that there are 16 banks that submit rates, that would mean about 13 of the 16 involved would need to be complicit.

As a very good friend of mine put it earlier this week; at best this is a cartel, at worst it's outright fraud on a scale that is completely unprecedented. But which is it?

> *(UK Guardian): Criminal charges could be brought against traders implicated in the interest rate rigging scandal after the Serious Fraud Office announced on Friday that it had*

begun a formal investigation into attempts to fix Libor.

The director of the SFO David Green said he had "decided to formally accept the Libor matter for investigation" after reviewing the information provided by regulators which last week fined Barclays £290m for attempting to manipulate the price of the key interest rate known as Libor - the London interbank offered rate.

The investigation is understood to be into the wider market and not just Barclays.

The decision to embark on a formal investigation appears to been taken quickly as on Monday the SFO had said it was considering "whether it is both appropriate and possible to bring criminal prosecutions".

"... The FSA has identified price-rigging dating back to 2005, yet some current and former traders say that problems go back much further than that."

"The issues are complex and the assessment of the evidence the FSA has gathered will take a short time, but we hope to come to a conclusion within a month," the SFO had said on Monday.

OK... I guess that answers that question.

But this fraud/manipulation couldn't have been hidden from the world because it was just too big, surely?

Let's go back to September 2007 and an article that appeared in the FT, written by Gillian Tett and titled 'Libor's Value Is Called Into Question' (courtesy of Jim Bianco and Barry Ritholtz):

(FT): ...the recent turmoil is prompting suggestions that Libor is no longer offering such an accurate benchmark of borrowing costs as before.

As a result, some bankers are beginning to suggest that the status of these indices may need to be reconsidered in the future.

"The Libor rates are a bit of a fiction. The number on the screen doesn't always match what we see now," complains the treasurer of one of the largest City banks.

Such criticism is, unsurprisingly, rebuffed by those who compile the index each day. However, it highlights two other trends that have emerged in the money markets in recent weeks.

One of these is a growing divergence in the rates that different banks have been quoting to borrow and lend money between themselves.

For although the banks used to move in a pack, quoting rates that were almost identical, this pattern broke down a couple of months ago – and by the middle of this month the gap between these quotes had sometimes risen to almost 10 basis points for three month sterling funds.

Moreover, this pattern is not confined to the dollar market alone: in the yen, euro and sterling markets a similar dispersion has emerged. However, the second, more pernicious trend is that as banks have hoarded liquidity this summer, some have been refusing to conduct trades at all at the official, "posted" rates, even when these rates have been displayed on Reuters.

"The screen will say one thing but people are actually quoting a different level, if they are quoting at all," says one senior banker.

So for five years there have been attempts to fix the Libor rate and, take it from me, during that time, many inside the financial industry were familiar with the rumours of such manipulation but it was another huge scandal with such high-powered connected interests that it would no doubt be brushed squarely under the carpet.

Forget 'too big to fail'. This was 'too deep to prove'.

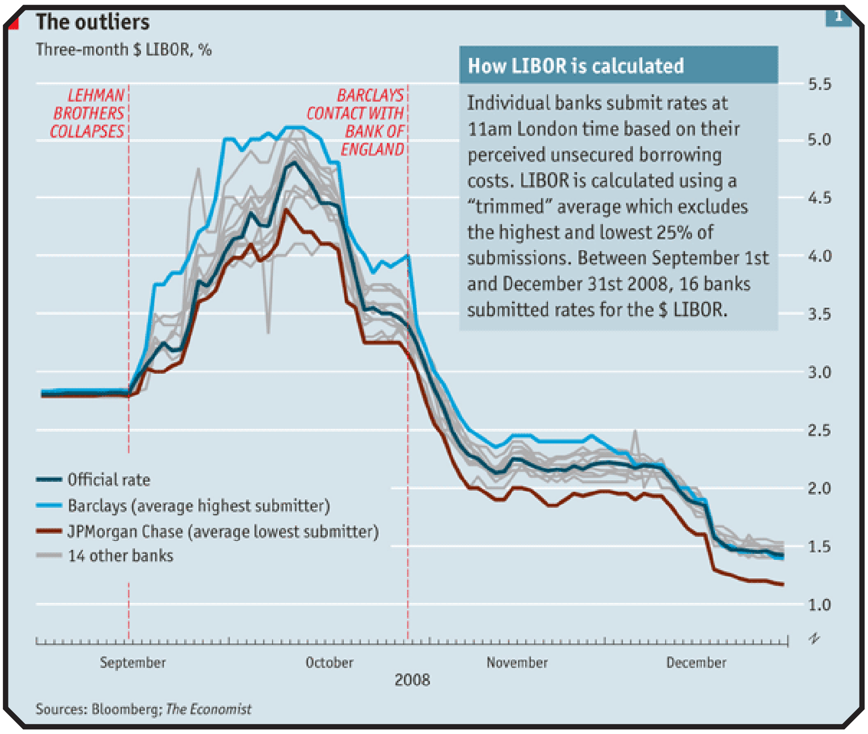
But what if the deception has been going on far longer than five years?

(Economist): The FSA has identified price-rigging dating back to 2005, yet some current and former traders say that problems go back much further than that. "Fifteen years ago the word was that LIBOR was being rigged," says one industry veteran closely involved in the LIBOR process. "It was one of those well kept secrets, but the regulator was asleep, the Bank of England didn't care and... [the banks participating were] happy with the reference prices." Says another: "Going back to the late 1980s, when I was a trader, you saw some pretty odd fixings...With traders, if you don't actually nail it down, they'll steal it."

Damning indeed.

Libor is so important to so many people in the financial industry that the question of why it was manipulated really ought to be framed differently:

> *Assuming you COULD manipulate something as important and potentially beneficial as the Libor rate with such ease for years, why* **wouldn't** *you?*



SOURCE: BLOOMBERG/ECONOMIST

The answer to this question would ordinarily be:

> *"Because it's illegal and government regulators would throw the book at us"*

But—and here's the crux of the whole thing—in this particular case it would appear that the UK Labour government which was in power at the time serious doubts first came to be raised had, shall we say, vested interests of their own in keeping Libor down (a point Bob Diamond was only too happy to make during his recent testimony to the Treasury Select Committee):

> *(UK Daily Telegraph): During almost three hours of cross-examination by MPs, Bob Diamond claimed there had been a series of private conversations with senior Government figures, thought to include Baroness Vadera, during the autumn of 2008.*
>
> *Mr Diamond claimed that the Government and regulators were repeatedly warned by Barclays that banks were improperly fixing the Libor rate, which is used to set borrowing costs for millions of consumers, businesses and investors... Mr Diamond suggested that other banks were more culpable in the growing rate-fixing scandal – which also implicated the Treasury, Bank of England and Financial Services Authority (FSA), the City regulator.*

The missing piece for *ANY* successful manipulation is the acquiescence of those charged with preventing such a manipulation from taking place in the first place. The first line of defence is the regulators but behind them stand the government and it is in government that the *real* power to manipulate lies.

Barclays' attempts to influence Libor were, it would appear, two-fold. At ground level it was the tired old cliche of derivatives traders trying to manipulate the rate in order to increase their profits (or reduce their losses) but more troubling is the second suggested reason:

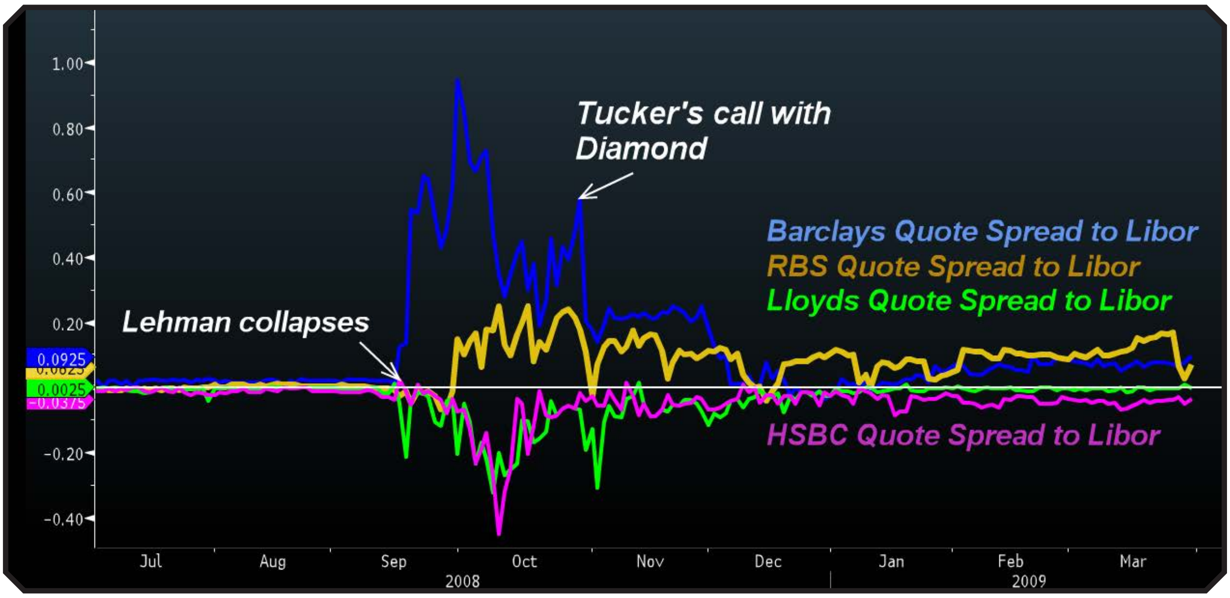
(Economist): Barclays and, apparently, many other banks submitted dishonestly low estimates of bank borrowing costs over at least two years, including during the depths of the financial crisis. In terms of the scale of manipulation, this appears to have been far more egregious—at least in terms of the numbers. Almost all the banks in the LIBOR panels were submitting rates that may have been 30-40 basis points too low on average. That could create the biggest liabilities for the banks involved (although there is also a twist in this part of the story involving the regulators).

As the financial crisis began in the middle of 2007, credit markets for banks started to freeze up. Banks began to suffer losses on their holdings of toxic securities relating to American subprime mortgages. With unexploded bombs littering the banking system, banks were reluctant to lend to one another, leading to shortages of funding system-wide...In these febrile market conditions, with almost no interbank lending taking place, there were little real data to use as a basis when submitting LIBOR. Barclays maintains that it tried to post honest assessments in its LIBOR submissions, but found that it was constantly above the submissions of rival banks, including some that were unmistakably weaker.

At the time, questions were asked about the financial health of Barclays because its LIBOR submissions were higher. Back then, Barclays insiders said they were posting numbers that were honest while others were fiddling theirs, citing examples of banks that were trying to get funding in money markets at rates that were 30 basis points higher than those they were submitting for LIBOR.

This version of events has turned out to be only partly true. In its settlement with regulators, Barclays owned up to massaging down its own LIBOR submissions so that they were more or less in line with those of their rivals. It instructed its money-markets team to submit numbers that were high enough to be in the top four, and thus discarded from the calculation, but not so high as to draw attention to the bank. "I would sort of express us maybe as not clean, but clean in principle," one Barclays manager apparently said in a call to the FSA at the time.

As the fallout gathered pace, Barclays swiftly produced a memo which detailed a conversation between Mr. Diamond and Paul Tucker, the deputy governor of the Bank of England.



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SOURCE: BLOOMBERG/ECONOMIST

The document suggested that the Bank had encouraged Barclays to cut the key Libor rate during the credit crisis

Unsurprisingly, the effect of Tucker's call was immediate (chart, previous page).

> *(UK Daily Telegraph): ...when Tucker made a telephone call on Wednesday, October 29, 2008, to Barclays' then investment banking head, Bob Diamond, he would have known for nearly a year that Libor rate-setting could have been compromised.*
>
> *As Diamond's publicly-released note of the call records, he asked Tucker to relay to the then Labour government much the same warning that the man who is now deputy governor of the Bank of England had received nearly 12 months earlier. The message was simple: "Not all banks were providing quotes at the levels that represented real transactions."*

"... when Tucker made a telephone call on Wednesday, October 29, 2008 to...Bob Diamond, he would have known for nearly a year that Libor rate-setting could have been compromised."

> *The response of Tucker to this request is recorded in the note as "Oh, that would be worse." Diamond then went on to say in the contemporaneous "file note" of the conversation that Tucker talked of ill-defined figures in "Whitehall", desperate it seems for lower Libor rates which would in turn ease credit conditions for businesses, asking why Barclays' Libor submissions appeared unusually high. The note said: "Mr Tucker stated that the levels of calls he was receiving from Whitehall were 'senior' and that while he was certain we did not need advice, that it did not always need to be the case that we appeared as high as we have recently."*
>
> *Giving evidence to the Treasury Select Committee last week, Diamond denied that he had taken this to be a Bank instruction to "low-ball" Barclays' Libor submissions. Andrew Tyrie, the committee's chairman, remarked drily: "It reads that way to anyone that looks at it."*

So, working from the ground up; we have a set of traders looking to produce the best profits they can for personal gain, the major bank they work for and who should be supervising them with a need to disguise the level of its own funding costs and above them all, a government seeking to keep borrowing costs down in the middle of a gigantic financial storm.

From such alignments of interest are the greatest of conspiracies born.

In my humble opinion, the Libor scandal (which has a LONG way to go before it has played out and which will claim a LOT more scalps) will mark a fundamental change in the treatment of financial conspiracy theories in the media. The sheer amount of coverage it will undoubtedly receive will signal a shift in attitude towards the exposing of such scandals rather than the blind-eyes that have been regularly turned in recent years.

It could well signal the return of the Woodward & Bernstein school of journalism that has been so notably absent in our celebrity-obsessed culture (believe me, when Libor can knock TomKat's divorce off the front pages—even for a day or two—good things are beginning to happen) and it will encourage whistle-blowers to come forward.

But perhaps, most-of-all, watching how quickly those in high places begin to throw each other under the bus, it will hasten the end of many other possible government conspiracies as exposing such events becomes an exercise in self-preservation.

Prime amongst conspiracy theories that may soon be finally proven to be either valid or the figments of overactive imaginations, are those alleged in the gold and silver markets.

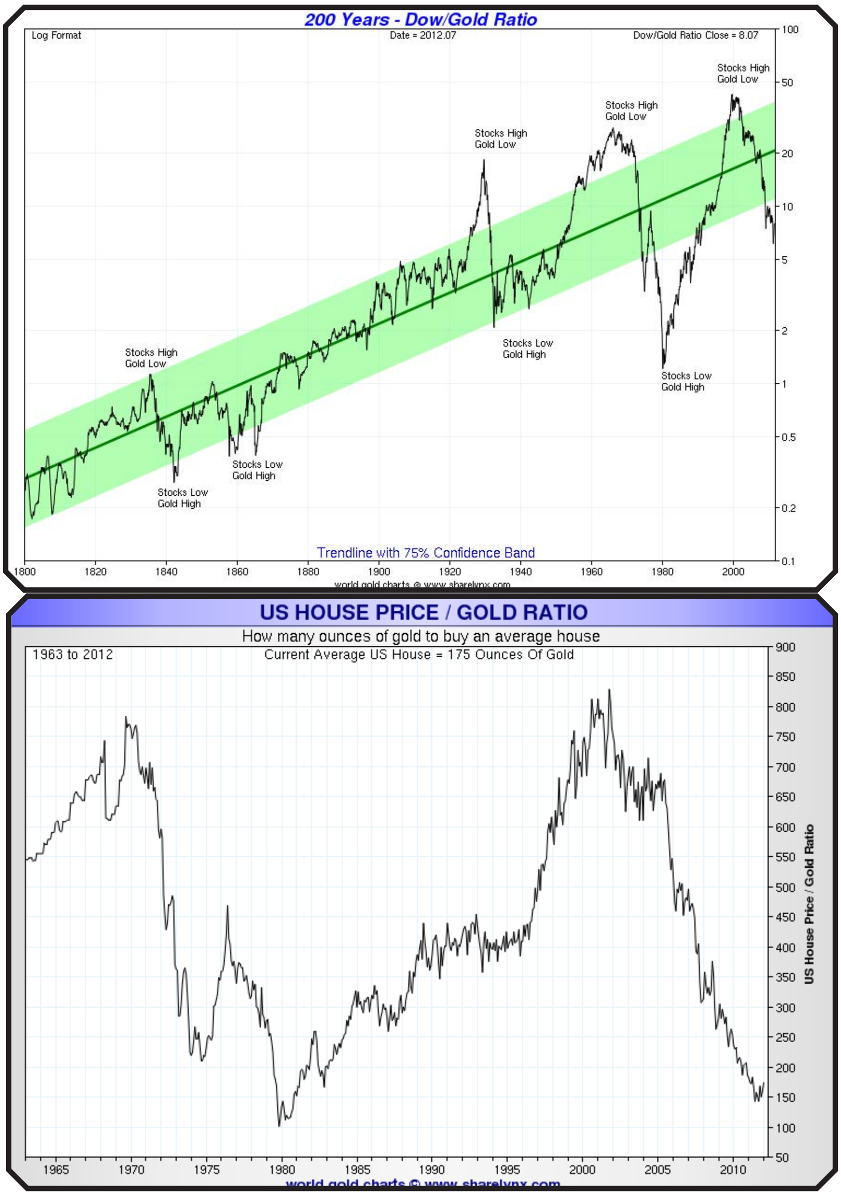
The allegations concerning precious metal price manipulation predate those surrounding Libor by decades but until now day they have remained similarly acknowledged within financial circles and ignored without. That may well be about to change.

Unencumbered by liability, the rising price of gold has always been a barometer of governmental failure to protect the purchasing power of fiat currency and the best indication of the damage that inflation does.

Forget inexorably rising gold prices. Forget the corrections that shake loose hands from the wheel at every turn. In the broader context they carry far less relevance than the intrinsic values that gold provides a consistent yardstick to.

A look at the value of assets measured in ounces of gold remains the most consistent way to get a sense of their real value and the charts below demonstrate all too clearly the *true* performance of the Dow Jones Industrial Average and average US house prices over the long term when measured in gold ounces.

On March 29, 2008, the Wall Street Journal published an article entitled ‘Libor May Have Been Affected By Low-Balling Dollar Calculation’:



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SOURCE: SHARELYNX

(Marketwatch): Banking giants including Citigroup Inc., J.P. Morgan Chase & Co. and UBS AG are contributing to erratic behavior in a major global lending benchmark, The Wall Street Journal reported Thursday.

Citi, J.P. Morgan and UBS are all members of a 16-bank panel that reports rates used to calculate the London interbank offered rate, or Libor, in dollars. An analysis of those 16 banks by the Journal suggests they may have been reporting much lower borrowing costs than they should have been, judging by another market measure.

No mention of Barclays and yet, almost five years later, that story is now exploding into mainstream consciousness.

If the long-stated claims about government-sanctioned, bank-led manipulation of precious metals markets put forward so eloquently by the likes of Ted Butler, Bill Murphy & Chris Powell at GATA as well as Messrs. Sprott, Sinclair, Davies et al are eventually proven to have any validity whatsoever, the fallout from the Libor scandal will prove to be (to use the words of Jamie Dimon) just another “tempest in a tea pot” as the precious metals are the very underpinnings of the entire global financial system. Conspiracy or no, it would be a blessed relief to get closure no matter what the truth turns out to be.

The manipulation of the gold market by Gould and Fisk back in 1869 ultimately failed in short order because it lacked the vital ingredient in keeping such things going—official support—but the damage caused to markets, once it was exposed, was significant:

> *(NY Times): The economic fallout caused stock prices to fall 20%, export agricultural products (mainly grain crops) to plummet over 50%, several brokerages to go bankrupt, and severe disruption in the national economy for months.*

In today's Things That Make You Go Hmmm..... Gordon Brown's sale of UK gold reserves once again comes under scrutiny and, in light of the Libor revelations, the circumstances surrounding that sale look eerily familiar:

"... While the market manipulation which occurred when the gold reserves were sold was not illegal as the abuse at Barclays may have been, the moral atmosphere in which it took place was identical."

> *(UK Daily Telegraph): Faced with the prospect of a global collapse in the banking system, the Chancellor took the decision to bail out the banks by dumping Britain's gold, forcing the price down and allowing the banks to buy back gold at a profit, thus meeting their borrowing obligations.*
>
> *..."[Brown] was facing a problem that was a world scale problem where a number of financial institutions had become voluntarily short of gold to the extent that it was threatening the stability of the financial system and it was obvious that something had to be done."*
>
> *While the market manipulation which occurred when the gold reserves were sold was not illegal as the abuse at Barclays may have been, the moral atmosphere in which it took place was identical.*
>
> *The crash which began in 2007 and endures still was the result of an abdication of responsibility across the financial sector. This abdication ranged from the consumer whose thirst for goods pushed him beyond into grave debt to a government whose lust for popularity encouraged it to do the same.*
>
> *Responsibility is evaded by all bar those on whose shoulders it ought to rest. The gold panic of 1999 was expensively paid for by the British public. The one thing politicians ought to have bought with that money was a lesson in the structural restraints which needed to be placed on banks now that the principle that they were ultimately public liabilities had been established.*
>
> *It was a lesson which could have acted to restrain all players in the credit market boom of the 2000s. It was a lesson which nobody learnt.*

Watch carefully how the Libor scandal plays out and pay particular attention to how swiftly those accused at every level roll over and point the finger at those above them, after all, as we discussed earlier:

> *Assuming you* **COULD** *manipulate something as important and potentially beneficial as the ~~Libor rate~~ gold price with such ease for years, why* **wouldn't** *you?*

I get a sense that important precedents are about to be set; precedents that will have profound and far-reaching consequences.

As for our good friends Gould & Fisk, things eventually worked out just fine.

They were acquitted on all charges thanks to "...a combination of expert legal counsel, led by David Dudley Field, and Tammany Hall judges".

Funny how things turn out sometimes.

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That's all from me for another week. I'll leave you to delve into the pages of Things That Make You Go Hmmm..... under your own steam.

Until next time...

Contents

09 July 2012

The Gonnie, Gonnie Banks

#	Bank	Assets ($m)	Deposits ($m)	Cost ($m)
32	Montgomery Bank & Trust, Ailey, GA	173.6	164.4	75.2
	Total Cost to FDIC Deposit Insurance Fund			**75.2**

Melbourne has the largest and fastest-growing stock of available housing in Australia, which is likely to put further pressure on house prices in the city.

In June, Melbourne's residential listings grew at a monthly rate of 6.1 per cent - almost four times the national average - and recorded a yearly jump of 27.7 per cent, more than 27 times Sydney's annual growth of 1 per cent.

Melbourne now has 55,293 unsold homes and apartments, according to today's report, published by independent property researcher, SQM Research.

SQM Research managing director Louis Christopher said the Melbourne result was a record, surpassing the flood of homes and apartments put up for sale in 2008 during the global financial crisis.

> "...I fail to see how the other data providers can record rising dwelling prices in Melbourne when there is this much stock on the market,"

''I fail to see how the other data providers can record rising dwelling prices in Melbourne when there is this much stock on the market,'' Mr Christopher said.

In June, home prices rose 1 per cent in Melbourne for the month, according to figures by RP Data. However, Melbourne's house prices were still down 6.6 per cent from a year ago.

Melbourne's ''over-supply'' of unsold homes and apartments can be explained, Mr Christopher believes, by a combination of prolonged weakened demand for housing and a glut of new developments that have been added to the housing pool.

Mr Christopher said he expected Melbourne's residential prices to continue falling.

Aspiring home owners will welcome the news, which comes 18 months after Melbourne scored near the bottom of an international ranking of housing affordability.

Last January, the Demographia International Housing Affordability Survey, which ranked 325 markets by affordability, described Melbourne as ''severely unaffordable'' and listed it as the world's 321st most affordable city.

The city had a rental vacancy rate of 3.1 per cent in May, the highest among capital cities and an increase from 2.4 per cent a year earlier, SQM said in a release last month.

Permits granted to build or renovate homes soared 27.3 per cent in May from the prior month after the central bank cut interest rates, a report this week showed.

The number of homes approved in Victoria climbed 31.8 per cent from April, the biggest increase among all states, Australian Bureau of Statistics figures showed.

THE AGE / **LINK**

Spanish and Italian borrowing costs soared back into the danger zone as traders bet that the policy action by central banks was inadequate defence against the continued political and financial chaos in the eurozone.

The yield on Spain's benchmark 10-year bond rose above the 7pc bail-out level amid fears that opposition in Germany and Finland could crush the rescue plans agreed in Brussels last week.

The Finnish finance minister, Jutta Urpilainen, said her country was not prepared to keep the euro "at any cost." She said the euro was "use for Finland", one of the eurozone's last remaining AAA-rated countries, but added: "Collective responsibility for other countries' debt, economics and risks; this is not what we should be prepared for. We are constructive and want to solve the crisis, but not on any terms."

European stockmarkets fell sharply, the euro dropped to its lowest level for three and a half years against the pound, and the yield on Italian 10-year bonds rose to 6.25pc, despite the move by the European Central Bank, the Bank of England, and the Bank of China to pump liquidity into their economies.

On Friday a frustrated Joerg Asmussen, an ECB board member, said too much was being expected of the Bank. "We must explain what the limits of our powers and mandate are," he said in a speech. "The ECB cannot compensate for what others - notably political authorities - fail to do." He added: "There is no substitute for good policies."

In Brussels there were promises of more solutions at the Eurogroup meeting on Monday. One official told reporters that the 17 finance ministers intended to reach a "political decision" on how to support Spain.

> **"...It was a European problem... "I believe we should have shared that loss fairly on a level playing field,"**

In Cyprus, the finance minister blamed Greece for the island being forced to appeal to Russia, Brussels and the IMF for help. Vassos Shiarly said it was "not fair" that Cyprus lost €4.2bn - or 24pc of GDP - when Greece took at 50pc hair-cut on its debt. "It was a European problem," he added. "I believe we should have shared that loss fairly on a level playing field."

In Athens, Antonis Samaras, the new prime minister, started a three-day finance debate amid confusion over whether he would try to renegotiate Greece's bail-out conditions.

Meanwhile, a Portuguese court said that plans to cut civil servants' pay was unconstitutional.

Italy unveiled a further €26bn to be imposed by the end of 2014 but at the same time announced that the 2pc increase in VAT would be delayed until July next year.

"Being able to avoid the VAT increase will have a [positive] effect on the economy," said Vittorio Grilli, Italy's deputy finance minister.

UK DAILY TELEGRAPH / **LINK**

Finland would consider

leaving the eurozone rather than paying the debts of other countries in the currency bloc, Finnish Finance Minister Jutta Urpilainen has said.

In a newspaper interview today she said she'd consider crashing her AAA-rated country out of the eurozone.

"Finland is committed to being a member of the eurozone, and we think that the euro is useful for Finland. Finland will not hang itself to the euro at any cost and we are prepared for all scenarios.

"Collective responsibility for other countries' debt, economics and risks; this is not what we should be prepared for. We are constructive and want to solve the crisis, but not on any terms," she said.

Meanwhile, eurozone officials are cautioning against expecting any quick action from the currency bloc's finance ministers when they meet on Monday to sort out the tangle of loose ends and disagreements left by last month's EU debt-crisis summit.

Banking supervision, the use of European Union bailout money, aid to Spain and Cyprus and how to deal with Greece -- together it could take months to finalise, despite pressure from financial markets for clarity on the details.

Leaders from the 17 nations sharing the euro reached a deal in the early hours of last Friday to give the European Central Bank greater oversight of the bloc's banks and to use the euro zone's rescue funds to reduce countries' borrowing costs.

But after going beyond what many diplomats, finance officials and investors had expected, critical elements were left vague. Time-frames may already be slipping and opposition is building in euro zone hardliners the Netherlands and Finland.

"You have a Finnish problem. You have a Dutch problem. You have a German problem too," said one euro zone diplomat, pointing to the reservations of those countries about what was announced at the summit and German Chancellor Angela Merkel's reluctance to help its partners without strict conditions.

"I don't see a package done by Monday. They will work until the end of July or the beginning of

August on these things," said the diplomat, who is involved in preparations for the Eurogroup meeting of euro zone finance ministers.

The meeting's crowded agenda may hamper progress. Discussing an aid package for Spain's banks, dealing with a request from Cyprus for emergency help, and whether to ease the conditions of Greece's second bailout are also on the table.

Euro zone leaders have committed to ECB-led supervision for banks, which would then allow the permanent rescue fund - the European Stability Mechanism - to recapitalise banks directly, rather than having to lend to governments.

That is seen as a major concession to Spain, which has requested a bailout of up to 100 billion euros ($125 billion) for its banks, but does not want to see that money added to its national debt and possibly push it towards a sovereign rescue.

"...Finland will not hang itself to the euro at any cost and we are prepared for all scenarios,"

Leaders agreed to remove the ESM's preferred creditor status when it lends to Spain, to calm investors who were worried they would not be repaid the money they had already lent.

They also decided that the ESM and the euro zone's temporary bailout fund, the EFSF, can buy euro zone bonds at auction and in the open market to lower borrowing costs, with some conditions attached but without a full programme.

IRISH INDEPENDENT / **LINK**

A group of German economists has denounced decisions made during last week's European Union summit, arguing Thursday that they risk increasing the exposure of taxpayers, retirees and savers to the debts of struggling banks.

EU leaders agreed in Brussels that the European bailout fund could in the future pump money directly into banks, rather than via governments, once an effective, independent European supervisor is established — meaning that the aid wouldn't further add to governments' debt burden.

Leaders also agreed in principle to let the fund buy government bonds to drive down countries' borrowing costs if they comply with EU economic recommendations — meaning that countries such as Italy, which are carrying through economic reforms but still face high borrowing rates, wouldn't face the kind of deep austerity programs required of Greece.

In an open letter published by the daily Frankfurter Allgemeine Zeitung, a group of 160 economists wrote that German Chancellor Angela Merkel found herself forced to make "wrong" decisions during the gathering. The economists said they "view the step toward a banking union, which means collective liability for the debts of the banks of the eurosystem, with great concern."

"Banks' debts are nearly three times higher than government debts ... the taxpayers, retirees and savers in the so-far solid countries of Europe must not be made liable for backing these debts, particularly since gigantic losses are foreseeable from financing the southern countries' inflationary economic bubbles," they added.

The economists include Hans-Werner Sinn, the head of the prominent Ifo think-tank and a vocal critic of European leaders' rescue policies. They argued that "banks must be allowed to fail," with creditors who knowingly took investment risks bearing the burden.

Merkel rejected the criticism.

SF CHRONICLE / **LINK**

A great deal of Gordon Brown's economic strategy would strike a sane man as troubling. Not a great deal was mysterious. The orgy of consumption spending, frequent extensions of the cycle over which he would "borrow to invest", proclamations of the "end of boom and bust": these are part of the armoury of modern politicians, of all political hues.

One decision stands out as downright bizarre, however: the sale of the majority of Britain's gold reserves for prices between $256 and $296 an ounce, only to watch it soar so far as $1,615 per ounce today.

When Brown decided to dispose of almost 400 tonnes of gold between 1999 and 2002, he did two distinctly odd things.

First, he broke with convention and announced the sale well in advance, giving the market notice that it was shortly to be flooded and forcing down the spot price. This was apparently done in the interests of "open government", but had the effect of sending the spot price of gold to a 20-year low, as implied by basic supply and demand theory.

Second, the Treasury elected to sell its gold via auction. Again, this broke with the standard model. The price of gold was usually determined at a morning and afternoon "fix" between representatives of big banks whose network of smaller bank clients and private orders allowed them to determine the exact price at which demand met with supply.

"... One decision stands out as downright bizarre, however: the sale of the majority of Britain's gold reserves for prices between $256 and $296 an ounce"

The auction system again frequently achieved a lower price than the equivalent fix price. The first auction saw an auction price of $10c less per ounce than was achieved at the morning fix. It also acted to depress the price of the afternoon fix which fell by nearly $4.

It seemed almost as if the Treasury was trying to achieve the lowest price possible for the public's gold. It was.

One of the most popular trading plays of the late 1990s was the carry trade, particularly the gold carry trade.

In this a bank would borrow gold from another financial institution for a set period, and pay a token sum relative to the overall value of that gold for the privilege.

Once control of the gold had been passed over, the bank would then immediately sell it for its full market value. The proceeds would be invested in an alternative product which was predicted to generate a better return over the period than gold which was enduring a spell of relative price stability, even decline.

At the end of the allotted period, the bank would sell its investment and use the proceeds to buy back the amount of gold it had originally borrowed. This gold would be returned to the lender. The borrowing bank would trouser the difference between the two prices.

This plan worked brilliantly when gold fell and the other asset – for the bank at the heart of this case, yen-backed securities – rose. When the prices moved the other way, the banks were in trouble.

This is what had happened on an enormous scale by early 1999. One globally significant US bank in particular is understood to have been heavily short on two tonnes of gold, enough to call into question its solvency if redemption occurred at the prevailing price.

Goldman Sachs, which is not understood to have been significantly short on gold itself, is rumoured to have approached the Treasury to explain the situation through its then head of commodities Gavyn Davies, later chairman of the BBC and married to Sue Nye who ran Brown's private office.

Faced with the prospect of a global collapse in the banking system, the Chancellor took the decision to bail out the banks by dumping Britain's gold, forcing the price down and allowing the banks to buy back gold at a profit, thus meeting their borrowing obligations.

UK DAILY TELEGRAPH / **LINK**

Premier Wen's recent attack on the Chinese banking system last month has highlighted what was already a very interesting debate on Chinese banks and the Chinese financial system. There is a growing sense that the

Chinese banking system is deeply flawed and needs to be reformed.

But why should China reform its banking – hasn't the financial system been a key component of China's economic success in the past three decades? Just as importantly, what does financial reform mean – what kind of changes would need to be implemented for a real reform to have occurred?

Before addressing these questions we should be clear that there is no meaningful difference between China's banking system and its financial system. Commercial banks dominate the country's financial system and they largely determine pricing even in the informal banking system and in non-bank financial institutions. It also seems pretty clear that much of the funding within that ambiguous thing called the informal banking sector originates in the commercial banks. For example SOE's seem to be increasingly involved in financing activity, but they are probably doing so largely as a function of the "arbitrage" between the rates at which they can obtain funding from the banks and the rates at which they can lend.

"... Financial repression is a way of describing a system in which the rates of return and the direction of investment of domestic savings are not determined by market conditions and individual preferences."

So China's financial system is, for the most part, its commercial banks, and the key characteristic of the banking system is what we would call financial repression. What is a financially repressed system and why does it matter? In a recent paper ("Financial Repression Redux", Finance & Development, June 2011) Carmen M. Reinhart, Jacob F. Kirkegaard and M. Belen Sbrancia described a financially repressed system this way:

> *Financial repression occurs when governments implement policies to channel to themselves funds that in a deregulated market environment would go elsewhere. Policies include directed lending to the government by captive domestic audiences (such as pension funds or domestic banks), explicit or implicit caps on interest rates, regulation of cross-border capital movements, and (generally) a tighter connection between government and banks, either explicitly through public ownership of some of the banks or through heavy "moral suasion."*
>
> *Financial repression is also sometimes associated with relatively high reserve requirements (or liquidity requirements), securities transaction taxes, prohibition of gold purchases, or the placement of significant amounts of government debt that is non-marketable. In the current policy discussion, financial repression issues come under the broad umbrella of "macroprudential regulation," which refers to government efforts to ensure the health of an entire financial system.*

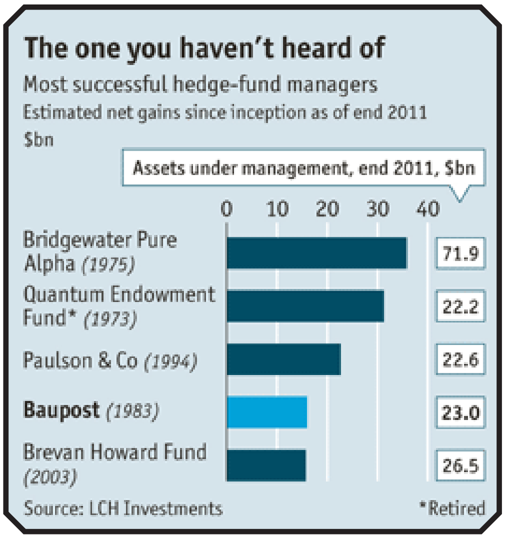
As the passage above implies, most savings in financially repressed countries, like most of the countries that followed the Asian development model, are in the form of bank deposits. The banks, furthermore, are controlled by the policy-making elite, and they determine the direction of credit, socialize the risks, and set interest rates. Financial repression is a way of describing a system in which the rates of return and the direction of investment of domestic savings are not determined by market conditions and individual preferences but rather are heavily controlled and directed by financial or political authorities. At the extreme the financial system is often little more than the fiscal agent of the government.

★ ★ ★ MICHAEL PETTIS / **LINK**

Hedge-fund bosses rarely

double as cult authors. But an out-of-print book by Seth Klarman, the boss of the Baupost Group, sells for as much as $2,499 on Amazon. A scanned version of "Margin of Safety: Risk-Averse Value Investing Strategies for the Thoughtful Investor" has been circulating around trading floors. One hedgie likens Mr Klarman's book to the movie "Casablanca": it has become a classic.

Why are Wall Street traders such avid readers of Mr Klarman? Baupost, which manages $25 billion, is the ninth-largest hedge fund in the world. Since 2007 its assets have more than tripled, as other funds have wobbled. Baupost has had only two negative years (in 1998 and 2008) since it launched in 1982, and is among the five most successful funds in terms of lifetime returns (see chart), a particularly striking record given its risk aversion. Long closed to new investors, Baupost counts elite endowments like those of Yale, Harvard and Stanford among its clients.



SOURCE: ECONOMIST

Soft-spoken and based in Boston, a safe distance from the Wall Street mêlée, Mr Klarman keeps a low profile and rarely speaks at industry shindigs. He is probably the most successful long-term performer in the hedge-fund industry who has managed to stay out of the spotlight.

Mr Klarman is a devotee of "value investing", a discipline forged by Benjamin Graham (see article) and popularised by Warren Buffett, which involves buying stocks at a discount to their intrinsic value. He will look beyond equities for bargains—a good example is Lehman Brothers, which at the end of last year was Baupost's largest distressed-debt position. But in every investment he insists on a "margin of safety", the buffer between what investors pay for the stock and what they think it is worth, so they are protected against unforeseen events or miscalculations

Mr Klarman first became an acolyte of value investing when he worked at Mutual Shares, a value-investing mutual fund, as an intern and again after he finished Harvard Business School. One of his former Harvard professors then recruited him to run a family office for him and three other families, with an investment pot of $27m (Baupost is an acronym for these families' surnames). Although the fund is significantly larger today, Mr Klarman still runs Baupost like a family office. He is extremely risk averse; his primary goal is not stellar returns but preservation of capital.

In other ways, too, Baupost is not a typical hedge fund. It uses no leverage, which is partly why Mr Klarman is not famous for one stunningly profitable trade, like George Soros's bet against sterling or John Paulson's against the housing bubble. Baupost has few short positions and often holds its positions for years, rather than days or months. Mr Klarman is patient and confident enough to do nothing. He currently has around 30%—and has been known to have as much as 50%—of his portfolio in cash. In 2008 Baupost was one of the few firms that had the scale and the available capital to buy up lots of assets from distressed sellers. "The ability to be one-stop shopping for an urgent seller is very advantageous," he says.

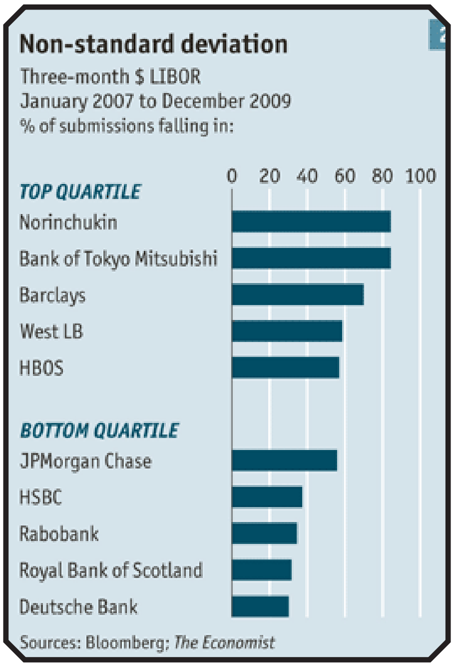
★ ★ ★ *ECONOMIST* / **LINK**

Regulators around the world have woken up, however belatedly, to the possibility that [Libor rates] may have been rigged by a large number of banks. The list of institutions that have said they are either co-operating with investigations or being questioned includes many of the world's biggest banks. Among those that have disclosed their involvement are Citigroup, Deutsche Bank, HSBC, JPMorgan Chase, RBS and UBS.

Court documents filed by Canada's Competition Bureau have also aired allegations by traders at one unnamed bank, which has applied for immunity, that it had tried to influence some LIBOR rates in co-operation with some employees of Citigroup, Deutsche Bank, HSBC, ICAP, JPMorgan Chase and RBS. It is not clear whether employees of these banks actually co-operated or, if they did, whether they succeeded in manipulating rates.

Continental Europe is focusing on cartel effects rather than digging into the internal culture of banks. Separate investigations, by the European Commission and the Swiss authorities, focus on the possible effects of inter-bank rate manipulation on end users. Last October European Commission officials raided the offices of banks and other companies involved in trading derivatives based on EURIBOR (the euro inter-bank offered rate). The Swiss competition commission launched an investigation in February, prompted by an "application for leniency" by UBS, into possible adverse effects on Swiss clients and companies of alleged manipulation of LIBOR and TIBOR (the Tokyo inter-bank offered rate) by the two Swiss and ten other international banks and "other financial intermediaries".

The regulatory machinery will grind slowly. Investigators are unlikely to produce new evidence against other banks for a few months yet. Slower still will be the progress of civil claims. Actions representing a huge variety of plaintiffs have been launched. Among the claimants are investors in savings rates or bonds linked to LIBOR, those buying derivatives priced off it, and those who dealt directly with banks involved in setting LIBOR.



SOURCE: BLOOMBERG/ECONOMIST

Deciding a figure for the potential liability facing banks is tough, partly because the cases will be testing new areas of the law such as whether, for instance, an Australian firm that took out an interest-rate swap with a local bank should be able to sue a British or American bank involved in setting LIBOR, even if the firm had no direct dealings with the bank. The extent of the banks' liability may well depend on whether regulators press them to pay compensation or, conversely, offer banks some protection because of worries that the sums involved may be so large as to need yet more bail-outs, according to one senior London lawyer.

A particular worry for banks is that they face an asymmetric risk because they stand in the middle of many transactions. For each of their clients who may have lost out if LIBOR was manipulated, another will probably have gained. Yet banks will be sued only by those who have lost, and will be unable to claim back the unjust gains made by some of their other customers. Lawyers acting for corporations or other banks say their clients are also considering whether they can walk away from contracts with banks such as long-term derivatives priced off LIBOR.

The revelations also raise difficult questions for regulators. Mr Tucker's involvement in the Barclays affair may harm his prospects of being appointed governor of the Bank of England, although he may well have a benign explanation for his comments (he is due to appear before parliament soon).

Another issue is the conflict central banks face, in times of systemic banking crises, between maintaining financial stability and allowing markets to operate transparently. Whether the BoE instructed Barclays to lower its submissions or not, regulators had a pretty clear motive for wanting lower LIBOR: British banks, in effect, were being shut out of the markets. The two hardest-hit banks, RBS and HBOS, were both far too big to fail, and higher LIBOR rates would have made the regulators' job of supporting them more difficult.

This highlights a deeper question: what is the right level of involvement in influencing or regulating market interest rates, in a crisis, by those responsible for financial stability? Central banks get a slew of sensitive information from banks which they rightly do not want to make public. Data on deposit outflows at banks could trigger unnecessary runs, for example. Yet LIBOR is a measure of market rates, not those picked by policymakers.

ECONOMIST / **LINK**

Proponents of Asian integration have always looked to Europe for inspiration. Since Europe built a free-trade area, they observed, Asia should similarly consider creating a regional free-trade bloc. When the Europeans then completed their single market in 1992, the conclusion was that Asia needed to step up the pace of integration. And, perhaps predictably, the Europeans' creation of the euro in 1999 prompted a flurry of speeches about the desirability of Asian monetary integration.

The crisis in the eurozone clearly demands that this consensus be rethought. Above all, Europe's crisis makes clear that a single Asian currency is unrealistic and undesirable and that it will remain so for the foreseeable future.

> "... Europe's crisis makes clear that a single Asian currency is unrealistic and undesirable and that it will remain so for the foreseeable future"

The European mess reminds us that it is critically important for the preconditions for a smoothly functioning monetary union to be met before moving to a regional currency. The Europeans assumed that the necessary preconditions would develop in response. Policy shocks affecting the participating national economies would become more similar as a result of the act of sharing a currency, they argued. Indeed, not just policies but the very structures of the participating national economies would become more similar, or so it was believed.

This turned out to be naive. While the monetary policies of different European countries became more similar – by definition, since they shared a single central bank – fiscal policies did not converge. Economic structures, if anything, diverged further, and with them competitive positions. Rather than becoming easier, life with a common European monetary policy became harder with the passage of time.

A second lesson of European experience is that Asia should consider adopting a single currency only if governments are prepared to give up national oversight of their banking and financial systems. Monetary union, we now understand, requires banking union. Supervision and regulation, deposit insurance and arrangements for dealing with insolvent banks all must be turned over to a supranational authority. The alternative, a national banking system without a national central bank to backstop it, is a recipe for disaster.

The third lesson of European experience is that monetary union requires the participating countries to take significant steps toward fiscal union. They will have to contribute tax revenues to their common deposit-insurance and bank-resolution fund. There will have to be budgetary transfers from booming to depressed regions to help the latter cope with banking, debt and social problems.

★ ★ ★ *BARRY EICHENGREEN* / **LINK**

Deputy Bank of England governor, Paul Tucker, will be grilled by MPs over the Libor scandal and whether regulators decided to turn a blind eye to misconduct.

The deputy governor of the Bank of England was warned that UK lenders were manipulating interest rates a year before he allegedly gave Barclays "a nod and a wink" to rig its own, in a call with former chief executive Bob Diamond in 2008.

Paul Tucker will on Monday be grilled by MPs on the Treasury Select Committee (TSC) over the Libor scandal, where he will be asked whether regulators decided to turn a blind eye to misconduct during the banking crisis in the interests of financial stability.

Specifically, he is expected to be quizzed about a meeting he chaired of the Bank's Sterling Money Markets Liaison Group in November 2007, at which several members warned they "thought that Libor fixings had been lower than actual traded inter-bank rates through the period of stress".

Mr Tucker will also be asked to explain why he did not want to relay a message from Barclays' chief executive Bob Diamond to Westminster that other banks were low-balling their Libor submissions on Oct 29, 2008, according to Mr Diamond's record of the event.

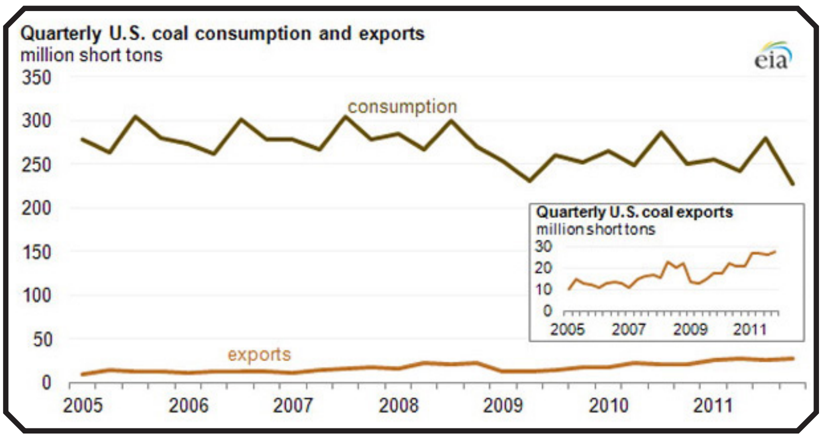
TSC sources yesterday said Mr Tucker must have known that Royal Bank of Scotland and Lloyds Banking Group were posting false rates because their Libor submissions were lower than Barclays even after they had been locked out of markets and forced to take £60bn in secret loans from the Bank.

Andrew Tyrie, the TSC chairman, has described the note of the conversation between Mr Tucker and Mr Diamond as "a nod and a wink" for Barclays to rig their Libor rate.

"The question will be whether Mr Tucker knew Libor was being manipulated and whether he was allowing it for the sake of market confidence," one source said. He will also be asked to clear up speculation about whether Baroness Vadera and Cabinet Secretary Sir Jeremy Heywood were preparing to nationalise Barclays in 2008 or encouraging banks to lower Libor submissions.

UK DAILY TELEGRAPH / **LINK**

Oil, natural gas, and alternatives dominate the headlines when it comes to energy. But there's a big and largely-overlooked revolution occurring with the energy source likely to become the most preferred fuel for a world in economic decline: coal.



SOURCE: **EIA/GREGOR**

The United States coal sector has been hit very, very hard this spring. Demand has been crushed by over 10%, as warm weather and bountiful supplies of cheap natural gas have induced power plant operators and all other users where possible to switch away from domestic coal. The rapid change in fortune has sent the stock prices of big, listed names such as Peabody and Arch down by double digit percentages, as the Dow Jones US Coal Index has fallen below 160 from above 225 at the start of 2012.

From Bloomberg:

> *Central Appalachian thermal coal futures, the U.S. benchmark, averaged $60.20 during the first quarter, down from an average of $73.58 in the year ago period and down from a high of $143.25 in July 2008. "It's like a perfect storm," Mann said. "The three main challenges are the really mild winter, a lethargic economy and on top of that, with gas prices being so low, those utilities that can burn gas have opted to burn gas instead of coal because gas is so cheap." Cheap gas has undercut power producers' revenues because it drives down wholesale electricity prices, squeezing margins for plants that run on nuclear, renewable and coal power. Moody's Investors Service changed its outlook for the U.S. coal industry to "negative" from "stable" on May 7, citing weak prices and a drop in power demand, and said it expects a 5 percent decline in prices for coal deliveries in 2013. The U.S. Energy Information Administration expects the industry to see a 10.9 percent decline in coal consumption this year and Moody's expects U.S. coal demand from power plants to plunge by 100 million tons by 2020, the ratings company said in the report.*

...Is coal finally going away as an energy source?

Not a chance..

GREGOR / **LINK**

CLICK TO ENLARGE

SOURCE: BAML

Bank of America Merrill Lynch recently released a comprehensive set of charts going back 100 years and covering just about every financial instrument of any importance.

This is definitely one to bookmark.

(via zerohedge)

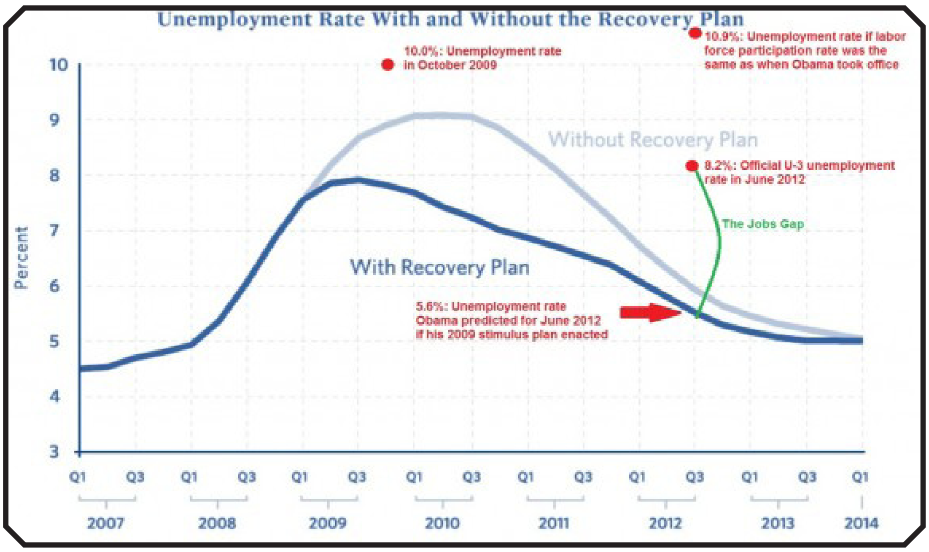
This was not the employment report either the American worker or the Obama campaign wanted to see right now. The Labor Department said the U.S. economy created just 80,000 jobs in June, less than the 90,000 economists had been forecasting. And private-sector job growth was just 84,000, down sharply from 105,000 in May. Not doing fine.

The unemployment rate stayed at a lofty 8.2%.

As a research note from RDQ economics put it: "The good news is that employment growth is not slowing further but there is no sign of it picking up either. At this pace, job creation is not fast enough to lower the unemployment rate with the labor force growing at close to 150,000 per month on average." Shorter: Stagnation Nation

This continues to be the longest streak — 41 months — of unemployment of 8% or higher since the Great Depression. And recall that back in 2009, Team Obama predicted that if Congress passed its $800 billion stimulus plan, the unemployment rate would be around 5.6% today. (via zerohedge)

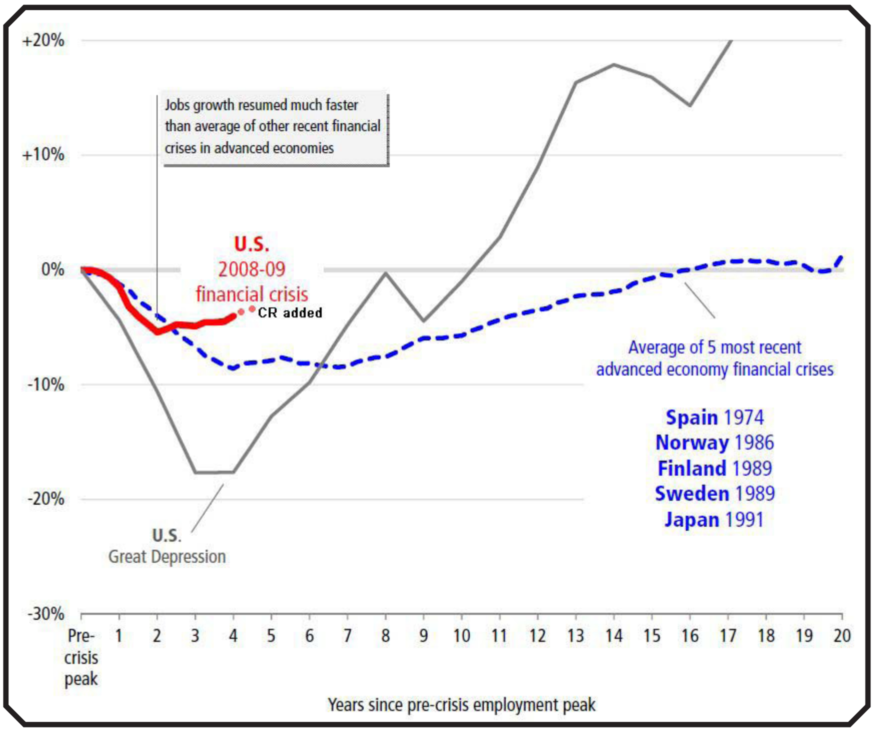
JAMES PETHOKOUKIS / **LINK**

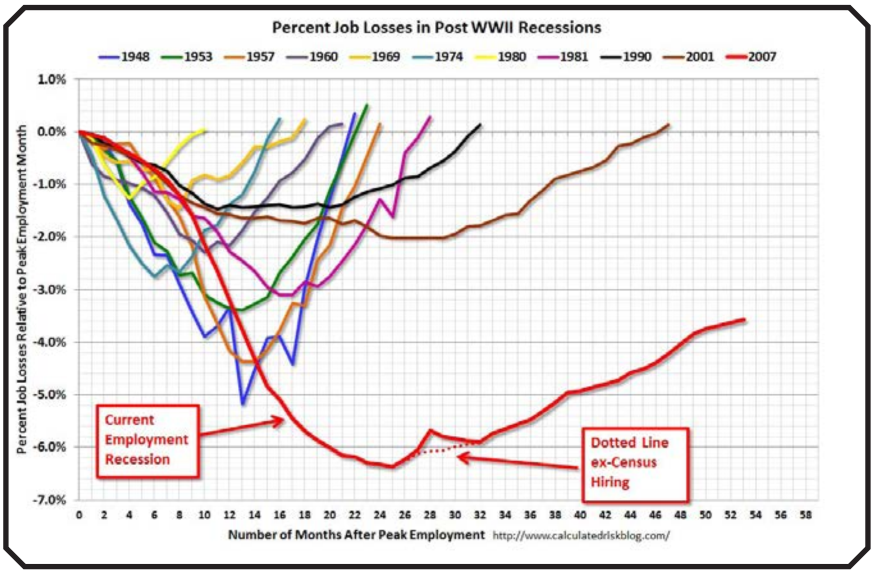


CLICK TO ENLARGE

SOURCE: AEI IDEAS

The causes of the Great Recession were similar to the Great Depression - as opposed to most post war recessions that were caused by Fed tightening to slow inflation - and I'm frequently asked if we could compare the percent job losses during the two periods. Unfortunately there is very little data for the Great Depression.





CLICK TO ENLARGE

SOURCE: CALCULATED RISK

Back in February I posted a graph based on some rough annual data.

In April, Treasury released a slide deck titled Financial Crisis Response In Charts. One of the charts shows the percentage jobs lost in the current recession compared to the Great Depression.

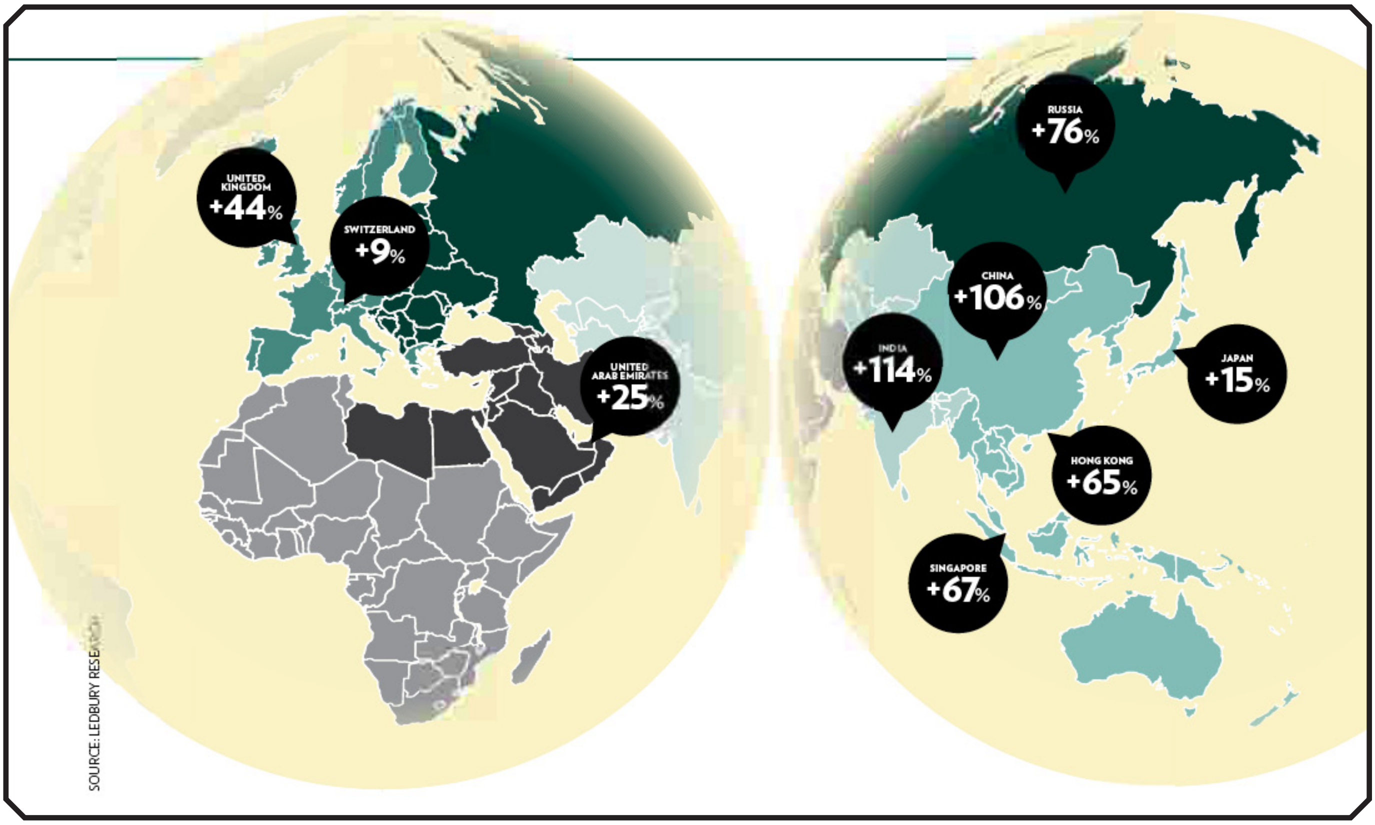
Here is that graph (I've added a couple of dots to update the current recession).

This graph compares the job losses from the start of the employment recession, in percentage terms for the Great Depression, the 2007 recession, and the average for several recent recession following financial crisis.

Although the 2007 recession is much worse than any other post-war recession, the employment impact was much less than during the Depression. Note the second dip during the Depression - that was in 1937 and the result of austerity measures.

For reference, the second graph shows the job losses from the start of the employment recession, in percentage terms, compared to other post WWII recessions.

CALCULATED RISK / **LINK**



CLICK TO ENLARGE

SOURCE: LEDBURY RESEARCH

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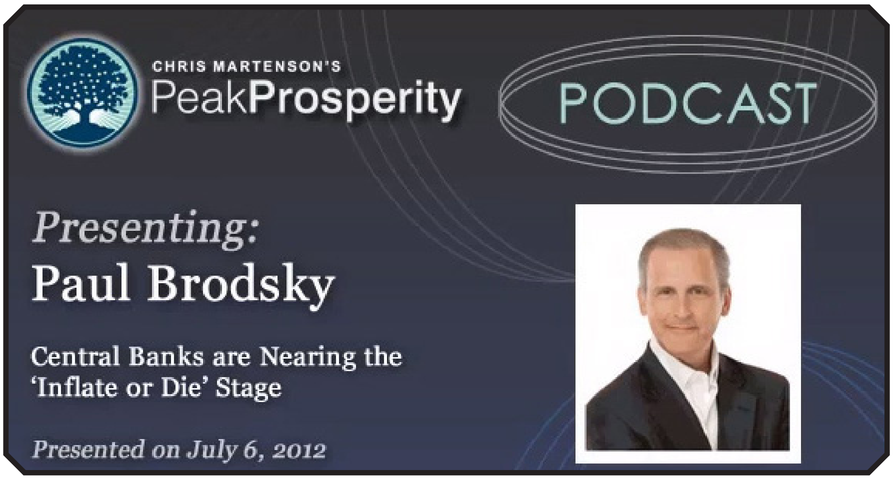
SOURCE: RITHOLTZ

The distribution of the world's super-rich is shifting. Grainne Gilmore seeks out future global wealth hotspots and discovers it's not all about China

London School of Economics professor Danny Quah has calculated that the world's economic centre of gravity – the average location of economic activity by GDP – is on the move. By 2050, the steady rise of emerging economies in Asia will have pushed the theoretical centre of gravity modelled by Professor Quah from its location in 1980 in the Atlantic Ocean to somewhere between China and India by 2050. He predicts that political infl uence will follow a similar trajectory eastwards.

★ ★ ★ *THE BIG PICTURE* / LINK



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My friend Paul Brodsky spends some time talking to Chris Martenson about the difficulties of trying to solve a balance sheet problem through political means.

As always, Paul's thoughts are clear, logical and presented beautifully.

Paul's conclusion, that Central Banks are 'approaching the 'inflate or die' stage' is, in my opinion, spot-on.

Nigel Farage just won't go away (much to the chagrin of his 'old friends' van Rompuy and Barosso), but while that's not great news for them, it's good news for those of us that take our information straight up.

This week, Farage explains the futility of Euro 'summits' and how Europe is unraveling on its way to 'total collapse'.

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Manipulation? Conspiracy? Banking misdeeds? You can't talk about these three things without including Gerald Celente in the debate. Celente is always entertaining and has a style all of his own, but behind the hyperbole there lies a serious message and today he takes on, you guessed it, Europe, Libor and gold...

Truth in advertising...

(thanks AZ)

SOURCE: STUPIDEST.COM

SOURCE: UNKNOWN

Hmmm…

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Grant Williams

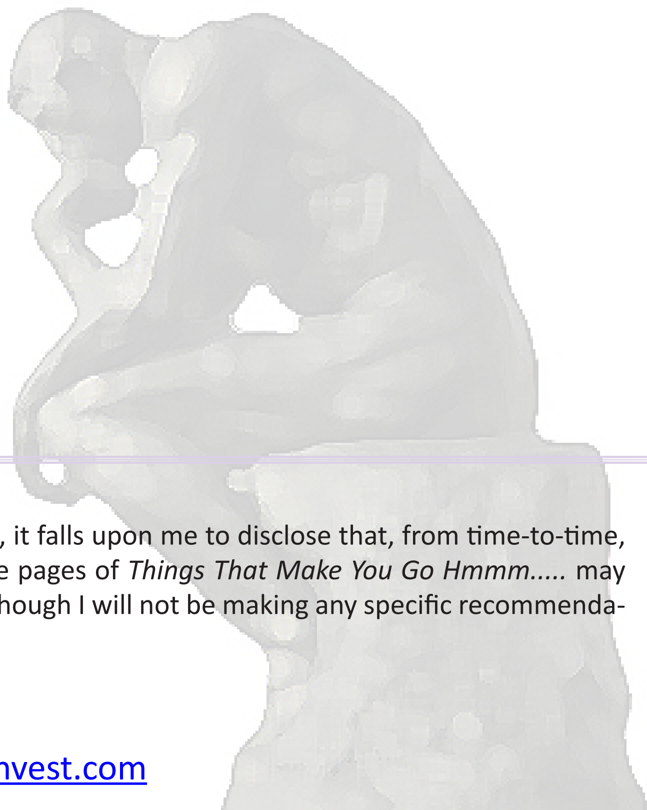
Grant Williams is a portfolio and strategy advisor to Vulpes Investment Management in Singapore - a hedge fund running $200million of largely partners' capital across multiple strategies.

In 2012, all Vulpes funds will be opened to outside investors.

Grant has 26 years of experience in finance on the Asian, Australian, European and US markets and has held senior positions at several international investment houses.

Grant has been writing 'Things That Make You Go Hmmm.....' for the last three years.

For more information on Vulpes please visit www.vulpesinvest.com



As a result of my role at Vulpes Investment Management, it falls upon me to disclose that, from time-to-time, the views I express and/or the commentary I write in the pages of *Things That Make You Go Hmmm.....* may reflect the positioning of one or all of the Vulpes funds - though I will not be making any specific recommendations in this publication.

Grant

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