Patient Capital.... Positioned for Profit

A PEEK AT THE WEEK THAT WAS - August 24, 2013

Last week we took a look at the history of the all conquering Fed, which we continue this week. We love history and this is a particularly fascinating story...and one that, unfortunately, seems to go on and on, with potentially disastrous consequences...unless you're a banker, of course.

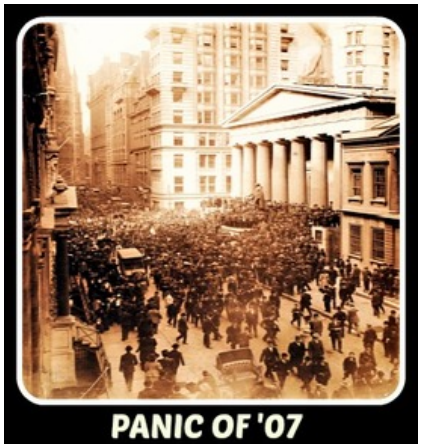
Last week, we also shared some charts on silver, which we found interesting. Both silver and gold have continued their upward movement this past week. Silver is up over $4 per ounce (from less than $20 to $24) in the past two weeks...a 20% gain That's impressive.

During roughly the same time frame, gold is up a bit less than 10% from $1,280 / oz to close on Friday at $1,398. Not bad either.

Will they retrace? As usual, we have no clue but if forced to take a position, we would suspect not...or at least not much and for not too long. We've given a multitude of reasons for our thinking in past Peeks but we'll risk one more reason why...and it has to do with a certain piece of nifty Manhattan real estate.

Meanwhile, over at Mr. Market's Club S&P, the much vaunted "1700" sign is still down. And Ms. Bond is still waving her sobriety banner ever higher.

We think it's worth keeping a close eye on Ms. Bond. She's much more thoughtful and level headed than Mr. Market. And she has Bartender Ben worried. We'll take a peek at why this may be so. In the process, we'll show you a couple of charts, including one illustrating the percentage rise in the 10 year US Treasury, which we think is alarming enough to qualify as our chart of the week.



THE OFFICIAL, APPROVED HISTORY OF THE FEDERAL RESERVE...WELL, ALMOST! (PART II)

We started off last week with a peek at the initial history of the Fed. We got up to the part where the geniuses of the time decided that it would be a good idea to develop a "banker-controlled plan" to fix all the booms and busts that were plaguing their financial world.

Of course, it was human nature and a combination of banker hubris and avarice that were largely responsible for these woes but that didn't stop them from thinking that they could "fix it".

Question is...fix it for who? Or is that "whom". Never mind. Just fix it.

You can click here to see the full official history of the Fed. It's official and approved but we prefer to do our own sleuthing anyway. It's just how we are. A sleuthing we shall go.

So we find ourselves in a private rail car in Hoboken in November of 1910. We are surrounded by bankers primarily representing the interests of the houses of our major benefactors, JP Morgan and JD Rockefeller. These sly bankers are only using their first names so that the porters will not recognize this merry band for who they actually are. No cell phone cameras or texting here. The smoke hangs low.

This nefarious gathering has been called and coordinated by none other than Nelson W. Aldich, the co-sponsor of the Aldich-Vreeland Act of 1908...passed in response to the panic of 1907 (of which we spoke last week).

We learn that the panic really set in just three years before our fateful train ride...when our bankers realized that they...their mighty selves...might go to the wall along with all the other punters and speculators they had so ably aided and abetted.

Nothing panics a banker quite like the potential of being relegated to the ranks of the rabble they are quick to finance yet otherwise find so repugnant.

In those desperate hours of October 1907, as a bank run looked imminent, our wise and friendly bankers indeed realized that they needed a super deep pocketed lender of last resort to bail them out should another panic come about...which, of course, they knew was inevitable.

From Wikipedia...

> *The Panic of 1907, also known as the 1907* ***Bankers' Panic*** *[interesting that bankers should actually panic....aren't they masters of the universe?] or Knickerbocker Crisis,[1] was a financial crisis that occurred in the United States when the New York Stock Exchange fell almost 50% from its peak the previous year. Panic occurred, as this was during a time of economic recession, and there were numerous runs on banks and trust companies. The 1907 panic eventually spread throughout the nation when many state and local banks and businesses entered bankruptcy.* ***Primary causes of the run include a retraction of market liquidity*** *[ooops....we can never let that happen again] by a number of New York City banks and a loss of confidence among depositors, exacerbated by* ***unregulated side bets at bucket shops****. [substitute "bucket shops" for hedge funds and proprietary trading desks post the repeal of Glass Steagall] [2] The panic was triggered by the failed attempt in October 1907 to* ***corner the market on stock of the United Copper Company****. [when will these guys learn?...clearly never...copper, aluminum?...who cares....click here for their latest shenanigans] When this bid failed, banks that had lent money to the cornering scheme suffered runs that later spread to affiliated banks and trusts, leading a week later to the downfall of the Knickerbocker Trust Company—New York City's third-largest trust.* ***The collapse of the Knickerbocker spread fear throughout the city's trusts as regional banks withdrew reserves from New York City banks****. [hmmm...nothing panics a banker like withdrawal of real money...especially from those hokeys in the countryside...how dare they?] Panic extended across the nation as vast numbers of people withdrew deposits from their regional banks [don't worry...now we have FDIC insurance and Ben at our back...what could go wrong].*
>
> **[yes, the emphasis and snide comments are ours as usual]**

Yes, my fine feathered fancy friends, said the bankers to one another, we can't let that happen again. It was just too close for comfort. Those darned regional banks. Why...they could have brought us down. We need a bigger patsy. We need a central bank with unlimited printing power...that we control, of course. We need to set it up so that when those hokeys and their depositors want their money back....you know...the stuff we've already wagered out....we'll just have some "independent" institution print more to keep them happy.

How hard can it be? Thank you Mr. Gutenberg. We are just a printing press away from salvation!

So...such a great plan...why all the secrecy with private railcars in far off stations? Well, even back then, there was a public and private suspicion of bankers and particularly a central bank. In those days, people actually spoke to each other. They conversed at some intellectual level far removed from today. There was no texting, no TV, no internet, no distracting screens or useless noise in the taverns and bars of the time. Somehow, without all the social media, they were more social...and suspicious...especially of bankers. Wise folk indeed.

Moving forward...or backward, in this case...our private railroad car takes us from Hoboken, on the northern frontier of New Jersey, to Brunswick, on coastal Georgia, where we board a

private launch to the exclusive retreat (for the well to do, of course) called the Jekyll Island Club.. Lovely club...coincidentally owned in part by none other than good ol' JP himself.

Happily ensconced on Jekyll Island, we work hard for a week hammering out what would ultimately become the Federal Reserve Act.

Early on, we realize we need to be both stealthy and smart to make our ugly creature appear pleasing to the casual observer. We would not call it a central bank (people already hated those because they recognized them for what they were). We would call it a Federal Reserve System and it would be comprised of a number of member banks, although we would dominate it from New York, of course. We would make it appear that it was part of government and therefore subject to control and scrutiny by democratically elected representatives (he he). We would launch the equivalent of a massive PR campaign to put the prettiest face possible on our creation. We would recruit Woodrow Wilson to our side. Against the odds he will be elected president and become a worthy ally.

We are brilliant and determined and we are ultimately successful. Things go well indeed. As they should....after all...we are masters of the universe!

Our legislation is passed into law on December 23, 1913...just in time for Christmas. By the time the Europeans start the war to end all wars in 1914, we are ready for business.

Oh...and by the way...we did our job so well that the House of Representatives passed the Federal Reserve Act by a vote of 298 to 60 and the Senate passed the measure 43 to 25. Best of all, in both chambers of Congress, it was the anti-banker Democrats that overwhelmingly supported the Act, while for the most part the pro-banker Republicans opposed it.

And, the rest, as they say...is history!

Speaking of history, the proof of the pie is in the pudding...and that pudding is called Citibank. Two of the banks respresented in that little Jekyll Island jaunt, Rockefeller's National City Bank and Morgan's First National Bank ultimately merge to become the First National City Bank of New York...or as we know it...Citibank.

From Reuters...back in the dark days of late 2008...

> *NEW YORK | Mon Nov 24, 2008 6:52pm EST*
>
> ***Citigroup gets massive government bailout***
>
> *(Reuters) - The U.S. rescued Citigroup Inc, agreeing to shoulder most losses on about $306 billion of the bank's risky assets, and inject new capital, bolstering investor hopes that the government will support big banks as the economy sinks into recession.*

Without a massive tax-payer funded bailout in 2008, Citibank was gone. Who funded the bailout. The taxpayer of course. Who facilitated the transaction and made it all possible. Why...the Fed, of course...with the assistance of Helpful Hank (Paulson) over at Treasury. The plan worked to perfection.

Simply brilliant, if we do say so ourselves. You can read our little legislative gem called the Federal Reserve Act by clicking here....and we didn't need anything like Barry Obamacare's 2,000 pages.

We created the most powerful financial entity in the history of the world in just 31 pages...and yes..Nancy...we did read it before it was passed. Every word. Trust us on that!

Space eludes us this time but next week, we'll take a look at who actually owns the creature we created on Jekyll Island.

VERY LARGE GOLD VAULT FOR SALE...COMES COMPLETE WITH YOUR OWN 60 FLOOR SKY SCRAPER WITH GREAT ACCESS TO YOUR FRIENDLY FED

In our June 22 Peek At The Week, we made reference to a certain building owned by Jamie Dimon's crew at JP Morgan located at 1 Chase Manhattan Plaza, just across the street from the Federal Reserve building. Apparently there is a nifty underground tunnel connecting the two.

We're happy to report that with enough dollars...or presumably gold...you can now acquire this legendary building (developed by David Rockefeller no less) for yourself. In addition to handy access to the Fed, it is located just a very quick walk from Wall Street and a quiet handsome church where the more than occasional lost soul or losing trader can be found lighting candles and seeking succor.

We have thought about acquiring these fancy digs ourselves but we are just a tad short of the expected $600,000,000 asking price. Perhaps we should light more candles?

> From Bloomberg...By David M. Levitt - Aug 20, 2013 9:19 AM ET
> ***JPMorgan Marketing Downtown's 1 Chase Manhattan Plaza***

But why would JP Morgan want to sell their vault and the skyscraper above it? The official line is to consolidate its employees and downtown operations with its other mid-town Manhattan complexes. We suspect, however, it has more to do with Jamie and the crew getting out of the physical commodities business.

> From Reuters...
> ***JPMorgan to quit physical commodity trade amid scrutiny***
> *NEW YORK | Fri Jul 26, 2013 5:54pm EDT*
> *(Reuters) - JP Morgan Chase & Co is exiting physical commodities trading, the bank said in a surprise statement on Friday, as Wall Street's role in the trading of raw materials comes under intense political and regulatory pressure.*

Who needs a football field sized vault if you're out of the gold business. And that presumably includes the gold shorting business. Hmmm....maybe that helps to explain the great April gold heist. If JP Morgan were short gold...reputedly because of what they may have inherited from legacy Bear Sterns positions (remember them?), then it's conceivable that they might have forced down the price in order to go long the shiny stuff to cover their positions.

The chart below illustrates how much the gold holdings of the ETFs (Exchange Traded Funds like GLD) have decreased since the great paper gold sell off in April. Remember, only the big boys are allowed to redeem their ETF shares for gold...all other punters (holding less than 100,000 shares) must settle for cash. That gold went somewhere. Maybe it's in the vault at 1 Chase Manhattan Plaza. Unfortunately, it is not part of the transaction so don't expect it to be there after you complete your acquistion.

But all this does beg the question. If JPM...one of the big dogs in the gold and silver biz...is out of the market, will that allow the market to act in a more orderly supply and demand (read...less manipulated) fashion. If so, then we suspect that both gold and silver have a nice ride ahead of them.

Maybe that's why one of our favorite smarties...self made Seth (Klarman) and his Baupost Group are buying up the precious metals miners. As we have said many times, Mr. Klarman is no idiot. You can click here to learn a bit more about what he is buying.

The miners have been acting well of late. Maybe it's time to take a closer look. Rocky Balboa is no longer on the mat. He's up..and the music is playing. Watch out Apollo!

CHART(S) OF THE WEEK - MS. BOND IS BECKONING...
EXCEPT IN THE LAND OF THE SETTING SUN!

Bartender Ben is so envious of Happy Haruhiko (Kuroda). While Ms. Bond is becoming a much more expensive date for Bartender Ben, his counterpart in Japan is still getting away being a cheap host. In fact, bond yields seemingly everywhere else are increasing as Ms. Bond and her band of bond vigilantes become increasingly wary of Ben's bunch of merry money printers losing control of their presses.

There are two charts below that illustrate this graphically. The first, courtesy of the great Grant Williams shows the increase in interest rates around the world over the past three months...with the notable exception of Japan (how does Happy do it?).

The second shows the recent and dramatic increase in the US 10 year treasury...which we consider one of the most important barometers out there.

So what's the big deal if interest rates increase? Isn't that evidence that the economy is bouncing back...just as Ben promised?

Here's the problem...remember all that money that Ben has printed...it is technically and practically a debt that has to be paid back. Those treasury bonds are, after all, a promise by the US Government (that's us taxpayers, folks) to pay the holder their money back plus interest along the way. Every point that the interest rate increases, the burden of paying increases too.

You can read more about this ugly phenomenon here and here and here.

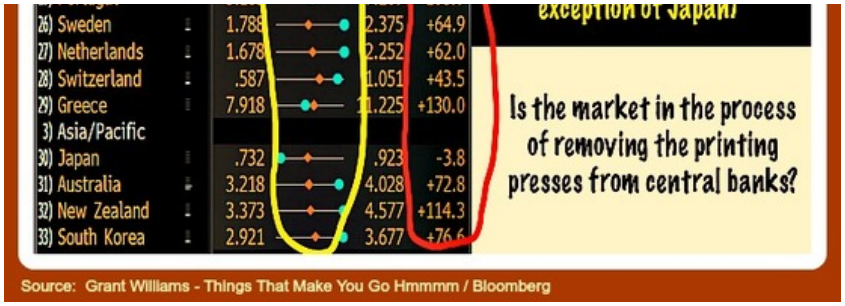
To make matters worse, we have big holders of treasuries (think China and Japan) selling.

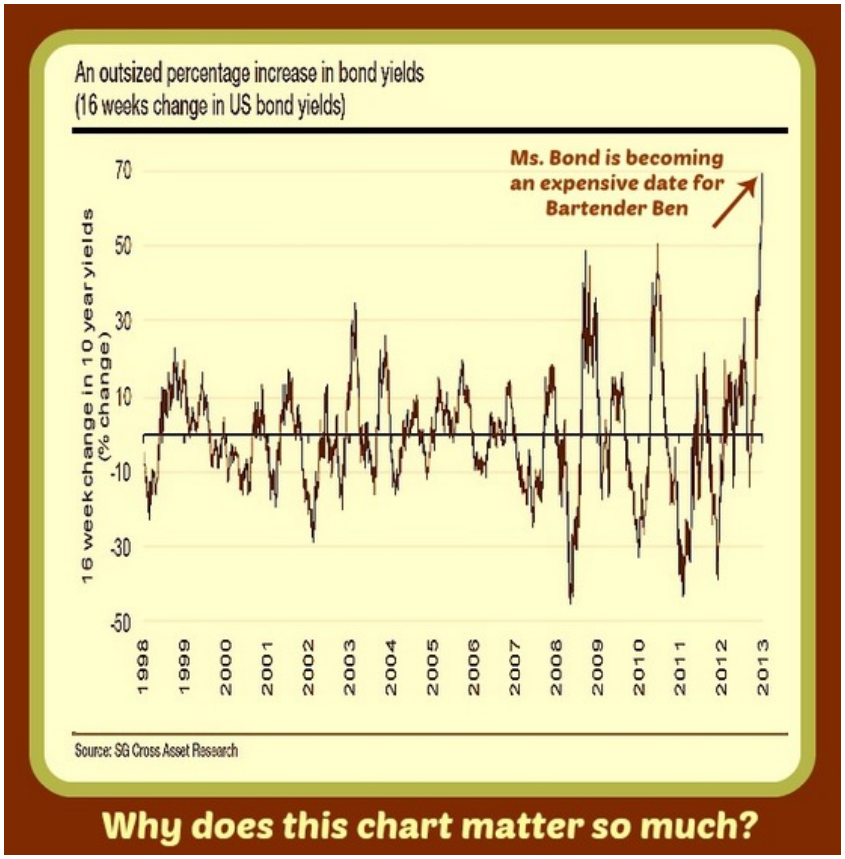
From Reuters, August 16, 2013:

> ***China, Japan lead record outflow from Treasuries in June***
>
> *China and Japan led an exodus from U.S. Treasuries in June after the first signals the U.S. central bank was preparing to wind back its stimulus, with data showing they accounted for almost all of a record $40.8 billion of net foreign selling of Treasuries.*
>
> *The sales were part of $66.9 billion of net sales by foreigners of long-term U.S. securities in June, a fifth straight month of outflows and the largest since August 2007, U.S. Treasury Department data showed on Thursday.*

So, we have more sellers than buyers. Even Ben is considering stepping away from the table...remember he has been buying up to 30% of the treasury issues. Less buyers, more sellers equals a demand for higher rates from the ever sober, ever smart Ms. Bond. Higher rates make it more expensive to service the national debt and ultimately inhibit the economy's growth.

No wonder Bartender Ben is calling it a day at year's end. Perhaps he'll sojourn in the land of the setting sun. After all, Happy Haruhiko has it all under control over there...or does he?





Til next week...

"Ignorance is the curse of God. Knowledge is the wing wherewith we fly to Heaven."
William Shakespeare

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