

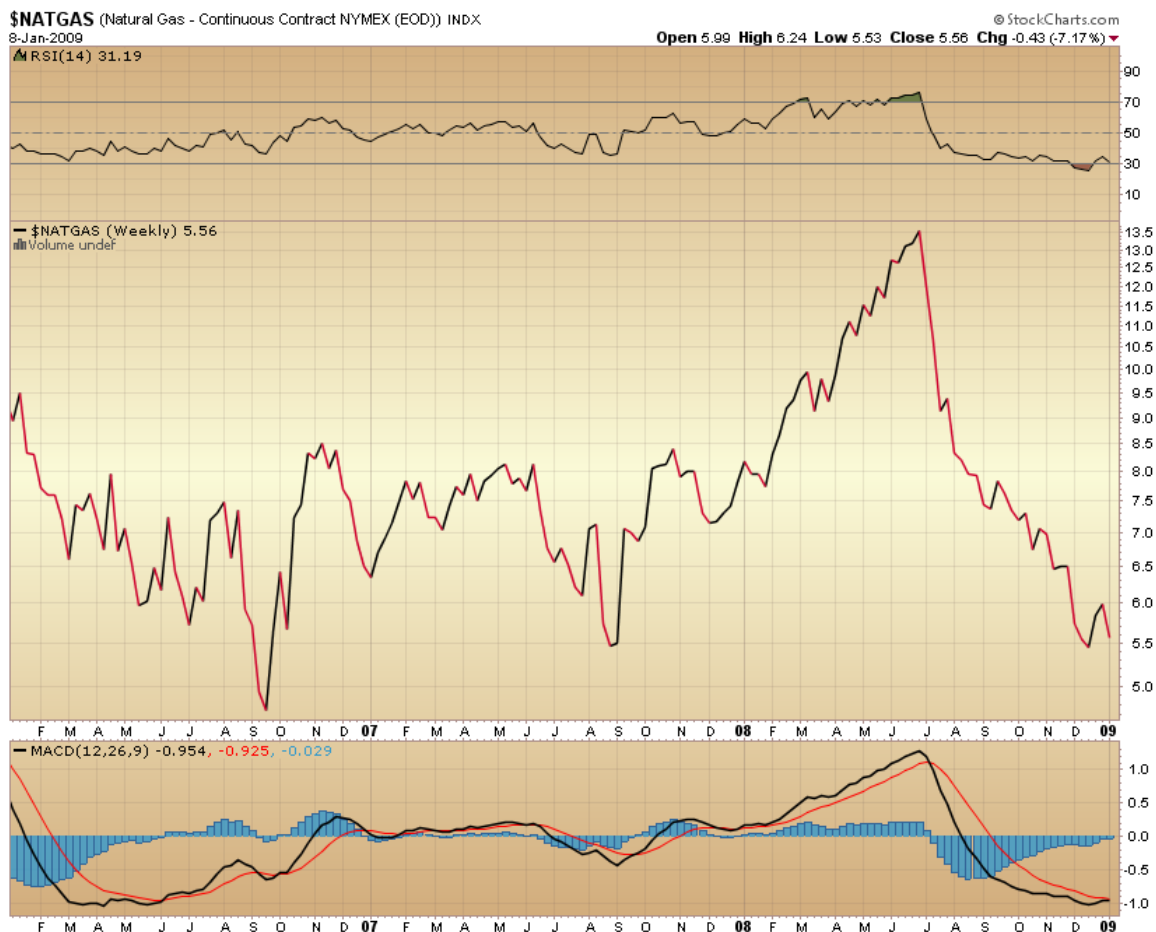
Today's Notes:

1. Throw More Money

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It's getting nasty out there. The weather in Europe is very cold. The streets in Paris are icy according to David Kotok Chief at Cumberland Advisors (thanks to Jim Currie for that). Paris may be freezing but it is buzzing this AM with a Sarkozy / Brown sponsored symposium on the New Capitalism. One hopes that a new market allocation mechanism is not so constrained as to raise the cost of capital to levels so high that commerce stops. One also hopes globally we can agree to agree on market structures; more on that later.

In the Northwest of this country and the Canadian West it has been snowing and raining for more than a month. So much for human induced global warming. The Globe mentioned that all of Canada was white for Christmas for the first time since early in the 1970s. Flooding and avalanches are everywhere from Whistler to Seattle. Here in New York we expect snow this weekend and colder temperatures, though on the East Coast it has been relatively mild.



Nevertheless, with all the cold weather around the world (no sunspots this year you see) the supplies of crude and natural gas are inundating storage capacity. WTI, in contango, is selling for a little above \$40 a barrel and natural gas has fallen to a 2 year low of \$5.50 where it must hold. All this provides a massive tax break for Canadians and Americans though it is less sanguine for the fossil fuel producers. Chesapeake Energy is selling gas assets at bargain prices and cutting employees to raise cash. Cash is king – no doubt about that - and the US \$ is still the Emperor. There is strong sentiment that this recession is deepening and demand destruction is everywhere. Whenever it occurs, there is a belief that the US will emerge first.

This price decline is not sanguine for Venezuela, Russia and Iran however. Russia, Iran and Algeria are attempting to form an OPEC gas cartel to buoy natural gas prices. 60% of Russia's export earnings are energy-related. Her daily oil production is declining by about 1 million barrels each year. Venezuela is 94% dependent on oil revenues.

Two weeks ago Russia began to cut off gas supplies to Western Europe. The problem was Ukraine's intransigence to paying market rates for her gas. Ukraine, you see, was once part of the Soviet Union and became inured to the "benefits" of cheap gas. The Russian Bear deserves market prices, of course, but she shows once again her true nature as she did in the invasion of Georgia in August and bullying and expropriation of the assets of foreign energy companies in Russia. There will be little interest in more investment in Russia for quite a long time. Russia like Venezuela will experience increasingly difficult efforts to produce oil and gas without access to global capital.

The social ramifications of these lower energy prices and declining production curves in Iran, Russia and Venezuela will be felt very soon. This then has potential for further geopolitical consequences. It is imperative that the West embark on a program to free ourselves from dependence on such undependable suppliers of energy. This program will take a decade or more. In the meantime conservation makes sense and a gasoline tax is one way though painful indeed to assure that approach.

In the meantime no matter how much money is being created in Washington (and around the world) , no matter how much the FED's balance sheet is expanded (now \$2.2 trillion) the money seems to be stuck "under the consumer's mattresses." Retail sales and profit numbers for the holidays were terrible. In September US consumers borrowing increased \$6.7 trillion. That fell by \$2.8 trillion in October and fell even more by \$7.9 trillion in November, according to Bloomberg. This was the first drop for 2 successive months in 17 years. Mom and Pop are most definitely on the sidelines and this is very bad news for the US economy (70% consumer driven) and more importantly the global market place (20% driven by the US consumer). The Obama Administration and the Federal Reserve can print all they want but they cannot make banks lend and consumers spend. The psychology of the marketplace is in full force and has capped those dynamics to date. This will take time, dear D.I.

And now we come to market psychology and perhaps the first major blunder of the Obama Presidency. You do realize that we now have two presidents in the US do you not? Yes of course, President Elect Obama has taken it upon himself to propose legislation before he is sworn in. This is a poor precedence for a person who has NEVER run anything in his life, never made a payroll and never had to hire or fire an employee and one who promised change and

decided to reinvent the Clinton administration. Some change! But that is not the most egregious sin that he committed yesterday. Yesterday this young silver-tongued orator said,

“... that will lead to an even greater deficit of jobs, incomes, and confidence in our economy. It is true that we cannot depend on government alone to create jobs or long-term growth, but at this particular moment, only government can provide the short-term boost necessary to lift us from a recession this deep and severe. Only government can break the vicious cycles that are crippling our economy - where a lack of spending leads to lost jobs which leads to even less spending; where an inability to lend and borrow stops growth and leads to even less credit.”

In this statement he did not console and reassure the world. Instead he stoked the fear of US consumer and the world. Perhaps this was simply a bold attempt to quickly force a multi-trillion dollar spending plan through Congress. And who spends money well? Not the government dear D.I. Not the government.

In his speech of 17 minutes, Mr. Obama was short on details. Will tripling spending on “Green Technology” in 3 years lessen our dependence on the Russians and their motley OPEC crew? Will placing all our medical records on computers in 5 years (cannot be done in a decade, believe me) save the economy? Will placing new light bulbs in 75% of government buildings make work for 200,000 Wall Streeters out of work now? In short individual freedoms will be stripped away by such massive and poorly conceived government spending. It is not true that “only the government “ can save the economy.

Historically, most government spending is a boondoggle and this one will be as well. Will tax breaks be spent or tucked away? Every dollar that government spends is a dollar that private industry does not spend. That is the key problem to solving this mess. While Mr. Obama and his minions (Larry Summers for example argued against regulation of the Investment banks during the Clinton years) propose this stimulus and use scare tactics to pass it, I am reminded of the \$700 billion Paulson TARP boondoggle which turned out to be a gift to the financial industry. What has that accomplished? We are running on the spot and badly deceived if we think that the government is the answer.

I am afraid the young Senator needs better handlers. Where is George Soros when we really need him? Kate says I must have some positives when I speak the end of the month in at the Cambridge meetings in Vancouver (Jan 24th through 26th). She says people want to hear positive things - that we are likely to emerge from this self-induced, global economic nightmare (which we are). Tell that to the incoming – but not yet, President. In the meantime I hope there will be snow on the mountains in Whistler when I am out there. Have a peaceful weekend.

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