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# CAPITOL MARKET REVIEW

A Global Margin Call on Sovereign Debt is Underway. Multiple Trades are Being Unwound. Global Central Banks are Straining to Keep Pace with Cross-Boarder Capital Flows

Into the Close: SPX 1229 US10Y 1.96% Gold \$1770 Oil \$95.94

Nov. 9, 2011

There is a global “margin call” underway. The spreads between Bunds, (German Sovereigns,) the Italian Sovereign, and other Eurozone Sovereigns has reached the point where Eurozone investors are being forced to pledge more cash to back the leverage they are using to bolster and hedge their existing portfolios.

Today’s action is a function of a global demand for liquidity most notably in the Eurozone where there is less liquidity every day.

In yesterday’s post, CMR noted that Italian sovereign debt had inverted, (wherein longer dated maturities are selling for less than shorter dated matured.) A negatively sloping yield curve is always a danger sign in credit markets. Today’s action is moving the longer end of the Italian yield curve sharply higher. However, as the curve struggles to again become positively sloped, the benchmark Italian 10Y Sovereign is now trading at 7.25%. CMR has maintained that Italy cannot fund its sovereign portfolio when rates are in the 6.5% – 6.75% range. A yield over 7.0% is flashing crisis. Today the Italian 10 Year Sovereign traded at 7.48% intraday.

The only reason the ECB is not meeting in emergency session is because calling an emergency meeting, might set-off an even greater panic, which would force additional global margin calls.

Bloomberg, Dow Jones, and a host of investment banking research are warning that things in the Eurozone are getting worse, not better. Reuters has even reported that there are discussions between Germany and France about establishing a multi-level Eurozone. One group of Member-States where there is a common taxing policy, currency and theoretically monetary policy, and another category for lesser nations. This is a remarkable turn of events, and for those with any sense of history, who would have conceived that Germany and France would join forces in this manner and without Italy? CMR is NOT predicting this will happen. However, Reuters has done an excellent job reporting on the Eurozone, and the fact that they published this story at all is stunning.

US stocks have been lower all day in a reflex trade. As the Euro declines the US Dollar strengthens and US stocks leveraged to the US Dollar are sold. In spite of the numbers the sell-off in equities remains within technical parameters. However, this cycle could break at any moment and many traders have already put-on what the Street calls “fat-tail” trades; these are trades that will quickly leverage down moves.

Due to global concerns investors have been rushing to the safety of US Treasuries. But US investors should not assume all is well here. Today, Fannie-Mae, (now a ward of the US taxpayer,) reported yet another loss and made a request for an additional \$7.8B in capital. Fannie Mae has reported losses in 16 out of the last 17 quarters and continues to hemorrhage money. CMR agrees with housing market analysts who have said that home values have not bottomed and that foreclosures will continue. Therefore so will losses at Fannie Mae and Freddie Mac.