



POTOMAC
STRATEGIC INVESTMENT

CAPITOL MARKET REVIEW

In This Issue: The Last Fed Day of 2011 Brings No Surprises, Credit Downgrades Still Pending for Eurozone, Equities Trading on Technicals with Little Volume

On the Fed News: SPX 1230 US10Y 1.95% Gold \$1647 Oil \$99.96 Dec. 13, 2011

Today marks the last Federal Reserve Open Market Committee Meeting of the Year. To no one's surprise, the Fed signaled that its zero interest rate policy, (ZIPR) will remain in effect through the end of 2012 and into 2013.

Language in the statement dealt with how the Fed intends to communicate policy changes in the future. And these changes were signaled in previous statements.

The only news on the wires today is the belief that regardless of what the Fed said in its statement, it intends to act if other central banks and sovereigns do not. If the ECB and Eurozone policymakers fail to reach an accord on the Eurozone debt crisis and the Eurozone experiences a credit meltdown, the Federal Reserve will immediately provide global liquidity in the form of US Dollars through aggressive quantitative easing.

Here are the key elements of the statement. The Fed still sees significant downside risks. The Fed sees the US economy expanding moderately. Previously announced "Operation Twist" remains in operation. Consumer spending is continues to advance, but at a slow pace. Unemployment will remain high. Remarkably, the only dissenter on the FOMC argued for more easing now.

On the news, stocks gave up their gains; US Treasuries remained stable at recessionary yields; gold sold off. Oil contracted only slightly due to geo-political risk from Iran.

The statement today is yet another reminder that Europe is holding the rest of the world's economies, as well as fiscal and monetary policymakers at bay pending a real action plan for Europe.

The broken record continues. The only clarity is a lack of clarity. There are many theories regarding ramifications for a Eurozone collapse. The problem is no one knows how bad it might be. And as was the case in the US credit-crisis, until markets re-price assets, its impossible to know how much capital might be required to solve the problem.

There are no measures of political risk on the tape. If there was such a metric it would be at an all-time high.