DAILY SURVIVAL GUIDE

BBG Tip of the Day: WBG <go>

WBG is the Economist's Big Mac Index. See what a Big Mac costs you from Bangkok to tha' Bronx.

Quote of the Day:

"This is a mess. This is a mess. I have listened here very carefully. I have heard things about curves, business practices. You make profits at one point then you don't make a profit. The bottom line is the people are being put out of their houses… I gotta tell you, something doesn't smell right."
– Rep. Elijah Cummings (D-MD), March 2009

MRA Daily: *Foreclosure-Gate* - Available via email and on our MRAD page on Bloomberg.

Flow Recap: http://www.macroriskadvisors.com/layout/pdf/20101008_FR.pdf

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Daily Risk Metrics

Below we summarize the performance of popular risk assets relative to the SPX and the VIX. We provide the changes in popular risk assets and how each has performed relative to the SPX and the VIX. We use a 20-day beta to the SPX and VIX to determine whether the asset has under or outperformed in the context of this beta. We view the band of "expected" performance as +/- one standard deviation.

Market Moves and Implied Volatility Moves
(Relative Performance Calculated Using 20 day Beta)

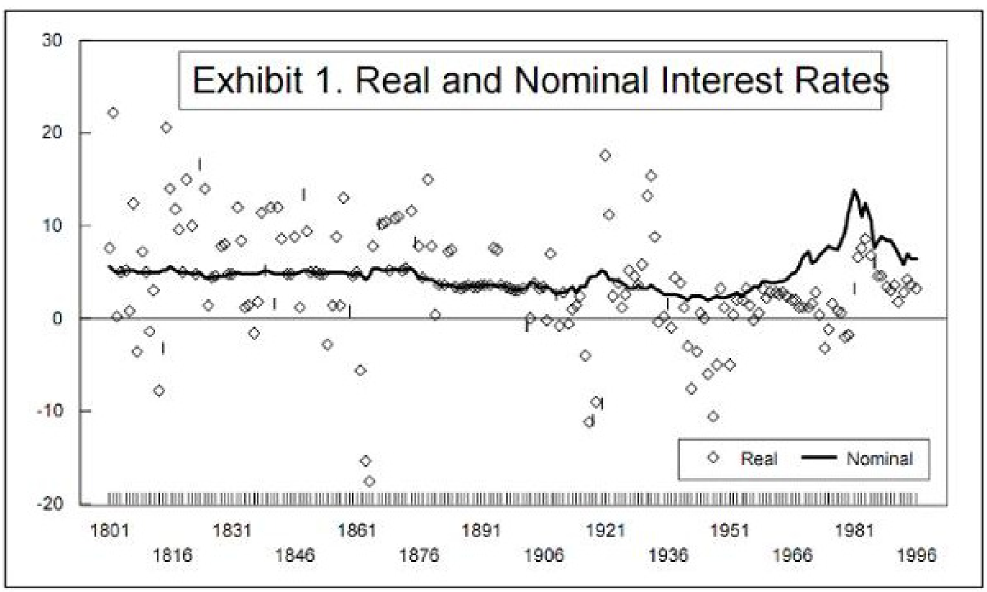
	Price	1d % chg	Out / Underperforming Relative to SPX
SPX	1158.06	-0.16%	
Crude	81.67	-1.87%	Underperforming SPX
Gold	1333.55	-1.15%	Underperforming SPX
Euro	1.3926	-0.03%	Expected
US 10yr Fut	127 5/32	0.04%	Expected

Implied Volatility	1m I-Vol	1d chg (pts)	Out / Underperforming Relative to VIX
VIX (S&P 500)	21.56	0.07	
OVX (Crude)	32.29	1.36	Outperforming VIX
GVZ (Gold)	21.43	1.59	Outperforming VIX
EVZ (Euro)	14.82	0.56	Outperforming VIX
US 10yr Fut 1m ATM	6.08	-0.06	Underperforming VIX

INFLATION DEFLATION

How low can Tips (yields) go?

FT points out that five year TIPS are now yielding -45 bps. How low can yields go? The article points to a research piece that shows real rates of -18% in 1861…So whose buying TIPS here? See the next article below…



Link: http://ftalphaville.ft.com/blog/2010/10/07/363201/how-low-can-tips-go/

INFLATION DEFLATION	**Pimco Scoops Up TIPS on Bets Fed Will Prevent Deflation** The WSJ reports that PIMCO is buying TIPS: > Pimco has scooped up Treasury Inflation-Protected Securities at a time when speculation has grown that the Fed will step up government-debt purchases, known as quantitative easing, to prevent the U.S. economy from falling into the deflation scare that has hurt the Japanese economy since 1990s. > "I have been a large buyer of TIPS over the last couple of months, and I am comfortable with my position here," said Mihir Worah, who manages Pimco's flagship $18.5 billion Pimco Real Return Fund, one of the largest TIPS funds by assets. > "The Fed has indicated that inflation is currently lower than where they want it to be. Hence, one of the goals of [quantitative easing] is to raise actual inflation as well as inflation expectations," Mr. Worah said in an interview. "Hence, TIPS benefit." > A closely monitored gauge of inflation expectations is the yield spread between TIPS and conventional Treasury securities, known as the break-even rate. On Thursday, the benchmark 10-year break-even rate traded at 1.90 percentage points, up from the recent trough of 1.47 percentage points in August, though still below this year's peak of 2.49 percentage points in January. Additionally, the WSJ reported on Sept 30th that the **Fed is also buying TIPS**: > If the Fed artificially forces down the yield on regular Treasurys through central-bank purchases and leaves TIPS untouched, it would make inflation expectations appear lower than they really are. That would run counter to the Fed's desire to push a higher rate of inflation. > Such inaction may lead investors to wrongly assume the Fed isn't supportive of the TIPS market. More worrisome, it could undermine investor confidence in the inflation-expectations signal, making the gauge less useful. > So the Fed is also buying TIPS, attempting to compensate one distortion with another. Tuesday, it bought about $550 million of TIPS. Yet gauging just how much to buy to make sure the relationship is exactly as it would be absent Fed purchases of any kind is an inexact science. Link: http://online.wsj.com/article/SB10001424052748704011904575538302857175696.html Link: http://online.wsj.com/article/SB10001424052748704116004575522301807274736.html
FED	**Kansas City Fed's Hoenig Still Wants to Raise Rates** Federal Reserve Bank of Kansas City President Thomas Hoenig speaks out against further stimulus, calling for tightening of monetary policy. This is not a surprise as Hoenig has been the lone dissenter in the past six meetings. From the WSJ article: > I don't think we should go that way at all." The official repeated his previous call that the fed funds rate should be raised off its de facto zero-percent level, saying, "I don't want high interest rates" and "I want non-zero interest rates." > Hoenig was speaking with a local group in Norfolk, Neb. In his comments, he also countered those who see little good in the economy right now. While he agreed labor

> markets are not doing very well, he argued that observers need to look at the longer term, saying "we continue to grow modestly" and there remains the strong chance the expansion will continue on that path.

The chart below of the implied Fed Funds target rates for the 9/2011 meeting, show that the market thinks the chances of no rate moves (or a rate decrease) one year from now are increasing.

Link: http://blogs.wsj.com/economics/2010/10/07/kansas-city-feds-hoenig-still-wants-to-raise-rates/

FED

Dallas Fed's Fisher Rebuts Calls for More Action

Federal Reserve Bank of Dallas President Richard Fisher, a non-voting member, also spoke out against further easing actions. From the WSJ article:

> The reality of fiscal and regulatory policy inhibiting the transmission mechanism of monetary policy is most definitely present and is vexing to monetary policy makers," Fisher said. "It is indisputably a significant factor holding back the economic recovery."
>
> Rather than the Fed intervening again in markets, Fisher said "the key is to remove or reduce the tax and regulatory uncertainties." Removing these headwinds would be "a far more desirable outcome than being saddled with a bloated Fed balance sheet."
>
> …
>
> Fisher also worried about that what appears to be a global tilt toward greater central bank action via asset purchases could be problematic. Citing "the specter of competitive quantitative easing," Fisher said "such a race would be something of a one-off from competitive devaluation of currencies, a beggar-thy-neighbor phenomenon that always ends in tears."

Link: http://blogs.wsj.com/economics/2010/10/07/dallas-feds-fisher-rebuts-calls-for-more-action/

FINANCIALS	**Europe Weighs Limits on Bankers' Pay** The FT reports that European regulators are planning tough restrictions on banker bonuses: In response to the EU legislation linking the size of bonuses to base pay, the draft regulations call on banks to set a maximum ratio between salary and bonuses. The acceptable ratio is likely to depend on each national regulator's view on whether a bank under their supervision is effective in linking pay to performance and risk. Such a ratio would force a wholesale restructuring of pay policies at many investment banks and almost certainly increase fixed costs because salaries would be inflated. Link: http://www.ft.com/cms/s/0/0adec5ca-d205-11df-965c-00144feabdc0.html?ftcamp=rss
FED	**Greenspan Says U.S. Creating `Scary' Deficit By Borrowing** Greenspan is back on the tape and with so much Fed-speak recently you knew he couldn't resist. From the Bloomberg article: Former Federal Reserve Chairman Alan Greenspan said the U.S. fiscal deficit is "scary" and the federal government needs to cut spending on entitlements. "We're involved in a dangerous game," Greenspan said yesterday at a foreign-exchange conference in New York sponsored by Bloomberg LP, the parent of Bloomberg News. "We're increasing the debt held by the public at a pace that is closing" the gap between our debt and "any measure of borrowing capacity," Greenspan said. "That cushion is growing very narrow." Link: http://www.bloomberg.com/news/2010-10-08/greenspan-says-u-s-engaged-in-dangerous-game-as-debt-deficits-increase.html
CHINA	**China Not Buying Yen** A Japanese Finance Ministry report released Friday showed that China actually sold 2 trillion yen ($24 billion) in August, essentially dumping most of the 2.3 trillion in yen it had purchases in the previous seven months of the year. China accumulated yen earlier in the year at a pace five times what it had in any previous year. When that trend became apparent, economists speculated that this was the beginning of China's move to diversify its $2.5 trillion currency reserves away from dollar Treasurys and into other currencies such as the yen. However, the report leaves open the possibility that China has once again been buying Yen the past 5 week and the second gray area is if China wasn't buying yen, would I have been even stronger in August? **Monthly Net Yen Purchases by China, in hundred-millions:** January 438 February 2,115 March 879 April 1,978 May 7,352 June 4,567 July 5,830 August -20,182 2010 Total 2,977

	Link to Japan report: http://www.mof.go.jp/bpoffice/ebppi.htm Link: http://blogs.wsj.com/japanrealtime/2010/10/08/actually-china-was-dumping-yen/
ECONOMY	**America's Fiscal Choices: Strengthening the Economy and Building for the Future** Video of Krugman, Feldstein and Hatzius from the Economic Policy Institute conference on October 5, 2010. Panelists represented a range of perspectives on how to facilitate economic growth, spur public investment and reduce the national debt. Link: http://www.epi.org/publications/entry/americas_fiscal_choices