Quote of the week : “In many ways, faith in the Federal Reserve today is roughly equivalent to faith in the words dot com in 1999" - John Mauldin - *if so, the consequences are far-reaching; for like any ordinary bank, the only **real** of the Fed is its credibility.*

Quote No. 2 of the week : “It was probably a mistake to allow gold to rise so high.” - Paul Volcker - *does he mean that the powers that be should have manipulated the price of gold or should have done a better job of manipulating it?*

Johyn Mauldin was one of two speakers at Wednesday’s Edmonton CFA Society Annual Forecast dinner (attended by 600+ people at $125 a pop). He certainly is an entertainer. One keypoint he made related to the “Unsustainability” of both consumer-, & government-, debt (he is bearish on the outlook for US government debt). A second point was that the world is in the midst of a currency war & that Japan will need a 12% **annual** Yen devaluation to achieve its 2% inflation target. On a third point, the outlook for the Eurozone, he seemed unduly optimistic; for there is little, if any, recent evidence that Churchill’s quote he had used earlier to good effect to justify his faith in America’s ability to eventually excavate itself from the hole it is in (“Count on Americans to do the right thing - after they’ve tried everything else”) can be expected to apply to Europe, *especially given the amount of political polarizing that’s occurring there (at both the national-, & supra-national-, levels)*.

During the Cold War era Germany, for reasons of security, stashed most of its official gold holdings in the vaults of the Bank of England & of France, and of the New York Fed. In the fall of 2012 the German Court of Auditors informed the Bundestag that this gold, over half the country’s official gold holdings, had “never been verified physically” & that 150 tonnes should be repatriated over three years to test its weight & quality. This raised this issue’s public profile to the point where in January 2013 the Bundesbank announced it would repatriate nearly 700 tonnes, over half of it from New York, so as to have half of its official gold holdings in its own vaults by 2020. Over Christmas rumours started flying in the blogosphere that in 2013 only 37 tonnes had been repatriated (& that the 5 tonnes thereof from the US had been found wanting in quality & identity).

Then, on January 16th Elke Koenig, President of Bonn-based BAFIN (the Bundesanstalt für Finanzdienstleitingaufsicht, German for “Federal Finance Supervisory Authority”) made a speech in Frankfurt in which she said, among others, “the possible manipulation of currency rates and prices for precious metals is worse than the Libor-rigging scandal”[1] (that has led to US$6BN in fines being levied on several banks - *chump change, however, compared to what JPMorgan alone has so far paid out in the US to in fines to regulators & reimbursements to injured third parties*). Also that this could be far more “politically serious because such reference values are based - unlike LIBOR ... on transactions in liquid markets and not on estimates of banks.” And finally, as to the growing number of investigations of market manipulations, “That the issue is causing such a public reaction is understandable ... (*for*) The financial sector is dependent on the common trust that it is efficient and at the same time honest.” This came after BAFIN last month interviewed Deutsche Bank employees as part of a probe of the potential manipulation of gold & silver prices, and the UK’s Financial Conduct Authority having earlier

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[1] This could be the opening salvo in a ‘Second Front” in a war ‘gold nuts’ have long been fighting against the US government’s alleged manipulation of the price of gold. If so, it could result in global pressure on the US to allow an independent third party audit of its official gold holdings, something that could be a lose-lose proposition for it.

launched a review of gold price benchmarks as part of a more broadly-based investigation into how rates are set (which in the case of gold will no doubt focus on the London twice daily gold price 'fix', during which there have for some time been price movements suggestive of skullduggery, as documented by Bloomberg last summer, to which the regulators should woken up long ago.

While on the subject of gold, the news is mixed. Most big banks, incl. Goldman & Credit Suisse, are bearish & attribute its YTD relative price strength to short-lived demand out of China associated with the start of the Year of the Horse[2] on January 31st. On the other hand Eugen Weinberg of Frankfurt-based Commerzbank AG says its price will "probably" rise to US$1,400 by year end as investors quit liquidating their gold ETF holdings & Asian demand remains strong (*the difference between them may well be that the former are short-, & the latter is long-, gold*). One US-based money manager commented "The gold bears ignore physical demand and think that gold is not relevant when there's no economic crisis.". On January 16th the assets of the SPDR Gold Trust, the biggest gold ETF around, hit a post-January 2009 low, only to be hit the next day with an influx of buyers that had it post the biggest daily gain in assets in over two years. Physical demand by retail end investors (as opposed to institutional speculators[3]) appears to be strong not just in Asia, but also in the US; thus last year the US Mint sold 856,500 troy ounces-worth of American Eagle gold coins, up 14%, the biggest YoY increase since 2011, as well as 42,675,000,000-worth of American Eagle silver coins, up 26% YoY, a remarkable performance in a year prices cratered & the experts almost unanimously trashed gold. And its coin sales were strong too in the first half of this month (amounting to 11% of **total** 2013 sales), as shown below[4] :

	2014 sales to January 17th	December 2013 sales	2013 sales to January 18th
$50 Gold Eagles	56,500	53,500	104,000
$25 " "	10,000	-	15,000
$10 " "	28,000	4,000	22,000
$50 Buffaloes	150,000	15,000	100,000
Silver Eagles	3,464,000	1,200,000	6.007,000

And it seems counter-intuitive that the price of gold should have weakened overnight January 20th (New York Time) after South Africa's AMCU (Association of Mineworkers and Construction Union) announced its members would down tools on January 23rd to back up their demand for a massive wage increase (*although that may have been the reason why the price of gold jumped 1.8% to US$1,260 on the 23rd starting at 0200 hrs New York Time - often is a time of price weakness -, albeit with over half of it coming in the two hours after New York's opening bell*) .

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2 The horse is deemed impulsive (*& impetuous*); so those born in the Year of the Horse are deemed prone to recklessness & well-advised to stay away from gambling & speculation. For everyone else it's a year not to expect to make much money & to value what one has.

3 Although they too appear to have turned more bullish recently; for at last report, according to the CFTC (Commodity Futures Trading Commission) the net-long open position of futures & options had increased for the third week in succession.

4 While the bears will point to the YoY comparison as proof of diminished demand, the MoM comparison may at this juncture be the more meaningful one.

And the last time the People's Bank of China (PBOC) reported its official gold holdings was in April 2009 when it said they totaled 1,054 tonnes. But according to Kenneth Hoffman of Bloomberg Industries' Precious Metals Mining Team they are today more like 2,710 tonnes (after adding 380 tonnes in 2012 & 622 tonnes in 2013). *The latter number is interesting; for while the previous years' numbers closely match China's (rapidly expanding) domestic gold production, & may have been a behind-the-scenes' way of subsidizing domestic producers, the 622 tonne number for 2013 is 50+% greater than China's newly mined gold production, suggesting that the PBOC accelerated its gold accumulating program in 2013 by buying gold in the market.*

The world of finance is changing. Wall Street has lost the Dodd-Frank war (with Goldman's latest quarterly earnings being down QoQ, & significantly so from five years ago, evidence thereof?); for the seemingly endless, & still waxing, string of revelations that Wall Street's & London's once much-hyped 'Masters of the Universe' had been little more than self-serving cheats & narcissists of little 'value-added' merit for the real economy gave US lawmakers little choice but to bite the bullet & the hands that have long fed them. In this context it's interesting that on January 16th Stephan Leithner, the member of the Deutsche Bank's 'management board'[5] responsible for personnel & legal matters, , told the German business paper Handelsblatt "If you don't have the necessary moral compass[6], you can't work for us ... Acceptance in society is a very valuable asset for Deutsche Bank", going on to say "some of our employees may have left to pursue transactions at other firms no longer possible at Deutsche Bank", *thereby insinuating that, while the bank had gotten the message, there were others who still haven't.*

Standard & Poor's aggregates on an ongoing basis analysts' earnings' forecasts for its S&P 500 stocks. While at yearend this had generated US$106 for 2014, up 6.6% YoY, two weeks later it had jumped 13% to US$119.70 (implying 20+% higher earnings in 2014). Might this be a function of 'irrational exuberance'? For annualized 20+% S&P 500 earnings growth occurred in just 15 of the 79 calendar quarters to September 30, 2013, five of them after the nine quarters of negative earnings growth ended December 31st, 2009. A 2010 McKinsey study found that in the 24-year period 1985-2009 January 1st analysts' earnings' estimates for the new year had overestimated the eventual outcome in all but five years (they had been low in 2005 & 2006, and spot-on in 1988, 1995 & 1996). Last year S&P 500 earnings grew by 8% while the S&P500 Index was up 30%; so most of the rise in the Index was due to 'valuation adjustments', i.e. the ratcheting up P/Es, rather than earnings growth. BankAmerica just published the results of its recent a survey of global fund managers; it had found the % believing US stocks overvalued to be at a post September 2000 high (in line with a Goldman note to clients last week saying equity valuations are too high). Finally, US corporate earnings as a share of GDP are not just at an all-time high, but way above their historical range (& averages more often than not regress back to their mean) *although that may be partly attributable to more US corporations generating more of their profits from their foreign operations.*

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5 In Germany all major companies have two boards : a Supervisory Board, half elected by shareholders & the other half employee representatives, which appoints a Management Board to be responsible for the day-to-day running of the business, subject to the approval by the Supervisory Board of all its major business decisions.

6 While said to mean "being honest & putting clients' interest first", it remains to be seen what the real world outcome would be when 'the rubber hits the road'.

Since last summer the world's largest seven currency trading banks, that control almost 70% of the global FX market[7], have, pending the regulators' ongoing investigations of the past manipulation of FX markets, fired, suspended or put on *unpaid* leave at least 17 of their senior currency traders

At Davos Japan's Prime Minister Shinzo Abe compared the current tensions between his country & China to those between Britain & Germany pre-WW I, saying that the fact they had a strong trading relationship didn't prevent the outbreak of WW I (more & more well-informed Chinese living abroad are beginning to think that war between to the two is becoming more & more likely, if only because their two peoples seem to increasingly hate each other.

Zhu Tian, an economist at the China-Europe International Business School in Shanghai claims China's consumption is not as low as generally believed because many consumers routinely get their employers to buy things for them.

During, & after, the financial crisis, Moody's was the only of the three big ratings agencies to cut Ireland's bonds to junk status. But on January 17th it hiked them from Ba1 to Baa3, i.e. investment grade, &, what's more, with a positive outlook. The yield on Ireland's promptly fell 17 bps to 1.625%, down from 18% a few years ago at the nadir of its fortunes & the lowest level in the Republic's 92-year history, and through the 1.709% yield on five year UK bonds &, albeit by the thinnest of margins, that on five year USTs. Nevertheless, those who say this makes Ireland a success story are likely a bit rambunctious in their assessment; for there is still a lot of pain on Ireland's Main Street & many of its young and/or well-educated people are leaving.

Exactly one year ago the French-born Chief Economist of the IMF, Olivier Blanchard (who has spent his entire career teaching in the US, first at Harvard, but mostly at MIT), warned the Cameron government that austerity could plunge Britain into recession. But on January 22nd he 'ate crow' when he hiked his 2014 GDP growth forecast for Britain to 2.4%, the largest upgrade of any major Western economy. Meanwhile, in preparation for next year's general election Prime Minister Cameron replaced Chancellor of the Exchequer George Osborne with Australian Lynton Crosby as his political strategist. While most see this as a good move since Crosby is seen as being less manipulative & having a clearer political mind than Osborne, and since this will give the latter more time to devote to his role as Chancellor, Osborne not surprisingly doesn't see it that way, especially since Crosby advocates an election strategy quite different from the one he had been pushing.

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NEW WARNINGS FROM AN INVESTING PIONEER (WSJ, Jason Zweig)

- Dean LeBaron was a pioneer in the early US professional money management business. He founded Batterymarch Financial Management in 1969, invested in small cap stocks when no one else did, pioneered quantitative investment (using computer-driven analysis rather than human judgement to pick stocks), was among the first to offer index funds & invest in farm land, and was an early investor overseas, incl. from 1987 in

[7] Deutsche Bank with a 15.2% market share, Citi with 14.9%, Barclay's (10.2%), UBS (10.1%), HSBC (6.9%), JPMorgan (6.1%) & Royal Bank of Scotland (5,6%).

the "Third World" countries & not long after in the early privatization of Russian state-owned companies. In 1995 he sold out to Legg Mason. Today, at age 80, he just manages his own money, with his strategy being to "follow the *Chinese* money into Africa, Canada & Mexico" & his objective less to make money than to "lose as little ...as possible." For "If we are in a transition world, then the person who is in the most danger is the one who has recently done well." He believes the central banks' easy money policies have created "administrative markets" with prices affected more by government policies than by market forces.

There is lots of 'corporate memory' in these old financial 'bull elephants' of those who, after harking to the siren song "this time it's different", got their heads handed to them.

<u>NO NEGOTIATIONS ON DEBT LIMIT</u> (Politico, Seung Min Kim)

- Later today, January 24th, Senate Budget Committee Chair Patty Murray (D.-Wash.), who earlier negotiated the spending bill deal with Rep. Paul Ryan (R.- Wisc.), will release a letter saying the Democrats will heed no GOP demands in exchange for raising the debt limit next month, & more specifically "We will not negotiate over whether the United States of America should pay its bills ... And once again before they get further down this damaging path we call on our Republican colleagues not to play politics with our economic recovery."
- But a spokesman of House Speaker John Boehner (R.- Ohio) already said, in response to a letter by Treasury Secretary Jack Lew earlier this week urging the law makers to deal with the debt limit issue by the February 7th deadline & telling them that his ability to keep paying the nation's bill with 'extraordinary measures will be exhausted by late February, that there zero chance of a "clean" debt limit bill passing the GOP-controlled House & on January 23th Rep. Paul Ryan told a San Antonio audience that the Republicans are discussing potential points of negotiation in the debt limit issue.

Among the latter is approval of the Keystone XL pipeline (which, if they don't make it a key demand, will make it that much more likely not to be approved in the end). Be that as it may the world better be prepared for another game of 'silly bugger' on Capitol Hill.

<u>PIMCO'S EL-ERIAN RESIGNS AS HODGE NAMED CHIEF EXECUTIVE</u>
(BB, Alexis Leondis)

- On January 21st Munich-based Allianz SE, the world's largest insurance company, announced Mohamed El-Erian, age 55, CEO & Co-CIO of its Newport Beach, Cal.-based subsidiary PIMCO will relinquish his posts in mid-March. In an email to employees El Erian said "The time has come for me to step down ... What happens longer term is an open question. I have no plans now." He will be replaced as CEO by COO Bill Hodge (who didn't come up the investment side of the business; so this creates a clear split between operations & money management) & as Co-CIO by two Deputy CIOs, Daniel Ivascyn (who runs a fund that over the past three years outperformed 99% of its peers & was recently named Fixed Income Manager of 2013 by Morningstar), and London-based Andrew Balls (whose funds' performance was only mediocre but whose brother, Ed Balls, is the Labour Treasury critic in the House of Commons). This will leave PIMCO founder Bill Gross, who twittered "PIMCO is fully engaged. Batteries 110% charged. I'm ready to go for another 40 years" (*which seems unlikely since he is 69 years of age*), in total control of the business.

- El Erian is Egyptian by birth, has undergraduate-, & graduate-, degrees in economics from Oxford, and a Ph.D. from Cambridge *& since December 2012 has been Chair of Obama's Global Development Council*. He is fluent in English, French & Arabic, worked for the IMF for 15 years to 1988 &, after a stint as a Managing Director at Citigroup in London, joined PIMCO in 1999. From there he went to run the Harvard Endowment Fund (where had good results) only to have Gross in 2007, after two years at Harvard, bring him back to PIMCO since, as he told Bloomberg in 2010, "Mohamed could fill an important part of the puzzle in planning my succession." Upon his return he became responsible for diversifying PIMCO away from the bond business which proved problematic. Last year PIMCO had a truly ghastly year with US$30.4BN in net redemptions (incl. US$41BN from in its flagship, & Gross' 'marquee', US$237BN Total Return (bond) Fund (vs. US$62.7BN net inflows in 2012) *as higher bond yields, & lower bond values, made clients restless.*

He will, however, remain on as a member of Allianz's International Executive Committee, advising it on global economic & policy issues & reporting directly to 60 year-old CEO Michael Diekman. While this has given rise to rumours he might in due course succeed Diekman, there are those who pooh-pooh the idea given his inability to speak German. But he will be "hot property" & his fluency in English, French ***and*** *Arabic may be more of an asset than his inability to speak German is a liability. And, if that icon of German high finance, Deutsche Bank, can have a CEO of Indian origin, it wouldn't be a big step for Allianz to have an Egyptian-American at the helm; it will likely all depend on what Diekman comes to think of him when he has him working directly for him.*

<u>ANGER AND APPLAUSE FOR PM AT KNESSET</u> (CP)

- In the first ever address by a Canadian Prime Minister Stephen Harper told it that those who oppose the Jewish state are "little more than hateful anti-Semites"[8], earning him several prolonged ovations. But two Arab-Israelis MKs walked out when he attacked the "twisted logic" of those who compare the Israeli situation with South Africa's apartheid regime.

Netanyahu & he had a love-in. At one point the former called him a "Canadian rock star" which prompted Harper to belt out a few lines from a Beatles song. Some of the rest of his time there was spent getting an honourary doctorate from the University of Tel Aviv (where in response to a question he said he had not been elated by the Arab Spring in Egypt & had welcomed the stability following the ouster of President Morsi), & laying the cornerstone at a visitor centre named after him at a Hula Valley bird sanctuary. And he did find time for a perfunctory visit to Mahmoud Abbas in Ramallah & a longer one to King Abdullah of Jordan whom he promised $105MM over five years in new aid. Meanwhile Netanyahu c.s. cheerfully ignored the fact that, at least until recently, the Department of Foreign Affairs had called the West Bank, East Jerusalem & the Golan Heights "occupied territories", and the settlements & The Wall "illegal".

<u>LEAKED RECORDS REVEAL OFFSHORE HOLDINGS OF CHINA'S ELITE</u>
(The International Consortium of investigative Journalists, Marina Walker Guevara)

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8 In all fairness to him, however, he also said that, while criticism of Israeli government policy is not anti-Semitic, criticism that only targets Israel, & ignores violence & oppression in its neighbours is unacceptable.

- It took journalists from Hongkong's Min Pao newspaper, Taiwan's magazine Common Wealth & Süddeutsche Zeiting (as well as an unnamed Mainland China news organization that partway through had to withdraw after being warned off by the authorities) months to go through 2½MM files purloined from Singapore-based Portcullis TrustNet & BVI-based Commonwealth Trust & come up with the names of nearly 22,000 tax haven clients with Hongkong and/or Mainland China addresses (a task complicated by the fact that many names were entered in Romanized lettering, rather than Chinese calligraphy. But what a haul it was; it didn't just include 15 of China's richest individuals, members of the National People's Congress & SOE executives, but also Deng Jiagui, the brother-in-law of current President Xi Jinping, Hu Yishi, a first cousin of former President Hu Jintao, Wen Yunsong & Liu Chunhang, the son & son-in-law respectively of former Premier Wen Jiabao, Li Xiaolin, a daughter of Li Peng (Premier from 1987 to 1998) & Wu Jianchang, son-in-law of the *legendary* one-time Supreme Leader Deng Xiaoping.

In a way this is not news; for back in 2005 already Xinhua, of all people, had reported on Chinese individuals & companies using the BVI as a tax haven. Be that as it may, with such a lineup of illuminati with potentially "dirty hands" (Xi Jinping's recent choice of words), he & anti-corruption czar Wang Qishan will have their work cut out for them if they are serious about rooting out corruption(& might want to watch their backs as they go about doing so).

MEGA DEFAULT INCHINA SCHEDULED FOR JANUARY 31 (Forbes, Gordon G. Chang)

- On January 17th Chinese state media reported China Credit Trust had warned investors in one of its Wealth Management Products (WMP) that *required a minimum investment equivalent to US$496,000 & that* matures on January 31st, the first day of the Year of the Horse[9], that they may not be repaid. The "2010 China Credit - Credit Equals Gold #1 Collective Trust Product" had been marketed by the ICBC, the world's largest bank by assets, to its customers in Shanxi Province. But in a January 16th phone interview with Reuters the bank suggested "a situation completely does not exist in which ICBC will assume the main responsibility."[10] The reason for this impending default is simple : China Credit Trust lent the entire 3.03BN yuan (US$496MM) proceeds to Shanxi Zhenfu Energy Group, a coal miner that has declared bankruptcy with 5.9BN yuan in liabilities & 500MM yuan in assets. While in recent years there have been other WMP defaults, investors have always been "made whole", albeit sometimes from "mysterious sources". And right now there is at least one other WMP in trouble; one packaged by Jilin Trust & marketed by the China Construction Bank for the Liansheng Resources Group, another bankrupt Shanxi coal miner, with things shaping up as if investors will take at least a partial hit.

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[9] One feature of which supposedly is, seemingly rather appropriately, that you should 'not expect to make a lot of money but value the income you have'.

[10] But since then there have been two significant developments : a group of angry investors descended on the ICBC and rumours have started making the rounds of a possible deal in the making with the ICBC & China Credit Trust each contributing 25%, and the government Shanxi Province contributing 50% to a bailout fund (without any detail, however, as to whether there would be 100% recovery & if interest owing would be paid).

There are an estimated 11TR yuan (approx. 20% of GDP) in WMPs outstanding. This could become China's sub-prime crisis moment. But Beijing may find it easier to deal with because its political system is autocratic, rather than democratic, and because it will have the benefit of America's experience in dealing with it. That being the case, it may well try & use these companies as Washington used Fannie Mae & Freddie Mac, i.e to lower investor expectations that the government will always bail out investors[11] *(Shanxi Province is located to the West & Southwest of Hebei Province, which surrounds Beijing), & holds one-third of China's coal reserves. While way back it was a stronghold of the Communist Party & of the forerunner of the PLA, today it is among the most polluted of China's Provinces, has a below-average per capita GDP, and its population is a mixture of dirt-poor coal miners working under often appalling, if not deadly, conditions & rich coal mine owners who are among the most influential pressure groups in Beijing.*

95 TORY BACKBENCHERS[12] DEMAND CAMERON CHANGES LAW TO GIVE COMMONS THE POWER TO BLOCK EU LEGISLATION (Daily Mail)

- Their open letter drafted by MP Bernard Jenkin[13], a senior MP, says that, as recommended last month by a committee of MPs that scrutinizes EU laws & *regulations*, Parliament should pass a law to block anything emanating from Brussels that is against the "national interest" (at present the Prime Minister can only exercise a veto on defense & the budget). It says in part "Each time you have stood up for British interests in Brussels you have achieved a great deal[14] ... Building on your achievements , we would urge you to back the European Scrutinizing Committee proposal and make the idea of a national veto over current and future EU laws a reality." And it praised him for his insistence that national parliaments, not bureaucrats in Brussels , are the "true source" of democratic legitimacy in the EU.

This came three days after Viviane Reding, a Luxemburg citizen who is EC Vice President as well as EU Commissioner for Justice, Commission & Citizenship, attacked Cameron for urging other European leaders to curb immigration & "telling lies" to win votes to the detriment of the British people, and for saying immigrants were 'exporting' UK child benefits all over Europe. More specifically, she said "The supposed invasion by people who want to take advantage of the social security and health (benefits) is an invention of politicians who like to have populist movements in order in order to win elections." And while Cameron has gone on record as saying tackling immigration from Europe would be a key demand of his plan to renegotiate Britain's EU membership prior to an in-or-out referendum on the issue in 2017, Reding wants a United States of Europe & maintains "freedom of movement (within the EU) is not up for negotiation.". The back benchers faces an uphill battle. Deputy Prime Minister Nick Clegg, head of the Liberal Democrat Party, the Conservatives' junior coalition partner (with 56 MPs to their

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11 Ahead of the proposed introduction of a deposit insurance scheme.

12 With six more said to be supportive but unable to sign since they have government jobs, which would have their number account for exactly one-third of Cameron's caucus.

13 Who believes that, as things stand now, the Conservatives is at risk of losing as many as 50 seats to UKIP (that wants to get out of the EU altogether) in the next election.

14 Thus he succeeded last year in having the Council of Europe cut the next seven years' budget by 8% from that proposed by Brussels, the first ever that has ever happened.

303, & the Labour Party's 256), opposes the idea. Chancellor of the Exchequer George Osborne says Britain would be better off inside an, albeit reformed, EU. Foreign Minister William Hague says it would make the single market "unstable" (& his German & French counterparts respectively that "the UK cannot 'cherry pick' EU benefits" & that the UK leaving would be dangerous for both but that there cannot be "a Europe à la carte.") On the other hand, Justice Secretary Chris Grayling has demanded "a completely new relationship with the EU" and former Conservative Party Treasurer , businessman Peter Cruddas says that "Europe has to change ... after two decades of misrule." All this is playing out against the background of next September's independence referendum in Scotland (which if successful would undermine the Labour Party's position in Westminster), the general election in Britain scheduled for May 2015 (that could see losses for both Conservatives ***and*** *Liberal Democrats), & the referendum on EU membership notionally scheduled for 2017.*

<u>JPMORGAN SAYS BVG OWES IT $200 MILLION</u> (BB, Kit Chekel)

- BVG (Berliner Verkehrs Betriebe, German for the Transport Enterprise of Berlin) has run the German capital's trains & buses for 30+ years. In 2007 it entered into a transaction with JPMorgan in which, in return for an upfront US$7.8MM payment, it undertook to pay it up to US$220MM in case of a default by certain third party entities. Unfortunately for BVG, Lehman Brothers was one of the latter; but when JPM came looking for 'its' US$204MM, BVTG wouldn't pay up & JPM sued. After three years of court battles about where the suit should be heard (BVG wanted Germany & JPM London), in 2011 the European Court of Justice ruled in JPM's favour & their expected ten week court fight has started in London.
- BVG contends it was misled by JPM, that its staff misunderstood "the complex" credit derivative & had no experience in such a transaction, and that Clifford Chance[15], the law firm that had acted for both parties, had been in a conflict of interest. On the trial's first day JPM's lawyer told the court that "rather than simply accepting that it had been unfortunate ... (BVG) cast around for someone other than itself to blame, that the chance of any default for the underlying portfolio had been 0.19% when signed ... and that taking on a small risk, even a vanishingly small one, is not the same thing as taking no risk at all."

This trial is attracting more than the usual attention; for it is only one of many similar law suits waiting in the wings & the outcome could set a precedent. And while ignorance is no excuse, & one must wonder how anybody higher up in BVG's chain of command could ever have condoned such an outright gamble (even though that was a sign of the times), two considerations might swing the outcome. One is that anyone with any knowledge of the securities business knows securities are typically "sold" rather than bought (& the JPM sales staff may have seen the BVG staff as "rubes" ready for plucking), and the other that one must wonder why a sophisticated financial operator like JPMorgan would be prepared to pay a 3.5% upfront premium to 'lay off' a 0.19% risk.

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[15] A multinational law firm headquartered in London, it has 35 offices in 25 countries & is among the world's largest ten law firms by revenues (US$1.7BN) & number of lawyers (3,400).