

## BAD LANDS



An Ill Wind Blows  
Through the US Mortgage Market

| Edited by Gregor Macdonald

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## BAD LANDS

The debtor-class is getting restless. Armed with the emergent knowledge that the foreclosure process might be fraudulent, community activists are springing up across the nation to prevent people from being evicted from their homes. Meanwhile, that may be the least of problems for the creditor-class. Securitization itself is under attack, for a wholesale breach of property law. A nation of bad Titles makes for Bad Lands.



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## A NOTE FROM THE EDITOR

Welcome to StockTwits Macro Weekly, the weekly magazine of the StockTwits investment community. Each issue features a core essay, written by the Editor. Around this, we build in the key news events and observations, from the past week. [To have each issue sent to you, sign up here.](#)

You will also find StockTwits Macro Weekly functions as a live document, that is eminently clickable and is therefore a helpful launching pad to other relevant content. Feedback from readership is welcome, and we are always on the lookout for written contributions from the community: [gregor@stocktwits.com](mailto:gregor@stocktwits.com)

**BADLANDS**—An experienced property law attorney was once known to have said: “If you place a document on record at the Land Court declaring the moon is made of English Stilton, it does not make it so. However, at least a few people may have to research the matter, and make sure the document does not relate or affect an existing piece of land.” The observation is meant to convey that, although real estate law is not exclusively a triumph of form over substance, because of the nature of property law and titling of land such a system cannot operate along the contours of *intent*. This fundamental truth, that large property systems are synonymous with the letter of the law has been a very tough, intellectual concept for the New York financial press to “get its head around” the last few weeks. This is why, in typically American fashion, a rather [serious and emerging problem](#) for the nation’s financial system was once again downplayed in its earliest phases by the media. However, despite the hubris and snark of claiming that the foreclosure and securitization fiasco only represented a paperwork, not an economic problem, the magnitude of the situation finally worked its way into bank stock prices last week. In addition, analysts who actually understand the problem, such as Chris Whalen of Credit Risk Analyst who was [eloquent in his own explanation](#), also stepped forward and elevated the debate. In short, anyone who has had experience in property law knows that the system itself is not viable unless it can operate with a high level of exactitude. Periodic, small errors can be tolerated by such systems, and ultimately fixed. Allowing a conveyor-belt of foreclosures to take place by claimants who have neither title nor standing cannot. The implications are enormous.

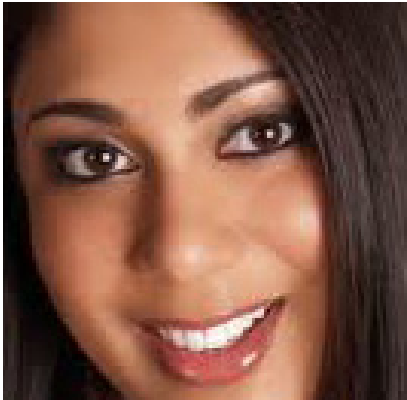


There are social implications as well. Last week, on the heels of spreading awareness about the legality of bank foreclosures, [groups emerged in cities such as Boston](#) that expressed a new

## Indexes

INDU 11132    TNX 2.56    GOLD    VIX 18.78    SPX 1183.08    DXY 77.392

## StockTwits.TV: Forex AM w/ Raghee Horner



Here in the midst of the global currency wars, it makes sense to check in with Raghee Horner and the entire [StockTwitsFX](#) team. This space provides excellent coverage

We go to press just as the G20 meeting in South Korea has come to a close. The outcome was predictably weak-willed, with participating nations agreeing to “refrain” from using their currencies as a way to cure imbalances.

You should watch the way Raghee handles the approach of these issues earlier in the week. Was Treasury Secty Geithner's tough talk on the USD, just for show? Did the PBOC rate hike really change the USDollar's downtrend? How far would the Australian Dollar correct downward, before resuming its uptrend? Raghee's discussion of all these currencies is sharp, and prescient, as she lays out the key probabilities. [Watch the show here.](#)

[StockTwits.TV](#) can also be taken as an iTunes subscription.

defiance of foreclosure. Lest more the more skeptical think such [Stand Up, Fight Back](#) movements are a flash in the pan, Chris Whalen wisely remarked that they were *inevitable*. Indeed, Whalen (in the above linked interview) went one step further and said that states would eventually halt foreclosures to preserve their stream of revenue from property taxes. But there may be other incentives for states to halt foreclosures. At some threshold which would be hard (but not impossible) to define, waves of foreclosures present a social problem for communities, ripping the fabric of neighborhoods and crushing the flow between demand and provision of municipal services. Whalen seems to be suggesting a new competitive phase, in which different parties scramble for what little spending ability remains among the nations' underwater homeowners. Currently at 23%, and surely going higher, the percentage of homeowners underwater already represents a threshold problem for the aggregate creditor-class, on the other side of that debt. The day of debt-reckoning has not yet come, but it's finally approaching.

Incredibly, the asset class that the nation's pension funds and institutions have crowded into the last few years has of course been *credit*. But whether its further declines in state tax revenues affecting municipal bonds, commodity inflation affecting corporate credit, or, lack of economic recovery affecting consumer debt, it appears the big money is now fully crowded into the next riskiest asset class. Pension fund exposure to equities has been cut from [70% to 45% in just the last five years](#). The shift in capital has not reassigned to commodities or gold bullion, but rather in credit, which is clearly reaching a new herding phase. That makes for a nice positive feedback effect, as the price of credit rises thus attracting more institutional flows. Of course, against commodities, credit is losing its purchasing power. Also, we appear to have entered a new era--a truly new era--in which *interest rate risk* has not only been forgotten. No, interest rate

risk apparently no longer exists, having been wiped from the hard-disk of money-management's collective memory. How pleasant it must be to not have to think of unpleasant things.

Let's consider, then, the various unpleasantness that could be visited on the financial system in the next twelve months, as a result of the mortgage fiasco. First, there are MBS investors who will sue the dealers of the securitized mortgages. That trend has already kicked off with the [PIMCO, NYFED, BlackRock lawsuit](#) against Bank of America's Countrywide (former) unit. Second, there is the *vicious rebuttal* to the foreclosure process that is about to blow back from the court system to the foreclosure mills, banks, and claimants. [Don Coxe](#) (and other others who have made this point) is absolutely correct that the court system takes fraud upon *itself* as a deadly serious matter. This is the lever which gets to the third, and final force coming for the banking system: local, community action with the aid of organizers, lawyers, [activist groups](#), and possibly even local governments. There is also an array of other headaches that trail along behind this looming quagmire. For example, it's going to be a problem to get any Title Insurance company to write insurance on property if foreclosure occurred by a claimant not in possession of the original Promissory Note. Second, the entire investor class that's been buying up REOs from drylands in economically shell-shocked parts of California, to sunscapes in Florida are also likely to recoil from the market. It is intriguing, to say the least, to imagine what a [halt to the entire foreclosure process](#) would mean. More broadly, this all adds up to some form of repudiation. Debt Jubilee, if you will.

Despite the historic expansion of the FED's balance sheet, the entire OECD financial sector is still carrying massive loads of unpayable debt. Debt collection and foreclosure makes economic sense when some other, larger portion of

## New Arabica High



Arabica Coffee in New York last week finally crossed the two dollar mark to [settle at \\$2.01 per pound](#), a 13 year high. This is a full 10% higher than six weeks ago, when StockTwits Macro Weekly took an in-depth view of world coffee markets in [City Roast](#), (5 September 2010). On the back of huge imbalances that emerged late last year coffee prices have been on the move throughout 2010. But even as late as this Summer, global prices had apparently not moved far enough to price in falling production and low inventories.

Lurking behind the prices posted at the commodity exchanges however is that the modern coffee market of estate grown, high-end consumption is now almost completely untethered from the grade of coffee that's traded at the exchanges. Current futures contracts are deliverable with bags from storage: [low quality/long-stored beans not up to current standards](#). As a result, a large portion of the contemporary coffee market are left with only imperfect hedging. Perhaps it's time for a new benchmark or even a new exchange, perhaps located on the West Coast. Seattle JO-X?

### China's Silver Experience



One year ago the Chinese government ran TV promotions, encouraging citizens to buy silver. That story was covered in the [www.gregor.us](http://www.gregor.us) post: [The Chinese Silver Down-load Experience](#). The government effort appeared to be a method to effect broad distribution of bullion, throughout the Chinese economy. But what was its purpose?

A year later, the story makes a lot more sense. Washington has gone to war against Beijing's CNY-USD peg by devaluing the dollar, thus putting extreme pressure on China via the lever of commodity inflation. What has China done in response? Well, threatening to halt or slow exports of rare-earth metals has been one way Beijing has met the attack. The other response has been to do what others are doing in the bullion markets: accumulate more.

Word comes that China is now [re-straining exports of silver](#), by as much as 40%. Perhaps another year of dollar devaluation has convinced China that during a time of Currency War, getting purchasing power into the hands of the people is an effective tactic to smooth the pressure from upwardly volatile inflation.

the economy is proceeding normally, and is therefore able (and willing) to infuse distressed property with the cure of its own health. That's no longer the case in the US housing market, which is not recovering in the midst of an economy which is also not recovering. In other words, systemically, there is no one to sell foreclosures to. What we have instead is a market that's operating as though losses will not be fully realized, supported by a government-banking complex that's trying to shield the creditor-class from inevitable losses. At some level of foreclosure, therefore, the debtor-class will take matters into its own hands, triggering the debt jubilee that the system will have to face regardless. We appear to be getting closer to that phase now.

--Gregor Macdonald, 24 October—Amherst, MA

### ~Chart of the Week~

Barack Obama's Quarterly Job Approval Averages



Gallup Daily tracking