

UNDERSTANDING LIQUIDITY

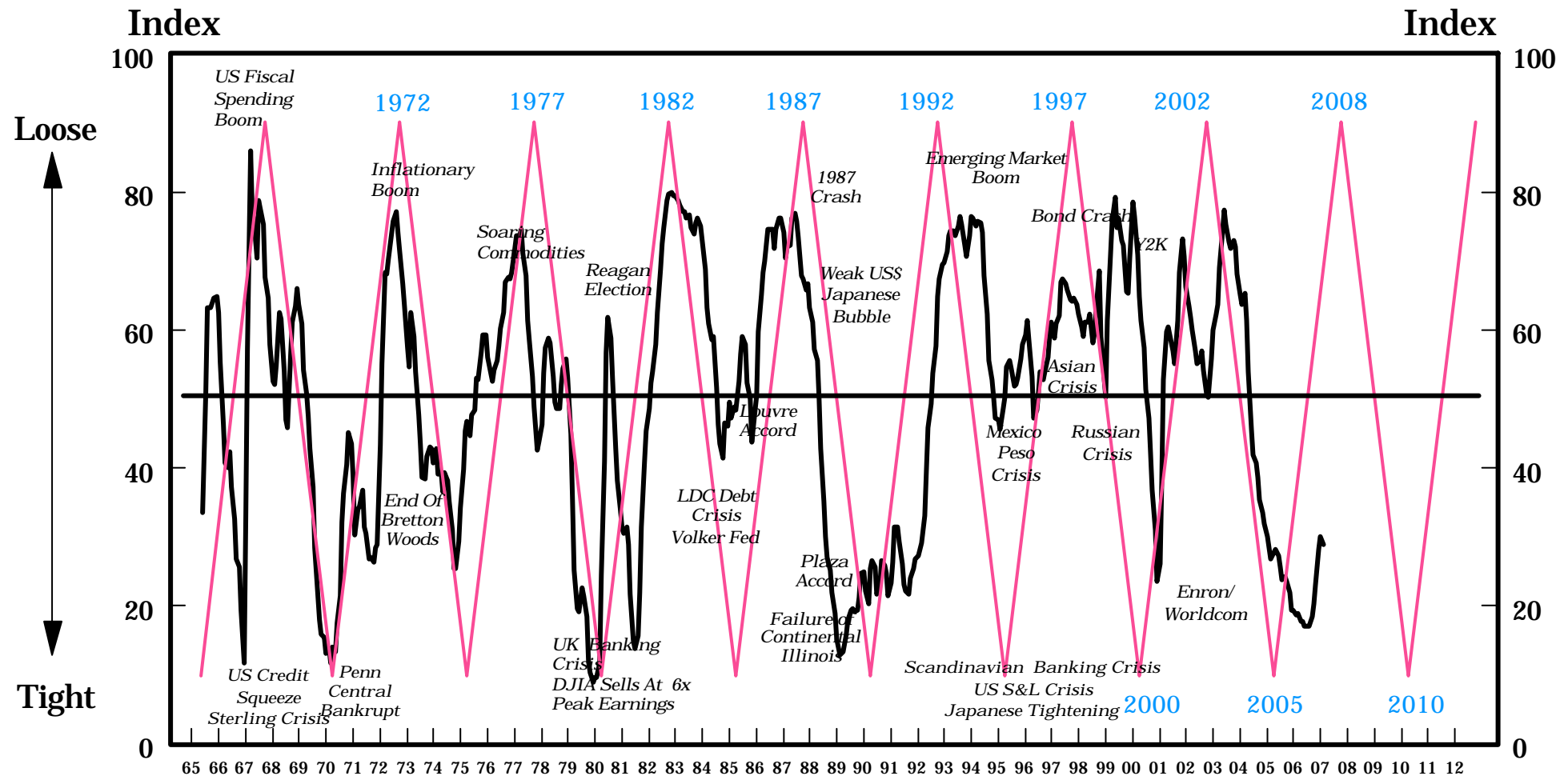
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March 2007

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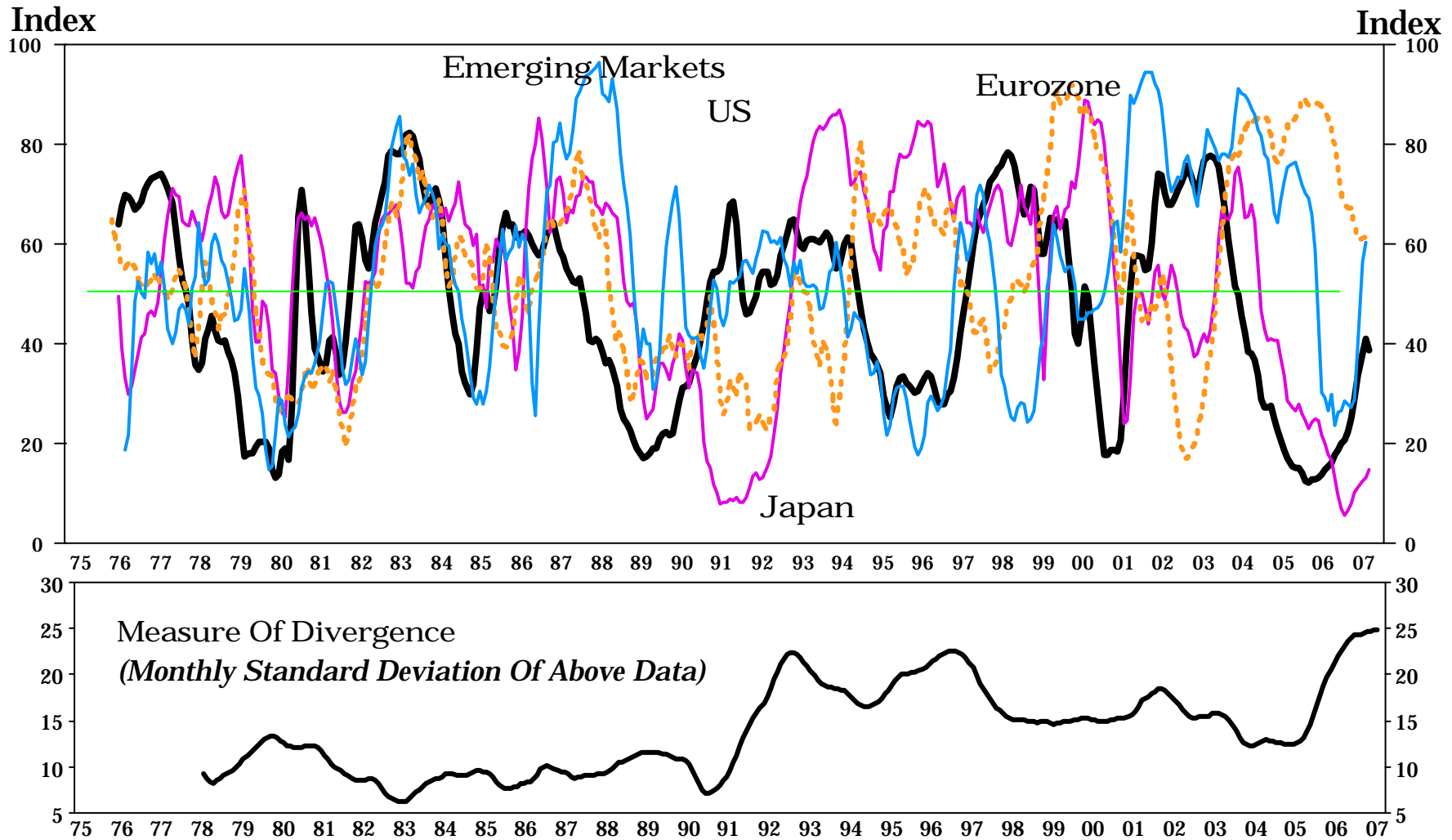
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A Regular Pattern: Global Liquidity Cycle And Theoretical 5-Year Cycle

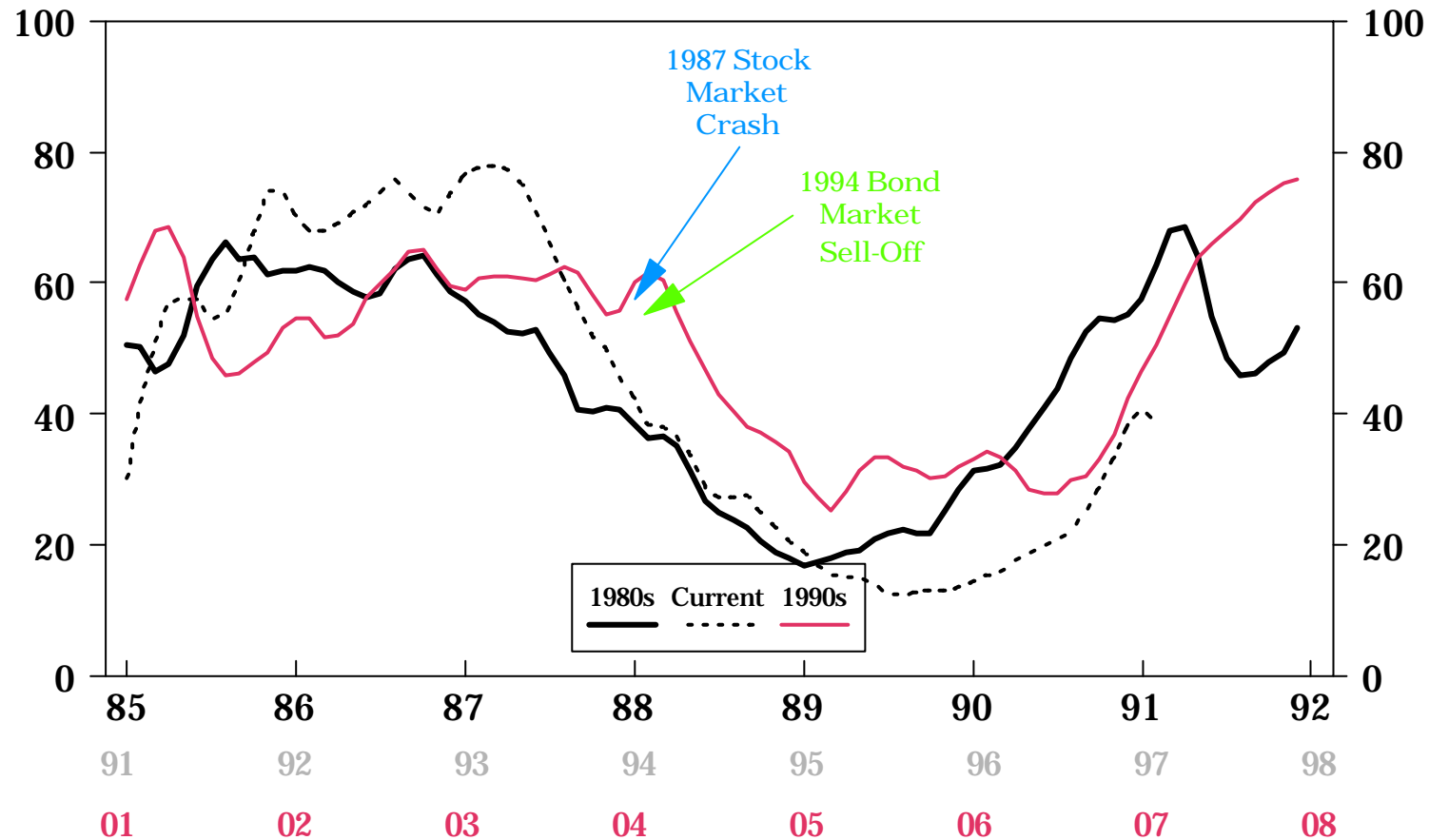


Liquidity - Tight Or Loose?

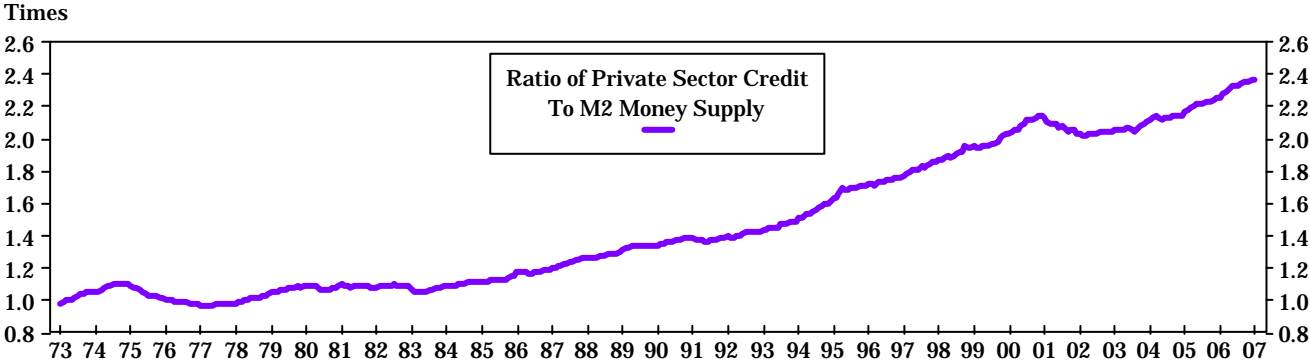
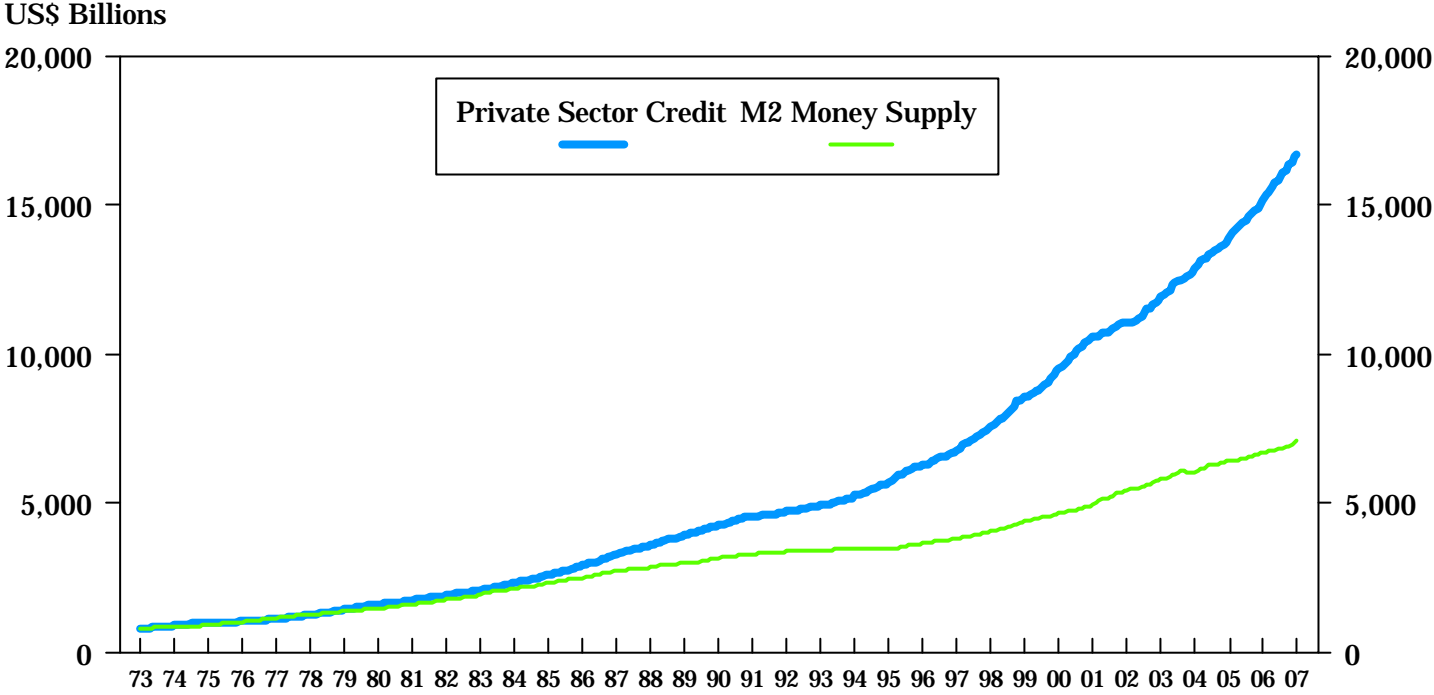
Choose Your Region



US Liquidity: History Rhymes

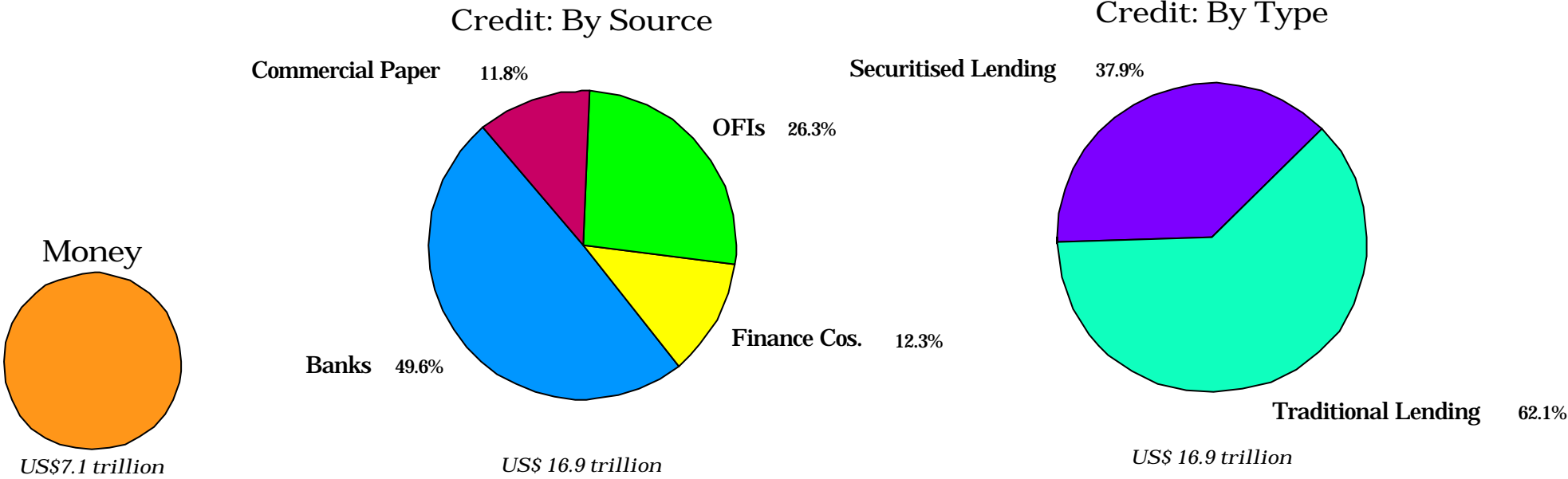


US Credit Growth Vs. Money Growth



US Credit Growth Vs. Money Growth

February 2007



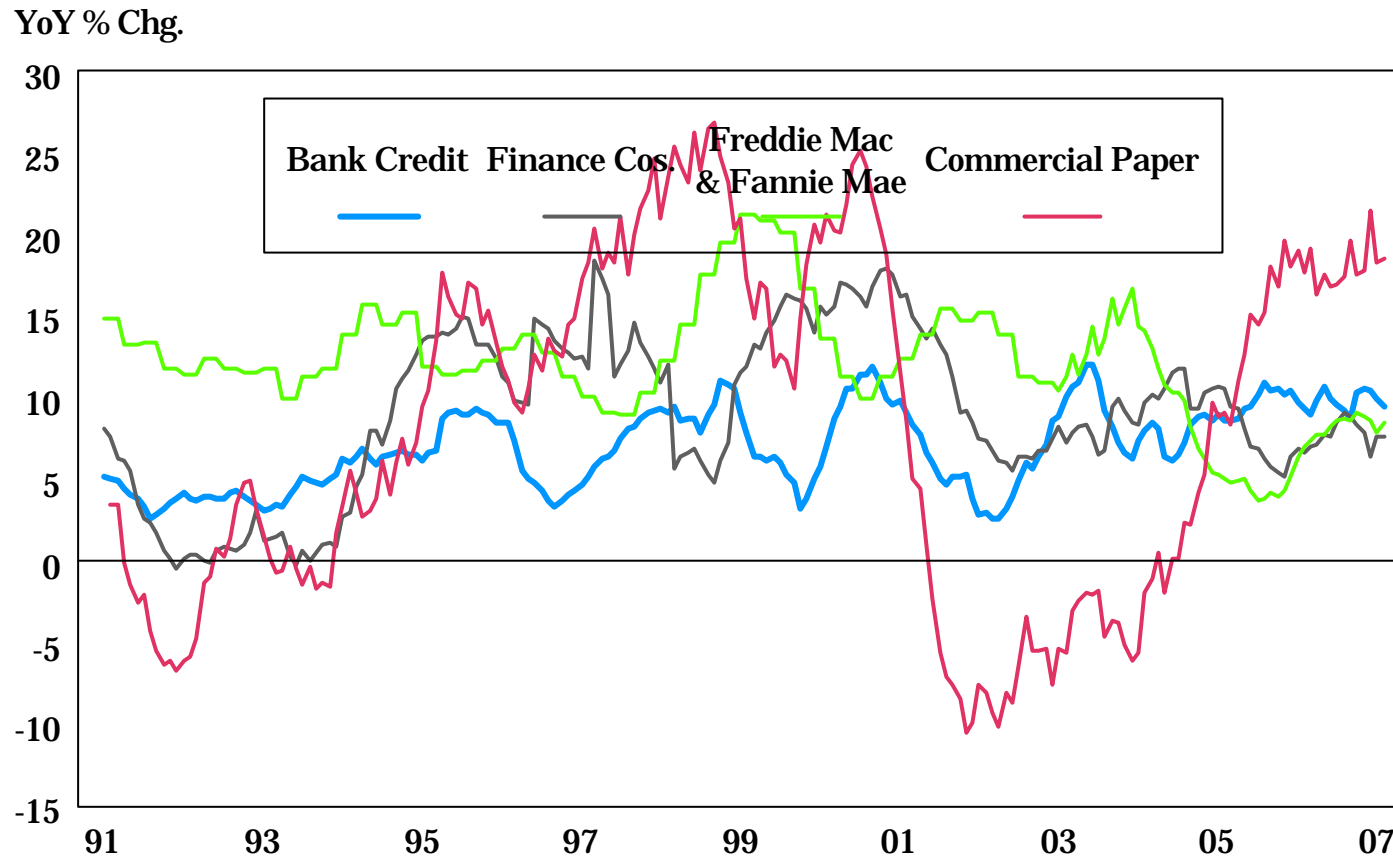
US Credit Vs. Money Supply

2006-2007

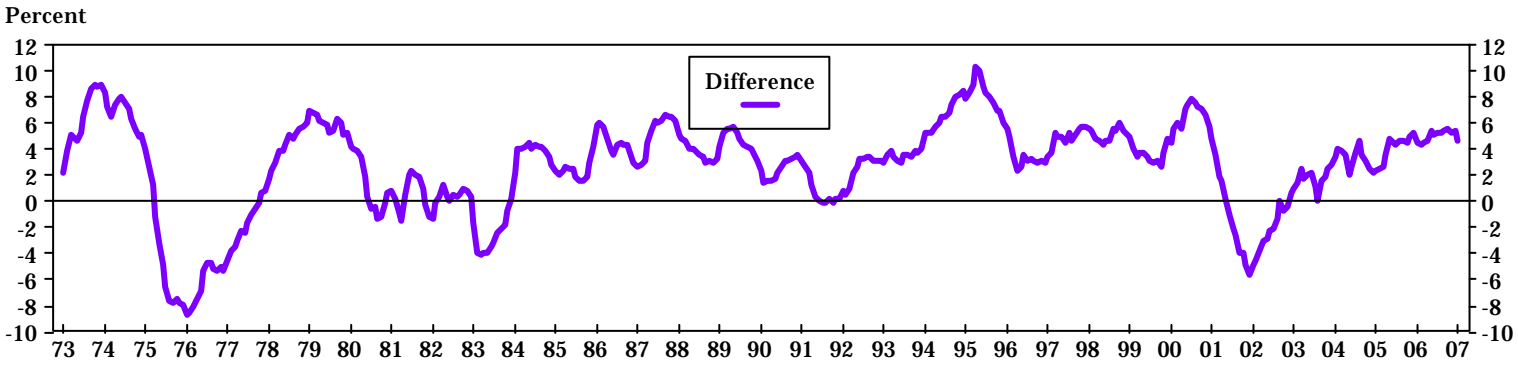
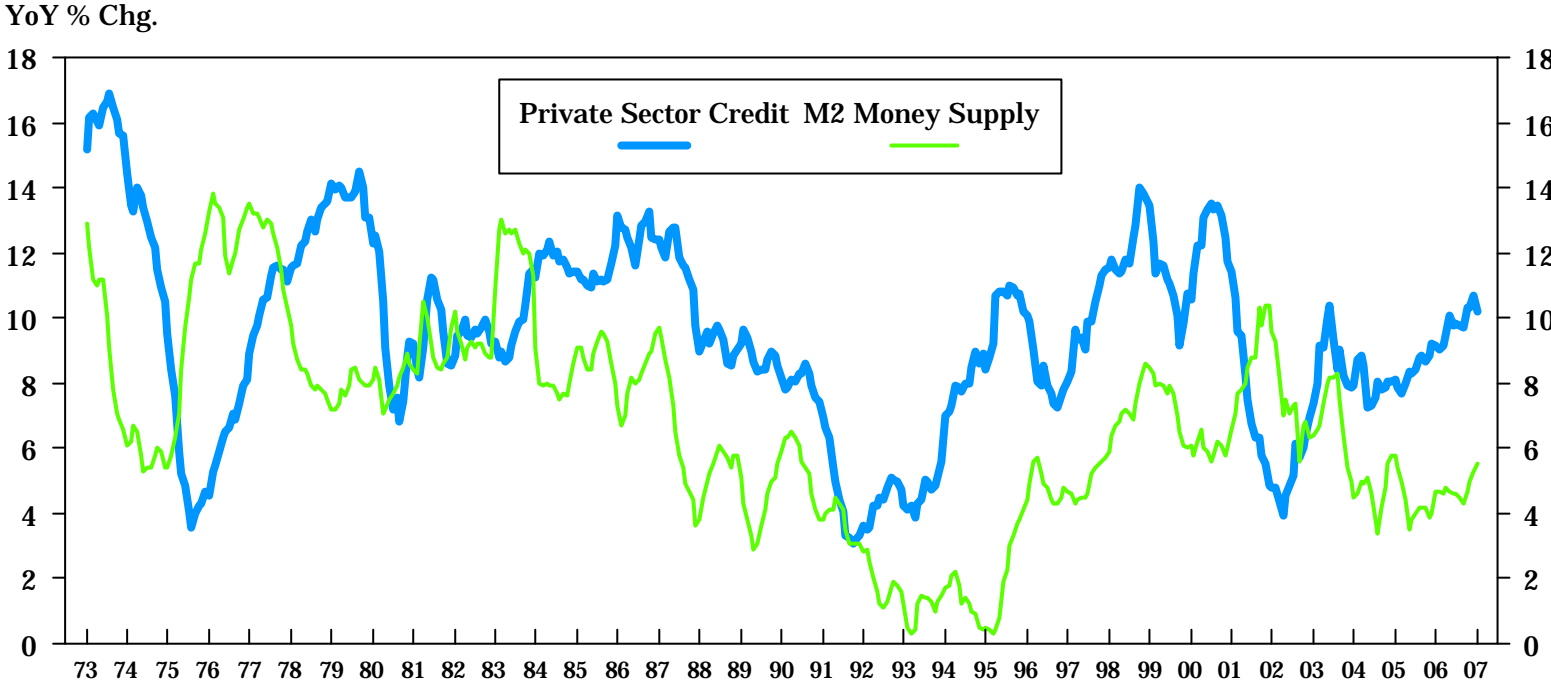
<i>US\$ bn</i>	<i>Banks</i>	<i>Finance Cos.</i>	<i>OFIs</i>	<i>Commercial Paper</i>	<i>Total Credit</i>	<i>M2</i>
Jan-06	7,558.7	1,916.3	4,064.7	1,672.7	15,212.4	6,713.6
Feb-06	7,647.8	1,931.4	4,097.4	1,687.5	15,364.1	6,737.0
Mar-06	7,717.4	1,945.1	4,120.3	1,705.1	15,487.8	6,755.8
Apr-06	7,807.9	1,954.9	4,144.3	1,734.6	15,641.8	6,774.9
May-06	7,923.8	1,969.1	4,159.6	1,765.4	15,817.9	6,785.7
Jun-06	7,930.9	1,977.2	4,192.6	1,775.9	15,876.6	6,811.2
Jul-06	7,981.8	1,991.1	4,203.8	1,796.7	15,973.3	6,835.8
Aug-06	8,040.8	2,001.5	4,231.0	1,840.6	16,113.9	6,863.4
Sep-06	8,060.0	2,005.2	4,267.9	1,887.2	16,220.3	6,886.5
Oct-06	8,193.1	2,001.3	4,296.9	1,885.8	16,377.1	6,936.3
Nov-06	8,233.3	2,004.8	4,319.9	1,930.3	16,488.4	6,977.0
Dec-06	8,286.3	2,018.7	4,354.3	1,981.4	16,640.7	7,021.0
Jan-07	8,312.2	2,061.3	4,386.8	1,978.9	16,739.2	7,081.1
Feb-07	8,375.6	2,077.5	4,444.1	2,000.9	16,898.1	7,144.5
<i>% Share</i>	49.6%	12.3%	26.3%	11.8%		



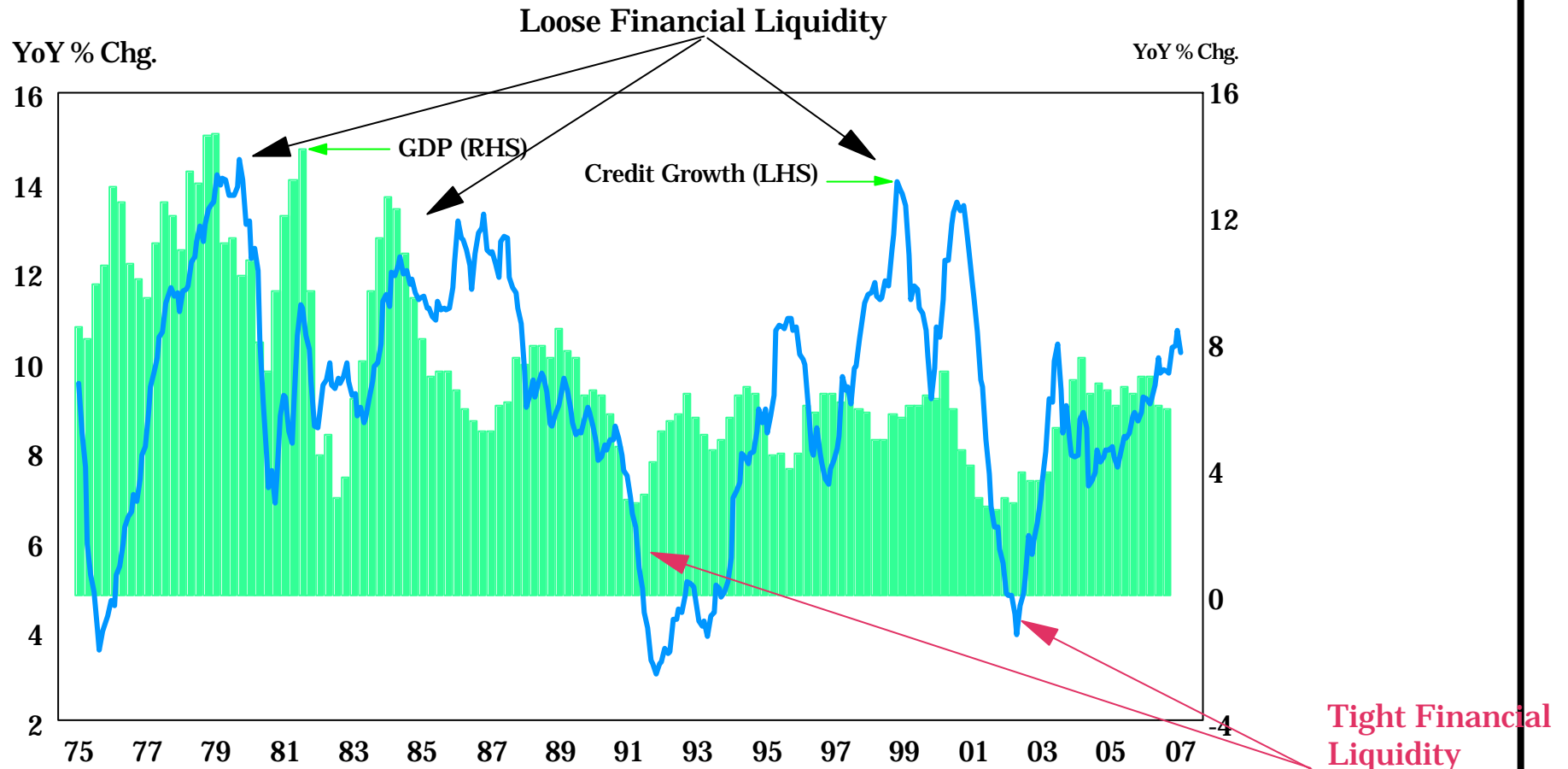
US Credit Growth: Components



US Credit Growth Vs. Money Growth

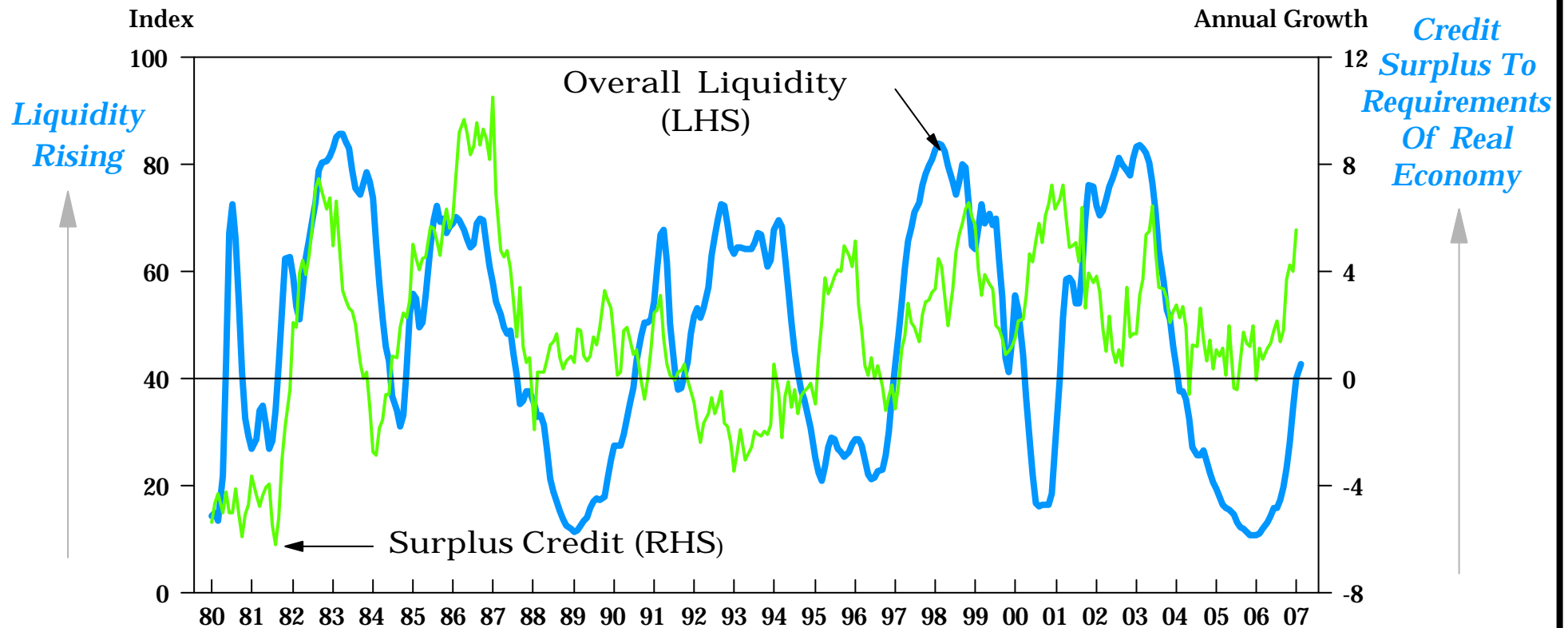


Excess Or Financial Liquidity: US Credit Growth Vs. GDP Growth



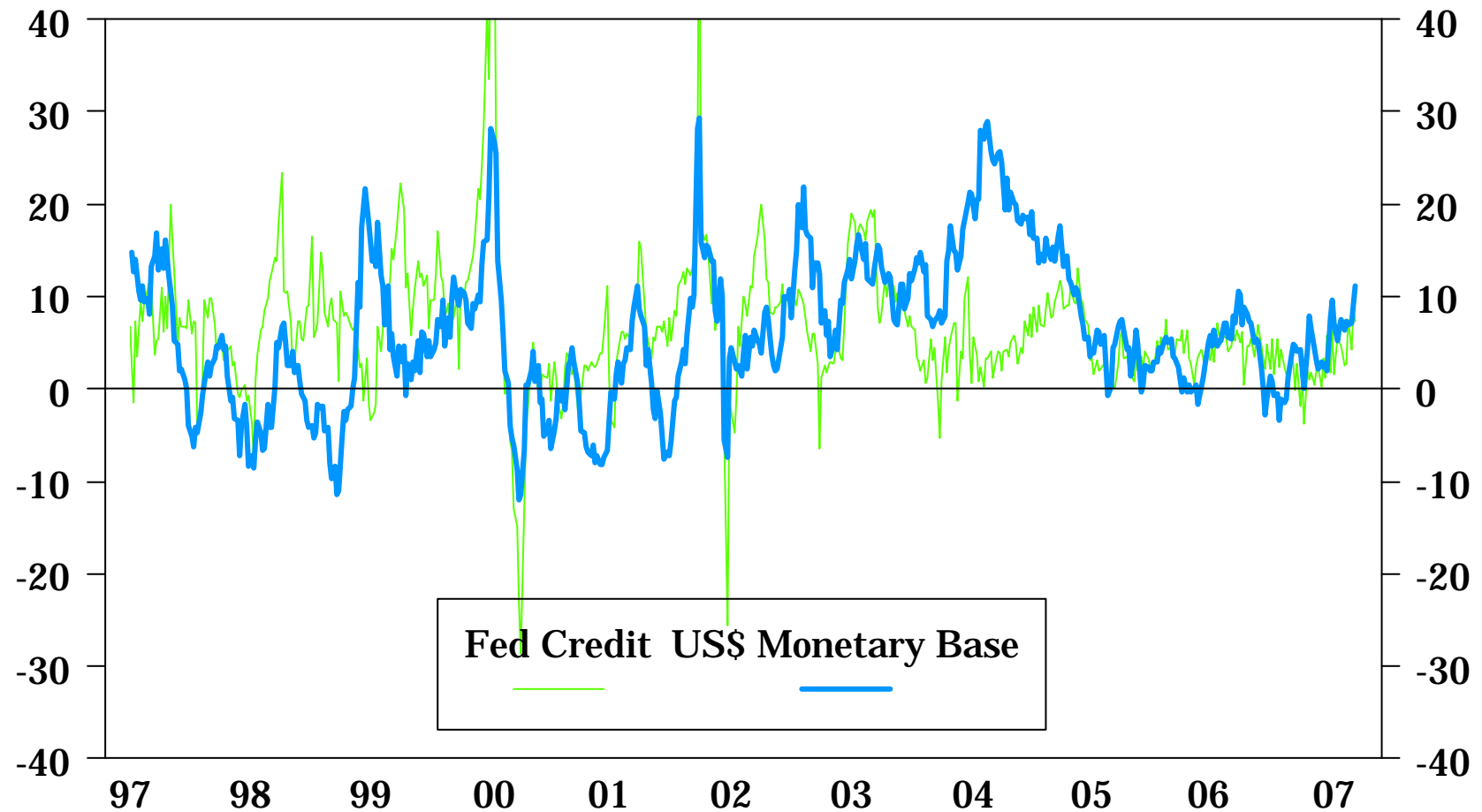
US Surplus Credit And The Liquidity Cycle

- *Surplus credit is a crude measure of financial liquidity, but still tracks closely*
- *Differences are: (a) Fed; (b) foreign inflows, and (c) 'cross-checks'*

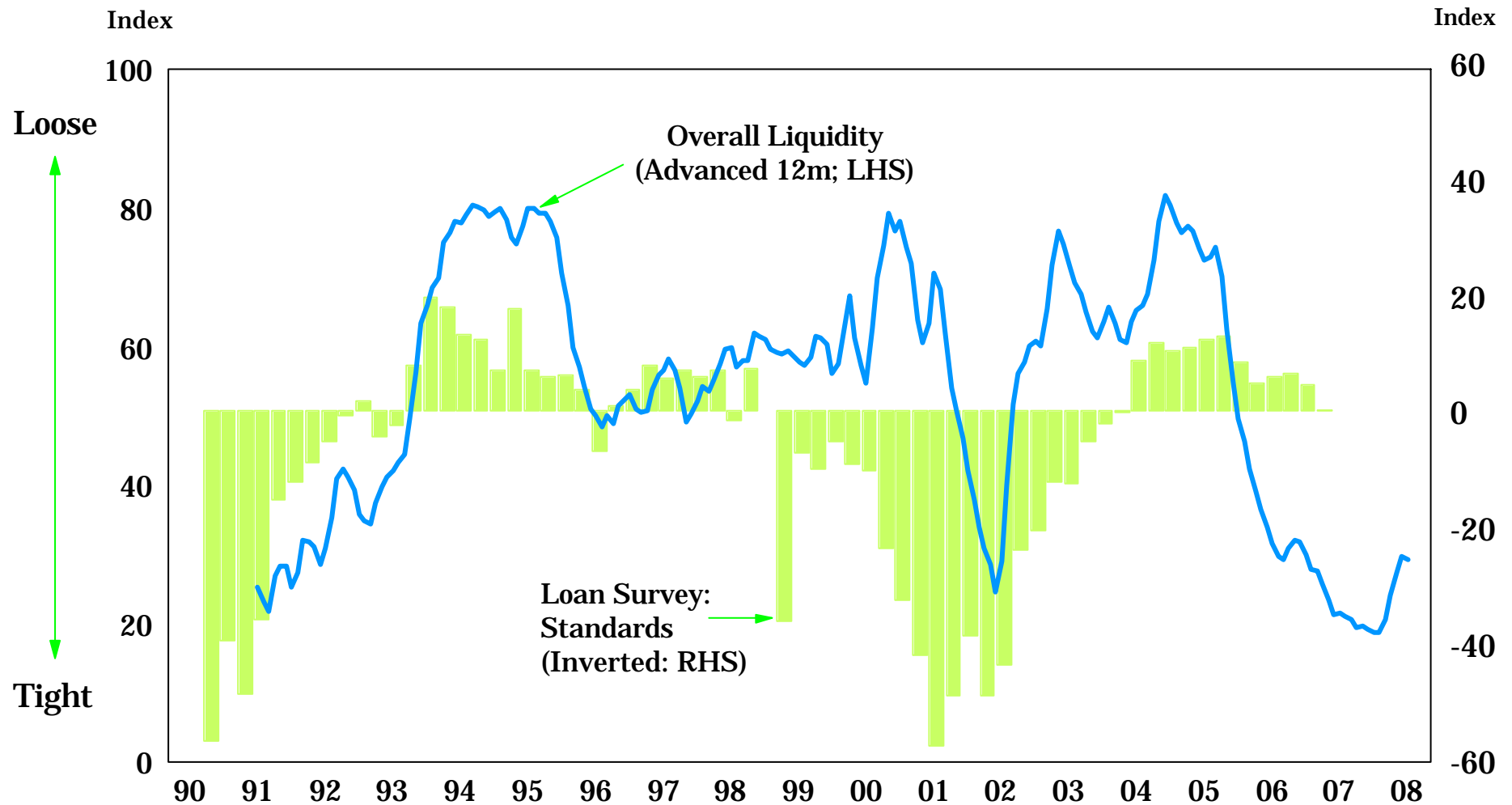


Fed Credit Vs. US\$ Monetary Base

3-Mth Ann Growth Rate (%)

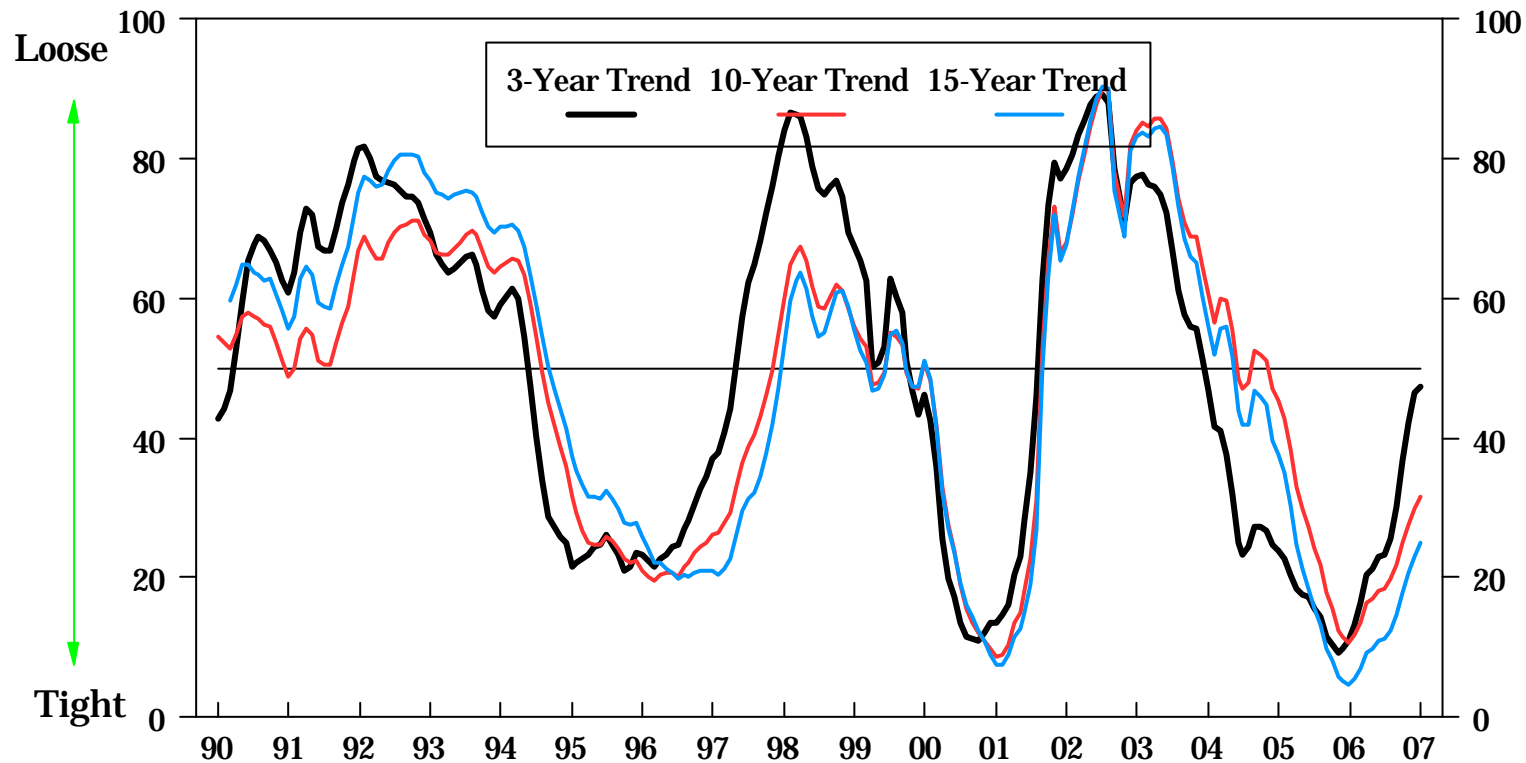


Global Loan Survey and Liquidity Cycle



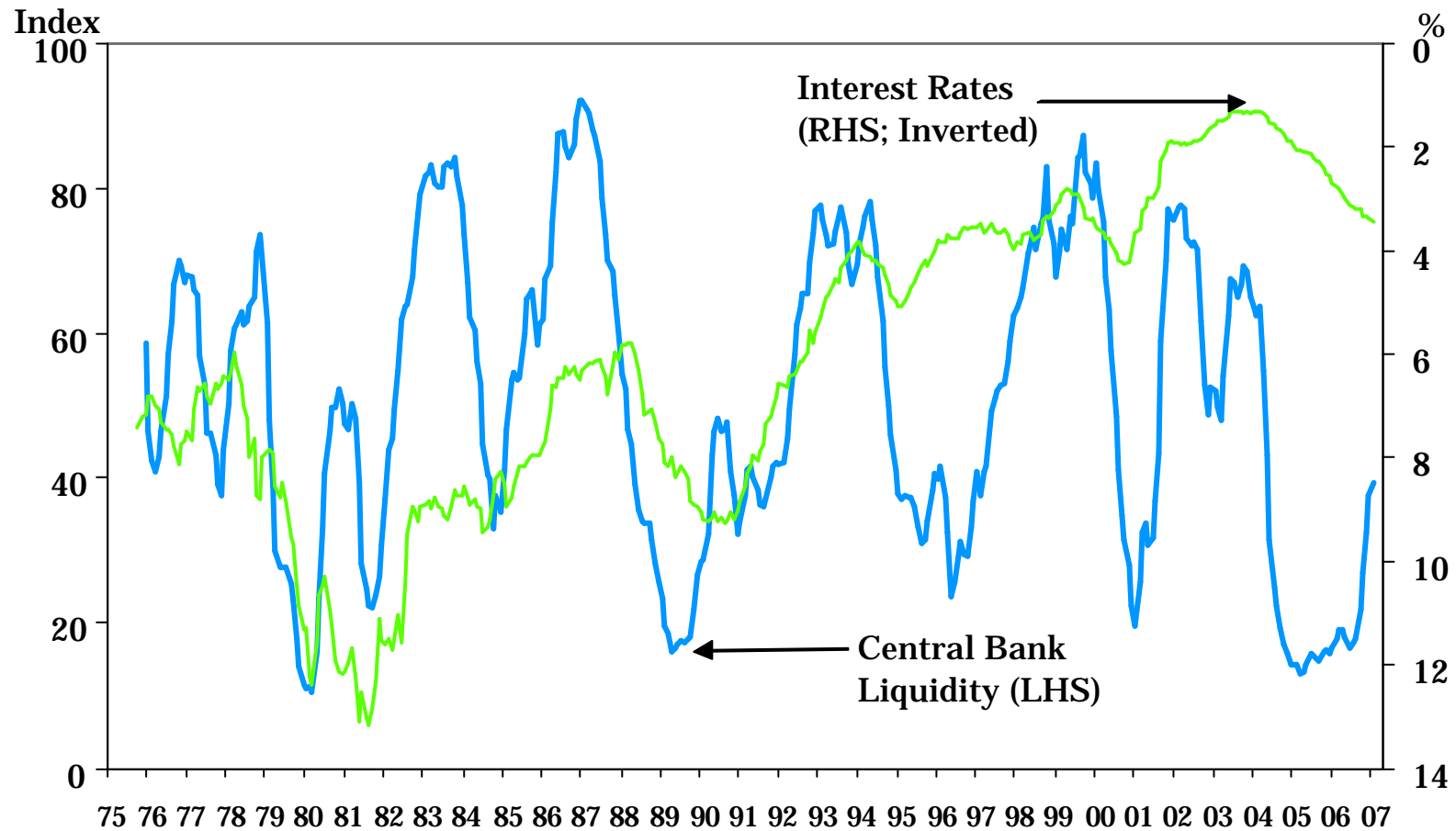
US Central Bank Liquidity

- *Our indexes use moving averages as trend filters. Does it matter which moving average length we use?*



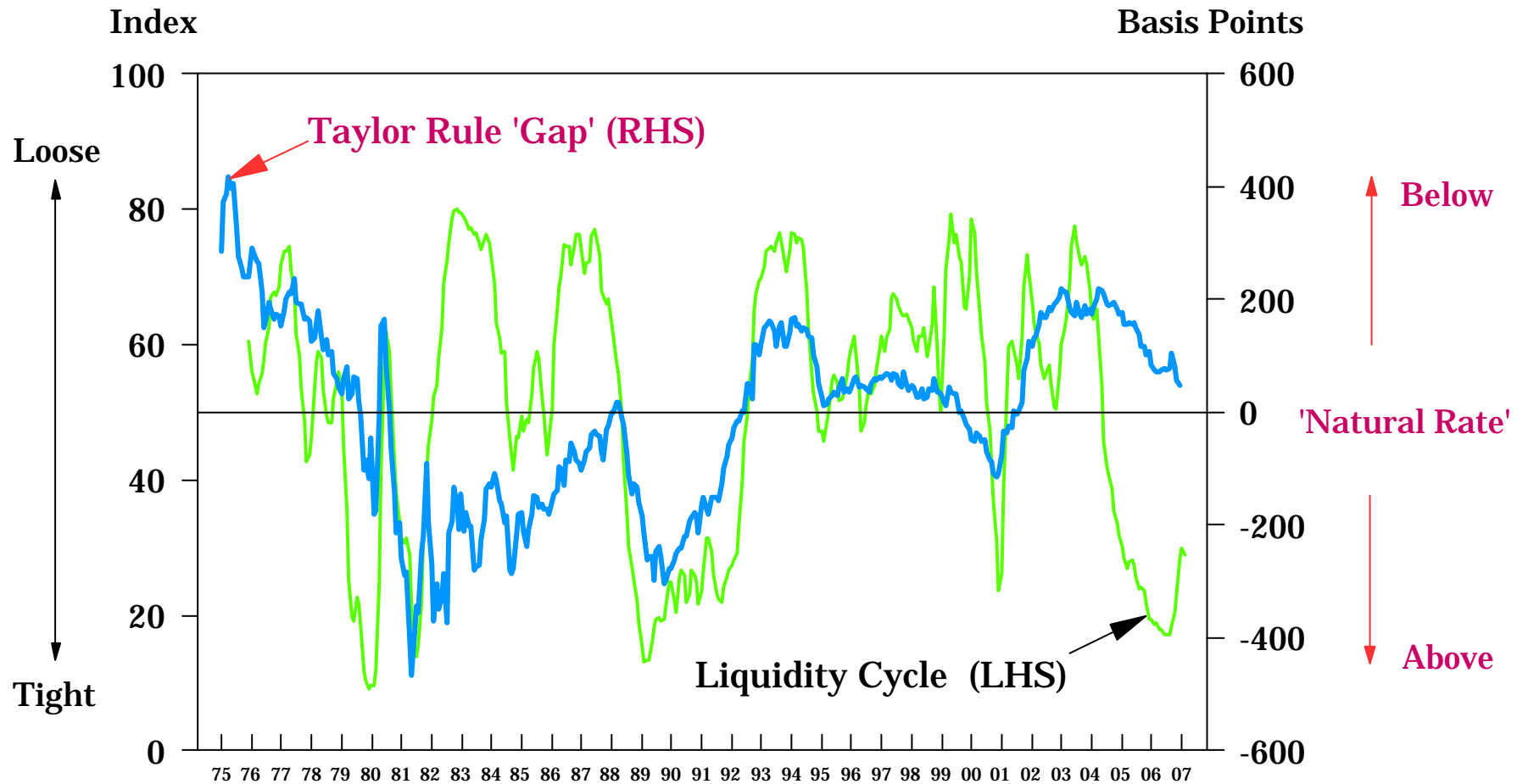
Global Liquidity And Interest Rates

- *Liquidity often leads short-term rates but no compelling correlation*



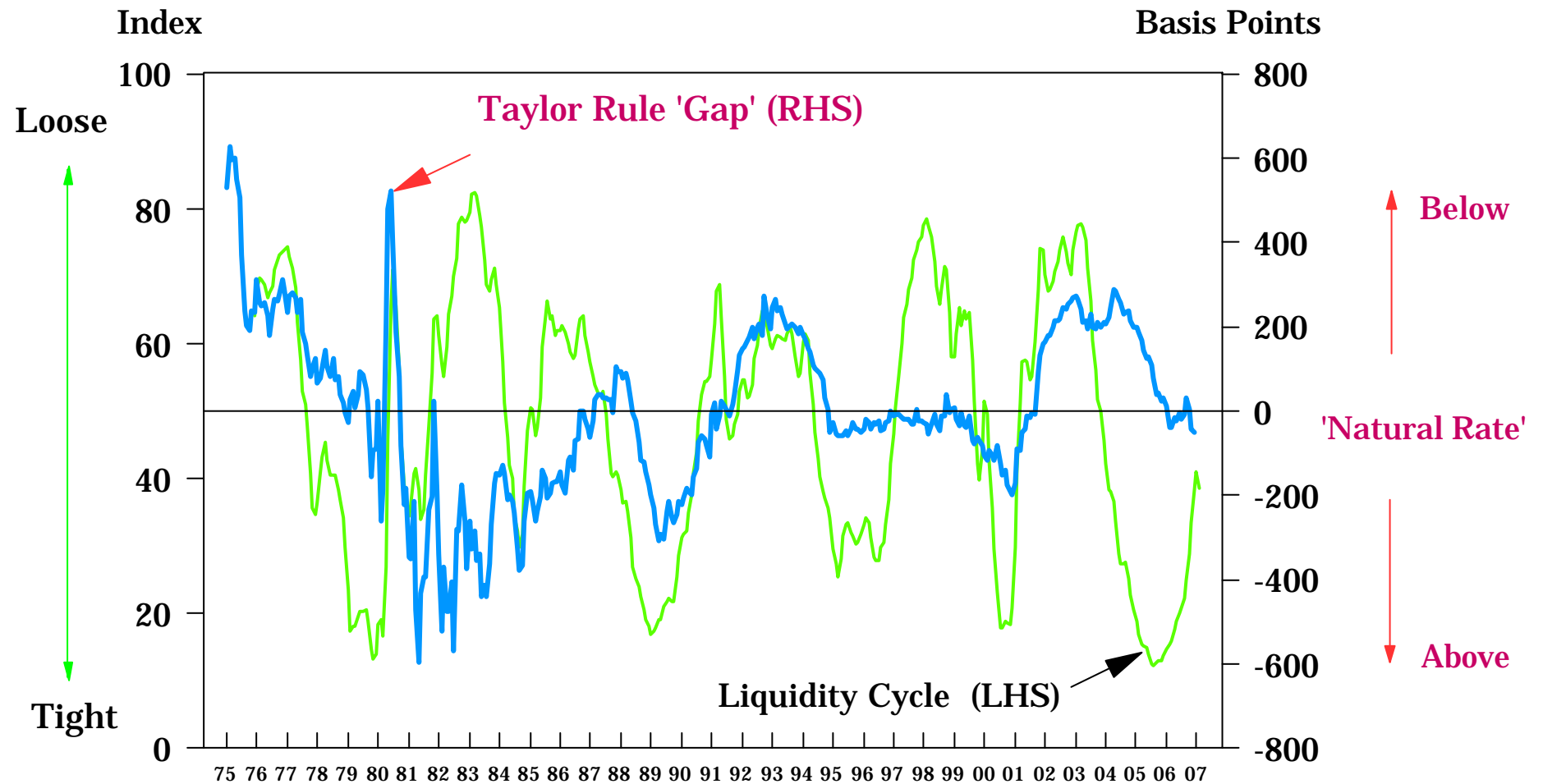
G7 - Taylor Rule And Liquidity Cycle

- *Interest rate setting relative to 'natural' rate (Taylor Rule) tends to capture direction of liquidity but rarely the full scale of the credit cycle*



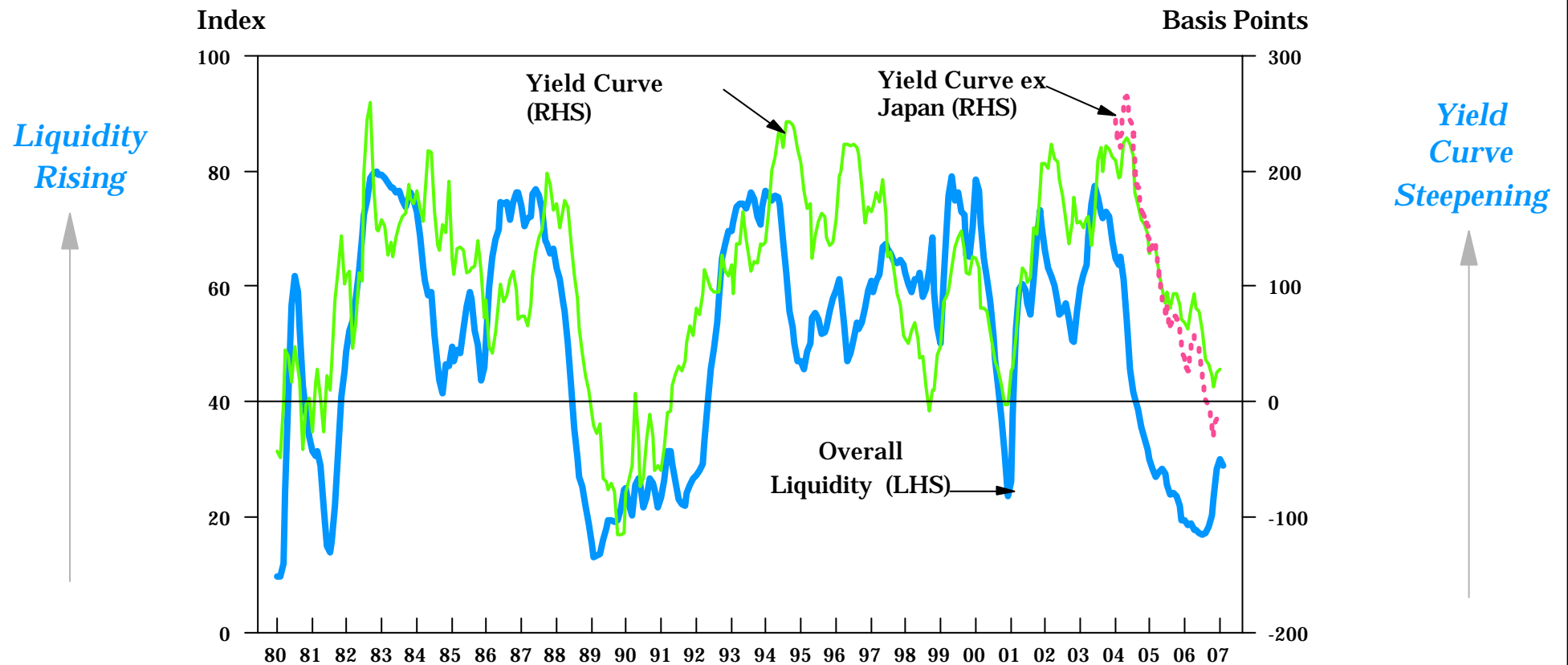
US - Taylor Rule And Liquidity Cycle

- *US interest rates lately appear consistent with Taylor Rule, but liquidity often different*



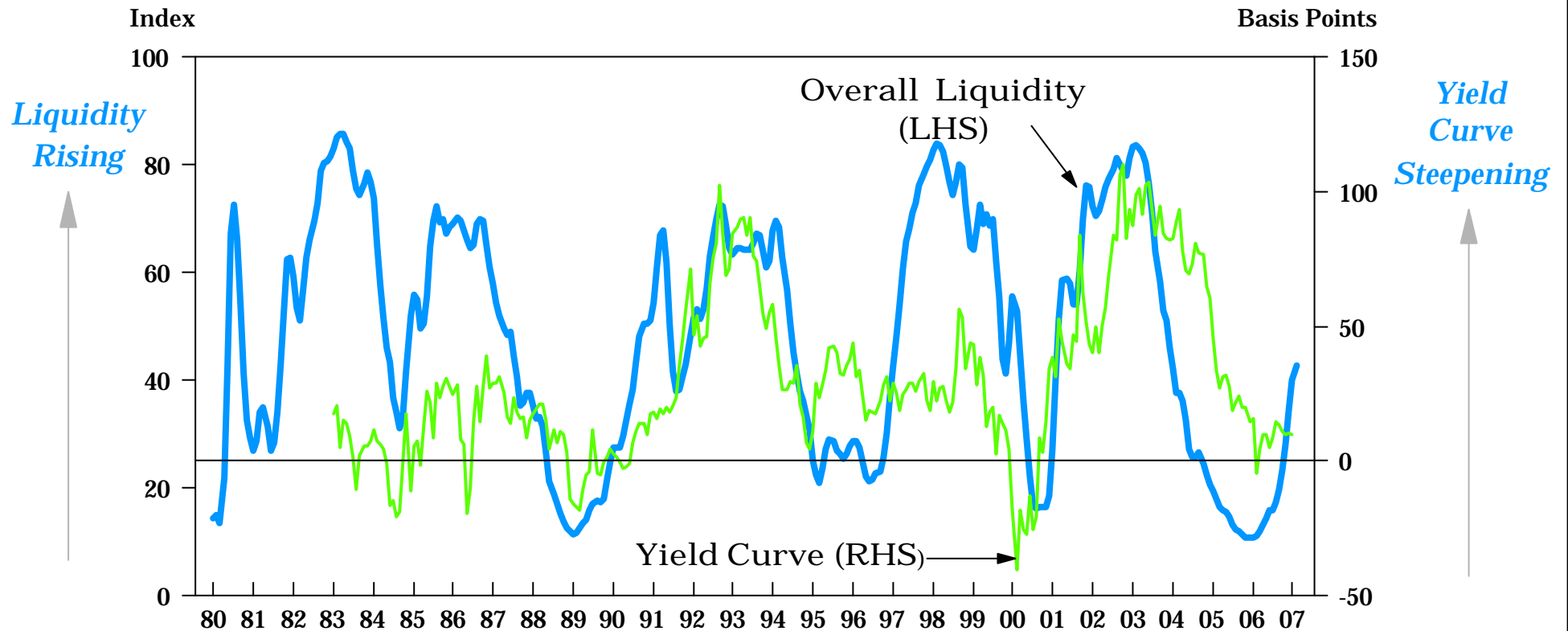
Global Liquidity And The Yield Curve

- *Liquidity leads yield curve by 6 - 9 months*
- *Falling liquidity flattens curves; rising liquidity steepens curves*



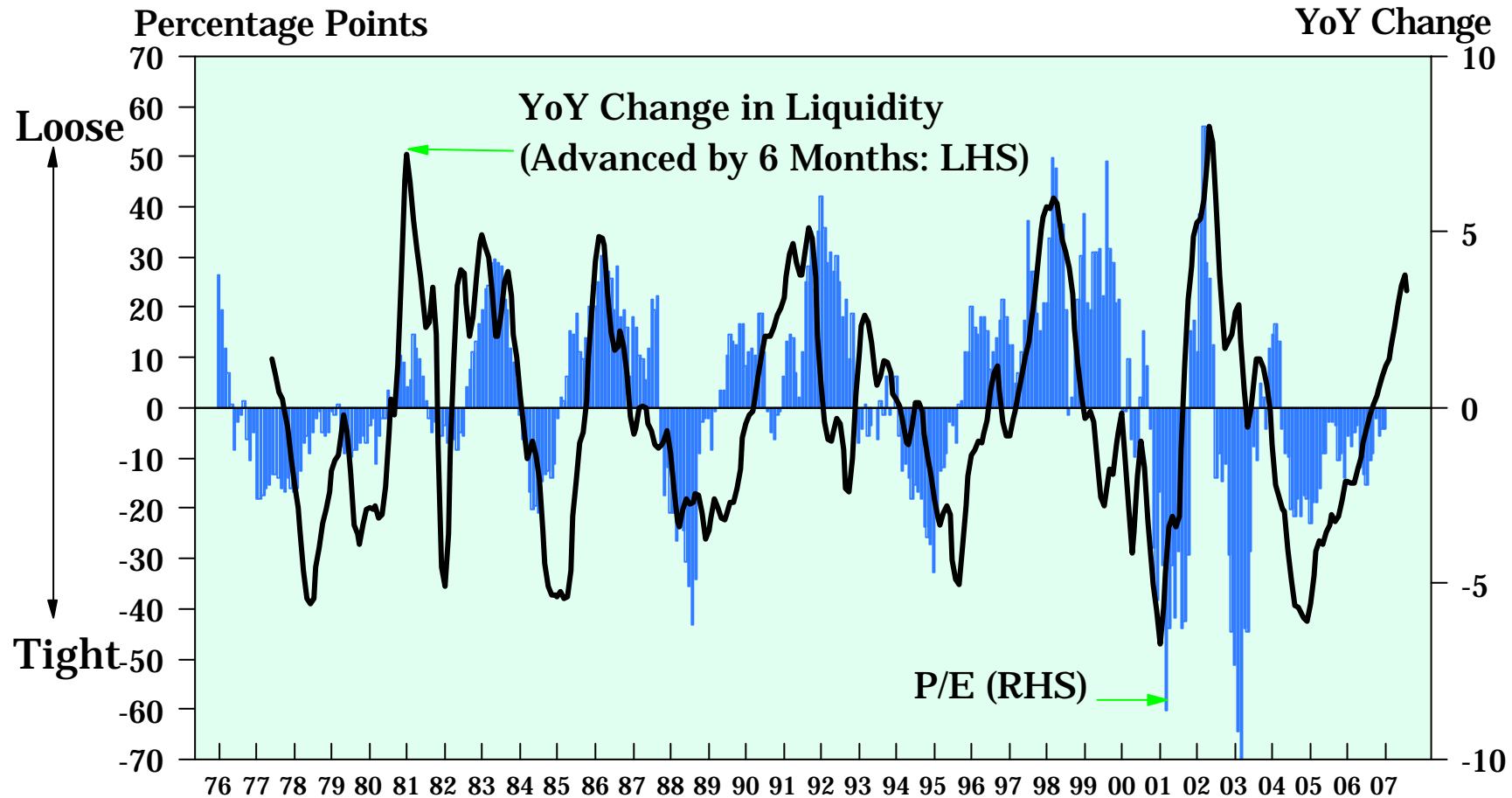
US Liquidity And The 30/10 Yield Curve

- *Liquidity determines interest rate spreads, not interest rate levels*
- *30-year less 10-year yields*
- *30/10 spread is a leading yield curve spread*



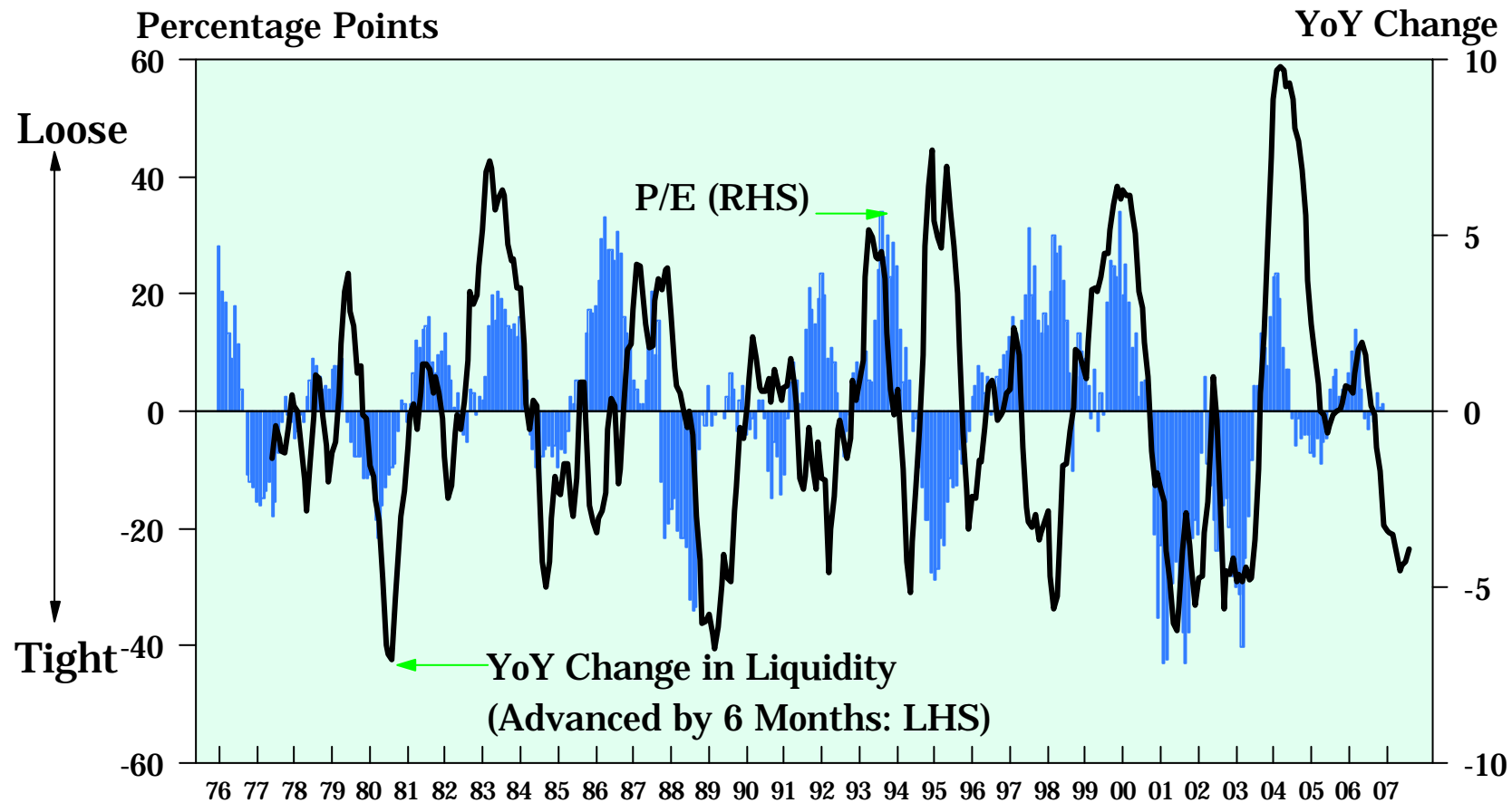
Change in US Liquidity And US P/Es

- *Change in liquidity determines valuation 6 months ahead*
- *Fall in liquidity 2004-2006 put negative pressure on P/Es*
- *Rising liquidity in 2007 should underpin P/Es*



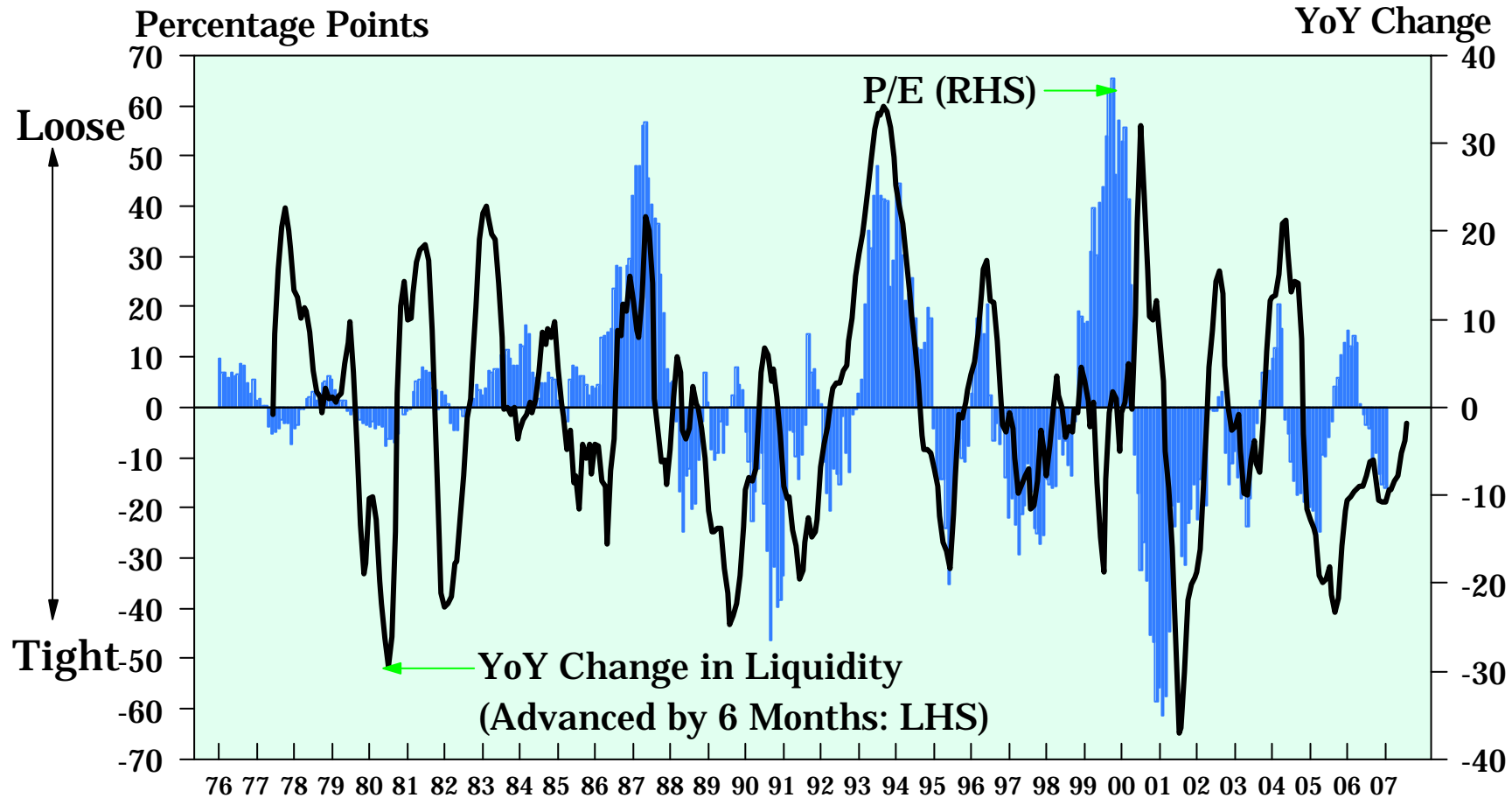
Change in Eurozone Liquidity And Eurozone P/Es

- *Change in liquidity determines valuation 6 months ahead*
- *Fall in liquidity in 2006 will put negative pressure on P/Es during 2007*



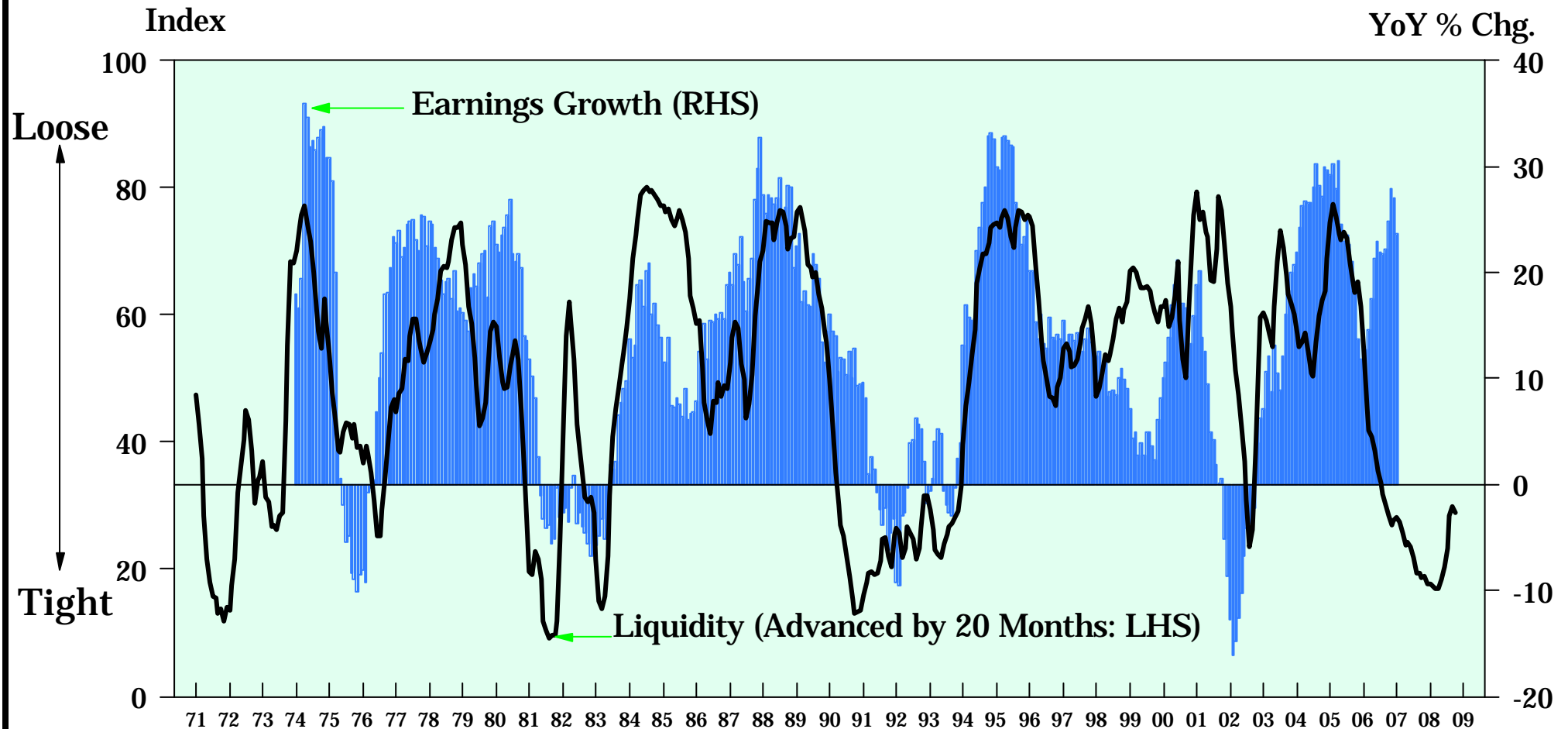
Change in Japanese Liquidity And Japanese P/Es

- *Change in liquidity determines valuation 6 months ahead*
- *Fall in liquidity during 2005-2006 will put negative pressure on P/Es during 1H 2007 but outlook improving for 2H*

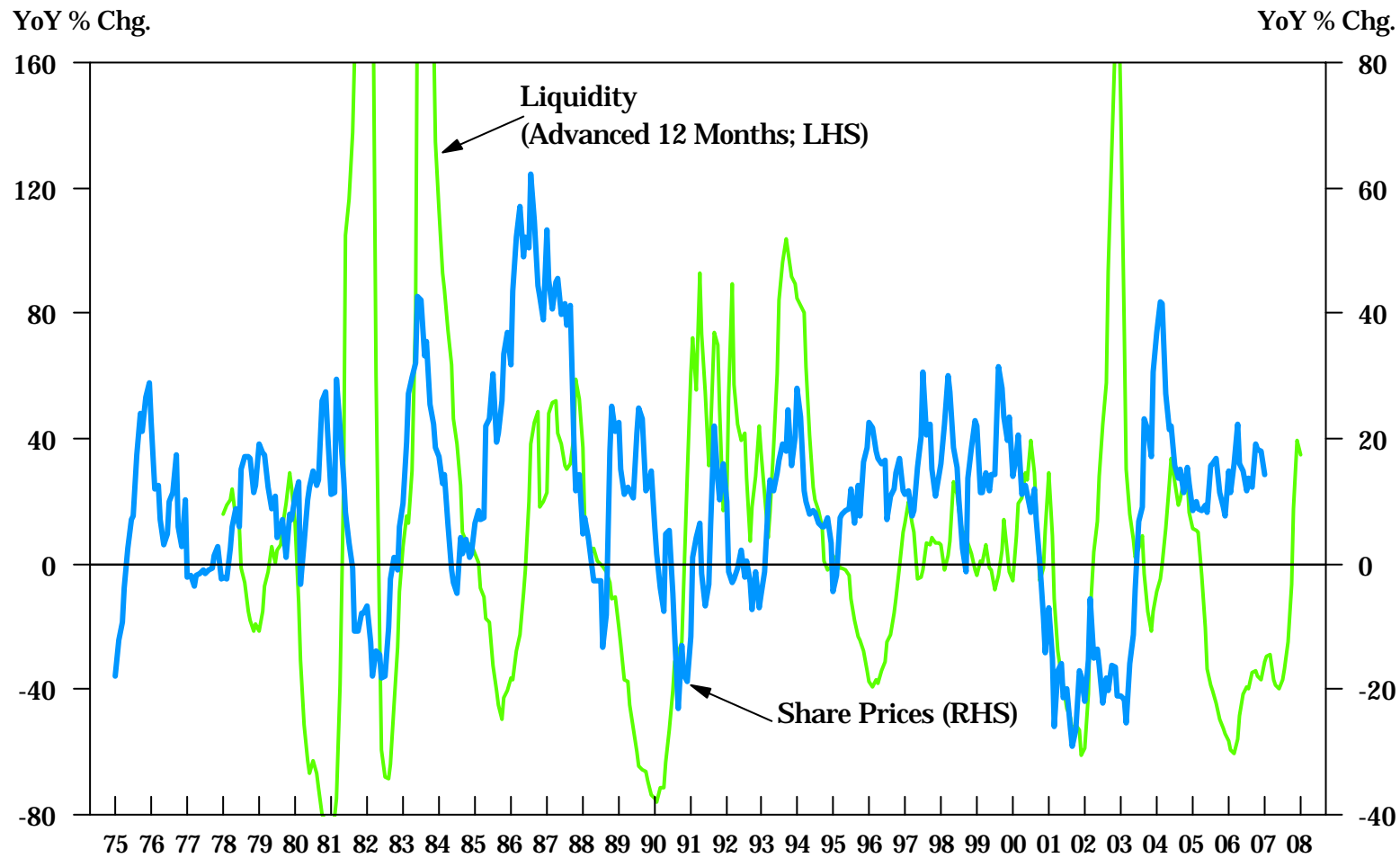


Global Liquidity Cycle And Corporate Earnings Growth

- *Liquidity leads corporate earnings growth (reported) based on the MSCI World Index by 20 months. Credit (liquidity) adds to purchasing power but not costs, so profits rocket*
- *Earnings growth weak in 2007*

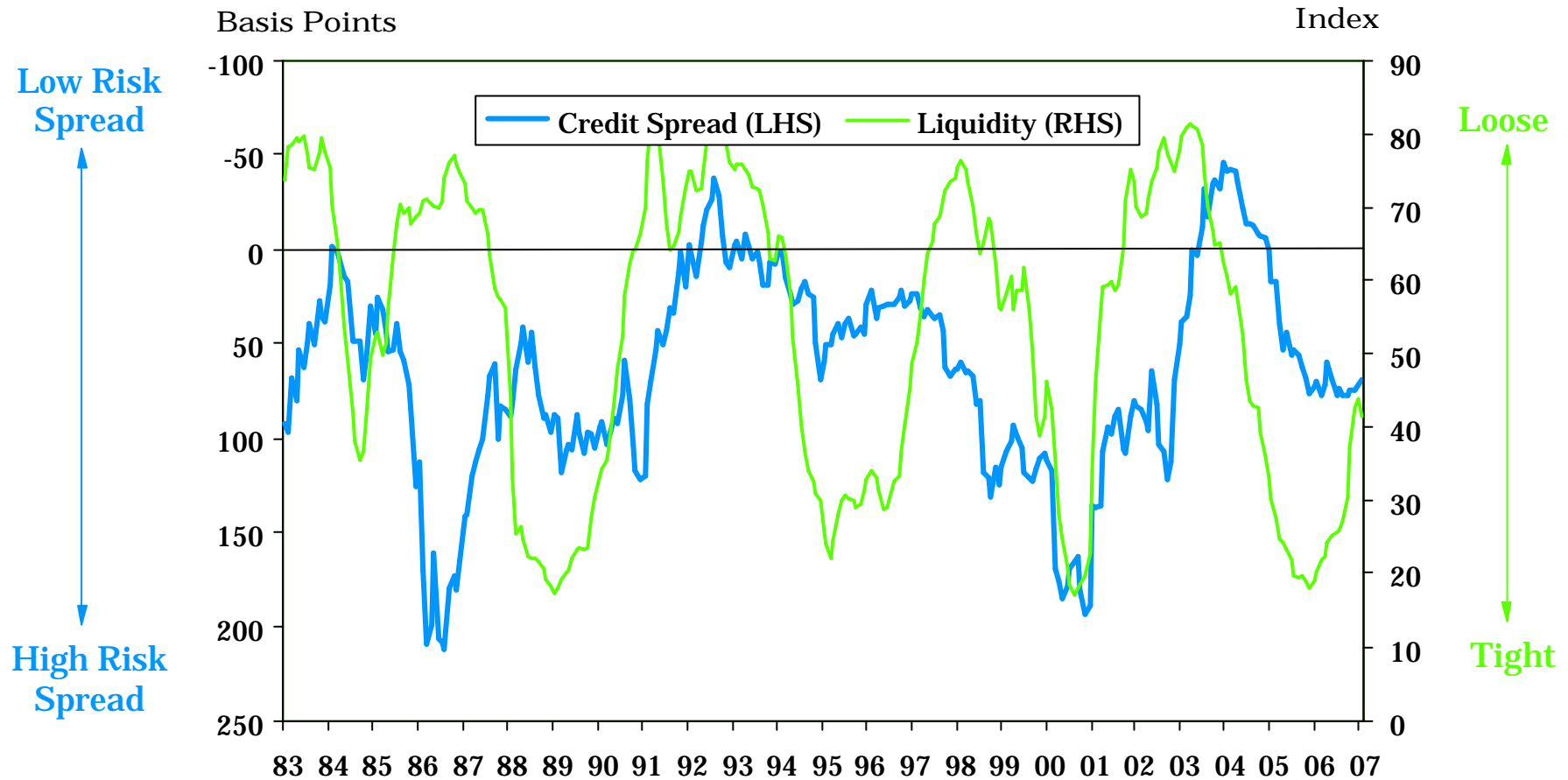


Global Liquidity Growth And Share Prices



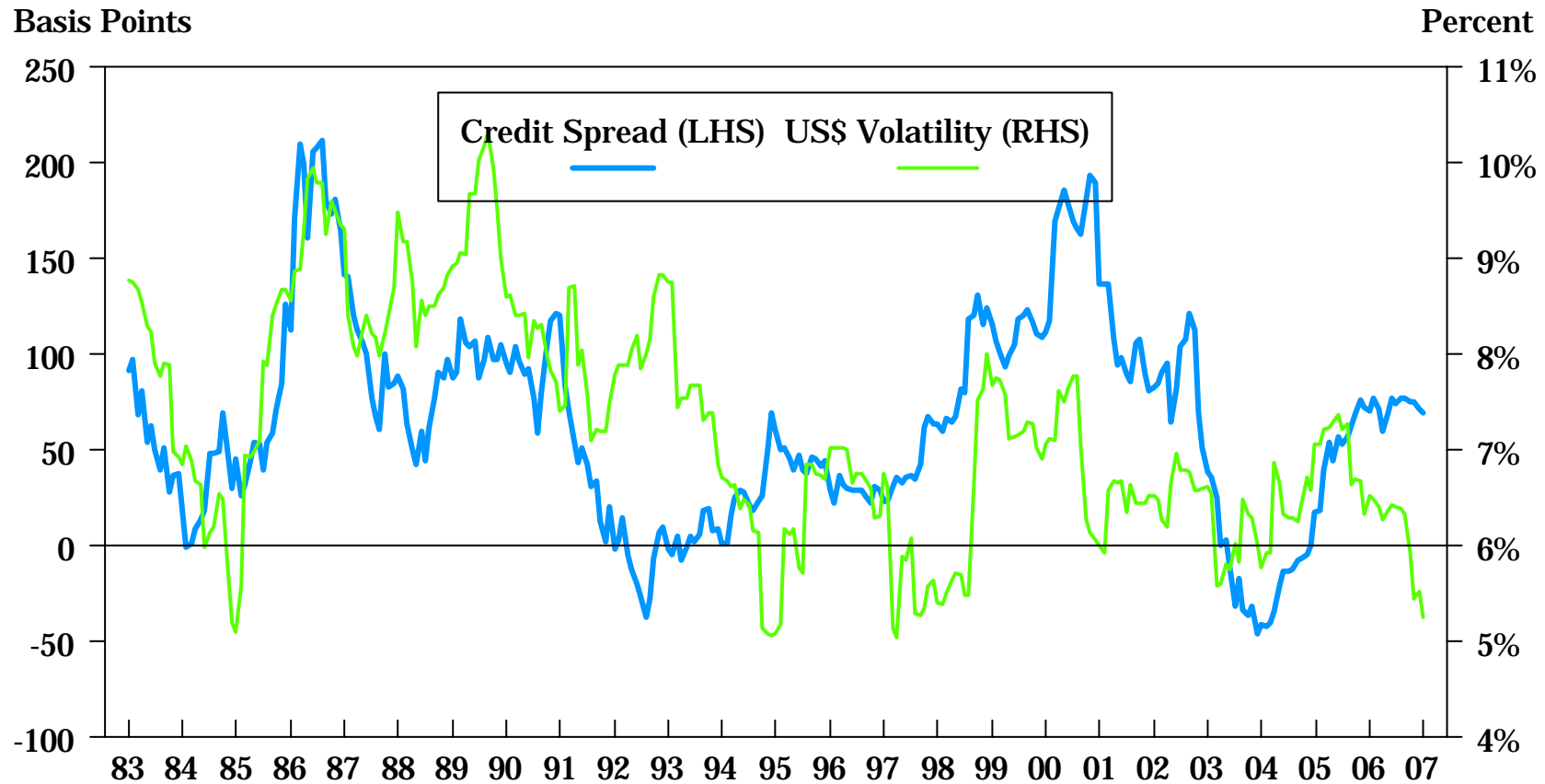
US Liquidity Vs. Credit Spreads (Inverted)

- *Levels of liquidity can have effect on credit spread, but not consistent*

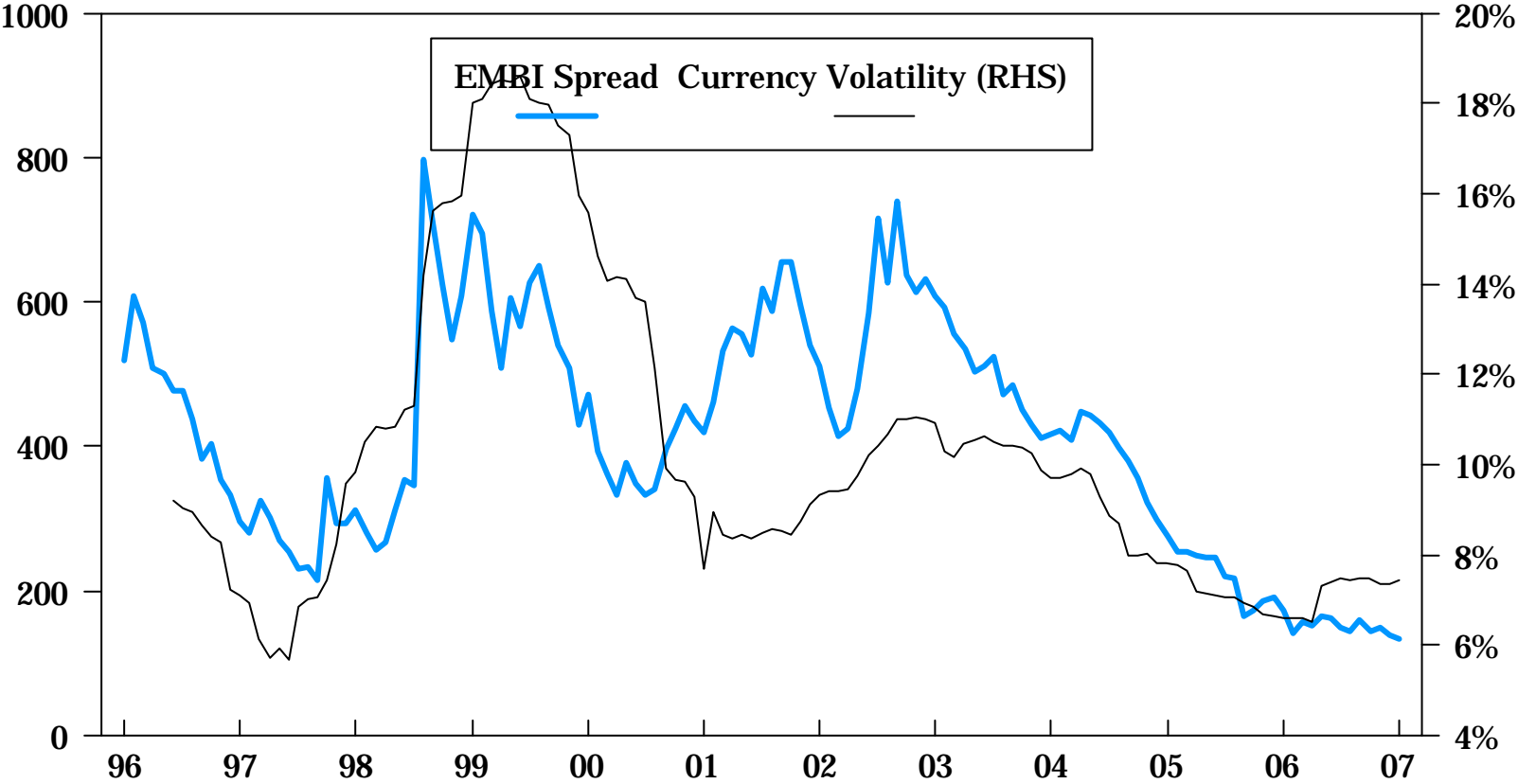


US\$ Volatility And Credit Spreads

- *US\$ volatility appears more important driver of quality spread since it highlights risk of monetary inflation and monetary deflation*

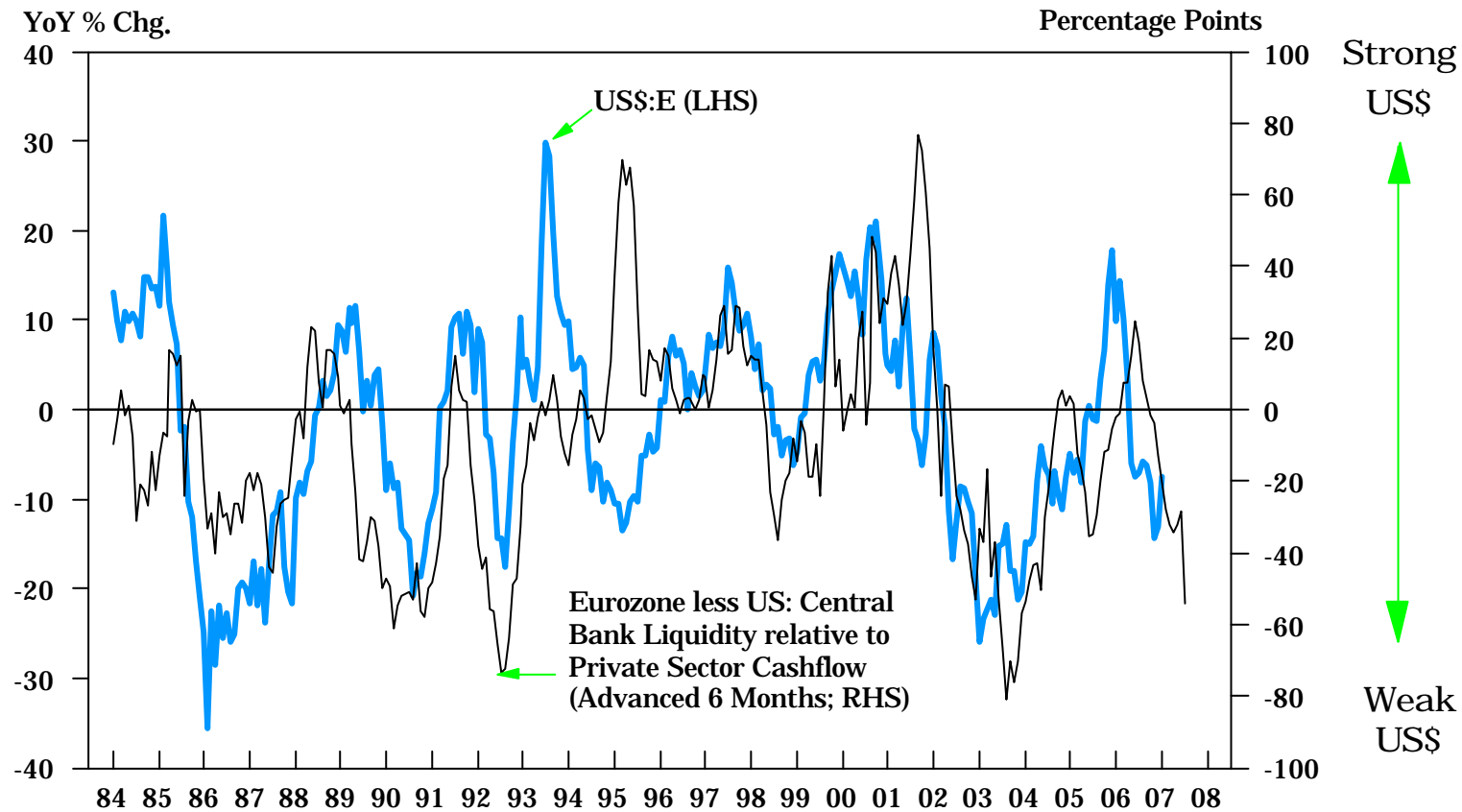


Emerging Market Currency Volatility And EMBI Spread



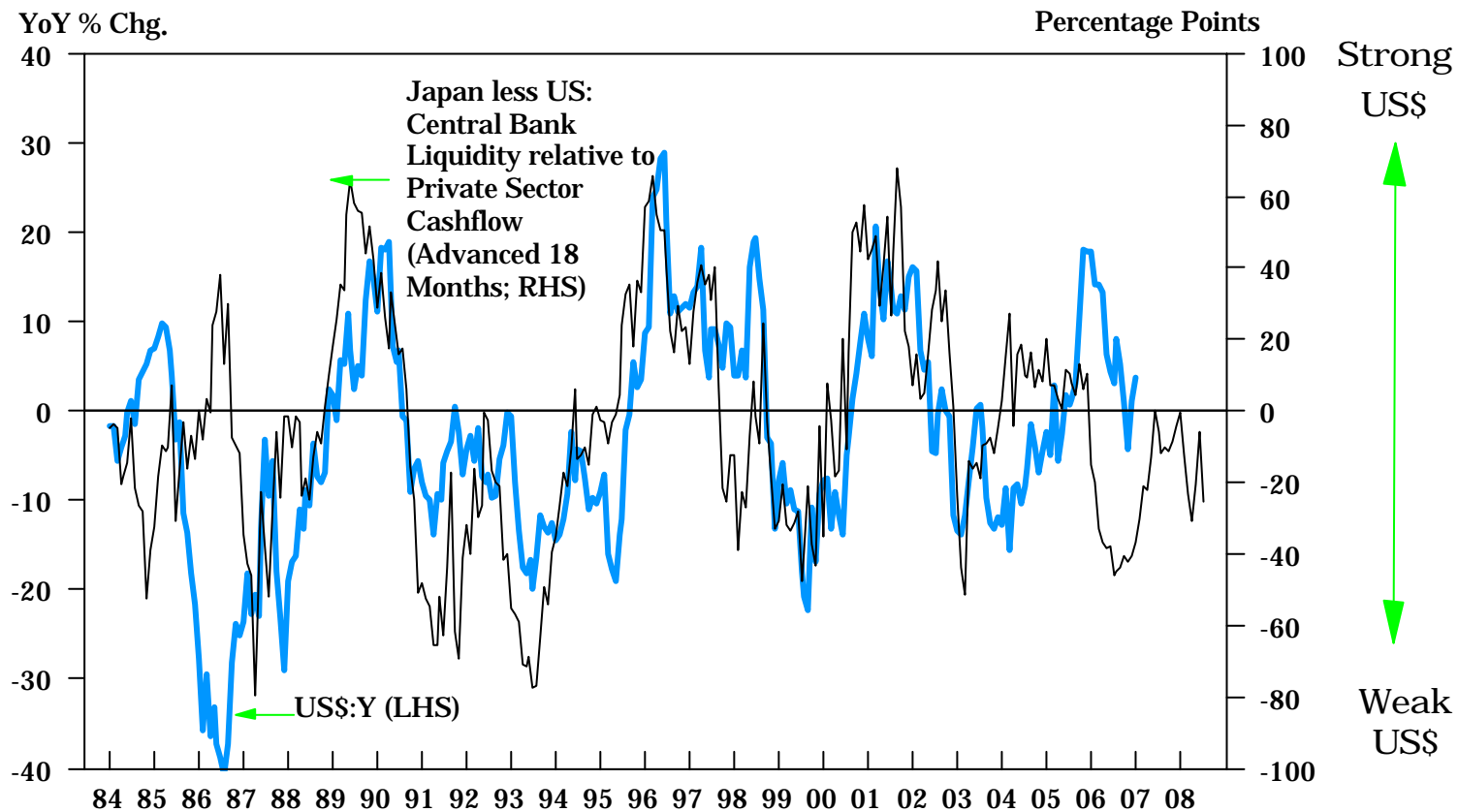
Relative Liquidity And US\$:€

- *Relative liquidity determines cross-rates*
- *Tight US liquidity through 2005 and 2006 should help the US dollar into 2007, but end of US\$ strength in sight as ECB catches up*



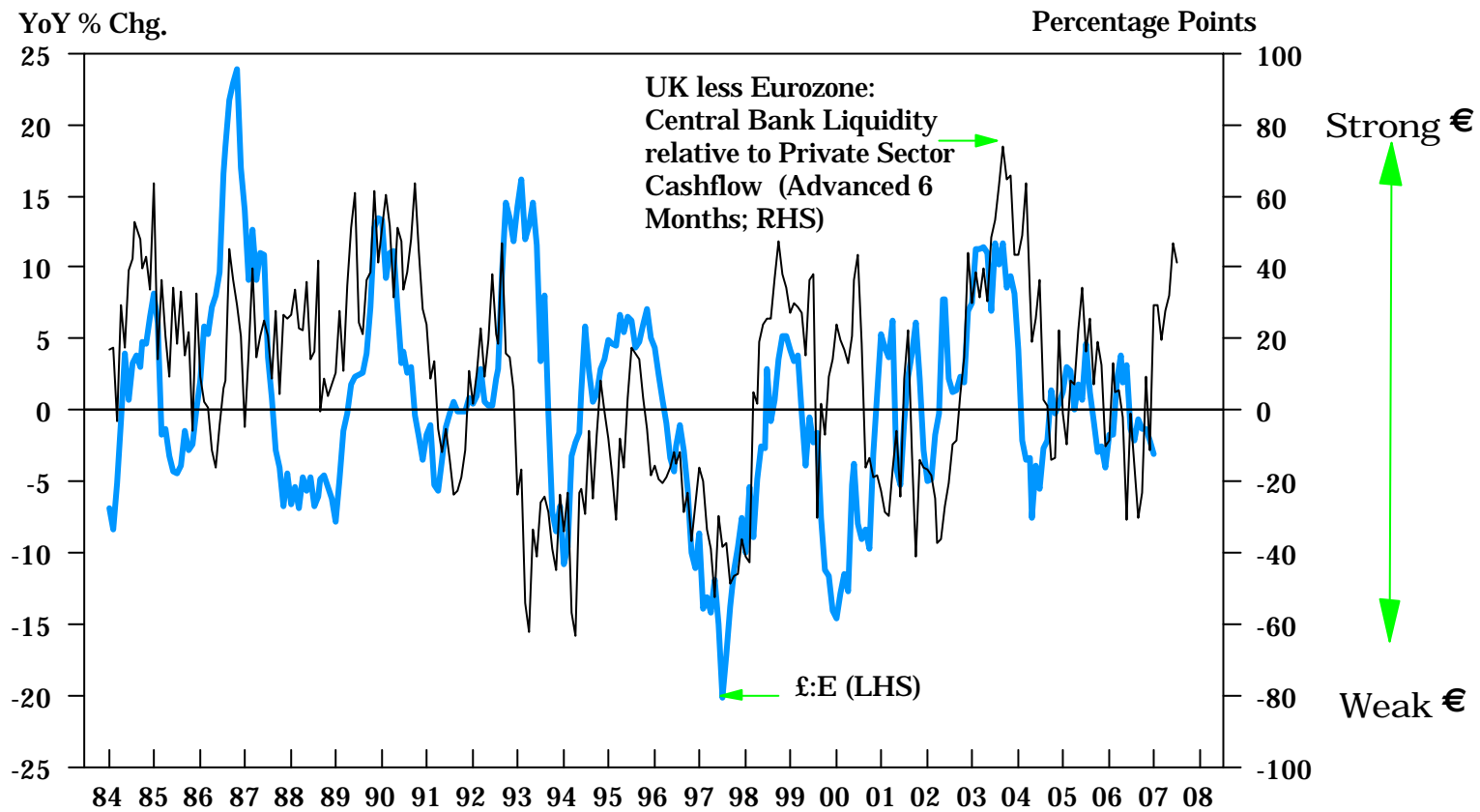
Relative Liquidity And US\$:Y

- *Relative liquidity determines cross-rates*
- *US dollar looks better supported in 2007*



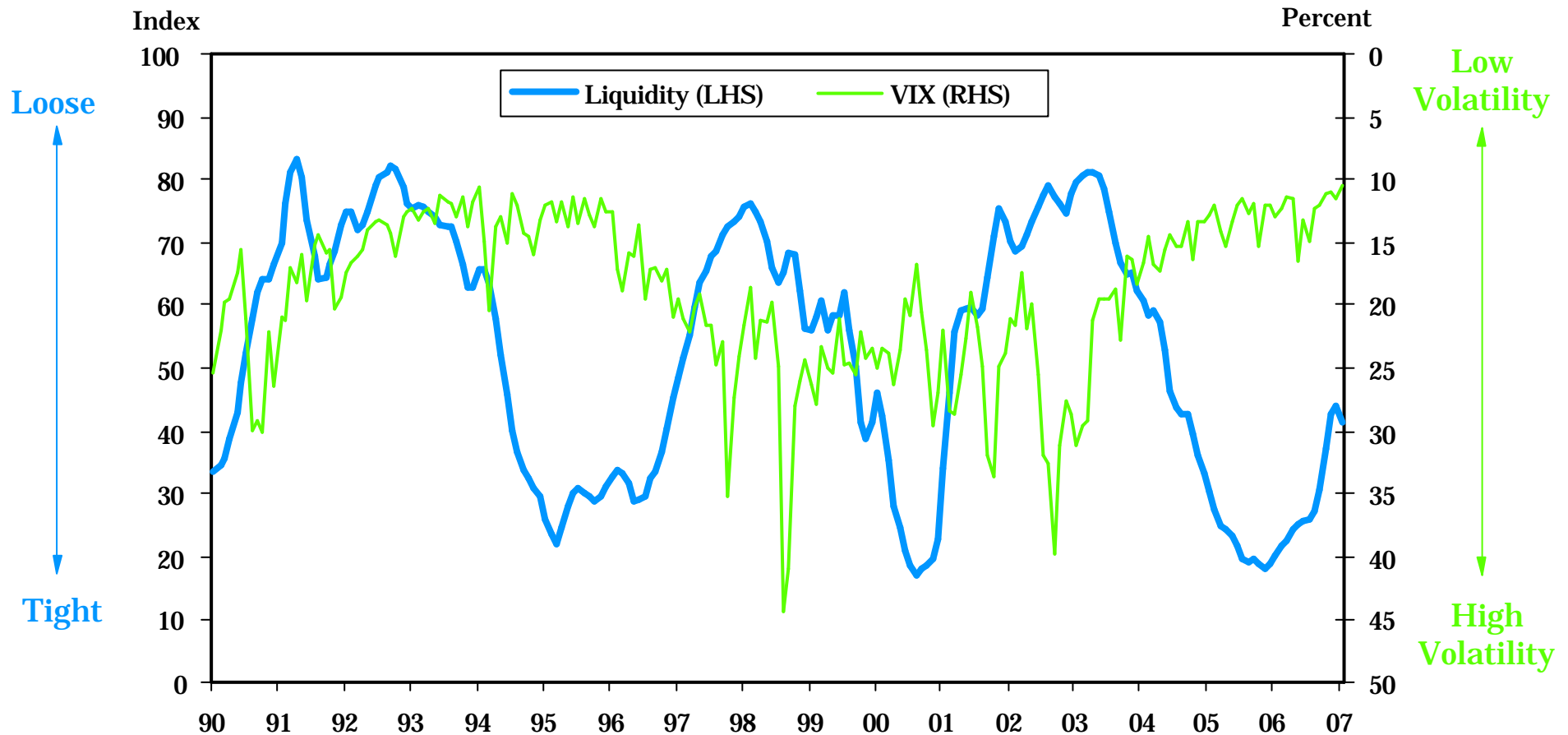
Relative Liquidity And €:£

- *Relative liquidity determines cross-rates*



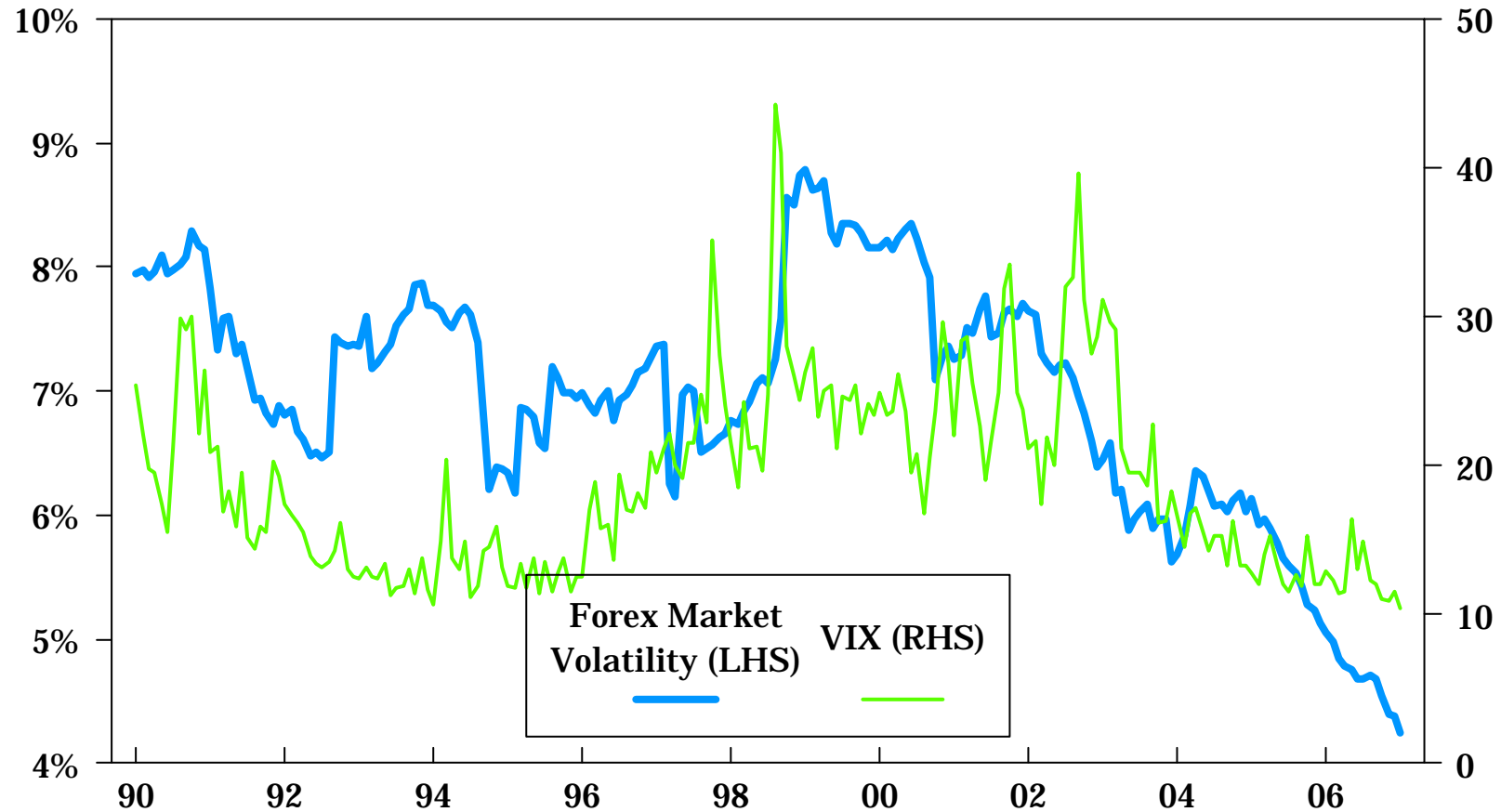
US Liquidity Vs. VIX (Inverted)

- *Again no consistent correlation between level of liquidity and VIX*
- *Volatility tends to jump around upper inflexion point of liquidity cycle*



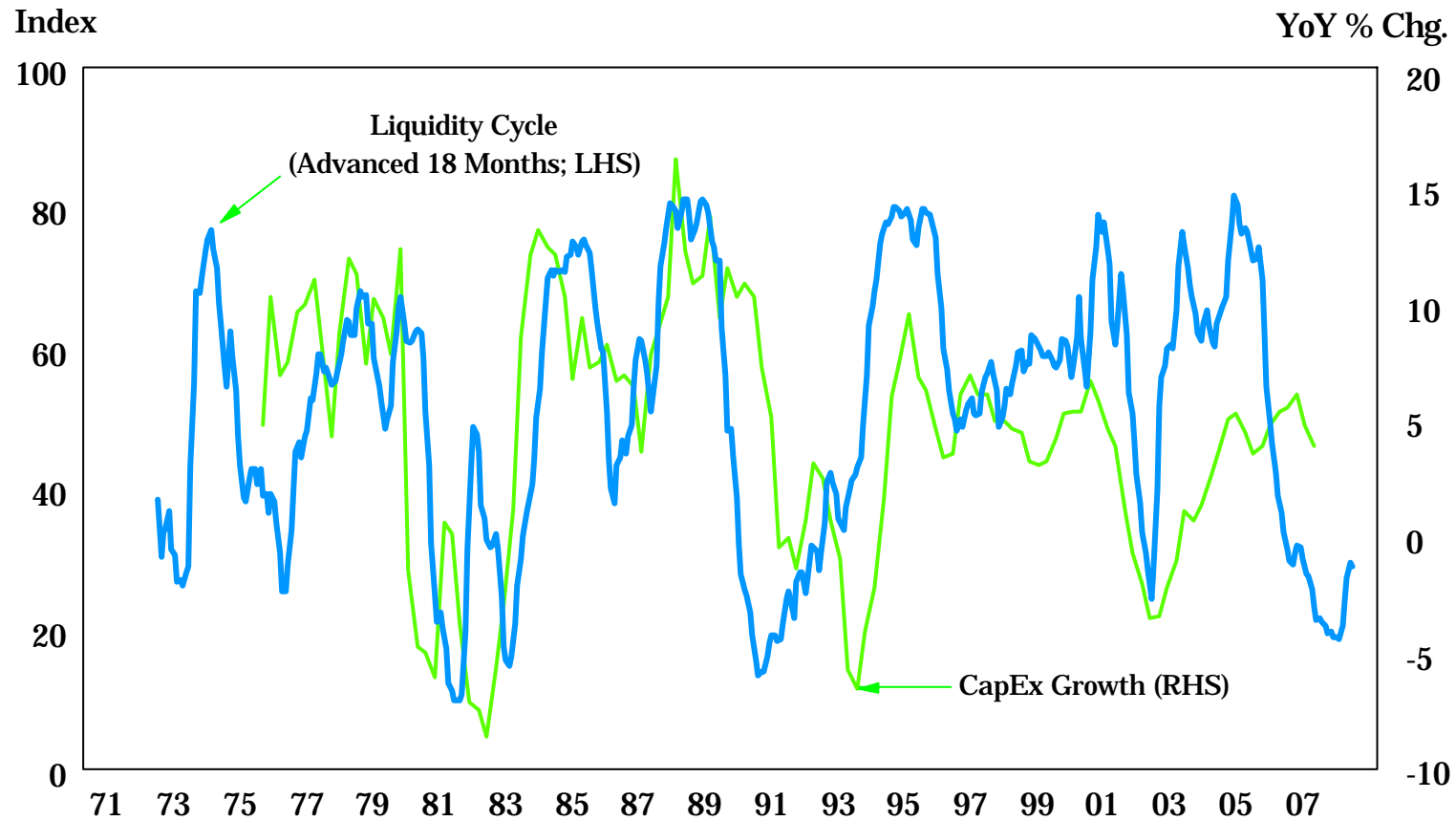
Forex Volatility Vs. VIX

- *VIX tends to be better correlated with Forex volatility*



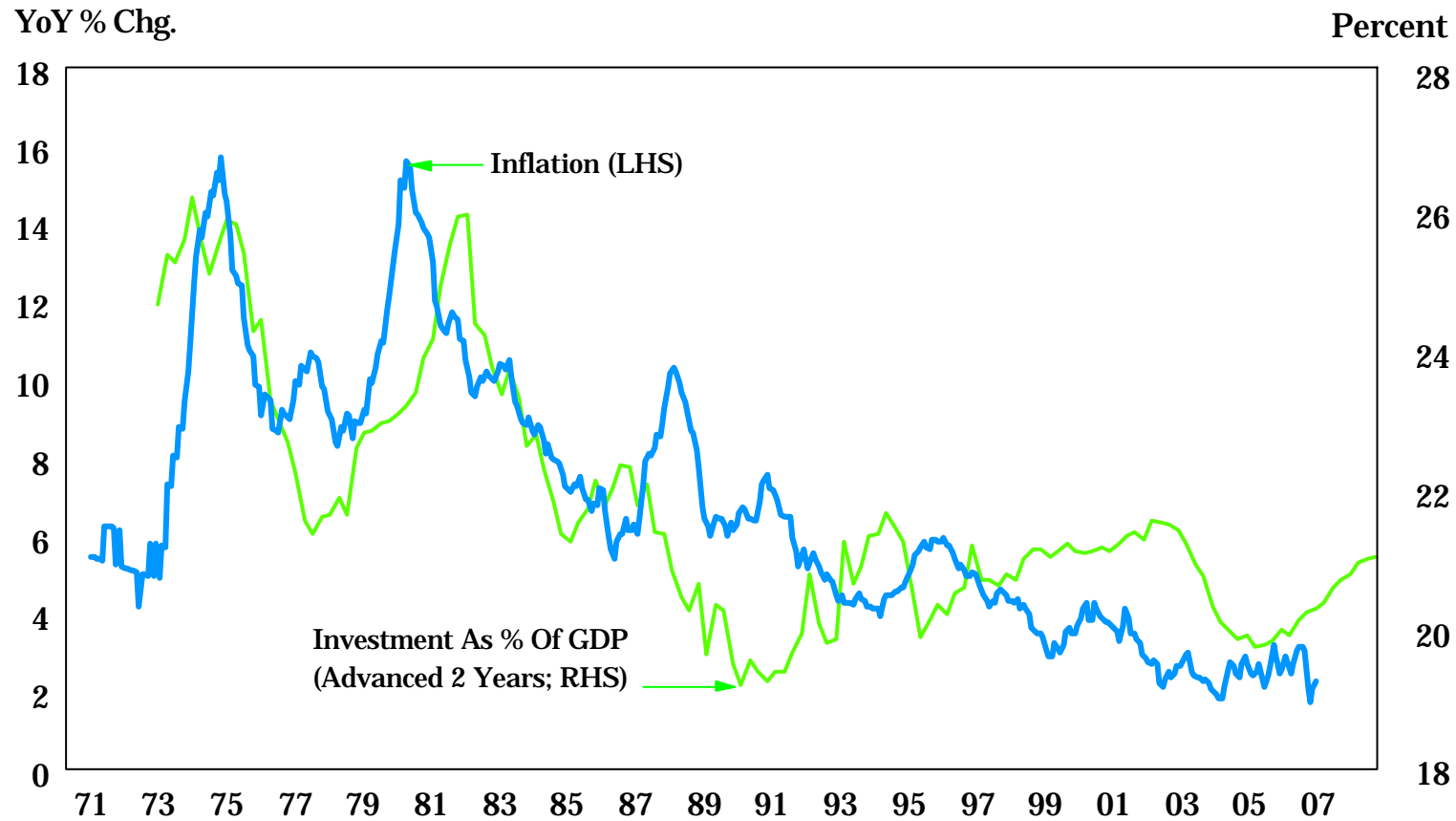
OECD Investment (% GDP) And Liquidity Cycle

- *CapEx is driven by Liquidity 18 months later*



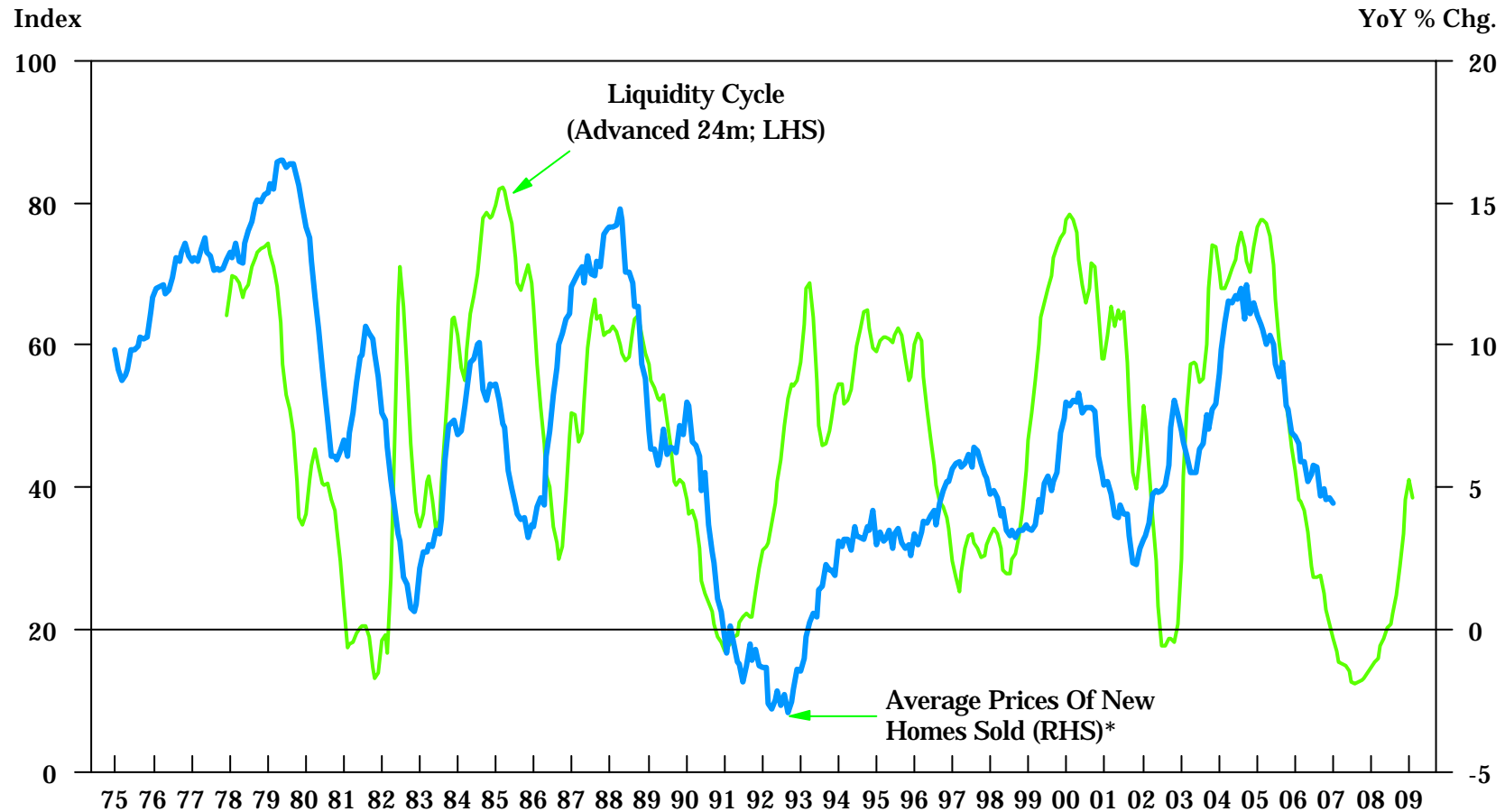
OECD Investment (% GDP) And Inflation

- *Inflation is driven by CapEx 2 years later*



US Liquidity Cycle And House Prices

- *House prices driven by liquidity 2 years later*



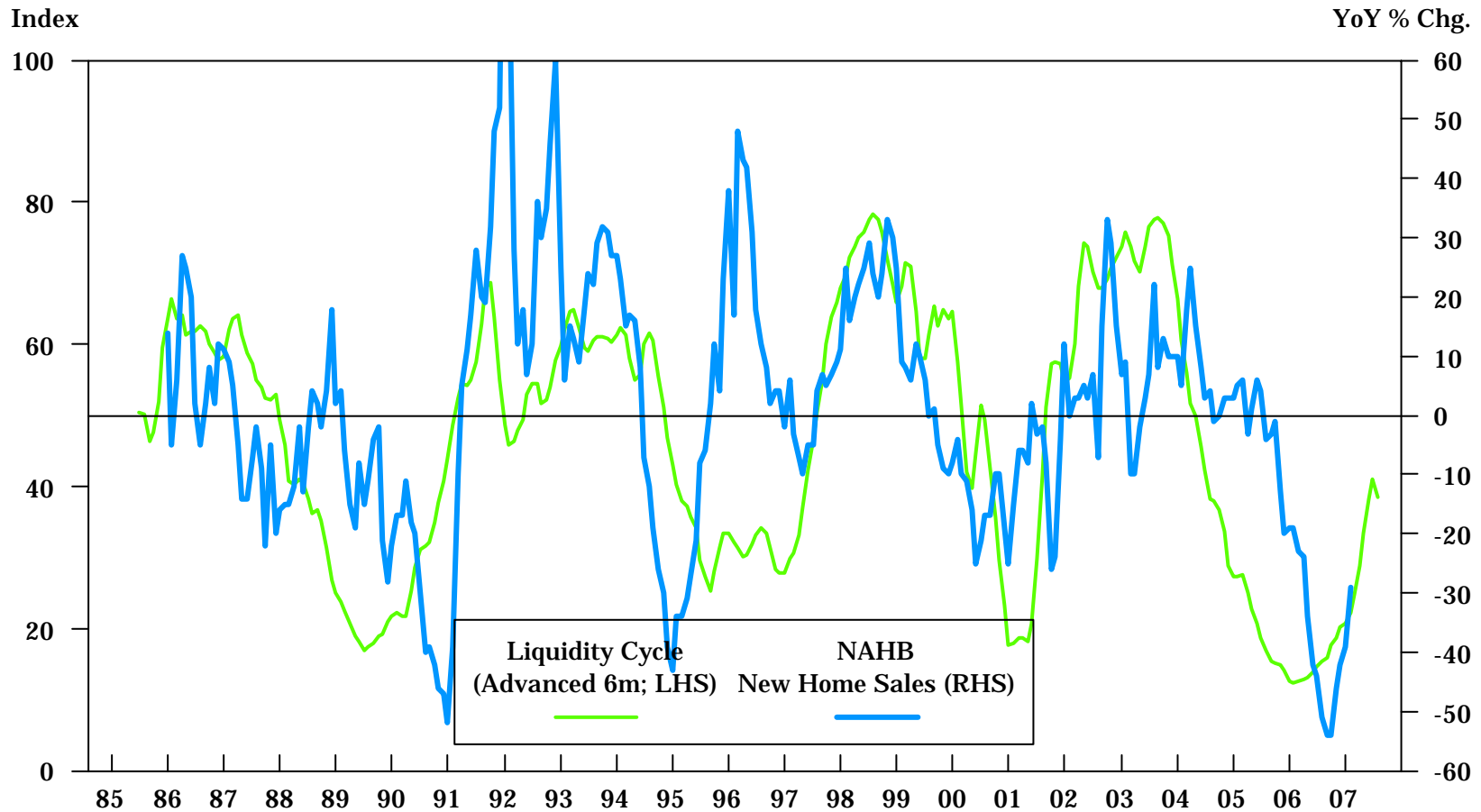
* US Census Bureau



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US Liquidity Cycle And New Home Sales

- *Liquidity leads new home sales by 6 months*



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