

Crescat

*Latin: to grow, increase, expand / spring forth, arise*

Crescat Macroeconomic Update  
June 2009

Crescat Capital LLC

## CRESCAT HAS DELIVERED STRONG ABSOLUTE RETURNS AND ALPHA BY PREDICTING AND EXPLOITING MANY KEY MACRO THEMES

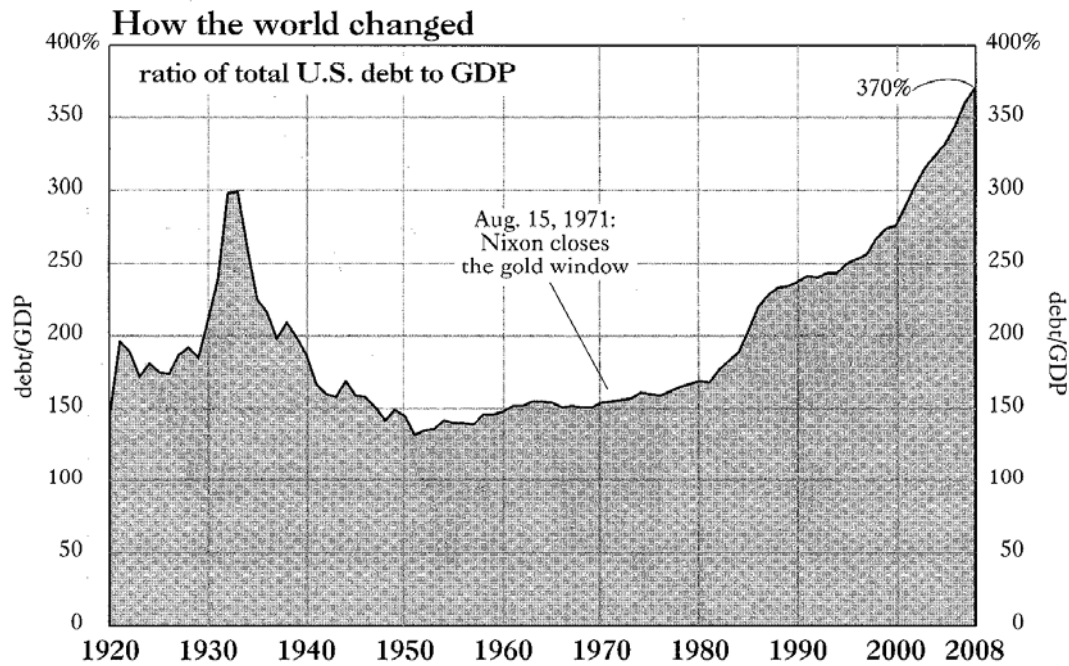
Theme	Crescat Prediction	Crescat Strategy
U.S. Residential Housing Bust	December 2005	Short mortgage stocks and construction stocks
U.S. Dollar Crisis	December 2005	Long JYen, Euro, \$Can and \$Aus; Long precious metals equities and futures
Scarce Energy	December 2005	Long crude and nat gas futures and energy equities
Financial Sector Bust	June 2006	Short banks, insurance companies, rating agencies
Global Economic Slowdown	June 2006	Short industrials and consumer discretionary stocks; long consumer staples
Emerging Markets Boom	June 2006	Long industrial metals equities and futures; long agriculture futures and equities; long Emerging Markets ETFs
Political Shift of Power	December 2006	Short defense; long renewable energy, healthcare IT and infrastructure

This presentation addresses the opportunity arising from the massive global monetary and fiscal stimulus, the most important macroeconomic themes facing today's markets.

# U.S. OBLIGATIONS ARE UNSUSTAINABLY HIGH AT 700% OF GDP

## On-Balance Sheet U.S. Debt

(includes U.S. Govt Debt and Private Debt but not Unfunded Entitlements)



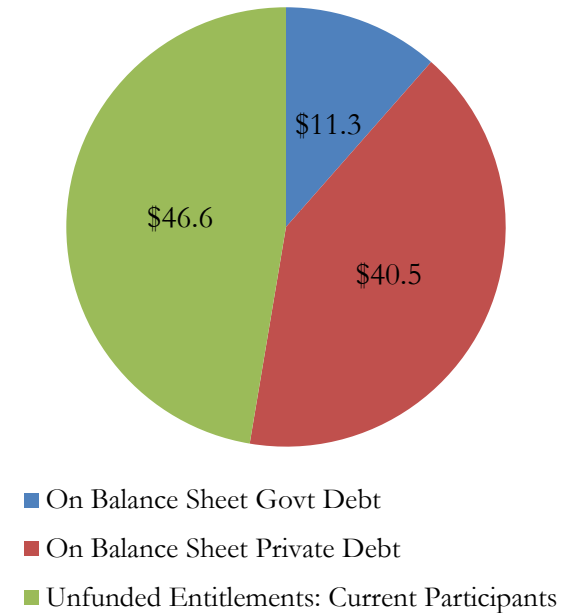
sources: Federal Reserve, Bureau of Economic Analysis, Bureau of the Census

Source: Grant's Interest Rate Observer

## U.S. Debt Including Unfunded Entitlements

(\$ Trillions)

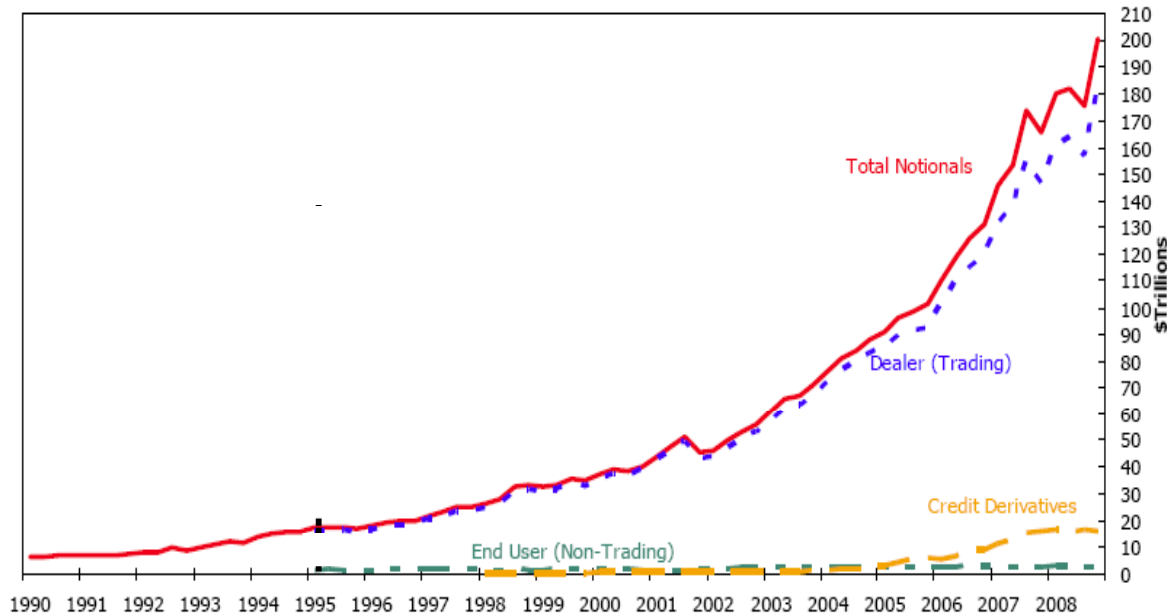
Total = \$98T (700% of GDP)



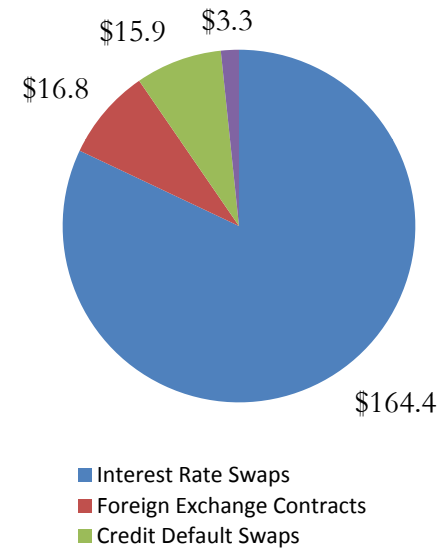
Sources: Government & Accountability Office's FY2008 Financial Report of the United States Government; Department of the Treasury; Grant's Interest Rate Observer; Crescat analysis

# NOTIONAL EXPOSURE AT US BANKS ADDS \$200 TRILLION IN RISK

## Derivatives Notionals by Type of User Insured Commercial Banks



## Derivatives Exposure by Instrument (31 December 2008, \$ trillions)



Source: US Office of Comptroller of Currency Quarterly Report on Bank Trading and Derivatives Activities, Fourth Quarter 2008

Interest rate derivatives exposure is roughly 10 times greater than the credit default swap derivatives exposure that caused the first major leg of the financial crisis. This exposure highlights another driver of the U.S. Treasury Bubble and its unwinding.

## ALL MAJOR US BANKS FAIL CRESCAT'S STRESS TESTS WHEN OFF-BALANCE-SHEET DERIVATIVES ARE CONSIDERED

### Largest U.S. Banks Derivatives Leverage (\$ millions, 12/31/08)

	<u>Derivatives</u>	<u>Equity</u>	<u>Total Assets</u>	<u>Equity % of B/S Assets</u>	<u>Equity as % of Assets + Derivatives</u>
JP MORGAN	87,362,672	166,884	2,175,052	7.7%	<b>0.2%</b>
BANK OF AMERICA	38,304,564	177,052	1,817,943	9.7%	<b>0.4%</b>
CITIBANK	31,887,869	141,630	1,938,470	7.3%	<b>0.4%</b>
GOLDMAN SACHS	30,229,614	64,369	884,547	7.3%	<b>0.2%</b>
WELLS FARGO	5,159,568	99,068	1,309,639	7.6%	<b>1.5%</b>

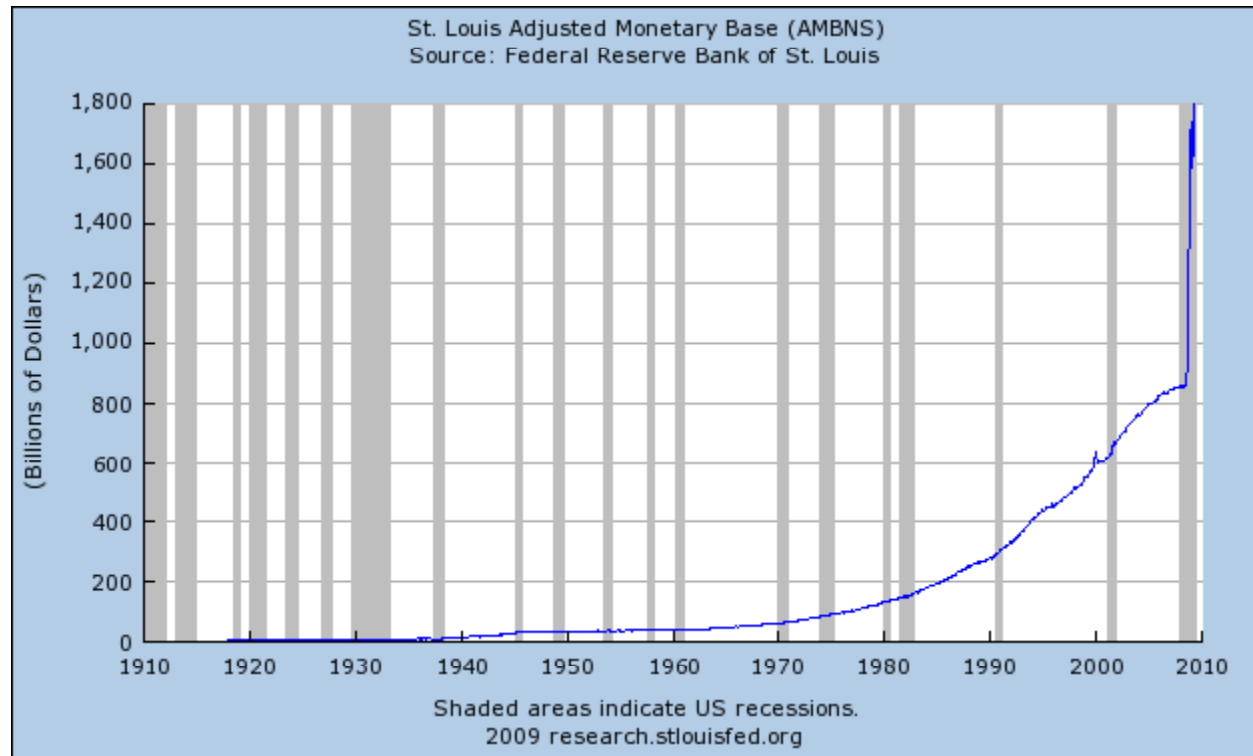
Total                    ~\$200 Trillion

Levels of derivative exposure remain absurdly high at all major banks, a ticking time bomb for round two of the financial sector bust and inflationary bailout.

# THE US FEDERAL RESERVE IS PRINTING MONEY AT A MASSIVE AND UNPRECEDENTED PACE

## US Monetary Base

(Source: U.S. Fed, 6/12/09)



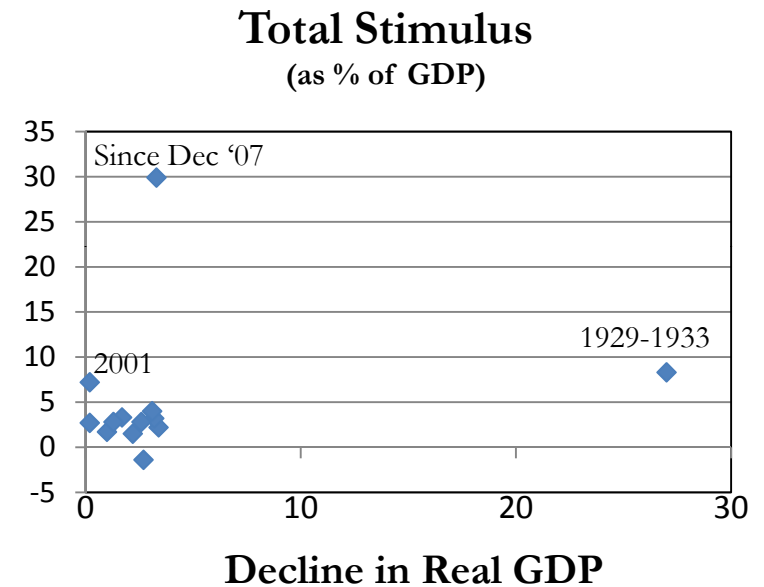
Monetary Base is already up 100% (\$1T) year over year, unprecedented, and is poised to increase by another \$1 Trillion in the next year based on already announced Fed policy.

## SEPARATELY AND COLLECTIVELY, THE FISCAL AND MONETARY STIMULUS ARE “OVER THE TOP”

Peak	Trough	Length (months)	Decline in real GDP	Stimulus as % of GDP		
				Monetary	Fiscal	Combined Stimulus (% of GDP)
<b>Aug-29</b>	<b>Mar-33</b>	<b>43</b>	<b>27</b>	<b>3.4%</b>	<b>4.9%</b>	<b>8.3%</b>
May-37	Jun-38	13	3.4	0.0%	2.2%	2.2%
Nov-48	Oct-49	11	1.7	-2.2%	5.5%	3.3%
Jul-53	May-54	10	2.7	0.0%	-1.4%	-1.4%
Aug-57	Apr-58	8	3.2	0.0%	3.2%	3.2%
Apr-60	Feb-61	10	1	0.7%	1.0%	1.7%
Dec-69	Nov-70	11	0.2	0.3%	2.4%	2.7%
<b>Nov-73</b>	<b>Mar-75</b>	<b>16</b>	<b>3.1</b>	<b>0.9%</b>	<b>3.1%</b>	<b>4.0%</b>
Jan-80	Jul-80	6	2.2	0.4%	1.1%	1.5%
Jul-81	Nov-82	16	2.6	0.3%	2.5%	2.8%
Jul-90	Mar-91	8	1.3	1.0%	1.8%	2.8%
Mar-01	Nov-01	8	0.2	1.3%	5.9%	7.2%
<b>Dec-07</b>		<b>15</b>	<b>3.3</b>	<b>18.0%</b>	<b>11.9%</b>	<b>29.9%</b>

\*Current fiscal stimulus estimated

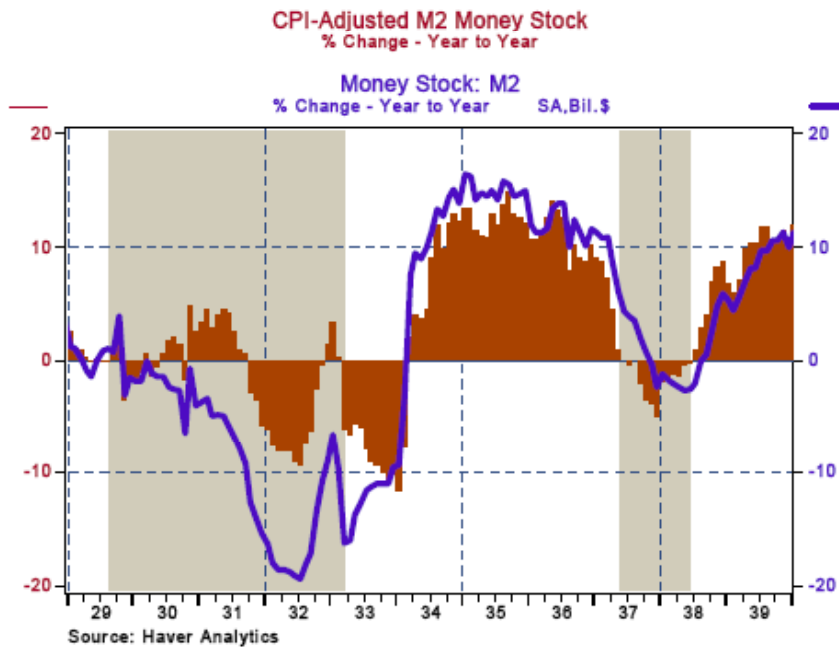
sources: Federal Reserve, Congressional Budget Office/Grant's Interest Rate Observer



Current stimulus relative to GDP is 3.5X the post Great Depression and 7X the inflationary 1970s!

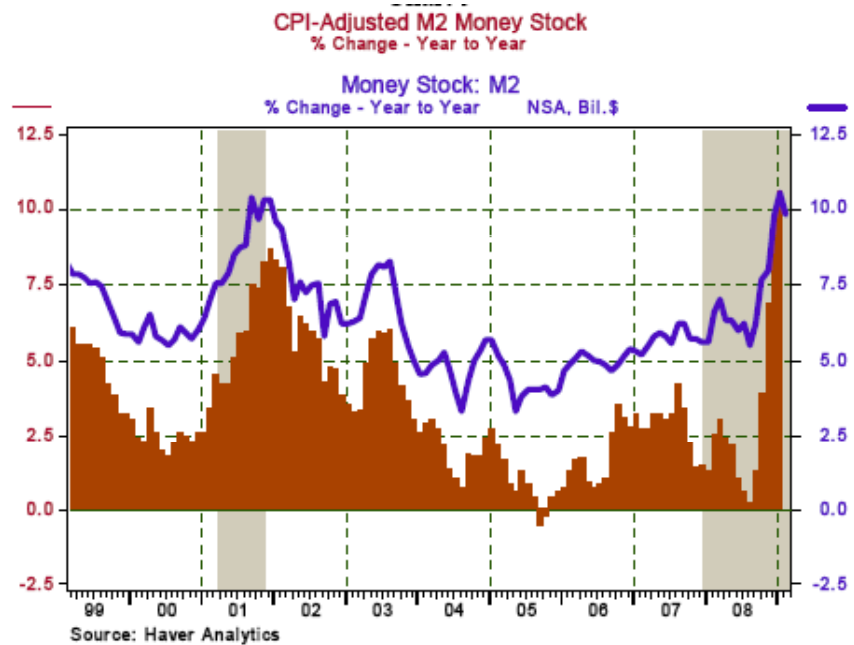
# UNLIKE DURING THE GREAT DEPRESSION, M2 IS NOW GROWING AND LIKELY TO CAUSE INFLATION

Plunged During the Great Depression (1929-1933), Causing Deflation



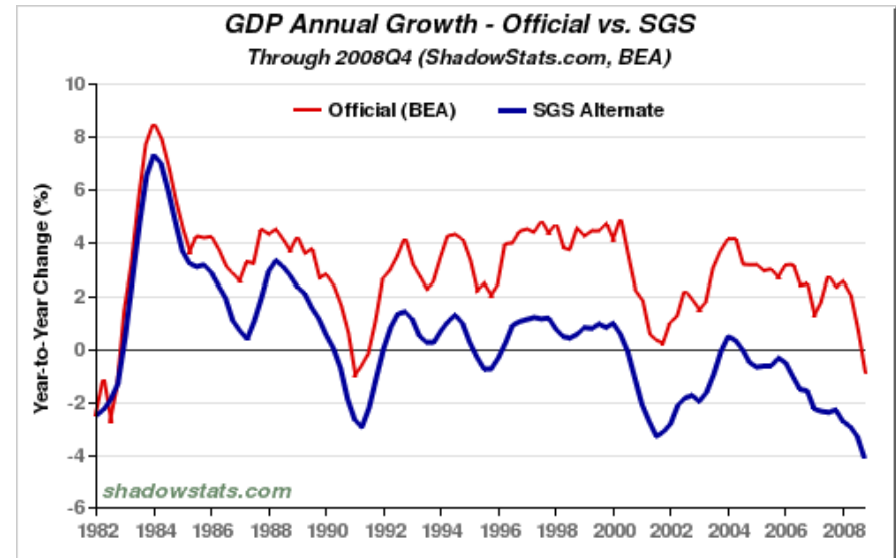
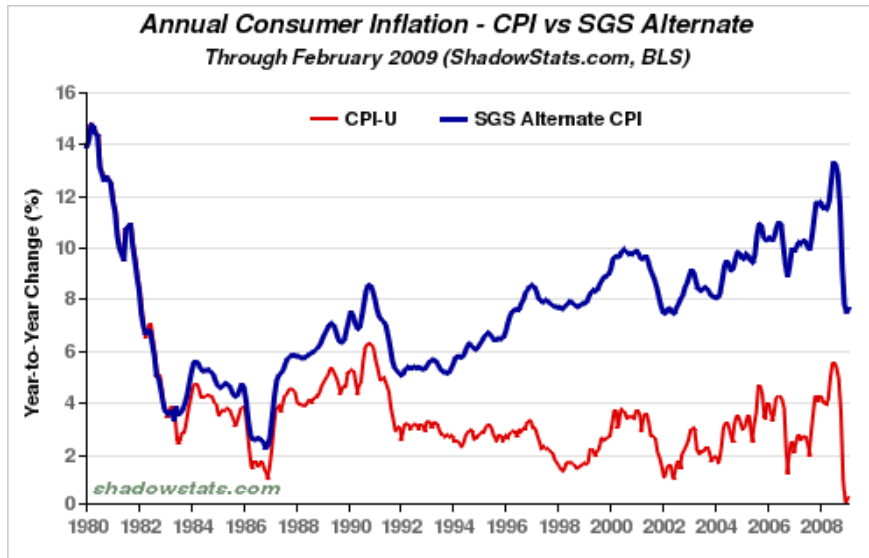
The post-1933 M2 spike was caused by FDR's confiscation of gold and subsequent devaluation of gold relative to the dollar.

High and Rising in the Current Decade, Driving Inflation not Deflation



Already high M2 growth is poised to accelerate off the chart based on monetary base expansion (a leading indicator for M2).

## INFLATION HAS LIKELY BEEN UNDERSTATED, AND GDP GROWTH HAS LIKELY BEEN OVERSTATED, SINCE 1982



Notes:

- Blue line uses the pre-1982 CPI methodology.
- Red line (reported CPI) incorporates the 1982 BLS adjustments to the raw CPI data: substitution, hedonics, geometric weighting, and inconsistent seasonal adjustments.

## GOLD HAS PERFORMED STRONGLY IN EVERY MAJOR WORLD CURRENCY SINCE 2001

Annual Performance of Gold in the Top Seven Global Currencies

Source: Gold Fields Mining Survey

	<b>USD</b>	<b>AUD</b>	<b>CAD</b>	<b>CNY</b>	<b>EUR</b>	<b>INR</b>	<b>JPY</b>	<b>CHF</b>	<b>GBP</b>
<b>2001</b>	2.5%	11.3%	8.8%	2.5%	8.1%	5.8%	17.4%	5.0%	5.4%
<b>2002</b>	24.7%	13.5%	23.7%	24.8%	5.9%	24.0%	13.0%	3.9%	12.7%
<b>2003</b>	19.6%	-10.5%	-2.2%	19.5%	-0.5%	13.5%	7.9%	7.0%	7.9%
<b>2004</b>	5.2%	1.4%	-2.0%	5.2%	-2.1%	-0.0%	0.9%	-3.0%	-2.0%
<b>2005</b>	18.2%	25.6%	14.5%	15.2%	35.1%	22.8%	35.7%	36.2%	31.8%
<b>2006</b>	22.8%	14.4%	22.8%	18.8%	10.2%	20.5%	24.0%	13.9%	7.8%
<b>2007</b>	31.4%	18.6%	10.4%	23.0%	17.9%	17.5%	24.7%	21.5%	29.2%
<b>2008</b>	5.8%	32.5%	32.4%	-1.1%	11.9%	30.4%	-14.9%	0.2%	44.3%
<b>Average</b>	<b>16.3%</b>	<b>13.3%</b>	<b>13.6%</b>	<b>13.5%</b>	<b>10.8%</b>	<b>16.8%</b>	<b>13.6%</b>	<b>10.6%</b>	<b>17.1%</b>

Gold has risen despite fiat government intervention (central bank gold sales) to suppress its price.

Gold has also outperformed cash, stocks, and bonds in each of these currencies since 2001.

# OUR PORTFOLIOS ARE CONSTRUCTED TO EXPLOIT TODAY'S MOST IMPORTANT THEMES

## Crescat Investment Themes

- Financial markets face a continued train wreck from decades of persistently easy fiscal and monetary policy, extraordinary leverage, and pervasive misperceptions regarding inflation
  - Global Fiat Currency Crisis (secular) ... long precious metals futures and mining stocks, long select foreign currencies
  - U.S. Treasury Bust (secular) ... short long term US Treasury bond futures
- Demand will again migrate from paper assets to commodity assets
  - Scarce Energy (secular and opportunistic) ... selectively long energy futures and stocks
  - Commodity SuperCycle (secular) ... selectively long agricultural and industrial metals futures and stocks
- The party is over, and the hangover will linger for a while
  - Financial Sector Bust (opportunistic) ... selectively short banking and insurance stocks
  - Commercial Real Estate Bust (cyclical) ... selectively short Commercial REIT stocks
  - Consumer Squeeze (cyclical) ... long undervalued consumer staple stocks. short highly leveraged consumer cyclical stocks with deteriorating fundamentals
  - Deep Value (opportunistic) ... long value stocks
- Opportunity will follow shifts in global power and in U.S. political power
  - Political Shift of Power (cyclical) ... long Generic Drugmakers, Healthcare IT, Renewable Energy, Smart Grid, Infrastructure
  - Emerging Markets (secular) ... long stocks from resource-rich emerging markets and those with strong domestic consumption growth

# For Further Information

Kevin Smith

Dan Hoskins

**Crescat Capital LLC**

Office: 303-271-9997

Fax: 303-271-9998

Email: [dhoskins@crescat.net](mailto:dhoskins@crescat.net)

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