

# GREEN PARTNERS<sub>LLC</sub>

September 30, 2011

**Dear Partner-Clients,**

Holmes and Watson are on a camping trip. In the middle of the night Holmes wakes up and gives Dr. Watson a nudge. "Watson," he says, "look up in the sky and tell me what you see." "I see millions of stars, Holmes," says Watson. "And what do you conclude from that, Watson?" Watson thinks for a moment, "Well," he says, "astronomically, it tells me that there are millions of galaxies and potentially billions of planets. Astrologically, I observe that Saturn is in Leo. Horologically, I deduce that the time is approximately a quarter past three. Meteorologically, I suspect that we will have a beautiful day tomorrow. Theologically, I can see that God is all powerful, and we are small and insignificant. Uh, what does that tell you, Holmes?" "Watson, you idiot! Someone has stolen our tent!"

The market volatility was roughly on schedule during the third quarter. The Federal Reserve's asset support program ended (QE II), at least temporarily as predicated, on June 30<sup>th</sup>, 2011.

I predicted Quantitative Easing (QE), also known as the balance sheet expansion of the Federal Reserve, would temporarily end and that a trillion dollars in asset support by the Federal Reserve ending would have market repercussions. It did.

While most investment advisors around the world didn't understand the significance of this kind of asset support ending, as equities roared higher (the stars) in the face of a contracting economy and sovereign debt (the tent), I remained resolute that it would have an impact, and it did.

The significant cash, perhaps excessive cash, in our accounts should be a terrific source of serious firepower for opportunities that may arise in this deflationary patch that we appear to be entering. Our future has never looked brighter, as assets have come down across the board we're in a strong position to take advantage of the turmoil. We're also well ahead of our benchmarks over the last twelve months, two years, three years, five years, etc.

On the deflationary front, I believe we've entered a temporary patch of deflation again as the Shadow Banking System continues to deleverage, from a peak of \$20.9 trillion in 2008 to roughly \$15.4 trillion today, which has been offset somewhat by the Federal Reserve's expansionary policies over the last two and half years. With no major offset to credit contraction for the time being (the end of QE II), shadow banking credit continues to plunge along with the velocity of money, which bodes poorly for growth. As a reminder, in a debt-based economy, without debt growth (money loaned into existence), it's very difficult to have economic growth, and therefore employment growth.

On the global front, Europe is aiding to the uncertainty, with insolvent countries and global banking counter-party risks, while growth in China is dramatically slowing now that their building boom is all but over for now. In other words, I wouldn't be surprised to assets get cheaper yet.

I'm staying diligent and cautious with our hard earned money in these uncertain economic times as these data points continue to develop. If the economy becomes too deflationary, I expect there will be—gasp!—another round of Federal Reserve money printing (according to Federal Reserve transcripts), for the simple reason that the sheer size and scope of our national deficits cannot handle a deflationary spiral should it occur (meaning far less tax revenues to the U.S. treasury, as if our treasury can afford that).

From a broad perspective, there are generally two types of investment risks: that of missing opportunity and those of risking money. With the macroeconomic data poor, and the balance sheet expansion of the Federal Reserve off, I am erring more toward the idea of missing opportunity and preparing for a better day. If you'd like me to get more aggressive please give me a call.

Otherwise, I will remain respectful of all the data points I've previously discussed in my letters to you: that sovereign debt and *funding them* is a problem for almost all developed countries, that banks around the world are overleveraged and counter-party risk is high, and that the enormous fiscal and monetary intervention will come with its own problems: deflation on/deflation off, inflation on/inflation off, dollar strong/dollar weak, and so forth.

By sticking to these data points, we are well prepared to be optimally allocated toward what could be the best days ever to come for investment partners (and we've had some good ones!).

### **Alignment of Interests**

Green Partners, LLC is my only business. I run my business as though it will be the only asset I, or my family, will have for the next 100 years. Our mutual long-term success is financial life or death for us. Doing it any other way wouldn't make any sense to me. You can count me in; I treat your money as if it were my own. It's equally important to me as it is to you.

I have a world-class, long-term partner base completely unrivaled in the financial industry. Your long-term disposition gives us the long-term arbitrage advantage! You are the best and my gratitude is simply beyond the reach of my pen.

Yours truly,

Nicholas Green