If you had more money than you knew what to do with…

So says Don Sturm, owner of two community banks in Colorado. And Mr. Sturm's complaint is not that he's been amply paid (although he may have), but that depositors are flooding in at a rate that outstrips his banks' ability to usefully redeploy the money. This is QE2 at ground level. Investors fleeing the treacherous equity markets are selecting safe bank deposits, but are receiving nothing in return. In some cases banks are actually charging large clients for the privelige of being depositors.

Banks are still struggling to find enough good places to put the money they have. Although the system is awash with liquidity that other necessary component of inflation which is velocity (in other words, how quickly money gets recycled) is notably absent. Hence the ballooning money supply is not yet translating into inflation. But M2 is growing at an increasing pace – according to figures from the Federal Reserve its annualized growth has quickened from 10% over the past year to 24% over the past three months. Still no sign of a problem, and yet ten year treasury notes yielding 2.25% or high grade corporate debt at just over 4% provide scant protection should money velocity reappear and link up with already ample money creation.

On a different topic, how exactly does an investor in Greek debt get comfortable with a "voluntary" 60% loss? To accept any negotiated settlement there needs to exist a worse alternative, and it's hard to imagine what that might be. Since the purpose of a voluntary loss is to avoid triggering a payoff on CDS contracts, it's a stretch to see why any holder of Greek debt who also owned such CDS insurance would accept an uninsured 60% loss rather than endure a bankruptcy and so retain the ability to claim on their insurance coverage. Maybe there are very few holders of CDS who use it to insure against risks they already have. It increasingly appears as if most buyers of CDS protection were smart enough to avoid actually needing the insurance. It’s as if most homeowners insurance was owned by people on their neighbour’s house rather than their own.

We continue to be short the Euro through a long position in EUO. Although Europe’s leaders are clearly focused on the issues at hand, the latest recapitalization needs are being dismissed by analysts as simply covering the loss from a mark-to-market of existing bond holdings at current levels rather than simulating a more stressful scenario than currently exists. The EU’s leaders are getting there but at a painfully slow rate, and southern Europe is most likely already in a recesson. As is often the case, it looks as if the economic cycle in the U.S. will be ahead of Europe’s, which should provide support for the $ against the €.