Bedrock Newsletter

Friday, November 22th 2013

We are starting to feel a year-end breeze… We have a small ironic note to underscore Obama's health(care) troubles- Having won his Presidential mandate against Mitt Romney because Mitt was "Private Equity job destroyer" it is amusing to note that Tim Geithner leaves his Treasury Secretary position to join a large NY based private equity group Pincus Warburg…

We have been advocates of the school of thought that an investor should read the markets in order to predict the next-day news, rather than read the papers to predict the markets... Whilst we maintain that predicting anything is difficult, especially the future… Well, this said, we read the markets and see ongoing upwards pressure on equities and in parallel, a "softness" in the fixed-income sector. We read in this a slow and steadily improving economy. The equity markets, whilst smaller than the bond markets in terms of absolute value, are probably a better indicator as there is less direct government and central bank influence. In confirmation of our "readings", on Tuesday, Federal Reserve Chairman Ben Bernanke said that the Fed would maintain its ultra-easy U.S. monetary policy for as long as needed and only begin to taper bond buying once it is assured that improvements in the labor market would continue. He noted that the Fed Funds Rate can remain near zero 'well after' the unemployment rate hits 6.5 percent and that unemployment targets are thresholds, not triggers. The U.S. unemployment rate is currently at 7.3 percent. In a speech to the National Economists Club that echoed dovish comments by his nominated successor, Janet Yellen, Bernanke also said that while the economy had made significant progress, it was still far from where officials wanted it to be. "The FOMC remains committed to maintaining highly accommodative policies for as long as they are needed," he said in prepared remarks, referring to the policy-setting Federal Open Market Committee.
Separately, the OECD on Tuesday knocked almost half a percentage point off its forecasts for global growth this year and next, blaming a slowdown in emerging markets, brinkmanship over the US debt ceiling and concerns over the Federal Reserve's tapering for the downgrade. The Paris-based organization promoting the world's largest advanced economies said the global economy would expand 2.7 per cent this year and 3.6 per cent in 2014, compared with estimates of 3.1 per cent and 4 per cent respectively, made in May.
Wednesday, Iran's Ayatollah reversed course on Atomic issues - Won't bend to the West's demands… adding that Israel will disappear in the near future. Even his negotiating team in Geneva is surprised. Maybe Netanyahu's distrust is well-placed? For us, it is a reminder that even as we smile as markets rise, there is at least one very big very dark cloud somewhere… just behind the Taper-Horizon…

A report on Wednesday from Bloomberg News cited two unnamed sources as saying the European Central Bank was considering lowering the deposit rate for cash it holds overnight for banks to below zero. That knocked the Euro down about 0.7 percent against the dollar, its steepest loss so far this month. And the single currency was still nursing its losses on Thursday as it hovered at $1.3426 in Asia trading. Whilst we don't think the ECB realistically has this on the table at the moment, it would make some sense in terms of nudging-up the Euro-zone inflation rate which has been dangerously drifting lower towards deflationary levels. Inflation in the 17-nation currency bloc slowed to 0.7 percent in October, the slowest pace in four years and less than half the ECB's target of just under 2 percent. Economic growth was 0.1 percent last quarter, down from the 0.3 percent in the three months through June that marked the end of a record-long recession. The jobless rate is at a record 12.2 percent!!
Bank of America equity strategists said that of the 272 investors that participated in a survey they conducted, two-thirds considered equities to be the best asset class to hold in 2014. "Clients are absolutely bearish on bonds and commodities with only 2 percent finding government bonds and commodities appealing for 2014," they said in a note published on Tuesday. Warren Buffet lent some support to this in a CNBC interview Tuesday "I would say that equities are in a zone of reasonableness,"
A weekend thought- If a man will begin with certainties, he shall end in doubts; but if he will be content to begin with doubts, he shall end in certainties.

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Currencies

- EURUSD looks to be almost unchanged on the week. In a data-light week we saw range bound trading. Until EC consumer confidence came in weaker than expected, lopping off 120 points and the EUR dropping from 1.3550 to 1.3430 only for the EUR to recover a little of the lost ground to be bouncing against the 1.35 figure at the end of the week. With German IFO numbers this morning, the pair made a dash higher but we are still at or around 1.35.
- EURCHF traded lower and lower through the week from 1.2347 to 1.2306 this morning. USDCHF, much like EURUSD, has been relatively unchanged on the week at about 0.9140. Although the EC data did move the pair from 0.91 to nearly 0.92 on Wednesday. The USD has continued to remain relatively static this week in a base building market… Will it be a merry Christmas rally for the USD?
- USDJPY moved steadily higher again this week, closing each day at or above 100.00. Post the FOMC notes and with the big rally in the Nikkei the pair moved to a recent high of 101.35 this morning. With the pair seemingly comfortable at or around these levels, we believe that the rally in equities and the continued weakening of the Yen will be one of the important moves going forward.
- AUD has slipped and slipped quite far. With the Chinese data fully digested the pair has dropped from 0.9450 to as low as 0.9150 this morning. As the Aussie songs says, "Tie me Kangaroo down, Sport. Tie m Kangaroo down!". If the trend continues they will need to tie down most assets; just as the Aussies may need a lifeline… so too may the currency!
- With the BOE continuing its path of low interest rates and asset purchase schemes and little changes on the horizon, the Pound has maintained its highs of 1.62 this morning. The strengthening of the pound for an importing nation is obviously a benefit, so perhaps a consumer led recovery will ensue… we just wonder how that reduces the 900% leverage that there is in the UK economy…?

Fixed Income

- The US 10Yr started the week at 2.70% and eventually peaked at 2.83%, only to slide back to 2.77% this morning. Again the rates are within the boundaries of 2.5% and 3.0%. The FOMC minutes (without anything really new in them) caused the bonds to sell off, but again until there is a true shift in policy we believe the yields will oscillate in the range.
- The yield on the German Bund moved higher on the US FOMC, having briefly dropped on the weak EC numbers. The yield for the majority of the week was between 1.70% and 1.72%, briefly spiking to 1.78% on the US FOMC wording. We have settled back a little, in true German style there should not be much deviation from the steady line, and we are currently at about 1.75%.
- Spanish yields were relatively stable and are now trading completely instep with Italy. The yield moved from 4.05% to a high of 4.16% only to settle lower this morning to 4.08%.
- Italy has regained is negative spread over Spain and is trading in lock step…. And with the fear of repeating ourselves… The yield moved from 4.07% to a high of 4.15% only to settle lower this morning to 4.08%. Looks familiar?

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Equities

- Developed equities lost 0.32% for the week – as of yesterday's close – as measured by the MSCI World index. Global equities lost on the back of a negative OECD growth forecast coupled with rising speculation that the Fed will start tapering its asset purchases.
- The EuroStoxx index lost 0.30% for the week. European equities started the week on a strong foot on news that Eurozone trade surplus grew more than expected in September, easing concerns on the current EUR strength. Shares were quick to reverse their gains as German Economic confidence figures came in lower than expected, and the OECD cut its global growth forecast. Stocks have since been modestly supported on ECB talks on potential negative deposit rates to stimulate the economy.
- The S&P 500 lost 0.13% for the week, as of yesterday's close. US stocks lost ground at the start of the week on increasing speculation that the Fed is coming close to start tapering. However, stocks rose sharply on Thursday as weak manufacturing data eased such speculation.
- The Nikkei outperformed for an additional week, rising 1.42%. Japanese equities reached a 6 month high as the BoJ said the country's economy was recovering moderately and said it had no plans of reducing its stimulus measures. As stimulus is expected to be maintained, economists widely forecast that the BoJ will need to postpone the time-frame of achieving a 2% inflation target.
- In terms of sectors, Material and Utility stocks were the worst performers (falling 1.32% and 0.85% respectively), while Healthcare and financial stocks gained 0.37% and 0.12% respectively.

Emerging Markets

- Emerging Market equities were more or less flat, dropping only 0.09% for the week – as of yesterday's close – as measured by the MSCI EM index. EM Latin American and EM Asian shares lost 1.27% and 0.28% respectively, while EM European shares gained 0.43%.
- The Shanghai Composite gained 2.83% for the week. Chinese shares rose sharply on Monday as Beijing released a detailed reform plan, set to increase foreign investment into the local financial sector and also average prices of new homes made fresh new highs. Chinese shares gave back some of the gains at the latter part of the week on news of weak manufacturing figures and on speculation that the government will announce property curbs.
- The Bovespa lost 1.43% for the week, as of yesterday's close. Brazilian equities rose on Monday following China's announced range of economic reforms. However, shares fell the most in 7 weeks the following day on worries that the Brazilian economy will remain static going forward.

Commodities

- Commodities gained 0.86% for the week, as measured by the S&P GSCI Total Return index. Energy was the best performing sector, rising 1.40% for the week, while Precious Metals and Industrial Metals lost 3.47% and 0.31% respectively.

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- Gold lost as much as 3.74% for the week, and is currently trading at $1'248 per troy ounce. The metal sold off as the Fed signalled it may ease stimulus in the coming months as the economy grows, cooling demand for an investment haven. Gold analysts are the most bearish on the metal since June, with Goldman Sachs predicting “significant declines” in gold prices, with bullion set to fall at least another 15% in 2014 in their view...
- Crude oil gained 0.85% for the week, and is currently trading at $95.50 a barrel. Oil lost at the start of the week on the back of tapering speculation and as Saudi crude exports approach an 8 year high. Gains were made at the latter part of the week as negotiations on Iran's nuclear program did not yield any prospects of easing of sanctions on the country.

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