Friday, January 25th 2013

Another uneventful week. We like this ☺

We did see elections in Israel which surprised the Prime Minister Netanyahu who had called the elections to strengthen his hold only to lose power. What will this mean? No one knows until we see a new coalition. France is entangled in Mali and the Algerian government is embroiled in its own terror-fight. The risks are seen in Oil prices which have been rising into this new uncertainty, now trading north of $96/bbl.

On Tuesday we saw Google [GOOG] and IBM [IBM] both strongly beating earnings expectations and both rose over 5% afterwards. Then on Wednesday the much maligned Netflix [NFLX] showed a nice profit with EPS of $0.13 vs. an expected loss and then told us they had substantial increases in subscribers, resulting in a 50% rise in the stock. Apple [AAPL] then disappointed with poor iPhone 5 sales, lower than expected sales of other products and a resulting disappointment in EPS. The shares got slammed over 12%. Given Apple's huge market capitalization, this big drop affected the indices (except the DJIA in which it isn't included). Amazingly, Apple has $137 billion in cash, which is about $150/share (fully a third of its market cap.). How far can it fall?
Somehow though, the S&P 500 managed to trade through the 1'500 level whilst falling back some for the close.

The market leadership has moved from technology to energy. Geopolitics or is it a further signal that the economy is pulling itself out of its morosity?

The International Monetary Fund cut its global growth forecasts and now projects a second year of contraction in the euro region as progress in battling Europe's debt crisis fails to produce an economic recovery. The world economy will expand 3.5 percent this year, less than the 3.6 percent forecast in October, the Washington-based IMF said today in an update of its World Economic Outlook report. While the fund projects growth this year increasing from last year's 3.2 percent pace, it expects the 17-country euro area to shrink 0.2 percent in 2013, instead of growing 0.2 percent as forecast in October.

We are increasingly concerned about the risks to social unrest which might develop on the back of poor employment data: In Spain, the unemployment rate exceeds 25% and for the young, it is now above 50%. Revolutions were started for much less reason than this! World unemployment could top record levels this year and continue rising until 2017, the International Labor Organization (ILO) said on Tuesday in its annual employment report. 2009 currently stands as the worst recorded year for world unemployment, with 198 million people across the globe without work. In its 2013 Global Employment Trends report, the ILO forecasts unemployment numbers will rise by 5.1 million in 2013 to reach 202 million, topping 2009's record. The report also predicts unemployment will rise further in 2014 to reach 205 million.

Where is the world going? We are never certain and listening to the Davos luminaries talking, they don't have much clearer insights than we have. Whilst we sense an improvement of mood in the markets, we do recognize that these have gained more ground over the past few years than the general state of the economies warrant. As such, we acquired some protection on equities- One can't change the direction of the wind, but one can adjust his/her sails to always reach the destination. For us, the destination is firstly keeping what we have and then finding a little more…

To expect the unexpected shows a thoroughly modern intellect. Oscar Wilde. Have a fine wintery weekend!

Bedrock Newsletter

Currencies

- EURUSD did nothing all week trading around 1.3320, except for the Twitterati comments on the (false) rumours of the resignation of the head of the German Bundesbank. The mid-week move caused the EUR to drop from 1.3360 to 1.3260, only to be back to where it was within a couple of hours. With good Zew figures out of German and positive performance in the equity markets the EUR has rallied into the end of the week. Finally charging up to 1.3460 this morning. With the exception of the Goldman Sachs trading desk, most technical analysts are screaming for a pullback in the EUR, we reiterate that we agree – and strongly agree at that!
- The CHF has pulled back some of its weakness from last week against the USD, but is exactly where it finished last week against the EUR (exactly as you would expect as EURUSD is higher on the week). The USDCHF has moved from 0.9350 to as low as 0.9265 this morning. The SNB freight train will be very happy to see the EURCHF at these elevated levels. Moving from 1.2450 to 1.2325 on Wednesday and roaring back to the highs since then. With the majority of Corporates and institutions still long their CHF balances the next move higher in EURCHF will be swift and direct. If the move occurs, 1.30 would be very much the target.
- There is more drama in the JPY currency markets this week than in Puccini's Madame Butterfly. USDJPY opened the week at 90.10 only to see the JPY strengthen on a trading view that the JPY was oversold and on expectations from the BOJ meeting minutes. The USDJPY dropped to as low as 88.00 on Wednesday morning. Clearly, post this up move in the JPY, both Abe and the Finance Minister felt they needed to be MORE explicit and left the market in no doubt that the JPY will weaken, and weaken a lot further – the USDJPY is now at 90.80. We suggest that whilst Abe is at the helm, heed his words – the JPY will weaken. The Japanese want inflation… and they want it now.
- AUD saw some strength at the beginning of the week moving from 1.0510 to 1.0580. This strength was short lived though, and the AUD has moved lower ever since, trading to 1.0440. With a general USD bid tone in the market we feel that this could be the start of a move lower, especially if the equity markets turn lower as we expect.
- Cable… cable… cable. Unfortunately the British pound is not faring well at the moment. Along with the other historically higher yielding currencies (CAD, AUD etc), the weakness is clear, obvious and unashamedly one directional. With the UK Q4 GDP coming in worse than expected the pound has plummeted from as high as 1.5880 in the week to 1.5740 on the news. Unfortunately we do not see anything that will reverse this trend and see continued weakness in Cable to come.
- The ZAR had yet another poor week of trading against the USD weakening from 8.85 to 9.09 on the week. A general pattern of severe weakening of the EM and old-school HY currencies seems to be emerging. This is not positive for global risk in general.

Fixed Income

- Treasury yields on the 10-year were bought after the US holiday on Monday seeing the yields slide a little lower from 1.86% to as low as 1.80%. With better than expected Jobless figures the bonds reversed course rapidly and sold off sending the yield to 1.89% this morning. The 30-year bonds have followed the same pattern as the 10 Year moving to as low as 3.00% on Thursday, jumping post Jobless Claims to as high as 3.08%.
- The German 10-year Bund was sold at the start of this week seeing the yield move from 1.56% to as high as 1.62%, only to see it bought heavily through to the jobless claims

yesterday, causing the yield to sink to 1.51%. We are now trading 1.60% after the US jobless figures.

- Spanish yields showed a similar pattern to last week. They issued short term paper at the lowest yields for a very long time, halving the rates they paid in the last auction. The issues were in fact 4 times oversubscribed. This picture does not translate to the longer part of the curve though, the 10 Year note moved up from 5.07% to 5.25% across the week. It also looks like Corporates are taking their opportunity to refinance at these levels with a plethora of Spanish Corporates coming out with new issues this week.
- The Italian 10 Year debt was bought quite soundly this week. The yield moved from 4.20% to 4.08%. We do not see how this will last unless the banks are forced to buy up the debt a la Berlusconi-era economics.
- This week the data is a little distorted as the US was shut on Monday but the US HY seems to have fared better this week on a relative basis, with the EU HY sinking the most at -0.53%.

Equities

- Developed equities rose by 0.58% for the week as measured by the MSCI World index (as of yesterday's close) as upbeat global factory data encouraged investors to take on more risk, offsetting disappointing earnings from Apple.
- European stocks rose by 1.15% this week, as German shares led Eurozone exchanges higher as strong Ifo figures sent the DAX to a 5-year high on Friday. Earlier in the week, news of a pickup in Chinese factory activity bolstered investor's sentiment.
- US stocks rose by 0.59% over the week, briefly sending the S&P 500 above 1'500 on Thursday for the first time since 2007, as an unexpected drop in jobless claims and better-than-forecast earnings offset a slump in Apple. The benchmark has climbed for seven days, the longest winning streak since 2006.
- Japanese stocks surged on Thursday, snapping up a three-day losing streak after strong Chinese manufacturing data helped firms with high exposure to the world's second-largest economy, while exporters gained ground after the yen finally weakened. As a result the Nikkei ended the week up 0.12%.
- In terms of sectors, Healthcare and Energy led the gains (+1.22% and +1.05% respectively), while Information Technology was the only sector to be negative (-0.41%), driven down by Apple's nearly 10% drop over the week.

Emerging Markets

- Emerging Market equities were down this week, as measured by the MSCI EM which lost 0.78% as of yesterday's close. EM stocks underperformed their developed counterparts as EM Asian shares fell 1.26%, offsetting gains in EM Europe and Latin American shares (+0.22% and +0.13% respectively).
- The Shanghai Composite dropped by 1.10% over the week. Signs of improvement in China's manufacturing sector were not enough to prevent stock markets to slide. The encouraging factory data only helped the index to reach an intra-day peak on Thursday close to 2'363 – the highest level in eight months – before it tumbled into negative territory amid profit taking.

- Meanwhile, the Brazilian Bovespa dropped by 1.27% for the week (as of yesterday's close), after Brazil reduced energy costs more than previously announced and policy makers said they will keep borrowing costs at a record low even as inflation exceeds targets. As a result, the Bovespa collapsed by 1.29% on Thursday.

Commodities

- Commodities rose by 0.51% this week, as of yesterday's close, as measured by the S&P GSCI broad commodity index. This week Industrial metals and Energy were the strongest performers (+1.09% and 0.79% respectively), while Precious metals and Agricultures declined (-0.96% and -0.78% respectively).
- Agriculture lost ground as Export inspection figures came in stronger than expected across the board, as well as speculation that high prices will curb demand.
- Gold fell %0.75 for the week and is currently trading at $1'671 per troy ounce. The precious metal was little changed at the beginning of the week, and has started losing ground on Wednesday following better than expected Eurozone confidence figures. Gold lost further on reports of a fall in Jobless claims on Thursday, providing further indications that the state of the world economy is improving.
- Oil traded in a choppy fashion during the week, rising from $95.70 to $96.80 at the start of the week, on the back of news that the US will lift its debt limit, only to drop down to $95 as the IMF released the forecast for slower global growth. Oil finally regained its uptrend on Thursday following better signs of global economic growth, as well as news of a drop in stockpiles, ending the week +0.17%.
