Friday, December 13th 2013

It is a scary Friday (for some), being the 13th… Last Friday optimism reigned as a CNBC article proclaimed "It's that special time of year, when stock traders say Santa takes the reins. Stocks should be buoyant in the week ahead, helped by year-end seasonality—or maybe Santa. The "Stock Trader's Almanac" says the official "Santa rally" takes place in the several days after Christmas, but traders expect to see a fairly merry market clear on through December now that the November jobs report is out of the way". Well Santa's Web connection must be down, as at least for this week, he didn't read this outlook… We have had a volatile, down-week.

On Wednesday, perhaps for lack of specific information, markets chose to reawaken fears of tapering... DJIA off 0.8% NASDQ off 1.4% and S&P -1.13% Then we learned that Stanley Fischer was about to be nominated as Vice Chairman of the Fed... just retired from running the Central Bank of Israel (with much acclaim); A master of inflation containment whilst reducing interest rates- is it a hint to the direction the Yellen Fed will follow?
Thursday we saw poor initial jobless claims at 368K, coupled with strong November retail sales (up 0.7%) vs. + 0.6% for October- conflicting and confusing data hitting soft and illiquid year-end markets. The Markets chose to overweigh the bad employment data and fell further.
An interesting observation; on the back of record highs of equity markets, scary tapering talk affecting bonds we see that hedge fund managers are attracting billions of dollars of fresh investments and launching new vehicles, even though their performance has fallen behind roaring equity markets this year. According to figures from the data provider Preqin Hedge funds have brought in $360 billion this year through investment profits and inflows from investors, an increase of 15.7 per cent on their assets under management since the end of 2012 It makes sense though… Buy equities at all-time highs? Buy bonds into tapering risks? Or go where both risks are hidden behind a veil of trading on the long and short sides?

U.S. household net worth climbed to a record in the third quarter as home prices marched higher and the value of stocks and mutual funds surged, boosting the economic outlook. The Federal Reserve said Monday net worth increased $1.9 trillion to $77.3 trillion in the third quarter, the highest level since records started in 1945. The grain of salt on this wonderful and uplifting data is that there are clearly many more US household now than back then- Is the average net worth at its highest? Probably not…

This week a research paper out of Goldman Sachs listed 8 reasons why the Fed will NOT commence tapering quite yet (the essence is summarized herewith;

1. Evans and Rosengren said earlier this year that a trend of 200K+ monthly job creation was a pre-requisite to tapering. We a sequence of 3 below, two at the number.
2. Unemployment at 7% appears to be on Bernanke's target, except that this is achieved through a low participation rate.
3. Core inflation ("PCE") fell again to 1.1% whilst the Fed targets 2%.
4. The FED says they care about liquidity conditions and financial stability so the timing presents an issue. We saw what happened in May and imagine it on Christmas week…
5. Mortgage rates are over 100bps higher than May when the first talk of tapering took place.

6, 7, & 8 are subjective, political reasons.

Now that the US$ has chosen to plunge against the Euro and rise against the Yen, and gold losing its lustre at $1'223/oz. we ask an intellectual question- Is the Euro the new reference currency? The only one with no intervention! It has no "daddy"… In the USA, the Fed manipulates interest rates sets and moves the FX, Japan using stimulus, the Swiss setting and managing CHF/Euro and the Yuan is set by decree. A neutral value set purely by markets… A long way from the premature announcements of its demise… "The most important thing in communication is hearing what isn't said". Peter Drucker

May your weekend be less cold than the Swiss one…

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Currencies

- EURUSD was range bound between 1.37 and 1.38, starting at the lows and creeping higher again through to Wednesday, only to slip to 1.3710 this morning. The US budget "solution" seems to be front and centre in the newswires, but agreeing that you agree on what should be done and voting in agreement is tantamount to treading water blindly waiting/hoping for someone else to throw you a life vest, rather than swimming for shore… All this does is push the worries out, or as was the phrase of 2012… 2011… 2010… kicking the can FURTHER down the road. We are less than impressed.
- EURCHF did not move on the week, finishing where it started at about 1.2230. USDCHF weakened on the week, gliding from 0.8920 to as low as 0.8840. The USD has bounced a little from yesterday's low but we are still at 0.8910. The Christmas USD rally (against the European currencies at least) has not arrived and the USD bulls are licking their wounds after a year of pain.
- USDJPY moved steadily higher again this week, closing each day at or above 102.00 (we are moving higher on a closing basis each week still!) and in fact closing above 103.00 for two of the trading days so far. Starting the week at 102.54, finally soaring to as high as 103.92 this morning. What year Mr. Shinzo Abe has had... We applaud him and maybe (just maybe) he would get our Central Banker of the year award… if he was actually a Central Banker and not a Politician!!
- The Aussie carried on down the soap covered slide to drop to 0.8905 by this morning, having been as high as 0.9167 on Tuesday. There are very few data points that seem to inflict so much pain on any one currency, but at the moment the Aussie is really getting crushed. This is not a pretty sight and it certainly would appear that Mr. Druckenmiller's prediction of the trade of the year is coming through to fruition.
- Cable is almost unchanged on the week so far at about 1.6280, although with some serious moves higher in the pair at the start of the week, seeing 1.6460 on Tuesday. When there is little data out and the USD is weakening, the Pound only really has one way to go. As the tide comes in all boats float, when the tide goes out you see who has been swimming naked…

Fixed Income

- The US 10Yr yield is moving slowly higher and higher, but again is still within out 2.5% to 3.0% band. The yield has moved from 2.85% to 2.88% by this morning, having briefly dipped back to as low as 2.79% on Wednesday. Coming into the holiday season we see very little movement and that the positioning for next year has probably already taken place. We believe until there is a policy shift, the yields will remain in the range.
- The German fear factor is slowly ebbing away and with that fear so too have the yields stopped moving lower. We started the week at 1.84% and we are trading at roughly the same levels now, although the yields did trade to a low of 1.81% on Wednesday.
- Spanish yields tumbled this week, seeing the 10Yr drop from 4.17% to as low as 3.99% on Wednesday as equity markets made new highs and the world was a rosy place. We are now trading at 4.09%.
- Italy's 10Yr moved in a similar fashion to that of the Spanish debt and slid from 4.18% to as low as 4.04%. With little news coming from the political news wires we shall await the follow up on Mr Berlusconi, even after Mr Letta secured the confidence votes and remains in power.

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Equities

- Developed equities lost 1.49% for the week – as of yesterday's close – as measured by the MSCI World index. Equities dropped following weaker than expected macro data from China and Europe, as well as increased concerns that the Fed will announce a cut in stimulus in next week's FOMC meeting.
- The EuroStoxx fell 1.7% for the week. European shares started the week in positive territory following better than expected Chinese export data, overshadowing an unexpected drop in German industrial production. Stocks reversed their gains soon after due to weak data from China and Europe, and on investor speculation that the case for tapering has strengthened.
- The S&P 500 lost 1.64% for the week, as of yesterday's close. US equities fell as a congressional budget accord increased speculation that the Fed will announce a reduction of stimulus in next week's FOMC meeting. In terms of data, better than expected retail sales outweighed a weekly increase in Jobless claims, sending stocks even lower.
- The Nikkei rose 0.67% for the week. Japanese stocks rallied as much as 2.3% on Monday's session as the Yen weakened against the Dollar following better than expected US job figures. Stocks reversed most of their gains on US tapering possibility as well as weaker than expected Chinese data.
- In terms of sectors, Healthcare and Materials stocks were the worst performers (-2.30% and -1.79% respectively), while Telecoms and Industrials suffered less (-0.65% and -1.05% respectively).

Emerging Markets

- Emerging Market equities lost 1.07% for the week – as of yesterday's close – as measured by the MSCI EM index. EM Latin American shares lost as much as 1.37%, while EM Asian and EM European shares lost 0.79% and 0.37% respectively.
- The Shanghai Composite lost 1.89% for the week. Chinese stocks fell following worse than expected data, overshadowing increased speculation that the local government will increase state-owned enterprise reforms to increase profitability. All eyes are set on today's government announcement on economic growth targets for 2014.
- The Bovespa lost 1.17% for the week, as of yesterday's close. Brazilian shares fell as news of China's reduced industrial growth and concerns that US stimulus is ending, overshadowed slower than expected inflation in Brazil.

Commodities

- Commodities dropped by 0.91% for the week, as measured by the S&P GSCI Total Return index. Energy was the worst performing sector (-1.25%) followed by Agriculture (-0.53%) and Precious Metals (-0.34%) while Industrial Metals rose by 1.42%.

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- Gold lost 0.55% this week, and is currently trading around $1'228 per troy ounce, as upbeat US retail sales data boosted the dollar and stoked expectations that the Federal Reserve could reduce its bond-buying stimulus soon. Taper fears have helped knock gold 25% lower this year, brightening US economic picture and a stronger dollar.
- Meanwhile, crude oil dropped by 0.65% and is currently trading around $97 a barrel. Futures declined on global cues, as dealers worried about a global oversupply in crude, while speculation the US Federal Reserve will soon scale back its stimulus program also weighed on sentiment.
