

Bedrock Friday October 2nd Newsletter

We are in day 2 of Q4, just out of Q3 which was rather horrific for equities (S&P 500 off 7%, MSCI World off 9%) and commodities (CRB index down 15%), surprisingly positive for high quality bonds (Bloomberg Dollar investment grade index up 0.60%), but the lower quality ones suffered (Bloomberg Dollar high-yield index off 5% for Q3). Even the wizards of the Hedge Fund world didn't get it right (again!) being taxed by 4.25% for the quarter (HFRX Global Hedge Fund Index).

We can only use the polite expletive, OUCH... As we all grimace from the discomfort of financial pains, the continuous influx of refugees into Europe ought to give us a perspective on what is true misery. The news of this has been displaced in recent days by scenes of Russian jets dropping bombs in Syria. Clearly the West and Russia agree on the severity of the ISIS threat and the need to stop the problem at its source. Unfortunately, the opposed sides of the compass do not agree on how to go about resolving the problem. In the interim, both sides are dropping bombs on anything that looks like a target.

IMF Managing Director Christine Lagarde said that her organization sees troubling signs in the world's finances, and that it is unclear if the current situation is cyclical or if it represents a fundamental downturn. "The simple answer is that there is no simple answer. Certainly, we are at a difficult and complex juncture," Lagarde said, explaining she is worried about recent global affairs — and international economics are similarly distressing. "The prospect of rising interest rates in the United States and China's slowdown are contributing to uncertainty and higher market volatility," she said. "There has been a sharp deceleration in the growth of global trade. And the rapid drop in commodity prices is posing problems for resource-based economies." Lagarde said that emerging economies will likely see their fifth consecutive year of declining rates of growth. Supporting her views we saw data on net capital flows for global emerging markets which will be negative in 2015, the first time that has happened since 1988, which was taken from the latest report from the Institute of International Finance (IIF). Net outflows for the year are projected at \$541 billion, driven by a sustained slowdown in EM growth and uncertainty about China. In other words, investors will pull out more money from emerging markets than they will pump in.

Depressing times. The Fed chose to refrain from raising interest rates (for now), in so doing suggesting to analysts and investors that things are not as rosy as they had believed. Incerititude reigns, erroneously, as Janet told us that rates will rise soon, albeit only gently. We offer Janet the advice of E.B. White "Be obscure clearly..."

Then data of negative inflation crept back into Japan and Europe. So much noise... We went to seek solace in statistics and averages and found some sunshine for the Fall (no pun intended!) - The stock markets' performance in the fourth quarter is statistically independent of what transpired up until the end of the third quarter. How much the stock market goes up or down in the fourth quarter — indeed, even whether it goes up or down — has nothing to do with how it performed in September, the third quarter, or the year to date. The fourth quarter has a lot going for it. Looking at all years since 1896, we find that the average Dow performance in the fourth quarter is a gain of 2.7% versus a 1.6% average for the other three quarters. Before rushing-out to buy, remember that History doesn't repeat itself, but sometimes it rhymes as per Mark Twain.

With the US ten year Treasury note (our preferred benchmark for valuation purposes) rallying to yield 2.03%, we compare the implied "P/E" of the bond at about 50X to the decimated Biotech Index trading at 14X or Apple, the world's most valuable company, trading at a P/E of 12X; we are comforted in our positive outlook for equities being relatively cheap!

With stocks lower on the year, the market on Thursday entered the final three months of 2015 with the prospect of a complete turnaround that could extend the bull market into a seventh year, so says Citi strategist Tobias Levkovich. "We're talking about kind of double-digit returns — mid teens to high teens % — type of returns," At the end of 2015, he expects 2,200 on the S&P 500, which would represent a 14.6% rise from the 1,920 level, where the index closed Wednesday. A gain of that magnitude would completely flip the script on 2015, and return 6.9%. We like this view, as it is close to our own prediction for the S&P for year-end, as stated last Christmas! The fourth quarter has traditionally been positive for the market, despite a historically scary October. But there's hope, because in recent years, the major stock measures have rallied in four of the past five Octobers. UBS strategist Julian Emanuel said the investment bank had cut its 2015 year-end S&P 500 price target to 2,125 from 2,225. Still a nice upside from here! Support for this optimism can be found in U.S. home prices which continued to rise in July. S&P/Case-Shiller's 20-City Index rose 5% in July. Well, next week as Q3 earnings' season unfolds, we hope to find further support for our optimistic outlook for Q4. Chinese equities seem to have stabilized, Russia stabilized its Rouble at 65 or so, Greece has defined its future and we keep our sights on the remaining trouble spot of Brazil. To whom we suggest they follow Churchill's words, "If you are going through hell, keep going..." Unless we all get "Trumped"!!

Market Weekly Highlights:

- The US Dollar is almost unchanged on the week, with the Dollar Index (DXY) currently at 96.30, just slightly off the highest levels of the week. The US\$ is now trading at about \$1.1160 against the EUR and at 0.9780 against the Swiss Franc. The Pound has dropped against the USD at 1.5140. We maintain our belief in the fundamental strength of the US\$ in the longer term. Again, this view is driven by the outlook for interest rates to hold or rise in the US and hold or decline elsewhere. The Japanese Yen regained a little footing versus the USD this week and is trading at 120. Gold gave back all of its strength from last week, dropping from \$1,145 to hit \$1,105 this morning. WTI is trading at \$45.35/Bbl. having remained relatively stable apart from a flurry yesterday to hit \$47.10, with Brent at \$48.10/Bbl. having also surged to nearly hit \$50.00. The Russian Ruble has traded around 66.00 throughout the week versus the USD. The Brazilian Real remains weak, closing last night at 4.00; we believe that we will see continued weakness in the Real.
- The US 10Yr Treasury yield has moved lower throughout the week and is trading at 2.05%. We are now lower than where we started the year! The German 10Yr Bund has dropped during the week in line with the US Treasuries and is yielding 0.56%. The Spanish 10Yr yield had been trading around 2% levels this week only to drop from 2.05% to 1.85%. Italian 10Yr yield has followed the same path as the Spanish yields to slip to 1.70% this morning. In the UK, the yield on the Gilts has remained well below 2.0%, sliding from 1.84% to 1.76%. The Swiss 10Yr yields have moved lower and now they yield -0.16%.
- Equity Markets were generally flat on the week as we await the NFP data this afternoon. The S&P500 closed last night at -0.39% for the week, but with the futures pointing to a positive open of +0.32%. The Dow Jones closed last night at -0.26% for the week and with the futures pointing to an open of +0.35%. The DAX is currently trading at -0.39% for the week (VW still weighing heavily on the performance for Germany), the CAC40 at +0.63%, SMI +1.22%, the UK FTSE trading at +0.88% and the EuroStoxx 50 at +0.25%. The Shanghai composite only traded for three days this week as Golden Week celebrations continue, but up to Wednesday the market was -1.28%. Whilst the Hang Seng Index was down -1.18% for the same three day period. In Japan the Nikkei was down by 0.87% for the week, unaffected by the three day week in China.

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Highlighted items are interesting data points for the week

MARKET INDICES PERFORMANCE

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INDEX NAME	CCY	Last Price	PRICE CHANGE IN % (unless indicated)									P/E
			1D	5D	MTD	1M	3M	6M	YTD	1Y	3Y	
EQUITY MARKET INDICES - BY REGION												
S&P 500 INDEX	USD	1923.82	0.20	-0.44	0.20	-1.28	-7.37	-6.93	-6.56	-1.15	33.07	15.92
DOW JONES INDUS. AVG	USD	16272.01	-0.07	0.44	-0.08	-0.49	-8.22	-8.40	-8.70	-3.15	20.69	14.80
NASDAQ COMPOSITE INDEX	USD	4627.084	0.17	-2.27	0.15	-2.59	-7.63	-5.32	-2.30	4.44	48.30	16.96
RUSSELL 2000 INDEX	USD	1097.552	-0.27	-3.52	-0.28	-4.23	-12.07	-12.59	-8.89	0.11	30.58	16.53
EURO STOXX 50	EUR	3069.05	-1.02	-0.23	0.17	-2.90	-10.31	-16.40	-1.28	-0.01	24.56	13.46
EURO STOXX 600	EUR	346.23	-0.43	0.25	0.68	-1.05	-9.16	-11.98	2.22	5.45	28.91	15.06
CAC 40 INDEX	EUR	4426.54	-0.65	0.06	0.63	-1.57	-7.29	-11.65	4.93	5.67	31.31	14.46
DAX INDEX	EUR	9509.25	-1.57	-0.70	-0.41	-4.25	-13.32	-19.61	-1.89	4.62	31.68	11.81
FTSE 100 INDEX	GBP	6072.47	0.21	0.43	1.22	0.86	-7.47	-10.21	-6.56	-4.82	5.61	15.19
SWISS MARKET INDEX	CHF	8510.56	-0.03	1.03	0.95	-0.38	-4.10	-5.88	-4.34	-0.70	29.94	16.76
NIKKEI 225	JPY	17722.42	1.92	-0.87	1.94	-2.05	-13.63	-8.22	1.57	13.17	101.74	16.71
HANG SENG INDEX	HKD	20846.3	1.41	0.64	2.85	1.20	-18.32	-14.52	-9.17	-6.51	2.88	10.71
SHANGHAI SE COMPOSITE	CNY	3052.781	0.48	-2.03	0.00	-3.80	-24.69	-19.88	-5.22	29.14	46.33	12.53
S&P BSE SENSEX INDEX	INR	26220.95	0.25	1.54	0.25	3.01	-6.17	-7.22	-4.65	-1.31	39.30	16.54
RUSSIAN RTS INDEX \$	USD	781.65	-1.02	-1.63	-1.78	-1.73	-16.77	-16.91	-1.90	-29.17	-48.55	5.33
BRAZIL IBOVESPA INDEX	BRL	45313.27	0.56	0.05	0.56	-2.48	-14.67	-14.70	-9.39	-15.33	-23.49	10.29
MSCI WORLD	USD	1587.98	0.39	-0.42	0.38	-1.71	-9.12	-9.22	-7.12	-4.80	20.35	15.39
MSCI WORLD HEDGED	USD	678.986	0.27	0.30	0.27	-0.42	-8.29	-7.98	-3.74	0.41	39.09	-
MSCI WORLD LOCAL	-	1210.4	0.26	0.19	0.26	-0.62	-8.69	-8.91	-5.12	-1.32	31.55	-
MSCI AC WORLD	USD	383.23	0.42	-0.28	0.41	-1.54	-10.04	-10.35	-8.12	-6.44	14.91	14.85
MSCI EM	USD	797.61	0.70	1.07	0.70	0.12	-17.90	-19.67	-16.60	-19.64	-20.73	11.21
MSCI AC ASIA x JAPAN	USD	486.16	0.61	0.81	0.61	1.09	-17.32	-18.56	-13.76	-13.20	-6.40	11.49
MSCI EM LATIN AMERICA	USD	1909.53	0.80	3.85	0.79	-4.35	-24.19	-25.05	-29.99	-38.54	-48.46	13.55
MSCI EM Eur, ME & Africa	USD	230.98	0.42	0.19	0.42	-1.74	-16.26	-18.02	-14.70	-22.52	-32.26	10.16
EQUITY MARKET INDICES - BY SECTOR												
MSCI ENERGY	USD	182.12	0.66	-0.47	0.66	-3.92	-17.92	-20.38	-23.42	-32.79	-26.59	17.89
MSCI MATERIALS	USD	178.72	0.70	-0.60	0.70	-5.59	-19.77	-21.04	-19.87	-21.70	-21.45	15.06
MSCI INDUSTRIALS	USD	180.99	0.39	0.05	0.39	-2.31	-9.56	-10.99	-9.20	-6.02	21.99	15.36
MSCI CONS DISCRETIONARY	USD	185.89	0.81	-0.17	0.81	-0.15	-6.70	-5.92	-0.17	7.67	48.57	16.47
MSCI CONS STAPLES	USD	196.81	-0.14	-0.28	-0.14	1.37	-2.56	-4.36	-1.56	3.06	21.71	19.80
MSCI HEALTH CARE	USD	198.22	0.64	-0.94	0.64	-4.55	-9.75	-7.61	-0.84	3.51	53.35	16.96
MSCI FINANCIALS	USD	94.05	0.59	-0.11	0.59	-1.23	-10.19	-9.62	-8.48	-6.12	22.70	12.41
MSCI INFO TECH	USD	134.91	0.09	-0.68	0.07	-0.49	-5.95	-5.62	-4.51	1.18	34.17	15.73
MSCI TELECOMS	USD	63.9	-0.66	-2.40	-0.67	-5.14	-10.13	-8.97	-6.52	-7.35	5.90	14.46
MSCI UTILITY	USD	110.11	-0.69	0.19	-0.72	2.02	-2.61	-5.79	-10.52	-5.91	6.71	14.63
MSCI WORLD REAL ESTATE	USD	183.62	0.74	0.45	0.71	2.76	-3.28	-9.70	-5.57	1.00	9.93	23.17
HEDGE FUND INDICES												
HFRX GLOBAL HEDGE FUND	USD	1181.26	0.48	-1.03	-2.07	-2.14	-4.27	-5.12	-3.05	-4.74	3.69	-
HFRX EQUAL WEIGHTED	USD	1180.04	0.38	-0.71	-1.19	-1.19	-2.41	-2.84	-0.93	-2.70	5.32	-
HFRX GLOBAL EUR	EUR	1079.48	-0.34	-1.68	-2.61	-2.67	-4.87	-5.61	-4.01	-5.96	1.78	-

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01/10/2015

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			1D	5D	MTD	1M	3M	6M	YTD	1Y	3Y	
FIXED INCOME INDICES - YIELD ON US GOVERNMENT BONDS (Change in bps)												
US 3 MONTH	USD	-0.0152	0.01	0.01	0.01	-0.03	-0.02	-0.03	-0.05	-0.03	-	-
US 2 YEAR	USD	0.6567	0.01	-0.04	0.03	-0.05	0.03	0.12	-0.01	0.13	-	-
US 10 YEAR	USD	2.0403	0.00	-0.12	0.00	-0.14	-0.34	0.13	-0.13	-0.38	-	-
FIXED INCOME INDICES - BY TYPE OF ISSUER												
GLOBAL AGG TR HEDGED	USD	480.51	0.12	0.11	0.12	0.70	1.70	-0.98	1.04	2.95	9.51	1.66
US GOVERNMENT TR	USD	2115.62	0.07	0.58	0.07	0.94	2.03	0.13	1.86	3.40	3.93	1.66
US CORPORATE TR	USD	2585.18	0.01	0.20	0.01	0.77	1.03	-2.58	-0.09	1.16	6.52	3.43
US HIGH YIELD TR	USD	1577.98	-0.21	-1.43	-0.21	-2.77	-5.29	-5.13	-2.65	-3.82	10.49	8.09
EU GOVERNMENT TR	EUR	242.1538	0.23	0.61	0.23	3.07	-2.47	1.28	3.75	19.44	0.74	-
EU CORPORATE TR	USD	242.09	0.20	-0.30	0.20	-0.35	0.04	-2.81	-1.42	0.02	13.03	1.57
EU HIGH YIELD TR	EUR	268.32	0.26	-0.84	0.27	-1.77	-1.71	-3.19	-0.17	0.59	23.74	5.24
BARCLAYS GLOBAL CONVERT.	USD	209.52	-0.10	-1.26	-0.10	-2.76	-6.71	-6.33	-2.39	-0.85	20.56	-
GLOBAL EM TR (HEDGED)	USD	321.8899	0.32	-0.20	0.32	-0.95	-1.97	-2.22	0.48	-1.15	5.25	5.60
S&P/LSTA U.S. LEV LOAN	USD	91.07365	-0.07	-0.99	-0.07	-1.68	-4.16	-5.36	-4.48	-6.03	-5.22	5.94
COMMODITY INDICES - BY TYPE OF ISSUER												
GSCI INDEX TOTAL RETURN	USD	2584.551	-0.73	-0.45	-0.73	-2.75	-18.40	-15.05	-20.05	-42.05	-48.97	-
GSCI ENERGY TR	USD	485.716	-0.96	-0.99	-0.96	-4.45	-22.97	-18.23	-22.90	-52.72	-55.61	-
GSCI INDUSTRIAL METALS TR	USD	1009.412	-1.21	-0.07	-1.21	-1.70	-12.03	-16.18	-20.21	-24.33	-38.35	-
GSCI PRECIOUS METALS TR	USD	1365.419	-0.13	-3.54	-0.13	-2.13	-5.17	-8.93	-6.52	-9.76	-41.59	-
GSCI AGRICULTURE TR	USD	468.7901	0.37	2.96	0.37	4.38	-11.12	-5.99	-13.42	-5.97	-42.70	-
GENERIC 1ST 'CL' FUTURE	USD	44.74	2.03	-0.11	1.24	-2.42	-21.48	-14.08	-22.18	-52.92	-51.96	-
GOLD SPOT \$/OZ	USD	1113.56	-0.44	-3.29	-0.57	-2.24	-4.93	-7.81	-6.43	-8.72	-37.53	-
CURRENCIES												
DOLLAR INDEX SPOT	USD	96.18501	0.06	-0.02	-0.11	0.44	0.14	-1.22	6.62	12.44	20.69	-
Euro Spot	EUR	1.1195	-0.26	-0.26	-0.10	-0.54	0.74	2.63	-7.70	-11.86	-13.58	-
Japanese Yen Spot	JPY	119.93	-0.17	0.38	-0.21	0.17	2.45	-0.34	-0.29	-9.75	-34.94	-
British Pound Spot	GBP	1.5131	0.07	-0.25	0.09	-1.03	-2.99	2.11	-2.79	-6.21	-6.15	-
Brazilian Real Spot	BRL	4.0095	-1.55	-1.47	-1.55	-7.75	-21.46	-21.07	-33.72	-38.12	-49.45	-
China Renminbi Spot	CNY	6.3571	-0.02	0.40	-0.02	0.11	-2.45	-2.50	-2.38	-3.42	#N/A	N/A
Singapore Dollar Spot	SGD	1.4307	-0.20	-0.57	-0.79	-1.26	-5.98	-5.29	-7.54	-11.27	-14.16	-
Norwegian Krone Spot	NOK	8.427	-0.25	0.89	0.80	-2.41	-5.74	-5.42	-11.79	-23.71	-32.45	-
VOLATILITY / LIQUIDITY INDICES												
CBOE SPX VOLATILITY INDX	USD	22.55	-7.96	-3.92	-7.96	-13.57	34.31	53.72	17.45	39.54	43.54	-
USD SWAP SPREAD SEMI 2YR	USD	12.85	-9.11	15.30	0.09	-12.18	-55.92	-54.87	-49.08	-56.64	-19.45	-
TED SPREAD	USD	34.94	1.19	7.05	1.19	17.09	30.23	36.70	58.75	57.03	27.43	-

All data is compiled from Bloomberg

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