

# Bedrock Friday October 16<sup>th</sup> Newsletter

Another week has flowed and passed, offering no events of significance to inspire our thoughts. We are shaking-off the horrors of the past quarter, tracking the now unfolding Q3 earnings season. So far, of the 34 S&P companies which have given us their earnings, 71% have beaten expectations on average by 4.5% and the rest missed on average by 70% - effectively a 10% miss when excluding Monsanto! This is supportive for the markets which have indeed shown their appreciation - The S&P has risen by 5.4% this month, now showing a loss of 1.7% YTD. Not too shabby, and the index itself is at 2'023. From here, the index must rise 10% to meet our year-end target of 2'229 set at year-end 2014... But then again, is it earnings? Top line sales? Or is it the Fed that drives markets? Clearly, the former define the long-run, but we know that "long-run" is a sequence of short-term events, and these are clearly driven by the central banks. This said we have seen a change in market sentiment and expectations as to the Fed's actions; the tone has changed from quasi certitude of an impending rise in rates to a view that it will be later and smaller. The bottom line, according to Oppenheimer's head of portfolio strategy Andrew Burkly, is that stocks needn't worry about a looming Fed shock.

An unusually public rift between the Fed chair and two governors is adding to an already confused policy message that has been hurting the central bank's credibility with markets. The split in views inside the Fed became very apparent this week when two Fed governors Daniel Tarullo and Lael Brainard each spoke against raising rates this year because of concerns about the economy. Yellen, Vice Chairman Stanley Fischer and Dudley have said they would like to raise rates this year, depending on the economic data. The data, just in the last week has been mixed, with softer retail sales, weaker than expected producer prices, flat business inventories, but low weekly jobless claims; in fact at the lowest level in four decades! Core CPI gained 0.2% in September, as expected, while PPI was weaker. Overall, U.S. economic activity continued to expand modestly from mid-August through early October. It's not stellar, but there is expansion. Deflation talk these days is mostly centred on the Eurozone and parts of the emerging markets, but the U.S. is dancing on the brink itself. In fact, if not for a comparatively high inflation rate in the Western quadrant, the U.S. itself actually would have had a negative CPI rating in August, driving its economy into the same deflationary malaise found in other slow-growth regions.

Seven years after the West went 'all-in' on QE and ZIRP, the U.S./Japan/Europe could shift toward fiscal stimulus via government spending on infrastructure or more aggressive income redistribution.

Asset returns have jumped while global economic growth has been anaemic in what we could call the most deflationary expansion of all time. GDP gains in the U.S. have averaged barely 2% during the post-Great Recession recovery, bringing some economists to believe a global recession could hit in 2016. Easy-money measures have helped boost Wall Street, with the S&P 500 up about 200% since the March 2009 lows as companies have spent some \$2 trillion on stock repurchases. Dividend payments also have soared during the period, with the second quarter's \$105 billion increase being the biggest in 10 years. Income growth disparities have jumped in the past 10 years. The highest-paid 10% of workers saw wages increase 4.6% annually from 2003-2013, while the lowest 10% saw their wages decline 2.2% - (a trend synonymous with the 1920s, another period infamous for 'inequality'). Consequently, the top 0.1% of the U.S. population now controls 22% of the wealth, while the bottom 90% of U.S. households control just 23%. Inequality may become the driver for a policy shift towards infrastructure investing - led by populist politicians See Trump (R) and Sanders (D)?

A yellow flag for Investors who fear a "black swan" catastrophic event in the financial markets can be verified in the CBOE Skew Index. Its goal is to determine the S&P's tail risk or the "risk of outlier returns, two or more standard deviations below the mean". Put simply, traders are buying options that pay off only if the stock market drops massively. At its Monday closing level of 148.92, the Skew Index is higher now than levels hit in 2006 before the housing bubble popped and 1998 amid the Long-Term Capital Management implosion. But then, to be sure, black swan events by definition are supposed to be unpredictable. And a history of the Skew Index shows that its track record is mixed. That being said perhaps we should take a little look at the energy sector again. Geopolitical developments have market participants rebuilding an oil-price risk premium attached to potential production outages in the Middle East. Fighting in Syria (and Russia's intervention there), plus attacks by ISIS on production facilities in northern Iraq - all of this has raised the risk of outages occurring. UBS's Wealth Management analysts have raised their expectations for Brent oil going to \$72/Bbl within 12 months... Maybe the White Swan is just covered in oil?!

In case you are feeling disillusioned with the markets, the market savvy wizards of the Hedge Fund universe had the fourth losing month in a row in September, something that hasn't happened since 2008!

More seriously, we ask what the world is coming to now that Playboy has decided to stop nudity on its pages ☹

## Market Weekly Highlights:

- The US Dollar has lost a little ground this week against the majors, with the Dollar Index (DXY) currently at 94.50, off the lows of the week that we saw yesterday. The US\$ is now trading at about \$1.1370 against the EUR and at 0.9530 against the Swiss Franc. The Pound has strengthened against the USD and is at 1.5470. 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 has marginally strengthened over the last three days and is trading at 119.20. After the initial weakness in the USD, Gold rallied to as high as \$1,191 but has slipped back to \$1,175. WTI slid throughout the week, finding a footing at \$45/Bbl. and is now at \$47/Bbl. With Brent trading at \$50.30/Bbl. The Russian Ruble is almost unchanged at 61.30, with the Brazilian Real steady as well at 3.80.
- The US 10Yr Treasury yield has moved lower throughout the week and is trading at 2.01%. We are now marginally lower than where we started the year after the rate rise has been postponed and the market has positioned for a rise later than previously expected. The German 10Yr Bund has also moved significantly lower during the week slipping from 0.62% to 0.54%. The Spanish 10Yr yield has followed the move and is trading around 1.79% having started the week as high as 1.85%. Italian 10Yr yield moved with a similar pattern to the Spanish yield and is trading at 1.62% this morning. In the UK, the yield on the Gilts has drifted lower from 1.86% to 1.78% as we write. The Swiss 10Yr yield moved from -0.17% to -0.21%.
- Equity Markets were generally all positive on the week as the earning seasons kicked off and the continuation of accommodative Fed monetary policy. The S&P500 closed last night at +0.45% for the week. The Dow Jones night moved back well above 17'000 points at +0.34% for the week and with the futures pointing to a flat open. The DAX is currently trading at +0.5% for the week; the CAC40 remains positive at +0.2%, SMI +0.7%, the UK FTSE trading at -0.3% and the EuroStoxx 50 at +0.5%. The Shanghai composite closed the week on another positive note of +6.5% whilst the Hang Seng Index was up +2.7% for the same period. In Japan the Nikkei was up by 0.83% for the week.

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Highlighted items are interesting data points for the week

## MARKET INDICES PERFORMANCE

15/10/2015

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	2023.86	1.49	0.52	5.41	1.43	-4.73	-3.85	-1.70	8.65	39.10	16.77
DOW JONES INDUS. AVG	USD	17141.75	1.28	0.53	5.26	2.40	-5.40	-5.32	-3.82	6.36	26.49	15.53
NASDAQ COMPOSITE INDEX	USD	4870.1	1.82	1.23	5.41	-0.39	-5.68	-2.75	2.83	15.48	57.04	17.91
RUSSELL 2000 INDEX	USD	1162.771	2.27	-0.04	5.64	-1.06	-8.65	-8.65	-3.48	7.08	39.18	17.45
EURO STOXX 50	EUR	3238.81	1.48	0.21	5.04	0.16	-11.41	-13.18	3.52	13.30	27.83	14.40
EURO STOXX 600	EUR	360.99	1.46	0.03	4.36	0.30	-10.48	-11.68	5.96	17.07	32.28	15.78
CAC 40 INDEX	EUR	4675.29	1.44	-0.11	5.40	1.08	-8.31	-10.11	9.91	19.84	34.14	15.23
DAX INDEX	EUR	10064.8	1.50	0.29	4.82	-0.99	-13.57	-15.61	3.27	17.98	37.28	12.94
FTSE 100 INDEX	GBP	6338.67	1.10	-0.78	5.03	2.20	-6.33	-9.83	-3.04	2.75	8.45	15.96
SWISS MARKET INDEX	CHF	8653.35	0.93	-0.24	1.72	-2.38	-8.45	-7.86	-3.60	7.47	27.84	17.18
NIKKEI 225	JPY	18096.9	1.15	0.83	5.20	0.66	-11.21	-8.02	4.82	24.11	110.22	17.35
HANG SENG INDEX	HKD	22888.17	2.00	2.60	10.54	4.90	-8.42	-16.93	-2.38	0.62	8.66	11.52
SHANGHAI SE COMPOSITE	CNY	3338.073	2.32	6.54	11.09	7.58	-11.29	-19.15	4.84	43.91	61.58	13.85
S&P BSE SENSEX INDEX	INR	27010.14	0.86	-0.51	3.01	3.77	-5.29	-6.01	-2.03	3.63	45.02	17.31
RUSSIAN RTS INDEX \$	USD	876.23	1.50	0.97	13.28	6.83	-2.74	-15.73	13.14	-14.41	-39.89	5.97
BRAZIL IBOVESPA INDEX	BRL	47161.15	-	-3.58	4.66	-2.87	-11.13	-13.74	-5.69	-13.14	-21.06	10.49
MSCI WORLD	USD	1675.77	1.38	0.12	5.93	1.33	-5.96	-6.20	-1.98	5.22	26.05	16.19
MSCI WORLD HEDGED	USD	711.779	1.33	0.31	5.11	2.19	-5.48	-6.20	0.91	11.12	46.20	-
MSCI WORLD LOCAL	-	1267.564	1.32	0.27	4.99	1.96	-5.98	-7.18	-0.64	9.11	38.18	-
MSCI AC WORLD	USD	405.49	1.42	0.17	6.25	1.69	-6.18	-7.48	-2.79	3.41	20.84	15.59
MSCI EM	USD	864.73	1.81	0.63	9.18	5.11	-8.17	-17.82	-9.58	-10.91	-13.82	11.67
MSCI AC ASIA x JAPAN	USD	528.25	2.01	1.83	9.32	6.06	-6.77	-16.82	-6.29	-3.87	2.24	12.33
MSCI EM LATIN AMERICA	USD	2034.75	0.88	-2.03	7.40	-0.63	-18.56	-23.49	-25.40	-34.10	-45.82	13.91
MSCI EM Eur, ME & Africa	USD	253.32	1.54	0.15	10.13	4.57	-7.29	-14.40	-6.44	-12.44	-24.78	9.75
EQUITY MARKET INDICES - BY SECTOR												
MSCI ENERGY	USD	206.12	1.28	-0.28	13.92	7.36	-5.34	-15.79	-13.33	-17.58	-17.07	19.94
MSCI MATERIALS	USD	197.04	0.77	-0.91	11.02	2.06	-10.73	-14.85	-11.66	-10.23	-13.67	16.93
MSCI INDUSTRIALS	USD	192.02	0.95	-1.18	6.51	1.08	-4.97	-7.19	-3.66	4.04	28.30	16.23
MSCI CONS DISCRETIONARY	USD	194.82	1.26	-0.07	5.66	1.25	-3.86	-2.47	4.62	17.35	53.92	17.27
MSCI CONS STAPLES	USD	207.27	1.20	0.59	5.17	4.04	-1.46	-1.03	3.68	11.34	27.54	20.75
MSCI HEALTH CARE	USD	203.41	2.03	0.96	3.28	-4.16	-10.78	-7.55	1.76	12.27	55.14	17.34
MSCI FINANCIALS	USD	98	1.63	-0.13	4.81	0.66	-8.44	-7.35	-4.63	1.98	24.75	12.87
MSCI INFO TECH	USD	143.01	1.28	0.87	6.07	2.44	-2.47	-1.78	1.22	13.52	43.35	16.76
MSCI TELECOMS	USD	66.46	1.45	-0.15	3.31	-0.78	-8.24	-6.34	-2.78	1.17	13.59	14.86
MSCI UTILITY	USD	116.24	1.18	1.46	4.81	5.99	-0.45	-1.28	-5.54	0.93	11.77	15.36
MSCI WORLD REAL ESTATE	USD	191.03	1.25	0.33	4.78	4.93	-1.72	-6.22	-1.76	4.30	12.99	23.77
HEDGE FUND INDICES												
HFRX GLOBAL HEDGE FUND	USD	1188.39	-0.05	-0.09	0.60	-1.04	-4.10	-5.41	-2.46	-1.45	4.31	-
HFRX EQUAL WEIGHTED	USD	1184.96	-0.04	-0.02	0.42	-0.62	-2.37	-2.98	-0.52	-0.20	5.82	-
HFRX GLOBAL EUR	EUR	1090.65	-0.05	-0.10	0.56	-1.11	-4.28	-5.80	-3.02	-2.12	2.85	-

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15/10/2015

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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	-0.0051	0.00	-0.01	0.02	-0.06	-0.02	-0.02	-0.04	-0.03	-	-
US 2 YEAR	USD	0.5927	0.00	-0.04	-0.04	-0.22	-0.06	0.11	-0.07	0.25	-	-
US 10 YEAR	USD	2.0122	-0.01	-0.08	-0.02	-0.28	-0.34	0.12	-0.16	-0.14	-	-
FIXED INCOME INDICES - BY TYPE OF ISSUER												
GLOBAL AGG TR HEDGED	USD	481.68	-0.12	0.30	0.37	1.03	1.54	-0.88	1.29	2.23	9.52	1.63
US GOVERNMENT TR	USD	2119.49	-0.23	0.43	0.25	1.58	1.94	0.15	2.05	2.18	4.54	1.63
US CORPORATE TR	USD	2601.5	-0.32	0.55	0.65	1.66	1.52	-2.29	0.54	0.51	6.54	3.35
US HIGH YIELD TR	USD	1611.8	-0.02	0.34	1.93	-0.96	-3.22	-4.14	-0.57	-0.65	11.92	7.68
EU GOVERNMENT TR	EUR	242.4141	-0.09	0.28	0.34	1.44	1.92	-2.62	1.39	4.14	19.10	0.72
EU CORPORATE TR	USD	243.57	-0.06	0.24	0.82	0.33	0.27	-2.62	-0.82	0.33	12.86	1.48
EU HIGH YIELD TR	EUR	271.88	0.06	0.29	1.60	-0.31	-1.02	-2.44	1.16	2.82	23.87	4.92
BARCLAYS GLOBAL CONVERT.	USD	214.91	0.72	0.38	2.47	-1.27	-4.41	-6.12	0.12	4.83	23.21	-
GLOBAL EM TR (HEDGED)	USD	328.0106	0.19	0.66	2.22	1.11	-0.37	-1.63	2.39	0.46	5.87	5.30
S&P/LSTA U.S. LEV LOAN	USD	90.72798	-0.03	0.08	-0.45	-2.07	-4.52	-6.06	-4.84	-5.19	-5.76	5.95
COMMODITY INDICES - BY TYPE OF ISSUER												
GSCI INDEX TOTAL RETURN	USD	2632.109	-0.44	-3.57	1.09	0.79	-11.88	-17.39	-18.58	-36.65	-47.79	-
GSCI ENERGY TR	USD	491.923	-0.45	-6.36	0.31	0.60	-15.00	-23.63	-21.91	-46.66	-55.45	-
GSCI INDUSTRIAL METALS TR	USD	1044.695	-0.22	3.37	2.24	-0.30	-7.03	-13.93	-17.42	-21.18	-32.46	-
GSCI PRECIOUS METALS TR	USD	1462.749	0.61	3.64	6.99	8.24	3.71	-1.43	0.14	-5.48	-35.42	-
GSCI AGRICULTURE TR	USD	470.1813	-0.71	-0.61	0.67	1.62	-9.88	-3.48	-13.17	-10.47	-40.32	-
GENERIC 1ST 'CL' FUTURE	USD	46.38	1.60	-5.06	4.50	-1.17	-9.59	-22.37	-19.67	-46.85	-50.51	-
GOLD SPOT \$/OZ	USD	1183.1	-0.59	1.62	5.47	5.05	2.68	-1.88	-0.74	-5.07	-32.70	-
CURRENCIES												
DOLLAR INDEX SPOT	USD	94.371	0.14	-0.33	-1.92	-0.96	-3.24	-2.99	4.69	11.24	19.01	-
Euro Spot	EUR	1.1386	-0.13	0.11	1.74	0.72	4.56	5.67	-6.01	-11.23	-12.89	-
Japanese Yen Spot	JPY	118.9	-0.23	0.91	0.59	1.17	4.17	-0.13	0.50	-10.78	-33.81	-
British Pound Spot	GBP	1.5459	0.12	1.01	2.31	-0.10	-0.85	3.64	-0.64	-3.79	-3.94	-
Swiss Franc Spot	CHF	0.9506	-0.28	0.87	2.10	1.88	0.47	0.28	4.30	-1.13	-2.85	-
Brazilian Real Spot	BRL	3.7994	0.35	-0.37	3.90	1.65	-17.36	-20.28	-30.05	-35.32	-	-
China Renminbi Spot	CNY	6.3463	-0.12	-0.14	0.03	0.27	-2.27	-2.47	-2.34	-3.63	-	-
Singapore Dollar Spot	SGD	1.3781	-0.25	0.94	2.95	1.09	-1.07	-2.31	-4.06	-7.77	-11.73	-
Norwegian Krone Spot	NOK	8.0975	0.06	-0.17	5.22	0.61	0.86	-4.25	-7.92	-19.13	-30.07	-
VOLATILITY / LIQUIDITY INDICES												
CBQE SPX VOLATILITY INDX	USD	16.05	-10.98	-12.77	-34.49	-24.82	32.54	27.38	-16.41	-36.31	5.45	-
USD SWAP SPREAD SEMI 2YR	USD	11.43	6.12	4.49	3.94	12.52	-51.73	-53.90	-47.12	-56.68	28.36	-
TED SPREAD	USD	32.03	-0.59	0.22	-7.24	15.05	15.05	21.19	45.52	50.45	34.13	-

All data is compiled from Bloomberg

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