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Monthly Commentary *3rd September* 2012

August was a mixed month for asset markets with some major equity markets such as the US and Europe modestly up, while UK and Emerging Market equities were slightly down. Commodities had a good month as markets are pinning their hopes on the Fed providing new stimulus through QE3.

It is becoming increasingly challenging to find evidence that will help us determine future market direction. Despite the well-publicised worries of the upcoming US Fiscal Cliff, the never-ending Euro crisis, slowdown in China and turmoil in the Middle East, the summer was kind to risk assets, as if the markets are tempting a troubled world with a yawn and arrogance: “Is that all you’ve got?”

But do policymakers really know what they are doing, and do market strategists have any better insights than ordinary investors?

In a telling comment in the Financial Times, and referring to Bernanke’s latest words of wisdom from Jackson Hole, a Lex columnist wrote:
“...sometimes investors should pay close attention, if only to remind themselves that elite policy makers have as little clue about the state of the world as they do. For example, as house prices fell around his ears in 2007, Mr Bernanke’s Jackson Hole speech reminded delegates that “past efforts to strengthen capital positions . . . place the global financial system in a relatively strong position”. Oops!”

As far as “top” strategists are concerned, a recent survey just published in Barron’s found most of them to be bullish on risk assets – with only a minority ringing alarm bells, but with no new obvious worries to justify their bearishness. Is this complacency a contrarian signal, or are markets indeed “cheap” and promising?

This month we supply three themes that may be interpreted by you:

1. **China-Commodities**. Below is a chart that shows the divergent summer fortunes of the commodity index (in black) and the Chinese Stock Market (in orange). Isn’t China, to a large extent, supposed to be driving the demand for commodities? Which of the two is the leading indicator?

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2. **BRIC Currencies**. In the last year, the USD has appreciated considerably vs most BRIC currencies – the Chinese Yuan being the exception. From below, the USD is up 23% vs the Brazilian Real, 21% vs the Indian Rupee and 11% vs the Russian Rouble. Does this mean a return to risk aversion? If so, the markets have ignored it. Or are deteriorating trade conditions forcing developing countries to revert to old habits of competitive devaluations? If so should we be worried that slowing economies will impact asset markets negatively?

3. **Top equity markets in August**. In looking at the best performers in August, it is like reading a Who-is-Who of the most problematic countries. Venezuela was up a whopping 16%. The periphery of Europe is well represented with Madrid, Athens, Lisbon, and Milan featuring prominently in the top 7. Have the markets started to discount a resolution to the Euro crisis, as many believe, or can dead cats still bounce? The aforementioned markets are in good company – Egypt, Pakistan, Roumania.

Ranked Returns: Equity Indices Page 1/ 6

Total: 93 Indices Ret Period 3 Region 0 Base Curr USD Adjust? Y

Best Performing Indices

World Equity Indices Currency Adjusted
Start Date 7/31/12 - End Date 8/31/12

1)	VENEZUELA STOCK MKT INDX	16.57
2)	IBEX 35 INDEX	11.62
3)	Athex Composite Share Pr	9.89
4)	PSI 20 INDEX	9.63
5)	EGX 30 Index	9.33
6)	PRAGUE STOCK EXCH INDEX	8.97
7)	FTSE MIB INDEX	8.63
8)	BUCHAREST BET INDEX	6.86
9)	OBX STOCK INDEX	5.18
10)	KARACHI 100 INDEX	5.02

In the context of the above, alternative funds were mixed. We still believe that with so much uncertainly they will deliver better risk-adjusted returns than traditional equity portfolios. As Winton Capital recently said, referring to the lacklustre YTD performance of their flagship fund, "*consider your investments panning out for decades rather than years or months*". At least they have the 15-yr track record and continuing massive R&D investments on their side.