Monthly Commentary 2nd October 2017

September was a good month for equity markets. US and European (ex-UK) Equities were up. Bonds fell as government bond yields rose. Commodities were especially strong, aided by the strong gains in crude oil prices. In currencies, the pound sterling was the standout winner as it gained 3.69% vs the dollar and 4.50% vs the euro.

The UK markets

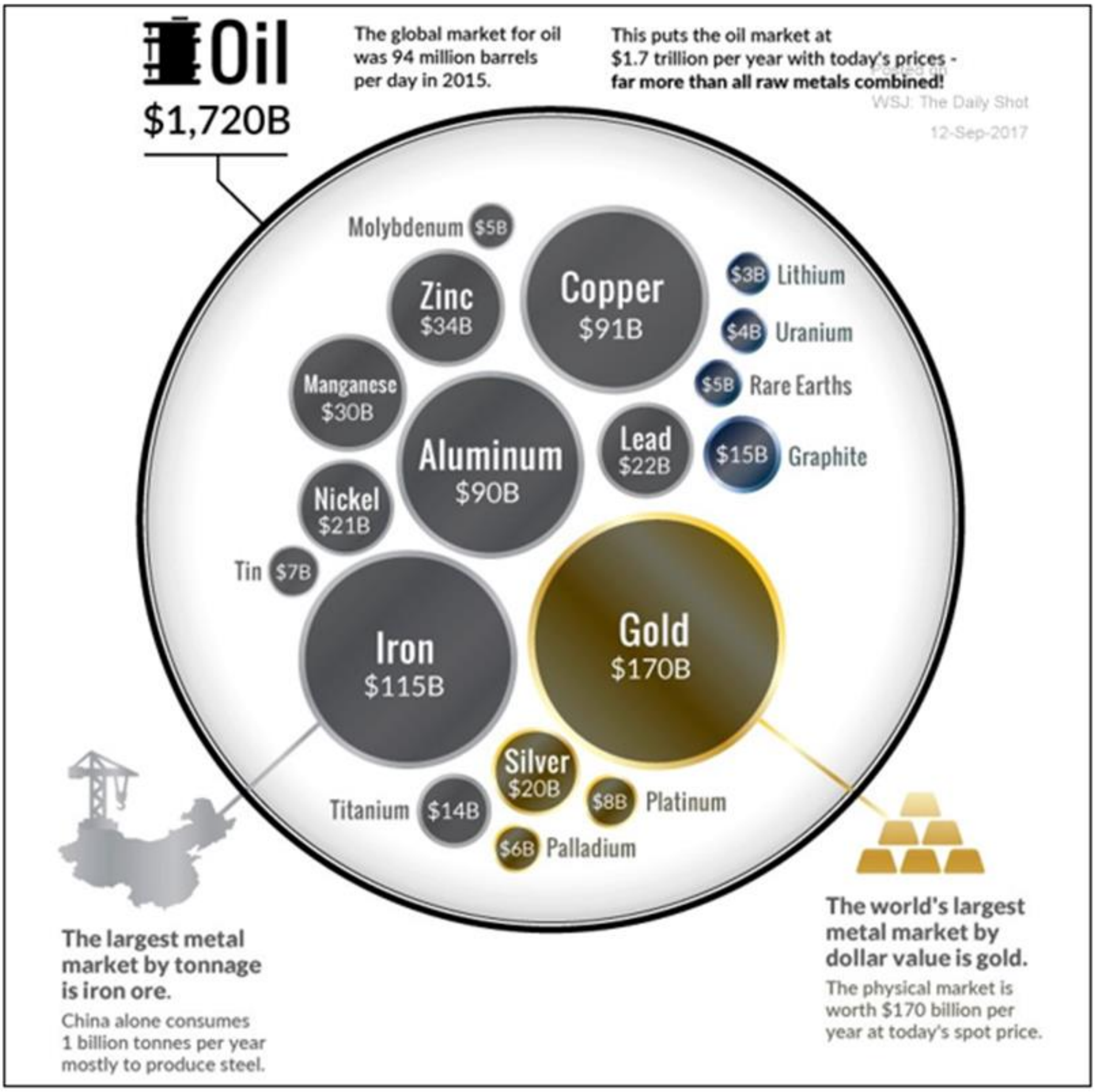
There was notable movement in UK markets, triggered by the Bank of England's more hawkish mid-month communication on the path of interest rates. Gilt yields rose sharply (bond prices fell), the pound rose strongly and the FTSE reacted negatively. We have been asked repeatedly where we think sterling will be over the next 12 months, and frankly our answer is as it always has been when predicting currency exchange rates. I.e. we do not know.

Big-bank foreign exchange strategists always have a view but their forecasts turn out to be anything but reliable. For example, as recently as Sep 14th (the day the Bank of England met), HSBC had a longstanding forecast of a GBPUSD rate of 1.20 by yearend. The actual rate in mid September was around 1.33 to 1.34. Then, the day after the meeting, HSBC changed their forecast dramatically to "1.35 by yearend". Yes, it's commendable that they change their mind as facts change, but the fact that the currency had already moved to a value that is very close to their new forecast shows how reactive they were. If one was to have believed their previous forecast of 1.20, they would have sold sterling at 1.25 or 1.28 or 1.30 and waited until the end of the year to buy it back at 1.20. This would have resulted in sizeable losses.

We repeat that one of the reasons our clients have limited (up to 15%) assets invested in securities outside of their home currency is because foreign exchange predictions can go very wrong.

The size of commodities markets

If you have ever wondered how big each commodity market is (by traded value on an annual basis), the picture on the next page, courtesy of Visual Cap shows it quite elegantly.



As you can see, the oil market is ten times as large as gold, which is the second biggest. Will the lithium market grow as demand for electric vehicles explodes?

Bitcoin anyone?

With the price of Bitcoin soaring more than 300% so far in 2017, digital currencies have become big news. We are asked repeatedly what our opinion is, and how we one can access a bit of the action.

We readily admit that we are not knowledgeable enough to form an opinion on digital currency developments, even though we are watching in fascination what is happening.

Some prominent figures in finance such as Jamie Dimon, the CEO of JP Morgan, and George Soros, the legendary investor, publicly stated that Bitcoin is a bubble that will crash and burn. Others like Tom Lee, the ex chief investment strategist for JP Morgan and currently at Fundstrat disagrees and says Bitcoin could rise to a range of between $20,000 to $55,000 in the next five years. With today's price around $4,000, that's a potential gain of 5 to 14 times today's price!

So how does one buy it? We are aware of two ways.

The first is to register on a site called Coinbase https://www.coinbase.com/ . It is quite straightforward. You'll need to give your full name and email, upload your ID or passport and provide the bank details from where you will send the money to Coinbase. You will need to send a token small amount (say $5) to them in order to verify your account. It takes a few days and then you can start buying and selling Bitcoin or Ethereum or Litecoin (two other digital currencies). You may also use a credit card, but the transaction size is limited and when you sell, you'll still need to provide a bank account.

The second is to buy (through your broker or online broker), the only Bitcoin-related ETF called the Bitcoin Investment Trust (ticker GBTC). This tracks the value of Bitcoin and has already grown to $1.3B in assets. Due to the dearth of other similar products there is huge demand for this ETF and as such it trades today at close to a staggering 100% premium over its net asset value. As such we would avoid it until there are more ETFs around and the premium collapses. Still, for people like Tom Lee who believe there is huge potential upside, even paying double today to buy Bitcoin, will be a blip if the price does indeed move up multiple times that.

Elgin will be happy to assist you in opening an Interactive Brokers online account and facilitate buying digital currencies.

PIMCO UK Low Duration Fund GBP

On a different note, PIMCO has recently announced the pending closure of the PIMCO UK Low Duration fund. The decision was made following a review of their existing fund range as well as the relative size of the fund's assets. The reason we have been investing in the fund is because it invests in low-duration high-quality bonds that are not subject to much interest-rate risk should rates rise (as they have been doing in the UK lately). Our clients who are invested in the fund will not be negatively affected by any means. The fund is still 100% liquid and has not lost from its value. Pimco has given us notice until the 18th of December to replace the fund with another fund in their range at no cost.

Alternatively, if we don’t place instructions to sell, they will distribute the net cash proceeds at the termination date. We will then use the proceeds to invest in a fund of our choice. The bottom line is that no investor will be negatively affected by this action.

The Elgin Analyst Team

Disclaimer

The information in this article should neither be regarded as an offer nor a solicitation to buy, sell or otherwise deal with any investment referred to herein. As a regular rule, the value of any investment may rise or fall. Past performance is not an indicative of future results. Do not take unnecessary risk and always request advice from an investment professional before undertaking any investment.