

Investment Commentary

From the Investment Desk
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Interesting Times

Many beliefs, hypotheses and models, even temper, will be tested, again and again:

- The US elects the country's first African-American president (44th) since independence on 4-Jul-1776. Pre-announcement, US equity indices rose >3%, but plunged by >5% last night (Asia, up >1% to >4% this morning). Porkier spending could inflate American deficits to a record 12% of the country's GDP; Democrats are known to be more protectionist and insular. The US government asks for US\$550 billion to rescue failed financial institutions, several trillion could be in the pipeline to resuscitate the entire US economy. *And that's just the US*. At this rate, central banks in Asia, GCC, Russia should be seriously questioning their holdings in US debt (read: USD). Jim Rogers is shorting treasuries. Gold bugs are shouting delivery. Gold has failed as inflation hedge, it seems, but the value has been manipulated by commodities exchange paper traders. Actual demand for bullion still holds (although Bombay Bullion Association reported -27% year-on-year in Oct volume).
- After Iceland, Argentina, Pakistan and Ukraine could be facing bankruptcy. Many several highly leveraged small economies could be part of the dominoes. IMF is getting busier and more stressed.
- Globally, simultaneous but uncoordinated interest rate cut programs and liquidity injection (which gets hoarded by banks) fail to shore up investor confidence. The US and Japan are running low on monetary ammo (Fed and BOJ rates of 1% & 0.3% respectively). Several countries will be forced to take fiscal measures. China fast-tracks its infrastructure build-up; the country's equities could be one of the firsts to bounce. GCC is cash-rich, but falling crude oil price is putting some pressure. If foreign reserves get depleted like the ways of South Korea (-11% or US\$24b), then we could be in trouble. Good luck to UK Prime Minister Gordon Brown in his courting GCC SWFs to top up IMF's kitty.
- Like fashion, inflation came and went, for now. Commodities could test another low (crude oil at US\$50? gold at US\$640?). But with major advanced economies printing money, inflation could haunt us in a matter of time. OPEC is cutting production. Gold is getting more expensive to extract, so are most minerals.
- Hedge funds, prop desks¹ and other black boxes failed to see how correlated most asset classes and trading ideas have become. Across-the-board redemption and deleveraging are killing them. No one could have thought that the governments would ban all forms of short selling. China bucks the trend by recently introducing shorting.
- Expect temper to flare. Food riots aside, countries are easily tempted to draw their guns over oil (Myanmar & Bangladesh, Russia and Georgia), piece of history (Thailand & Cambodia), territory (Israel & religious rivals).

The spotlight shines on European financial institutions (Societe Generale, Commerzbank, UBS), which now disclose financial losses and appear with hats in their hands. Europe is another financial epicenter, as their banks are more leveraged (relative to those in the US) and exposed to credit-strapped emerging economies.

Global economies are retrenching. Conversely, I imagine that criminals are hiring recruits in desperation for food (and so will law enforcers for peace). Currencies are driving us nuts.

Equities seesawed, and could see a bear rally in the short term (until year-end?). LIBOR rates steadily slide (from 4.8% to 2.7% for USD), providing relief, for now. Then investors will see that current financial problems are still an overhang. Jittery clients could take the opportunity to gear down their risk exposure.

¹ Proprietary trading units of banks

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