Musings From The Barstool. 10 Seconds Into The Future…

Additional Disclaimer: The following thoughts are musings and not advice.

Our current view of the global economy is that Trump's policies may provide some turbocharging to an economy that is already in a growth phase, but that the short term stimulus is in fact a temporal wealth transfer and that growth slows due to higher rates and tighter financial conditions from 2018 onwards. The US equity market has therefore built in significant hope and optimism and while it may head higher, is a risky bet. The corporate credit markets are similarly pricing in such optimism but technical factors, namely the demand for yield and the supply of corporate paper will be sufficient to support the credit markets and push them into ever tighter territory.Europe is clearly in a growth phase which will lift corporate prospects, however, political concerns will cap upside in equities and credit. With Dutch, French, German and possibly Italian elections on the horizon, and with Brexit hanging over the region, it is hard to see valuations improving. Europe is a buyer's market, but investors may be forced to be patient.

More immediate and tactical opportunities present themselves in the commodity markets.

Energy:

The demand and supply dynamics of oil imply a significantly stronger oil price. More than all the fundamentals and demand and supply is the Aramco IPO, which requires a stable oil price between 50 to 65 to price decently, is the main driver of oil and the Saudi's will defend this range come hell or high water. For the delta driven trade, the Exploration and

Production sector has the most potential. Within this, tight oil is attractive, it is relatively small and will not drive pricing but is efficient enough to worry OPEC. *XOP is a natural candidate for expressing such a trade.*

There are other trades one might attempt, such as a Long Brent Short WTI trade, betting on relative demand and supply imbalances between the US and Europe/Middle East.

An indirect play which also expresses a Trump energy policy element to it is a simple long position in MLPS LN, the tax efficient UCITS MLP ETF tracking the Morningstar MLP Index. MLPs are yielding over 7% in a rising energy price environment.

Industrial metals:

China's reflationary policies and efforts to put a floor under its growth metrics played no small part in the recovery in commodity markets. There are, however, reasons to believe that the recovery has more to go and is built on a firmer base. The last assault in the global trade war which involved reorganizing manufacturing to face a domestic audience is complete and has resulted in global manufacturing coming out of recession. Industrial commodities should, by implication, also exit recession, and has. The new structure of manufacturing will grow and prosper in its current state until it exhausts domestic demand. Until then, however, commodities will follow suit. *XME is a natural candidate for expressing this trade.*

If we had to make more conventional country bets: Japan and India.

The demonetization in India is misunderstood. Ostensibly to root out the black economy, demonetization was an immediate reduction in money supply which basically disabled the majority of the cash economy for a period of time. However, money supply will in all likelihood rise significantly. The

demonetization is basically an exercise which transfers cash from physical form (and thus subject to no multiplier) to electronic form (subject to the multiplier inherent in the fractional reserve system.) Note the RBI's initial shock absorbing 100% reserve ratio requirement immediately after demonetization which has now been rolled back. The impact on the Indian economy and assets will be significantly reflationary. The RBI will likely halt any rate cuts until the liquidity injection is absorbed.

Economic growth in Japan has been sub-par for a long time. Abenomics is getting long in the tooth and the BoJ has deployed an array of unconventional policies from QQE to NIRP to buying ETFs and now near total control over the yield curve, to stave off deflation and recession. It is difficult to see Japan achieve escape velocity, however, the current environment presents some interesting opportunities.

With growth coming from such a low base and expectations so dire, the potential upside in growth and small cap growth companies could be substantial.

The yield curve control policies of the BoJ present the banks with a profitable trade, involving buying long dated JGBs, allowing them to roll down the steep long end (intentionally steep by BoJ policy), before selling them to the JGB (which cannot buy directly at auction as it is deemed monetization.) This trade is very profitable for banks and insurers.

The multiple fronts on which the BoJ operates is exhausting its options and it is unlikely that the BoJ can accelerate its activities on any front any further, thus no further easing. Coupled with a hawkish US Fed, this implies a weaker JPY which is generally positive for Japanese equities and especially positive for exporters or multi nationals.

And finally a word about Singapore…

It is tempting to be too bearish about the prospects for

Singapore. The world is in a cold trade war which threatens to go hot, and trade is some 400% of Singapore's GDP, interest rates are rising and the MAS policy of targeting the exchange rate imports rate hikes from the US, China, Singapore's 2nd largest trading partner is reining in monetary policy to manage the surge in credit from 2016, and energy prices while having recovered from deeply distressed levels, hover in a tight range insufficient for saving Singapore's oil and gas, and shipping sectors.

Energy prices are rebounding and are likely to rise further. The impact on the energy and the related maritime sectors (collectively some 12% of the economy) will be significant. In the next 12 months, growth is likely to exceed expectations.

In the longer term, Singapore's fortunes will be dependent on its ability to reinvent itself in the face of a more insular world.

PS: European Convergence Trade.

The impending French elections are hardly having any effect on European equities. In the bond markets, however, political risk is being priced in. One trade which might pay off, and to be sure this is clearly a bet, a wager, a gamble, is to buy the French 10 year bond and short teh 10 year bund. The spread is currenlty 0.7 and could well head below 0.5 if Le Pen does not win the election, and she is not expected to. Why are the bonds pricing up like this? A Le Pen victory is a very low probability event indeed, but if it did happen, she has promised a referendum on euro membership, and this would create a very uncertain environment in the Eurozone. No one knows how a member would extricate itself from the single currency, yet the question is become more and more topical, to the extent that the Dutch have commissioned a study into how to effect an exit and what the consequences might be. For some countries exit might be difficult but for others, particularly those with big TARGET2 deficits, exit might well be

intractable.