Weekly Investment Bulletin

20th August 2012

MITHRIL ASSET MANAGEMENT

Market Roundup:

*****We wish to point out that Mithril Asset Management, Mauritius has no affiliation whatsoever with Mithril Capital Management*****

Western stock markets marched on in defiant mood. The Euro dared to trade at some of its highest levels in 6 weeks as the market expects some kind of stimulus program in the form of a debt purchase program. The words of Angela Merkel soothed market tensions as she proclaimed leaders were committed to do ‘everything’ to safeguard monetary union. Realistically, would she say anything else?

Merkel is also rumoured to be testing the relations with her coalition and fellow Euro zone members by considering easing Greece’s bailout terms. Generous? Certainly. Foolish? We’ll have to see.

News from the US reported on Thursday that building permits jumped to their highest level since August 2008, a hint of stronger construction in the coming months as commented in previous bulletins. Meanwhile good news from bulge bracket corporations always lifts the general market mood, with networking equipment giant Cisco reported earnings that beat expectations. Apple now trades at an all time high, after paying its first ever dividend to investors in 17 years.

Other than housing permits, economic data was a little light, with US consumer data the only worthy addition. Consumer sentiment increased to 73.6, the highest level since May, from 72.3 the prior month. After 2 months of declining sentiment, this month’s numbers indicate consumers may be feeling the benefits of growing payrolls. This can filter through to a hike in retail sales, which would set the pace for stronger growth for the remainder of the quarter.

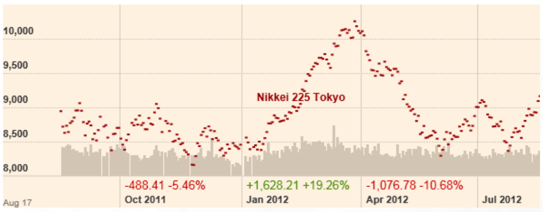
Market Data (12 month):

S&P 500:

FTSE100:

FTSE Eurofirst 300:

Nikkei 225:



Shanghai Composite:

Source: www.ft.com

Registered Office: 3rd Floor, Ebene House 33, Cybercity, Ebene, Mauritius. Licence Number: C108007141. Company Number: 086547 C1/GBL

Rebuilding Europe:

With the introduction of the Euro it became possible for some Euro zone countries to borrow at much cheaper rates than previously. This is because although the debt was still national debt, the assumption was made that being within the Euro meant that the risk of these countries had declined as a result of the economic rules they were now bound into. The principle rules required Euro zone members to ensure that government debt did not exceed 60% of GDP and that any budget deficit should not exceed 3% of GDP. Effectively the gloss of the good credit rating of countries such as Germany rubbed off on countries such as Portugal, Ireland, Italy, Greece and Spain.

So what went wrong? Unfortunately while Germany continued its tradition of investing in research and development and other productive purposes, others used too much of the available credit to consume more, build generous social systems and fund a construction boom. Not to say that it's just the PIIGS at fault, this excess consumption was encouraged by others as it helped demand and growth in their own economy. Think of second homes in sunny South European climates and German auto motive expansion on the back of a weaker currency than its predecessor.

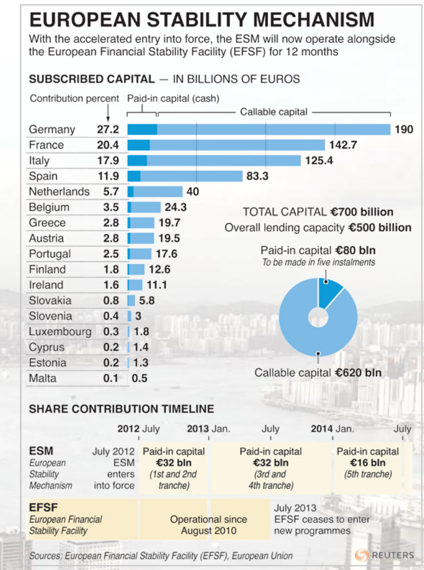
As a result of the growth in consumption, many of the countries now in trouble built up large balance of payment deficits that are clearly not sustainable at their levels of GDP. This model can only lumber forward so long as we don't have an economic downtown, and credit markets stay liquid. What if then the GDP levels required to sustain repayments come under risk, and furthermore, credit markets freeze?

European Union (EU) Emergency measures taken by the EU:

- Increasing the minimum level of bank capitalisation to aid their stability and ability to withstand further shocks.

- European Financial Stability Facility (EFSF). This was created in May 2010 to raise the funds needed to provide loans to Euro zone countries in financial trouble, to buy sovereign debt and to recapitalise banks. The EFSF is jointly and severally guaranteed by the Euro zone countries.

- European Financial Stabilisation Mechanism (EFSM). This was created in January 2011 and involves the European Commission raising funds using the EU budget as collateral. The EFSM has lent funds in conjunction with both the EFSF and the International Monetary Fund (IMF).



Source: Thomson Reuters

Cont:

The financial crisis which started in 2007 caused problems with the liquidity of banks and, as a result, lending and economic growth faltered. However, many of the loans made to both governments and private organisations had assumed certain levels of growth and when these failed to materialise problems arose with repaying and servicing the debts.

The failure of some countries to stay within the economic rules set for the Euro zone and the failure of the Euro zone as a whole to police these rules, which effectively let countries get away with ignoring the rules, has meant that countries are now tied to a currency over which they have little control and which, due in part to their own failure to abide by the criteria, is no longer suitable for their needs.

As a member of the Euro they do not have the power to devalue their currency or the monetary policy flexibility to take other action to try and resolve the situation they find themselves in. For instance, in Greece tourism, which accounts for 18% of Greek GDP and employs about one in five Greek workers, has been significantly reduced as a result of the strength of the Euro.

What has been done so far? No country has been allowed to default for fear that this could cause a domino effect and cause defaults of other banks and nations, known as the dreaded contagion.

In order to reduce the risk of further and ongoing crises, a closer fiscal union between Euro zone members is envisaged. This will involve more stringent fiscal rules and greater penalties for countries not abiding by those rules. Euro zone members have individually lost control of their interest rates, exchange rates and capital controls that they need to adjust exports or consumption.

For example, Germany needs to promote domestic consumption while Greece needs to reduce consumption and promote exports. It will be a difficult task for Greece to achieve this whilst they remain in the Euro. The European Stability Mechanisation (ESM) is a permanent scheme which took over from both the EFSF and EFSM in July this year. It will act as a financial firewall and through guarantees; limit the potential for default by any one country and hence the risk of contagion.

If Europe works together then it should be possible to overcome the current debt crisis. But at times of economic hardship it is not easy for the nation states within Europe to put aside their own self-interest for the common good.

Action to reduce the harmful levels of uncertainty has been taken and a full-blown crisis has so far been avoided. However, there is a need to ensure that the demands for austerity do not extinguish the potential for much needed growth. Too much austerity could condemn nations to persistent stagnation, the social cost of which should not be underestimated. Youth unemployment in Spain is currently at 40%. While within Europe there seems to be a political acceptance of these costs in support of the Euro project, a sovereign nation and its population are unlikely to want to bear such pain for too long.

Weekly Investment Bulletin

20th August 2012

MITHRIL
ASSET MANAGEMENT

Currencies:

EURUSD

EURUSD remains in downtrend from 1.3486, the rise from 1.2042 is treated as consolidation of the downtrend. Key resistance is located at 1.2747, as long as this level holds; we'd expect downtrend to resume.

EURGBP

Despite a dip to 0.7811, there was no follow through selling in EURGBP. Initial bias is neutral this week for some more sideway trading. Key resistance is at 0.7962. Below 0.7811 will target 0.7755.

GBPUSD

GBPUSD stays in a trading range between 1.5393 and 1.5776. Lengthier consolidation in the range would likely be seen in a couple of weeks. Key resistance is at 1.5776, a break above this level will target 1.5900 area.

USDCHF

USDCHF remains in uptrend, with the fall from 0.9971 treated as consolidation of the uptrend. Support is at the lower red line and uptrend could be expected to resume after touching the channel support, and one more rise to 1.0200 would likely be seen.

USDJPY

USDJPY has fully broken above the upper line of the price channel, suggesting that a cycle bottom has been formed at 77.92 (lower red line), and the downtrend from 80.61 has completed. Further rise could be expected this week, and next target would be at 80.50 area.

USD Weighted Index

With FOMC Minutes forthcoming, the fresh batch of central bank rhetoric may fuel a short-term rally in USD should the Fed report an improved outlook for the region. As central bank officials see the recovery gradually gathering pace over the coming months, the committee may continue to soften its tone for policy intervention, and it seems as though the Fed is slowly moving away from its exit strategy as the economy gets on a more sustainable path.

Gold:

As long as prices remain above $1600 the sentiment is mildly bullish but we must not overlook that prices have been in a $100 trading range for the last 3 months. Gold posted its biggest one-day gain (1% on Thursday) in two weeks after Merkel voiced support for European Central Bank President Mario Draghi's crisis-fighting strategy paving the way for bullion-friendly stimulus.

Crude:

Oil climbed above $95 a barrel for the first time in three months as U.S. building permits reached a four-year high and equities advanced, adding optimism that faster economic growth will boost demand. The price reached $95.75, the highest intraday level since 14th of May. July's housing permits, a proxy for future construction, surpassed the 769,000 pace forecasted.

Registered Office: 3rd Floor, Ebene House 33, Cybercity, Ebene, Mauritius. Licence Number: C108007141. Company Number: 086547 C1/GBL

MITHRIL ASSET MANAGEMENT

Summary:

The holiday season remains for this week so expect trading volumes to be lighter and equity indices to hover with no concrete direction. The same is likely to be for energy markets. Whilst the rhetoric is pleasing to hear, the words of central banks and politicians will require action and policy to back them up. Until then, it remains just talk – and the resulting optimism can only go so far. Forthcoming FOMC minutes and initial jobless claims from the US market will have the potential to add some joy if greeted positively but whether it can propel a sustainable market rally is unlikely.