Weekly Investment Bulletin

25th February 2013

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Market Roundup:

Activity in markets was mixed for the week, after a very strong start to 2013.

Japan's Nikkei advanced 1.9% whilst the Shanghai Composite slumped 4.9% and the Hang Seng Index gave up 2.8%. Concerns that policy makers in China might keep home prices controlled with additional tightening measures kept investor sentiment subdued for the week. Efforts from the Chinese central bank to recoup excess liquidity from the money markets signalled their intention to tighten monetary policy for the near term.

European markets ended the week flat. The good news was that banks in the euro zone have prepaid another €5 billion of the three-year loans issued by the European Central Bank in late 2011, reducing the volume of the balance sheet, a broad measure of risk in the single currency zone. Banks can now repay their loans early on a weekly basis. January 30th marked the first day that this was possible and banks repaid €137 billion, in a show of confidence that financial markets are returning to health. The FTSE 100 momentarily flirted above 6400 (a 5 year high) as Bank of England comments suggested willingness to launch more quantitative easing.

The mood was checked as investors took note of euro-zone consumer-confidence data for February showing a softer-than-expected improvement. Upbeat data out of Germany helped lift matters. The Ifo Business Climate index jumped to 107.4 in February, exceeding expectations of a 104.7 reading on Friday.

US markets broke a 2 day losing streak to advance later in the week, influenced by German business data and strong first quarterly revenue from HP lifted indices.

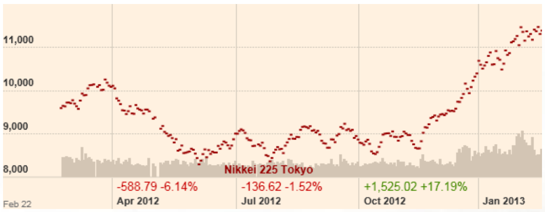
Market Data (12 month):

S&P 500:

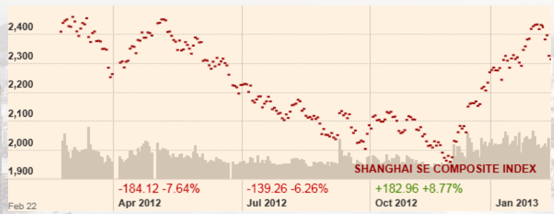
FTSE100:

FTSE Eurofirst 300:

Nikkei 225:



Shanghai Composite:



Source: www.ft.com

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Where Strength is the Weakness:

During the last 2 years, the Euro zone has been through some very dark times, which at times threatened its very existence. Make no mistake, it's not out of the woods, however confidence in Europe's ability to tackle the crisis has led to its stock market advancing since last summer and caused the single currency to advance.

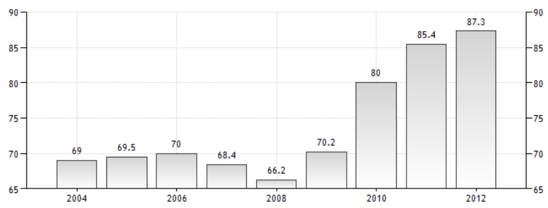
So when European finance ministers met this week in Brussels, the topic was that of strength rather than its many weaknesses. So during a period of such economic fragility for Europe a strong currency, and the resulting expensive exports is not going to help matters. In contrast, imports become cheaper making resources such as oil less expensive.

On Monday, France, which traditionally favours market intervention, renewed its calls for remedial steps that could include establishing a target level for the euro's value.

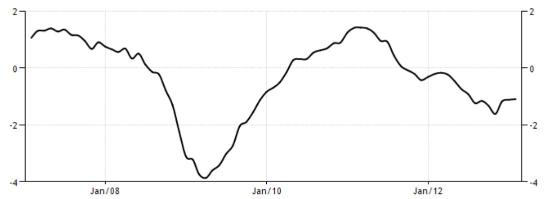
This was immediately met with resistance from Germany, who saw this as a poor alternative to policy upheaval which has crippled the system in the past. Above all, and quite poignantly put, this offers a welcome smokescreen for making ones economy more competitive. Indeed any policy measure designed to artificially weaken ones exchange rate ultimately ends up in higher inflation.

ECB Chief Mario Draghi, warned last week that the strength of the euro could weigh on the ability of Europe to pull out of recession. Those comments were enough to send the euro down sharply against the dollar — to $1.36 from $1.34. The euro was trading at $1.339 on Monday after falling to the low $1.20s last year.

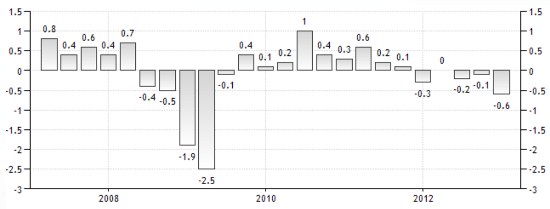
Euro zone Government Debt To GDP:



Euro zone Business Confidence:



Euro zone GDP Growth Rate:



Source: www.tradingeconomics.com

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Cont:

The push for intervention by the French is unlikely to make much real progress. The general consensus went against them as the French seem to think that allowing the market to determine fair value is a concern. Instead, this just rewinds us back to late 2011 and the way that economic policies in the euro area are a result of a back-and-forth between states like France and Germany.

France is likely to have an agenda. Despite its poor economic indicators, it wishes to retain control over the speed at which it reforms, as well as the creation of euro zone backed debt.

The latter remains at the back of people's minds. Unlimited ECB liquidity has helped bring the individual nation debt markets under control. The next task is to bring the bloc out of recession. For that to do so, it's biggest economies need to perform.

Hopes that the euro zone might emerge from recession soon were set back on Thursday as data showed that a downturn in business activity in the region worsened unexpectedly this month, especially in France, where the gap with Germany is at its widest since 1998.

While companies in Germany sustained a healthy rate of growth, French services companies were experiencing their worst slump since early 2009, when the financial crisis and subsequent recession were at their worst.

The figures came a day before the European Commission was due to announce interim economic forecasts for the 27-nation bloc, including which countries did not meet European Union targets on budget deficits.

The Markit's purchasing managers' index for service industries in the euro zone would add to tentative signs that a recovery was in the offing.

But the indicator fell in February to 47.3 from 48.6, marking a year it has been below the 50 threshold for growth. Expectations were of an increase to 49.

By far the most worrying aspect of the data released Thursday was the dismal performance of French companies, which were more befitting of peripheral economies such as Spain and Italy.

By contrast, Germany has had a good start to the year. German investor morale soared to its highest level in nearly three years this month. Still, there are limits to what German prosperity can do for the rest of the region, blighted by harsh budget austerity and rising joblessness.

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Currencies:

EURUSD

EURUSD broke below the trend line, suggesting that lengthier consolidation of the uptrend from 1.2042 is underway. Further decline is still possible this week, and the target would be at 1.3000-1.3050 area.

EURGBP

EURGBP rose further to as high as 0.8764 last week. Initial bias is neutral this week first and some more consolidations could be seen below 0.8764 first. We expect downside to be contained above 0.8446 support and bring rally resumption. Sustained break of 0.8764 will target 0.9000 psychological level.

GBPUSD

GBPUSD's downward movement from 1.6339 extended to as low as 1.5131. Further decline is still possible this week, and next target would be at 1.5000 area.

USDCHF

USDCHF is facing the resistance of the upper trend line, a clear break above the trend line resistance will suggest that the downtrend from 0.9971 had completed at 0.9021 already, then further rise to 0.9700 area could be seen.

USDJPY

USDJPY stays above the trend line, and remains in uptrend from 77.14. Support is at the trend line, as long as the trend line support holds, the uptrend could be expected to resume, and another rise towards 100.00 is still possible. Key support is located at 92.00.

USD Weighted Index

We may see the bullish pattern pan out in the week ahead should we see a growing number of Fed officials strike an improved outlook for the US. In turn, we may see USD set another high during the final days of February, and we will maintain a bullish outlook for the reserve currency as the FOMC appears to be slowly moving away from its easing cycle.

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Gold:

Gold futures ended Friday's session at the lowest level since July, as speculation the Federal Reserve might end its bond-buying program sooner-than-expected continued to dampen its appeal. Moves in the gold price this year have largely tracked shifting expectations as to whether the US central bank would pump more money into the financial system. The possibility that the Federal Reserve could end its quantitative easing program earlier than expected helped lift USD, which also hampers gold's attractiveness.

Crude:

New York-traded crude oil futures were higher for the first time in three days on Friday, as investors returned to the market to seek cheap valuations after prices fell to a seven-week low. Oil prices came under heavy selling pressure earlier in the week as a broadly stronger US dollar and concern the Federal Reserve may scale back its stimulus program weighed on appetite for assets linked to GDP growth in the US.

Summary:

As we said last week, with the March 1st US debt ceiling deadline approaching, markets are likely to become volatile. We can see how recent Fed comments (hinting at reducing monetary stimulus) have sent major commodity markets into spirals and as the latest fiscal cliff deadline looms, Washington still has worked to do. Should no compromise be in place by Friday, the Fed may have to rethink its strategy.

Much maligned Italy headed to the polls yesterday for the first of its 2 day elections. With technocrat Mario Monti not running, markets appear to have priced in the best case scenario of a centre-left victory by Pier Luigi Bersani's Democratic Party in the lower house and a Senate result that forces Bersani to team up with Monti for an upper-house majority. But as ever, Silvio Berlusconi lurks and should he have a strong showing of votes, disappointment will creep into European markets.

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