Occasional Commentary from the Chief Investment Officer, Wednesday, March 11, 2015

Interim Update

In our 2014 year-end review, we felt that EU was screening as being fundamentally cheaper than the US and sensed that for 2015 this could set up a period of sideways action in the US and perhaps relative EU outperformance. This has happened nicely for Q1 but any non-Euro denominated investors would have had to have hedged the Euro in order to benefit from this outperformance. Going forward, the outlook for the Euro and its recent volatility may dissuade some international investors from allocating capital to the EU, which may slow down or limit the upside.

For now at least, on balance, we still think that the fundamental valuations of blue-chip Europe are more attractive than those of the US and hence we would continue with this relative trade view for the time being, with a close eye on the FX markets. We have traded the US Dow Transports tactically from the short side of late and still retain a short bias, no real change in our view on that front,

Oil has started to show signs of sideways distribution but we still feel that there could be another leg down before any stabilisation could take hold. Oil majors and energy services companies are at various 'self-help' stages and we continue to accumulate, selectively and gently, with a medium term view looking well beyond 2015 and into 2016.

For a considerable time, we have been negative on Miners, Resources and some Financials (Banks). We have started to lighten our negative stance on Miners and Resources as some of the larger names are approaching valuations which represent good entry points from a long term perspective. Forward curves for the materials they produce still seem sickly and hence we are not anticipating huge surprises in the near term. But with strong balance sheets and the optionality and flexibility which that brings, we feel that the levels might soon give us a margin of safety to take positions.

We remain optimistic on Japan but since increasing our bias to Japanese equities further in late 2014, the appreciation has been welcome but steeper than expected – and steeper than seems justified. Hence, we advocate lightening up for the time being, with a view to securing a re-entry point a little lower. Should the economic and political landscape continue to flourish, we are not averse to re-establishing our positions.

On Commodities, we have started to build a small position in Wheat as the current level is approaching the cost of production in some regions and likely below in a few areas as well. On a medium to long term cyclical view, such times seem to be decent entry points. On FX, we're continuing with our pre-existing Longs in USD/ZAR, Long GBP/CHF and Short EUR/GBP. However, the recent volatility in these crosses means that we have placed all three under close watch.

In relation to other tactical positions, the exit from our Long position in US Treasury 10's which we had held for many months was shared via Twitter on 2nd Feb 2015, at a yield of c.1.66%. We are flat at the time of writing but this can change at short notice. Since then, yields for the US Treasury 10's have risen (bond prices fallen since) to 2.25% so our timing was fortuitous. We have used the recent fall in the VIX to reinstate a position and at these entry levels, such a position provides an asymmetrical tactical trade opportunity and also gives us portfolio insurance at good value.

We are retaining our weighting in Real Estate but as the compression in yields is still part of the dynamic, we increasingly look for dislocations in valuations between adjoining areas that may be just a short journey time apart, sites for re-development and locales a little further afield where the money flows have yet to reach and which therefore have not yet been materially touched by the QE-led appreciation.

It remains the case that large cap blue chip equities with a value bias and real estate represent our top (1st equal to be precise) allocations.

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