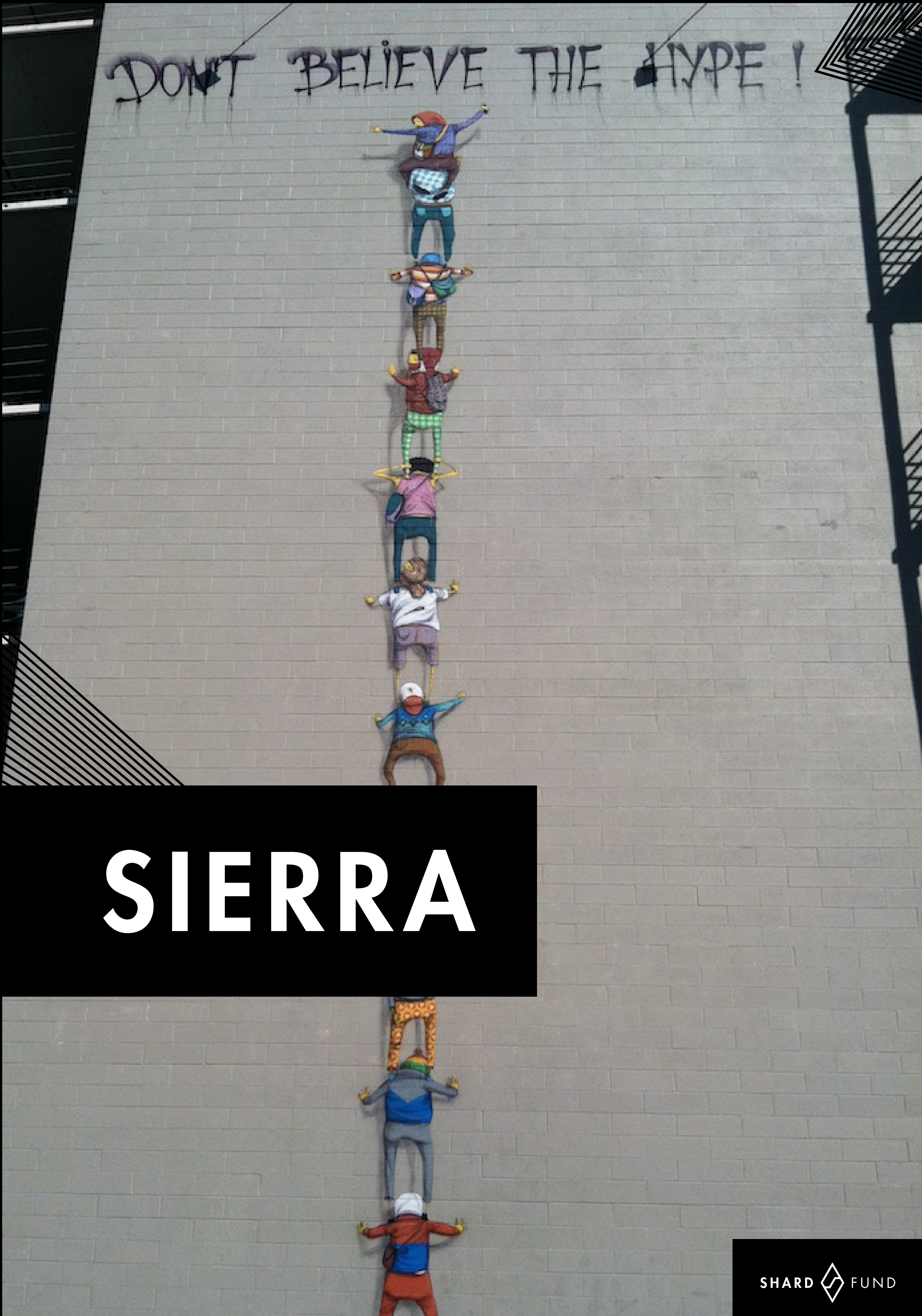

SIERRA

SHARD FUND

A JOURNEY ACROSS FINANCIAL MARKETS

March 1st - March 7th, 2014 | Issue 10

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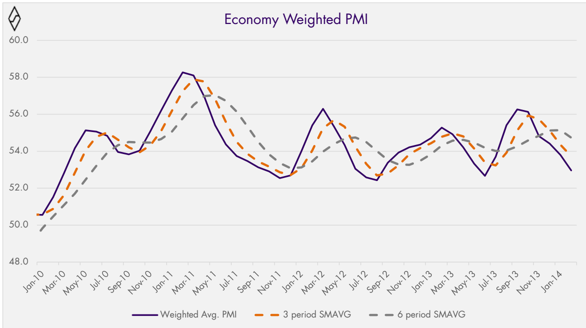
USA

Lost in translation

From the raised tension in Crimea on Monday, to the jobs report on Friday, it has been a genuinely interesting week for the US market. The Bureau of Labour Statistics released the monthly employment report, which looked quite positive and distracted pundits from the weather concerns. Meanwhile the Institute of Supply Management (ISM) presented the industry conditions in its monthly reports. Overall, the market didn't seem ecstatic, given that the S&P grew by about 0.5%, if we neglect the bounce from the Monday slump, attributable to Ukraine, the index grew by a total of 1% during the week. Bonds seemed a bit more responsive, with the 10 year treasury yield climbing 13 bps for the week, to 2.79%. The dollar was trading stronger throughout the week but selling at the end of the week brought it back down to roughly no change for the week.

Financials	3.09%
Industrials	1.81%
Materials	1.51%
Consumer Discretionary	0.82%
Consumer Staples	0.73%
Energy	0.42%
Technology	0.19%
Healthcare	0.02%
Utilities	-1.14%

Firstly, let's start with the industry reports by the ISM. Generally, both reports (manufacturing and services) were mediocre and did not give us any reason to cheer. We continue to see a strong downward trend in the moving averages of the two separate PMIs, as well as the weighted average one. This trend started in the beginning of Q4 2013, which makes the slower GDP growth in that particular quarter not so surprising. An especially bad leading indicator (for at least 1 month) is the low levels of new orders in both reports.



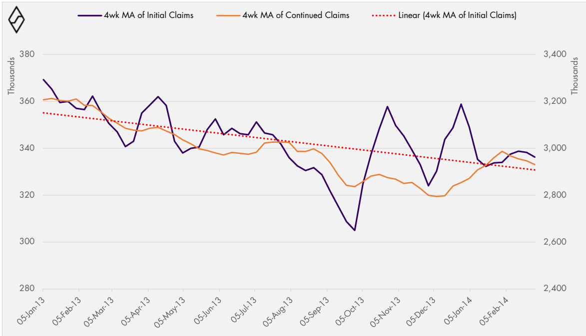
Source: Institute of Supply Management

We continue to see a strong downward trend in the moving averages of the two separate PMIs, as well as the weighted average one.

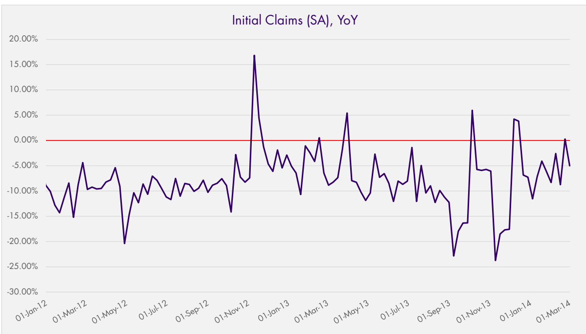
January's drop (largest in more than 30 years) in manufacturing new orders has clearly weighed on production in February, which went into 'contracting' territory to 48.2. On the other hand, employment in services also went negative (47.5) in February for the first time since July 2012, despite the upbeat nonfarm payrolls report later in the week. The only thing rising is prices, which is normal, considering that commodities are the largest gainers year-to-date. The commerce department also supported that thesis with its report on consumption in January. According to this, real personal consumption grew by 0.3%, however spending on goods (durable and non-durable) was negative. Most of the spending supported higher energy bills, which are understandable, just look at the price of natural gas.

The employment report on Friday came as a real surprise and a very positive sign to all market participants occupied by the bad weather. The economy added 175,000 jobs as the unemployment rate inched up to 6.7% due to increase in the labour force. The report looks quite good if we compare it to the low expectations and January's report, but it comes nowhere close to an average report from last year. As for the weather influence, the amount of people that didn't go to work due to bad weather in January is actually well below the 10 year average for that month of the year. On the other hand, the same number for February is above the average, so it could be concluded (with big margin of error) that there was a weather impact, which might have disturbed the economy in February. However, from that particular angle, January looks undisturbed and all the bad data is just a continuation of the weak final quarter of 2013. This is not a good sign for 2014, given the 3% target for economic growth that many people are expecting.

Another reason not to be cheerful about the employment gains comes from the analysis of weekly initial claims, which are a significantly better leading indicator. 2013 was a strong year for jobs, as the economy added an average of 200,000 payrolls per month. This could be extrapolated from the steep slope of the 4 week moving average of initial and continuing claims during 2013. It is also easy to observe in the accelerating decrease in initial claims from the previous year. However, all of that has changed now. Continuing claims have been rising since December, while the rate of change (YoY) in initial claims has decelerated significantly. If this trend continues, we don't see any reason to expect a strong employment improvement in the intermediate term. Maybe the bad weather will continue all year and save us from the truth. Then again, maybe not...



Source: Department of Labour



Source: Department of Labour

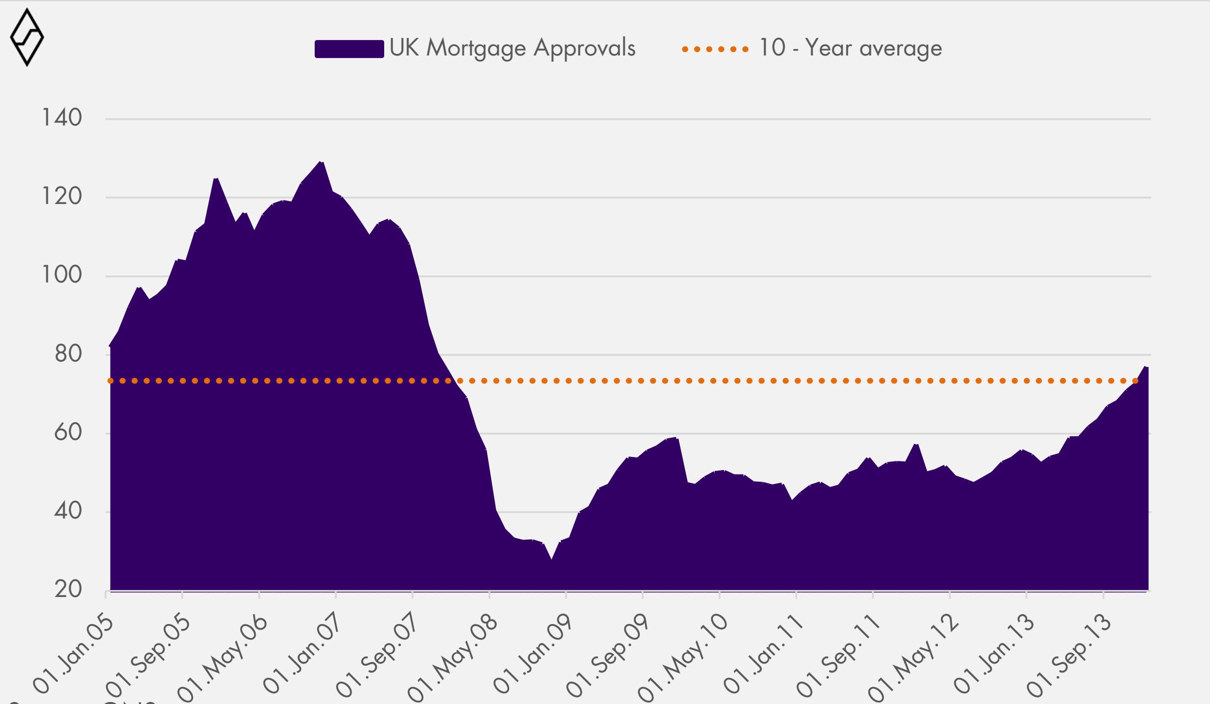
Day	Country	Indicator	Actual	Forecast	Previous
Monday	United States	ISM Manufacturing Index	53.2	52.0	51.3
		Real Personal Consumption (MoM)	0.3%		0.1%
		Personal Spending (MoM)	0.4%	0.1%	0.1%
Wednesday		ISM Non-Manufacturing Index	51.6	53.5	54.0
Thursday		Initial Jobless Claims	323K	338K	349K
		Continuing Jobless Claims	2,907K	2,973K	2,915K
Friday		Nonfarm Payrolls	175K	149K	129K
		Unemployment rate	6.7%	6.6%	6.6%

EUROPE

On the edge 2.0

Looking at the last week's performance of the European stock market, it was an absolute massacre. As you may guess, the source of the panic was coming from the hottest spot in the world, where the real life massacre is taking place – Ukraine. Thus the FTSE 100 decreased by 1.42%, the CAC 40 went down by 0.95 %. Germany's DAX index, considered the most vulnerable to tensions in Ukraine and Russia, fell 3.52%. Investors have piled into the options market for protection against any future fall in the DAX, with Eurex data showing a rise in the ratio between "put" and "call" options. Puts are a bet on a fall in the DAX; calls a bet on a rise. The put/call ratio on DAX options due to mature in March jumped to 3.13 at the start of March from 1.47 in early February. However, mid-week the situation was calmed down by the Diplomatic efforts to cool the

We are keeping our positive outlook for the Continent in the middle/ long run, but for now hedging our portfolios is required.



Source: ONS

crisis in Ukraine. Then tensions rose again, with U.S. President Barack Obama ordering visa bans and asset freezes for unidentified but presumably Russian people who were deemed responsible for threatening Ukraine's sovereignty. So, we are keeping our positive outlook for the Continent in the middle/ long run, but for now hedging our portfolios is required.

In terms of macro figures, the U.K. mortgage approvals rose more than forecast in January to the highest level in more than six years. Business loans in UK fell 623 million pounds ($1 billion), down 3.9% from a year earlier. At the same time the U.K house-price growth accelerated in February to the fastest in seven years. Prices in England and Wales rose 0.7% from the previous month, the most since April 2007. Looking at the big picture, the housing bubble concerns are starting to be discussed again, fueling the panic "mode" at the investors exposed to that particular sector of the UK economy. Of course, that may be perceived as opening short opportunities – for instance Workspace Group PLC.

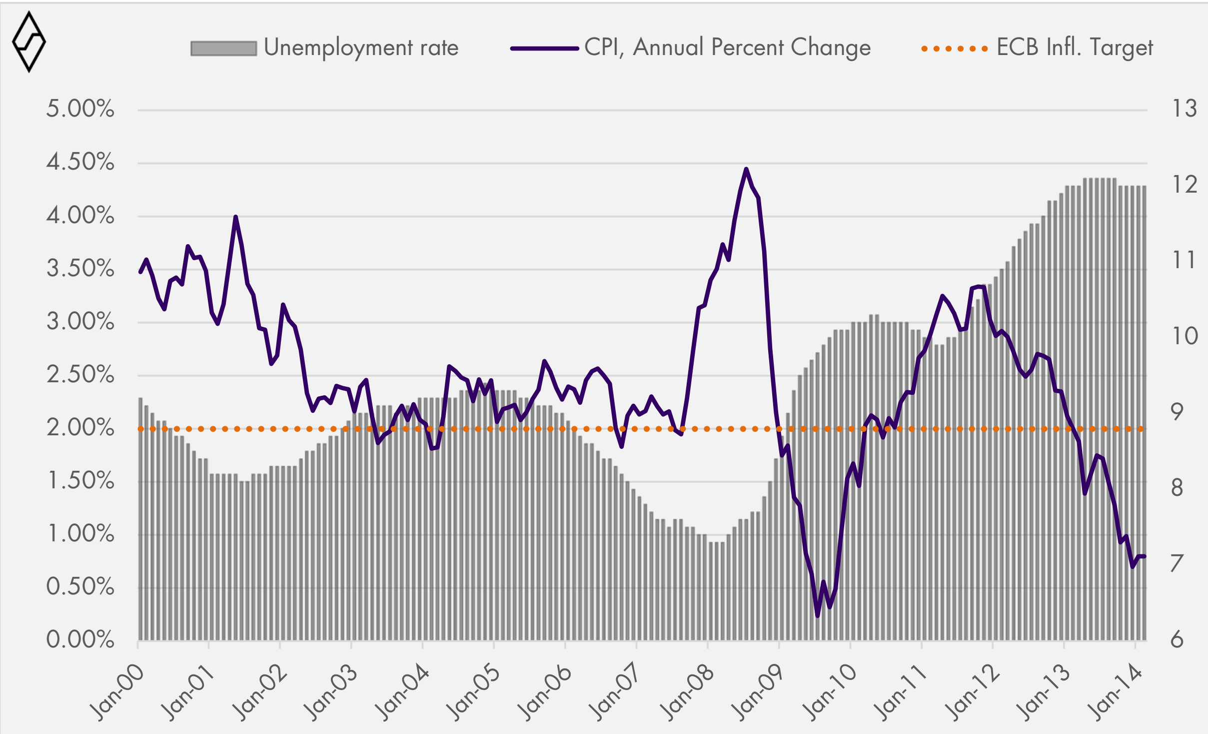
WATCH OUT

On Thursday's ECB press conference, its President, Mario Draghi, emphasized that there is sure slack in the economy. We are still of the opinion that the inflationary pressures may eventually force the Governing Council to ease monetary policy again.

"If I have to flag to you a key point of the discussion (it) is the attention that the presence of slack in the economy received... we mean low capacity utilization rates — output gap — which is indeed hard to measure but according to any measure you want to take it's fairly wide and according to any estimate at the present juncture it's estimated to close itself very slowly.", said Mario Draghi.

The output gap has led the Governing Council to maintain its easing bias. He added:

"Our monetary policy stance — interest rates will stay at the present level or lower — will continue even though we will be seeing



Source: Thomson Reuters

improvements in the economy because of the existing slack... I think this was really the point of major consensus if not unanimity."

One indicator of the size of that gap is the level of unemployment. The jobless rate remained at 12 % in January, just a tick below the record-high reading of 12.1 %. Thus, together with the low inflation, this is putting some downward pressure on the Continent's economy.

Having said this, inflation appears likely to continue its downtrend as long as the output gap remains wide (look at the previous issue of Sierra). This is a problem which should be solved. Hence the Governing Council might be forced to provide additional stimulus.

Day	Country	Indicator	Actual	Forecast	Previous
Monday	EU	Final Manufacturing PMI	53.2	53.2	53.0
	United Kingdom	Mortgage Approvals	77K	74K	73K
		Manufacturing PMI	56.9	56.9	56.6
Tuesday	Spain	Unemployment Change	-1.9K	74.2K	113.1K
Wednesday	EU	Revised GDP q/q	0.3%	0.3%	0.3%
Thursday	EU	Official Bank Rate	0.5%	0.5%	0.5%

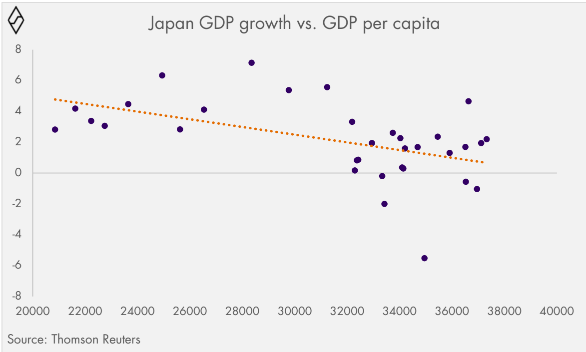
ASIA & OCEANIA

Underweighing focus on Chinese growth

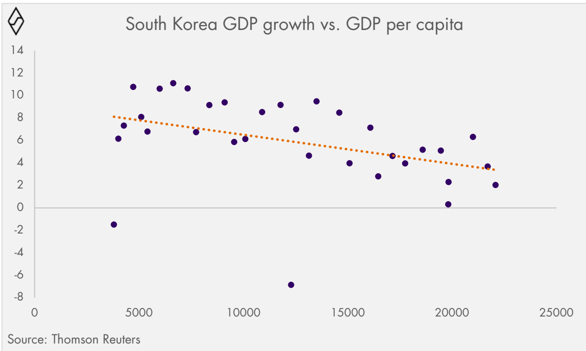
CHINA

This week we will take a more philosophical view on China. As noted previously in the US section, 2013 was a year of low expectations in the states. This, combined with positive economic data, yielded a strong stock market (pricing the new expectations). Looking at China, everyone is talking about how low the growth is. At the Cass Investment Conference, an interesting point was made by Sir Thomas Harris, Vice-Chairman of Standard Chartered. He noted that people have forgotten how Japan and South Korea also went through strong growth years and low per capita GDP. The natural consequences are a decrease in GDP growth along with an increase of GDP per capita. At ShardFund we tested his remarks in order to see where China is currently standing at, below we can see the results.

Japan and South Korea clearly show a downward sloping trend indicating that GDP per capita is increasing when GDP growth has come down from its peak levels. For China, there is still currently no such trend. By extrapolating we can conclude that further slowdown in growth along with an increase in GDP per capita can indeed be expected. Of course, such bold extrapolation for China (which is hard to compare with history) comes with some degree of risk, however it seems wrong to talk about below trend growth in China and for an unsustainable slowdown in growth, when the trend cannot be extrapolated from the current growth rate of China.



Source: Thomas Reuters



Source: Thomson Reuters

Source: Thomson Reuters

Looking at this week, it was a PMI week for China. Manufacturing fell to an 8-month low with key notes from the **source** as:

- Both output and new orders decline for the first time since July 2013
- Payroll numbers are cut at fastest rate since March 2009
- Solid reduction of output charges

From the Services side, things are looking a bit better. The key notes from the **source** are:

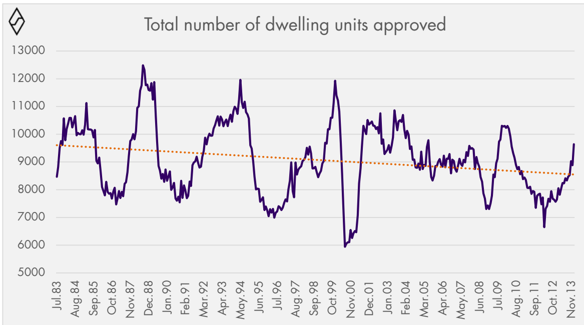
- Business activity and new orders both increase at service providers, but decline at manufacturers
- Employment levels cut at manufacturing firms, while payroll growth eases at service providers
- Outstanding business fell across both the manufacturing and service sectors

To conclude, most investors seem to be focused on the decline in China instead of focusing on how well the shift from export to consumer driven economy is going. This currently somewhat negative sentiment for China can be extremely good for the stock market, once the economy indicates more stable and positive numbers. The surprise could lead to investors re-prising the capital markets, as with the US.

AUSTRALIA

This past week, Governor of RBA – Glenn Stevens, made its **opening statement** to the House of Representatives Standing Committee on economics (last meeting was prior to Christmas 2013). We read those statements and pay strong attention to them, not to gain trading ideas, but to better understand the targets and sentiment of those responsible for Australia's monetary policy.

Our overall understanding is that the expectations are still for a below trend GDP growth, due to the anticipation of non-mining investment to come into play (something that has been noted on almost every RBA statement in the past year). Also, the inflation is viewed to be on point with the medium term target, therefore it's likely that the RBA will keep its rate unchanged for a while longer because "accommodative monetary policy is playing its part in supporting sustainable growth in demand, consistent with the inflation target." Which lead us to think that the housing sector has more to advance. In the statement, Mr Stevens notes that "Over the past three months, approvals to build private dwellings numbered almost 50,000. That is an increase of about 27 per cent from the figures of a year earlier, and is the highest three-month total in the 30-year history of this series."



Source: Australian Beureau of Statistics

Day	Country	Indicator	Actual	Forecast	Previous
Saturday	China	Manufacturing PMI	50.2	50.2	50.5
Monday	China	Non-Manufacturing PMI	55.0		53.4
		HSBC Final Manufacturing PMI	48.5	48.5	48.3
Tuesday	Australia	Building Approvals m/m	6.80%	0.70%	-1.30%
		Current Account	-10.1B	-10.1B	-12.5B
Wednesday	Australia	GDP q/q	0.8%	0.7%	0.6%
Thursday	Australia	Retail Sales m/m	1.20%	0.50%	0.70%
	Australia	Trade Balance	1.43B	0.11B	0.59B

COMMODITIES

The rise of Nickel

METALS

Physical prices of aluminium within Europe are likely to stay high as financing deals squeeze the availability of metals on the spot market. But what do these finance deals involve? Simply put, these financing deals involve a three step process: An investor borrows money at low rates to buy physical aluminium, get a cheap storage deal with a warehouse and then take advantage of the markets contango structure to sell it forward immediately at a profit. Furthermore, European aluminium premiums are at record highs. This further highlights the London Metal Exchange's (LMEs) limited ability to affect a market where low interest rates lock up aluminium as an investment.

Nickel held near nine month highs in the week just gone, making it the longest rally since October 2010. The steady price increase is largely due to worries that the ban on ore exports imposed by Indonesia will soon start tightening global supplies, particularly as Chinese stockpiles get depleted. The short term consequences are that there will be no supplier able to replace Indonesia, as a result, Chinese stainless steel producers would be forced to import refined nickel, boosting their costs. The only viable source of nickel that would likely meet Chinese demand is the Philippines, however the lower quality of ore would likely push up prices for producers, leaving Chinese stainless steel producers in a catch 22.

Physical prices of aluminium within Europe are likely to stay high as financing deals squeeze the availability of metals on the spot market.

ENERGY

Big oil companies gathered at the IHS CERA week conference to discuss issues of importance, one of which was cost inflation. Over the past decade oil companies have faced a doubling of labour and equipment prices, with the price of offshore equipment climbing by fivefold, putting a dent in their profits. This is despite an increase of over 120% in global drilling and exploration over the past decade. Cutting costs is likely to further dent

Cutting costs is likely to further dent profit as this pricing isn't from over-generous pricing but from shortages of skilled labour, equipment and high prices for raw materials.

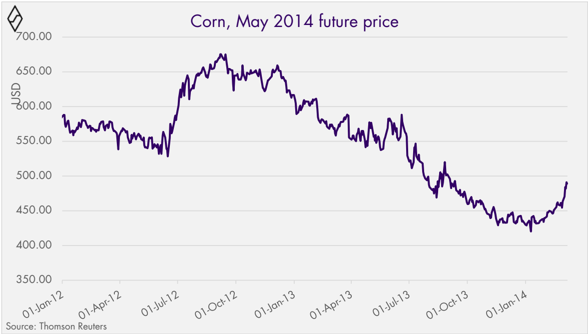
profit as this pricing isn't from over-generous pricing but from shortages of skilled labour, equipment and high prices for raw materials. In short, experience is now expensive and suppliers to big oil companies aren't in any position to change that, nor can the industry do much about steel prices increasing. Again cutting back on investment may initially seem tempting, but this may exacerbate another problem facing some of the biggest energy companies: stagnant output. For example over the past five years Exxon Mobile has managed to increase production by only 1% despite capital spending surging to 56%.

Iraq set March prices of Basra light crude for Asia at a discount of 60 cents to the average of Oman/Dubai quotes versus a discount of 30 cents for the previous month, indicating OPEC members are aiming to court Asian buyers like China with attractive price offers in an attempt to expand market share.

AGRICULTURE

Corn, wheat and soybeans all rose in the week just gone, largely due to uncertainty about the Russia Ukraine crises. Corn in the United States rose to 6 month highs as strong demand for US supply underpinned the market.

Things may be starting to look up for Brazil (at least from a commodities standpoint), as rains alleviated some of the stress on coffee, sugar and orange crops that had been occurring due to the prolonged draught in January and February. But the moisture from the rain isn't going to be sufficient to reverse the damage that has already been done.



FOREX

Pair	Open	Close	Weekly %	Monthly %	YTD
EUR/USD	1.3799	1.3872	0.53%	0.53%	0.92%
USD/JPY	101.75	103.26	1.48%	1.48%	-1.94%
USD/CHF	0.8793	0.8775	-0.20%	-0.20%	-1.71%
USD/CAD	1.1061	1.1084	0.21%	0.21%	4.37%
AUD/USD	0.8923	0.9064	1.58%	1.58%	1.69%
NZD/USD	0.8378	0.8459	0.97%	0.97%	3.08%
USD/CNY	6.145	6.126	-0.31%	-0.31%	-1.49%
GBP/USD	1.6737	1.6715	-0.13%	-0.13%	0.96%

PORTFOLIOS

MAVERICK

security	L/S	date
Tracker Fund of Hong Kong	Long	03.Sep.13
Corning Inc.	Short	23.Oct.13
CNY/USD	Long	04.Nov.13
ProShares UltraShort Lehman 20+ Yr(ETF)	Long	04.Nov.13

security	L/S	date
iShares MSCI Emerging Markets	Short	24.Jan.14
DBIQ Optimum Yield Diversified CI	Long	03.Feb.14
Wisdom Tree Europe Hedged Equite (ETF)	Long	10.Feb.14
iShares UK Gilts UCITS (ETF)	Long	10.Feb.14

CORTEZ

security	L/S	date
Pandora A/S	Long	03.Sep.13
Valeo SA	Long	03.Sep.13
Aspen Technology Inc	Long	03.Sep.13
USD/JPY	Long	07.Oct.13
Aeropostale Inc	Long	15.Oct.13
OZ Minerals	Long	15.Oct.13
Easyjet plc	Long	20.Oct.13
Chico FAS	Long	15.Oct.13

security	L/S	date
Claymore/AlphaShares China Real Est ETF	Short	04.Nov.13
Claymore/AlphaShares China Real Est ETF	Short	17.Dec.13
Royal Caribbean Cruises Ltd.	Long	13.Jan.14
Carnival Corp	Long	13.Jan.14
SPDR S&P Emerging Latin America	Short	24.Jan.14
Claymore/AlphaShares China Real Est ETF	Short	03.Feb.14
WisdomTree Europe	Long	10.Feb.14
Global IPO Plus Aftermarket (IPOSX)	Long	10.Feb.14

EVENTS

USA

- Retail sales
- CPI, PPI
- Consumer Sentiment

EUROPE

- UK: Manufacturing Production
- UK: Inflation Report Hearings
- EU: Employment Change

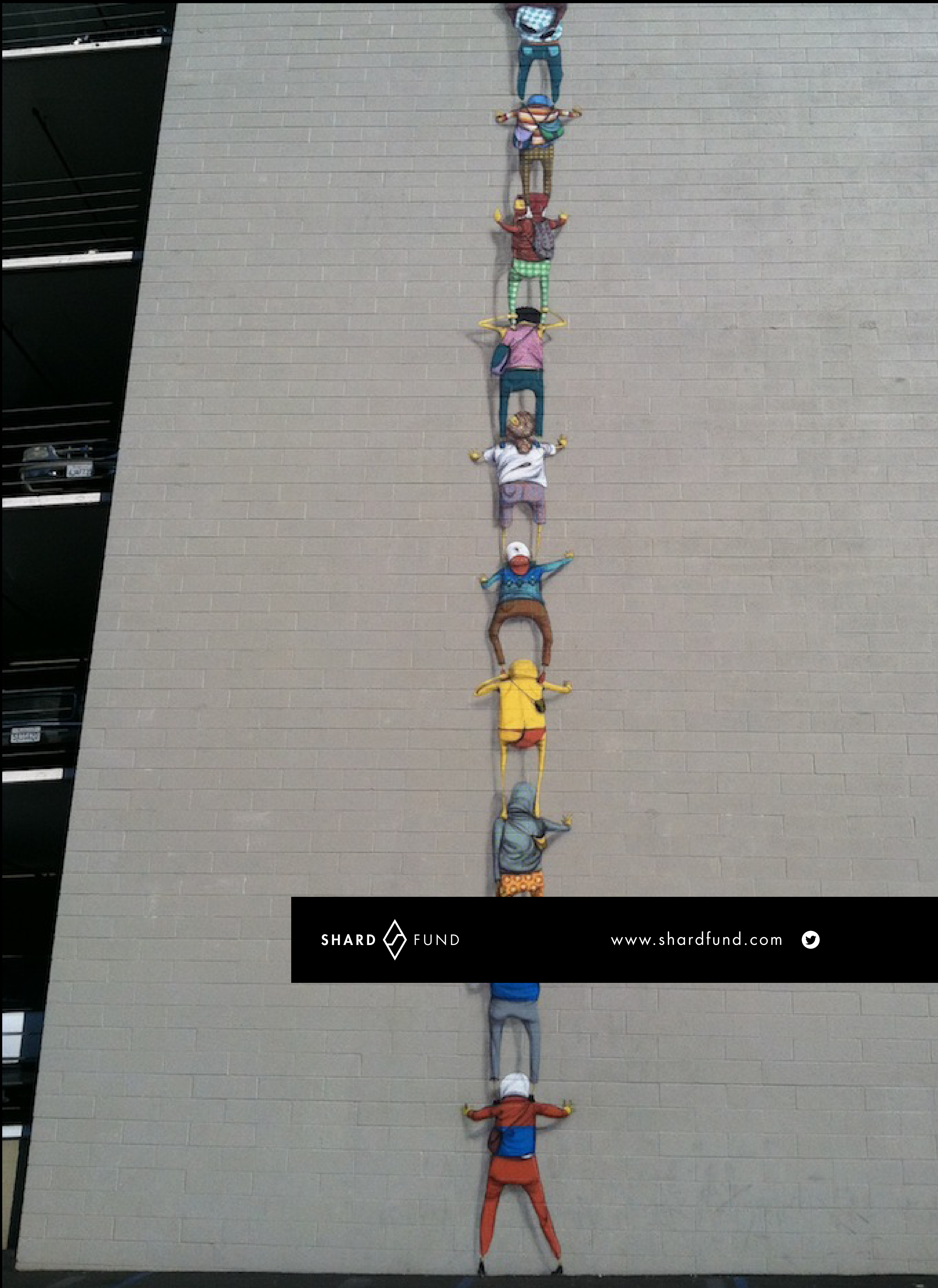
ASIA & OCEANIA

- China: Trade Balance
- China: CPI
- China: Industrial Production
- Australia: NAB Business Confidence
- Australia: Employment Change
- Japan: Final GDP

REFERENCES

Reserve Bank of Australia, Bank of Japan, Bloomberg, Thomson Reuters, Markit ,Eurostat, ECB, Bloomberg, Reuters, Berenberg, ONS, http://bit.ly/1pON4dj

DISCLAIMER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