SIERRA

SHARD FUND

A JOURNEY ACROSS FINANCIAL MARKETS

September 5th - September 12th, 2014 | Issue 26

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HIGHLIGHTS

USA

In the build up to the much-anticipated FOMC meeting next week we look at some of the most important points, raised (or not) in recent weeks, related to the meeting. Firstly, we have some educational entertainment with Mr. Krugman's recent endeavours. This is to illustrate the kind of philosophy accepted by most of the FOMC members. This then transforms into a discussion of what to consider before the FOMC meeting and what to expect from it. Go Janet, go!

EUROPE

Bank bailouts and country bailouts (also funded through the IMF) don't appear to have returned countries to growth, however it looks like officials do not want to learn and EU will try once again. The true size of the European QE will be announced on 2 October but Mario Draghi has stated that ““the aim is to steer the size of the balance sheet of the ECB towards where it was in 2012.” Considering the size of ECB's balance sheet peaked in June 2012 at 3.1 trillion euros and is currently at 2.04 trillion euros, the ECB might buy up to (or more than) 1 trillion euros of assets.

ASIA & OCEANIA

Britain announced that it is going to issue a Renminbi denominated bond, in order to finance its currency reserves in RMB. This is the first instance of a country outside of China to issue a bond denominated in RMB, which suggests a paradigm shift in global economics. The west is now open to collaboration and even George Osborne said the RMB may become the “the main global reserves currency”.

COMMODITIES

The coffee markets were quite volatile in August. The ICO composite indicator dropped 10 cents before reversing and jumping up another 12 cents to end the month. This volatility is most likely due to speculation over the Brazilian crop and funds, given the lack of fundamentals to act as a price driver. Brazilian Naturals jumped the highest, over 11%, reflecting mounting concerns over supply.

Weekly Change	
Indices	
Nikkei 225 (Japan)	1.78%
Shanghai (China)	0.21%
BSE (India)	0.13%
FTSE 100 (UK)	-0.70%
DAX (Germany)	-0.98%
CAC (France)	-1.00%
S&P 500 (USA)	-1.10%
S&P/ASX (Australia)	-1.21%
FTSE MIB (Italy)	-1.51%
IBEX (Spain)	-2.33%
Hang Seng	-2.55%
Currencies	
EUR/AUD	3.86%
GBP/AUD	3.38%
EUR/JPY	2.27%
USD/JPY	2.14%
USD/CAD	1.95%
GBP/JPY	1.78%
EUR/GBP	0.44%
EUR/CHF	0.32%
USD/CHF	0.24%
EUR/USD	0.10%
USD/CNY	-0.11%
GBP/USD	-0.35%
BTC/USD	-1.54%
AUD/NZD	-1.55%
NZD/USD	-2.11%
AUD/USD	-3.62%
Commodities	
WTI Crude Oil	-1.20%
Copper	-2.05%
Silver	-2.99%
Gold	-3.08%
Brent Crude Oil	-3.77%

Source: Thomson Reuters

CALENDAR

USA					
Day	Country	Indicator	Actual	Forecast	Previous
Thursday	United States	Federal Budget Balance	-129.0B	-105.5B	-95.0B
Friday		Core Retail Sales (MoM)	0.3%	0.3%	0.3%
		Retail Sales (MoM)	0.6%	0.6%	0.6%
		Michigan Consumer Sentiment	84.6	81.5	82.5
		Upcoming events		Forecast	Previous
Tuesday	United States	Core CPI (MoM)		0.1%	0.2%
Thursday		Building Permits		1.045M	1.057M
		Housing Starts (MoM)		-4.4%	15.7%
		Philadelphia Fed Manufacturing Index		23.0	28.0
EU					
Day	Country	Indicator	Actual	Forecast	Previous
Monday	Germany	German Trade Balance	22.2B	16.8B	16.2B
Tuesday	United Kingdom	Manufacturing Production (MoM)	0.5%	0.3%	0.3%
		Trade Balance	-10.19B	-9.10B	-9.41B
Thursday	Germany	CPI (MoM)	0.0%	0.0%	0.0%
	France	CPI (MoM)	0.5%	0.4%	-0.3%
Friday	EU	Industrial Production (MoM)	1.0%	0.3%	-0.3%
		Upcoming events		Forecast	Previous
Tuesday	Germany	German ZEW Economic Sentiment		4.8	8.6
	United Kingdom	CPI (YoY)		1.5%	1.6%
Wednesday	United Kingdom	Claimant Count Change		-30.0K	-33.6K
		Unemployment Rate		6.3%	6.4%
	EU	CPI (YoY)		0.3%	0.3%
Thursday	United Kingdom	Retail Sales (MoM)		0.3%	0.5%
Friday	Germany	PPI (MoM)		-0.1%	0.1%
Asia and Oceania					
Day	Country	Indicator	Actual	Forecast	Previous
Sunday	China	Exports (YoY)	9.4%	8.0%	14.5%
		Imports (YoY)	-2.4%	1.7%	-1.6%
		Trade Balance	49.83B	40.00B	47.30B
	Japan	GDP (QoQ)	-1.8%	-1.8%	-1.7%
Wednesday	New Zealand	Interest Rate Decision	3.5%	3.5%	3.5%
	Australia	Employment Change	121.0K	12.0K	-0.3K
	China	CPI (MoM)	0.2%	0.4%	0.1%
		CPI (YoY)	2.0%	2.2%	2.3%
		PPI (YoY)	-1.2%	-1.2%	-0.9%
Friday	Japan	Industrial Production (MoM)	0.4%	0.2%	0.2%
	India	CPI (YoY)	7.8%	7.8%	7.96%
Saturday	China	Industrial Production (YoY)	6.9%	8.8%	9.0%
		Upcoming events		Forecast	Previous
Wednesday	New Zealand	GDP (QoQ)		0.6%	1.0%
	Japan	Adjusted Trade Balance		-0.99T	-1.02T
		Exports (YoY)		-2.6%	3.9%
		Trade Balance		-1.209B	-964B

Source: Investing.com

USA

"You can argue, and I would, that the Fed should have done even more. " – Paul Krugman, NYT

Sectors	5D	1M	3M	YTD
Healthcare	-0.56%	5.56%	6.92%	15.10%
Technology	-0.17%	3.55%	6.09%	12.53%
Utilities	-3.12%	2.42%	-0.05%	11.30%
Materials	-1.80%	0.90%	1.61%	7.64%
Financials	-0.30%	4.19%	3.50%	7.00%
Energy	-3.63%	-2.44%	-4.03%	5.71%
Consumer Staples	-1.16%	2.04%	0.74%	4.82%
Industrials	-0.63%	3.31%	-0.59%	3.31%
Consumer Discretionary	-1.31%	2.80%	3.94%	2.27%
Indices				
Nasdaq	-0.33%	3.01%	5.96%	9.36%
S&P 500	-1.10%	2.68%	2.87%	7.42%
Dow Jones Ind. Avg.	-0.87%	2.02%	1.26%	2.48%
Russell 2000	-0.81%	1.65%	-0.18%	-0.26%

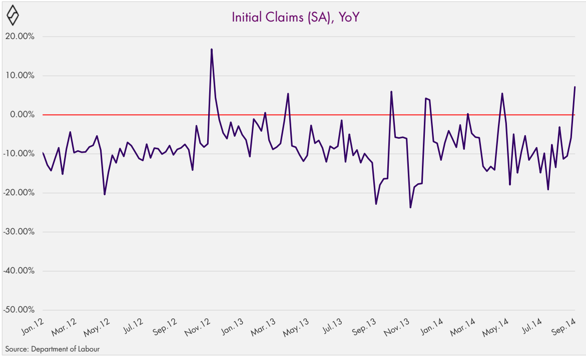
Source: Sectorspdr.com

In the build up to the much-anticipated FOMC meeting next week we look at some of the most important points, raised (or not) in recent weeks, related to the meeting. In a similar fashion like last week, we start by challenging a recent quote by a well-known and (allegedly) a top-tier economist — Paul Krugman.

Market participants have got used to "drowning" in fresh cash in the sign of a weakness.

He has a famous column in the New York Times, where he shares his views about world economics and markets. The quote comes from a post (**link**), which is part of rather bizarre trend in Mr. Krugman's recent publications (in NYT), focused predominantly on accusing 'sound money' economists and pundits of being wrong that QE (i.e. printing money) will cause severe inflation and won't produce growth. Without getting into this decades' long fight, it was kind of shocking for us (not really) too see how much attention Mr. Krugman has paid to the US and EU to build his argument, while carefully neglecting Japan in recent weeks. Why Japan? — you might say. Well, Mr. Krugman has been a strong voice in Japan's development since the 90s, when he proposed an unconventional monetary policy (QE) for the first time, to escape the supposedly dangerous liquidity trap (**source**). So, due to the lack of comments from his side on the recently "terrific" performance of Japan, we decided to use his own words, from slightly more than a year ago, and include the recent data. Have in mind that since that comment (**May, 2013**) there have not been any fundamental shift in policies in Japan, so Mr. Krugman's words are still valid:
"The good news starts with surprisingly rapid

(-7.1% YoY) Japanese economic slump in the second quarter of this year — actually, substantially slower than the US, while even Europe's economy is doing better. You never want to make too much of one quarter's numbers, so having a negative first half GDP is definitely the kind of thing we want to see.
Meanwhile, Japanese stocks have soared, while the yen has fallen. And, in case you're wondering, a weak yen is very good news for Japan because it makes the country's export industries more competitive. That is not just a fallacy coming from economics textbooks, it is actually supported (not really) by the slowing rate of change (YoY) in Japanese exports, which actually recorded negative growth in June and July (2014).
So the overall verdict on Japan's effort to turn its economy around is so far, so good. And let's hope that this verdict both stands and strengthens over time. After all, how much more could household spending (YoY) decline? It's been slowing since last year and it's been negative only for the past four months, which is typically normal, when inflation soars from negative to 3.4% in one year."
We thank Mr. Krugman for this thoughtful commentary and we hope he does not spare us his future views on Japan. As for how this rather long introduction is related to the US — it describes perfectly the type of thinking that has invaded the Federal Reserve at the moment. Why do you think that every sign of weakness drives the market up and bond yields down? Market participants have got used to "drowning" in fresh cash in the sign of a weakness. We spoke about potential cyclical weakness in employment last week (**Issue 25**) and initial claims this week reiterated the acceleration of this trend. Don't forget that initial claims are a leading indicator for the payrolls number.



Other important issues to consider before the FOMC meeting (16-17 September):

1. Same time last year there were high expectations the Fed would taper, which did not happen. Currently, expectations are high for a quite hawkish statement.
2. Ever since those expectations started building up, the dollar has soared, bond yields have jumped by almost 30 bps, volatility is creeping back and the market is rather nervous and unstable. The Fed has not tolerated those events so far we put a high probability on Janet trying to calm down the situation.
3. Articles on employment
   - "**Fed ignores likelihood of weaker growth**"
   - "**Work's for Squares**"
4. Articles on long-term trends
   - "**Where Have all the Shoppers Gone?**"
   - "**Economic Forecasters May Have Missed a Fundamental, and Depressing, Shift in the Economy**"

At the end of the day, everything is possible at an FOMC meeting so do not listen to 'experienced' advisors out there and consider the risks on your own. However, from a probabilistic perspective, chances are Janet Yellen will satisfy the market by calming things down and providing assurances.

EUROPE

ECBet 2.0

Indices	5D	1M	3M	YTD
STOXX Europe 600 Health Care	1.30%	9.03%	5.86%	18.25%
STOXX Europe 600 Real Estate Cap	-1.50%	2.85%	-0.66%	15.37%
STOXX Europe 600 Food & Beverage	-1.35%	4.30%	0.72%	7.92%
STOXX Europe 600	-0.95%	4.72%	-1.02%	4.88%
STOXX Europe 600 Personal & Household Goods	0.08%	4.45%	-1.32%	4.69%
STOXX Europe 600 Basic Resources	-2.50%	-4.71%	3.48%	4.69%
STOXX Europe 600 Oil & Gas	-2.61%	1.49%	-5.63%	3.98%
STOXX Europe 600 Travel & Leisure	-1.59%	4.44%	-3.85%	3.89%
STOXX Europe 600 Insurance	-1.04%	5.14%	1.90%	3.79%
STOXX Europe 600 Technology	0.60%	7.17%	4.78%	3.60%
STOXX Europe 600 Banks	-0.95%	7.13%	-2.02%	3.49%
STOXX Europe 600 Construction & Materials	-2.39%	3.42%	-10.12%	2.82%
STOXX Europe 600 Financial Services	-1.57%	3.16%	-4.23%	2.33%
STOXX Europe 600 Chemicals	-0.64%	5.09%	-2.66%	0.85%
STOXX Europe 600 Media	-0.71%	3.81%	0.29%	-0.01%
STOXX Europe 600 Telecommunications	-0.90%	4.02%	-2.73%	-0.21%
STOXX Europe 600 Automobiles & Parts	-2.98%	4.26%	-8.62%	-0.28%
STOXX Europe 600 Industrial Goods & Services	-1.26%	4.18%	-2.94%	-1.62%
STOXX Europe 600 Retail	-0.79%	2.03%	-4.58%	-6.52%

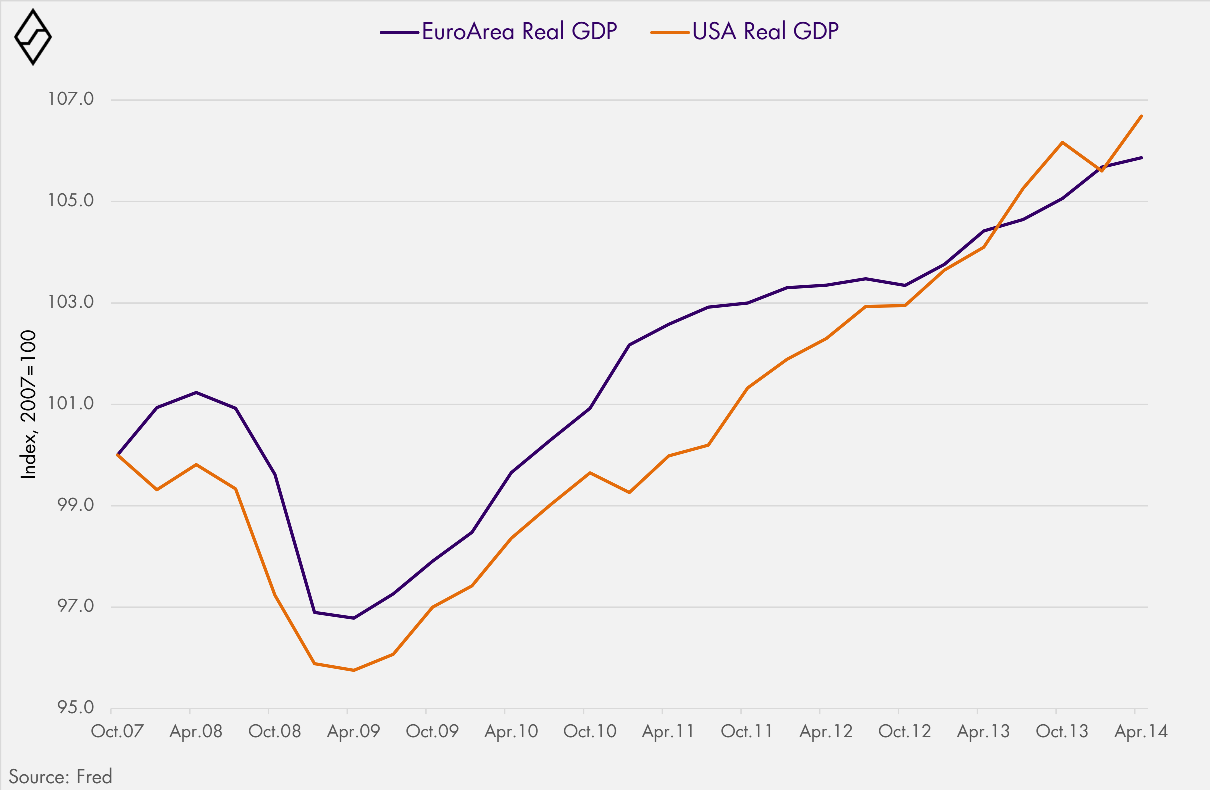
Source: Stoxx; quoted in EUR

After last week's speech of Mr. Draghi, Europe has become the hottest place in the financial world. All of the financial professionals speak about action taken by policy makers, and are wondering what the next move should be in terms of investment decisions (read more on the ECB policy in the previous issue of Sierra). However, in our opinion, the problems in Europe seem to be getting worse and the people in power don't seem to have the solutions at hand for its citizens. Bank bailouts and country bailouts (also funded through the IMF) don't appear to have returned countries to growth. Having said that, GDP figures for Europe are worrying. If when investing we say that the "trend is your friend", then Europe is coming up short. Since 2013, USA's real GDP has started to surpass the GDP of the Euro Area.

That's the situation from the macro side of the coin. On the other side, the so called stimulus might overjoy the bulls in the Continent. We

Bank bailouts and country bailouts (also funded through the IMF) don't appear to have returned countries to growth.

all know how much the stock markets adore fresh blood (money). The rationale follows one thing we know for sure about QE: it boosts asset prices and the stock market in



particular. So, even if the economy still flat-lines, odds are that equities will do well.

Taking the USA as an example, since the trough in late Q1 2009 the S&P has grown by roughly 190%, or 19.4% CAGR (assuming S&P stays flat until rest of 2014) . In short, the monetary expansion made its way into the financial economy instead of the real one. Europe could follow a similar path, at least in the short/mid-term.

Further information would be brought by the size of the expected stimulus. Although the size of the European QE has not been announced -it will be determined on October 2-, there are reasons to believe it will be substantial. The ECB's President, Mario Draghi, stated "the aim is to steer the size of the balance sheet of the ECB towards where it was in 2012." Considering that the size of the ECB's balance reached a peak in June 2012, at 3.1 trillion euros and is currently at 2.04 trillion euros, the ECB might buy up to 1 trillion euros of assets. Why stop there?! Let Mr. Draghi go nuts!

ASIA & OCEANIA

Shift in global economics

Indices	5D	1M	3M	YTD
STOXX Asia/Pacific 600 Technology	-1.17%	2.28%	7.49%	14.66%
STOXX Asia/Pacific 600 Health Care	-1.26%	3.29%	9.13%	11.31%
STOXX Asia/Pacific 600 Construction & Materials	-4.34%	-1.22%	3.99%	10.18%
STOXX Asia/Pacific 600 Oil & Gas	-3.99%	0.12%	0.21%	9.04%
STOXX Asia/Pacific 600 Food & Beverage	-2.40%	-0.82%	5.21%	8.87%
STOXX Asia/Pacific 600 Industrial Goods & Services	-0.79%	3.71%	7.18%	7.69%
STOXX Asia/Pacific 600 Chemicals	-1.55%	3.34%	10.48%	6.69%
STOXX Asia/Pacific 600 Personal & Household Goods	-2.03%	0.90%	3.79%	6.48%
STOXX Asia/Pacific 600 Telecommunications	1.17%	7.47%	7.59%	5.75%
STOXX Asia/Pacific 600 Insurance	-0.84%	5.00%	6.09%	5.71%
STOXX Asia/Pacific 600 Real Estate	-2.61%	2.51%	4.68%	5.63%
STOXX Asia/Pacific 600 Utilities	-1.06%	3.66%	6.68%	5.20%
STOXX Asia/Pacific 600 Index	-1.56%	2.16%	4.77%	4.19%
STOXX Asia/Pacific 600 Banks	-2.29%	2.24%	1.52%	1.53%
STOXX Asia/Pacific 600 Media	-2.22%	-2.69%	0.12%	-0.46%
STOXX Asia/Pacific 600 Automobile & Parts	0.82%	3.79%	5.99%	-0.53%
STOXX Asia/Pacific 600 Financial Services	-1.98%	3.84%	4.69%	-1.32%
STOXX Asia/Pacific 600 Basic Resources	-2.53%	-4.81%	1.85%	-3.59%
STOXX Asia/Pacific 600 Retail	-3.53%	-1.94%	-0.84%	-3.90%

Source: Stoxx; quoted in EUR

CHINA

A week with intense data feed took place in China, with mostly mixed indicators, which nevertheless pushed the stock market up in the Asian economy. On Friday Britain announced that it is going to issue a Renminbi denominated bond, in order to finance its currency reserves in RMB. There are two main points that should be noted here. This is the first instance of a country outside of China to issue a bond denominated in RNB, which suggests a paradigm shift in global economics. The west is now open to collaboration and even George Osborne said the RMB may become the "the main global reserves currency". Secondly, the bond issue suggests that the UK thinks the Chinese economy is strong and less uncertain, which is also reflected in this weeks' data.
The mixed economic data was seen as bullish for the stock market as speculation spurred for an introduction of a stimulus on part of the Chinese authorities. Industrial production and retail sales had slowed down to 6.9% and 11.9% YoY, interestingly on the back of strong exports and decreased imports of 9.4% and -2.4% YoY as follows. The CPI and PPI have ticked down to 2% and -1.2% YoY, which left speculators wanting policy easing, an unlikely event for today.

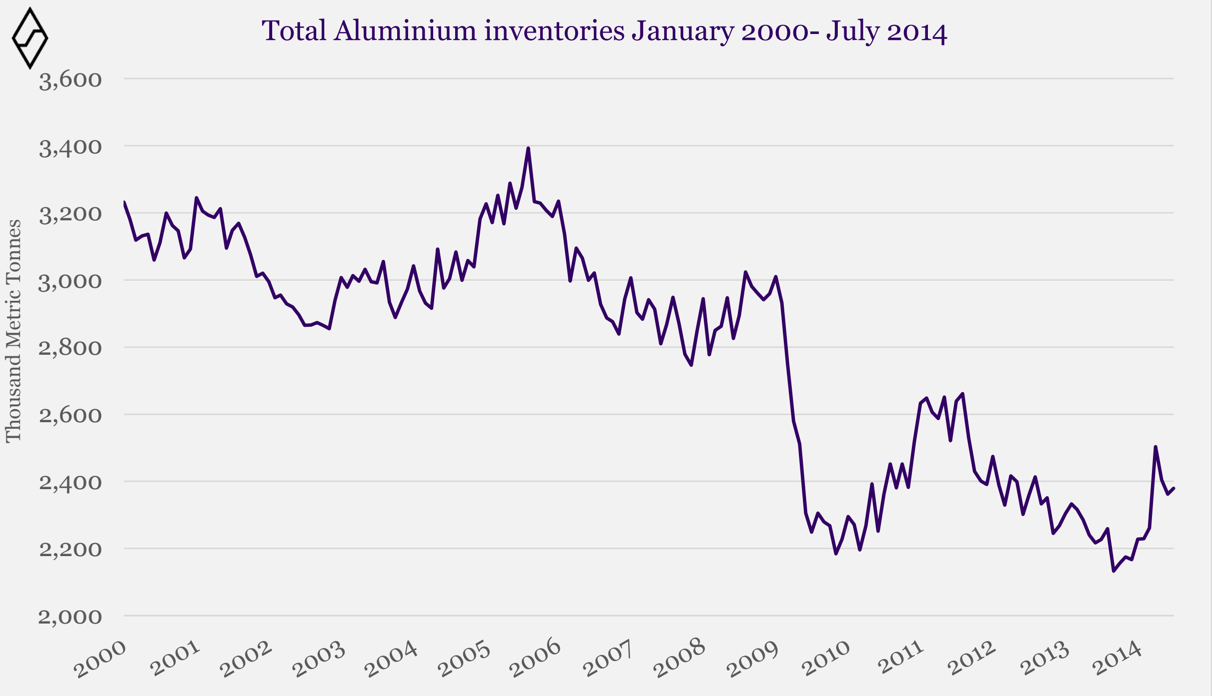
Source: Thomson Reuters

COMMODITIES

One Dollar Differential

METALS

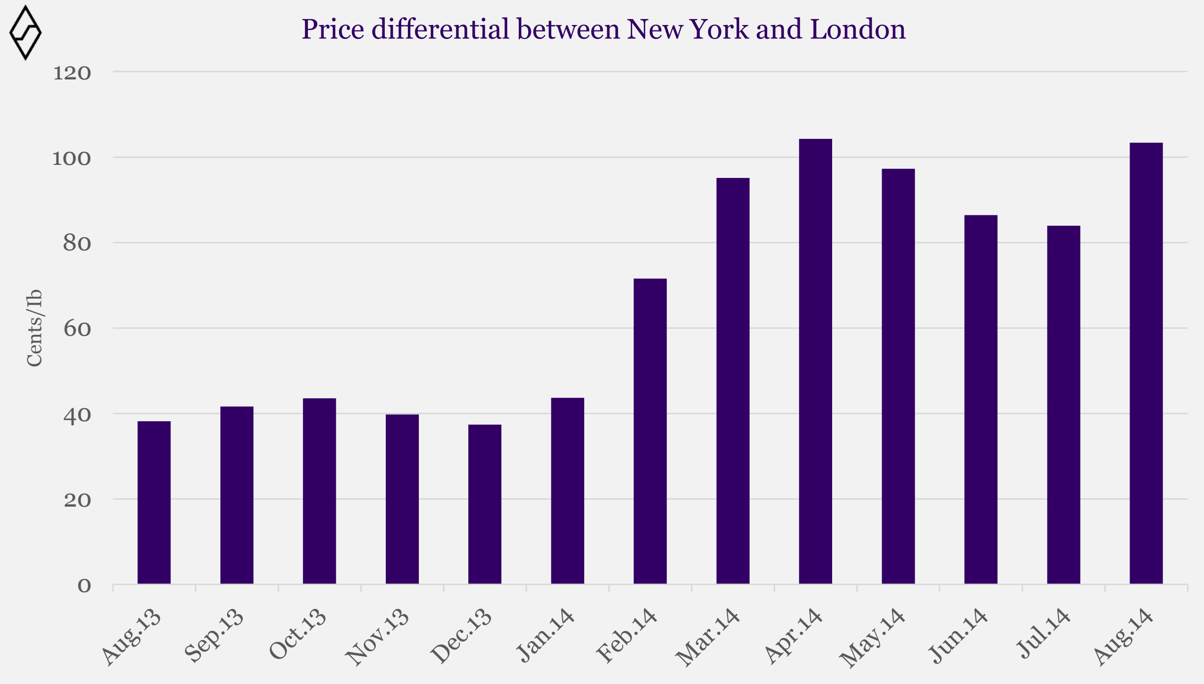
The London Metal Exchange (LME) has pushed back its aluminium premium contract launch to Q2 2015 as oppose to Q1. The premiums are paid over the spot price to cover the cost of freight and insurance, and reflect regional demand and supply. The LME is hoping investors will want to lock in future premiums, which have gone to all-time highs in recent years, the reason largely being due to a backlog of queues at LME warehouses.
Thus in order to be successful, the contract is going to have to account for queues. LME is tackiling this in two ways; firstly they are opting to use a warehouse-opt in mechanism for the contracts, in which warehosue operators agree to create premium warrents. Secondly it could potentially continue with reforms it attempted to make this year to cut the maximum queue length to 50days, but was stopped after Rusal filed a court appeal, the court resumes in October.



Source: IAI

AGRICULTURE

The coffee markets were quite volatile in August. The ICO composite indicator dropped 10 cents before reversing and jumping up another 12 cents to end the month. This volatility is most likely due to speculation over the Brazilian crop and funds, given the lack of fundamentals to act as a price driver. Brazilian Naturals jumped the highest, over 11%, reflecting mounting concerns over supply. Colombian Milds and Other Milds both increased by 9% and 8.2% respectively, whilst Robusta's fell 1.5%, as most of the damage in Brazil is expected to affect the Arabica crop. As a result, the arbitrage between Arabica and Robusta prices has widened, with the daily price differential between New York and London futures exceeding $1.00 for the first time since May. This widening arbitrage could increase consumer interest in Robusta's.



Source: ICO

PORTFOLIO

CORTEZ

				Price		Performance	
Security	Ticker	Entry date	Long/Short	Entry	Current	Weekly	Inception
Legg Mason Inc	LM	21.Jul.14	Long	50.4	50.2	5.2%	2.0%
T.Rowe Price Group	TROW	21.Jul.14	Short	81.4	79.5		
Maxim Integrated Products Inc	MXIM	21.Jul.14	Long	34.2	30.4	-1.3%	-5.7%
Linear Technology Corp	LLTC	21.Jul.14	Short	47.3	44.6		
Lazard Ltd	LAZ	31.Jul.14	Long	53.2	53.9	-2.6%	-2.2%
SPDR KBW Regional Banking ETF	KRE	31.Jul.14	Short	38.6	40.0		
iShares STOXX EU600 Utilities (DE)	EXH9	31.Jul.14	Long	32.4	32.8	-0.5%	1.0%
PowerShares DWA Developed Markets Momentum	PIZ	01.Aug.14	Short	18.8	19.6		
Wisdom Tree India Earnings ETF	EPI	04.Aug.14	Long	22.0	23.0	-2.5%	1.0%
iShares MSCI Italy Spain (ETF)	EWP	11.Aug.14	Long	39.1	40.3	-1.3%	-2.2%
iShares MSCI Italy Index (ETF)	EWI	11.Aug.14	Short	15.3	16.2		
EURGBP	EURGBP	18.Aug.14	Short	0.8	0.8	-0.4%	0.4%
iPath S&P 500 VIX ST Futures ETN	VXX	22.Aug.14	Long	27.8	28.6	4.3%	2.9%
iShares US Home Construction ETF	ITB	08.Sep.14	Short	23.9	23.5	0.9%	1.4%
iShares Russell 2000 ETF	IWM	08.Sep.14	Short	115.9	115.4	0.9%	0.4%
iShares 20+ Year Treasury Bond ETF	TLT	08.Sep.14	Long	116.5	113.4	-2.0%	-2.7%

Source: Thomson Reuters, ShardFund updated: 14.Aug.14 close prices

FOREX

Pair	Open	Close	Weekly %	Trend w/w	Monthly %	YTD
USD/CHF	0.9310	0.9332	0.24%	3	4.27%	4.53%
USD/CAD	1.0881	1.1093	1.95%	2	2.32%	4.45%
EUR/JPY	136.10	139.19	2.27%	1	0.36%	4.15%
AUD/NZD	1.1259	1.1084	-1.55%	1	1.13%	2.11%
USD/JPY	105.09	107.34	2.14%	3	5.54%	1.94%
AUD/USD	0.9377	0.9038	-3.62%	1	-2.88%	1.40%
USD/CNY	6.1405	6.1340	-0.11%	3	-1.51%	1.33%
GBP/JPY	171.56	174.62	1.78%	1	2.48%	0.22%
NZD/USD	0.8328	0.8152	-2.11%	3	-3.88%	-0.66%
EUR/CHF	1.2060	1.2099	0.32%	1	-0.82%	-1.73%
GBP/USD	1.6325	1.6268	-0.35%	2	-2.86%	-1.74%
GBP/AUD	1.7410	1.7999	3.38%	1	0.08%	-2.72%
EUR/GBP	0.7934	0.7969	0.44%	2	-2.03%	-3.94%
EUR/USD	1.2952	1.2965	0.10%	1	-4.88%	-5.67%
EUR/AUD	1.3811	1.4344	3.86%	1	-1.83%	-7.35%
BTC/USD	478.99	471.60	-1.54%	4	-18.36%	-35.44%

Source: Investing.com

DISCLAIMER

Interview: The views expressed in this interview are purely those of the author; they do not pretend to reflect any views that may prevail at Sussex University nor should they be taken as investment advice.


SOMETIMES
I THINK
SOMETIMES
I DON'T