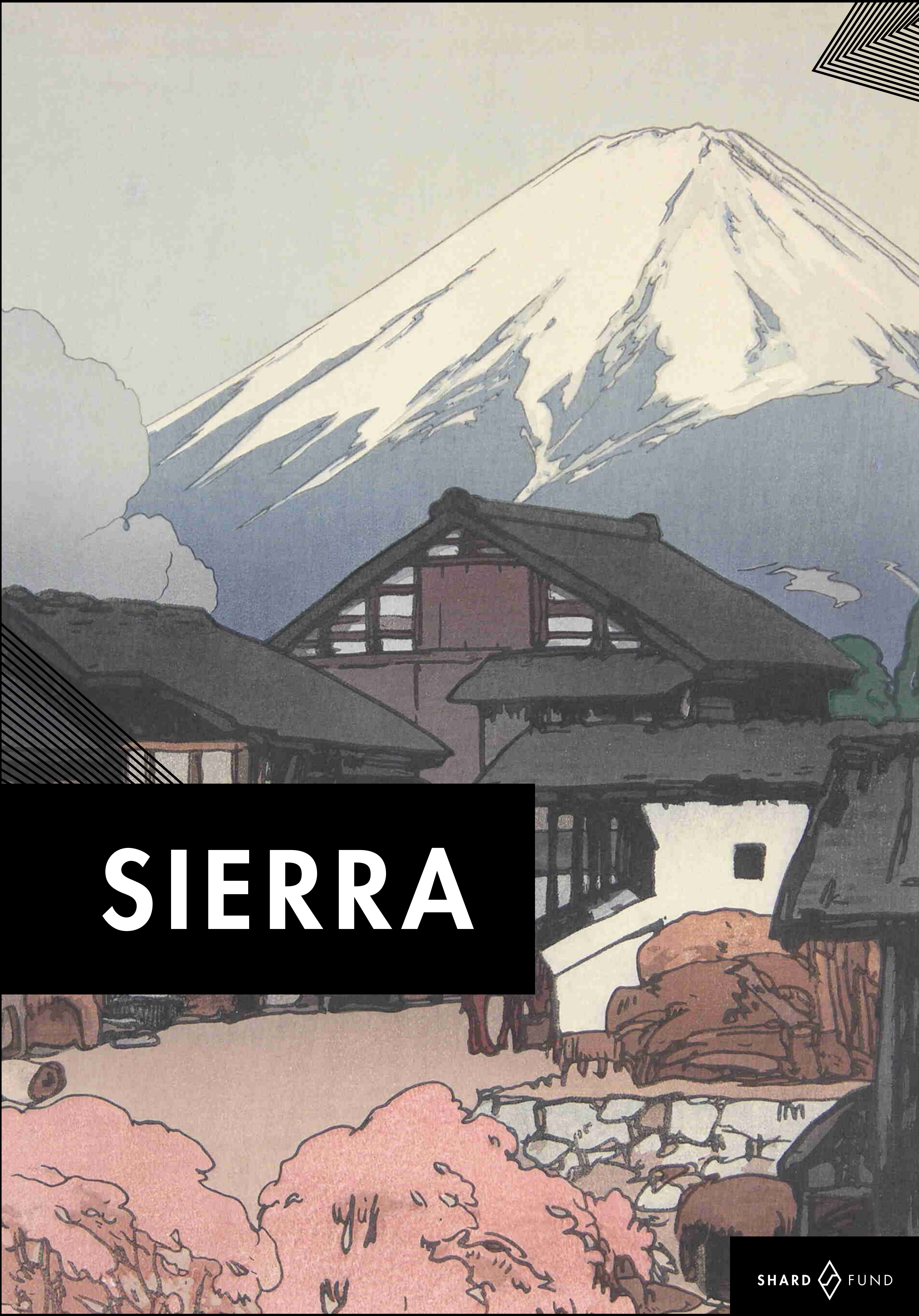

SIERRA

SHARD FUND

A JOURNEY ACROSS FINANCIAL MARKETS

November 15th - November 21st, 2014 | Issue 35

TEAM:

Georgi Stanoev USA
Angel Simbaev Europe
Stelian Nenkov Asia & Oceania: Japan
Ivan Natchev Asia & Oceania: China
Harry Collins Commodities
David Twomey Editor

SPECIAL ANNOUNCEMENT

ShardFund is a keen supporter of this charity every year. We encourage you to join us and help change the face of men's health together.
To join our team / donate / or simply follow the growth of our moustaches, click the purple moustache on the right (or this link: **http://bit.ly/1CFzhta)**, then click *join team*. If you are not from the UK, make a team of your own and join the **Shard Mo** network at the following link: **http://bit.ly/ZB9bKN**

MoBros & MoSistas:
Alexander Boradjiev
Alisa Simeonova
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Carlos Jo Loo
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Peter Tsachev
Plamen Popov
Stefan Sotirov
Stelian Nenkov
Svetla Nenkova
Zeshan Ahmad

Movember is an annual month-long charity (during November) where men are growing moustaches and raising money for prostate cancer awareness.

HIGHLIGHTS

USA

"...since the summer of 2014 volatility has started creeping back into the market and that is for every asset class not just equities. So overall we expect a lot tougher investment selection process as opposed to just 'riding the wave'. As for currencies and fixed income you just need to front run what a central bank will do and you could make a lot of money."

EUROPE

PMIs are down again: The flash Eurozone composite PMI fell to 51.4 from 52.3. German and French manufacturing PMIs are also down. The United Kingdom continues to be the only relatively good performer as Retail Sales alongside the CPI have both gone up, again.

ASIA & OCEANIA

Chinese one year benchmark lending rate was cut by 40 bps to 5.6% and the deposit rate by 25 bps to 2.75%. While everyone out there went crazy about the news, only 2 minutes of analytical thinking are enough to conclude: "Hey, that was so easy."
Japan is in recession, the second tax hike has been delayed with 18 months and there (mos likely) going to be an early election... I know, a lot can happen in a week.

COMMODITIES

As mentioned in previous issues, iron ore and thermal coal prices have been falling this year. Hard. One country particularly hit by this is Australia. The question being asked by many in the market now is "Will the free-trade agreement with China improve our terms of trade?" The market seems to think no.

Weekly Change

Indices	Weekly change	Current
FTSE MIB (Italy)	5.22%	19,954.51
DAX (Germany)	5.18%	9,732.55
CAC (France)	4.09%	4,374.23
IBEX (Spain)	3.67%	10,520.80
FTSE 100 (UK)	1.45%	6,750.76
S&P 500 (USA)	1.16%	2,063.50
BSE (India)	1.03%	28,334.63
Shanghai (China)	0.32%	2,487.11
Nikkei 225 (Japan)	-0.76%	17,357.51
Hang Seng (Hong Kong)	-2.70%	23,437.12
S&P/ASX (Australia)	-2.75%	5,304.30
Currencies	**Weekly change**	**Current**
USD/JPY	1.29%	117.79
GBP/JPY	1.21%	184.45
USD/CHF	1.15%	0.9700
GBP/AUD	0.91%	1.8063
EUR/JPY	0.21%	145.97
EUR/CHF	0.01%	1.2014
EUR/AUD	-0.06%	1.4292
USD/CNY	-0.08%	6.1249
GBP/USD	-0.09%	1.5658
NZD/USD	-0.30%	0.7882
USD/CAD	-0.48%	1.1233
AUD/NZD	-0.63%	1.0998
EUR/GBP	-0.99%	0.7915
AUD/USD	-0.99%	0.8672
EUR/USD	-1.09%	1.2391
Commodities	**Weekly change**	**Current**
Brent Crude Oil	1.16%	80.52
WTI Crude Oil	1.13%	76.68
Gold	1.09%	1200.9
Silver	0.77%	16.405
Copper	-0.26%	3.036
Rates	**Weekly change[1]**	**Current**
Italy 10Y	-13 bps	2.214%
Spain 10Y	-11 bps	2.019%
UK 10Y	-6 bps	2.048%
France 10Y	-3 bps	1.113%
Japan 10Y	-2 bps	0.460%
Germany 10Y	-1 bps	0.771%
US 10Y	-1 bps	2.312%

Source: Thomson Reuters — Note: [1] in basis points (bps)

CALENDAR

Day	Country	Indicator	Actual	Forecast	Previous
USA					
Past week (16-23 Nov. 2014)					
Tuesday	United States	PPI (MoM)	0.2%	-0.1%	-0.1%
Wednesday		Building Permits (Oct)	1.080M	1.040M	1.018M
Thursday		Core CPI (MoM)	0.2%	0.2%	0.1%
		Philadelphia Fed Manufacturing Index	40.8	18.5	20.7
Next week (23-30 Nov. 2014)					
Tuesday	United States	GDP (QoQ)			3.5%
		CB Consumer Confidence			94.5
		New Home Sales			467K
		Pending Home Sales (MoM)			0.3%
EU					
Past week (16-23 Nov. 2014)					
Tuesday	United Kingdom	CPI (YoY)	1.3%	1.2%	1.2%
	Germany	ZEW Economic Sentiment (Nov)	3.3	0.9	-3.6
Thursday	Germany	Manufacturing PMI	50.0	51.5	51.4
		Services PMI	52.1	54.5	54.4
	EU	Markit Composite PMI	51.4	52.3	52.1
	France	Services PMI	48.8	48.6	48.3
		Manufacturing PMI	47.6	48.9	48.5
	United Kingdom	Retail Sales (MoM)	0.8%	0.4%	-0.3%
Next week (23-30 Nov. 2014)					
Tuesday	Germany	GDP (QoQ)			0.1%
Wednesday	United Kingdom	GDP (QoQ)			0.7%
		GDP (YoY)			3.0%
Thursday	Germany	Unemployment Change			-22K
		CPI (MoM)			-0.3%
Friday	EU	CPI (YoY)			0.4%
		Unemployment Rate			11.5%
Asia and Oceania					
Past week (16-23 Nov. 2014)					
Sunday	Japan	GDP (QoQ)	-0.4%	0.5%	-1.8%
		GDP (YoY)	-1.6%	2.1%	-7.1%
Wednesday	China	HSBC Manufacturing PMI	50.0	50.2	50.4
Next week (23-30 Nov. 2014)					
Sunday	China	Manufacturing PMI			50.8
		HSBC Manufacturing PMI			50.0

Source: Thomson Reuters, ShardFund

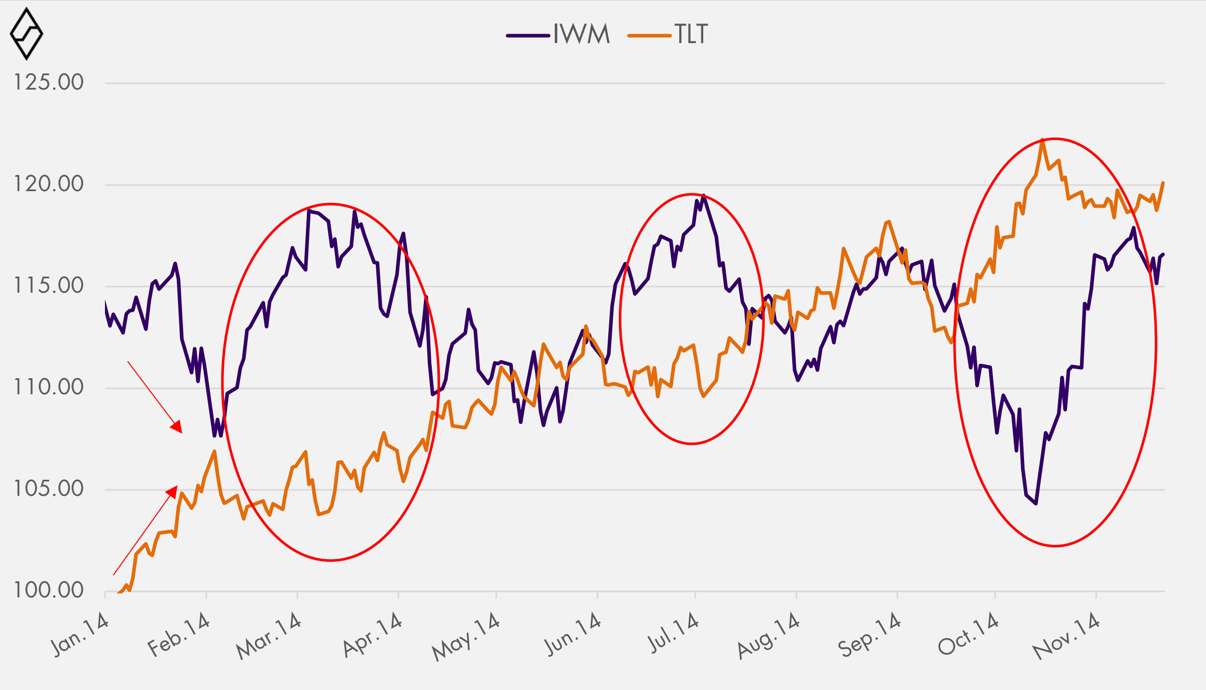
USA

Current state

Sectors	5D	1M	3M	YTD
Healthcare	1.59%	7.51%	8.57%	23.23%
Utilities	1.69%	4.46%	7.33%	20.86%
Technology	0.14%	7.79%	3.92%	16.59%
Consumer Staples	1.44%	6.58%	7.79%	12.73%
Financials	0.62%	5.86%	4.35%	10.75%
Materials	2.80%	4.80%	0.60%	9.63%
Industrials	1.55%	8.34%	5.23%	9.41%
Consumer Discretionary	1.17%	6.05%	2.31%	4.88%
Energy	2.66%	2.95%	-9.38%	-0.01%
Indices				
Nasdaq	0.52%	7.53%	3.84%	12.84%
S&P 500	1.16%	6.30%	3.57%	11.64%
Dow Jones Ind. Avg.	0.97%	8.19%	4.76%	7.44%
Russell 2000	-0.16%	6.89%	1.04%	0.75%

Source: Sectorspdr.com

Recently we received an email from a reader asking us about our view on fixed income and currencies going forward. My answer was rather broad:
"In regards to your question, since the summer of 2014 volatility has started creeping back into the market and that is for every asset class not just equities. So, overall we expect a lot tougher investment selection process as opposed to just 'riding the wave'.



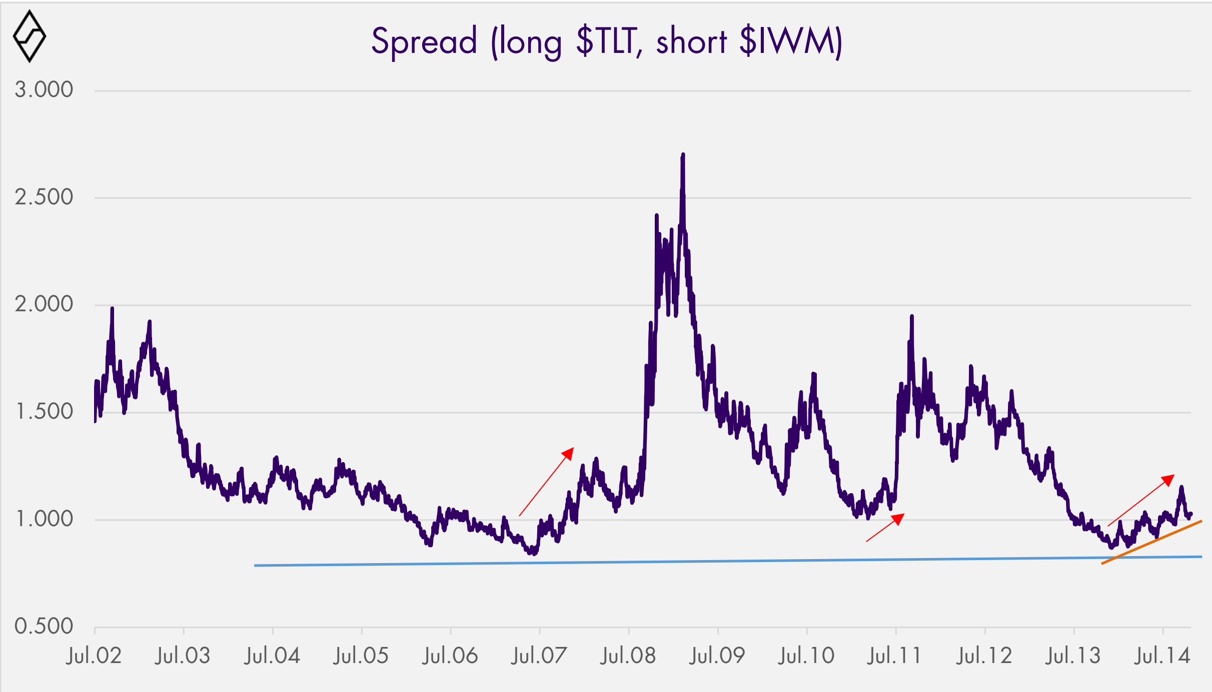
Source: Thomson Reuters

As for currencies and fixed income, you just need to front run what a central bank would do and you could make a lot of money. Unfortunately, we do not have free markets so taking into account decisions by central banks is more than essential."

This week reminded us once again how important the last part of my answer was but I will not focus on that now. In fact, from now on we will try to focus as little as possible on central banks in our weekly publications, as this distracts us from our main goal — not losing money. We need flexibility and focus to achieve that because while there are plenty of long and short opportunities out there (to name a few: healthcare, bonds on the long side; commodities and related currencies short), a great trade idea could easily be ruined by a random lunatic.

While I was updating our large database this weekend I was also thinking about our view, which should definitely reflect what is happening now, as opposed to what we hope for. I learned that lesson at an early age while playing poker, where, in order to stay profitable, I had to focus on the cards I was dealt. So, this week I focused on two particular data sets and a couple of versions of one chart. I am talking about the Russell 2000 ($IWM) and the bullish ETF on long term treasuries ($TLT).

It is quite clear that the two investments have a negative correlation (-0.4 YTD) and the chart looks relatively similar in a longer time frames as well. Since the beginning of November both ETFs (proxy for the underlying investment themes) have been flat, which signals that the market is indecisive. However, a look at their spread (constructed as long $TLT short $IWM) gives more conviction to stay with the underlying trend (for now). While we do have only 12 years of data, so far the trend has been a good friend (both on the up- and downside), so it would be logical to follow it once more (not an advice) with cautious adjustments of stop losses. Having said that, we are increasingly looking to re-enter out short position in the Russell 2000, as long as the current state stays the same. If you still think that yields cannot go any lower, just have in mind that now the 10 year treasury yield (2.32%) is significantly higher than its counterparts in Spain (1.97%) and Italy (2.18%), while Portugal is definitely catching up with a 10 year yield slightly below 3%. As for the Russell 2000, its performance divergence with the S&P 500 clearly shows that something is going on there.



Source: Thomson Reuters

EUROPE

The Draghi lift

Indices	5D	1M	3M	YTD
STOXX Europe 600 Health Care	2.07%	6.66%	6.40%	19.72%
STOXX Europe 600 Real Estate Cap	1.54%	5.78%	3.23%	18.53%
STOXX Europe 600 Food & Beverage	2.22%	7.36%	5.28%	11.71%
STOXX Europe 600 Travel & Leisure	1.66%	9.33%	9.50%	11.11%
STOXX Europe 600 Personal & Household Goods	2.55%	9.08%	6.57%	8.81%
STOXX Europe 600 Insurance	2.71%	8.91%	7.11%	8.33%
STOXX Europe 600 Telecommunications	2.75%	13.33%	9.42%	7.61%
STOXX Europe 600 Financial Services	2.19%	9.97%	3.95%	6.46%
STOXX Europe 600	2.95%	6.73%	2.38%	5.26%
STOXX Europe 600 Chemicals	4.52%	9.22%	5.54%	4.36%
STOXX Europe 600 Construction & Materials	4.34%	7.55%	0.23%	3.56%
STOXX Europe 600 Technology	4.63%	10.74%	3.17%	3.38%
STOXX Europe 600 Media	1.81%	7.97%	5.15%	3.17%
STOXX Europe 600 Automobiles & Parts	5.04%	9.31%	0.68%	0.27%
STOXX Europe 600 Basic Resources	2.55%	1.50%	-7.34%	-0.39%
STOXX Europe 600 Banks	2.62%	1.11%	-0.39%	-1.03%
STOXX Europe 600 Industrial Goods & Services	2.52%	7.72%	0.45%	-2.38%
STOXX Europe 600 Oil & Gas	4.71%	4.46%	-7.12%	-2.91%
STOXX Europe 600 Retail	2.60%	8.65%	-0.56%	-6.57%

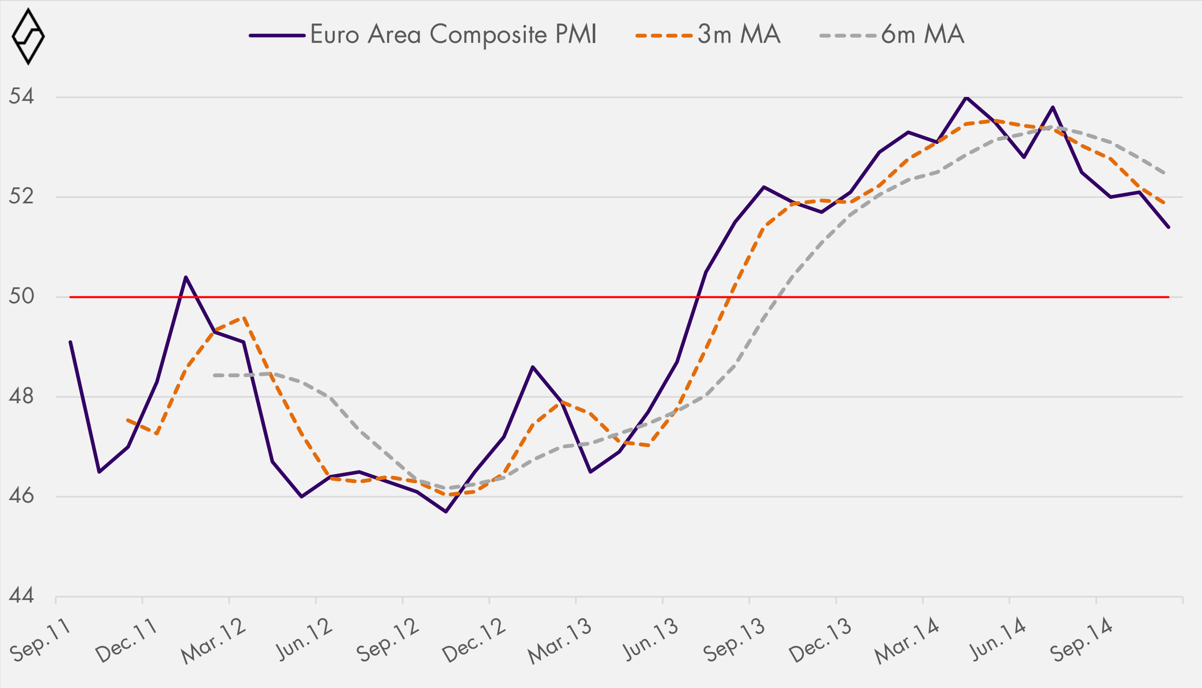
Source: Stoxx; quoted in EUR

A short data report before we start with the weekly commentary. PMIs are down again: The flash Eurozone composite PMI fell to 51.4 from 52.3. German and French manufacturing PMIs are also down. The United Kingdom continues to be the only relatively good performer as Retail Sales alongside the CPI have both gone up, again. The more interesting news is reflected in our commentary below.

Financial news reporters have named the rise in stock prices that occurs when Carl Icahn begins to purchase shares in a company, the Icahn lift. Applied to Europe this should be the Draghi lift given what happened in the course of a single day after his speech. George (US section) recently wrote, and I quote: “At this point I am starting to believe that there is a direct landline between all major central banks so they can arrange who is going to devalue next, in order to lift markets.” What I am talking about is Mr. Draghi’s speech on Friday when he mentioned he would do “anything in order to raise inflation expectations as fast as possible”. The result was a major drop in bond yields in the periphery, mainly Italy and Spain, and a jump to a two-month high in equity markets.

The United Kingdom continues to be the only relatively good performer

The central bank has started buying asset-backed securities alongside its covered bond purchases. However, it is quite interesting to watch what Mr. Draghi is doing. So far he has mentioned several times his willingness to



Source: Markit, Bloomberg

go 'all-in' for growth but it's been mostly talk without any action, while other nations have stepped up their game. Is it possible that he is simply taking advantage of the situation other central banks are creating simply to talk down the euro without having to do something? Only time will tell but it is definitely an interesting thing to consider.

Without being too critical, I believe central bankers, and most economists for that matter, need a quick introduction to the psychology of men and markets. As a basis for this I will use references from Soros' theoretical framework. I think it deserves more attention than it is actually getting as it provides a very useful insight. Essentially, the starting point of the analysis is that thinking participants have two main functions – the cognitive (the one that helps us understand the world around, call it observational if you wish) and the manipulative (man's actions in order to influence the world around). The main point is that "the participants' views influence the course of events, and the course of events influences the participants' views" and this creates feedback loops. These feedback loops in turn can be negative or positive. The negative feedback brings participants' views and the actual situations closer together, thus making it a self-correcting function. It can go on to a point where participants' views meet the actual course of events and this is what is supposed to happen to financial markets. The positive is self-reinforcing meaning that, and I stress, it cannot go on forever because at some point the participant's views become too removed from the objective reality and the process turns in the opposite direction. These self-reinforcing, self-correcting boom-bust cycles are in the heart of financial markets. I will not go any further than this as it would take too long. If you are interested in what one of the greatest fund managers has written you can find his framework in his book – The Alchemy of Finance.

Now, how does this apply to what is going on? Think about what happens when a central bank influences the self-correcting function. I leave this to you.

ASIA & OCEANIA

Abe voted best screenwriter

Indices	5D	1M	3M	YTD
STOXX Asia/Pacific 600 Chemicals	1.78%	12.77%	9.10%	17.22%
STOXX Asia/Pacific 600 Food & Beverage	1.54%	8.12%	5.01%	16.79%
STOXX Asia/Pacific 600 Technology	0.93%	7.09%	2.43%	15.83%
STOXX Asia/Pacific 600 Health Care	-2.03%	4.67%	2.38%	13.49%
STOXX Asia/Pacific 600 Personal & Household Goods	-0.02%	5.29%	2.47%	10.51%
STOXX Asia/Pacific 600 Insurance	-1.76%	8.89%	5.06%	8.68%
STOXX Asia/Pacific 600 Industrial Goods & Services	-0.65%	7.53%	3.05%	8.68%
STOXX Asia/Pacific 600 Utilities	-1.90%	6.11%	3.23%	7.88%
STOXX Asia/Pacific 600 Real Estate	-1.44%	6.54%	0.91%	7.41%
STOXX Asia/Pacific 600 Construction & Materials	-1.15%	1.73%	-6.74%	5.12%
STOXX Asia/Pacific 600 Index	-0.95%	6.39%	1.09%	5.09%
STOXX Asia/Pacific 600 Automobile & Parts	-0.01%	10.01%	7.09%	3.10%
STOXX Asia/Pacific 600 Telecommunications	-2.26%	4.35%	0.32%	2.74%
STOXX Asia/Pacific 600 Banks	-0.41%	4.52%	-0.04%	0.83%
STOXX Asia/Pacific 600 Media	-1.11%	7.43%	-3.57%	0.47%
STOXX Asia/Pacific 600 Retail	-3.56%	3.87%	-1.48%	-1.95%
STOXX Asia/Pacific 600 Financial Services	-3.80%	7.88%	-0.24%	-2.15%
STOXX Asia/Pacific 600 Oil & Gas	0.32%	-1.53%	-12.41%	-2.69%
STOXX Asia/Pacific 600 Basic Resources	-4.34%	-1.59%	-14.06%	-12.73%

Source: Stoxx; quoted in EUR

JAPAN

My view is that in the long run fundamentals' gravity is stronger, however, in the short, it seems that a few people are calling the shots. If all this sounds random... just keep on reading.

The week started with preliminary GDP going waaay below forecast to the negative territory. Meaning that Japan enters yet another recession. But I guess it's only fair, as previously, Q1 2013 was projected to be a recession maker too (forecast -0.1%; actual: 0.0%), but they dodged that one. This time, however, the economy will most likely be taking the hit (or to be technically correct, the economy took the hit and now journalists act all surprised about the picture in the rear-view mirror). I am saying most likely, because the final GDP number comes out on 8th Dec.

When you have an economy's future in your hands and you see the GDP sliding into recession due to a tax increase just prior to another tax increase the following year, what do you do? You push back the tax increase, thus easing a bit more on the financial side and hoping the economy will recover and better prepare for the other hit...exactly what Prime Minister Shinzo Abe did on 18th Nov.

He also unveiled that there will be a stimulus packages before the year's end and he called for a (pretty much) immediate election. As his ratings are starting to decrease he felt that a re-election (two years ahead of schedule) could be beneficial for him. Of course, there are possible headwinds, such as losing seats instead of gaining, which would weaken his position, but I will go in no further with my political thoughts (beyond my comfort zone).

Relating this to the market, the lesson learned here is that one should not go against such strong ideas (again, especially in the short run). Markets are going up, political intentions are strongly supporting them, fiscal and monetary policies are accommodative (for longer), so there seems to be no reason to go short now. We see that all this chaos causes uncertainty, so if a more favorable timing is apparent (the trade is quite milked so far).

CHINA

Just like in game theory, the participants in the global markets are motivated by the decisions of their counterparts. The PBOC decided to cut interest rates, for the first time since 2012. As a flashback from Japan's recent economic stimulus expansion, global stock markets rallied. Chinese one year benchmark lending rate was cut by 40 bps to 5.6% and the deposit rate by 25 bps to 2.75%. While everyone out there went crazy about the news, only 2 minutes of analytical thinking are enough to conclude: "Hey, that was so easy." Forget about how effective monetary policy is and what the final result would be. The fact is that China wants to be a consumption economy, which, however, has not been consuming that much recently. Inflation has been hitting low after low and GDP growth (official) is flirting with figures below 7%. Meanwhile the Chinese have to compete with their 'loving' neighbour Japan, which has devalued its currency by roughly 50% (USD/JPY) since the end of 2012. Those are all facts disregarded by a lot of people (us included), hence the shock and horror on Friday. However, if we have to be honest, Chinese interest rate cut should be the least surprising one. So what if they are inflating their huge bubble?

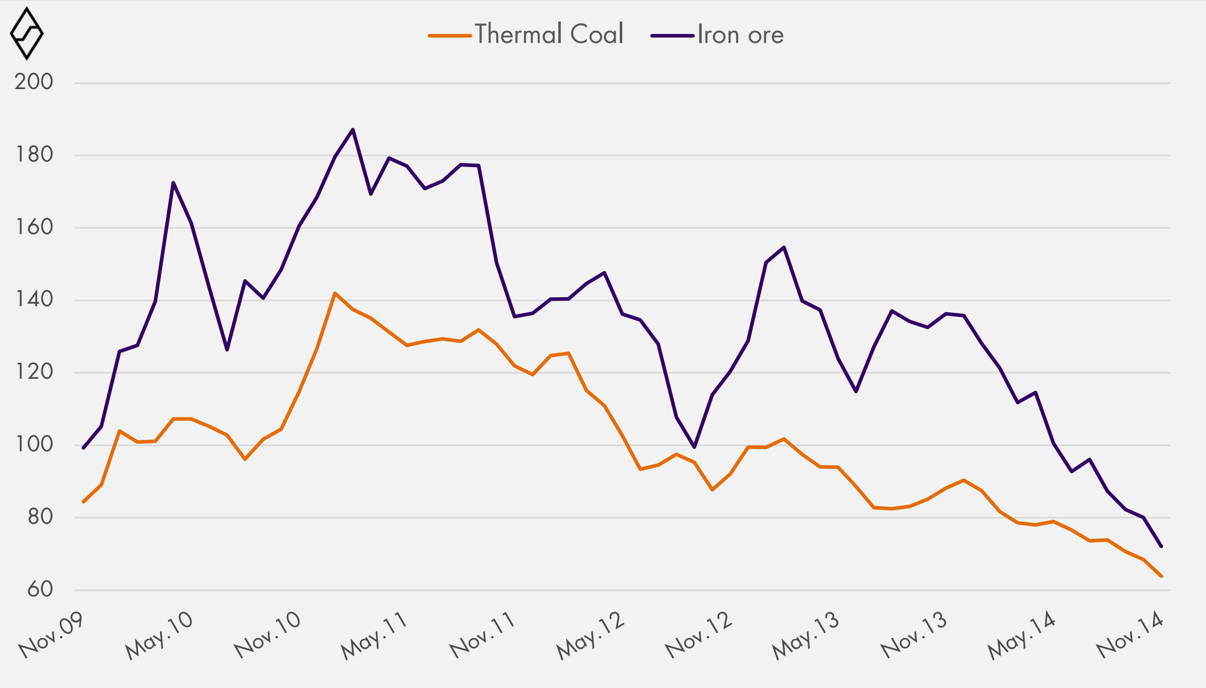
Something I have been thinking about is the exit strategy of loose monetary policy. If the rate hikes coincide with the peak of the business cycle, which I see as a possibility in the US, the consequences might be far from mild. Then again, it is almost certain that central bankers will only get more dovish as signs of contraction start manifesting themselves. The question is if this is sustainable. However, those are long term thoughts. In the meantime we have to stay flexible and trade the market we have, otherwise we end up being just a bearish newsfeed like....you know what I mean. No positions in China taken or considered at the moment.

COMMODITIES

Birth rate

METALS

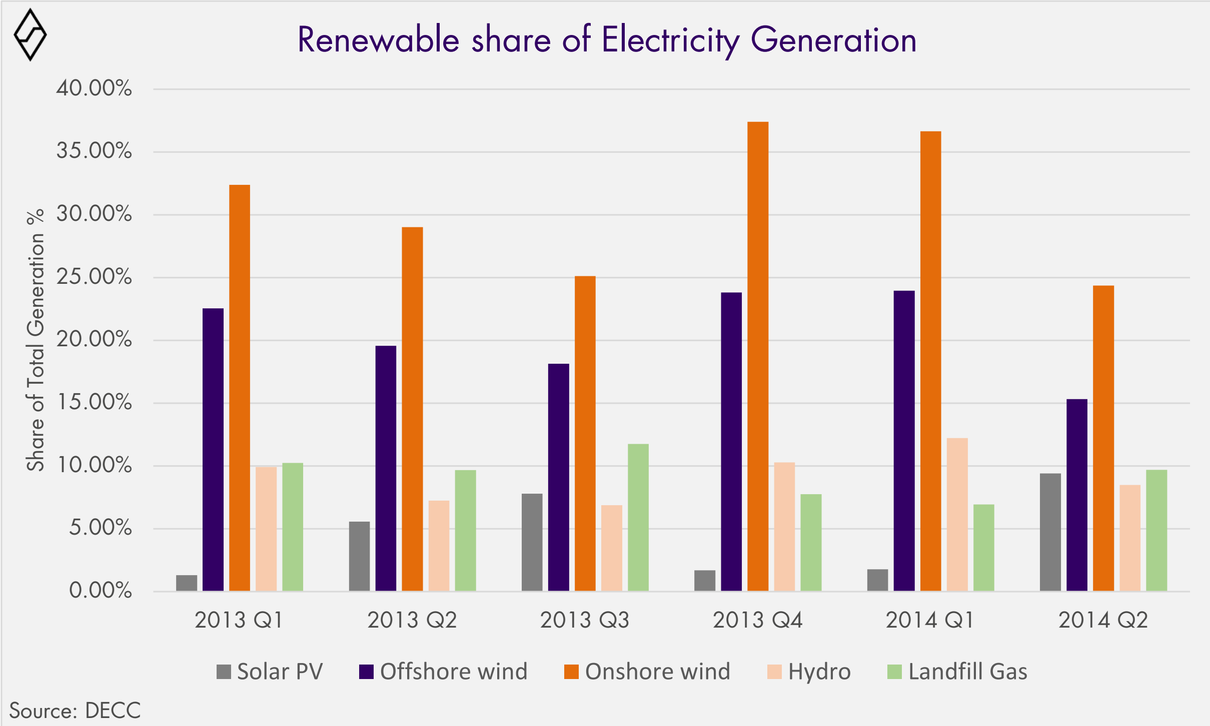
As mentioned in previous editions, iron ore prices have fallen this year, hard. In addition thermal coal has also fallen.
One country particularly hit by this is Australia. The question being asked by many in the market now is "Will the free-trade agreement with China improve our terms of trade?" The market seems to think no (at least where metals are concerned). Iron ore 2016 futures are trading below $70 [Thomson Reuters]. Furthermore if history is anything to go by then these deals don't always increase exports (as they are usually sold on doing), but merely change the destination of exports from other countries to the new country the agreement has been signed with.



Source: Thomson Reuters

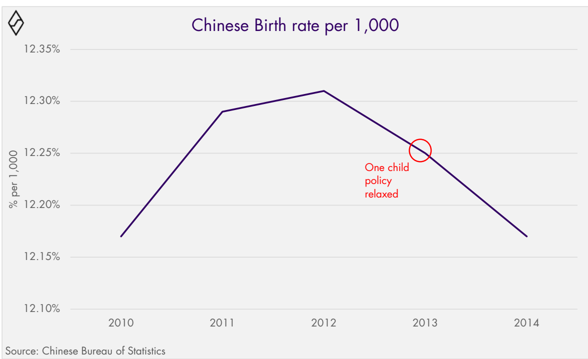
ENERGY

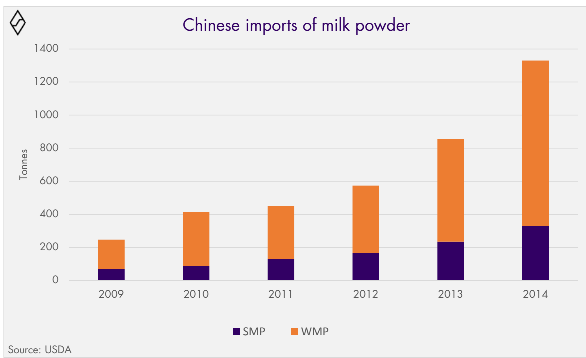
With December fast approaching the capacity mechanism auction will soon be here. In brief the capacity mechanism is a governmental scheme designed to ensure there is enough electricity in supply to stop the "lights going out", when renewable sources aren't producing any power due to being intermittent (e.g. wind). Blackouts could happen more frequently as more renewables come online, depending of course on what technology it is. The EU's target is that by 2020 20% of its energy will be from renewable sources. Below is a graph of the key renewable energy sources that generate electricity.



AGRICULTURE

In the first half of the year milk powder imports increased approximately 55.7%, and although the recent Chinese import data shows a decline of 23% in milk imports, the free-trade agreement between Australia and China suggests something is afoot. The deal allows all tariffs on dairy products to be phased out over four to eleven years, this seems likely to benefit Australia, particularly as its economy is shifting more to an agricultural based economy, following the slump in metal prices. This could suggest that China is preparing itself for a "baby boom" and would explain the ongoing trend in milk imports. However the counter argument, that the one-child policy was relaxed in 2013 and that birth rate growth has actually decreased, could suggest otherwise.





PORTFOLIO

CORTEZ

				Price		Performance	
Security	Ticker	Entry date	Long/Short	Entry	Current	Weekly	Inception
Legg Mason Inc	LM	21.Jul.14	Long	50.4	55.4	0.5%	8.9%
T.Rowe Price Group	TROW	21.Jul.14	Short	81.4	82.0		
iShares STOXX EU600 Utilities (DE)	EXH9	31.Jul.14	Long	32.4	31.3	2.1%	0.6%
PowerShares DWA Developed Markets Momentum	PIZ	1.Aug.14	Short	25.2	24.6		
iPath S&P 500 VIX ST Futures ETN	VXX	22.Aug.14	Long	27.8	27.9	-3.8%	0.4%
iShares 20+ Year Treasury Bond ETF	TLT	23.Sep.14	Long	115.0	120.1	0.5%	4.5%
Valeo SA	VLOF	12.Nov.14	Short	89.6	95.6	-4.5%	-6.2%

Source: Thomson Reuters as of 3.Oct.14 close prices

FOREX

Pair	Open	Close	Weekly %	Trend w/w	Monthly %	YTD
USD/JPY	116.29	117.79	1.29%	5	7.41%	11.86%
EUR/JPY	145.67	145.97	0.21%	3	5.38%	9.23%
USD/CHF	0.9590	0.9700	1.15%	1	1.55%	8.65%
GBP/JPY	182.24	184.45	1.21%	5	3.75%	5.86%
USD/CAD	1.1287	1.1233	-0.48%	2	0.30%	5.77%
AUD/NZD	1.1068	1.0998	-0.63%	3	-1.81%	1.32%
USD/CNY	6.1295	6.1249	-0.08%	1	-0.22%	1.18%
GBP/AUD	1.7900	1.8063	0.91%	1	-2.48%	-2.38%
EUR/CHF	1.2013	1.2014	0.01%	1	-0.44%	-2.42%
AUD/USD	0.8759	0.8672	-0.99%	1	-0.85%	-2.70%
NZD/USD	0.7906	0.7882	-0.30%	1	0.95%	-3.95%
EUR/GBP	0.7994	0.7915	-0.99%	1	1.59%	-4.59%
GBP/USD	1.5672	1.5658	-0.09%	5	-3.43%	-5.42%
EUR/AUD	1.4301	1.4292	-0.06%	2	-1.07%	-7.69%
EUR/USD	1.2527	1.2391	-1.09%	1	-1.91%	-9.85%

Source: Thomson Reuters

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.

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