General market up date

01 October 2010

Japan

The Japanese currency is testing all-time highs as a risk-averse market favors the yen over the dollar and the euro. The Bank of Japan and Prime Minister Naoto Kan may view this as an aberration. Their 30 August announcement of increased bank lending to just over US $355 billion, combined with an additional, albeit small, fiscal stimulus is likely an acknowledgement that the yen's recent rise is detrimental to Japan's economic and financial market stability.

- First, Japan's fiscal position is widely considered the worst in the developed world. The scale of adjustments necessary to stabilize the country's debt remains unprecedented, requiring deep spending cuts, large increases in taxation and other potentially onerous austerity measures.
- It also boasts the world's most elderly population; the country can expect to see a lower Support Ratio made worse by a decline in income tax revenues.
- The country will have no alternative but to seek new foreign investors. In a world where concern is growing over fiscal deficits, it is expected this will be no easy task.

There are clearly a number of drivers that may affect short-term movement. Yen-positive catalysts include increased global risk aversion; appreciation of the Chinese renminbi; and diversification of reserves by the world's central banks.

Conversely, there are several drivers that threaten to weaken the yen, including investors' demand for higher yield, the interest rate differentials between the US and Japan, the steepness of the US Treasury yield curve as a proxy for global growth, and finally the possibility of further intervention by the Japanese authorities to keep the yen weaker than 85.

As members who have received my latest report will know I have been taking advantage of the current yen/dollar position to post trades recently for the Professional Investors Fund, These trades have done well. I would point to the 3Ds of Japan – Debt, Demographics and Deficits which I believe conspire to cause a secular decline in the yen. The opportunity is ripe for investors to consider using short-term strength in the yen as a good entry point to reduce their JPY exposures or to short it outright.

U.S. - The U.S. is ready to print yet more dollars if the recent slowdown in the pace of recovery continues, the U.S. Federal Open Market Committee has signalled.

Federal Reserve chairman Ben Bernanke said recently that the committee would provide additional monetary support "if the outlook were to deteriorate significantly"

U.K. - The Bank of England signalled that it is moving closer to more asset purchases, joining the Federal Reserve in contemplating further stimulus to revive a flagging economic recovery. Policy maker Adam Posen said last week that a "plan B" approach for the Bank of England should be "heavy-duty credit easing."

Europe - Growth in private-sector activity across the 16-nation euro zone slowed sharply in September, a closely-watched survey of purchasing managers showed an underlining worry about the momentum behind the region's economic recovery.

Germany - German unemployment will decline to the lowest since 1992 next year and more people will be in jobs than ever before in re-unified Germany, as stated by the Federal Labor Agency's IAB research institute.

Money is on the move

Money is flowing into Asia, Australia and Brazil as growth is expected to continue with strong domestic demand. This trend is likely to continue because the economic recovery in developed countries like the U.S. is still weak at best.

Published data shows that India is another beneficiary, which has placed 787bn rupees in stocks this year, including 212bn rupees in the primary markets. The flows have helped the index rise above 20,000 for the first time since January 2008 and pushed the rupee up 4.8% from an eight-month low in May.

Commodities - Gold rose to a record high last month in London and New York as investors sought protection against turmoil in the global economy and financial markets. Silver rose to its highest price since March 2008 in the same period.

Members following my professional investors reports will know this since gold bullion climbed as high above my pre set sell price profits had already been taken for the RIO Professional Fund, on the back of my forecast that we should now see a correction in the metal's price. Before this commodity continues its upward trend the correction anticipated will afford me the opportunity to place trades as usual. There may be some who are surprised to see that just as predicted previously, people are worried about equities, debt, property and currencies and continue to run to gold as a safety at the slightest talk of trouble in other markets.

Are people finally starting to understand that quantitative easing will devalue the currency as I have said before? If so it is why we have recently seen a new wave of investors shifting into gold. That's good news for the yellow metal and excellent news for traders like me who will take full advantage of this situation to actively trade whilst opportunity is knocking.

My Recommendation: invest in RIO Professional Investors Fund' which trades gold and is currently outperforming both its bench mark return and the main markets. I will be sending a report on RIO Prestige Performance this week.

William Gray
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The RIO Club