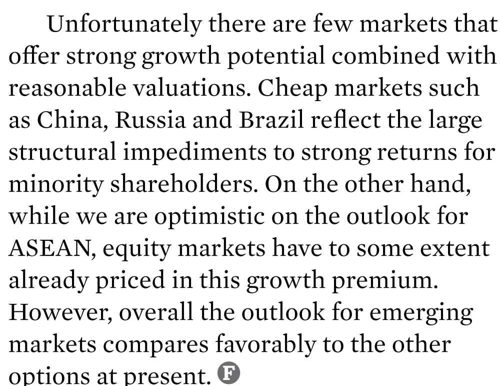
the next decade, with real returns highly likely to be negative.

While the U.S. stands alone in terms of its weak long-term prospects, Germany and Japan can hardly be considered cheap, and their economic and demographic outlooks adds more uncertainty. Peripheral Eurozone stocks are undoubtedly cheap based on long-term valuation measures such as price-to-book value, but this is in large part due to the high weighting of banking stocks on the major indices, which we believe are cheap for a reason. Furthermore, as we expect a significant U.S. bear market to develop soon, falling U.S. stocks will weigh on other markets.

EMERGING MARKETS FOR THE LONG TERM

This leaves the emerging markets (EM). Down 40% from its 2007 peak, the MSCI Emerging Markets Index is finally priced for solid long-term returns. While the days of rapid EM growth will not return soon as state-dominated economic models will remain to a large extent, our overarching view is that emerging markets are gradually undertaking efficiency-enhancing reforms to support growth and equity performance. The kind of dislocations that existed in the late-1990s EM bear market are less prevalent today (lower foreign debt being the main difference this time), while valuations are almost as cheap. Meanwhile, developed market monetary policy is likely to remain extremely accommodative as central banks' hands are partially tied by heavy government debt loads, thus allowing higher-yielding EM currencies to perform well in total return terms.

Unfortunately there are few markets that offer strong growth potential combined with reasonable valuations. Cheap markets such as China, Russia and Brazil reflect the large structural impediments to strong returns for minority shareholders. On the other hand, while we are optimistic on the outlook for ASEAN, equity markets have to some extent already priced in this growth premium. However, overall the outlook for emerging markets compares favorably to the other options at present. Ⓕ



GOLD OUTLOOK

THE STRONG CASE FOR GOLD

There are six powerful reasons why gold is about to rise in price.

BY WILLIAM GRAY

William Gray is the founder of the RIO Club, a private investment club, which was started in 1995. He has over twenty years experience as multi-asset investment manager, with a special focus on gold. During 2001 William forecast the arrival of the 2001 bull market in gold, trading this market from 2000 to September 2011 when he closed 100% of RIO's positions in gold, with profits over 630%. He re-entered the gold market in October 2013, and has produced 46% net gain to date providing if not the best, then among the best performing physical gold investments in the world to date, in terms of net gain.

The world's financial landscape has begun to change, which could soon cause a significant amount of money to move out of U.S. dollars. This significant change revolves around an announcement made last November 2015 by the International Monetary Fund (IMF) that China's yuan will join the elite currency basket, which includes the major currencies of the world, namely the U.S. dollar, Japanese

COURTESY OF WILLIAM GRAY

yen, the pound and the Euro. The inclusion of the yuan is recognition of the larger role China plays in world markets and its position as the second largest world economy.

Central banks now have an opportunity to move into the yuan, mostly at the expense of the dollar. The above is a strong case to buy gold, as it offers both insurance against uncertain outcomes in our financial system and, importantly, a hedge against a declining U.S. dollar.

Acquiring a significant quantity of gold perhaps to support a national currency is considered desirable, especially to become a reserve currency, a goal for China. China has been acquiring a considerable amount of gold in recent years through both their mining production and vast importing, underpinning the belief that China under-declared their gold reserves in 2015, thereby understating the full extent of these reserves.

Six Fundamental Reasons for Holding Gold

Gold will likely continue its current rally for six fundamental reasons:

1) **A rate hike by the U.S. Federal Reserve supports gold.** When the Fed raises rates, gold typically weakens then rallies. The hike of 25 basis points in December 2015 had a significant negative impact on markets. Consequently, the Fed has cut its forecast for the number of hikes this year from four to two—good news for gold. Scaling back on the forecast for lifting interest rates triggered a gold rally, and any further downplaying of rate hike expectations should keep the gold market buoyant. The longer the Fed delays raising rates, the better for gold.

2) **Fed caution weakens the dollar.** The broader theme is USD weakness, and a weakening dollar strengthens the support for a gold rally.

3) **Stock market had the worst start to a year on record and volatility is almost certain to continue.** The third reason is considerable volatility in equity markets, continuing from last year. The increased volatility coupled with what has can be described as a market sell out at the start of the year would indicate that a negative risk/reward position has started. Without substantially lower prices or structural reform, there would appear to be considerable risk in this market, and gold offers insurance against continued volatility.

GOLD HAS ALWAYS BEEN AN ASSET BUY IN TIMES OF TROUBLE.

4) **The Brexit issue in UK**. The Brexit vote on June 23 will also affect gold. An affirmative vote would hurt equities and be positive for gold. While I would forecast that a "yes" vote unlikely, having portfolio insurancein the form of gold would be wise given the additional risk from this political event.

5) **The spread of negative interest rates.** More countries are implementing negative rates, including Sweden, Japan and Switerland, with Norway signalling that it will follow. The longer central banks experiment with negative interest rates, the higher the chance of a rise in gold prices, as gold is a hedge against negative rates. While some regard gold as just another commodity, I classify it as a currency especially since bullion was lifted to a tier one asset class in 2013, and a strong one. Today it is my largest "currency" allocation.

Investors now need to assess the risk-reward of investing in assets with negative return expectations. The implications are far reaching—it fundamentally alters what it means to manage portfolio risk. As a result, I am confident that demand for gold will structurally increase, as negative rates reduce the opportunity cost of holding gold, and also what assets some investors are allowed to hold. It also erodes confidence and increases market volatility.

6) **Lower oil prices.** The last reason that could spur a gold rally is recent Saudi plans to increase oil production, thus lowering oil prices. This move would make gold more attractive as a safe haven.

Conclusion

During early 2016, investors poured money into the precious metal markets at some of the highest levels seen in almost six years. A total of $1.6 billion tracked by Bank of America/ Merrill Lynch was focused on gold and other precious metals, such as platinum and silver, and the significant flows showed that investors are losing faith in central banks, which is

a positive for gold. Gold has always been an asset buy in times of trouble. Investors always turn to precious metals during times of economic and financial uncertainty, and today's market position is troubling.

With more central banks implementing negative rates, investors should expect gold to be supported by this negative backdrop and more investment directed towards it. Another factor that will add volatility to markets are possible competitive currency devaluations which will direct investors to a safe haven, which gold can provide.

I would forecast that the U.S. dollar will weaken, which will mean a higher U.S. dollar price for gold. To date, gold is the best performing asset class in 2016. Investors should hold at least 10% of their investment portfolio in physical gold as portfolio insurance. If markets deteriorate more, then gold's price will rise markedly and provide protection against losses elsewhere in a portfolio. F

MAGNIFICENT SEVEN

Trading on the stock exchange is concentrated in the hands of a few brokers.

BY LANNY ALFIANI AND MARELLA PUTRI

The IDX has over 50 firms that are active traders on the exchanges. Yet over the years, a small handful of firms dominate most of the trading on the exchange, by value. The below are the top seven firms which, on average over the last five years, control about 33%, or one out of every three, trades. The top three are virtually unchanged, with Credit Suisse alone usually controlling about 6% of all trading, followed by CIMB and UBS, respectively, who control collectively about another 10%. Thus, three firms control about 15% of trading on the market. Another four take care of the rest. F

TOP SEVEN BROKERS SEVEN FIRMS WHICH ON AVERAGE OVER THE LAST FIVE YEARS, CONTROL ABOUT ONE OUT OF EVERY THREE TRADES.

	BROKERAGE	% OF TOTAL TRANSACTION (BY VALUE)					
		2011	2012	2013	2014	2015	Average
1	Credit Suisse Securities Indonesia	6.1	6.8	6.2	6.8	5	6.2
2	CIMB Securities Indonesia	6	6	5.2	6.1	4.8	5.6
3	UBS Securities Indonesia	3.5	3.9	5.5	5.9	4.5	4.6
4	Deutsche Securities Indonesia	4	4.8	4.9	4.3	4.1	4.4
5	Maybank Kim Eng Securities	4.9	4.7	4.8	3.8	3.9	4.4
6	CLSA Indonesia	4.3	4	4.6	3.7	4.5	4.2
7	Macquarie Capital Securities Indonesia	3.9	3.4	4.9	4.2	3.7	4
						Total	33

Source: IDX Factbook