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ECONOTE No. 61: "Cheer up, things could get worse! So I cheered up and things GOT worse!" 13/6/2017

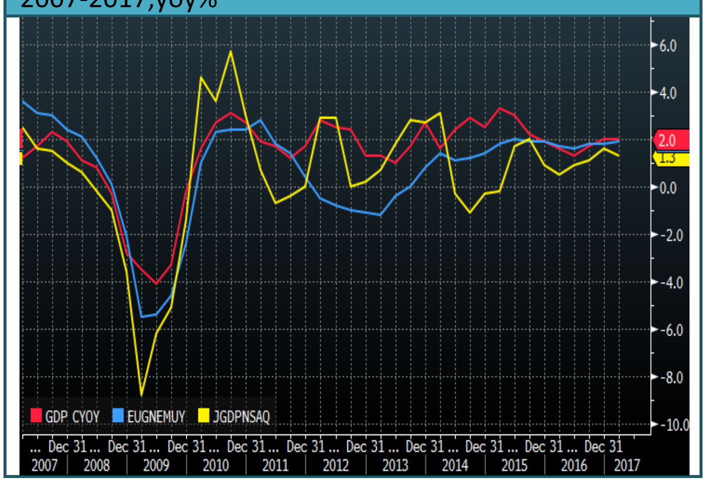
Summary	Investment Conclusions
As Shakespeare said, but in a different context " Let me count the ways": The Brexit referendum, Trump's election, then his dropping the Paris Climate Accord, then the UK Brexit elections and the terrorist attacks in the EU. But then the French (esp. the parliamentary elections) and the Dutch tell the world that they are staying in the EU, even Greece signs an agreement and drops out of the radar screen. So, is everything bad? Sounding like an economist, God forbid, in the short run (6 months) Yes, in the longer run (12 months) No. In-between chaos rules as the Brexit grinds to a halt, May resigns, UK grand coalition government forms and Recalls & Remains. Trumps keeps stumbling. Asia stays an island of stability.	"Sticking necks out" time. The Brexit will collapse within 6 months, latest a year, and, hence, very bullish on the GBP around Xmas and beyond, ditto for the FTSE100 and Euro Stoxx50.The EUR will start on a bull run earlier, as the signs become clearer. The UK staying (at least now) in the EU will be hugely bullish for the EU as it will show to all and sundry EU members what happens when you get genuinely stupid. In-between, the Fed will hike and will put UST on a double squeeze as Trump just cannot afford to backtrack on a wider fiscal deficit. Modestly bullish on the S&P, negative on UST. Meanwhile Asian equities, bar China and HK, keep doing well.

This time it is NOT different (actually it never was….)

Is the world in a mess or is it just me ? The truth is that there have been periods in the "postwar" period (well THAT was a misnomer !) when things did look grim, including the Cuban missile crisis, the end of the Viet Nam war etc. But then there was the fall of communism, soufle effect, just leave it out of the oven for three minutes and it collapses.Which brings us to the 2008-9 crisis.There are still commentarors which call it the crisis of capitalism and the worst since the 1930s.The 2008-9 crisis was not global ,ask China, India and most of the Asian economies which hardly felt it, and even some of the Latams did not do badly. In the EU, the Brits felt it as did the Spaniards and Portuguese as did other smaller countries such as Ireland and Iceland but the crisis was as American as cherry pie and its causes were incredibly unoriginal.The US banking sector overlent to property ! Gosh, whatever they will think of next ! Even Greece went belly -up starting in 2008 and not late afterwards, and that crisis, too, was also unoriginal-fiscal deficits funded from abroad.Welcome to S.Korea, Thailand and Indonesia about 11 years before, in 1997.So why raise all his now ? Simply to remind us that what we stare at now is neither unique, original nor unheard of, but simply a mixture of bad politics (UK, Trump) and less than exciting economics (Japan, for example).And in the middle of all this the G3 economies are coughing along (Fig. 1) with the EU doing better than expected, with monetary policies as divergent as ever with the Fed tightening, but ECB and BoJ not just yet, or not for quite a while. yet.

So where to from here ? To a couple more years of differentiated slow growth in the G3, the Asians, and China in particular, outperforming in terms of GDP growth, India steadily unfulfilling its potential as Modi, clearly, has no political will to supercharge the economy, and last but not least, Brazil unable to clear growth-restraining corruption.But then corruption becomes a problem and gets solved only when the middle classes have enough of it and stop it.

Fig.1 GDP growth, US (red), EU (Blue) Japan (Gold), 2007-2017,yoy%



Source: Bloomberg

ECONOTE No.61

It's the economy, stupid !

The outlook for the **US,** bar the doubts over how much the Fed will hike as the economy seems to be decelerating, will depend on whether the fiscal initiative promised by Trump will matarialise and that its impact on UST yields, combined with higher Fed funds, will not depress the property sector.The falling UST yields may simply indicate that the markets are not worried about inflation rather than the Fed policy of constraint is not working.But the twin combination of high equity values and very low yields point to something ending it up tears, and we prefer to keep out of UST. The **EU** outlook is, at least , better in terms of the ECB having arrived at the point where QE will stop, but hiking rates has not yet started.We are bullish on the EUR and EUR-denominated assets because the politics in the EU have now turned, and no one seriously doubts about the stability of the EUR and of the EU.

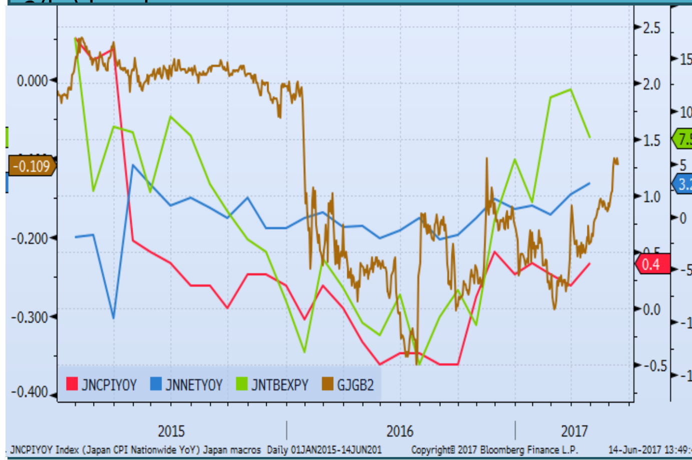
Fact Box: The UK Brexit election

The British people were asked whether they wanted to leave the EU and said Yes. Then the current government told them to give it full backing to get a good Brexit deal, and they said No. Does that mean that they don't want the Brexit? No one knows. But what everybody knows is that the momentous decision to leave the EU, and the terms of doing so, will now depend on the whims of 10 Democratic Unionist Party member and on a PM who is mistrusted by her own party and with zero leadership qualities. It will require an act of huge political courage for the Tories and Labour to join together and tell the people that elected them, that they, the people, are not ready yet for such a step. Hence withdraw the application of Brexit and spend another 10 years thinking.

Which brings us to the **UK** economy. The weaker GBP is basically temporary and will, eventually, reflect a huge relief when it is truly realized that the Brexit is dead. We will buy the relief rally around Xmas when the UK will start the process of cancelling the application or, at, least postponing it for a long, long time. As for **Japan's** continuing monetary policy, Samuel Johnson's quotation on divorce is totally apposite "The triumph of hope over experience". Fig.2 show anemic retail sales, uneven export recovery, inflation less than 0.5% and consequently negative 2Y JGB yield, albeit rising.

China's debt continues to preoccupy the markets. We repeat that the ratio of debt to GDP is meaningless (270% or so), because what matters is the cost of servicing the debt, and on which there is scant, if any, information. That is not a good reason not to worry about it as rates are being hiked by the

Japan: Infl (red), Retail (blu), Exp (gr) 10Y gov (br) 2015-7



Source : Bloomberg

Conclusions ? Who needs them !

Econotes is not keen on "what to avoid" type of investment advice, as it is about not making losses instead of making money.However, the Hong Kong property sector and property shares are such obvious candidates for a fall, that it is hard to resist saying so.We like the smaller Asians, including S.Korea,Taiwan,Singapore and the Philippines, India is too expensive and the economy is now slowing down with no reform initiatives of any kind in the horizon.As Asian interest rates have long decoupled from USD rates, the Fed hikes will have little or no impact on Asian domestic rates and the overall strength of Asian forex rates (accounting for a great deal of the strong USD, YTD stock returns !) will not be affected.Six months out we are more bullish on the GBP and the EUR, for reasosn explained, and that will include EUR sovereigns as the UST will become riskier unless Trump's fiscal initiative is completely derailed.

Top of our lists remains investment in real assets, and compliance issues notwithstanding, we will be returning to this in greater detail.

In-between see in our site www.ecognosisadvsiory.com Econotes Nos 45 & 47 which introduced our views on this topic. Regular nonsense now also appears in our Facebook page www.facebook.com/Ecognosis.

Andrew Freris (writing completed 13/6/2017)