Investment Insight

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ARIA | CAPITAL

Flow trade: *Investment flow data is watched carefully by investors. It gives them, particularly those focused on the short-term, an insight into what trends are apparent in investor behaviour. This can be very relevant – there's no point better on the FED if everyone else is betting against them; you might be right, but you'll still be wrong.*

Even over the longer term, investors can benefit from fund flow analysis to gauge positioning, assess where consensus is and draw conclusions about whether there is crowding in particular markets or assets. Flows measured on a sectoral or style basis also provide tentative conclusions about investor views of the maturity of the macro profits cycle. Post financial crisis, flows into assets associated with 'risk-off' and 'risk-on' were evident periodically, relating to external drivers such as geopolitics or regulation. In ***The Inside Track*** *we see what else flow data can tell us.*

It's just maths! *We, not infrequently, bore clients with maths trivia! One of the things we like to remind them is that if an investment falls in value by half, it then has to double to get back to where it started. Those who haven't fallen asleep at that point sometimes then declare themselves more risk averse than they thought they were! In* ***Pic of the Week*** *we return to integration, quadratics and the halcyon (ahem) days of 5th year maths.*

Quoted...

"Eight out of the 100 companies with the highest taxable income had an effective tax rates of zero"

– Comptroller and Auditor General

The Inside Track

Flow data is another tool in the investor toolkit. The following are examples of the information the data can contain.

Positioning: Flows are particularly useful in providing information about how investors are positioned, who is buying which markets and assets, and to what extent. For example, it tells a lot if we know whether movements in a market are supported by local buyers or are driven by international demand.

Trends: Since the global financial crisis an estimated $2 trillion in assets have been dis-invested from active strategies to the benefit of passives. The extraordinary stimulus provided by central banks in recent times has resulted in passive investors making above-normal returns solely by hitching their wagons to the market. As we have discussed in previous *Inside Tracks*, this trade may be close to having run its course.

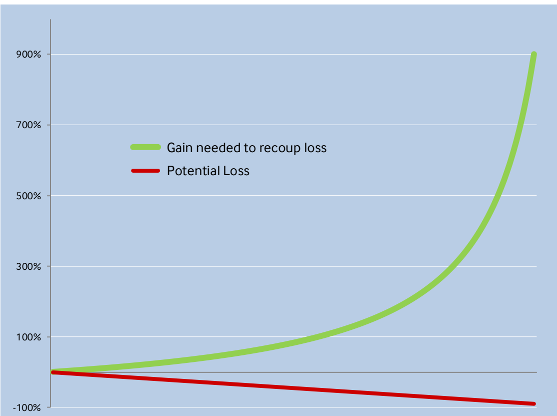
Psychology: Longer-term flow data shows that investors have a tendency to invest in last year's winners, despite warnings that previous performance is not a guide to the future. Typically, this proves, perhaps unsurprisingly, to be a losing strategy. However, equally unsurprisingly, flow data suggests a strong positive correlation between equity flows and equity, so at least in the short term it can pay to monitor the flow data and not hop off the train too soon.

Crowding: Investors like to know if they risk participating in a "crowded trade", and observing the momentum of flows is helpful in spotting this risk.

Distortions: As with any indicator, investors have to be conscious of factors that might distort the informational value of flow data. QE, for example, reduced the informational signal between bond flows and investor intent, as well as distorting credit rationing and resource allocation.

Pic of the Week

If you remember wondering when you would ever need $^{dy}/_{dx}$ in "real life", that time is now! The class is not Leaving Cert maths, but rather Adulthood Loss Aversion. By using integration we were able to derive the equation for the loss/gain curve which, courtesy of Excel, enabled us to quickly calculate and illustrate the amount of growth that would be needed to recover a loss of 1%, 2%, 3%....and so on. So if you've ever wondered how much your investment would have to grow to recover after losing, for example, 79% of its value, the answer is 376%. Class dismissed, and as it's Friday, there's no homework!



Market View

	Last 7 days (€)	Last 12 mths (€)	YTD (€)
Global equities	+0.4%	+11.3%	+6.9%
US equities	+0.8%	+9.6%	+5.5%
European equities	+0.3%	+16.3%	+10.2%
EM equities	-3.7%	+17.7%	+16.7%
Irish equities	+0.5%	+11.1%	+6.1%
Commodities	-1.9%	-4.3%	-15.0%
Hedge funds	-0.0%	+3.4%	+2.3%

Economic indicators	*Bond yields*	*Inflation*	*GDP YoY*
Ireland	+0.6%	+0.6%	+7.2%
Germany	+0.4%	+1.6%	+2.8%
USA	+2.4%	+2.0%	+2.5%
China	+1.9%	+1.9%	+6.8%

Currencies	*Current*	*YTD Δ*
EUR:USD	1.1917	+13.3%
EUR:GBP	0.8811	+3.4%
EUR:CNY	7.8774	+7.9%
GBP:USD	1.3527	+9.6%
Bitcoin	11,254	+1082.5%

Week ahead: Key events

04/12 Japan Consumer Confidence Index
04/12 Eurostat PPI
05/12 Japan & Eurozone PMI
05/12 Eurostat Retail Sales
05/12 US Retail Sales & PMI
06/12 Eurozone Retail PMI & US Mortgage Applications
07/12 Eurozone GDP & US Initial Jobless Claims
08/12 Bank of England Index of Production
08/12 US employment Data

Commodities	*Current*	*YTD Δ*
Gold	1,278.60	+11.1%
Copper	6,756.00	+22.8%
Oil	62.61	+10.3%
Wheat	412.00	+0.7%

Central Bank rates	*Current*
Eurozone	0.00%
USA	1.25%
UK	0.25%

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