



Investment Insight

Friday, 13 April 2018

Russian roulette: Driven by US sabre-rattling (a.k.a. tweeting), pressure has been heaped on the Russian stock market this week. Donald Trump's rhetoric has been backed up with economic sanctions that could have serious implications for many Russian companies. The reaction of the Russian currency, stock market and borrowing costs has been sharp and swift, with the stock market falling by 10% last Monday alone.

So is it a time to give Russian equities a wide berth? Looking at ETF flows this week, that's clearly what most investors think. However, there are some dissenting voices, Arjun Divecha of GMO being one. He doesn't buy it, or he does, if you see what we mean...In **The Inside Track** we share his perspective.

Lost in time. When investors describe themselves as "long-term", sometimes they may underestimate just how long their investment horizon actually needs to be. We came across some interesting research on "lost decades" recently – periods of approximately 10 years, although sometimes much longer – when investors made, literally, no money.

Could we be on the cusp of another lost decade? In **Pic of the Week** we look at the valuation conditions that preceded such periods and compare them to those we observe currently.

Quoted...

"If you're unreliable it doesn't matter what your virtues are." – **Charlie Munger**

The Inside Track

Penned during the middle of this turbulent week for investors in Russia, GMO's Arjun Divecha thinks the current turmoil is a decisive buying opportunity. The following are some extracts from his recent note.

On the heels of new U.S. sanctions and a chemical weapon attack in Syria, the Russian market fell 10% on April 9th, a much larger reaction than expected. It's not clear that the two situations are linked, but it suggests to us that the market perceives the risk of a major blowup with Russia, possibly taking the form of Iran or North Korea-style sanctions, has dramatically increased. We don't buy it.

Our Washington sources tell us that the new sanctions, and their timing, were a complete surprise to everyone in Congress and that this was purely a White House operation. Given the fact that Mr. Oleg Deripaska (who is closely associated with Mr. Paul Manafort) and the companies he controls were the primary targets, one might draw a conclusion that there's a political dimension to this. If the intent was to hurt Russia economically, sanctioning companies such as Gazprom and Sberbank would have had a much more profound impact. Our sources in Moscow suggest a similar view.

The new risk is that the White House is now actively involved with day-to-day Russian policy and everyone is uncertain as to what Mr. Trump might tweet tomorrow.

In short, we don't think the U.S. is exercising the "nuclear option" of trying to tank the Russian economy. While it will cause pain in certain areas, we do not think this action will have a profound impact on the Russian economy.

We've always said that you make more money when things go from truly awful to merely bad than when they go from good to great. Russia's relationship with the world is now approaching truly awful.

Pic of the Week

When we talk about the "lost decades", we're not alluding to a sci-fi novel or a maudlin retrospective. Rather, it refers to the long periods of wilderness that can be experienced by investors, testing the meaning of "patience" to its very limit. Conventional portfolio management theory would recommend a 60/40 stocks/bonds portfolio as ideally suited to most long-term investors. However, over the past century or more there have been surprisingly many extended periods, often a decade or more, during which such portfolios have generated no return. Interestingly, perhaps unsurprisingly, the start of these extended periods is usually characterised by expensive equity or bond markets. On one occasion, beginning in 1902, both equities and bonds were expensive at the outset. That period ended 19 years later and generated a return of -1.8% over the period. Guess what 2018 looks like?

Period	At beginning of period		Performance
	Equities expensive	Bonds expensive	
1902-1920	Yes	Yes	-1.8%
1930-1943	Yes	No	0.2%
1946-1954	No	Yes	0.4%
1962-1970	Yes	No	-0.1%
1973-1985	No	Yes	0.5%
1999-2009	Yes	No	-1.6%
2018-??	Yes	Yes	??

Week ahead: Key events

- 16/04 UK PMI & US Manufacturing Data
- 17/04 Japan Industrial Production & UK Unemployment
- 17/04 US Housing Starts & Retail Sales
- 18/04 UK House Prices & Eurozone CPI
- 19/04 UK retail Sales & US Initial Jobless Claims
- 20/04 Japan CPI & Eurozone Consumer Confidence

Market View

	Last 7 days (€)	Last 12 mths (€)	YTD (€)	5Y Ann. (€)
Global equities	+1.8%	-0.4%	-3.5%	+10.6%
US equities	+1.7%	-0.8%	-3.7%	+13.7%
European equities	+2.6%	+1.2%	-3.0%	+7.5%
EM equities	+0.4%	+7.2%	-1.8%	+5.6%
Irish equities	+0.5%	-2.0%	-6.5%	+10.9%
Commodities	+2.9%	-10.9%	-0.8%	-7.3%
Hedge funds	-0.2%	-1.6%	-3.1%	-1.6%

Currencies	Current	YTD Δ
EUR:USD	1.2312	+2.6%
EUR:GBP	0.8677	-2.4%
EUR:CNY	7.7370	-0.9%
GBP:USD	1.4190	+5.1%
Bitcoin	6,927	-52.2%

Commodities	Current	YTD Δ
Gold	1,342.68	+3.1%
Copper	6,930.00	-3.2%
Oil	71.92	+7.7%
Wheat	477.38	+11.9%

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

Economic indicators	Bond yields	Inflation	GDP YoY
Ireland	+0.9%	+0.2%	+7.2%
Germany	+0.5%	+1.4%	+2.9%
USA	+2.8%	+2.4%	+2.2%
China	+1.9%	+2.1%	+6.8%

66 Fitzwilliam Square
Dublin 2
D02 AT27
Ireland

T: (+353 1) 685 4100
E: research@aria-capital.ie
W: www.aria-capital.ie

UNDIVIDED ATTENTION

Important Disclosure. Aria Capital Limited is regulated by the Central Bank of Ireland. Financial data provided by Bloomberg. All values are indicative only. This Investment Insight has been prepared for information purposes only. It does not constitute investment advice or an offer to buy or sell securities. No investment decisions should be made without seeking appropriate professional advice. This document may not be reproduced in whole or in part without Aria Capital's permission. © Aria Capital Limited 2018. All rights reserved.