The Wise Investor

Vol 7 - Issue 2 | June 2013 | Rs.3.50

A Monthly Newsletter from Sundaram Asset Management

SUNDARAM MUTUAL
UNEARTHING OPPORTUNITIES

Mood in the blogosphere

If there is one place where you had, over the past eight years or so, for a credible reality check on the macro economic trends, financial crisis, economic crisis and patchwork efforts at solution, it is the blogs. Quite a few of them have been adept at linking macro picture and price trends for various asset classes. To rubbish, ignore and scare them still remains the mainstream media's attitude though a few have roped in bloggers as columnists. Where do the bloggers who saw all this turmoil well in advance stand now?

Perspective

Not one of them (among the long list of blogs we track) has had a decisive change of mind about state of the economy, especially in the developed world. Not one believes that sustainable solutions have been found. Everybody is agreed that close-to-zero interest rates are a harbinger of economic difficulty still lying ahead. Rare is the blogger who thinks a sharp spurt in interest rates is close on hand.

The Eurozone stays at the top of pecking order on concerns of where things could go more wrong in the near term. This does not mean that U.S is on its way to a healthy, sustainable economic outlook. The most recent effort at throwing more money at the Japanese economy has delivered higher growth numbers, but almost no one thinks this is sustainable. We have had so many such instances since 1989.

Quite a few have been spot on in calling the sharp slowdown in China and the popping bubble in Australia. Not many are convinced that China can credibly get back to about 10% growth, which has acquired a veneer of inevitability till a few years ago.

QUOTE

Being slow and steady means that you're willing to exchange the opportunity of making a killing for the assurance of never getting killed.

Carl Richards

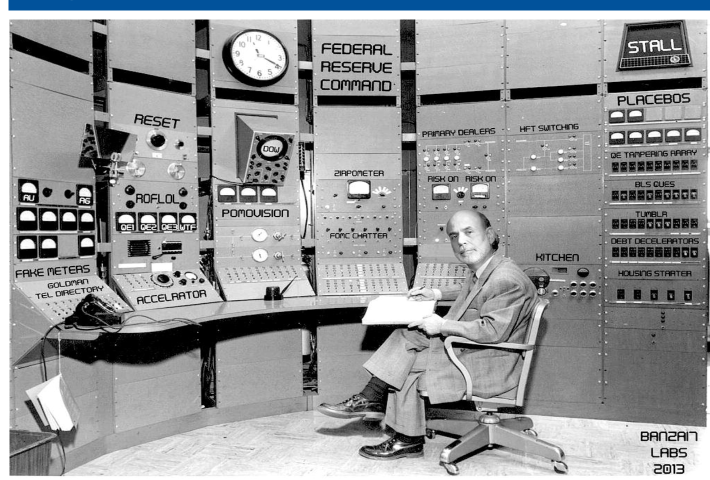
Very few have been taken in the so-called great rotation out of bonds and into stocks. A few of them have exhibited willingness to take part in the rally in U.S stocks but from a rent-the-rally perspective.

The bloggers who have called gold with a high degree of accuracy and conviction are not worried by the decline in price of about 25% in recent months. They stay bullish on gold, principally due to the weak macro economic situation in the developed world, massive sizes of the balance sheets of the U.S Federal Reserve and European Central Bank, and more recently growth trends even in big emerging nations such as China and India.

The zero-interest rates policy, versions of QE and approach of the central banks that is focused on safeguarding will most likely have a bad ending though it is tough to fix a time frame. With the exception of muscle flexing in Cyprus, a small nation, governments and central banks in other parts of the developed world stay focused on patchwork solutions and efforts to protect the Too Big To Fail outfits.

A decisive change in approach is needed to get out of the crisis in a sustainable manner.

Image of the Month — Federal Reserve Command Station



United States Federal Reserve Command Station

Source: http://williambanzai7.blogspot.in

A mixed bag

The Indian macro has significantly improved over the past two months. Inflation has declined by over 240 bps to under 5%. The weakness in global commodity prices, especially crude, is favorably impacting our twin deficits. The global sell-off in gold / precious metals is another positive from the equity perspective too.

The sustained implementation of diesel pricing reforms along with measures aimed at reducing fertilizer subsidies lends confidence on the trajectory of reforms. We expect the Government to continue with more reforms centered on energy, fuel pricing, land acquisition and measures to fast track infra projects.

The credibility of the Government's intent on fiscal consolidation and reforms is also visible in the positive surprise on the FY13 deficit figure. Government spending is expected to pick up in the next couple of months and that could improve both liquidity and growth.

We would continue to watch for revival in the investment cycle that could create more jobs, improve disposable incomes and help India to move to the next level of consumption growth.

The initial reaction to Fed's thoughts on tapering their QE program has had a short term impact on US yields with the US$ strengthening against most other currencies, triggering a wave of EM outflows.. The yield differentials between the US and Indian gilts have also narrowed, reacting to the noise around the tapering QE in USA.

Interestingly the debt markets have also seen a shift away from emerging markets that have currency weakness. While global liquidity indicators are still in positive territory, abrupt change in liquidity could be a risk to Indian macros and equities, given the low level of financial savings domestically.

Investment momentum continues to be weak while consumption seems to be holding up better than expected. There has been marginal downward revision to FY14E Sensex earnings to about 12-14% with the inflexion point on growth expected in the next six months.

We remain positive on the Indian equity markets on a medium-term basis. The run up to the elections may provide investors buying opportunities as markets continue to be volatile.

Equity Desk

A detailed view is available at **www.sundarammutual.com**

Volatility beckons

INR has depreciated sharply vis-à-vis the US dollar driven by both domestic and global factors. This has brought the focus back to the Current Account Deficit (CAD). The INR depreciated due to deterioration in the trade balance for April, 2013 that was driven by a surge in the volume of gold imports and pro USD trade in global Markets.

The FOMC minutes released during the month and stronger economic data in US made markets consider a scenario where QE 3 stimulus program could be tinkered with sooner than it expected. This resulted in sharp jump in US yields and stronger USD against all currencies especially emerging market currencies. INR with its structurally weak dynamics become the worst victim.

This at a time where US-Indian yield differential has shrunk by 100 basis points in the short time span of one month may result in some pull out from Indian debt markets as a part wider pull out from emerging market debt.

The latest WPI and CPI numbers have come off sharply in on the back of softer commodity prices and weak demand. This juxtaposed with 4.8% growth in March quarter and resultant ten-year low annual growth of 5% for FY 2013 has led market to believe that growth has bottomed out and there could be series of rate cut from here to stimulate growth. The sharp movement in G-sec yield last month is testimony to that.

The Current Account Deficit and its funding has become one of the biggest concerns of Indian economy. Further market would hope for normal monsoon as it will have impact on WPI numbers going forward. In this backdrop, it remains to be seen if Central Bank would go for further easing in upcoming meeting in month of June.

We expect interest rates to be volatile with the expectation that every economic data point in India will be scrutinized to assess its contribution towards policy formulation. We expect 10-year G-Sec to trade in the range of 7.10%-7.45%. Next month we expect government spending and OMOs to give some respite on liquidity front.

Fixed-Income Desk

A detailed view is available at **www.sundarammutual.com**

The Outside View

The key issue

For those investors not directly involved with the US capital markets, the key issue as regards America remains whether growth will be strong enough to induce a Bernanke-run Fed to start to normalise monetary policy. This is because any hint that the Fed would start to move out of a zero-rate world would likely lead to a sharp rally in the US dollar. This would not be bullish for the American stock market where 46% of S&P500 revenues are derived from offshore. But more importantly, it would also not be bullish for the US-dollar-financed carry trade invested in the likes of corporate debt and emerging market debt, a carry trade directly encouraged by Billyboy Ben's surprising and astonishing "forward guidance" issued in January 2012.

GREED & *fear* has been interested to read of late estimates of the US dollar global carry trade running to around US$2tn. CLSA's legendary investment guru Russell Napier has also highlighted the risk in his recent work on an emerging market debt bubble. Napier argued in that report that the current "yield bubble" is likely to fall victim to an emerging market balance-of-payments crisis and/or commodity price declines. He further argued that the conditions for such a bust are already well advanced, as indicated by the collapse in the growth of emerging market foreign reserves.

While this carry trade is indeed a concern, GREED & *fear* continues to believe that the bubble is less in the emerging markets themselves than in the conduct of American monetary policy. Indeed GREED & *fear* views Bernanke's "forward guidance" as the height of central banking irresponsibility since it encouraged everyone with access to cheap dollar funding to put on such a trade; for example the "high net worth" customers of global "private banking" franchises. But if this is highly irresponsible, it was also presumably Billyboy's intention. Meanwhile, if the above is the obvious risk, the practical issue for investors, having to deal with the demands of short-term performance, is when the carry trade blows up.

Christopher Wood, Managing Director & Strategist of CLSA Asia-Pacific, an independent research outfit and author of the weekly report GREED & *fear*.

Source: www.clsa.com

Investment Quiz

1 Who was the Chairman of Infosys before the return of N R Narayana Murthy?

2 What are the key interest rates set by the Reserve Bank of India?

3 Who is the head of the Bombay Stock Exchange?

4 Which organization that is linked to markets and investors recently celebrated its 20th year?

5 Name the person in the picture? He is perhaps the key person in structuring India's macro-economic policy?

Answers for April 2013 Quiz

1 Who is the author of The New Laws of the Stock Market Jungle?
Michael Panzer

2 Which type of bond is the safest in the Indian context?
Government of India bonds has no risk on repayment if held to maturity

3 Name the business newspaper published by the Hindustan Times group?
Mint (www.livemint.com)

4 Name the new firm that owns the independent research outfit CLSA?
Citic Securities, a Chinese company

5 Name the person in the picture? He is one of the several who saw the global crisis coming and the author of one of the most renowned books in recent times, The Black Swan?
Nicholas Nassim Taleb, celebrated thinker and author of The Black Swan among other books

Keeping tab

 # 1 Nouriel Roubini misguided on Gold et al – Mike Shedlock (http://globaleconomicanalysis.blogspot.in)

 # 2 Euro: Its worth fighting for – Jens Weidman, President of Bundesbank of Germany (www.bundesbank.de)

 # 3 Large `Short Dollar' faces the squeeze – Edward Chancelllor of GMO (www.ft.com)

 # 4 Global liquidity: where do we stand? - Speech by Jaime Caruana, General Manager of the Bank for International Settlements (www.bis.org)

 # 5 The Global Financial Crisis and the Indian Financial Sector – Duvvuri Subbarao, Governor Reserve Bank of India (www.rbi.org.in)

 # 6 The stock market is topping out – Comstock Funds (www.comstockfunds.com)

 # 7 It's Going to be Another Interesting Summer – Doug Noland (www.prudentbear.com)

 # 8 2009 vs 2013 – John Hussman, President, Hussman Funds (www.hussmanfunds.com)

 # 9 How alternative investments are a `misconception' – (www.ritholtz.com)

 # 10 Why the Fed hates the word tapering – Real Time Economics (blogs.wsj.com)

 # 11 Infosys gains in price, but surrenders its values – The Honest Truth by Ajit Dayal (www.equitymaster.com)

 # 12 Should the Fed lose control….Charles Gave quoted in Zero Hedge and analysis – (www.zerohedge.com)

Baruch's 10 Rules of Investing

Being so skeptical about the usefulness of advice, I have been reluctant to lay down any 'rules' or guidelines on how to invest or speculate wisely. Still, there are a number of things I have learned from my own experience which might be worth listing for those who are able to muster the necessary self-discipline:

 # 1 Don't speculate unless you can make it a full-time job.

 # 2 Beware of barbers, beauticians, waiters — of anyone — bringing gifts of "inside" information or "tips."

 # 3 Before you buy a security, find out everything you can about the company, its management and competitors, its earnings and possibilities for growth.

 # 4 Don't try to buy at the bottom and sell at the top. This can't be done — except by liars.

 # 5 Learn how to take your losses quickly and cleanly. Don't expect to be right all the time. If you have made a mistake, cut your losses as quickly as possible.

 # 6 Don't buy too many different securities. Better have only a few investments, which can be watched.

 # 7 Make a periodic reappraisal of all your investments to see whether changing developments have altered their prospects.

 # 8 Study your tax position to know when you can sell to greatest advantage.

 # 9 Always keep a good part of your capital in a cash reserve. Never invest all your funds.

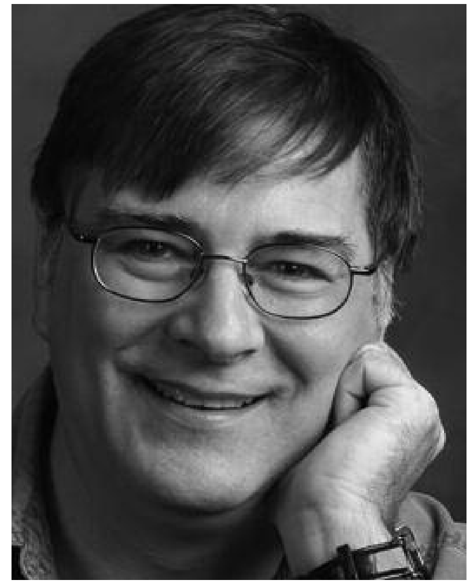
 # 10 Don't try to be a jack of all investments. Stick to the field you know best.

Bernard Mannes Baruch was an American financier, stock investor, philanthropist, statesman, and political consultant

Source: www.ritholtz.com

The views presented by the author (s) do not necessarily represent that of Sundaram Asset Management. The article / posts have been reproduced with permission or from reports available in the public domain in order to provide readers access to a diverse range of views on the economy and asset markets.

Eye opening sparring on Gold



Editor's Note: Mike Shedlock – who has consistently been correct in calling economic and market trends over the past several years – rips apart economist Nouriel Roubini on the latter's gold call. Though elaborate, it is worth a read to understand to different thought processes and what it means for investing.

I just finished reading Nouriel Roubini's seven point analysis on the **Bursting of the Gold Bubble** in which Roubini's asks and answer the question "*Gold skyrocketed to over $1,900 per ounce in the fall of 2011 from $800 in early 2009, but has since collapsed by around 27%. Why?*" *I (Mike `Mish) Shedlock)* offer a point-by-point rebuttal.

Roubini: First, tail risks are lower. Gold tends to spike when the global economy faces severe economic, financial and geopolitical threats; but, thanks to a variety of policy actions, the tail-risks argument for holding gold is less compelling today than at any time since the start of the financial crisis in 2007.

Mish: Japan is flirting with a Yen crisis thanks to Abenomics. Nothing has been fixed in regards to structural problems in the eurozone. A US recession is at hand. A China slowdown is baked in the cake. Trade wars loom between China and Europe. A full scale housing bust is underway in Australia. The UK threatens to leave the EU. The eurozone is unlikely to survive in its current state. Tail risks are enormous (and growing). I would have thought tail risks were so obvious that any serious economist would notice them. I was mistaken.

Roubini: Second, inflation is low and falling. Gold does best when there is a risk of high inflation, as it is a traditional store of value against inflation. But, despite the very aggressive monetary and quantitative easing from many central banks, global inflation is actually low and still falling as growth in most of the global economy remains below trend.

Mish: Gold actually does well in periods of deflation, in periods of credit risk, in periods of stagflation, and in periods of hyperinflation (the latter is obvious). Price inflation fell from 2000 to 2013 and gold rose from $250 to $1900. When was there risk of high inflation in that time-frame? To be fair, one also needs to look at the disinflationary period between 1980 and 2000 when the price of gold collapsed from $850 to $250. Yet, in disinflationary periods in the last decade, gold soared. The difference? Credit risk and global distrust of fiat currencies. It's easy to cherry pick a timeframe and say gold does this or that, when other timeframes and other factors disprove the thesis.

Roubini: Third, other assets provide better returns. Now that the global economy is recovering, other assets, such as equities or even real estate, are performing much better than gold.

Mish: Lovely! The same sort of argument regarding housing could have been presented in 2002, in 2003, in 2004, and in 2005. Yes, other assets are performing better, for now. But for how long? Is the current trend supposed to last forever? Has Roubini suddenly become a momentum trader in what is performing best?

Roubini: Fourth, exit from ZIRP will be bearish for gold. Real interest rates and gold prices are highly inversely correlated. Although real rates are still negative, the more positive outlook for the U.S. and global economy implies that the Fed and other central banks will gradually exit from QE and ZIRP. Real rates will rise over time rather than fall.

Mish: Precisely when is the Fed supposed to end ZIRP? Tomorrow? Next Month? Next year? A decade? If "real rates rise" won't that be a sign of increasing inflation? Is increasing inflation good for gold or not? Roubini attempts to make a case that rising inflation and falling inflation are both bad for gold and both are about to happen simultaneously. Let me also point out that Roubini thinks 'QE' won't end for another two years! He can't have it both ways.

Roubini: Fifth, highly indebted countries are planning to sell their gold. Some argued that a world full of highly indebted sovereigns would push investors into gold, as government bonds would become more risky. Instead, these countries are likely to dump their gold reserves to reduce their debts, or at least are considering doing so.

Mish: Roubini's thesis has gone from circular silliness to the point of complete absurdity. Other than Cyprus (and Cyprus was forced at gunpoint) what central banks are dumping gold? And what central banks are buying gold? Zero Hedge reports Russia, Greece, Turkey, Other Central Banks Buy Gold

Roubini: Sixth, U.S. dollar appreciation is bearish for gold. There is usually an inverse relationship between the value of the U.S. dollar and the dollar price of commodities, including precious metals like gold. Looking ahead, the relative strength of the U.S. economy and of U.S. asset prices compared with those of other DMs suggests that the dollar may appreciate—as it has done recently—against a basket of DM currencies.

Mish: The biggest gold rally of all time (1979) occurred while the dollar was going sideways with a slight upward bias. The dollar and gold both rose in 2005 as well. If the dollar were all-important for gold, it would never rise in terms of foreign currencies, but it definitely does do that.

Roubini: Seventh, gold has been hyped for irrational political reasons. Some extreme politically conservative gold bugs think that all government is evil, that there is a government conspiracy to expropriate most private wealth and that gold is the only hedge against this risk. This group also believes that we will return to the gold standard as central banks "debase" paper money and as hyperinflation ensues. However, inflation is falling globally and gold is not in any way a currency.

Mish: Yes gold has been hyped by many hyperinflationists. The same was true two years ago, five years ago, and 10 or more years ago.

That makes Roubini's own hype all the more laughable. Roubini ends his hype with this statement: "The price of gold may temporarily go higher in the next few years, but it will be very volatile and trend lower over time as the global economy slowly mends itself. RGE expects gold to go to $1,300 by end-2013 and $1,000 by 2015. For the most part, it is time to offload and underweight Keynes's barbarous relic."

People ask me all the time where the price of gold is headed. I do not pretend to know, especially in the short-term. However, I understand the fundamentals and Roubini clearly doesn't. Nor does Roubini have a clue about money or what causes economic growth. His statement "It is time to offload and underweight Keynes's barbarous relic" is quite telling.

Clearly Roubini believes that printing money creates wealth. The average 7th-grader (not yet influenced by Keynesian and Monetarist clown teachers) can easily figure out the fallacies of such ridiculous economic theories.

Who benefits from printing? The answer is those with first access to money (the banks, the already wealthy, and the government). Printing money does nothing but exacerbate the trend of income inequality. This is so obvious that Roubini cannot see it. Buying gold is a perfectly rational reaction to the crazy central bank and governmental policies that Roubini advocates.

Things Roubini is Wrong About: gold, tail risk, benefits of monetary printing, benefits of fiscal stimulus, on what causes economic growth, Inflation and stock market risk

That is one heck of a lot of things to be wrong about!

Mike "Mish" Shedlock

Source: http://globaleconomicanalysis.blogspot.com

Governments around the world are finally beginning to realize the gravity of the risk that exists in their banking sectors. The EU has decided to build upon the new template of the "bail-in" regime. The US, UK and Canada have all followed suit. This puts the onus squarely upon the depositor. The depositor is a lender to the financial institution that he banks with. However, most depositors naively assume that their deposits are 100% safe in their banks and trust them to safeguard their savings. Under the new "template" all lenders (including depositors) to the bank can be forced to "bail in" their respective banks. Several G7 countries already have provisions that allow troubled banks to be bailed in using depositor accounts.

We have been vocal about our concerns over the state of the global financial system for the better part of the decade. The Greek tragedy is now being played out in Cyprus with a new twist as depositors have been unwillingly turned into sacrificial lambs. Given the size of the banking sector in most G7 countries and the burgeoning government debts, the ability of the governments to bail out their banks is severely constrained, especially considering the political headwinds that exist today. For this reason, we strongly believe that real assets trump a fiat currency in a "savings" account. It is not our intention to be alarmist here, merely to say, "caveat depositor".

Eric Sprott (Sprott Asset Management, www.sprott.com)

In today's America, real (inflation-adjusted) wages are lower today than they were 10 years ago. Depending on how you adjust for inflation, they may be as low as they were at the end of the second Eisenhower administration. With so little in earnings, people are naturally careful with their money. They go to giant discount shops… in order to get as much for their money as possible. They want low prices. What is an economy for if not to satisfy the hopes and desires of the people who live in it? And what is the goal of activist economics if not to help people get what they want? So what does Paul Krugman do?

He urges the government to raise consumer prices — to consciously and intentionally sabotage the wishes of the people by raising the cost of living. That's the point of QE: to put more money in circulation so that prices rise. Then people will get less for their earnings and savings… and be more eager to spend now, rather than save for later (rightly fearing that their dollars will lose value over time). And that's why Krugman prefers to think of an economy as a machine. Machines can be manipulated and controlled. Real economies can't.

Bill Bonner (Daily Reckoning www.dailyreckoning.com)

The Fed will keep its current level of bond purchases going indefinitely only if the economy continues to look anemic. In that case, second half earnings will be highly disappointing. He has constantly made it clear that he would rather err on the side of staying easy too long than in tightening at a point he considers premature. It seems almost a no-brainer that an actual tapering of the bond-buying program would send rates soaring. In that case, an economy that has become overly dependent on low interest rates and abundant liquidity would be stopped in its tracks, and the market would likely undergo a substantial decline.

In our view the Fed has stretched the rubber band as far as it can go in the face of major fiscal restraint, and is facing the dilemma that whatever it does from this point, it cannot save the economy or the stock market. That is why economists and strategists, after Bernanke's congressional testimony, have been complaining about the seeming fuzziness of the Fed's goals and its perceived lack of transparency. The Fed simply cannot tell investors what it is going to do and when because it just doesn't know. Overall, it's not a situation that is conducive to continuing strength in the market, and we therefore reiterate our view that it will all end badly.

Charlie Minter, Marty Weiner (Comstock Funds, www.comstockfunds.com)

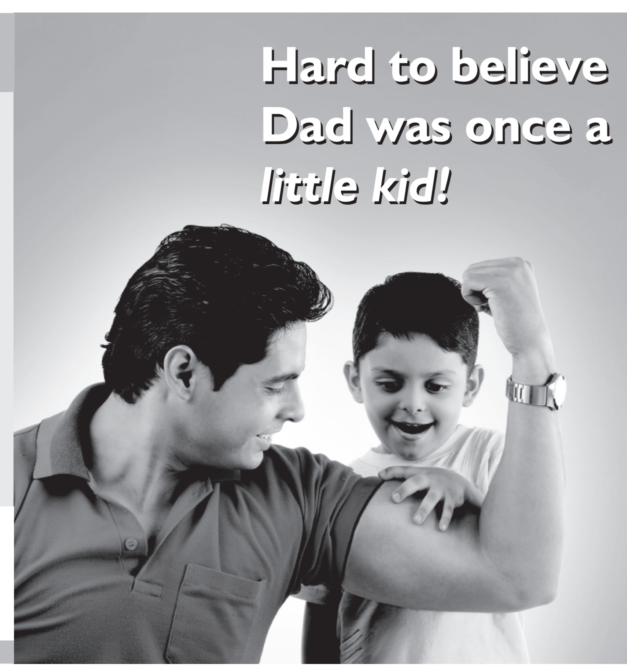
R DIS No.: 2266/06

REGISTRAR OF NEWSPAPERS FOR INDIA No.: TNENG/2007/22771
Postal Registration No.: TN/CH©/132/13-15
Licensed to Post Without Prepayment WPP No. TN/PMG(CCR)/WPP-93/2013-2015

Date of publication: 10th of every month

Registered Newspaper
Posted at : Egmore R.M.S., Patirika Channel.
Posted on: 17/06/2013

If undelivered please return to:
Sundaram Asset Management Company Limited,
Sundaram Towers, II Floor, 46, Whites Road, Chennai-600 014.



Published by Sunil Subramaniam on behalf of Sundaram Asset Management Company Limited, from its office at Sundaram Towers, II Floor, 46, Whites Road, Chennai 600 014.
Printed by R.Velayudhan at Paper Craft, No.25, C.P.Mudali Street, Pudupet, Chennai 600 002.
Editor: Sunil Subramaniam.