

Felix Stephen Podcast Transcript

18 January 2012

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Hi everybody. This is Felix Stephen bringing you my regular market update for you and trust you're keeping well.

It's about quarter past two in the afternoon here in sunny Sydney on Wednesday 18 January 2012. I'm just giving you the time because given the market volatility and so on you'll understand that I'm giving you my thoughts as I see the markets right now.

The macro backdrop, the economic fundamentals all are very supportive of growth assets and I think the trend you're seeing in growth assets reflect that and that's also backed by some anecdotal data showing that there's been a shift out of cash into growth assets, in particular to equities because of the attractiveness of the returns that are available. But it's not a lot. It's a little bit.

Now if you look at some of the indicators in terms of the risk appetite, risk appetite in an aggregate sense is just a shade, a fraction under the level which would say they're in panic. They're still in panic but coming back into more neutral territory.

But what's interesting for me, if I look at the retail investor surveys, the recent surveys show that the bullish consensus is about 49.1 versus a long term average of 39. The bears are at 17.2 versus 30, and neutral's at 33.7 versus 31. Now it actually reflects the reaction that we have seen in the marketplace in the search for yield and a slight uptake of risk given that we are in a risk-on/risk-off regime and the perception of risk is relatively comfortable now in the eyes of, or the belief of most people.

That again is reflected in most of the volatility indices that we are looking at, whether you are looking at the STOXX 50, whether you're looking at the FTSE, the S&P 500, the volatility indices, like the VIX and so on, are telling the same story. The tipping point though, I think, comes to a marketplace when they're getting to levels that are extremes - extreme bullishness or extreme bearishness and the reversal of the trend in the risk-on/risk-off regime can be for a trivial reason or for something substantial. It's almost like the straw that broke the camel's back.

I suspect that we are probably getting closer to a point where the market needs to take a pause and retrace. What's interesting about a pattern of this retracement and rallies and the whipsawing market is that it always happens, nine out of 10 times, when the market expects it the least. I always thought that the end of this month, sometime early February, would be a period where people would refocus on risk because it's all about risk this year, and the returns as we say will work out for themselves. I suspect that we are getting into a period where the risk-off regime is perhaps going to dominate for the next couple of weeks.

But that's not to say that the bull market is over. No, the bull market in growth assets is far from over. I think we still have probably two or three quarters before that is over. What is interesting is that some of the indicators that I watch very closely, the RSIs, the VIX index, the dollar index and so on, are beginning to diverge a fraction away from the overall trend in growth assets. In other

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words, the price movements upwards that you're seeing in equities are not fully discounted or reflected in the volatility indices or the currencies or even bonds. In fact sovereign bonds, technically, are looking extremely, extremely positive. Although it can be argued they're extremely overvalued.

So put all these things together, I think there is a chance that we might see a pullback or retracement from somewhere these levels. It need not happen today, but sometime very soon. If I look at the technicals though, the US equity market in particular, very strong positive technicals, whether they are looking at the ultra short term or the long term. You have the same in the FTSE. The DAX is somewhat short, medium term positive but long term not that positive. Similar to the ASX 200. And the Nikkei, in fact, is slightly positive in the short term but negative in the medium to long term. The US dollar is one of the very interesting things. It's beginning to show strength, which also tells me that perhaps the risk-off regime is at hand.

So watch that closely and developments in that market will tell you whether you should be waiting for another opportunity if you want to go along, or even if you have to take profits, it's not a bad level to lock in some of those profits and crystallise them.

Remember that this is a risk-off/risk-on regime and volatility and turbulence is part and parcel of what we are going through now. Because as you - as the global economy matures and goes towards eventual slow down in a cycle, the transition from that growth to the slow down phase is even more volatile and that's exactly what we're seeing now.

So, as always, enjoy investing, have fun and take good care of yourselves. Until I speak with you again, bye for now.

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