



*May 17<sup>th</sup> 2016*

***Has money died? US inflation up! Is the real economy about interest rates? UK referendum – more twists and turns – how will this end? Buffet takes a bite of the Apple – will he come back for more? Oil – a castle built on disruptions?***

***Is this “When money dies”? US inflation edging up***

*US core inflation is now running at 1.1 per cent, still well below the central bank’s target of two per cent but improving. We view this under a dual optic. Will the Federal Reserve now raise rates preemptively and if it does what shall this do the real economy?*

***US central bank shall raise rates this year at least once***

*We still see the Federal Reserve as positioned to raise rates again this year at least once. If it does not this is tantamount to admitting that the endless monetary tinkering has gotten us nowhere. This shall be the final consecration of the “bubble economy”.*

***Interest rates irrelevant to “real economy” – this is about availability of credit more than its price***

*As to the real economy, the key factor has not been the level of interest rates but the availability of credit, with banks increasingly constrained by capital requirements this is a long term problem.*

***US stock futures lower – oil thrill starting to fade***

*After a burst of enthusiasm yesterday the US stock futures are lower as investors await a spate of economic data and the FOMC notes tomorrow. Animal spirits are also being kept in check by a slight fall in oil prices as the impact of the supply disruptions starts to ebb.*

***Are disruptions becoming permanent?***

*We are starting to see a shift in investor perception where disruptions are starting to be seen as permanent. This raises the issue of who is running the oil market – the guerillas in the Nigerian Delta or Saudi Arabia? Shall a collapse in bloodshed of the Venezuelan regime echo the Iranian revolution in 1979?*

***UK referendum so important – whole world should vote!***

*Attention continues to be riveted on the upcoming UK – EU referendum. We believe that this is so important that the principal of “universal suffrage” should be applied in the literal sense of the word – the whole world should vote!*

***UK inflation data disappointing – what next for monetary policy?***

*Sterling had a slight bounce as the “remain” camp seemed to be edging forward but volatility remains high. The exit jitters are being compounded by disappointing inflation data – with the UK almost in deflation.*

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***Low inflation or deflation in economies where leverage is a way of life – see the UK housing sector – may make for an ill wind.***

***Italian GDP revised downwards – fighting a multi-front battle***

*Turning to the Euro Zone, we are not surprised to read of the Italian statistical office positing 1.1 per cent GDP growth in 2016. The Italian economy is fighting a multi-front battle with most of the difficulties structural, limiting upside in the event of a cyclical upswing.*

***Forecasts shall be revised downwards again***

*It is likely that the growth forecasts shall be once again revised downwards as exports continue to slow. While domestic demand is picking up, this is being fueled by massive discounting as companies opt for cash over profits.*

***US - Buffet counts more than New York manufacturing***

*With regard to the US – increasingly seen as the “last redoubt” of the global economy, yesterday’s Empire State miserable manufacturing data was brushed off by firmer oil prices and by Buffet’s purchase of Apple shares.*

***Warren Buffet sinks teeth into “The Apple” – Apple in G-20!***

*The US market took off yesterday with a vengeance following Warren Buffet taking a big bite out of the “Apple” signaling confidence in the market bellwether and global economic indicator.*

***Apple in G-20!***

*We have long argued that as at the Congress of Vienna in 1815, which recast Europe, we need to also recast the G-20 and include leading corporates. Apple’s results have a greater impact than French GDP.*

***Show me the moat!***

*The purchase is in line with Buffet’s traditional investment approach, focused on companies with a substantial “moat”. The “moat” can be either brand or massive barriers to entry. Apple hitherto seems fit both.*

***Can we compare Buffet’s Apple moment to Dimon’s El Alamein purchase of JP Morgan stock in February? Was this a turning point?***

***Focus on the oil price***

***Oil up on disruptions - what about Iran?***

*Markets have recently been lifted by continued strength in the oil price – with disruptions now seen as pushing the market into a short term deficit. Whether this shall be sufficient to offset a chronic excess of supply and prospective increased production by Iran, remains doubtful.*

***Iran has confounded the skeptics and shall do so again!***



*Iran has confounded the skeptics by increasing production far faster than expected. This was prior to improving their infrastructure which gives an indication of the potential ahead. As European banks and investors start to lose their reticence in dealing with Iran, events may move faster than expected.*

***Do not underestimate resilience of US shale!***

*The extent to which higher prices might also strengthen the resolve of the US shale producers may be underestimated. Current prices enable US companies to lock in protection via the options market at prices allowing cash costs break-even.*

***We may be seeing the last dramatic wave of bankruptcies in the US shale patch, with the survivors positioning for a comeback.***

***Oil a case study in political risk – is Venezuela on the brink of total collapse?***

*The present burst of enthusiasm stems not from a concerted pull back but from a perceived peaking of political risk in two key producers – Nigeria and Venezuela. Both of these countries have been floundering for some time. Nigeria has not known how to harness its oil wealth while Venezuela is now also widely seen as a failed state.*

***Asymmetry in perception of Venezuelan risk***

*The Nigerian disruptions have been constant but have historically not had a lasting impact. We see the risk of quasi civil war in Venezuela as a more dangerous outcome which could shake confidence. The Venezuelan situation hitherto seen as a national – regional crisis may soon start having more global repercussions.*

## Research Highlights

May 17, 2016  
Page 4 of 5

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May 17, 2016  
Page 5 of 5

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