AMERGERIS

STOCK AND BOND MARKET FRAGILITY

CURRENT RISKS OF OVER-EXPOSURE TO EQUITY AND BOND INVESTMENTS WITHIN CURRENT, FRAGILE STOCK AND BOND MARKETS

Amergeris analysts find great merit in Marcus Ashworth's Bloomberg article, 28 December 2016, explaining Albert Edward's pessimistic predictions concerning potential, future share and bond values.

All major Stock Markets are at all-time-record-high levels despite all major world economies being locked in *recession* according to all recognized *economic indicators* (see figure I : *Current Levels of O.E.C.D. Unemployment* and figure II : *Current Levels of O.E.C.D. Economic Growth*); this induces inherent Stock Market volatility with significant, potential downside risks to share values, especially since even the B.R.I.C.S. are now experiencing low rates of Economic Growth. *Current, bullish* Stock Markets could all so easily be transformed into catastrophic, *bearish* Stock Markets by any one of many potential, *endogenous* or *exogenous*, macro-economic, stochastic shocks to the interlocked, interrelated, global economic system (or indeed, it may even be a micro-economic event which would trigger *bear markets* to replace the presently-unjustified, illogical *bull markets,* such as the U.S. Department of Justice $7.2 billion fine imposed upon Deutsche Bank for *misselling* residential-mortgage-backed securities, December 2016). Once triggered, *bearish speculation* would continue under its own momentum since Stock Markets clearly have a *perverse* Demand curve; significantly-lower stock Prices would encourage *bearish speculators* to sell in expectation of further, future, falling share Prices who would thus self-fulfil their own self-perpetuating, self-reinforcing expectations (see diagram : Perverse Demand Curve for Speculative Goods).

Potential economic triggers of such *bearish, speculative* selling of stocks include:

- *Quantitative-easing* by *central banks* which has never been at higher levels may be stopped at any moment since it has left all major *central banks* holding record levels of government debt, it has recently been the major tool of *open, expansionist monetary policy/credit ease* which has itself been the major instrument of government, macro-economic policy to combat economic *depression/ slump* within all major economies; the massive *liquidity drain* by the People's Bank of China, CNY 245 billion of Net quantitative-squeezing in one week, January 2017, led to a Chinese inter-bank *freeze* and the P.B.O.C. has recently even temporarily halted trading in Chinese *gilt-edged* bonds on the Shanghai Stock Exchange on 2 separate occasions to avoid massive *speculative* selling of Chinese government bonds.

• Unprecedented levels of government National Debts, post-*banking crisis*, 2008, where untenable levels of *toxic debt* held by *commercial banks*, especially in the U.S.A. and U.K. were transferred *via* domestic government bail-outs into massive government debt, may lead to government debt repayment defaults; these are realistic possibilities, especially, but not only, in Portugal, Italy, the Republic of Ireland, Greece, Spain P.I.I.G.S. since supranational/E.U. *bail-outs* are only temporary-at-best solutions (see figure III : *Current Levels of O.E.C.D. National Debt*).

• *Current* growth in consumer credit, presently underpinning steady levels of household Aggregate Monetary Demand throughout the O.E.C.D. especially in the U.S.A. and the U.K. may be unsustainable when confronted with almost-inevitable increases in interest rates in the foreseeable future.

In addition to these potential, foreseeable, *endogenous* economic triggers of a cumulative, *vicious-circle* effect of global *bearish speculation* in stocks, there are an unlimited number of potential, unforeseeable, exogenous economic triggers which may also lead to a crisis of confidence in share Prices which would create the same self-fulfilling, continuous fall in world-wide equity values caused by resultant *bearish* selling; such as rising oil Prices, either due to renewed O.P.E.C. global hegemony or due to political instability in significant, oil-producing economies, especially in the Middle East. Indeed, potential political volatility in several regions of geopolitical uncertainty may act as an *exogenous* economic trigger initiating *bearish* selling of stocks due to the resultant collapse in investor confidence.

Moreover, bond Prices are clearly inversely related to market interest rates.

Universally-low interest rates in all major currencies have been imposed by *central banks* as an integral part of their *discretionary, credit-ease monetary policies* to stimulate Consumption Expenditure as part of government, economic management/ *reflationary* macro-economic policies to combat *recession/depression/slump*; these *current*, low interest rates have underpinned high bond Prices/buoyant bond markets.

Throughout O.E.C.D. economies, there is significant evidence of foreseeable increases in all national and international, government-managed interest rates:

• Governments may be forced to increase interest rates to maintain ever-larger amounts of necessary *leverage* to finance ever-higher Public Sector Borrowing Requirements and resultant National Debts in the face of ever-lower *credit ratings.*

• Interest rates may also rise as a *discretionary, credit-squeeze monetary policy* in response to inflationary pressures which may arise if powerful Labour unions, such as in France, manage to obtain significant raises in Real wages in compensation for continuously-falling Real wages in the recent past.

• The Federal Reserve Bank may have to increase interest rates as part of a necessary, *restrictionist monetary policy* in response to inevitable inflationary pressures and to finance high levels of Government Expenditure, especially domestic *producer subsidies*, which will be consequent upon the *reflationary fiscal policies* and Protectionism (the Trump *wall* will be a Protectionist *tariff wall*) proposed by the Trump Administration, post-20 January 2017.

Such almost-inevitable increases in interest rates will lead to resultant, concomitant decreases in bond Prices; this initial trigger will induce *bearish* selling of bonds and the same *vicious-circle* effect in bond markets will continue under its own momentum via the same self-perpetuating, self-fulfilling expectations of falling bond Prices until bond yields are equalized.

The Amergeris Investment Team's highly-logical response to these considerable, *current* downside risks within both equity and bond markets is to *crystallize* their many significant gains made in bond and stock valuations and to *hedge* their portfolio Investments against the significant risks to both stock and bond placements which clearly exist in the *current*, dynamic *external environment*; this has been a highly-profitable Investment strategy for them during similarly-turbulent economic conditions in the past and will surely prove so again in the present financial climate.

Neil Hugh Rilett, Non-Executive Director,
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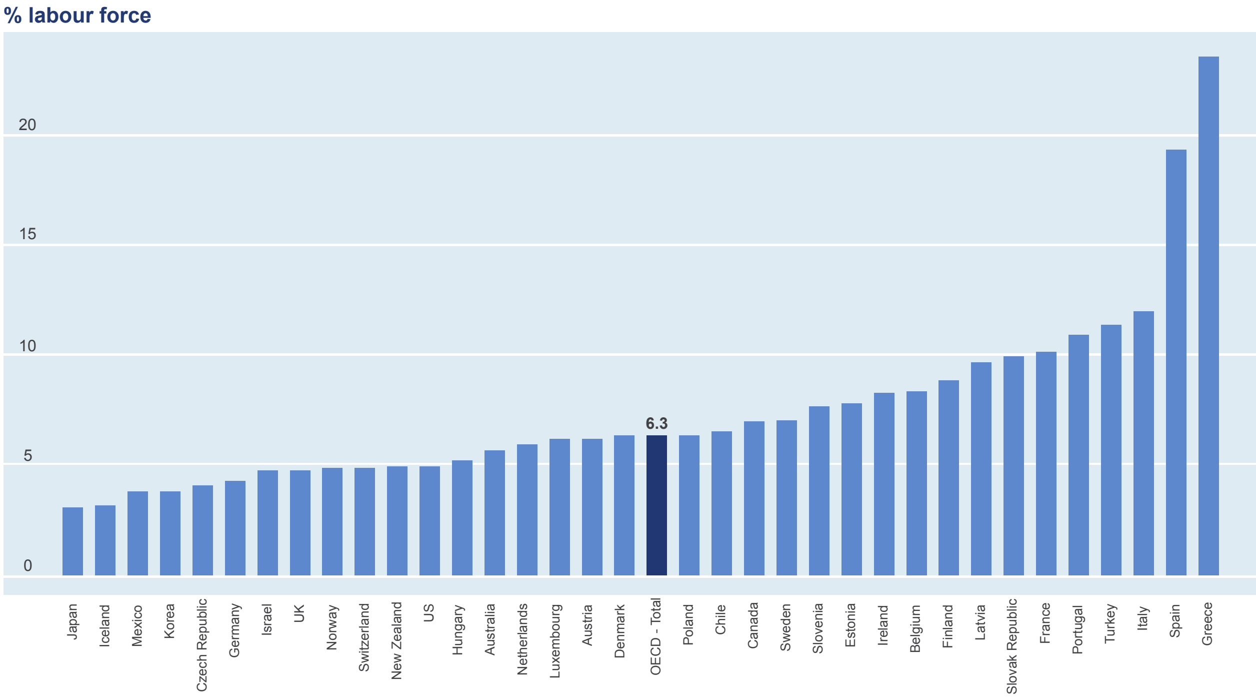
Statistical data/research supplied by M'hamed Lahlou, *Administrateur*, FibreNat S.A. www.fibrenat.ch

Figure I

CURRENT LEVELS OF O.E.C.D. UNEMPLOYMENT

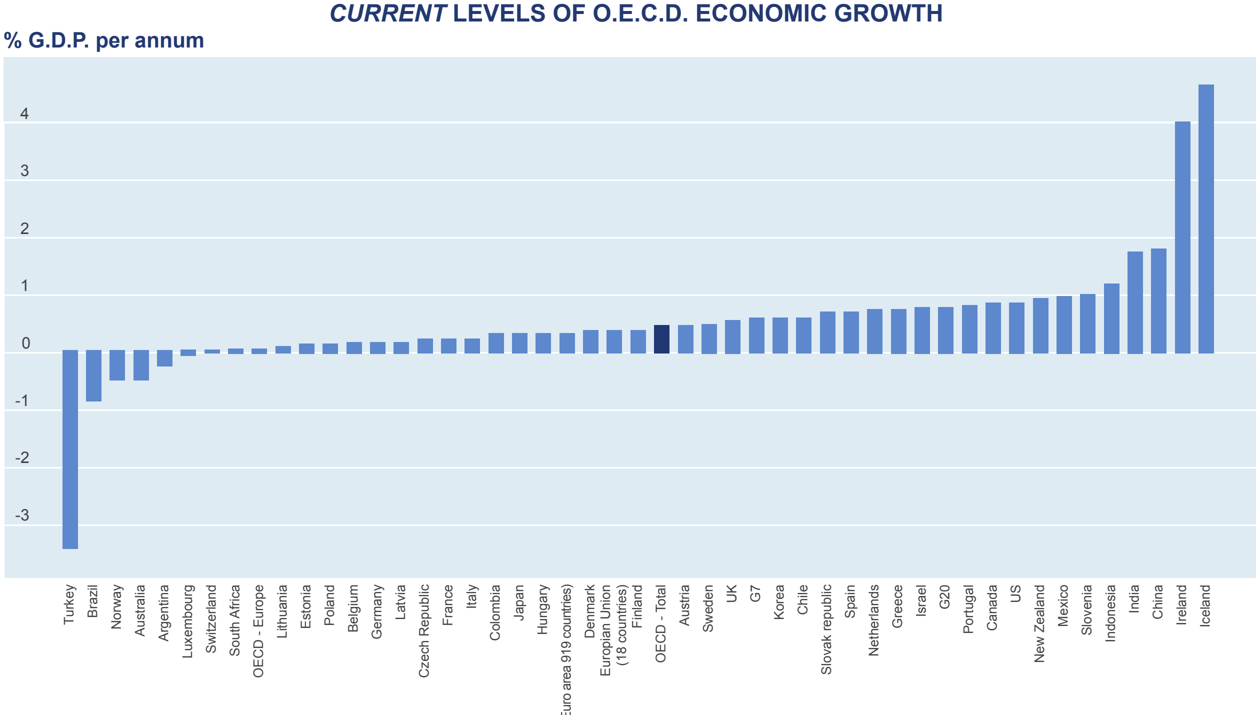


***Note** : National unemployment rates for individual, first-world O.E.C.D. member economies are measured and expressed as percentages of their total labour forces, third quarter, 2016.*

Source : O.E.C.D. Factbook. Economic, Environmental and Social Statistics, 2016. www.data.oecd.org.

Figure II

CURRENT LEVELS OF O.E.C.D. ECONOMIC GROWTH

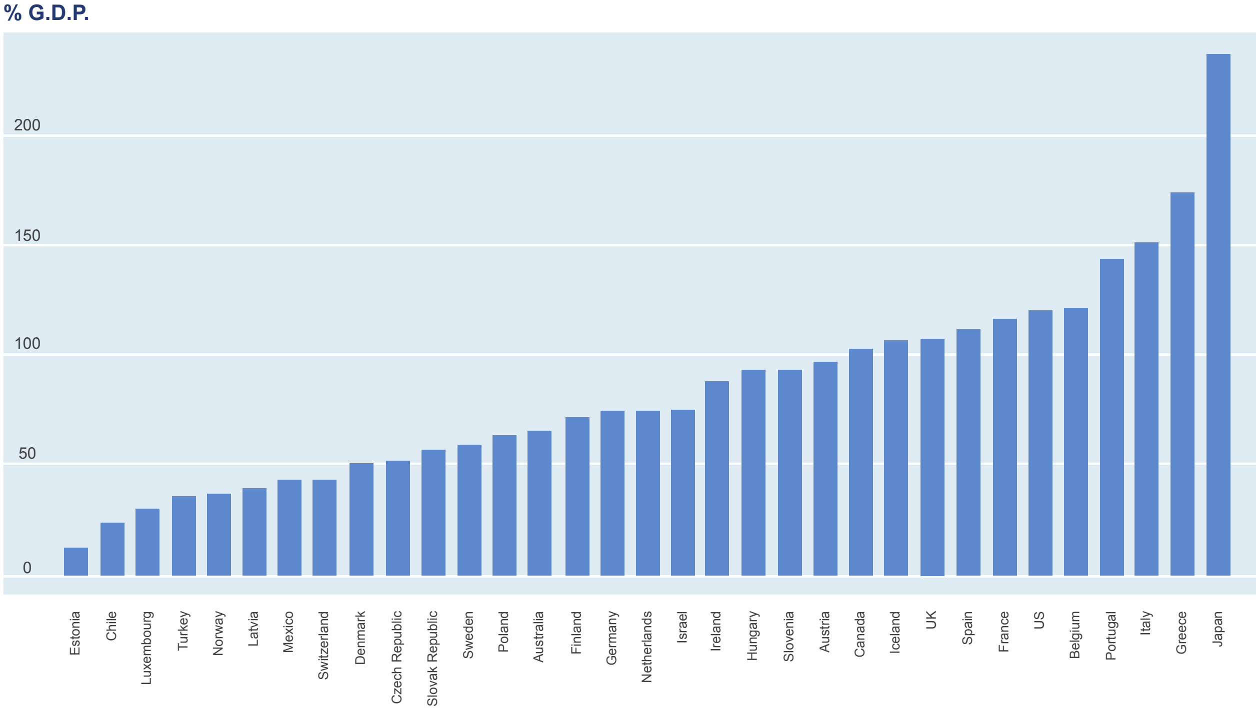


***Note** : National rates of Economic Growth for individual, first-world O.E.C.D. member economies are expressed as seasonally-adjusted, annualized percentage changes of Gross Domestic Product G.D.P. third quarter, 2016, measured from the previous quarter and from the same quarter of the previous year.*

Source : O.E.C.D. Factbook. Economic, Environmental and Social Statistics, 2016. www.data.oecd.org.

Figure III

CURRENT LEVELS OF O.E.C.D. NATIONAL DEBT

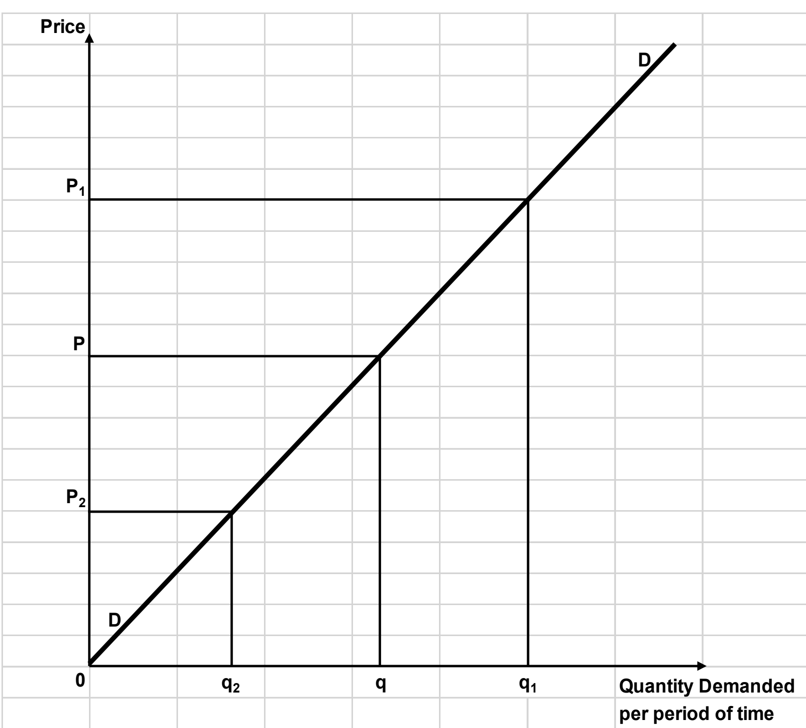


Note *: Domestic levels of National Debt for individual, first-world O.E.C.D. member economies are measured as the amount of a country's total, general, Gross government debt expressed as ratios/percentages of their Gross Domestic Product G.D.P. 2015.*

Source : O.E.C.D. Factbook. Economic, Environmental and Social Statistics, 2016. www.data.oecd.org.

Figure IV

PERVERSE DEMAND CURVE FOR SPECULATIVE GOODS



Perverse Demand curves are unusual and only exist in exceptional cases, such as speculative products; securities/ stocks/shares are speculative goods as a result of the expectations effects of bullish and bearish speculators.

P ↑ P - P₁ → Demand expands q - q₁
P ↓ P - P₂ → Demand contracts q - q₂

When Prices rise, bullish speculators/bulls buy more in expectation of further, future, Price rises i.e. speculative Demand expands.

When Prices fall, bearish speculators/bears buy less/sell in expectation of of further, future, Price falls i.e. speculative Demand contracts.

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