ARVEST

March 2012 | Issue no. 84

Investor Info

Investment Commentary

Stock market rally already over?

Stock markets have recovered strongly in recent months. This investment report shows how profits can be made on such market developments by making anti-cyclical investments. The current economic environment is also examined and an outlook for the full year ventured.

In the October 2011 investment report I pointed out that there are attractive buying opportunities when care is taken in selection. This investment report was published on cash.ch. The reaction to it in the form of readers' comments was consistently negative, because stock markets also trended lower a few days after publication.

Regular readers of my investment reports know that ARVEST never suggests short-term trading ideas and will also not do so in the future. Why? Because short-term trading ideas represent nothing more than pure speculation and are therefore diametrically opposed to ARVEST's investment philosophy. ARVEST always adopts a long-term investment horizon in managing assets. This implies making investment decisions although or even when the market mood is negative, as it is precisely during these phases that shares can typically be bought at cheaper prices. It goes without saying that markets are volatile during these periods, and therefore investors who accept such a strategy must also be prepared to tolerate fluctuations in the value of their portfolios over the short-to medium-term. In the meantime it has become apparent that October 2011 was actually a very good time to invest.

The chart below shows that the SMI (grey line) has risen by +11% since the beginning of

October 2011[1]. The ARVEST Global Stars Fund managed by myself and invested worldwide increased by +14% in the same period. At +18%, the S&P 1200 (red line) performed even better.

The negative feedback on my recommendation to increase the portfolio equity weighting in October has convinced me even more at this point that it was the right time to have increased the equity market risk in the portfolio. The more pessimistic market participants are, the cheaper prices become for buying equities. Although dealing in securities may also often seem complicated, success on the stock exchange is still ultimately based on the banal strategy of

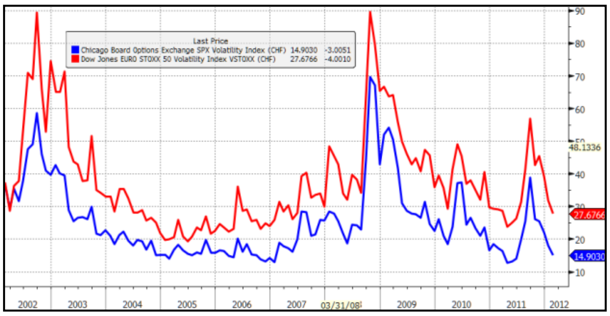
---

[1] up to 28.02.2012

buying low and selling high. No more and no less.

What now?

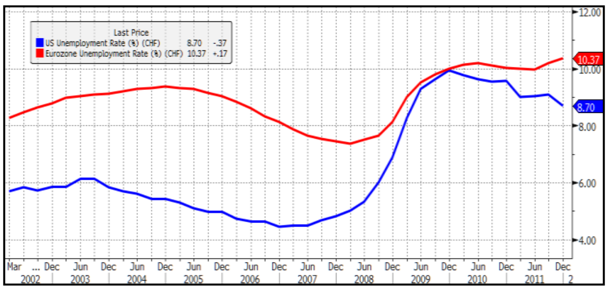
Currently, market conditions seem to be improving again. As can be seen in the next chart, volatilities have again fallen sharply



since October 2011 both for Europe (red line) and the USA (blue line) on rising stock markets and are again at typical levels prevailing prior to the financial crisis.

Monetary policy is one of the reasons underlying the stock market rally. Investors are still expecting an increase in inflation due to the quantitative easing implemented by the central banks. However, liquidity is not flowing into the private sector due to the balance sheet reconstruction required in the banking system, but, in combination with the low-interest policy that has made investing in bonds unprofitable, is being invested in riskier assets such as equities, at least temporarily.

Furthermore, even data on the real economy, which was better than expected, contributed to the stock exchange rally.
Contrary to the views of many pessimists the unemployment rate (blue line) continued to fall



in the USA and shows that the economy could again be on a job creation growth path. In contrast, unemployment continues to stagnate at a high level in the eurozone (red line) due to the debt crisis. The decrease in stock market volatility indicates that investors are no longer expecting an endogenous shock that would result from an uncontrolled collapse of Greece.

The rating upgrade of Iceland also fits into this overall picture (rating agencies seem to have not yet completely forgotten about rating upgrades). Fitch is assuming that its economy, severely battered by the financial crisis, will grow again this year by 2.5%, which makes a default appear less likely. With a BBB- rating, Iceland has again achieved the important investment grade status.

However, Japan's industry (like Switzerland's) is still combating a very high exchange rate, which is putting the competiveness of the export-based country under very severe pressure. It appears that the Japanese central bank is now making serious attempts to weaken its own currency. The announcement of an economic programme of JPY 10 billion is beginning to taking effect.

The ARVEST investment committee was prepared in good time for a possible depreciation in JPY. For example, I had already hedged a large proportion of the JPY positions held in ARVEST Global Stars at the beginning of 2012. At the currency level the fund is currently not generating any losses despite the depreciation in the JPY, but is benefiting from the rise in the share prices of export-based companies such as Toyota.

If there are no new unexpected shocks, the ARVEST investment committee continues to see good growth opportunities for stock exchanges in Asia and Europe. However, market values are comparatively high in the USA, which is why greater caution should be exercised there.

28.02.2012
On behalf of the Investment Committee
Beyzade Han, MBA
Fund manager