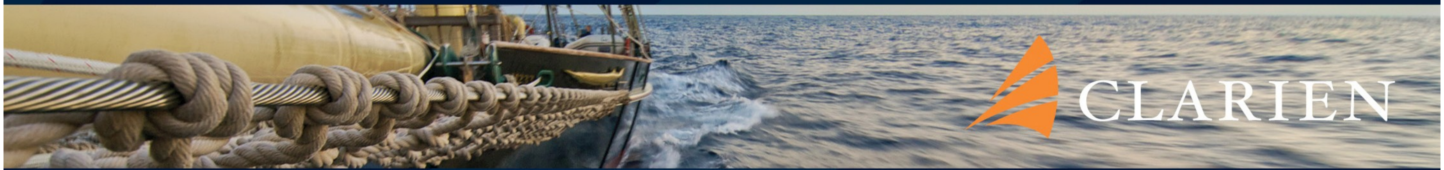

Risk Assets Refueled

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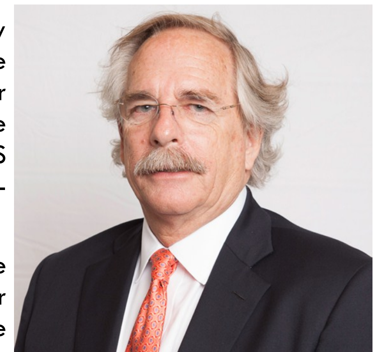
Stimulus can be found in many corners



Thomas Sowanick
Chief Investment Officer

China has now entered into the arena of Central bank monetary policy easing with a surprise cut of interest rates on November 21st. Unlike the European Central bank (ECB) that is trying to stimulate economic growth with easier monetary policy, China is only using interest rates in order to promote corporate refinancing. Regardless of the intention, the results should be nearly uniform globally, ie: higher equity prices and lower sovereign bond yields. What is unclear is whether respective economies will respond to more stimulus.

The ECB is now hinting at purchasing European sovereign debt at the turn of the year which has pushed European yields to new historical lows for many countries.

The strengthening of the US dollar is also having an impact on commodity prices. The CRB Index (Thomson Reuters/ Core Commodity Index) has fallen 16% since June of 2014. Over the same time period oil has fallen by 31%, corn prices by 17%, sugar by 19% and copper by 10%. These lower commodity prices which have now fallen by more than the 10% increase in the value of the US dollar should prove stimulative to consumers worldwide.

The tailwinds of lower commodity prices, lower interest rates, higher equity prices and select fiscal stimulus programs should help to elevate Q1 growth. We are less interested in the level of economic growth but much more interested in consumer confidence and the appetite for risk assets. In other words, we believe Central banks would be more than happy to see confidence levels rising along with equity prices even if GDP growth were to remain lackluster.

As we approach the end of the year, we are saddled with the task of evaluating financial markets for the next calendar year.

While US markets have been market leaders this year due to strong US growth and stable monetary policy against the backdrop of uncertain economic and monetary policy uncertainties abroad (specifically Europe), we suspect that these relationships will likely hold for the first several months of the new year. This will allow the US to provide strong relative performance.

Looking further into 2015, we can envision a shift in demand for European equities at the expense of the US market. To some extent, US financial markets have so far benefited from the Federal Reserve maintaining its zero interest rate policy (ZIRP) "for a considerable period of time". It is our belief that by the end of Q1 or early Q2 of 2015, investors will begin to anticipate the first of many rate hikes by the Federal Reserve.

It is clear that the Bank of Japan (BOJ), the ECB and now the People's Bank of China (PBOC) are all committed to maintaining an easier stance of monetary policy and willing to react more aggressively (if necessary). Record low interest rates in Europe should be sufficient to push investors out of low yielding fixed income instruments in favor of equities should the economy show signs of growth.

As we have argued in recent pieces, the risk to investing in countries that may benefit from further quantitative easing (QE) is their weaker currency. US dollar based investors may want to consider the potential impacts of lower local currencies against the back drop of rising local equity prices. The US dollar could very well surprise to the upside if the Federal Reserve were to move even modestly faster relative to current expectations.

The S&P 500 Index which has enjoyed a double digit return so far this year, could very well see another solid year of equity returns in 2015. Nonetheless, we think that Europe can overpass the S&P 500 Index in the second half of the year.