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# Weekly Market Summary

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## The Art of Forecasting ... And a Precious Leonardo da Vinci Art Work !!

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Financial markets are characterised by a large number of participants with different appetites for risk, different time horizons, different motivations and reactions to unexpected news, though a similar and common objective: Acing the next big market move and generating superior returns! As a result, the mathematical techniques and models used in the forecasting of financial markets have grown ever more sophisticated as traders, analysts and investors seek to gain an edge on their competitors. That includes - amongst other things - modelling with high frequency data, applying genetic algorithms to financial time series and analysing autocorrelations and variance ratio tests.

In his bestselling book entitled "*Forecasting Financial Markets ..The Psychology of Successful Investing*", the author - Tony Plummer - details the three dimensions essential to achieve successful trading, including an ability to understand the forces at work in logical terms, recognize (and neutralize) any emotional responses to market fluctuations, and design an investment process or trading system that generates objective 'buy' or 'sell' signals. Tony also provides a compelling insight into the psychology of trading behaviour and shows how "*following the herd*" can have disastrous results, whilst also demonstrating how one's ability to make money in the world's financial markets depends critically on his/her ability to make decisions independently of the crowd and irrational emotions.

Overnight, Goldman Sachs announced the first seven of their recommended Top Trades for 2018. These trades usually represent the Bank's Top Ten Market Themes for the year ahead. They are also in line with some of GS' highest conviction market expressions of the economic outlook that was laid out in their latest Global Economics Analyst ("*As Good As It Gets*", Global Economic Analyst, November 15<sup>th</sup>, 2017), as well as in their Top 10 Market Themes for 2018 ("*Late-Cycle Optimism*", Global Markets Analyst, Nov. 16<sup>th</sup>, 2017). Some of the key market themes reflected in GS' trade recommendations include:

- **Strong and Synchronous Global Expansion:** GS forecast global GDP growth of around 4% in both 2017 and 2018, suggesting that next year's global economy will likely surprise on the upside of consensus expectations.
- **Relatively Low Recession Risk:** Given the low inflation and well-anchored inflation expectations across developed market economies, GS thinks central banks have little reason to risk '*murdering*' this expansion with the kind of aggressive rate hikes that would have historically been warranted to fight the risk of inflation becoming entrenched.
- **But Relatively High Drawdown Risk:** Even if growth remains strong in the coming year, markets are still susceptible to temporary drawdowns, especially given the high level of valuations. GS reckons the two most prominent risks to markets in 2018 are (1) pressures on US corporate margins from rising wages and 2) a swing in market psychology around the withdrawal of QE, which could lead to a faster re-pricing of interest rate markets than we assume.
- **More room to grow in Emerging Markets (EM):** While most developed economies are currently growing well above potential, most emerging market economies still have room for growth to accelerate in 2018.

**Top Trade #1:** Position for more Fed hikes and a rebuild of term premium by shorting 10-year US Treasuries (last at 2.36%).

**Top Trade #2:** Go long EUR/JPY for continued rotation around a flat Dollar (last at 132.75)

**Top Trade #3:** Go long the EM growth cycle via the MSCI EM stock market index.

**Top Trade #4:** Go long inflation risk premium in the Euro area via EUR 5-year 5-years forward inflation (last at 1.675%).

**Top Trade #5:** Position for 'early vs. late' cycle in EM vs the US by going long the EMBI Global Index against short the US High Yield iBoxx Index.

**Top Trade #6:** Own diversified Asian growth, and the hedge interest rate risk via FX relative value (Long INR, IDR, KRW vs. short SGD and JPY).

**Top Trade #7:** Go long the global growth and non-oil commodity beta through long BRL (Brazilian Real), CLP (Chilean Peso), PEN (Peruvian Sol) versus short USD.

In a late-February 2016 market summary, entitled "*No Straight Answers to Recent Market Carnage .. Better Ask the Red Indian Chief*", I did point out that market visibility at times could become so little, that even the "*crème de la crème*" Goldman bankers (the house that always wins .. or otherwise gets immediately bailed out whenever proven wrong!) become under pressure to abandon few or all of their projected trades for the new year within a very short period of time! Whether a similar scenario materializes again in 2018 remains anyone's guess!

Elsewhere, whilst analysts/speculators continue assessing the increased volatility and future direction of bitcoin prices - which staged a spectacular recovery in the past 24 hours following a dramatic sell-off last Monday (effectively climbing within a few dollars short of a record \$ 8,000 just days, after a plunge of as much as 29% from the previous high - to a low of \$ 5605 on Monday - tested the confidence of advocates of the cryptocurrency!) - a piece of art was being "quietly" sold at an exorbitant price! The last Leonardo da Vinci painting in private hands was sold for US\$ 450 million on Wednesday evening after a fevered, 19-minute round of bidding at Christie's in Manhattan, shattering the record for the most expensive piece of art ever sold. "*Salvator Mundi*", Latin for "*saviour of the world*", is one of roughly 15 surviving works by Da Vinci and depicts Jesus Christ in a flowing robe, holding a crystal orb and raising his right hand in benediction. The 67.5 cm tall portrait, painted around 1500 and once owned by King Charles I of England, was presumed lost until its rediscovery in 2005. Jussi Pylkkanen, auctioneer for the evening, opened bidding at US\$ 70 million. There were gasps throughout the saleroom in the Rockefeller Centre when it hit US\$ 200 million. The undisclosed buyer was represented on the phone by Alex Rotter, Christie's co-chairman of post-war and contemporary art. "*It was wild,*" Mr Rotter told the Financial Times about representing the buyer over the phone. "*It was one of the experiences of a lifetime.*" The US\$ 450 million figure includes US\$ 50.3 million of premiums paid by the buyer to Christie's for its services. And to think that a small group of critics have questioned the painting's authenticity - referring to it as a fake, or piece of junk!!



Leonardo Da Vinci's *Salvator Mundi*, which sold at Christie's on Wednesday for \$450 million (Source: Christie's)

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