



Ineichen Research and Management ("IR&M") is a research firm focusing on investment themes related to absolute returns and risk management.

17 May 2013

www.ineichen-rm.com

Alexander Ineichen CFA, CAIA, FRM
+41 41 511 2497
ai@ineichen-rm.com

"It's pretty shocking data. The figures for Italy, Spain and France are very worrying... There's a very, very strong case for aggressive monetary relaxation across the eurozone now."

—Simon Tilford, Economist at the Centre for European Reform*, Financial Times, 2 May 2013

*European Reform: arguably an oxymoron

Update

Risk management research

Pretty shocking

	page
• Global economic growth is low but stable.	3-6
PMIs are marginally below 50 and are falling but not collapsing.	7-8
Business sentiment is falling with consumer sentiment rising.	9-10
• US economy is improving, consumer sentiment shocking positively; with a red flag here and there though.	10-18
• European economy remains in recession.	19-26
• China's economy is either at an inflection point or in decline.	27-29
• Japan's economy is improving, cost of capital is rising.	30-32
• Inflation is falling, deflation currently the bigger risk.	38
• Bond valuation is lofty: If you think equities were in a bubble in 2000, try bonds now.	39
• Equity valuation : is lofty too.	40
• Abenomics : A collapsing Yen in 1995-97 was the precursor to the Asian crisis that followed.	48

Summary

Changes vs. last update from 3rd May are circled.
The ratio between green and red changes is 8:4,
i.e., changes are positively biased. Surprises are all
negative.

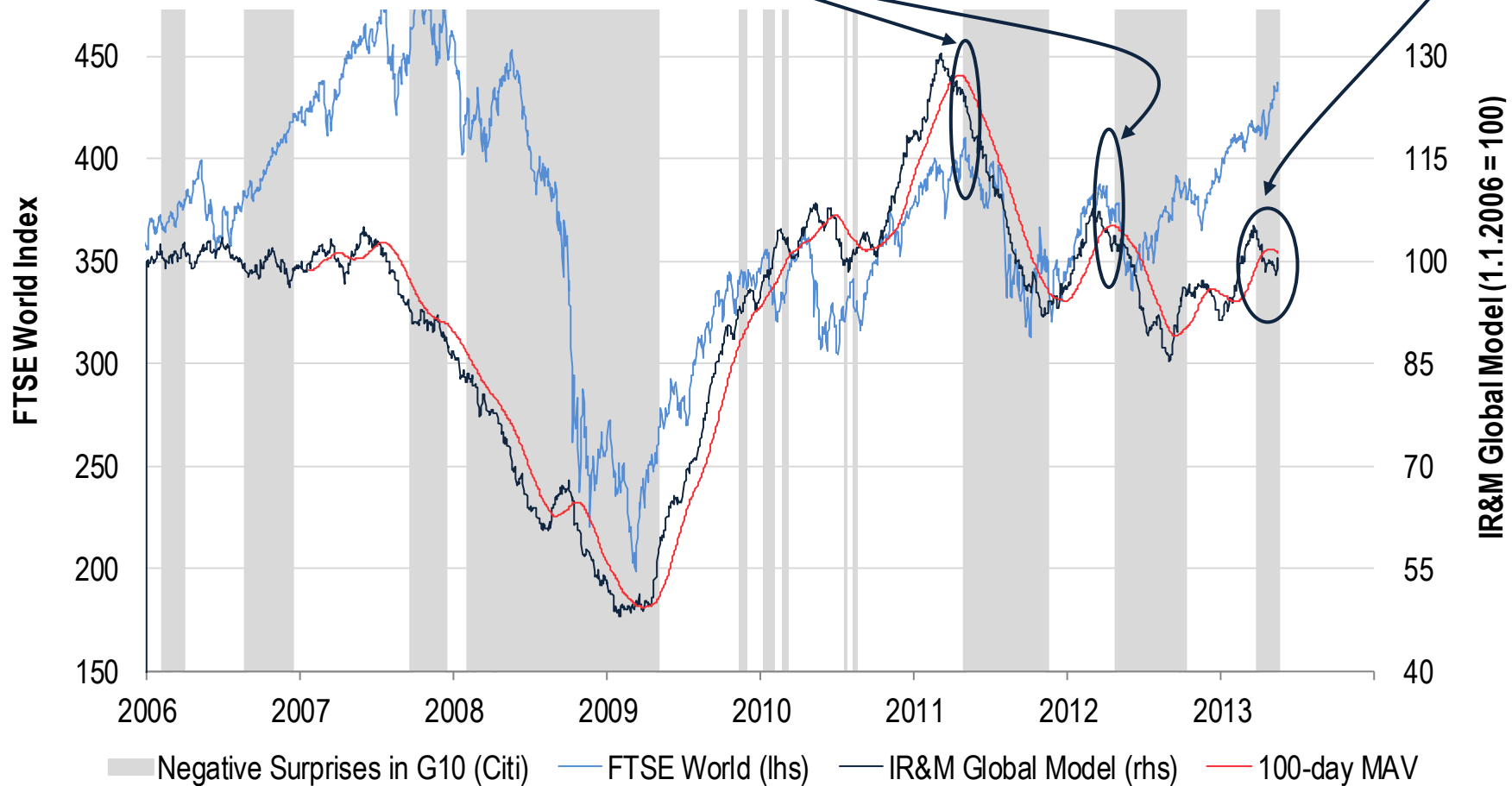
	Fundamentals						Remarks	Technicals		
	IR&M Models				Surprises**	Moving averages				
	Percentile (2006-)	Change*** (3 May 13)	Direction* (10-day)	Average (100-day)		Above average?		50D	200D	50D> 200D?
17 May 13										
Global	57	-0.7	Falling	Falling	No	Negative	At inflection point.	Rising	Rising	Yes
US	93	-1.9	Rising	Rising	No	Negative	Improving.	Rising	Rising	Yes
Europe	47	3.6	Rising	Rising	No	Negative	At inflection point.	Rising	Rising	Yes
Germany	47	0.1	Falling	Rising	No	Negative	Improving, sort of.	Rising	Rising	Yes
France	21	1.2	Rising	Rising	No	Negative	Declining.	Rising	Rising	Yes
Italy	25	2.3	Rising	Falling	Yes	Negative	Declining.	Rising	Rising	Yes
UK	68	3.8	Rising	Rising	Yes	Negative	Improving.	Rising	Rising	Yes
Switzerland	57	1.4	Rising	Rising	Yes	Negative	Improving.	Rising	Rising	Yes
Japan	35	0.9	Falling	Rising	Yes	Negative	Improving.	Rising	Rising	Yes
China	18	-0.4	Falling	Falling	No	Negative	At inflection point.	Falling	Rising	Yes

Notes:

* Direction: average last ten days versus previous ten-day average; ** Surprises are from Citigroup except Germany, France, and Italy (which are our own). *** Change in percentile points relative to date shown in brackets.

Global economy: at inflection point

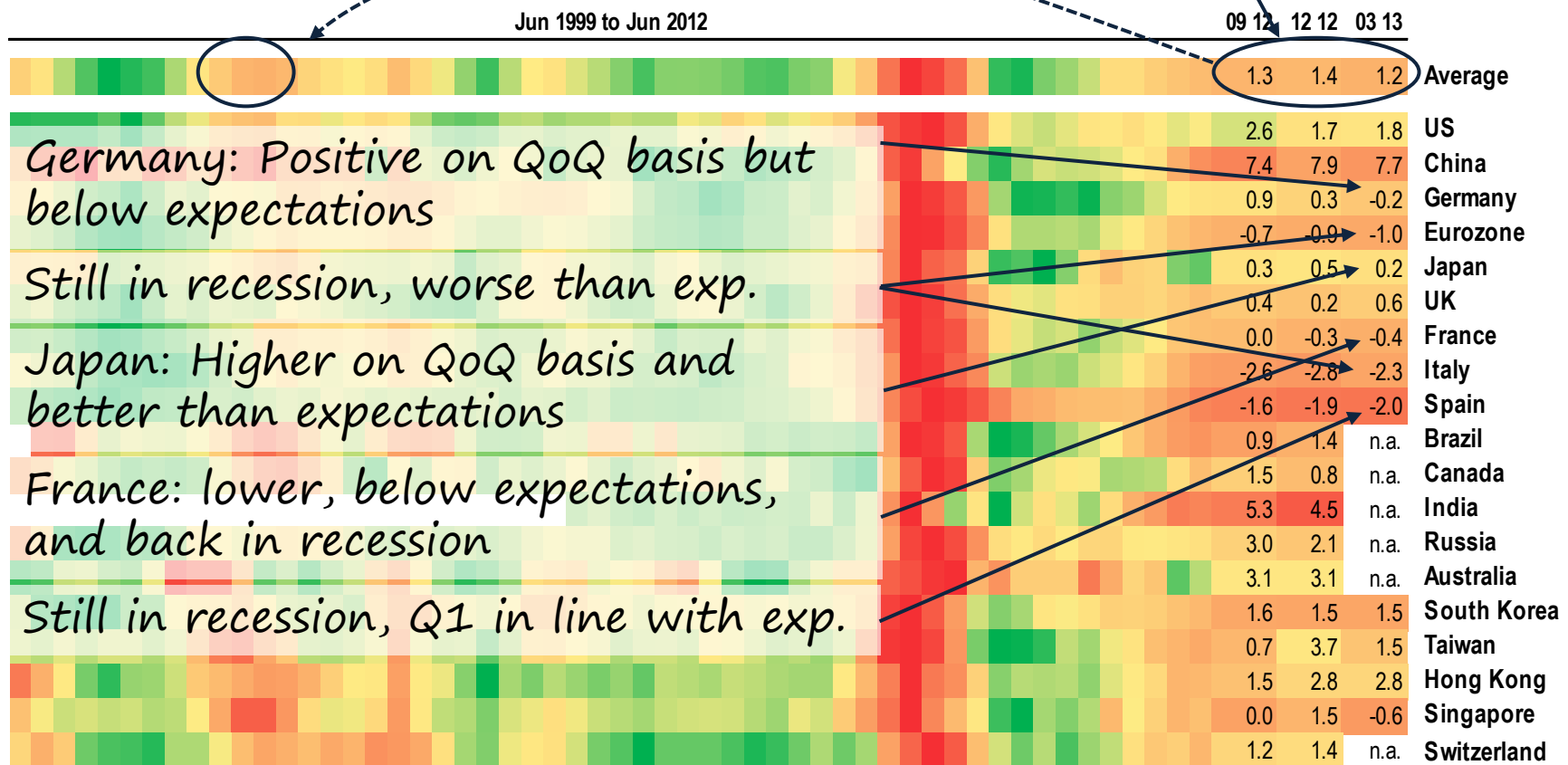
Surprises have turned negative on 28 March. Both in 2011 and 2012 the change from positive to negative was close to an interim peak in the stock market. This time seems different; thanks to helicopter Benny bucks.



Source: IR&M, Bloomberg. Model consists of 20 indicators and is designed to give a data point nearly every day. The model is work in progress.

Global economic growth: low and stable

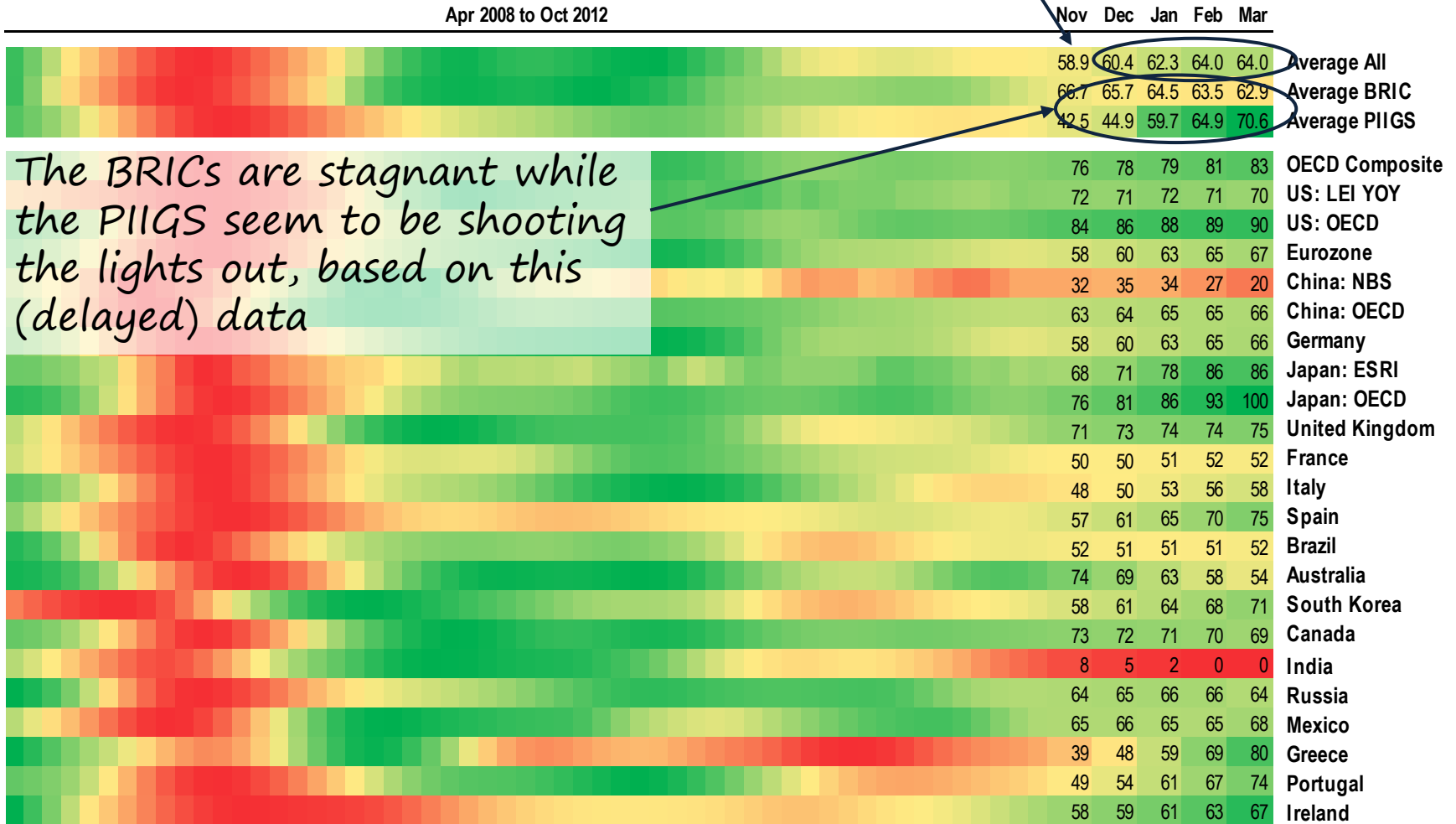
Stable low growth rate, somewhat akin to Q3 2001 to Q1 2002.



Source: IR&M, Bloomberg. Notes: Based on real GDP, SAAR (seasonally adjusted annual rate). The average is equally weighted.

Leading indicators*: improving

Apr 2008 to Oct 2012



Source: IR&M, Bloomberg. Notes: Figures are shown in percentiles. 100 is the highest figure for the period shown (green), 0 the lowest (red). * Leading indicators are often lagging and include stock market performance and changes in the yield curve, ie, are often not "pure".

Industrial output: **not great**

Lower, negative on MoM basis, and below expectations

May 2008 to Jan 2013



Source: IR&M, Bloomberg. Notes: Based on yoy industrial production. Industrial production is generally perceived as a lagging indicator. The average is equal weighted. In the case of a figure not available, the previous one is used to calculate the latest average.

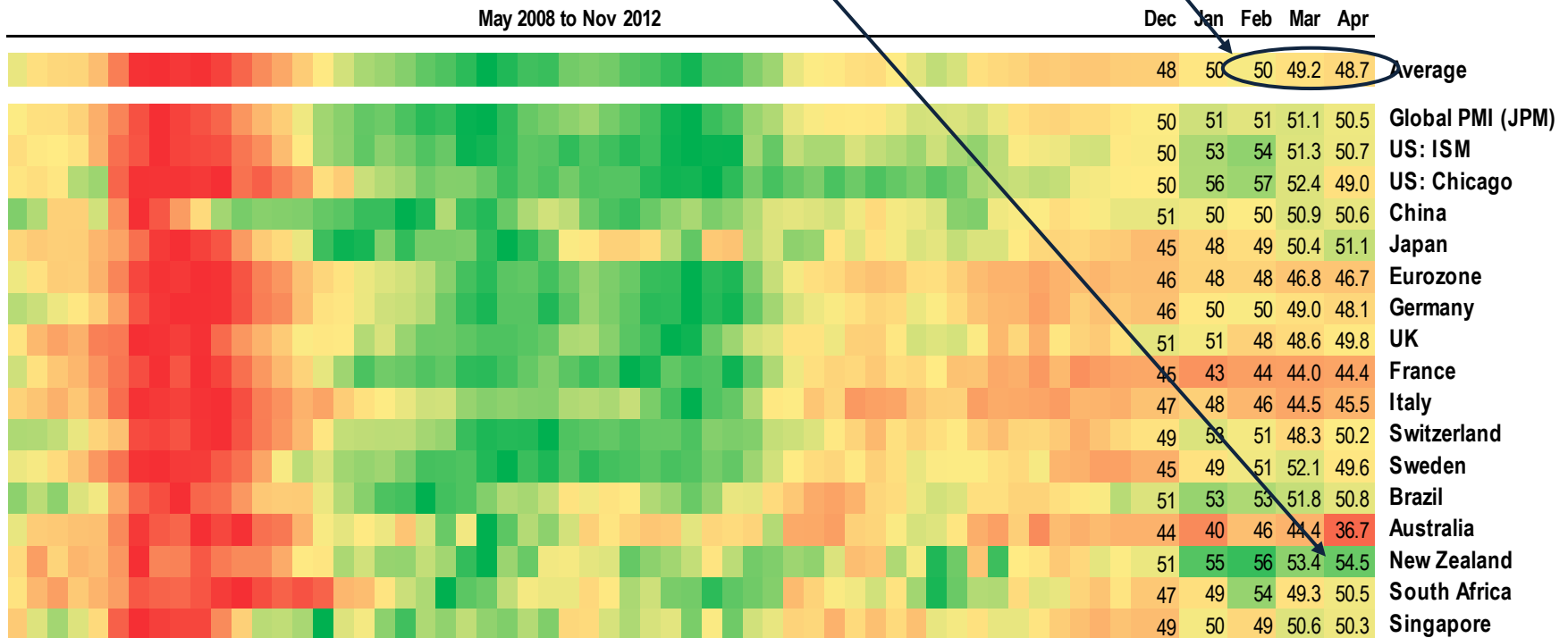


PMI: below 50 and falling*

* A 1.5-point move is one standard deviation (SD).

Higher, highest among peers, and the gap to Australia reaching a new all-time-high at 17.8 since 2002.

May 2008 to Nov 2012



Source: IR&M, Bloomberg. Notes: PMI is a diffusion index. A figure below 50 means economy is contracting. The global PMI is a composite by JPM. The average is equally weighted and excludes the JPM composite. "SD" stands for standard deviation.

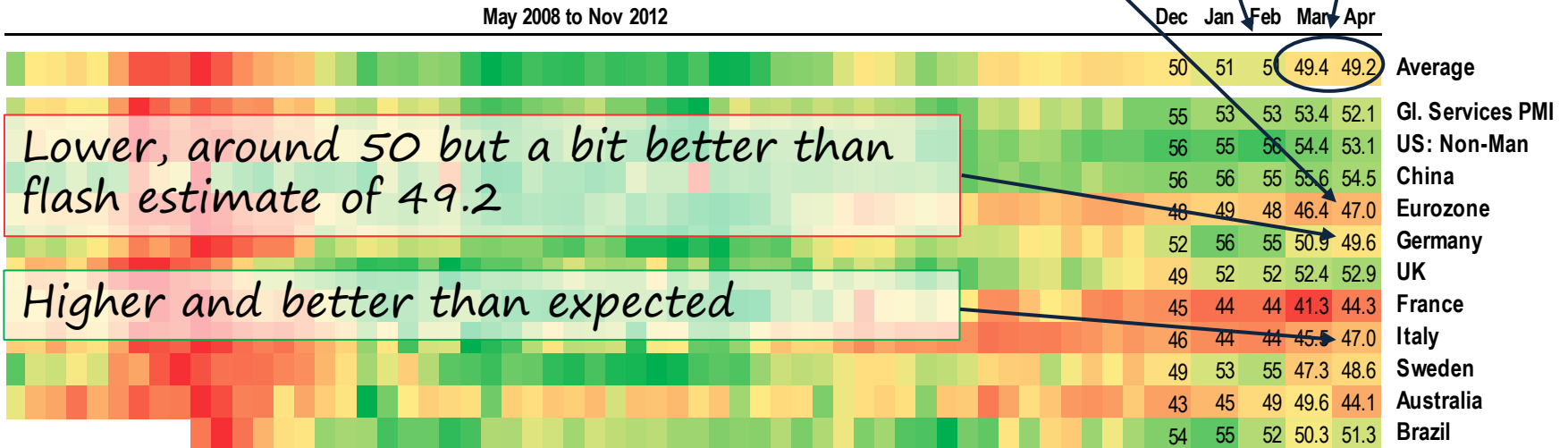
PMI services: below 50 and falling*



* A 1.5-point move is one SD (standard deviation).

A bit higher and a bit better than preliminary (flash) estimate

May 2008 to Nov 2012



Lower, around 50 but a bit better than flash estimate of 49.2

Higher and better than expected

Source: IR&M, Bloomberg. Notes: PMI is a diffusion index. A figure below 50 means economy is contracting. The GI. Services PMI is a composite by JPM. The average is equally weighted and excludes the JPM composite.

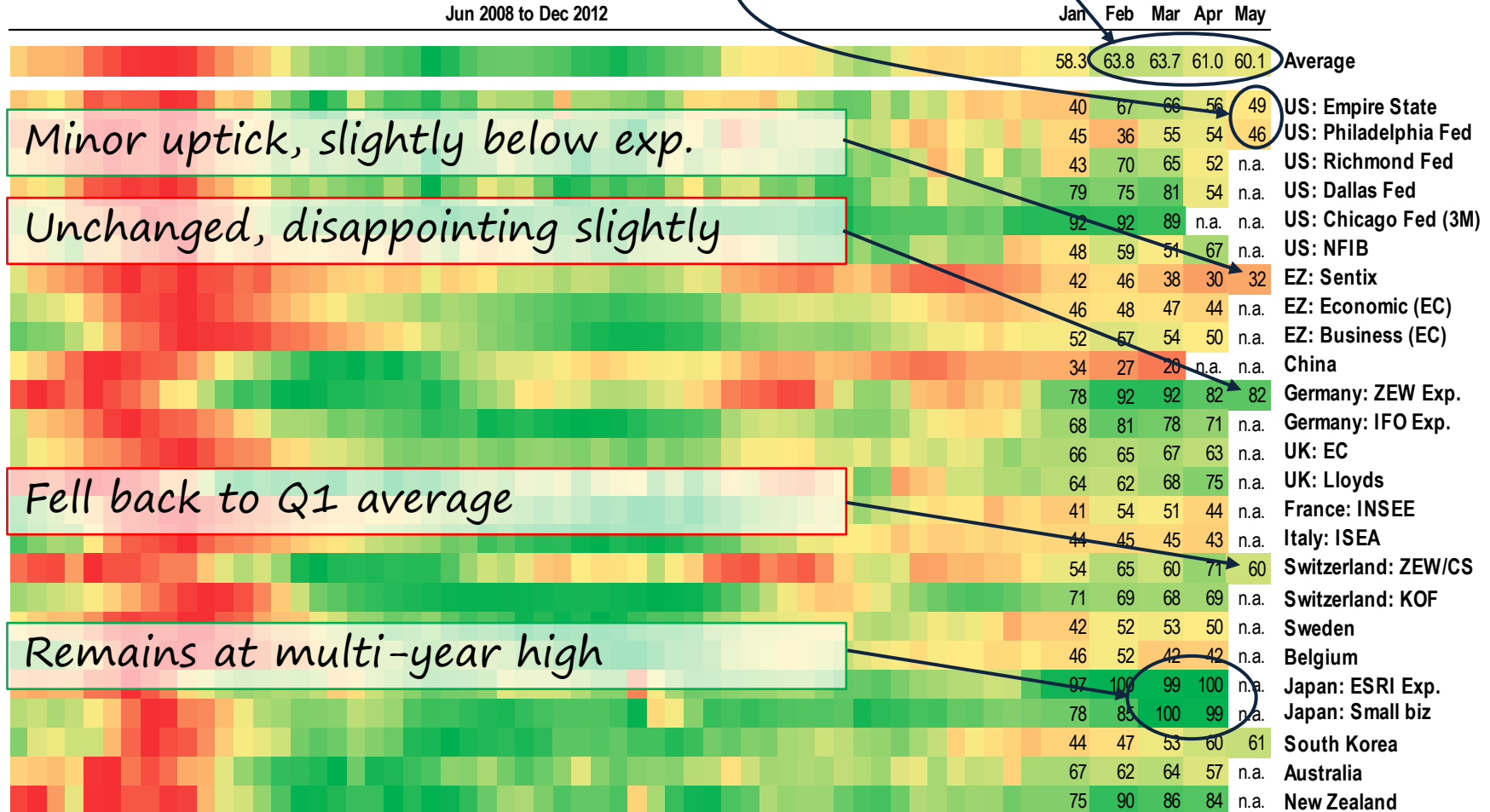
* Based on flash estimates from 23 April. Final estimates due 6th May.

Business sentiment: falling*

Lower, negative and way below expectations

* A five-point move is one standard deviation.

Jun 2008 to Dec 2012



Minor uptick, slightly below exp.

Unchanged, disappointing slightly

Fell back to Q1 average

Remains at multi-year high

Source: IR&M, Bloomberg. Note: Figures are shown in percentiles. The average is equally weighted.

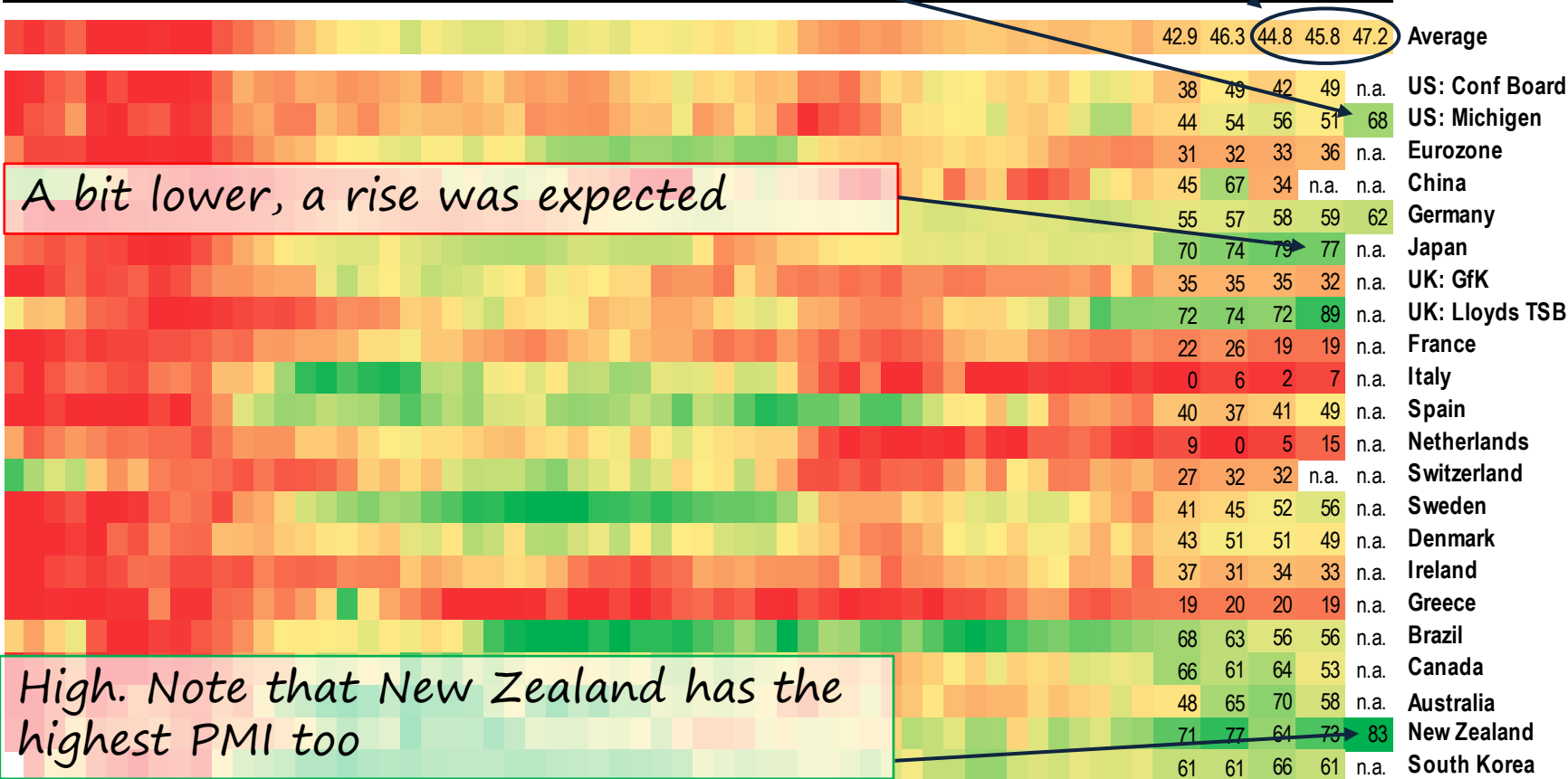
Consumer sentiment: rising*

Pretty shockingly positive and above expectations

* A four-point move is one standard deviation.

Jun 2008 to Dec 2012

Jan Feb Mar Apr May



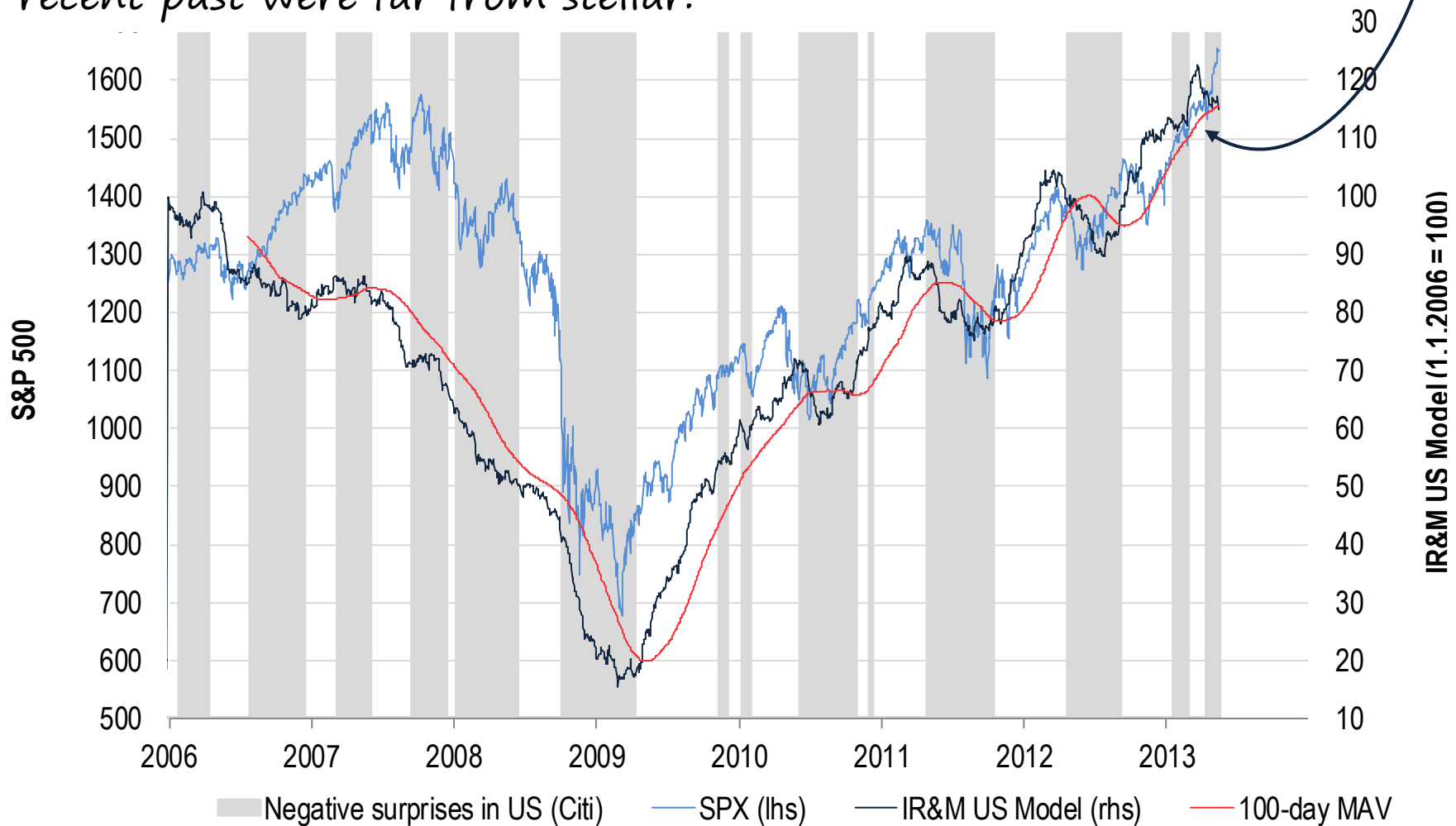
A bit lower, a rise was expected

High. Note that New Zealand has the highest PMI too

Source: IR&M, Bloomberg. Note: Figures are shown in percentiles, ie, high and low over seven years were normalised to 100 and 0. The average is equally weighted.

US economy: improving*

* when judged by the moving average. Surprises have been negative since mid April and various indicators in the most recent past were far from stellar.

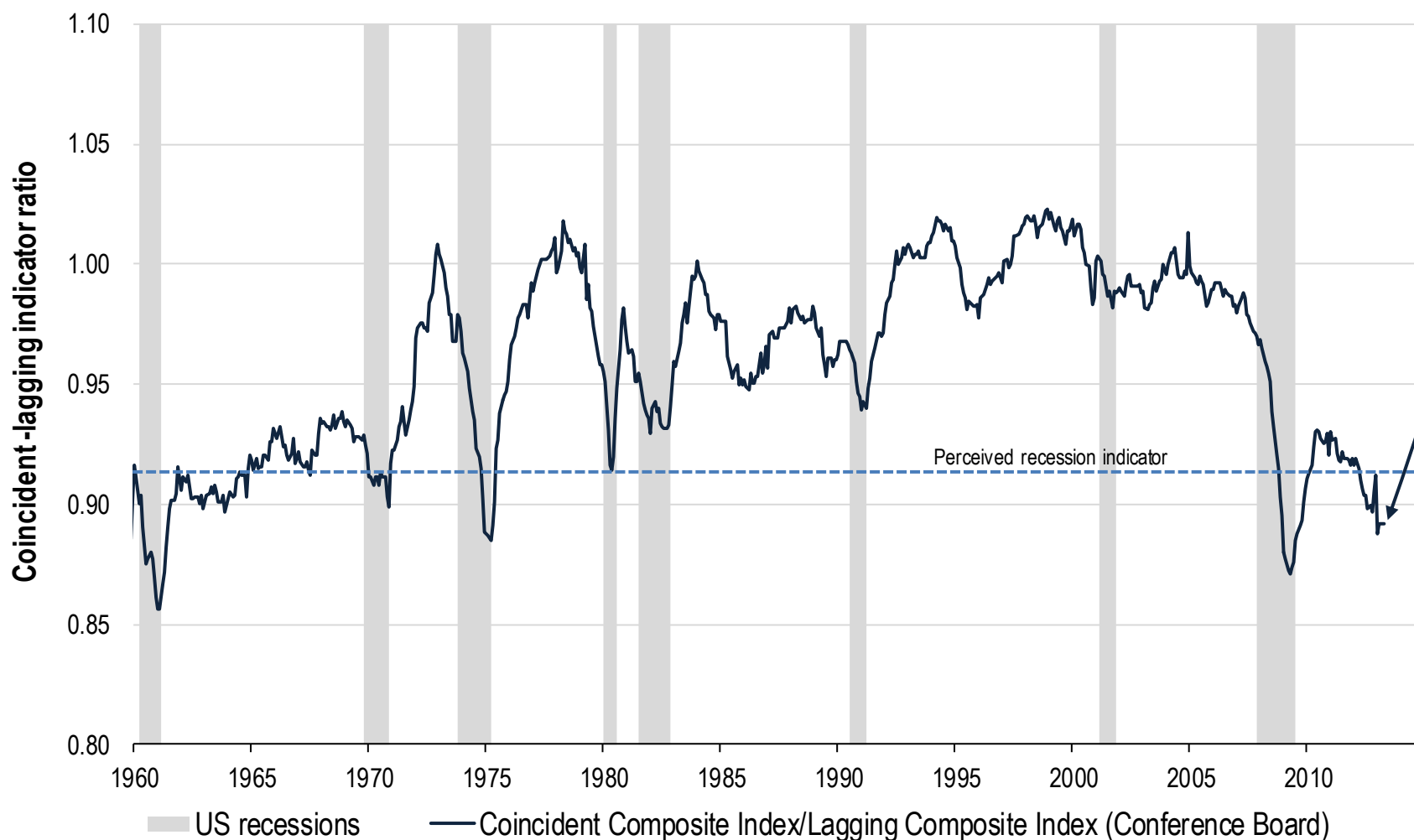


Source: IR&M, Bloomberg. Note: Model consists of three weekly and 15 monthly indicators and is designed to give a data point nearly every day.

US recession indicator: **recession**



This perceived early recession indicator continues to point towards recession.



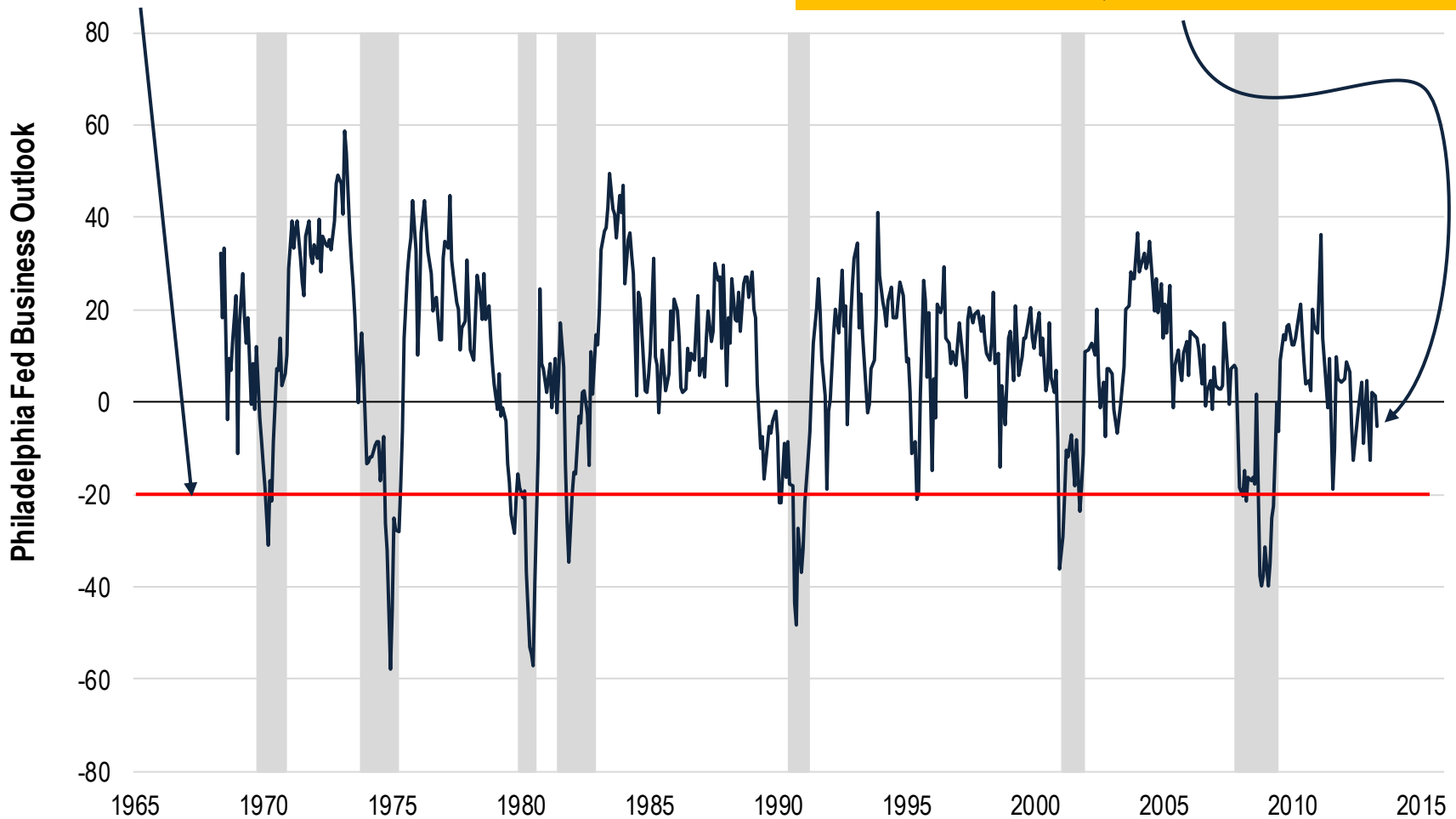
Source: IR&M, Bloomberg, Big Picture

Philly business outlook: **negative**



Fall below -20 nearly guarantees a recession.

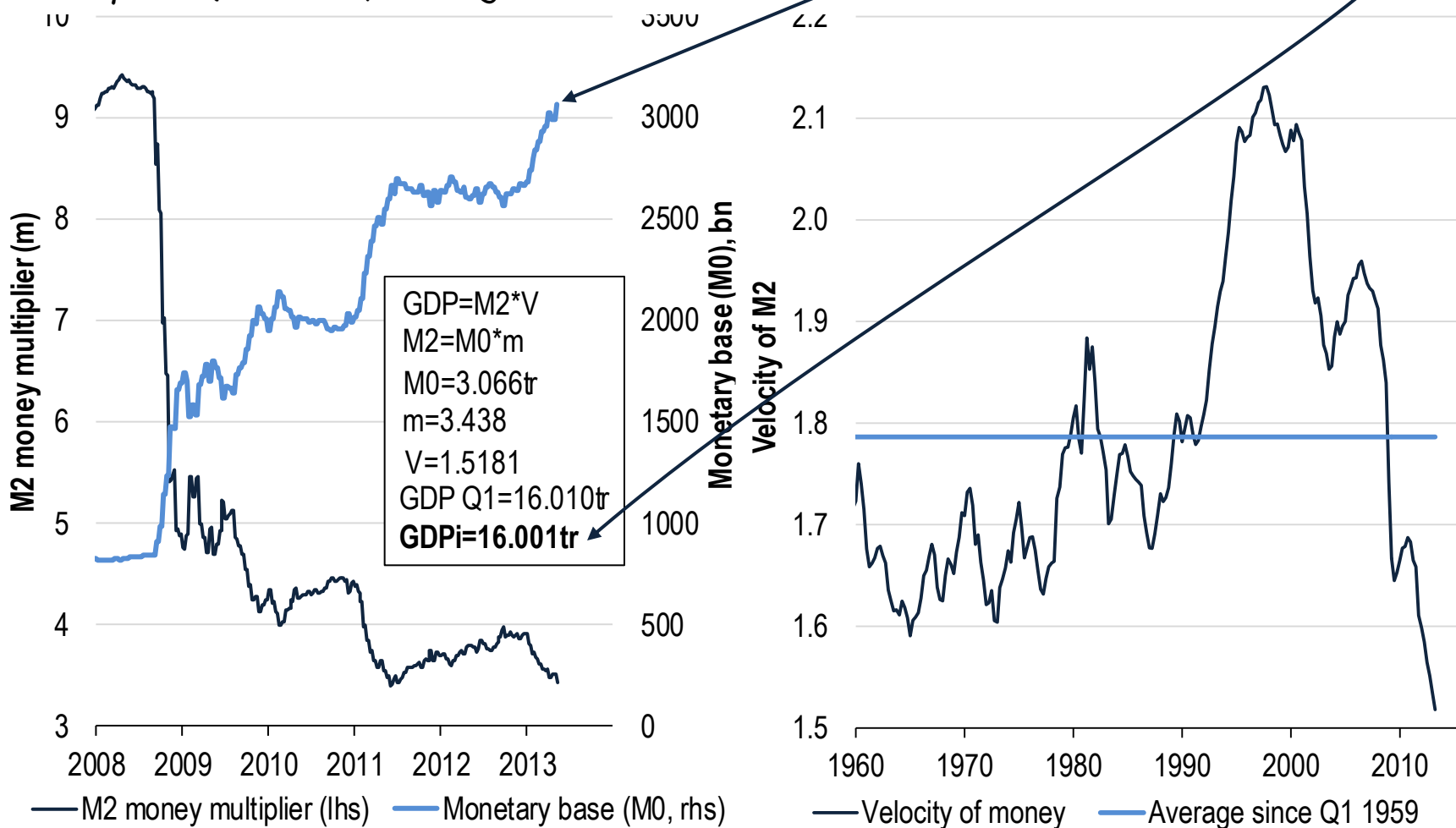
-5.0 for May was negative and worse than expected



Source: IR&M, Bloomberg. Grey areas show US recessions.

US implied GDP: slightly higher

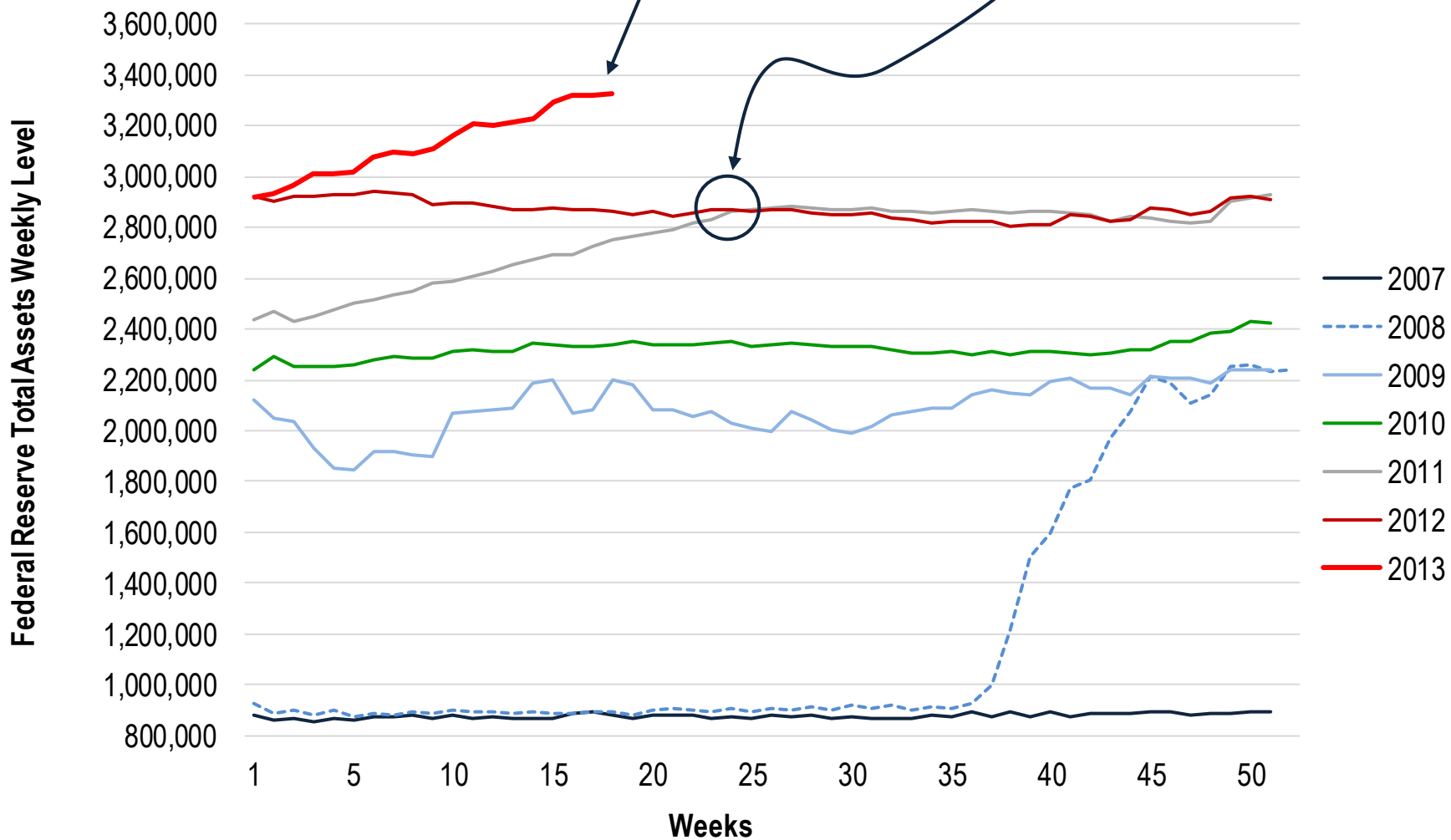
The monetary base (M0) has risen from \$3.025tr to \$3.066tr since our last update. This resulted in a slightly higher implied GDP, despite the multiplier (M2/M0) falling a bit.



Source: IR&M, Bloomberg, Hoisington. M2 is published weekly, M0 fortnightly. This allows us to calculate an implied GDP ("GDPi") given the most recent figure for M2, M0, m, and V (published quarterly).

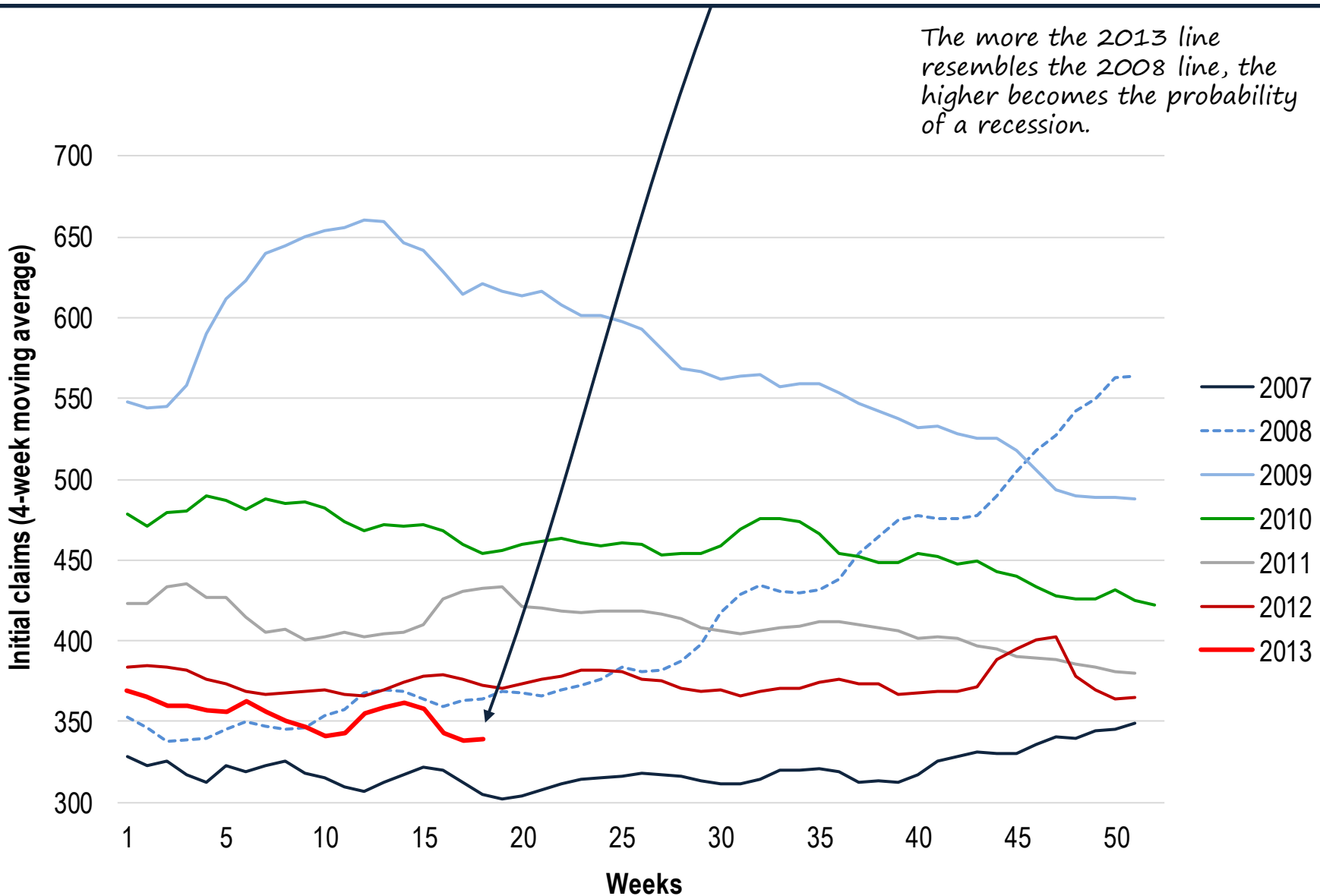
Fed balance sheet: **expanding**

In 2011, the expansion stopped in the calendar week number 26-27, i.e., at the end of June, early July. Risk was off then.



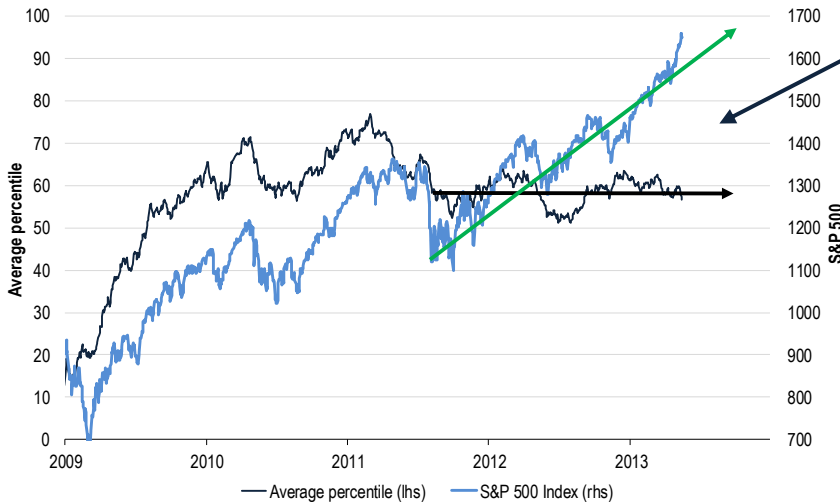
Source: IR&M, Bloomberg.

US labour market: stopped improving



Source: IR&M, Bloomberg. Note: Graph shows 4-week moving averages per calendar year.

US high frequency indicators: stable



The gap is widening.

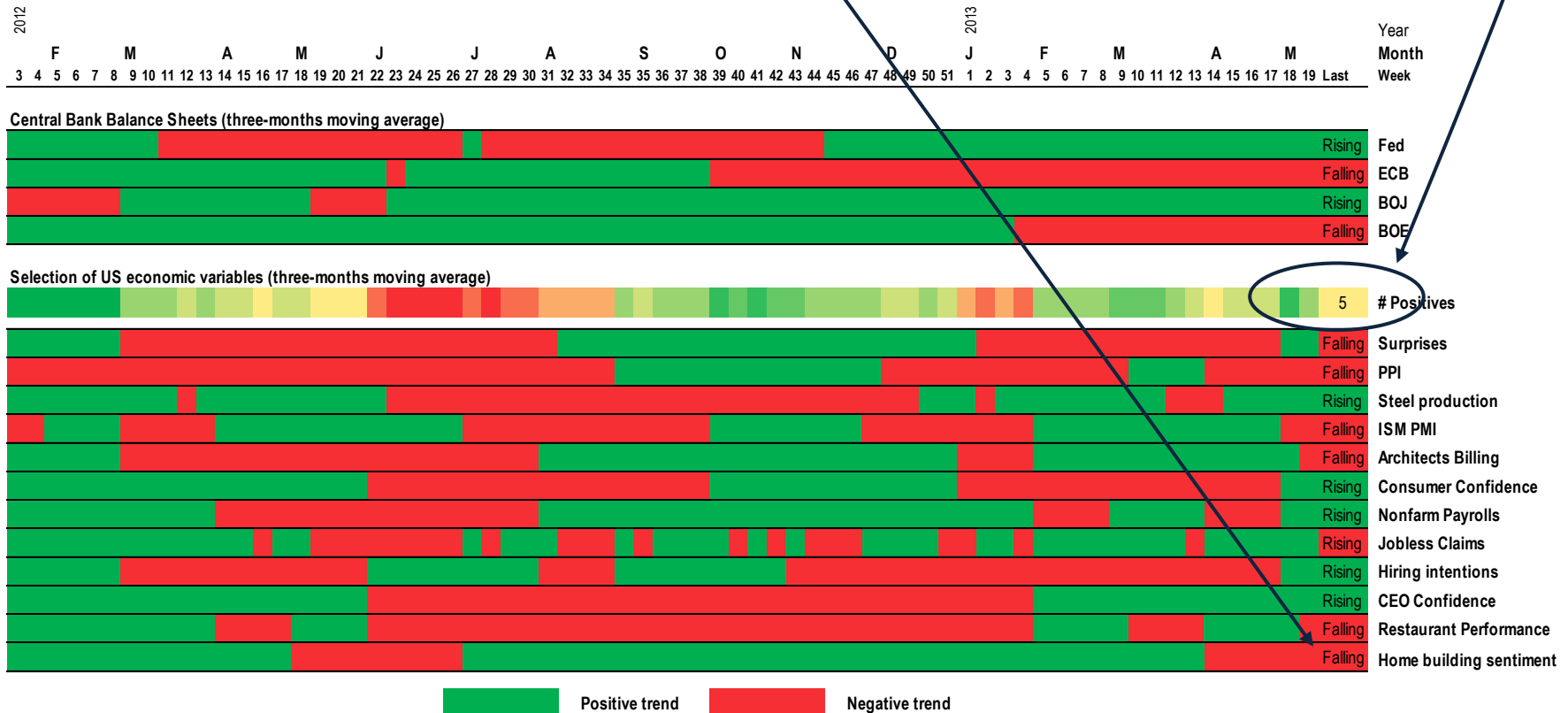
Consumer sentiment according to Bloomberg is low but stable. Surprises have fallen sharply though.

2007-			Jan		Feb			March				April				May				Economic proxy			
High	Low	Median	W1	W2	W3	W4	W5	W6	W7	W8	W9	W10	W11	W12	W13	W14	W15	W16	W17		W18	W19	Last
77	10	61	61	61	60	61	58	60	61	59	61	62	62	61	58	57	59	57	57	60	60	57	Average percentile
98	-141	8	34	11	2	-2	-28	-13	-2	-5	8	21	27	29	19	8	8	-5	-12	0	-7	-23	US Surprise Index
291	-3	183	164	162	159	168	175	170	174	171	161	179	174	168	161	148	149	148	145	152	166	164	US Yield curve (10-2Y)
2	-54	-41	-32	-34	-36	-36	-38	-36	-36	-33	-33	-32	-32	-34	-34	-34	-34	-29	-30	-29	-30	-30	Bloomberg Cons Comfort
1.13	0.57	0.93	1.04	1.04	1.05	1.06	1.04	1.04	1.04	1.01	1.02	1.05	1.05	1.03	1.02	1.02	1.03	1.00	1.02	1.04	1.06	1.05	Cons Discret vs. Staples
0.87	-4.04	-0.24	-0.44	-0.69	-0.79	-0.72	-0.44	-0.14	0.06	0.17	0.17	0.11	0.01	-0.09	-0.19	-0.29	-0.39	-0.44	-0.47	-0.48	-0.48	-0.47	Aruoba Diebold Scotti
670	282	382	372	373	350	343	374	361	348	366	348	340	334	341	357	388	348	355	342	327	328	360	US Jobless claims
5.5	-2.5	2.6	2.7	4.0	3.3	3.2	2.0	2.6	2.1	1.8	2.9	1.8	1.8	2.3	1.0	1.9	2.1	2.0	1.9	2.6	2.4	1.2	US chain store sales, YoY
638	316	489	530	532	535	541	545	538	544	534	535	540	544	540	539	534	533	529	527	527	527	524	CRB RIND
463	127	341	369	365	368	365	378	376	374	353	348	351	352	347	340	334	335	315	318	331	335	332	Copper
81	-70	10	6.7	7.3	8.8	10.5	12.8	13.3	11.5	11.5	7.5	9.1	7.6	9.9	9.6	9.7	8.3	9.9	7.2	7.5	4.6	2.6	JoC-ECRI Industrial Price
1022	237	413	351	351	350	350	351	353	352	353	354	355	359	361	364	365	367	369	370	373	374	375	Container Ship Index

Source: IR&M, Bloomberg. Table shows eleven variables that are of higher frequency and supposedly have predictive power for the US (and or global) economic cycle. "W" stands for calendar week number.

US economic health check: **worsening**

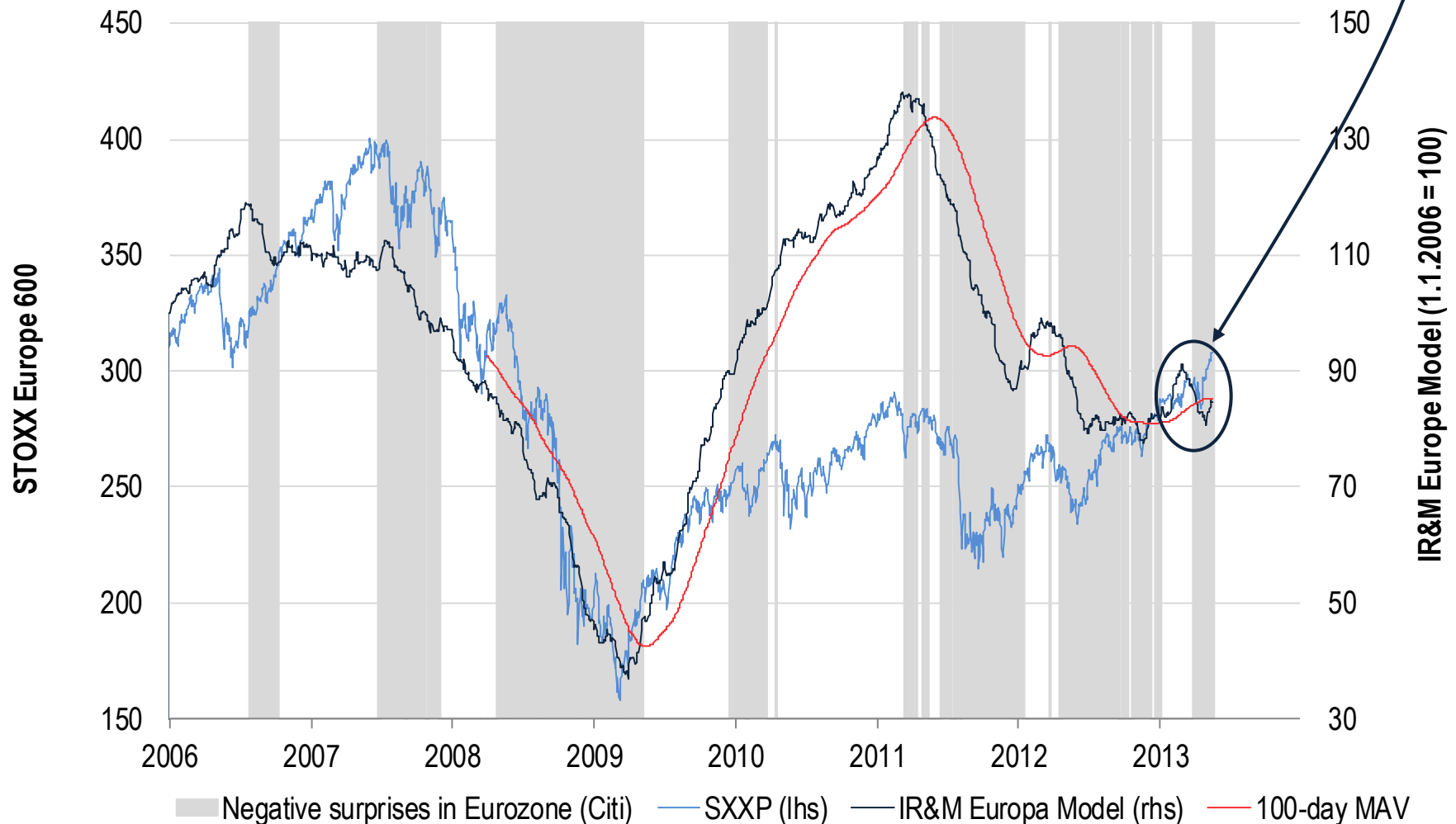
Both home building sentiment and housing starts (not shown) are in decline. This contradicts a statement by Richard Fisher (page 33), president of the Dallas Federal Reserve Bank, who “declared victory on the housing front” recently.



Source: IR&M, Bloomberg. Table shows three-months moving average of four main central bank's balance sheets as well as twelve economic variables that have cyclical/trending characteristics. Surprise index from Citigroup. Steel production is from AISI. The US Architecture Firms "Work-On-The-Boards" Billing Index is from AIA Economic & Market Research Group. Consumer confidence, CEO confidence, Help wanted ads from Conference Board. The Restaurant Performance Index is from the National Restaurant Association, home building sentiment from National Association of Home Builders.

Europe: at inflection point

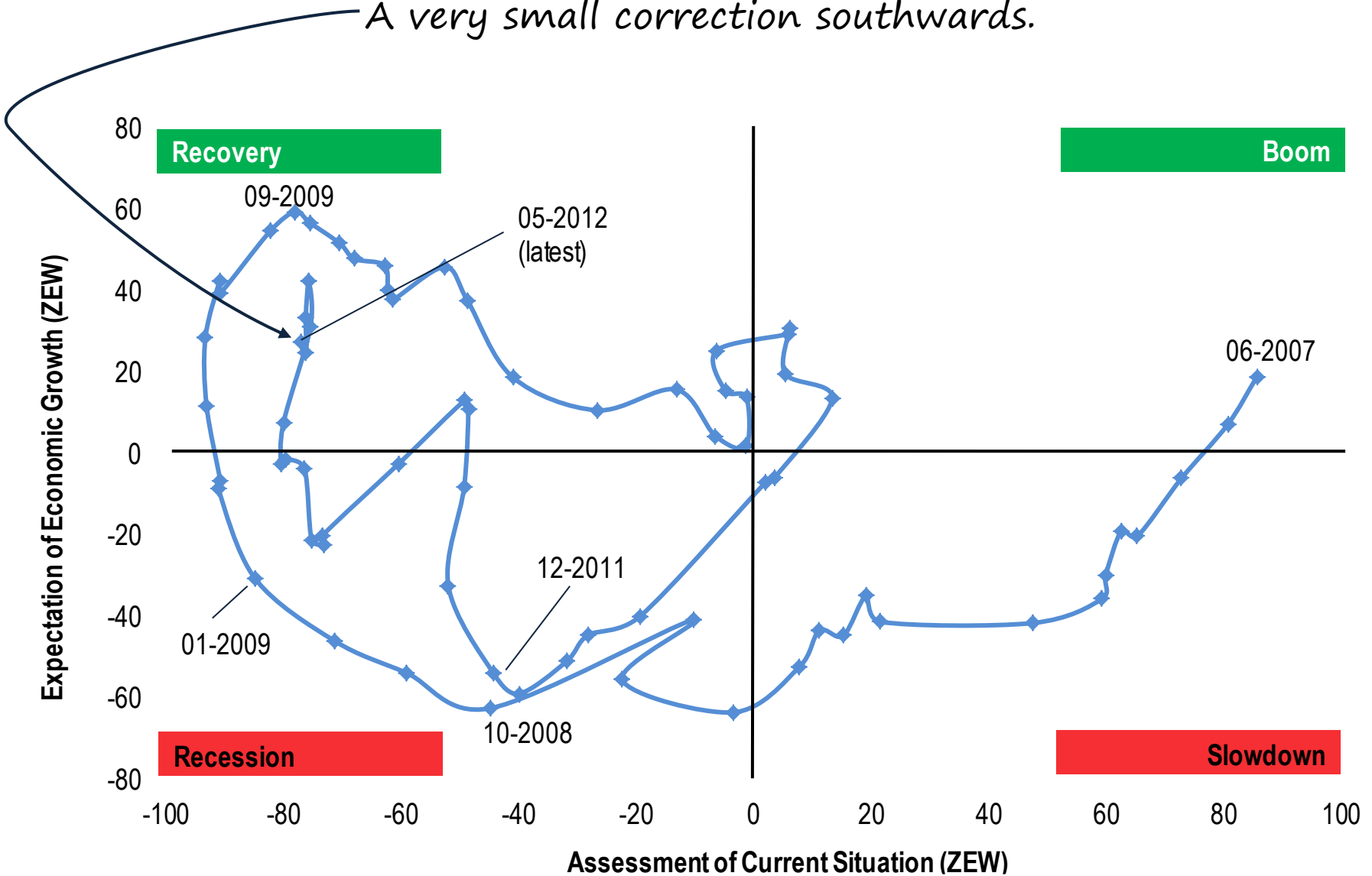
Surprises have been negative since the end of March. The Eurozone remains in recession when judged by official Q1 GDP statistics.



Source: IR&M, Bloomberg. Note: Model consists of 26 economic variables and is work in progress. The model is for Europe, the surprise index is for the Eurozone only.

Eurozone: recovering

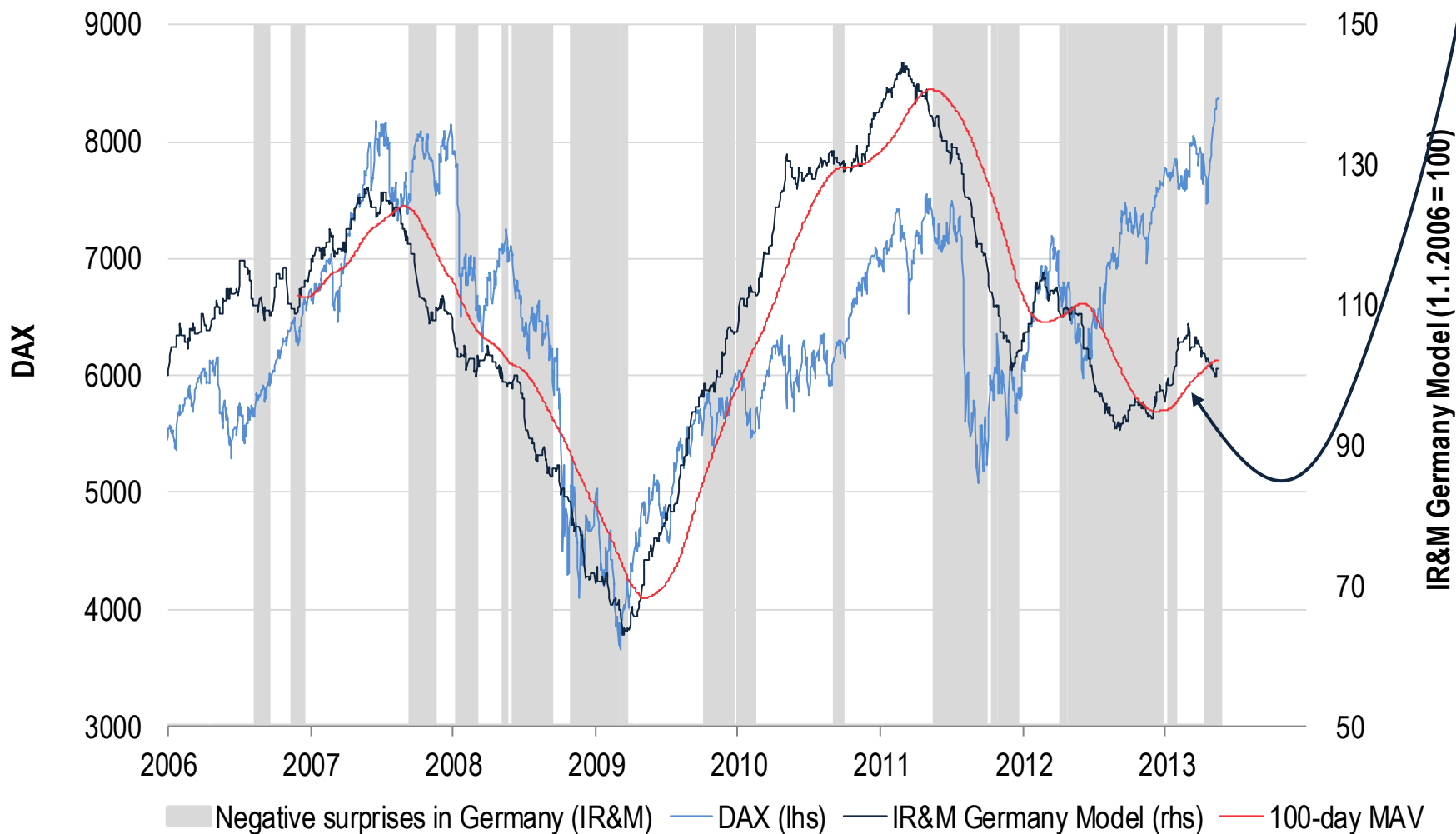
A very small correction southwards.



Source: IR&M, Bloomberg.

Germany: still improving, sort of

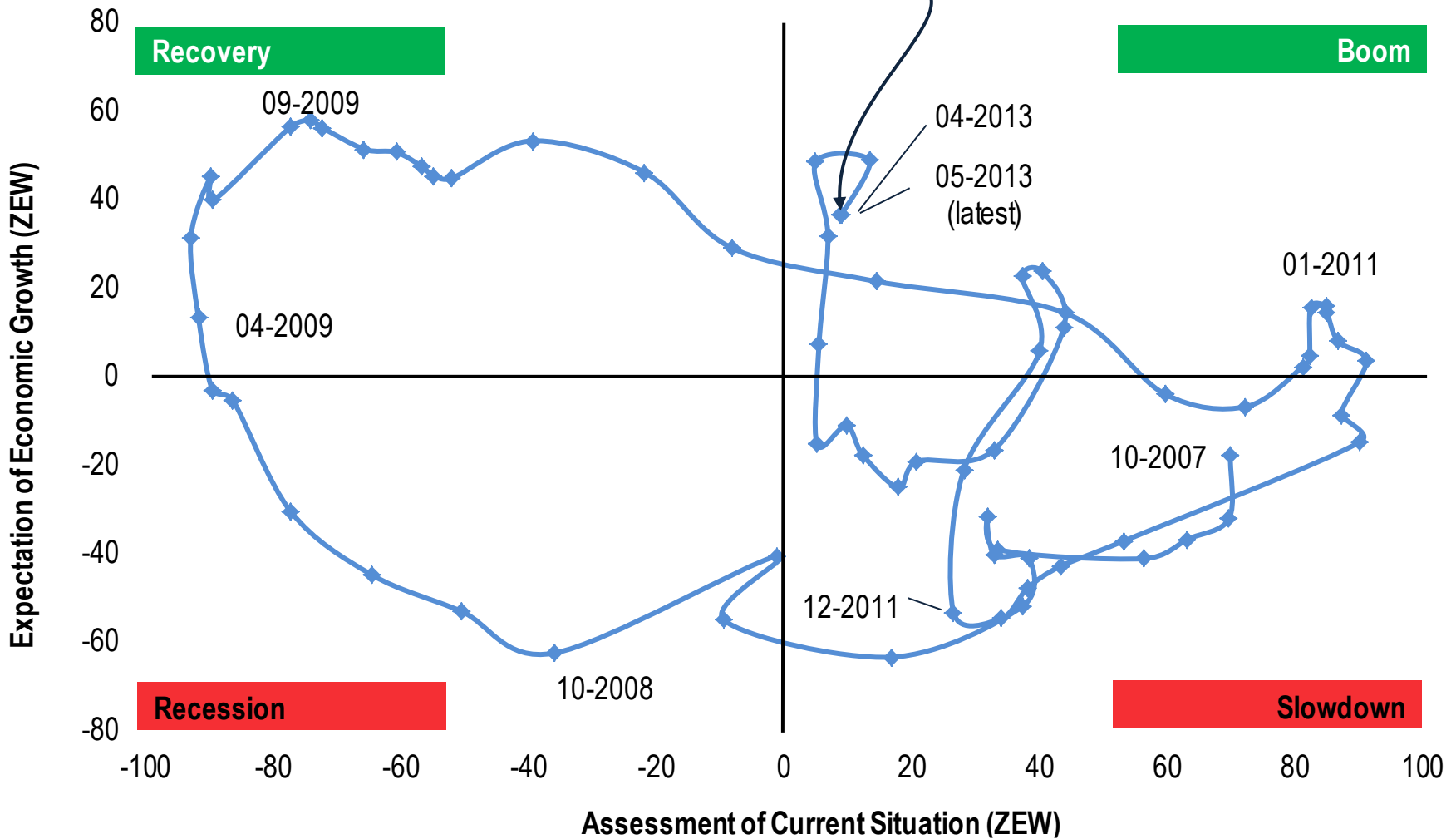
Q1 2012 QoQ GDP was positive but below expectations.



Source: IR&M, Bloomberg. Note: Model consists of 16 economic variables and is work in progress. Surprises index is our own.

Germany: in boom territory

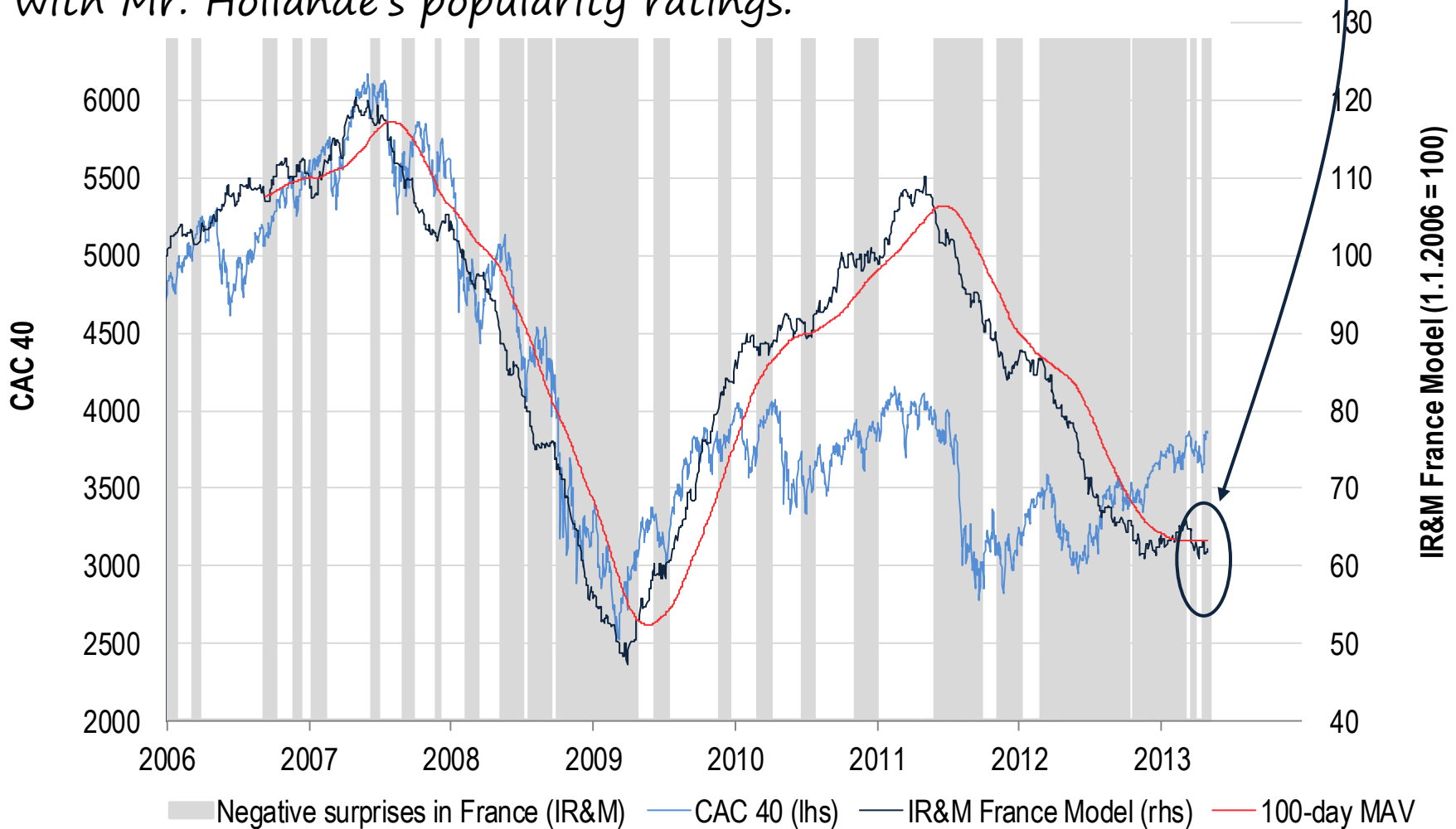
Unchanged, for all practical purposes.



Source: IR&M, Bloomberg.

France: declining

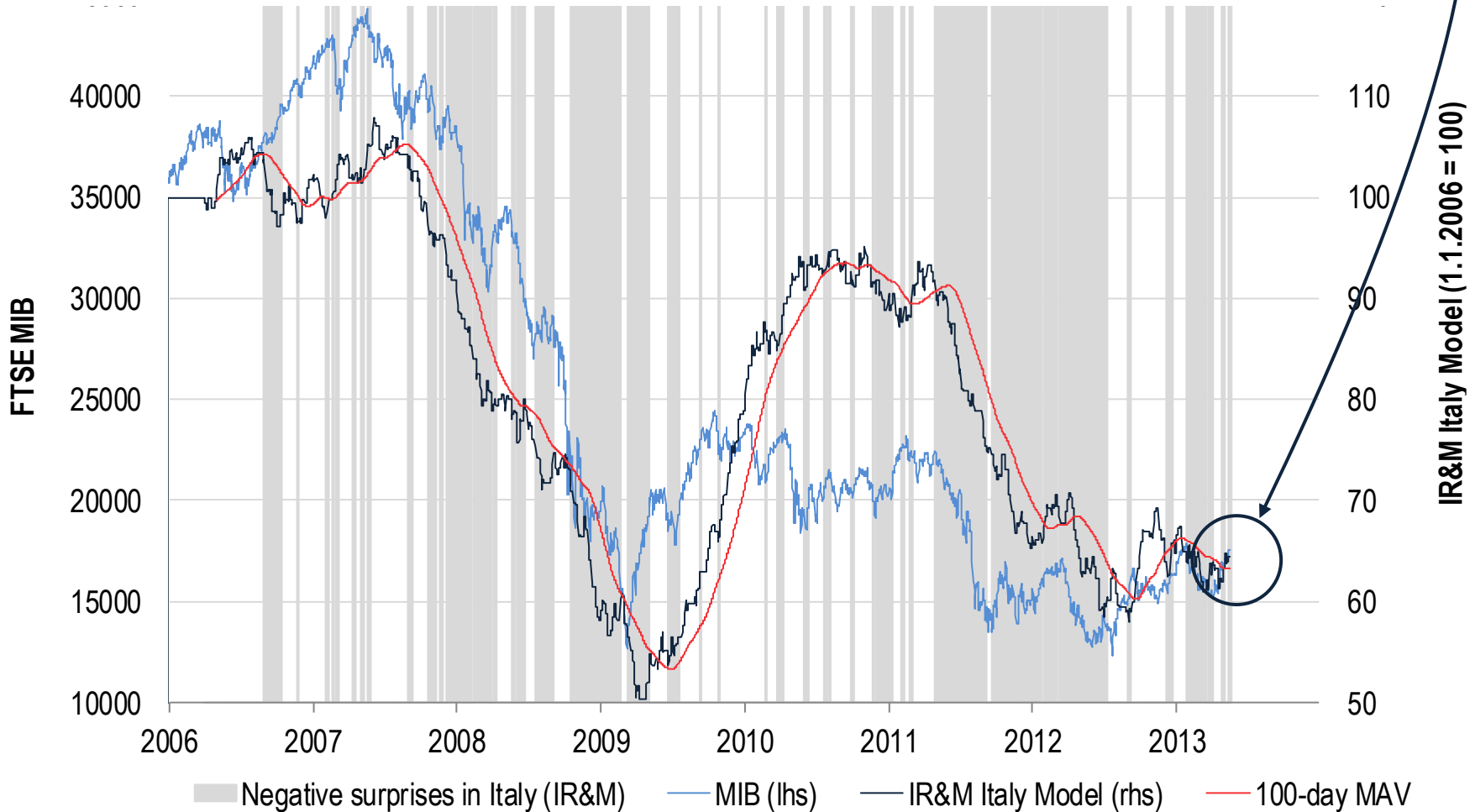
Q1 GDP was negative at -0.2% and compares to Q2-Q4 2012 of -0.2% , 0.1% , and -0.2% . GDP seems correlated with Mr. Hollande's popularity ratings.



Source: IR&M, Bloomberg. Note: Model consists of 15 economic variables and is work in progress. Surprises index is our own.

Italy: declining

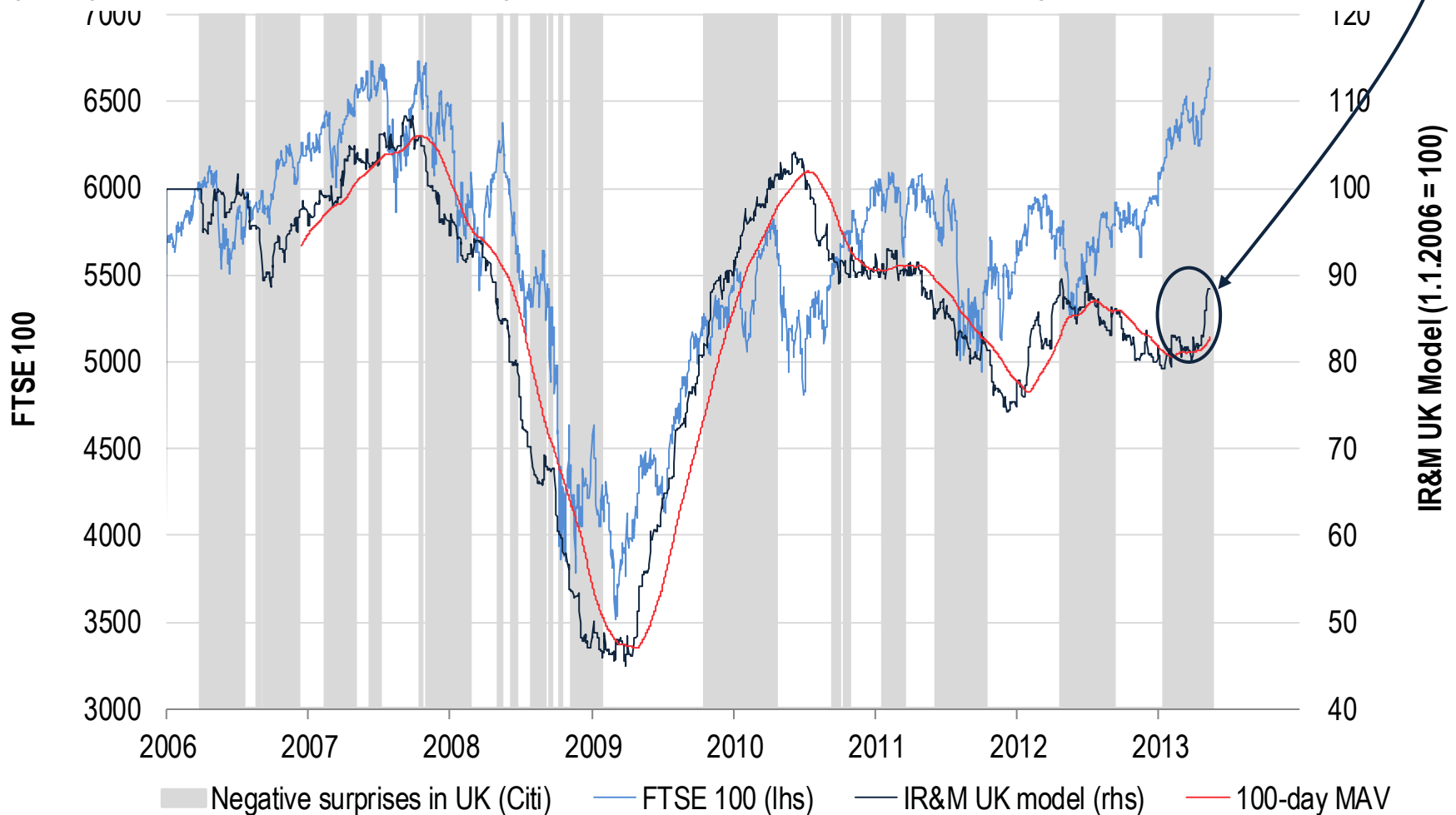
Industrial production for March (announced 10.5.) was bad, in decline, and below expectations, same as February; and same as Q1 GDP figures announced 15.5.



Source: IR&M, Bloomberg. Note: Model consists of 12 economic variables and is work in progress. The surprise index is our own.

UK: improving

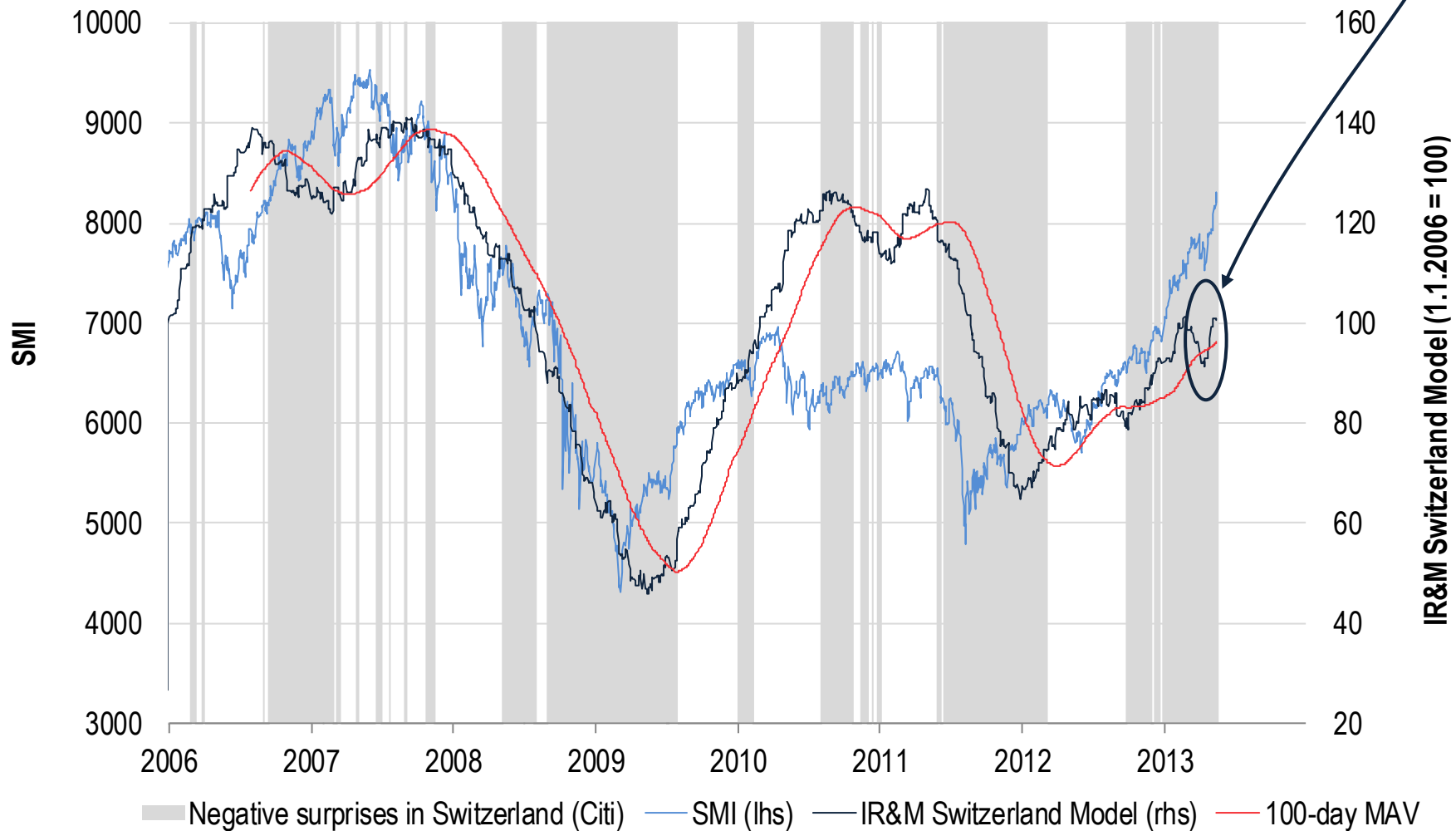
FTSE 100 close to all-time-high of 6950.6 in December 1999 (which is actually quite meaningless as the FTSE All Share Total Returns Index has been going from one all-time-high to the next since mid last year).



Source: IR&M, Bloomberg. Model consists of 22 indicators and is designed to give a data point nearly every day. The model is work in progress.

Switzerland: improving

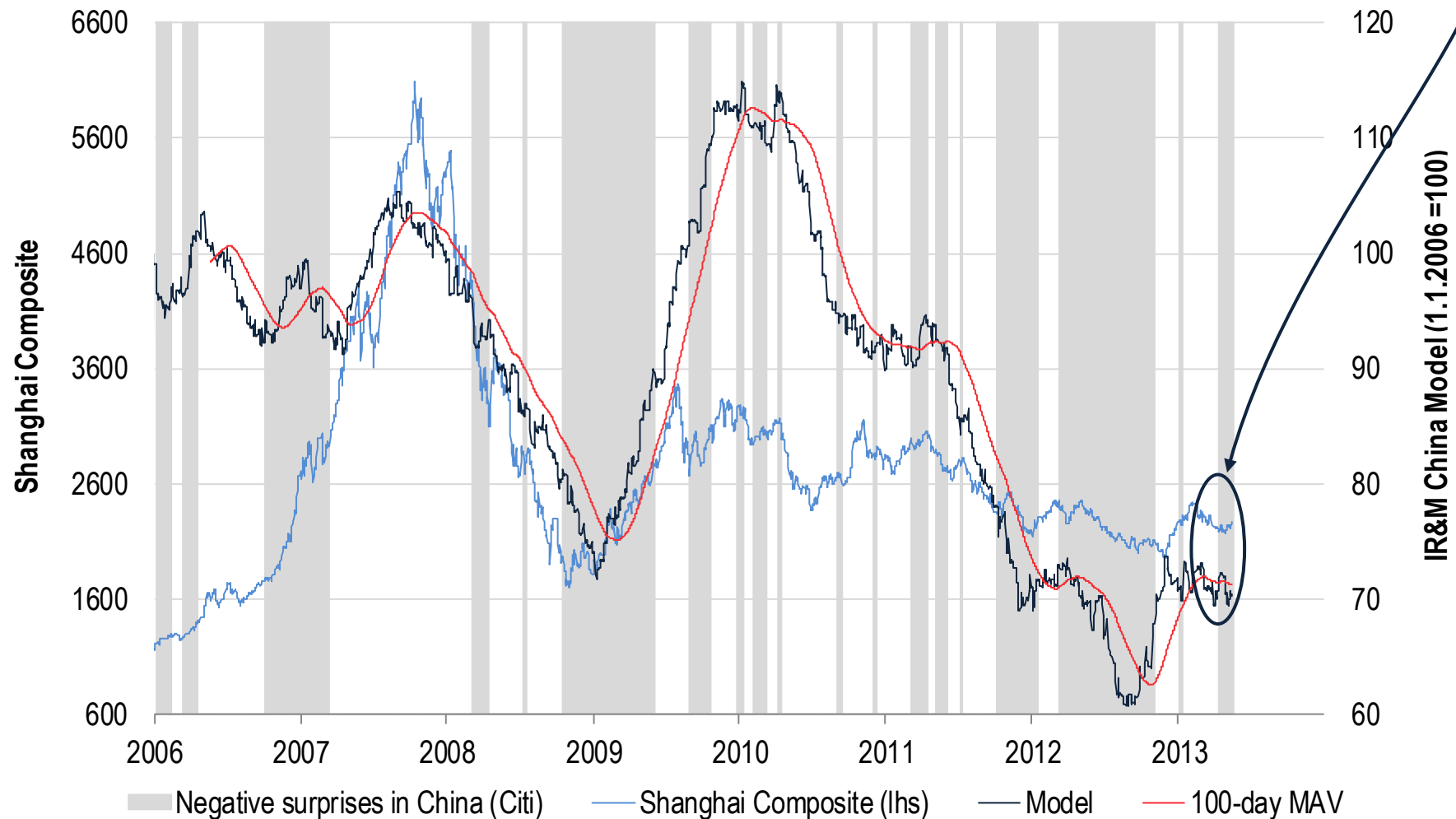
Note that surprises have been negative nearly uninterrupted since September.



Source: IR&M, Bloomberg, NZZ am Sonntag 10 March 2013. Model consists of 14 economic indicator and is work in progress. Surprise index is from Citigroup.

China: at inflection point

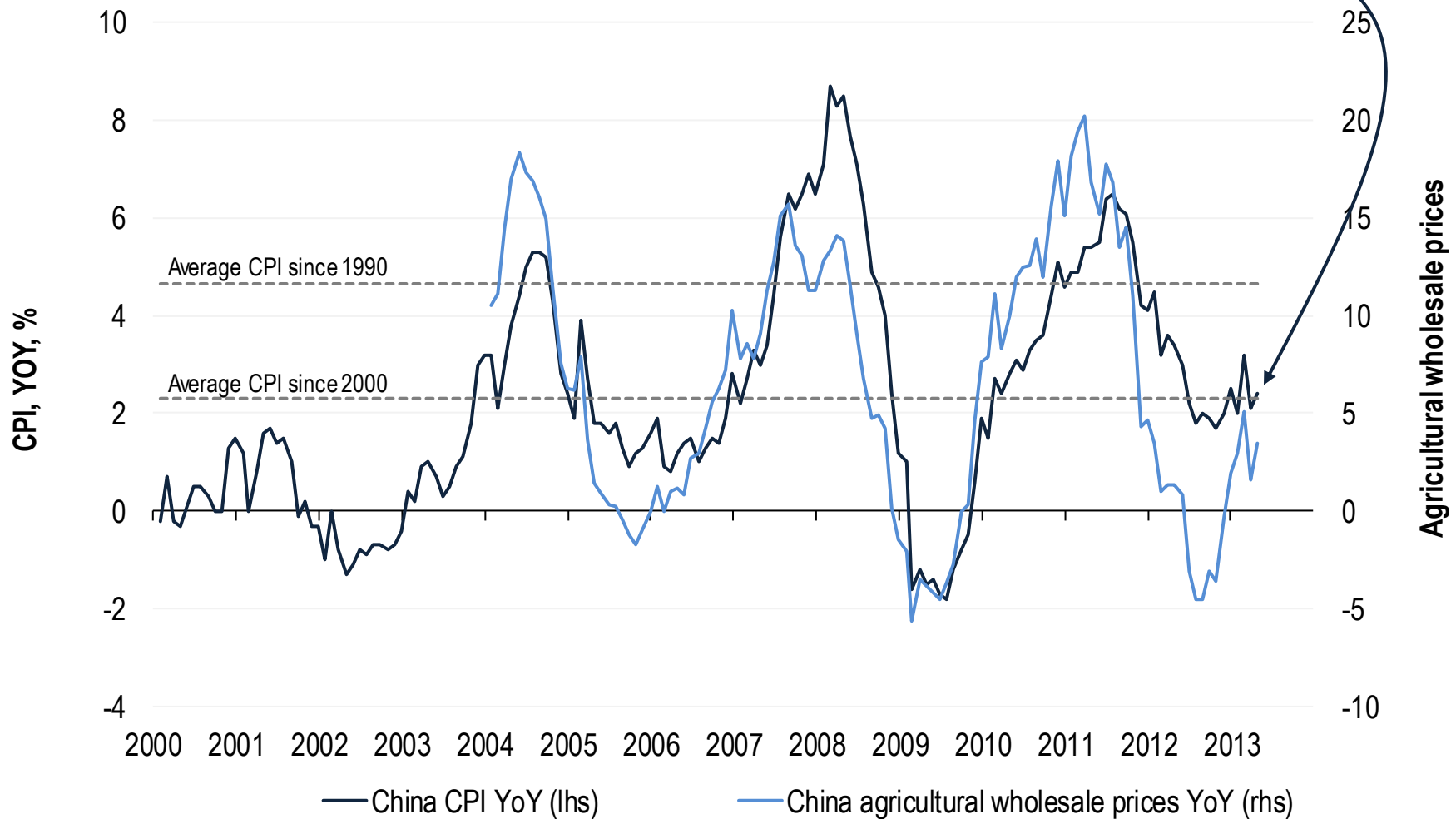
Surprises for China have been negative since mid-April, since the end of March for Asia Pacific as a region.



Source: IR&M, Bloomberg. Note: Model consists of 18 indicators and a weekly read of change in yield curve. Model is work in progress. Note that we had data problems in the past.

China inflation: seems under control

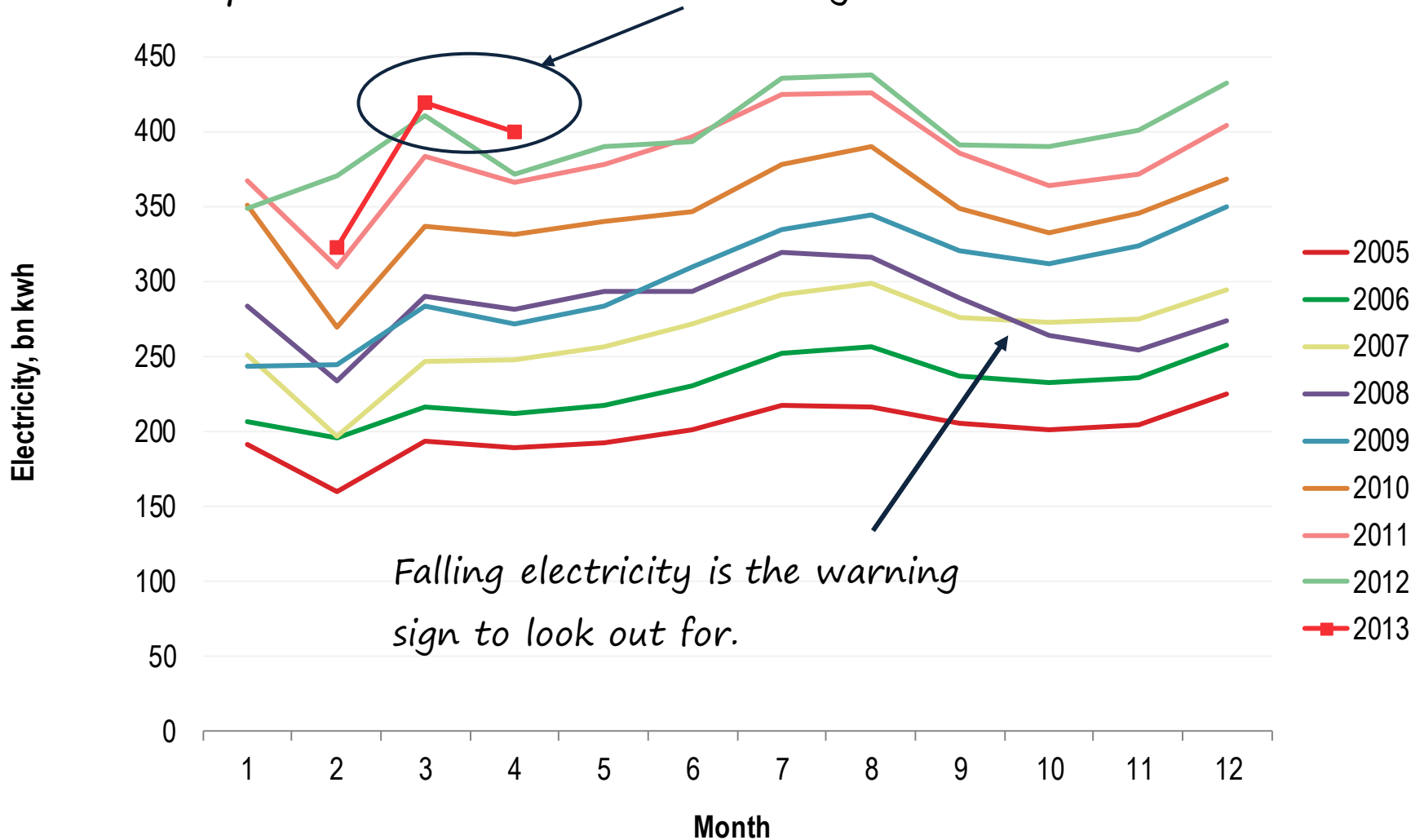
The most recent rise was minor.



Source: IR&M, Bloomberg. Note that food accounts for roughly one-third of CPI.

China econ. health check: Electricity

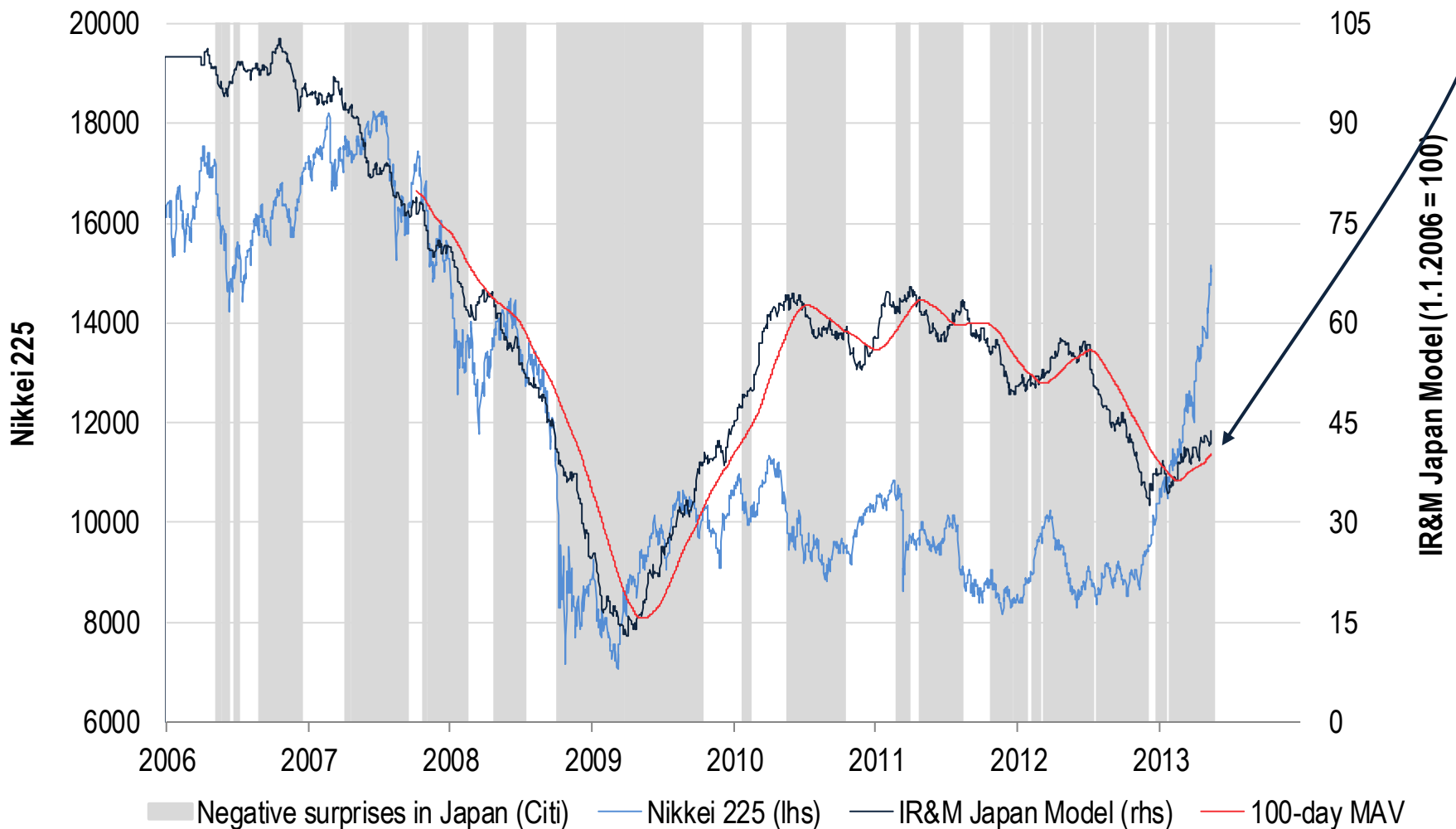
This “box” can be ticked and we can move on. Electricity, one of the least corruptible indicators, is above last years.



Source: IR&M, Bloomberg. Note: There is great seasonality in the data. This year's line needs to be above last year's and, ideally, should be rising.

Japan: improving

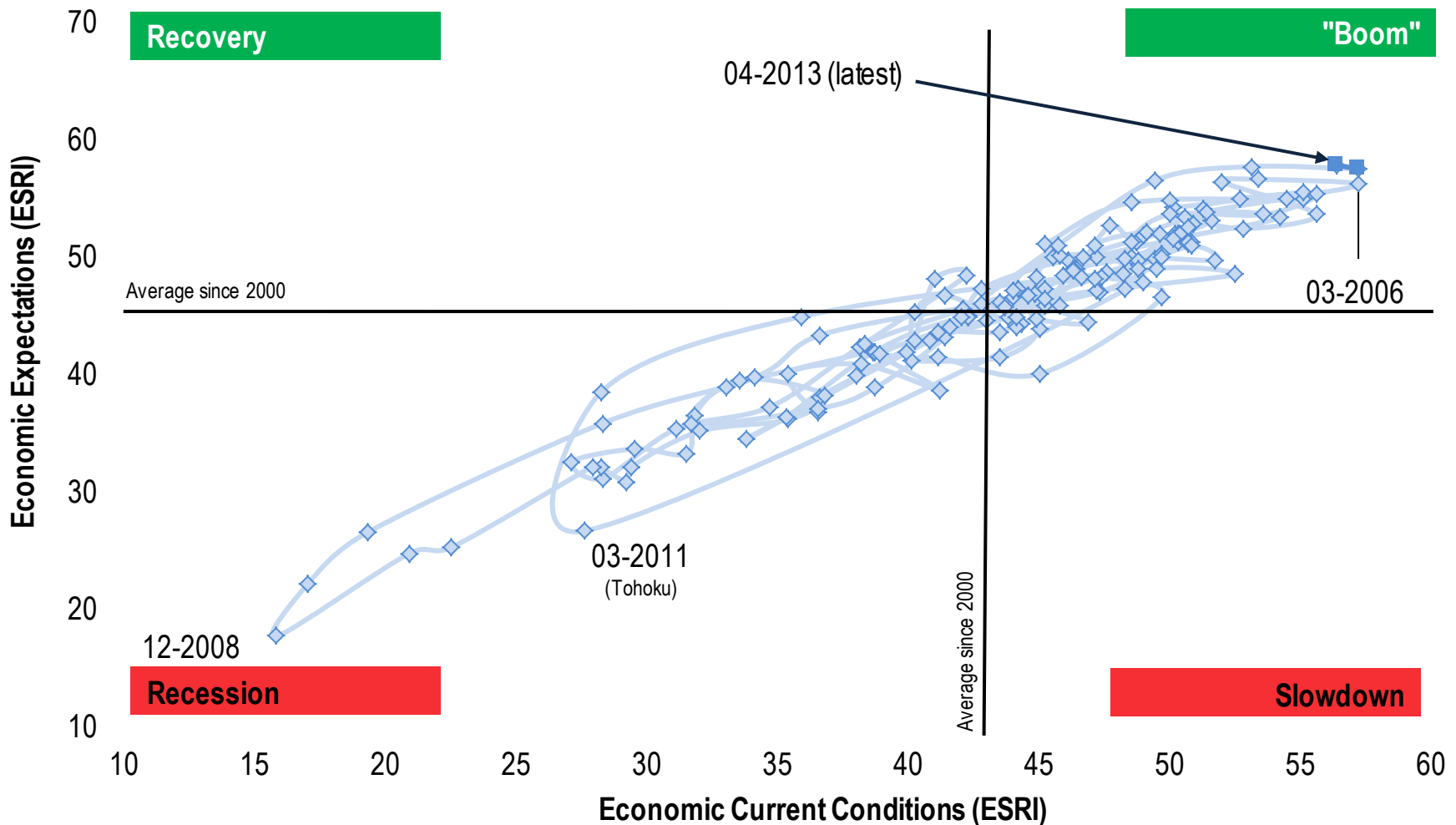
Q1 GDP rose 0.9% vs 0.7% expected, its fastest pace of growth in a year due to rising domestic consumption and exports.



Source: IR&M, Bloomberg

Japan: in “boom” territory

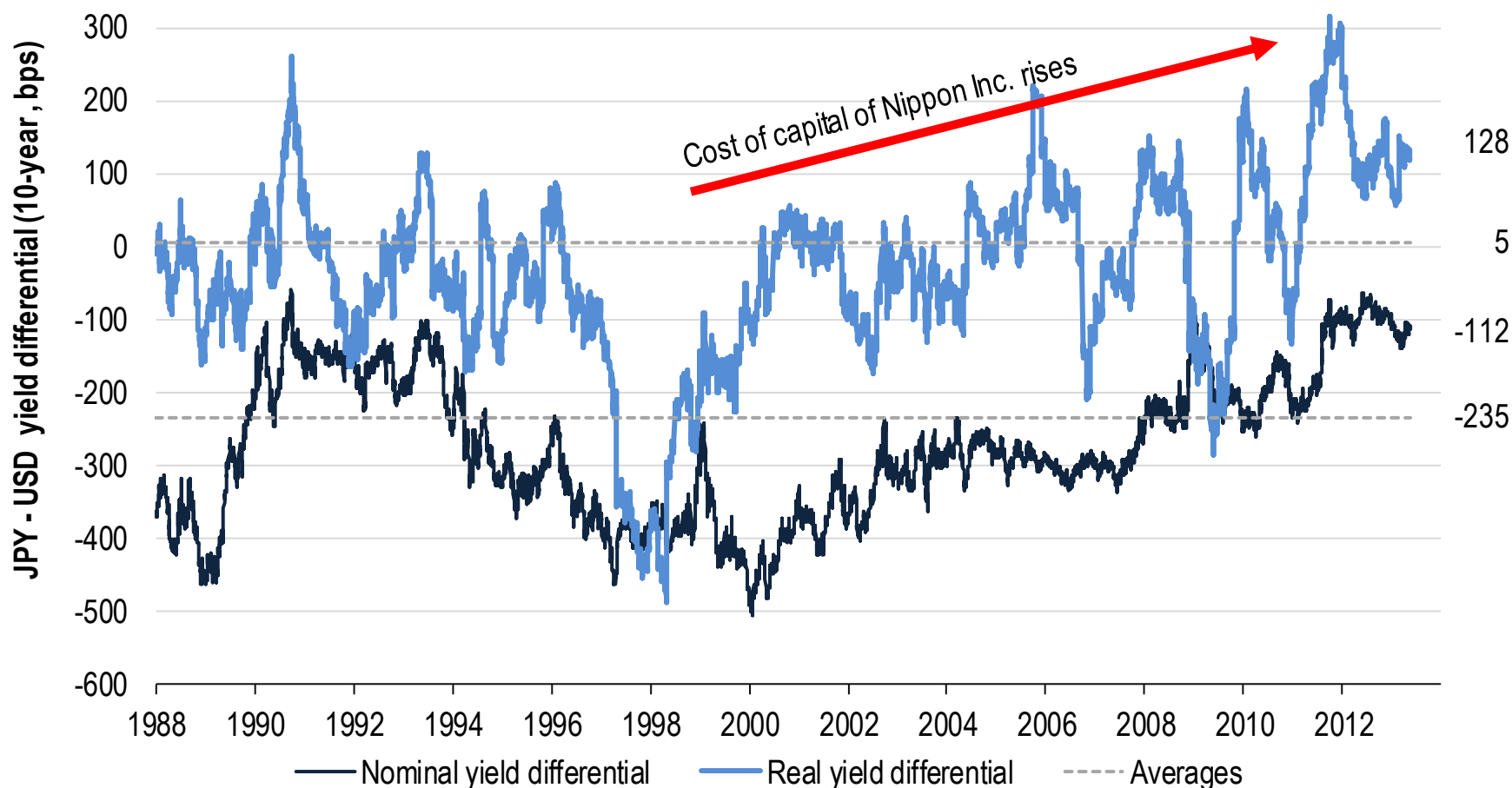
Japan remains in “boom” territory according to this exhibit. For all practical purposes, there was no change from March to April.



Source: IR&M, Bloomberg. Note: cross bars are based on averages since 2000.

Japan's cost of capital: rising

Both, the Zimbabwean-esque debt burden as well as baby-averse demographics should increase the cost of further debt. This is good for investors because the yield pickup increases; assuming there is no day of reckoning of course.



Source: IR&M, Bloomberg. Note: Real yield differential is based on official yoy consumer price inflation.

Hitting the proverbial nail on its head

*"I am definitely **bullish**. The budget deficit is shrinking massively. Guys who are short, they better have a shovel to get out of the grave."*

—David Tepper, Appaloosa Management LP, CNBC, 14 May 2013

*"Never have investors reached so high in price for so low a return. Never have investors stooped so low for so much **risk**."*

—Bill Gross, Pimco, 14 May 2013

*"We can rightly declare victory on the housing front and (reduce) our purchases, with the aim of eliminating them entirely as the year wears on. I believe the efficacy of continued purchases is **questionable**."*

—Richard Fisher, president of the Dallas Federal Reserve Bank, National Association for Business Economics, 16 May 2013

*"It will take further gains to convince me that the '**substantial improvement**' test for ending our asset purchases has been met... We could reduce somewhat the pace of our securities purchases, perhaps as early as this summer. Then, if all goes as hoped, we could end the purchase program sometime late this year."*

—John Williams, president of the Federal Reserve Bank of San Francisco, Reuters, 16 May 2013

*"The balance of risks of prolonged very low interest rates and unconventional policies is shifting. The **costs** are growing in relation to the benefits."*

—BIS, Reuters, FT Alphaville, 16 May 2013

Inflation-linked govt bond yields: **negative**

Repressiononomics continues of course.



Source: IR&M, Bloomberg.

Target rates: low and falling

BoE: Left unchanged, as expected.

RBA: Lowered target rate unexpectedly to 2.75%

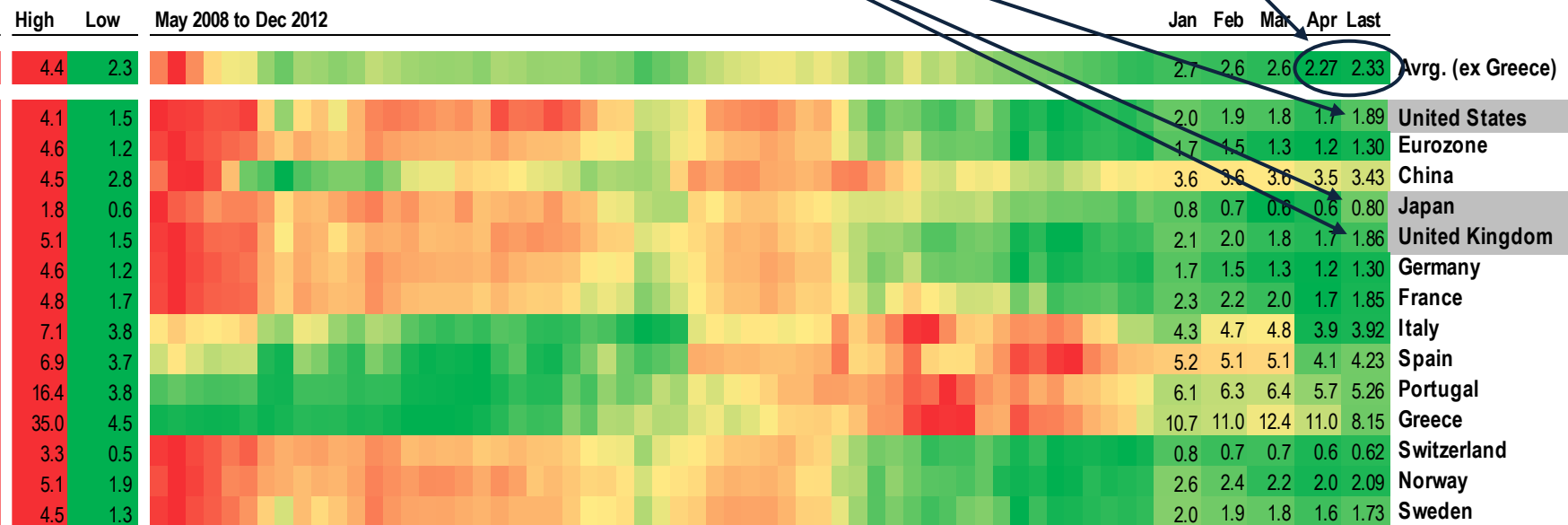
BoK: Lowered target rate unexpectedly to 2.50%

10-years			2011			2012						2013											
High	Low	Median	11 11	12 11	01 12	02 12	03 12	04 12	05 12	06 12	07 12	08 12	09 12	10 12	11 12	12 12	01 13	02 13	03 13	04 13	Last		
5.17	0.91	2.17	1.30	1.58	1.58	1.55	1.53	1.53	1.49	1.44	1.37	1.37	1.35	1.30	1.30	1.26	1.26	1.26	1.26	1.26	1.19	Average ex Brazil	
5.25	0.25	1.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	United States
4.25	0.50	2.00	1.25	1.00	1.00	1.00	1.00	1.00	1.00	1.00	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.50	Eurozone
4.14	1.98	2.25	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.25	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	China
0.50	0.00	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.40	0.10	0.10	0.10	0.10	Japan
5.75	0.50	3.75	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	United Kingdom
4.50	0.25	2.25	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	Canada
14.00	3.00	5.25	4.50	4.25	4.25	4.25	4.25	4.25	3.75	3.50	3.50	3.50	3.50	3.25	3.25	3.00	3.00	3.00	3.00	3.00	3.00	2.75	Australia
26.27	7.11	12.17	11.40	10.91	10.40	10.40	9.65	8.90	8.39	8.40	7.89	7.39	7.39	7.14	7.14	7.29	7.11	7.20	7.16	7.40	7.40	7.40	Brazil
2.75	0.00	0.25	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	Switzerland
4.75	0.25	2.00		1.75	1.75	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.25	1.25	1.25	1.00	1.00	1.00	1.00	1.00	1.00	Sweden
5.75	1.25	2.25		1.75	1.75	1.75	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	Norway
5.25	2.00	2.75	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.00	3.00	3.00	2.75	2.75	2.75	2.75	2.75	2.75	2.75	2.75	2.50	South Korea

Source: IR&M, Bloomberg.

10Y yields: low but rising?

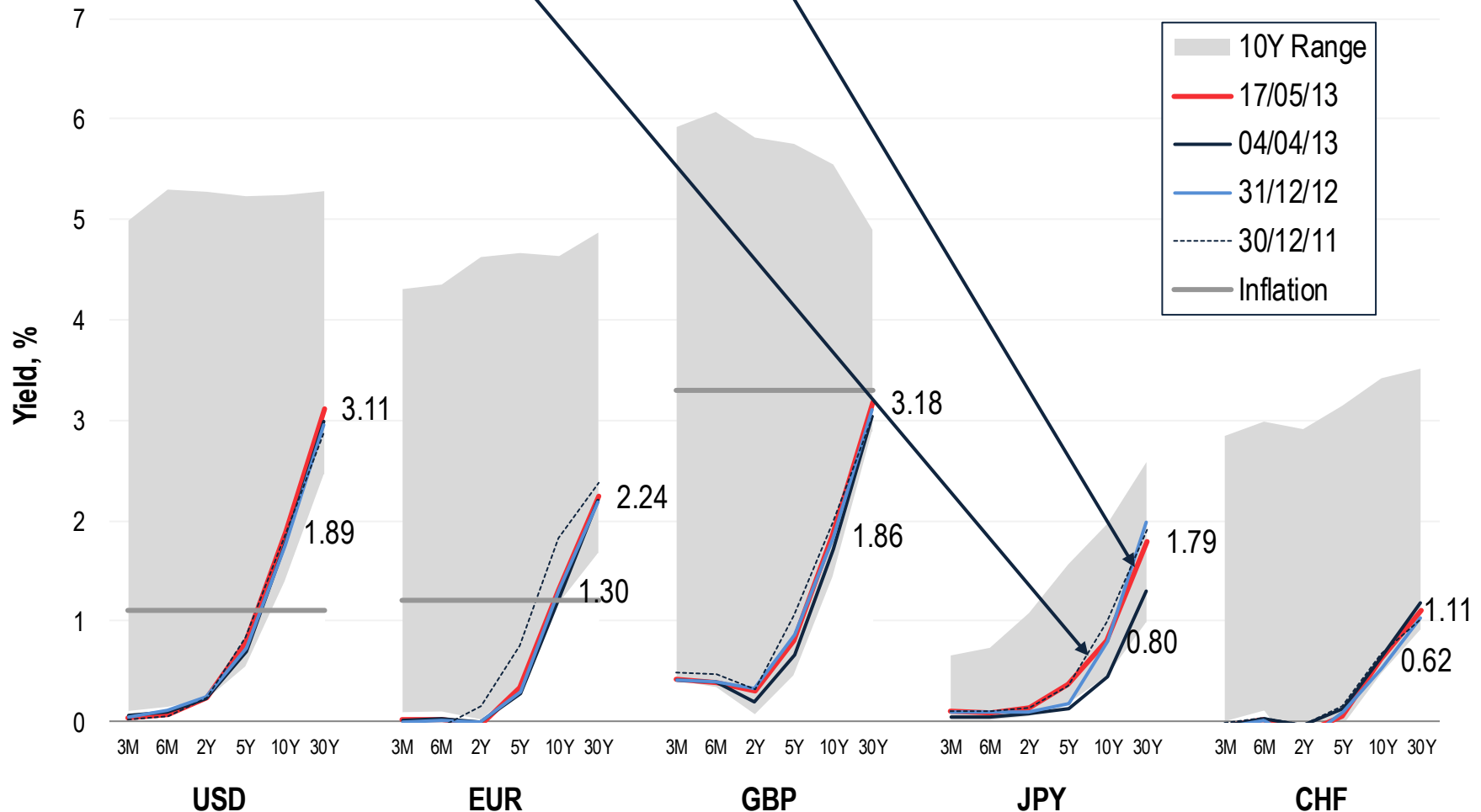
Has risen more than 15bps this month



Source: IR&M, Bloomberg. Note: Table is based on month-end 10-year yields; except "last". Colour coding: red applies to high yields (low bonds).

Yield curves: jumpy

Note that nearly the whole JPY yield curve is moving.

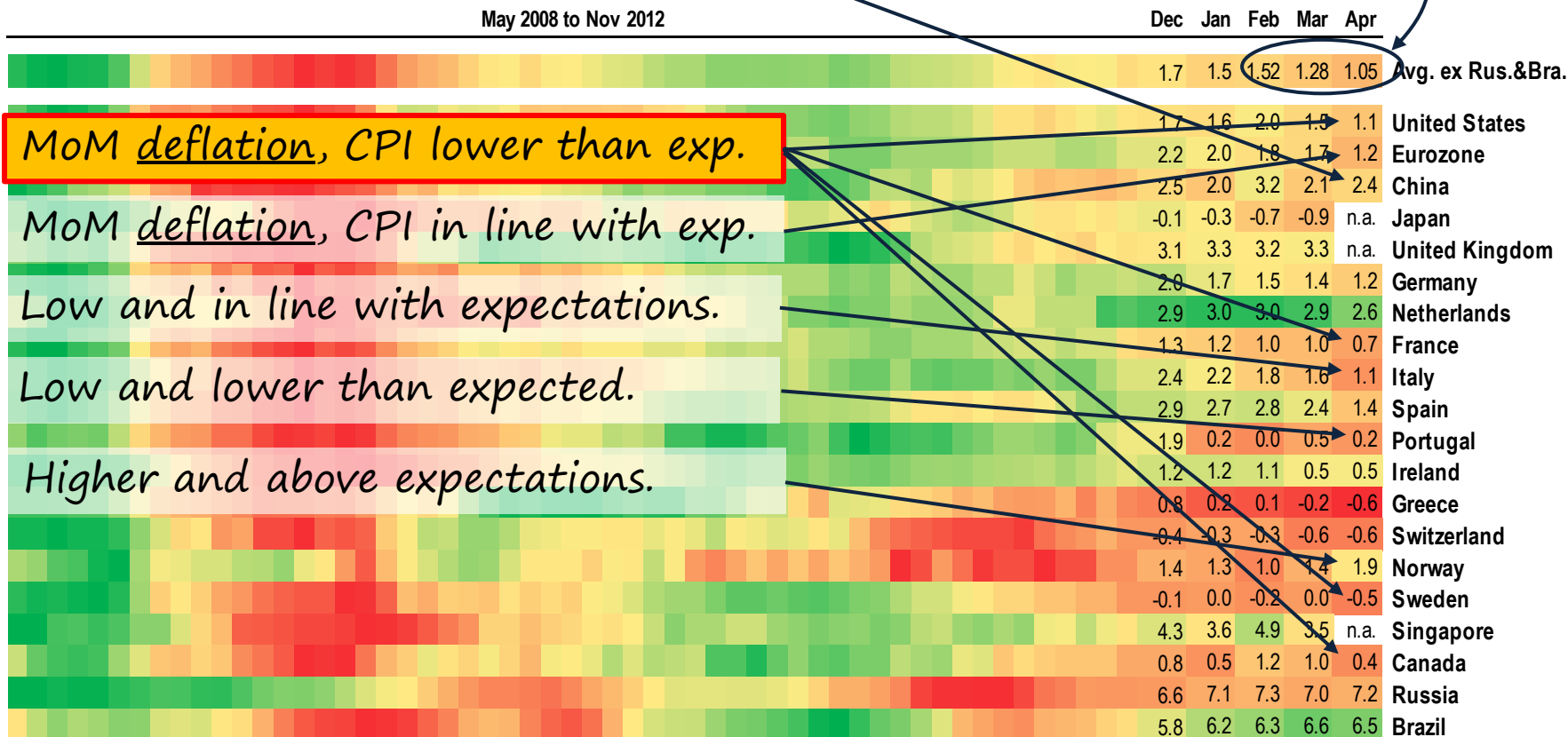


Source: IR&M, Bloomberg. Note: Figure in graph shows ten and thirty year yields. The high and low of the yield curves are measured by the sum of the six yields of the term structure. Inflation: latest official yoy CP figure, RPI in the UK.

Consumer price inflation: **falling**

China: CPI a bit higher and marginally above expectations. (PPI lower and below expectations.)

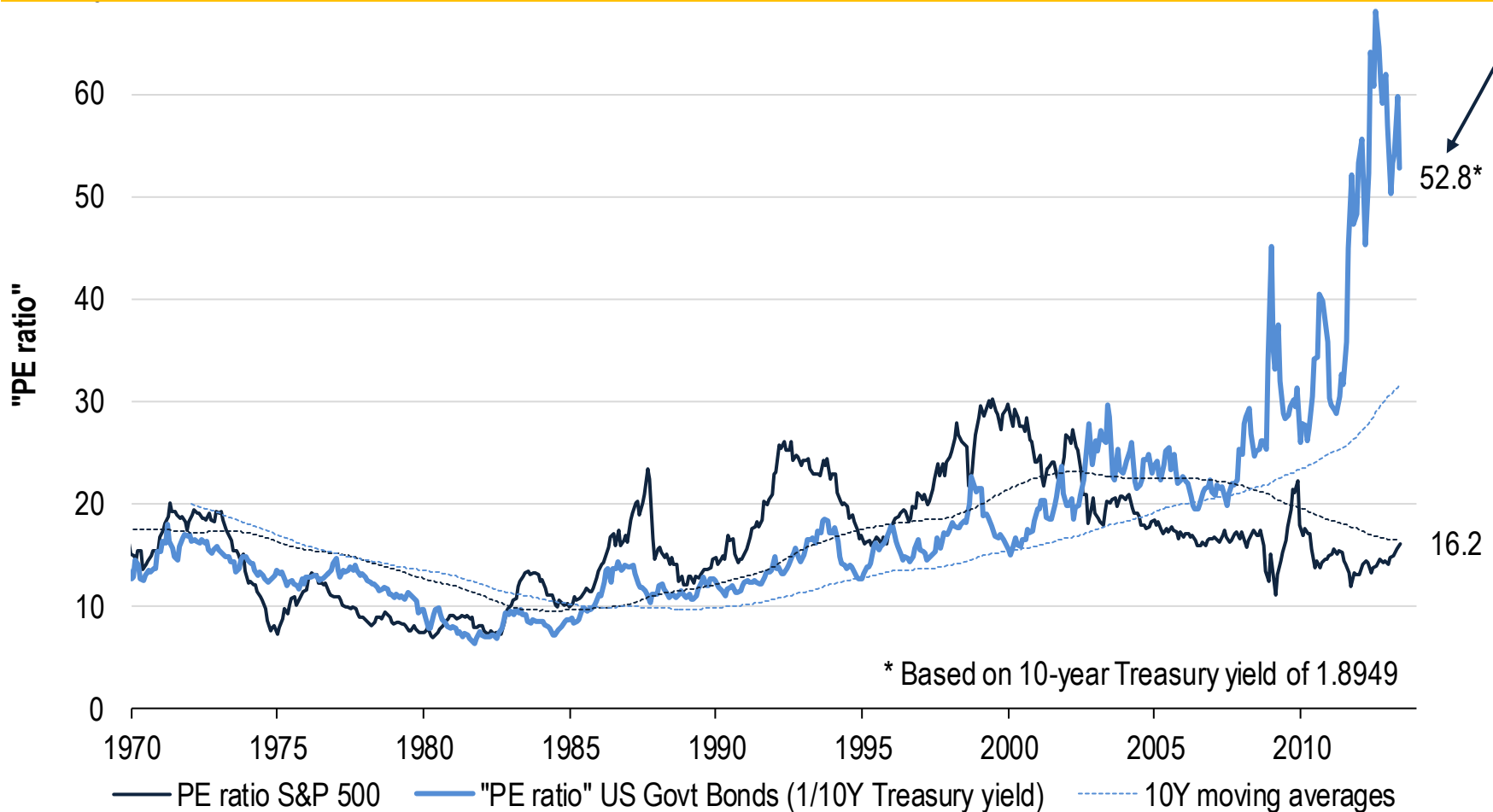
May 2008 to Nov 2012



Source: IR&M, Bloomberg. Based on official yoy CPI, except UK, which is based on RPI (Retail Price Index.). Average is equally weighted excluding Russia and Brazil; a 0.32 change is one standard deviation.

Bond valuation: lofty

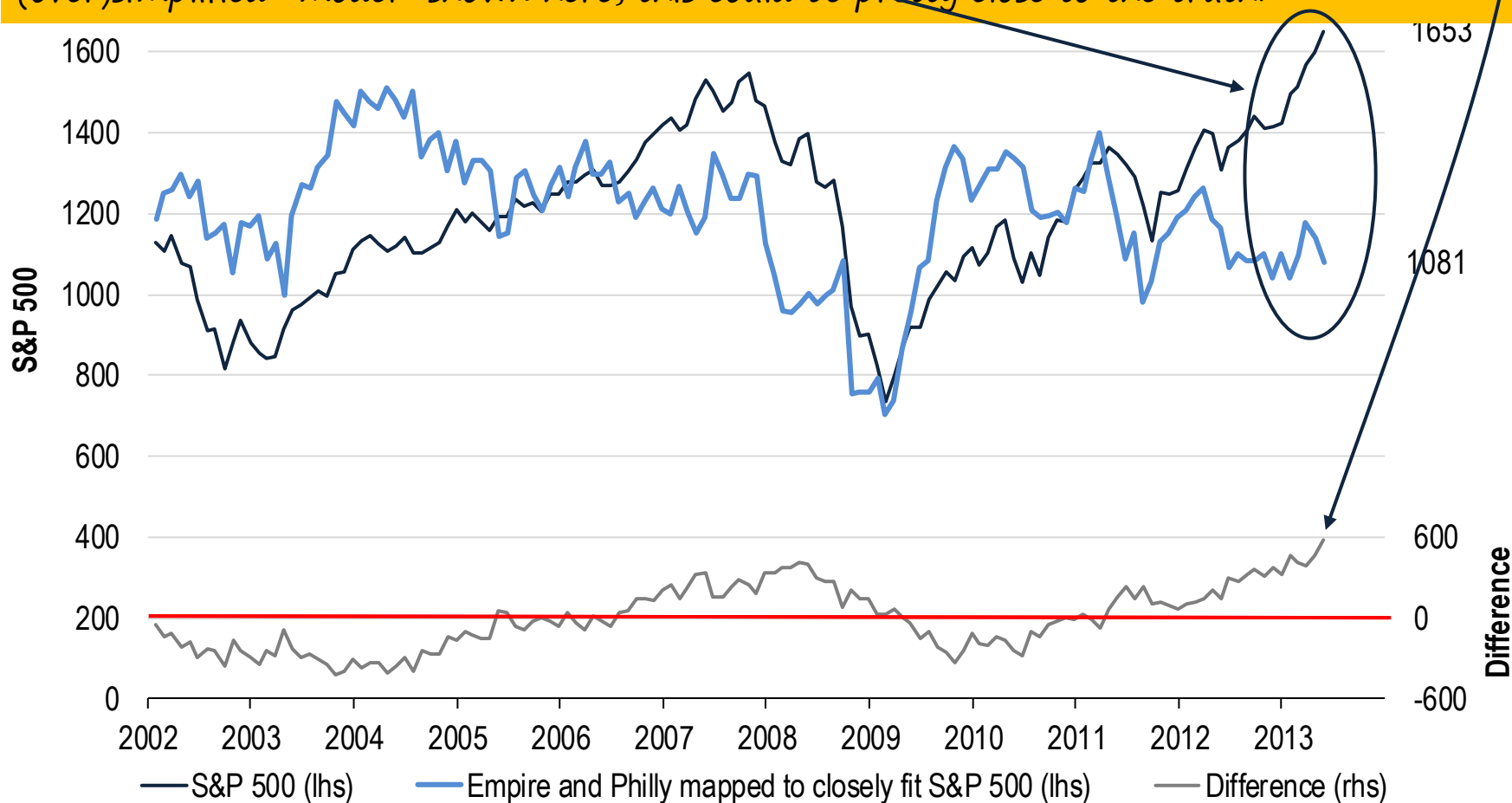
Bond valuation is arguably "lofty". Derek Bok once said: "If you think education is expensive, try ignorance." Rephrased: "If you think equities were in a bubble in 2000, try bonds now."



Source: IR&M, Bloomberg. Notes: Based on trailing PE ratio and inverse 10-year Treasury yield.

S&P 500 valuation: **lofty too**

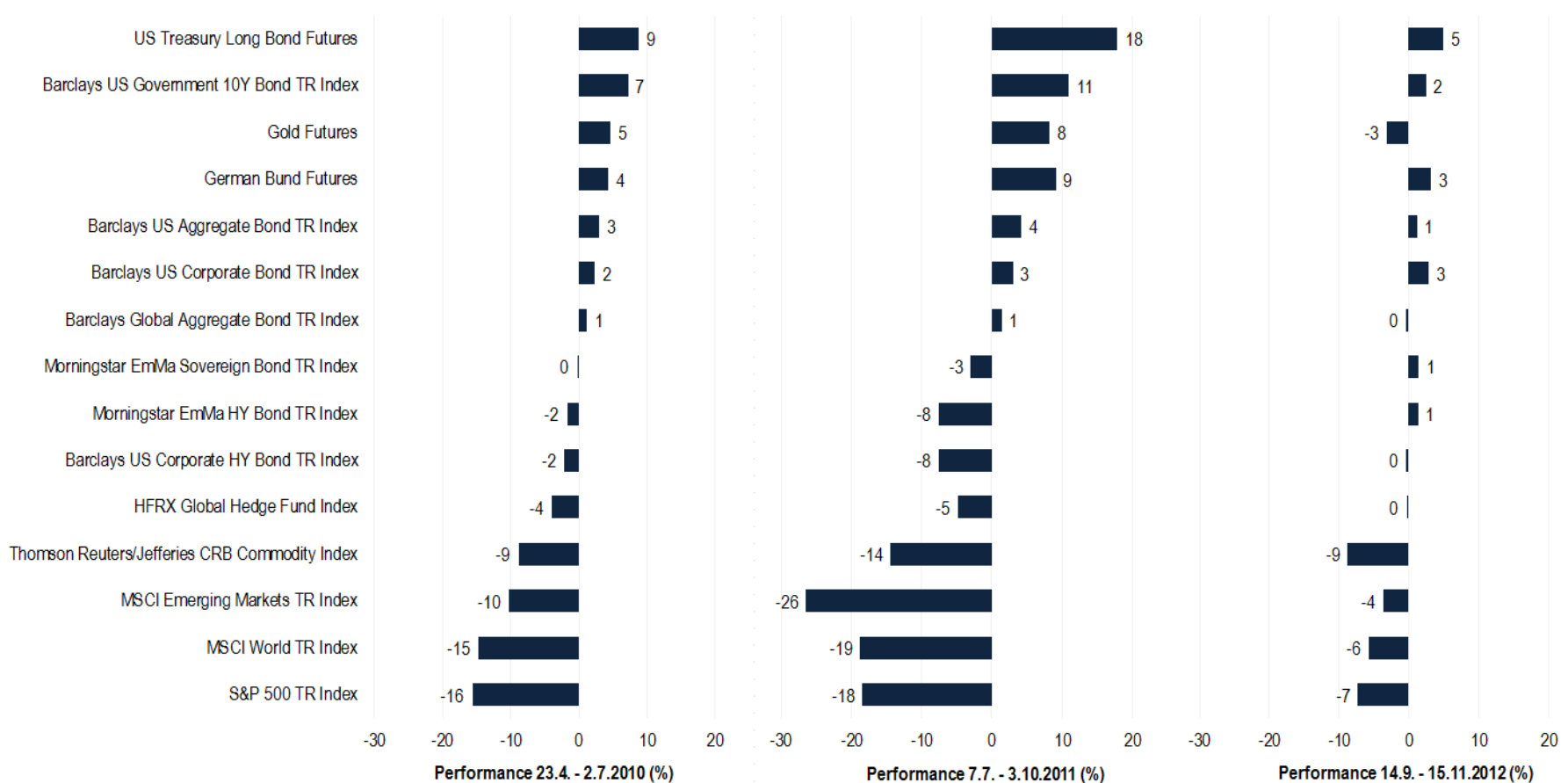
This graph is not very fascinating unfortunately, as it shows what everyone already knows, i.e., the disconnection between a muddling through economic environment and a run-away stock market. Economist David Rosenberg estimates the Fed's contribution to the current S&P 500 level at something around 500 index points. According to our (over)simplified "model" shown here, this could be pretty close to the truth.



Source: IR&M, Bloomberg. Note: The two first published local Fed business diffusion indicators (Empire State and Philadelphia) were mapped to best fit the S&P 500.

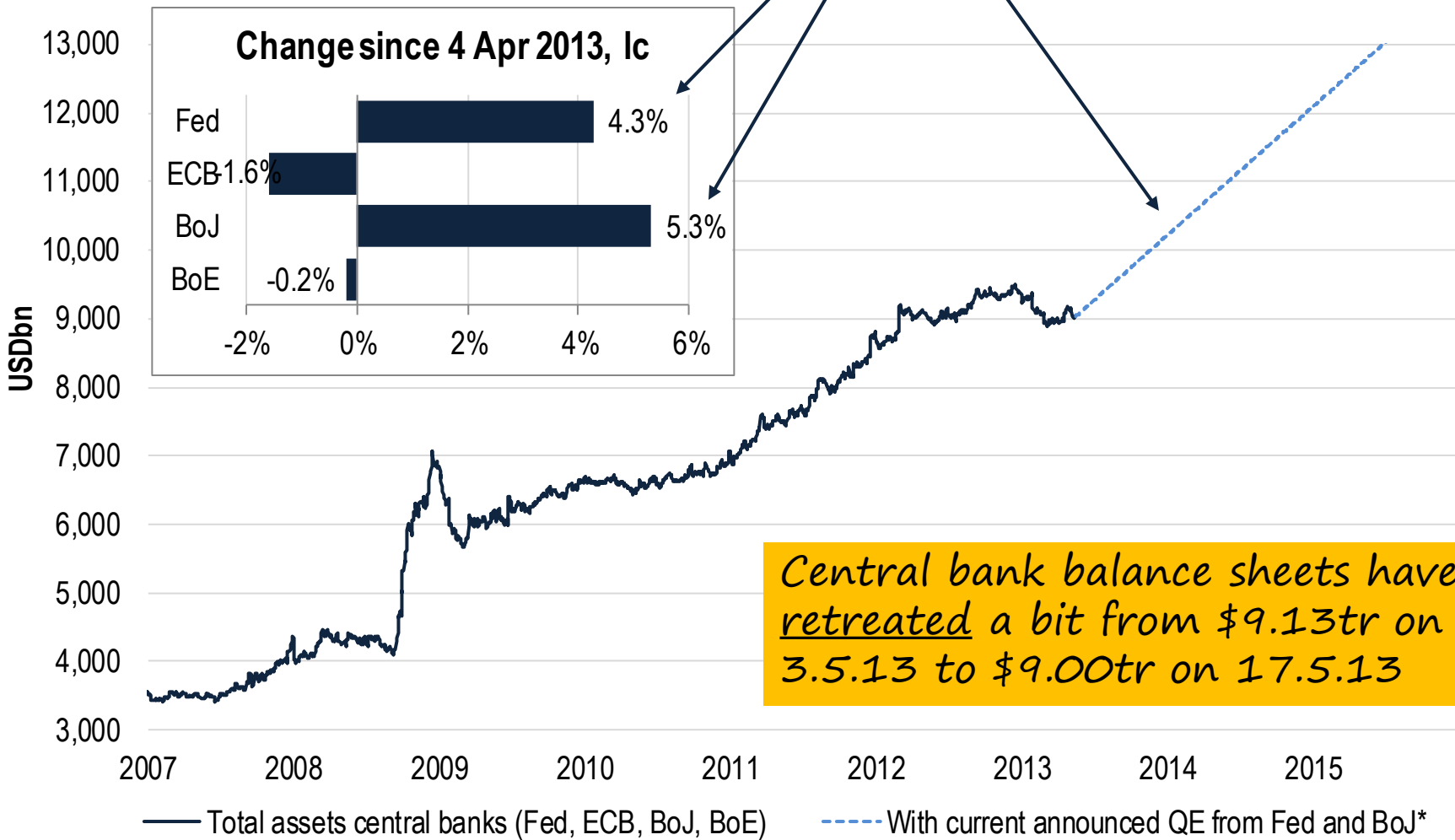
The where to hide slide

“Don’t fight the Fed” applies. However, corrections happen, even during liquidity deluges. The slide shows performance of some indices during the last three equity market corrections.



Source: IR&M, Bloomberg, dates adapted from Breakfast with Dave, David Rosenberg, Gluskin Sheff, 14 May 2013. Table was sorted by 2010 correction.

Central bank assets: **expanding**



Source: IR&M, Bloomberg. *Assume Fed adding \$85bn per month and BoJ doubling by \$1.7tr over two years.

Financial risk: easing

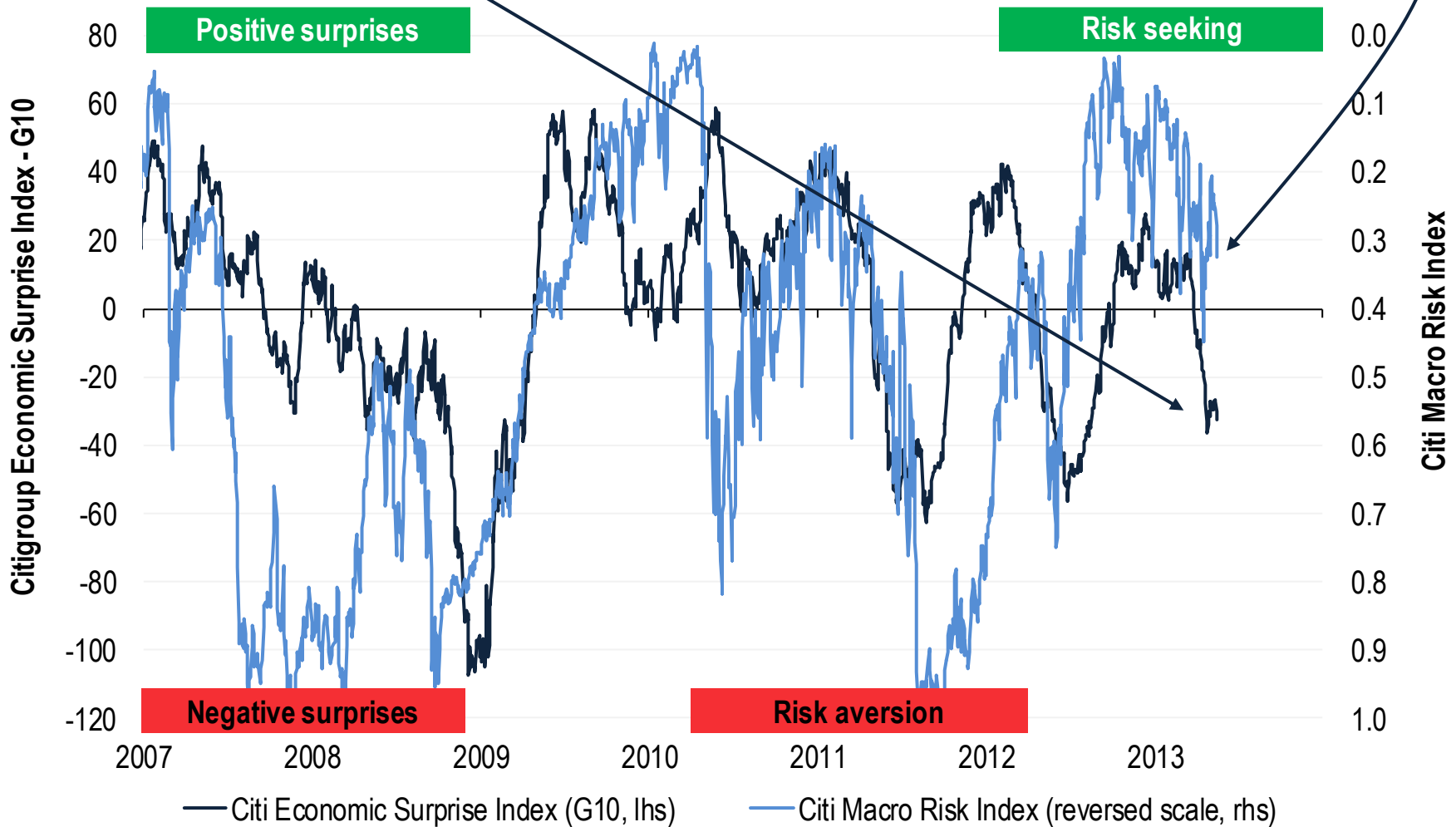
Nearly all indicators improved, i.e., risk eased, since our last report. The only indicators that are a bit worse YTD as well as MTD are related to liquidity. We have added Japan CDS to the list as this needs careful monitoring.

Market	Risk proxy	10-year*			2011		2012						2013						Last						
		High	Low	Median	09	10	11	12	01	02	03	04	05	06	07	08	09	10		11	12	01	02	03	30-04
Composite	St. Louis Fed Stress	6.0	-1.4	-0.3	0.8	0.4	0.7	0.4	0.2	-0.1	-0.2	-0.2	0.0	0.0	-0.1	-0.3	-0.5	-0.5	-0.5	-0.5	-0.7	-0.7	-0.7	-0.7	-0.8
	BB Financial Conditions	1.3	-12.7	0.1	-1.8	-1.0	-1.0	-1.0	-0.5	-0.1	0.1	0.0	-0.7	-0.1	0.0	0.1	0.5	0.6	0.7	0.6	1.1	1.0	1.0	1.0	1.1
	Citi Macro Risk	0.99	0.0	0.38	0.97	0.82	0.85	0.79	0.59	0.47	0.36	0.35	0.72	0.36	0.32	0.24	0.12	0.15	0.18	0.24	0.15	0.28	0.27	0.27	0.33
Liquidity	LIBOR 1M OIS Spread	338	1	9	15.1	16.5	18.2	21.5	17.2	13.1	11.8	10.1	7.5	7.6	10.6	10.3	7.2	4.9	5.7	5.9	6.7	6.2	5.9	7.4	7.7
	Euro Libor-OIS Spread	196	-2	28	81	81	98	97	77	63	42	39	39	42	33	21	13	11	13	12	9.3	13.3	12.9	13.6	13.8
	Euro Basis Swap Spread	-3	-300	-35	-105	-92	-131	-114	-72	-67	-51	-45	-50	-54	-42	-32	-26	-25	-25	21	-12	-20	-19	-18	-17
Credit	TED Spread	464	9	32	35	44	53	57	49	41	40	37	40	38	35	35	27	20	23	27	23	19	21	23	24
	EmMa Spread	865	149	287	422	352	371	377	368	334	319	327	419	362	325	313	285	274	269	248	259	276	297	278	273
	CDX.NA.IG	279	29	98	144	121	128	120	101	94	91	95	123	112	107	102	99	101	99	94	89	88	91	75	72
	iTraxx 5Y Europe	217	20	101	202	162	185	173	143	129	125	140	180	166	160	149	136	129	123	117	113	116	126	96	94
	iTraxx 5Y E. Crossover	1150	150	430	839	660	757	755	620	568	613	650	719	662	633	592	568	524	497	482	443	447	486	396	389
Sovereign CDS (5Y)	iTraxx 5Y E. Sovereign	386	47	167	339	304	327	357	338	343	269	275	326	282	256	230	148	107	105	111	103	104	105	94	89
	Ireland	1192	5	210	700	694	711	726	621	603	572	566	726	553	512	441	319	173	179	220	190	169	190	159	151
	Portugal	1527	4	56	110	970	1060	1093	1484	1175	1076	961	1185	805	834	662	515	503	498	449	394	392	403	362	331
	Spain	641	3	68	382	340	408	394	376	368	437	476	599	531	534	518	387	305	284	295	270	270	302	241	228
	Italy	592	6	73	470	445	487	503	416	381	397	445	563	488	485	466	356	274	244	278	252	278	305	252	237
	Belgium	406	2	27	260	269	304	316	245	238	233	252	282	240	177	160	128	75	76	83	76	74	76	70	65
	France	250	2	29	187	176	200	222	181	176	169	193	219	189	161	140	114	68	80	91	87	81	77	75	70
	Japan	560	16	104	202	162	206	186	160	138	155	183	193	177	183	211	224	203	166	159	136	125	113	82	78
Rates	BBOX (swaption volat)	138	68	90	94	96	97	94	86	91	89	86	82	80	80	81	78	78	77	77	79	81	81	79	79
Bonds	MOVE (bond volat)	265	49	90	101	107	100	91	72	76	79	63	74	73	70	69	61	71	52	59	66	56	57	49	56
Equities	VIX (equity volat)	81	10	18	43	30	28	23	19	18	16	17	24	17	19	17	16	18	16	18.0	14.3	15.5	12.7	13.5	13.1
	Skew Index (CBOE)	142	106	119	115	121	117	116	122	125	125	120	119	119	114	121	126	119	117	121	122	127	123	119	121
FX	VXY (G7 FX volat)	24	6	10	14	12	13	12	11	10	10	9	11	10	9	9	8	7.5	7.5	8.2	8.8	9.5	9.2	8.7	9.9

Source: IR&M, Bloomberg. *Note: 10-year history where available.

Economic surprises vs macro risk

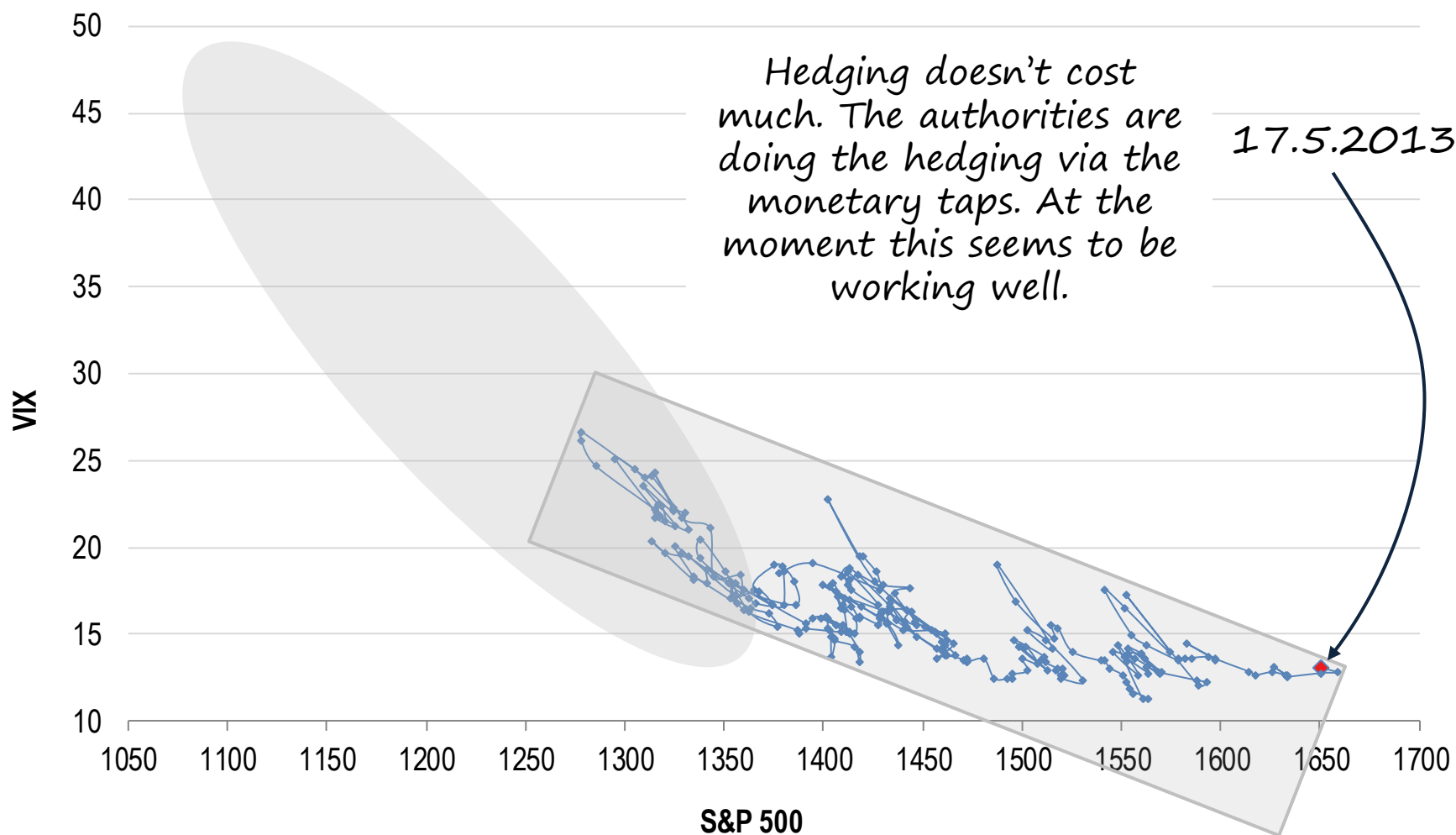
Risk is still on.
Surprises on a global level have continued to fall.



Source: IR&M, Bloomberg, FT 27 March 2013

VIX: 2013 vs 2011 and 2012

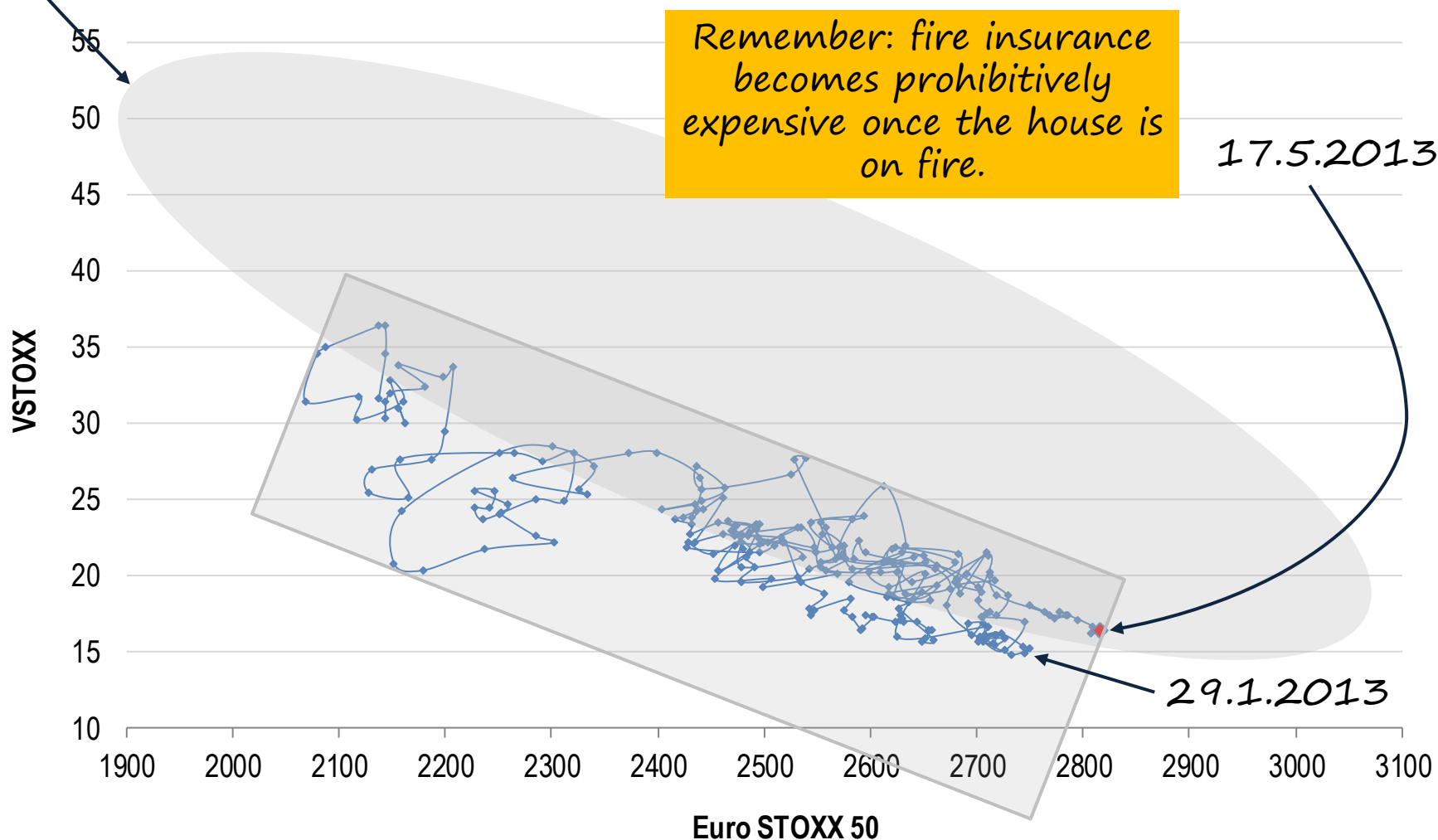
Shaded area shows all closing SPX/VIX combinations during 2011 (oval) and 2012/2013 (rectangle). Dots show 2012 and 2013.



Source: IR&M, Bloomberg. As of 17 May 2013 3:34pm CET.

VSTOXX: 2013 vs 2011 and 2012

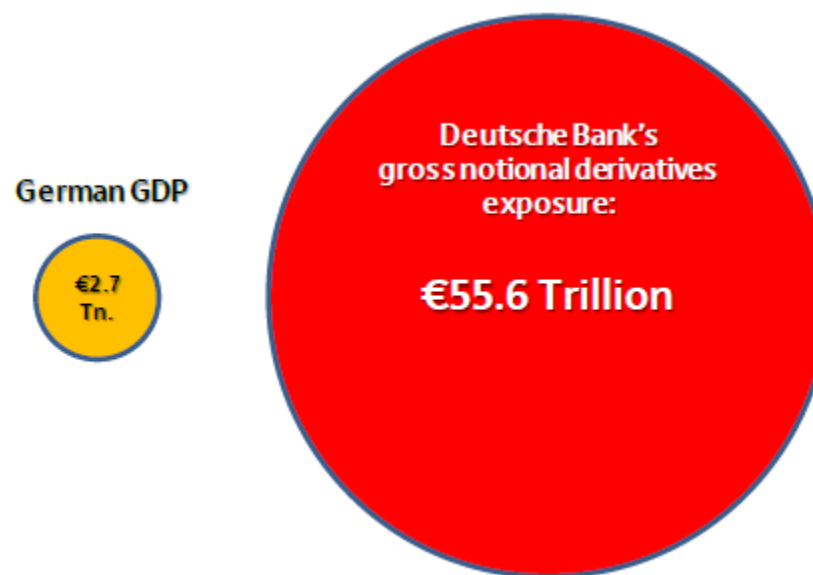
Shaded area shows all closing Euro STOXX 50/VSTOXX* combinations during 2011 (oval) and 2012/2013 (rectangle). Dots show 2012 and 2013.



Source: IR&M, Bloomberg. * Eurozone VIX equivalent: Measures implied volatility of index options on the Euro STOXX 50 index. As of 17 May 2013 3:37pm CET.

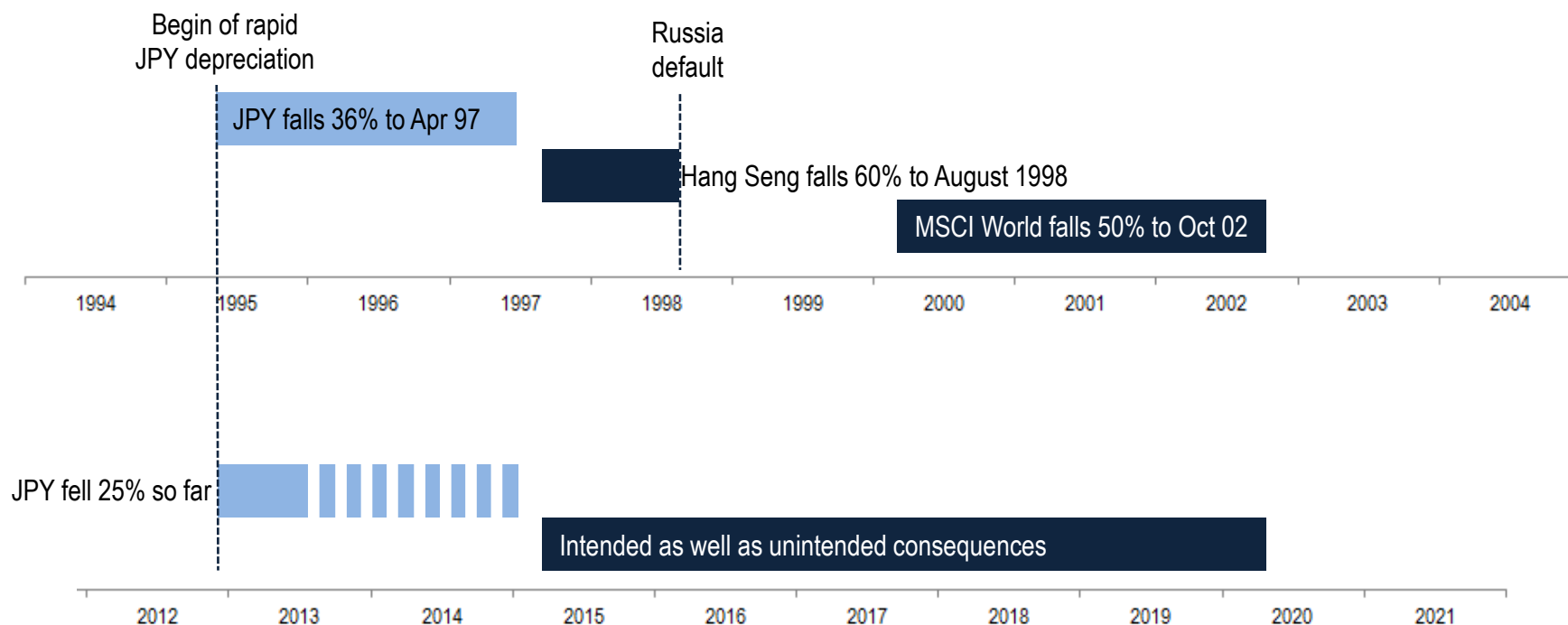
Graph of the week – for what it's worth...

We all know the benefits of netting; it is the net exposure that matters. However, gross exposure is still exposure. It is the “interlinkedness” that is the Achilles’ heel. It only takes one small, disingenuous, fraudulent, or grumpy snowflake to set off an avalanche.



Graph of the month – for what it's worth...

A collapsing Yen was the precursor to the Asian crisis that followed. (Currency war is called war for a reason. War “flattens” things.) Below a tale of two time scales. Abenomics could well be the proverbial butterfly wing flap that causes the tornado elsewhere.



Source: IR&M, Bloomberg. Note: JPY returns against USD. Hang Seng return in local currency terms. MSCI World in USD.

Trivia

Everyone thinks of himself as most compassionate.

Stereotyping in Europe
Who Is Trustworthy, Arrogant and Compassionate
EU nation most likely to be named...

<i>Views in:</i>	Most Trustworthy	Least Trustworthy	Most Arrogant	Least Arrogant	Most Compassionate	Least Compassionate
Britain	Germany	France	France	Britain	Britain	Germany
France	Germany	Greece	France	France	France	Britain
Germany	Germany	Greece/Italy	France	Germany	Germany	Britain
Italy	Germany	Italy	Germany	Spain	Italy	Germany
Spain	Germany	Italy	Germany	Spain	Spain	Germany
Greece	Greece	Germany	Germany	Greece	Greece	Germany
Poland	Germany	Germany	Germany	Poland	Poland	Germany
Czech Rep.	Germany	Greece	Germany	Slovakia	Czech Rep.	Germany

PEW RESEARCH CENTER Q44a-Q46b.

Note that Germany and France, arguably the key players* in the EU, agree on many things...

Source: PEW research, <http://www.pewglobal.org/2013/05/13/the-new-sick-man-of-europe-the-european-union/>

* Judged not by political brilliance and statesmanship but by political capital invested in the project.

Selected publications*

IR&M's risk management research consists of four thematic reports, 25-35 updates, and 45-50 momentum monitors per year.

No understanding – no assurance	3 May 2013	No money	20 July 2012
IR&M momentum monitor (inaugural issue and tutorial)	3 May 2013	Wriston's Law of Capital (Q3 2012 report)	10 July 2012
A new dimension (Q2 2013 report)	19 April 2013	Pompous meddling continues	2 July 2012
A bit of friction here and there	4 April 2013	Empty monetary bag of tricks	22 June 2012
As long as it takes	22 March 2013	Helping hand rather than an invisible one	15 June 2012
Keep it coming	12 March 2013	Fed recommends to hedge too	8 June 2012
The end of a system	1 March 2013	Waiting for the next fix	1 June 2012
Great Unrecovery continues	22 February 2013	Hopium running low	25 May 2012
Showing mettle	15 February 2013	Euro area tearing itself apart	18 May 2012
Currency wars	1 February 2013	PMIs make for horrid reading	7 May 2012
Repressionomics (Q1 2013 report)	18 January 2013	Just in the middle of the river	2 May 2012
Far from over	3 January 2013	Risky fragility	19 April 2012
Wriston's Law of Capital still at work	19 December 2012	What makes bears blush (Q2 2012 report)	11 April 2012
A very long process	5 December 2012	Conditionally well but subject to revision	4 April 2012
In search of a real fix – obviously	22 November 2012	Not yet out of the woods	22 March 2012
Socialising losses	7 November 2012	Eerily unchanged	15 March 2012
No risk (Q4 2012 report)	26 October 2012	Ltroveaneous double liquidity whammy	2 March 2012
No panacea	12 October 2012	Bullish middle-game: an intermezzo?	17 February 2012
No knowledge, no experience	1 October 2012	Shooting the economic lights out	3 February 2012
QE infinity	18 September 2012	Confidence rally	27 January 2012
Draghi put kicks in	7 September 2012	Relatively difficult (Q1 2012 report)	16 January 2012
Enormously ineffective	27 August 2012	Global economy stabilises a bit	22 December 2011
They want your money	16 August 2012	...	
Whatever it takes	6 August 2012	Europe doubling down (Q4 2011, inaugural report)	3 October 2011

Source: IR&M

* IR&M's risk management research is subscription based. Research related to "absolute returns" in general is freely available under www.ineichen-rm.com

Disclaimer

Copyright © 2013 by Ineichen Research and Management AG, Switzerland

All rights reserved. Reproduction or retransmission in whole or in part is prohibited except by permission. The information set forth in this document has been obtained from publicly available sources, unless stated otherwise. All information contained in this report is based on information obtained from sources which Ineichen Research and Management (“IR&M”) believes to be reliable. IR&M provides this report without guarantee of any kind regarding its contents.

This document is for information purposes only and should not be construed as investment advice or an offer to sell (nor the solicitation of an offer to buy) any of the securities it refers to. The information has not been independently verified by IR&M or any of its affiliates. Neither IR&M nor any of its affiliates makes any representations or warranties regarding, or assumes any responsibility for the accuracy, reliability, completeness or applicability of, any information, calculations contained herein, or of any assumptions underlying any information, calculations, estimates or projections contained or reflected herein. Neither this document nor the securities referred to herein have been registered or approved by any regulatory authority of any country or jurisdiction.

This material is confidential and intended solely for the information of the person to whom it has been delivered and may not be distributed in any jurisdiction where such distribution would constitute a violation of applicable law or regulation.

While this document represents the author’s understanding at the time it was prepared, no representation or warranty, either expressed or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein, nor it is intended to be a complete statement or summary of the securities markets or developments referred to in the document. It should not be regarded by recipients as a substitute for the exercise of their own judgment.

Investing in securities and other financial products entails certain risks, including the possible loss of the entire amount invested. Certain investments in particular, including those involving structured products, futures, options and other derivatives, are complex, may entail substantial risk and are not suitable for all investors. The price and value of, and income produced by, securities and other financial products may fluctuate and may be adversely impacted by exchange rates, interest rates or other factors. Information available on such securities may be limited. The securities described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. You should obtain advice from your own tax, financial, legal and accounting advisers to the extent that you deem necessary and only make investment decisions on the basis of your objectives, experience and resources.

Past performance is not necessarily indicative of future results.

Unless specifically stated otherwise, all price information is indicative only.

No liability whatsoever is accepted for any loss (whether direct, indirect or consequential) that may arise from any use of the information contained in or derived from this document. IR&M does not provide tax advice and nothing contained herein is intended to be, or should be construed as a, tax advice. Recipients of this report should seek tax advice based on the recipient’s own particular circumstances from an independent tax adviser.