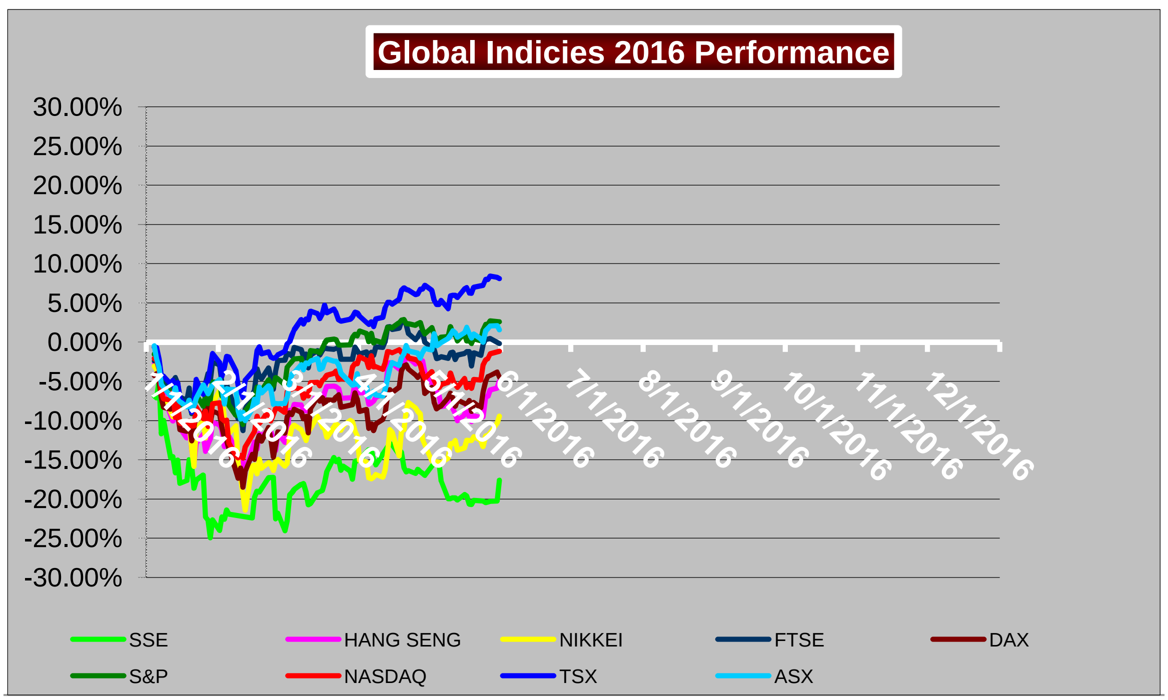
GDB June 2016 Newsletter

Monthly Market Summary:

2016 May Market Activity		
SSE COMPOSITE	***2,916.62***	-21.70 (-0.74%)
HANG SENG	***20,815.09***	-251.96 (-1.20%)
NIKKEI 225	***17,234.98***	+568.93 (3.41%)
FTSE 100	***6,230.80***	-11.10 (-0.18%)
DAX	***10,262.74***	+223.77 (2.23%)
DOW	***17,787.20***	+13.56 (0.08%)
S&P 500	***2,096.95***	+31.65 (1.53%)
NASDAQ COMPOSITE	***4,948.05***	+172.69 (3.62%)
ASX 200	***5,378.60***	+126.40 (2.41%)
TSX COMPOSITE	***14,065.80***	+114.30 (0.82%)



Investment Themes:

On Thursday June 24, the United Kingdom held the United Kingdom European Union Membership referendum to decide its fate in the EU. An overwhelmingly 73% of the 46.5 million registered voters turned out to cast their vote. And the results caught many traders and investors blind sighted. 51.89% of the people voted to withdraw UK's membership in the EU, while 48.11% chose to remain. The result of the vote began UK's path to what has been termed "Brexit", an uncertain and unprecedented journey in the history of the European Union.

The immediate fallout from the global financial market was swift and drastic. Investor had been confident before the vote that a Brexit vote would not be a possible outcome were left scrambling to reposition. The British Pound took the brunt of the sharp market reaction, falling at one point 11% to 1.3230. It recovered some of the losses at close, nonetheless, still down 7.54% for the day, logging in the currency's worst single day drop in history. The global equity markets were reminded of the volatility not seen since the days of the financial crisis. On the day following the Brexit vote, a total of $2.1 trillion in market cap vanished from the global equity markets, surpassing the previous one-day record of $1.9 trillion set on September 29, 2008, during the peak of the financial crisis. By the close on the following Monday, global equity markets shed another $930 billion. Indiscriminate selling in risky assets led investors to pile money into safe heaven assets. Gold breached $1,300 an ounce, nearly up 5% on the day. The Yen soared as much as 18.5% against the Pound intraday before settling at 139.5325 Yen, up 13.2% against the Sterling at day end. Government Bonds saw yields falling to record lows as investors flock to safety. Prices and demands move inversely to yields. In Europe, the 10-year yield on UK government bond tumbled below 1% for the first time ever. The yield on the German bund fell deep into negative territory at -0.10%. In the US, the yield on 10-year bond fell to near record low of 1.406%, last seen during the flight to safety in 2012 European sovereign debt crisis.

The shock to the financial markets from the Brexit vote though severe, did not prevent investors from jumping right back in, at least observing from the performance in the equity market in the week immediately following. The FTSE at the end of the month actually closed higher than pre-Brexit level. So were the astonishing recoveries in the major US indices, recouping much of the losses during the two consecutive days of relentless selling. Markets usually over-react to bad news, but given the uncertainty that could manifest from the UK leaving the EU, the absence of a definitive time table, the lack of preparedness and leadership from the British government, and the serious ramification imposed on the political stability of the European Union, the Brexit event has introduced a considerable new element of geopolitical risk to the modus operendi. In turn, the V-shaped rebound seen in the equity markets could be a reversed over-reaction from traders, hoping an eventual Brexit would not materialize and further speculating central banks would step in to stimulate. However, at the current low interest rate environment and unconventional monetary policies, we would question how much room the BOE or other central banks have to maneuver. Just look at the surging Yen in recent month and BOJ's ongoing promise to intervention without any decisive action.

Compared to the equity market, the much larger currency market, tend to agree with the above notion. In the week following while equities rallied, the currency traders betted with much reserved caution best seen in the follow-on performance in the Sterling. The British Pound continues to trend lower below the 1.3660 close on the day following the Brexit vote. As at the writing of the newsletter, it is fetching 1.3243 dollar. As the turmoil unfolds and the real visible economic impacts become apparent, we believe the British Pound will the most visible asset class that reflects the economic deterioration in the UK. Even if UK eventually ends up not severing its membership ties, it will take substantial time and patience for investors to regain confidence in the currency. And if the BOE stimulates as promised? Well, it puts additional pressure on the Pound. So from all angles, it's a lose-lose situation for the Pound.