Alpesh Patel's April Newsletter

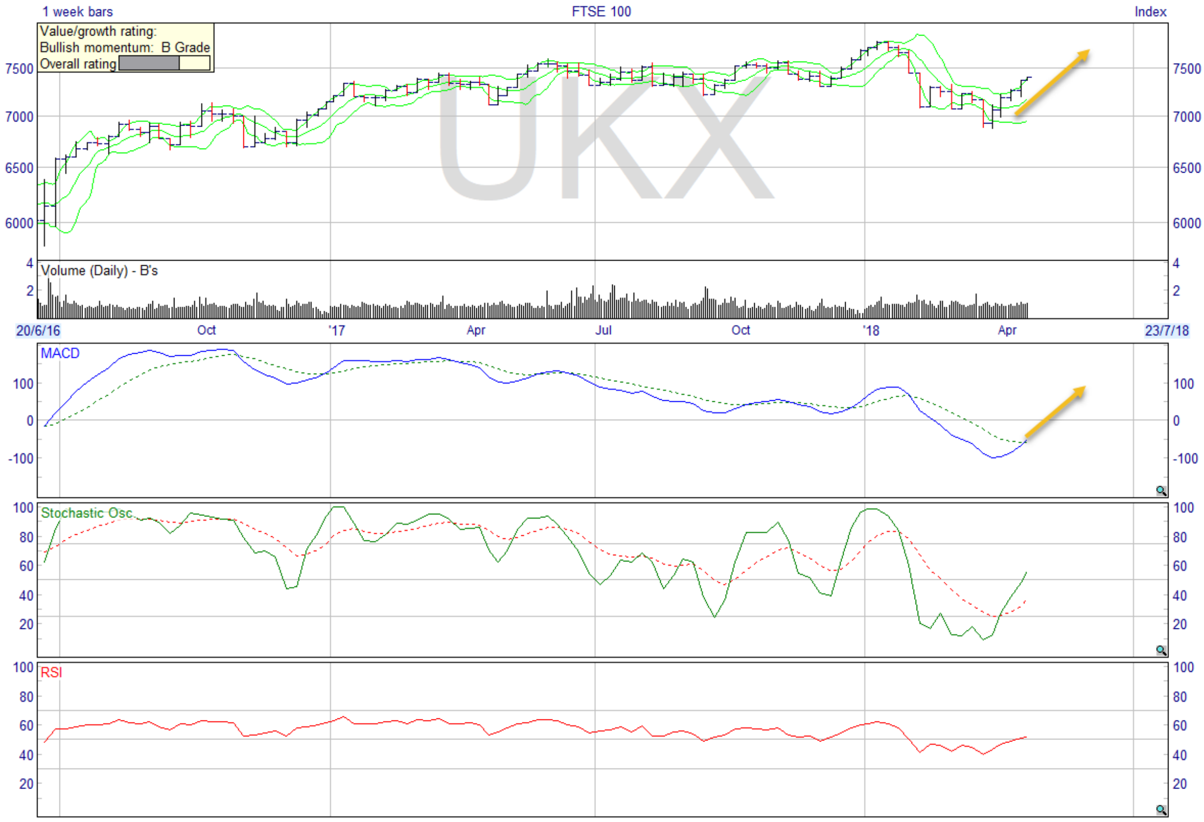
Exclusively for ShareScope Alpesh Patel Special Edition Subscribers

25 April 2018

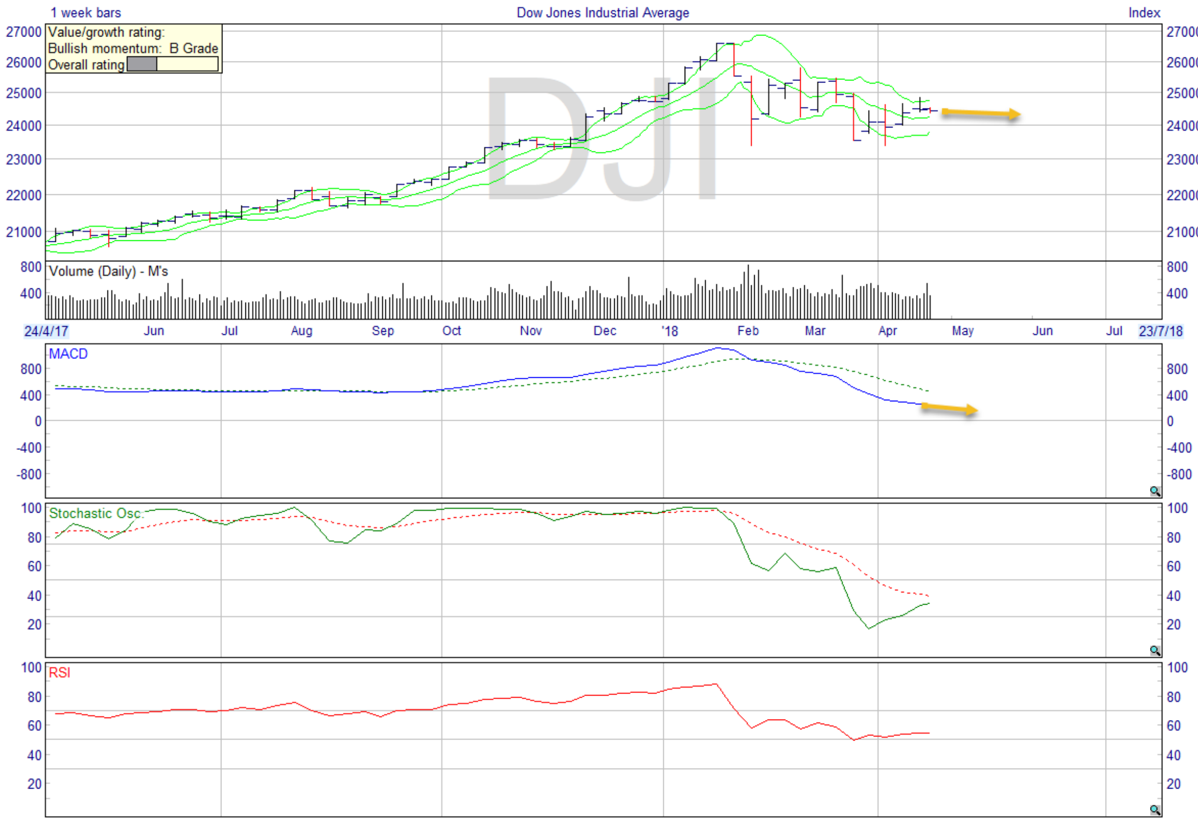
Welcome to my April newsletter. May you live in interesting times – but this interesting?! So where are the opportunities given OPEC, Russia, Syria, Brexit, Chemical Warfare, Trump, Korea…have I missed anything?

My view on the markets

Well you wouldn't have expected the FTSE's recent April run. I like to follow the trend.



As for the Dow, it's momentum is suggesting sideways for now:



Top insights from the City

The threats keep coming: Russia, Syria, Brexit, inflation, trade wars, radioactivity, Middle East, Korea. The IMF's Global Financial Stability report did not help allay my concerns; instead it added to them.[1] Add to that 75% of the ultra rich say a recession is likely in 2 years.[2]

IMF

They even said:

"Financial vulnerabilities, which have accumulated during years of extremely low rates and volatility, could make the road ahead bumpy and could put growth at risk."

"Valuations of risky assets are still stretched, with some late-stage credit cycle dynamics emerging, reminiscent of the pre-crisis period…This makes markets exposed to a sharp tightening in financial conditions, which could lead to a sudden unwinding of risk premiums and a repricing of risky assets."

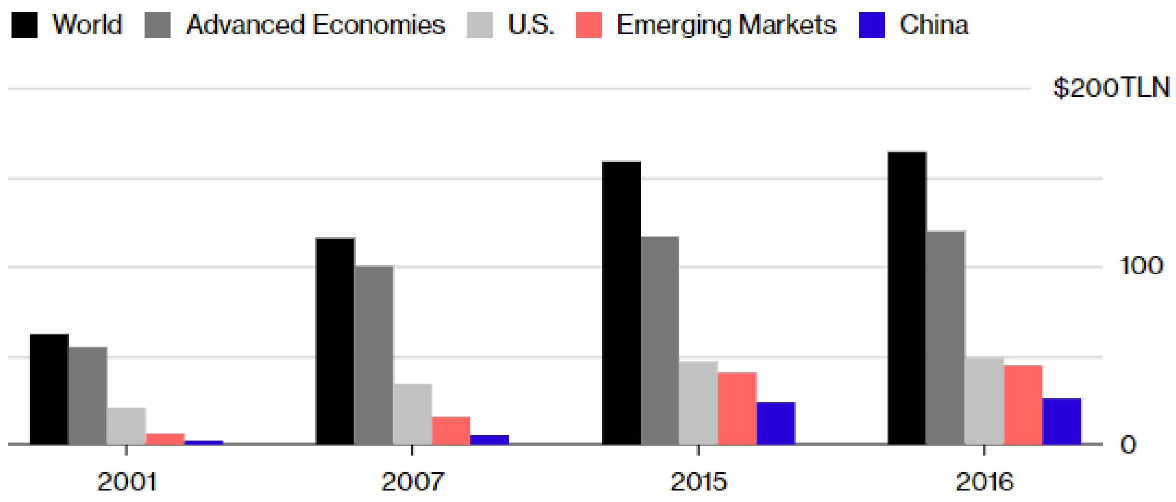
---

[1] http://www.imf.org/external/mmedia/view.aspx?vid=5771229551001

[2] https://finance.yahoo.com/news/75-ultra-rich-forecast-us-104100334.html?guccounter=1

World Debt

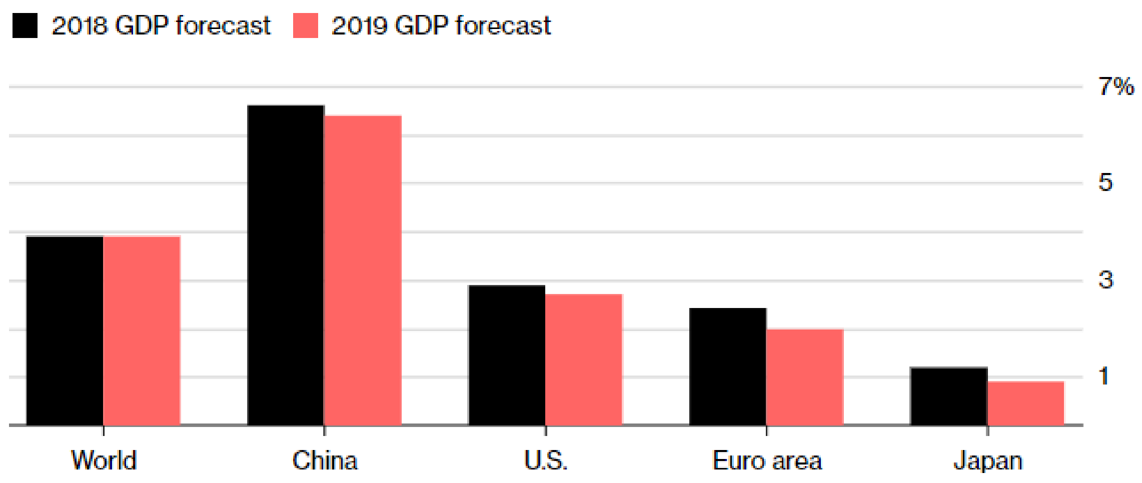
Add to this that world debt is at a record $164 trillion, just as EU, UK and US Central Banks are raising rates.[3]



Sources: Global Debt Database; and IMF staff calculations

GDP Growth

And there is more, GDP growth is set to slow in 2019 compared to 2018.



Source: International Monetary Fund

Interest Rates

Combine with this rising rates, as warned by the likes of Goldman Sachs, and you have an explosive mix potentially. [4]

[3] https://www.bloomberg.com/news/articles/2018-04-18/world-debt-hits-record-164-trillion-as-crisis-hangover-lingers

[4] https://www.housingwire.com/articles/43061-goldman-sachs-fed-to-raise-rates-once-a-quarter-until-2019

Oil

What possible reason with growth on the cards worldwide would OPEC and Russia have to cut supply? It's hard to work out any reason so a bubble up in the price of oil would be the logical deduction. [5] You only have to look at oil consumption to know that demand is in place. China and India are the second and third largest consumers and continue to grow their GDP. [6]

And now for the good news

Well Goldman Sachs is not worried. The CEO of the firm says it looks 'awfully good'. [7] UBS think the risks will start in 3 years.[8] Like Goldman Sachs, they do not see a trade war coming. I love it when big banks are direct:

"Global equities are supported by solid earnings growth. US companies, which make up about half of the global stock market, are benefiting from tax relief and a new fiscal spending package. By price-to-earnings ratio, the global stock valuation is slightly below long-term average. We remain overweight Eurozone versus UK stocks. Given their cyclical sector composition and high operational leverage, Eurozone companies are well placed to benefit from robust global demand, while UK firms should lag other regions in terms of earnings growth. We are also overweight emerging market (EM) versus Australian stocks."[9]

	We like...	We don't like...
Equities	Global equities	UK equities
	Eurozone equities	Australian equities
	Eurozone value opportunities	
	Emerging market equities	
	Sustainable value creation in EM	
	"Buy write" strategy on US equities (↗)	
	US smart beta	
	Some protection via equity put options	
Bonds	Corporate hybrids	Developed market high grade bonds
	US leveraged loans	"Well-worn" bonds
	EM sovereign bonds in USD	Euro high yield
	Selected EM bonds (↗)	10-year Japanese gvt bonds vs. JPY cash
	10-year US Treasuries vs. USD cash	
Foreign exchange	EUR	USD
	CAD (↘)	USD (↗)
	EM FX (BRL, INR, RUB, TRY)	DM FX (AUD, HUF, NOK, TWD)
	GBP	CHF
	JPY	NZD

[5] http://www.businessinsider.com/goldman-forecasts-80-dollar-oil-as-trump-says-opec-keeping-prices-high-2018-4/?IR=T
[6] https://www.eia.gov/tools/faqs/faq.php?id=709&t=6
[7] https://www.cnbc.com/2018/04/18/goldman-sachs-ceo-lloyd-blankfein-my-expectation-is-david-solomon-will-succeed-me.html
[8] https://www.ubs.com/content/dam/static/wm/CIO/monthly-base/CIO-monthly-base-en.pdf
[9] https://www.ubs.com/content/dam/static/wm/CIO/monthly-base/CIO-monthly-base-en.pdf

Traders at brokers such as 24option are able to use ‘long’ and ‘short’ positions and it is times when the fear of falls rises, that the ability to short comes in handy.

Exhibit 2: World stock market returns (local currency)

2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	YTD
MSCI EM 28.8%	MSCI Asia ex Japan 38.0%	UK FTSE 100 -28.3%	MSCI Asia ex Japan 67.2%	MSCI Asia ex Japan 15.6%	US S&P 500 2.1%	Japan TOPIX 20.9%	Japan TOPIX 54.4%	US S&P 500 13.7%	Japan TOPIX 12.1%	UK FTSE 100 19.1%	MSCI Asia ex Japan 35.9%	MSCI EM 0.8%
MSCI Asia ex Japan 28.6%	MSCI EM 33.6%	US S&P 500 -37.0%	MSCI EM 62.8%	US S&P 500 15.1%	UK FTSE 100 -2.2%	MSCI Europe ex UK 20.0%	US S&P 500 32.4%	Japan TOPIX 10.3%	MSCI Europe ex UK 9.1%	US S&P 500 12.0%	MSCI EM 31.0%	MSCI Asia ex Japan 0.5%
MSCI Europe ex UK 22.5%	UK FTSE 100 7.4%	Japan TOPIX -40.6%	MSCI Europe ex UK 29.0%	MSCI EM 14.4%	MSCI Europe ex UK -12.1%	MSCI Asia ex Japan 19.7%	MSCI Europe ex UK 24.2%	MSCI Asia ex Japan 7.7%	US S&P 500 1.4%	MSCI EM 10.1%	Japan TOPIX 22.2%	US S&P 500 -0.8%
US S&P 500 15.8%	MSCI Europe ex UK 6.6%	MSCI Europe ex UK -42.7%	UK FTSE 100 27.3%	UK FTSE 100 12.6%	MSCI EM -12.5%	MSCI EM 17.4%	UK FTSE 100 18.7%	MSCI Europe ex UK 7.4%	UK FTSE 100 -1.3%	MSCI Asia ex Japan 6.4%	US S&P 500 21.8%	MSCI Europe ex UK -3.0%
UK FTSE 100 14.4%	US S&P 500 5.5%	MSCI EM -45.7%	US S&P 500 26.5%	MSCI Europe ex UK 5.1%	MSCI Asia ex Japan -14.6%	US S&P 500 16.0%	MSCI Asia ex Japan 6.2%	MSCI EM 5.6%	MSCI Asia ex Japan -5.3%	MSCI Europe ex UK 3.2%	MSCI Europe ex UK 14.5%	Japan TOPIX -4.7%
Japan TOPIX 3.0%	Japan TOPIX -11.1%	MSCI Asia ex Japan -47.7%	Japan TOPIX 7.6%	Japan TOPIX 1.0%	Japan TOPIX -17.0%	UK FTSE 100 10.0%	MSCI EM 3.8%	UK FTSE 100 0.7%	MSCI EM -5.4%	Japan TOPIX 0.3%	UK FTSE 100 11.9%	UK FTSE 100 -7.2%

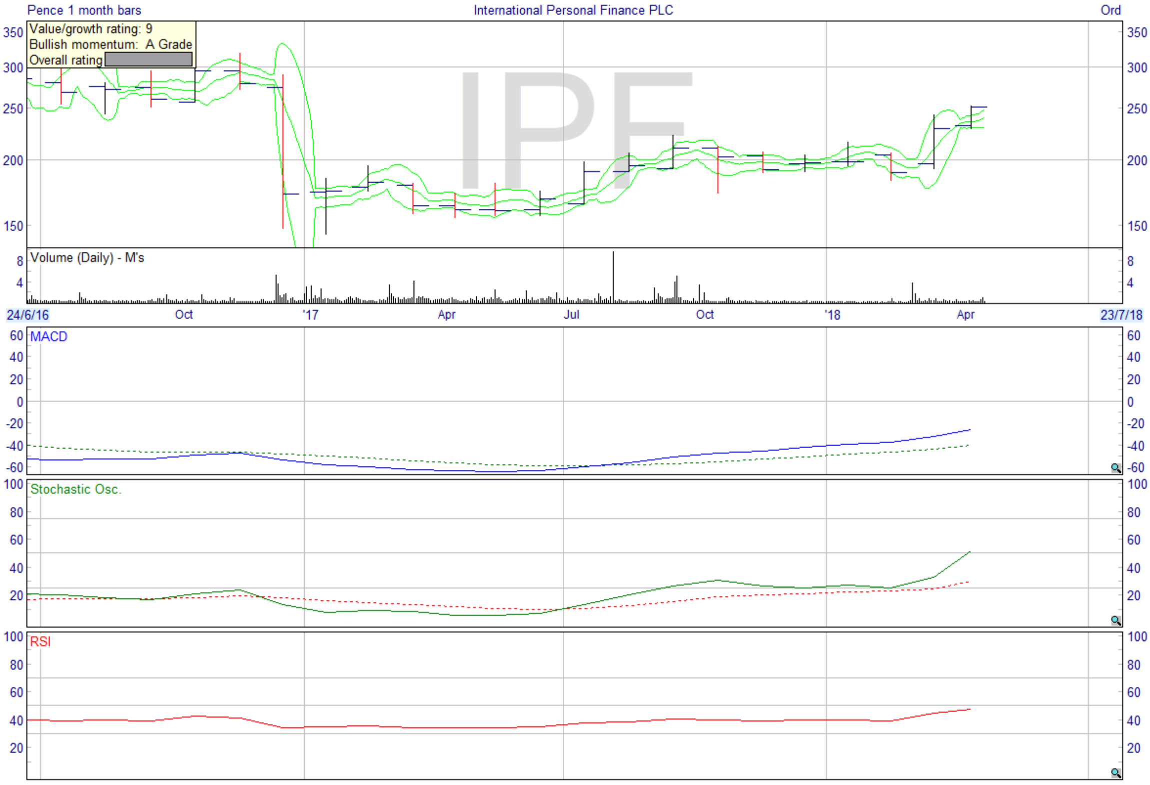
Source: FactSet, FTSE, MSCI, Standard & Poor’s, TOPIX, J.P. Morgan Asset Management. All indices are total return in local currency. Data as of 31 March 2018.

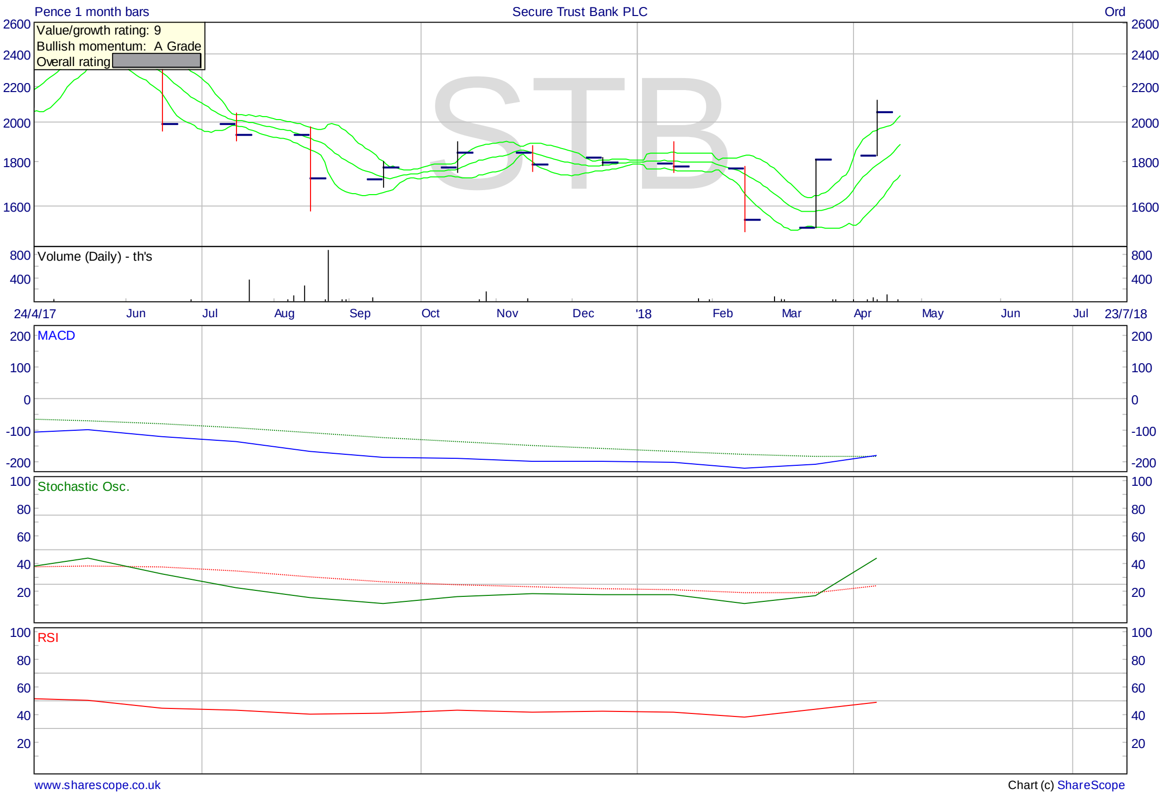
My favourite Value/Growth picks this month

I’ve applied the APSE Value Growth data mining filter to the LSE shares list. Look at the 9s – they are my most highly rated for a 12 month hold, for those who like buy and hold.

No.	Name	EPIC	**Alpesh value/ growth rating**	Alpesh bullish momentum rating	Alpesh overall rating	Close	Price% 2 trading days ago	Price% 5 trading days ago	Price% 2 weeks ago	Price% 3 months ago	Price% 6 months ago	Capital (£m)	Rolling PEG 1	Rolling PE 1
1	International Personal Fina	IPF	9	A Grade		£2.51¾	1.37	5.18	5.36	22.11	26.22	561.8	0.29	10.51
2	Keller Group PLC	KLR	9	A Grade		£10.34	1.57	6.60	14.00	-0.58	14.44	744.5	0.90	11.46
3	Miton Group PLC	MGR	9	A Grade		48p	6.67	9.09	14.97	7.26	20.00	82.9	0.85	13.93
4	National Express Group PL	NEX	9	A Grade		£4.07¼	0.84	-0.88	1.90	11.07	18.41	2,083.8	0.67	15.17
5	Premier Asset Managemer	PAM	9	A Grade		£2.44	-3.94	0.83	8.93	-2.79	21.39	258.2	0.48	19.75
6	S & U PLC	SUS	9	A Grade		£25.25	3.27	5.21	7.91	9.31	23.62	303.0	0.64	11.93
7	Secure Trust Bank PLC	STB	9	A Grade		£20.55	4.58	9.75	9.16	14.80	10.63	379.7	0.33	16.51
8	Vp PLC	VP.	9	A Grade		£8.80	-2.22	-3.30	-0.90	-0.11	9.32	353.4	0.61	11.04
9	Ibstock PLC	IBST	8	A Grade		£3.02½	1.14	3.07	4.49	14.55	22.28	1,229.0	0.77	16.81
10	Spectris PLC	SXS	8	B Grade		£27.09	0.63	1.31	1.57	2.54	9.50	3,219.8	0.62	22.23
11	easyJet PLC	EZJ	7	B Grade		£16.28	1.24	0.28	-1.66	-0.94	23.33	6,466.5	0.76	16.84
12	Huntsworth PLC	HNT	7	A Grade		98½p	0.61	2.71	3.79	18.80	24.81	325.5	0.56	19.53
13	IWG PLC	IWG	7	A Grade		£2.61½	0.58	5.02	12.57	-5.94	23.35	2,383.5	0.82	19.68
14	Smurfit Kappa Group PLC	SKG	7	B Grade		£31.08	-2.51	1.17	3.19	18.63	38.75	7,371.5	0.86	17.46
15	St Ives PLC	SIV	7	B Grade		87p	-1.25	-0.69	-1.59	14.34	13.22	124.1	0.51	6.90
16	Haynes Publishing Group F	HYNS	6	A Grade		£2.38		1.71	2.59	17.82	17.53	36.0	0.33	21.96

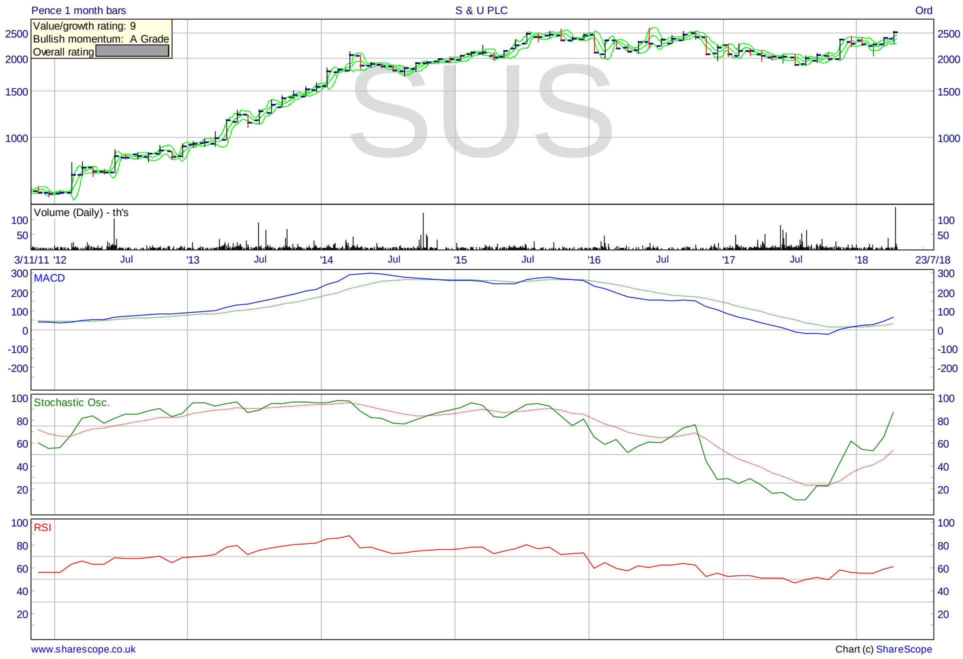
Catching my eye in particular are these for their ratings based on valuation, growth and income:





My favourite Momentum/Value picks this month

The point of this filter is to find undervalued stocks showing some momentum.



Top trades for this month

Last month I picked this: Huntsworth, Vitec and Dechra.

This month: I still like these trades and Dechra has done especially well. This month I will add Tesco – Growth, momentum, income all in place.

Trading Psychology

When I wrote my first book, there was a very good reason I called it 'The Mind of a Trader'. Every one of the 10 leading traders of the world I interviewed for the book told me that psychology was key to success and wealth.

Detachment

Hedge fund manager, Bernard Oppetit, put it this way to me, "Whether I get out at a profit or loss does not matter." And this surprised me. I expected the world's leading traders to be more attached to their results and performance. In fact what was a key characteristic of them all was their detachment to the outcomes of their actions; all were far more focused getting the process right and concentrating on that.

Detachment was important for another reason. All those I interviewed were at the top of their professions. They were managers and leaders, not just traders. That sense of mental calm was a critical part of their success.

Pat Arbor, Chair of the Chicago Board of trade put it like this, "The trouble with the loss is not only the loss of money but it's the ego."

But detachment also meant, in the opinion of legend David Kyte, "I think the best traders are those who don't read the papers'. These are people detached from broader noise in other words. He would look to see if the bulls were 'running out of steam' and the bears taking over – regardless of what the news might be or what *should* be happening.

Discipline

Linked to detachment, was their discipline. Again, as Oppetit put it, "it takes a lot of patience and energy and motivation". You need to have a sense of discipline for that. But discipline for what? It was discipline in following their processes to get in and out of a trade as per their processes and system, and not deviate. This means not adding to losing trades in the case of all the hedge fund managers I spoke to. It means not making excuses when you know you are suffering a loss and should exit according to your system. It also means not being greedy when you know the profits have run their course.

Key to the psychology was having a systematic approach in mind and following it and ignoring extraneous matters (such as baby needs new shoes) which can play with your mind and seduce you from deviating from your discipline.

As Bill Lipschutz, Global Head of Forex at Salomon Brothers put it, "If most traders would learn to sit on their hands, they would make a lot more money."

Tenacity, Fearlessness & Ambition

Do not think from these psychology traits, that these leading profitable traders are not passionate. Jon Najarian, a floor trader, put it this way, “Unless you are willing to bang your head against the door until you break through, you are not going to make it.” But there is tenacity and pushing your luck too from a psychology view. David Kyte, another legendary floor trader said, “You make your own luck. If you get in at 50, and it goes to 60, 70, 80, you were lucky and that’s also pushing your luck”.

The underlying theme of letting your profits run, not being too fearful either is clear to me. But, Brian Winterflood, who has managed many traders in his life as a City of London legend, noted in the book how important ambition is for success. His point being you do have to love what you do as a trader to succeed!

Trade Size

You may think money management, trading strategy and psychology are different. Actually, they are inter-related. Again, what surprised me about the leading traders in the world that I interviewed was that they did not take big risks or big bets. Of course they had lots of capital, but in terms of how much of that was risked on any one trade, it was tiny.

This, traders like David Kyte, explained was not just in case they were wrong in a trade (they did not try to be right all the time) but also for the psychology – that with less at risk in each trade, it was easier to maintain calm and therefore your disciple, especially when it came to cutting your losses.

Therefore, these leading traders made their lives easier as a result of their trade size rules. They also had the benefit of avoiding big losing trades, which otherwise could easily wreck a good record or month and additionally it also meant that they were not pressuring themselves to be right, because if they were wrong, the loss was small.

It’s these small changes which allowed me, learning from these legends, some of whom became my mentors, to go from a University student to 10 years later a hedge fund manager.

In the words of Bernard Oppetit, “You do not need to risk a lot to profit a lot”. In the words of Pat Arbor, then Chairman of the world’s largest exchange – the Chicago Board of Trade, “A good trader ends up being one who accumulates capital over a period of time”.

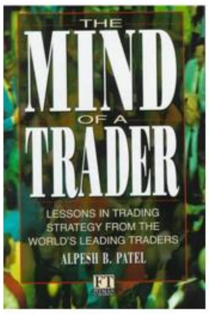
Risk Aversion
The leading traders are well aware trading is about fear and anxiety. “You have to know what it’s like to feel pain, but you can’t be afraid of it” said Lipschutz. They had an aversion to risk however. They ensured that they stacked the odds in their favour on any trade using their methodologies. Most of the traders I met were trend followers (either following trends after a breakout or a reversal).

The way they put the odds in their favour was to ensure that based on their experience of such trades before, they could start small, and if they were wrong, therefore lose small, but if in profit, could add to the winning trade from their profits and so risk their profits to make more, rather than risk too much capital. Capital preservation was the most important thing.

Martin Burton, another trading legend, this time out of London, said “I am totally at ease with cutting out a position too early that I am at unease with.”

Biases
One of my favourite interviewees was Bill Lipschutz, who was Global Head of Forex at Salomon Brothers so pretty much the largest forex trader in the world. His Chairman was Warren Buffett. I used these interviews as a source of my lectures as a Visiting Fellow in Business and Industry at Corpus Christi College, Oxford University. These were at a time when for the first time the Nobel Committee recognized the significance of behavioural finance with their prize to Daniel Kahneman.

MY MENTOR FROM MY BOOK: BILL LIPSHUTZ & HIS CHAIRMAN



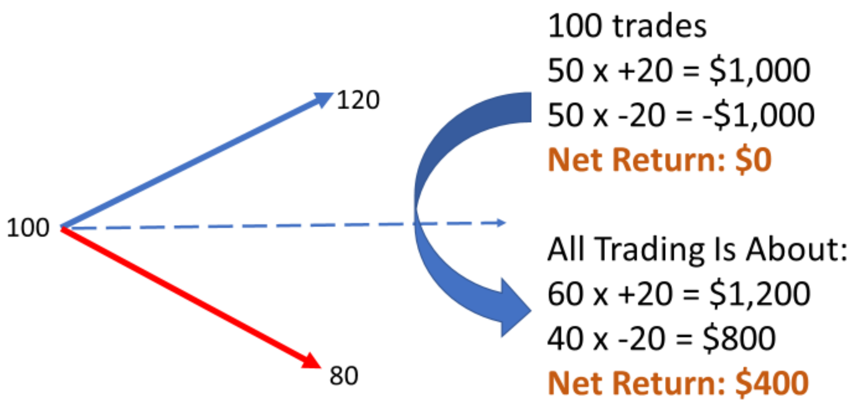
Your Mind is Your Profit

There are many biases that influence our reasoning. Popular literature recognizes 53 different types of cognitive biases (Hilbert, 2012); however, four of them are particularly important and significantly influence risk calculations and strategic decision making (Das, & Teng, 1999). These cognitive biases are:

- **Prior hypotheses and focusing on limited target** - this happens when a decision maker brings hypothesis and personal beliefs into decision-making process without previously inspecting the relevant data. Consequently, the decision-maker tends to overlook the information and evidence that can prove the opposite of what he thinks. This is a major problem for traders because instead of being detached and dispassionate when looking at data, they let their pre-existing trades and losses affect their future decisions.

- **Exposure to limited alternatives** - in the situation when data is incomplete, decision makers tend to focus on limited numbers of alternatives because they usually fill in the missing data with intuition instead of trying to get additional information. Traders here do trades they shouldn't. Instead of waiting for high probability trades, instead they dive in impatiently.

- **Insensitivity to outcome probabilities** - if a manager is influenced more by the value of possible outcomes then by the magnitude of probabilities, he/she will tend to make very risky and hazardous decisions that are not based on statistical calculations of probabilities. Here the trader thinks how much money he will make, not how likely he is to make it. In trading, all we are trying to do is make small incremental gains, not huge windfalls. In trading we need high probability trades. In essence we are trying to do this:



- **Illusion of manageability** - when decision-makers intuitively believe that success is more probable than what statistical models predicted they can become overly optimistic. Consequently, they tend to overlook risks and develop illusion of control in uncontrollable situations. In addition, in these situations, they irrationally think that they can and will solve every possible problem that arose as a result of their decisions (Das, & Teng, 1999).

Personal Activities

I found this article in the Daily Express about me from January! But I only came across it this month!

'The EU looks like a closed shop!' Financial boss LOSES IT on air in FIERY TV interview

FINANCIAL expert Alpesh Patel condemned the EU for threatening to exclude financial services from a post-Brexit trade deal with the UK.

EXPRESS.CO.UK

Also I kept on top of the BBC Newsroom!

I gave a talk in Parliament for the City Hindu Network and City Sikh Network with Shadow Chief Secretary to the Treasury.