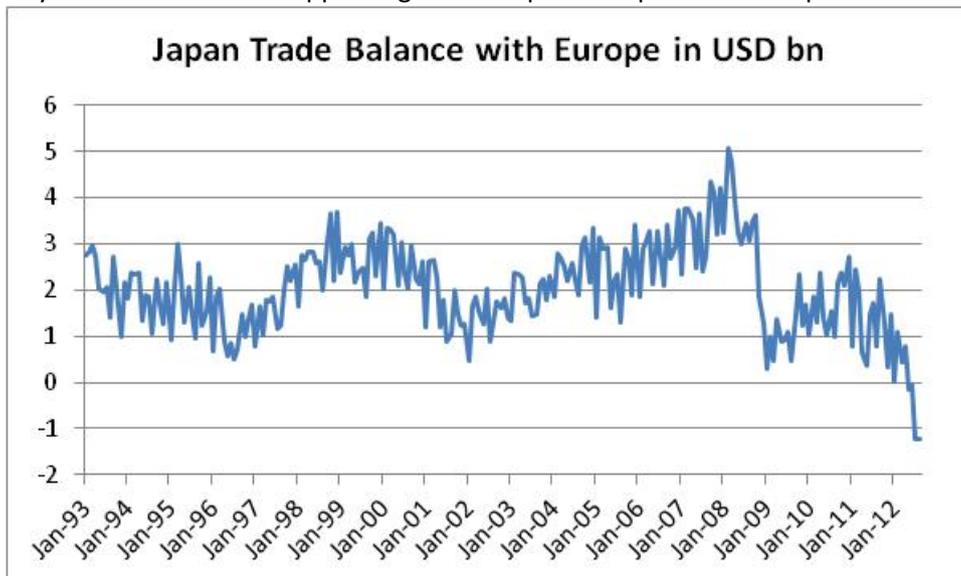




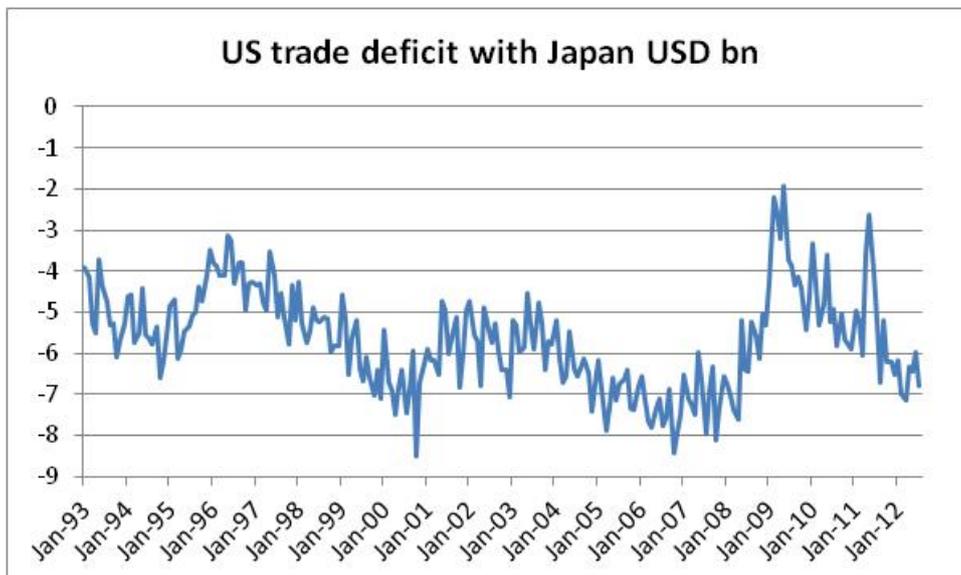
Lessons from Japan

One of the most amazing things about the investment industry is how it can get things repeatedly wrong over many years and then never pause to reflect on where it went wrong. The most extreme example of this is the market for Japanese yen and Japanese government bonds (JGBs). While the yen and JGB are now more popular than they were, for most of my working career most fund managers have been very bearish on the yen and Japanese bonds. Despite market bearishness the yen and JGBs have been good investments. There are three reasons in my view. Firstly, is the current account surplus which has meant that Japan has not needed foreigners to fund their government spending and hence Japan has been very much in control of its own destiny. Secondly, a relatively high savings rate has meant that the Japanese have had the ability to soak up the supply of JGBs issued by the government. Finally, a mildly deflationary environment has made bonds attractive to domestic investors.

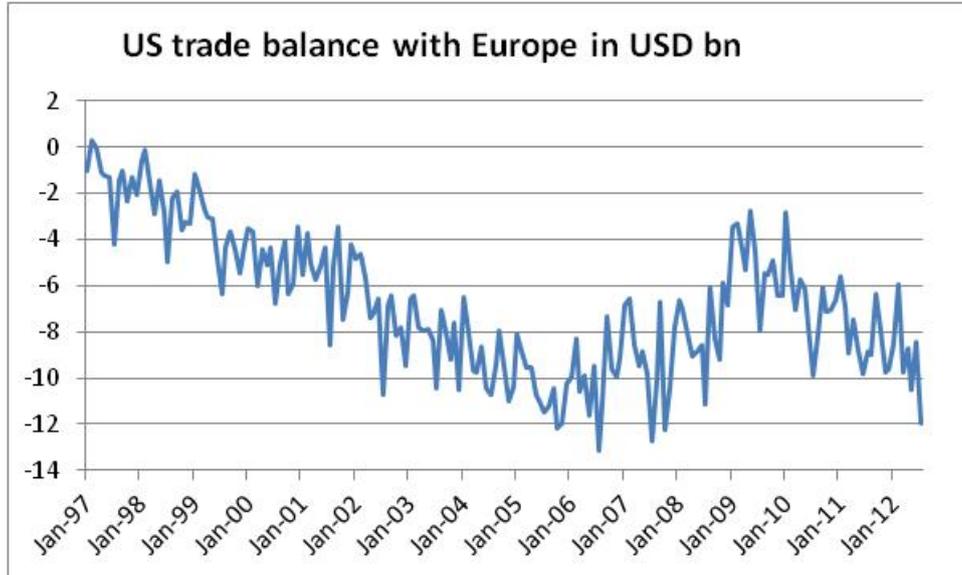
In my view, the market is about to make a similar mistake in terms of the Euro and European bonds. I believe that market values follow economic trends, and the biggest returns are available to investors when they look for break in trends, which in turn will lead to long term changes in the markets. One of the most interesting trend changes in the last year has been the disappearing trade surplus of Japan with Europe.



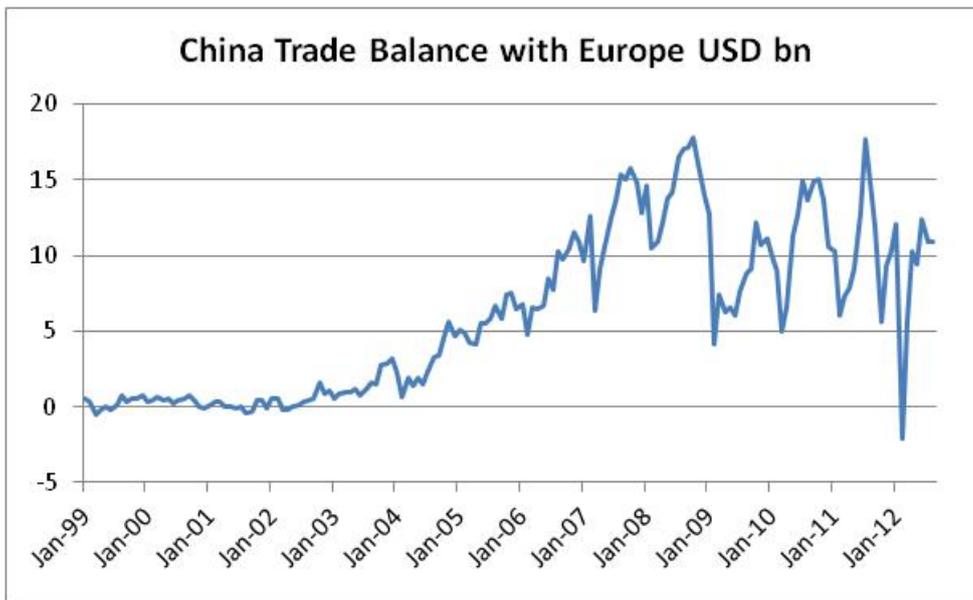
As can be seen Europe is running a trade surplus with Japan. This is the first time in at least 30 years. Intriguingly, the US trade deficit with Japan has not seen a similar decrease, suggesting a massive improvement in European competitiveness.



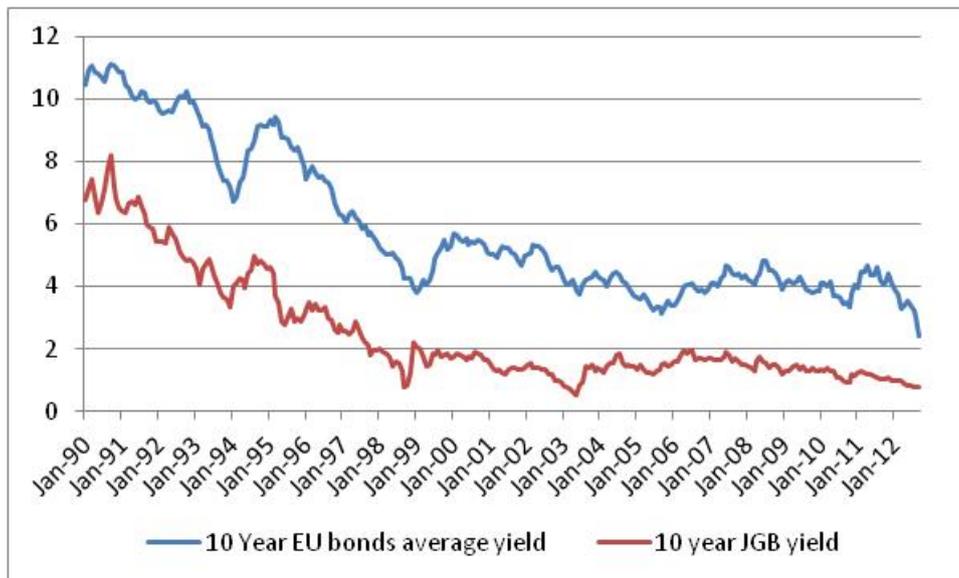
Europe has also managed to move back to close to all time high trade surplus with the US.



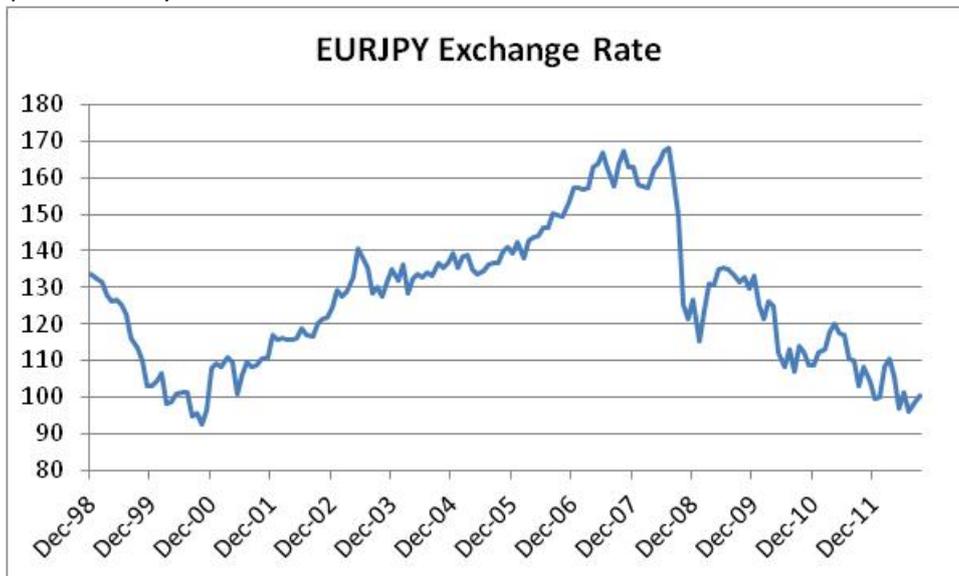
And has managed to improve its trade deficit with China.



The European data is also reflecting a dramatic improvement in the current accounts of peripheral Europe, with Italy, Spain and Portugal all reporting best current accounts for many years. The combination of an improving current account, slowing population growth, high domestic savings rate and the prospect of a prolonged deleveraging cycle in Europe all lead me to believe that Europe is closely resembling Japan. To my mind the trade data is suggesting that European bonds offer much better value than Japanese bonds. Compared to Japanese bonds, yields have a long way to converge.



It is also suggestive that the Euro is more likely to become a safe haven currency going forward. Certainly it looks too cheap versus the yen.



In my view, much like JGBs were seen as a bad investment 10 years ago, with yields too low and the currency destined to be weak, the trade data is suggesting that European bonds and the Euro are likely to be much stronger than the market expects.

Information

- Issue date: 10th October 2012
- Source: Bloomberg, unless otherwise stated
- Investor Relations: Alain Zakeossian, Carol Brown
- Email: info@horsemancapital.com
- Telephone: +44 (0)20 7838 7580
- Website: www.horsemancapital.com
- Business and registered address: Horseman Capital Management Limited, 9 Chester Close, Chester Street, London SW1X 7BE, United Kingdom. Registered in England and Wales - Company number: 04034280

This newsletter has been prepared and issued by Horseman Capital Management Ltd, (the "Firm"), authorised and regulated by the Financial Services Authority. This newsletter has been approved as a financial promotion by the Firm and as such is intended **only for professional clients and eligible counterparties in the United Kingdom and it is not available for retail client use**. It is not intended for distribution to any other country where such distribution or use would be contrary to local law or regulation. This newsletter is provided for information purposes only and should not be regarded as an offer to buy or sell any investments or related services that may be referenced herein. The views expressed in this newsletter are the views of the Firm at time of publication and may change over time. Nothing in this newsletter constitutes investment, legal tax or other advice nor is it to be relied upon in making an investment decision. No recommendation is made positive or otherwise regarding individual securities mentioned herein. No guarantee is made as to the accuracy of the information provided which has been obtained from sources believed to be reliable. Past performance is not indicative of future performance. The price of shares can go up as well as down and can be affected by changes in the rates of exchange. The information contained in this document is strictly confidential and is intended only for the use of the person who has been provided the newsletter by the Firm. No part of this newsletter may be divulged to any person, distributed, resold and or reproduced without the prior written permission of the Firm.

The links provided in this document are maintained by third parties, the Firm makes no representations in regard to the content, suitability or sponsors of these internet sites.