

## On death, and rebirth

"Fidel taught us to read !"

"What did you read ?"

"I read state propaganda and an old cereal box from 1947."

"And your Dad?"

"He was shot."

– Tweet from @charlescwcooke.

"CIA finally kills Fidel Castro using innovative "old age" technique."

- Tweet from @\_Almaqah.

**Has there ever** been a year like 2016 ? The gang that couldn't shoot straight, a.k.a. the CIA, were allegedly behind 638 separate attempts to assassinate Fidel Castro, all of which failed, including the ones involving exploding cigars, but even Castro couldn't survive 2016.

Canadian Prime Minister Justin Trudeau inadvertently created his own Twitter trend, #TrudeauEulogies, after issuing a commemorative statement that was a little less than critical of the man Donald Trump described as a "brutal dictator". Some of our favourites:

"We mourn the death of Vlad the Impaler, who spearheaded initiatives which touched the hearts of millions";

"It's with a heavy heart that I say goodbye to the Black Death. Thank you for teaching us to wash our hands, old friend";

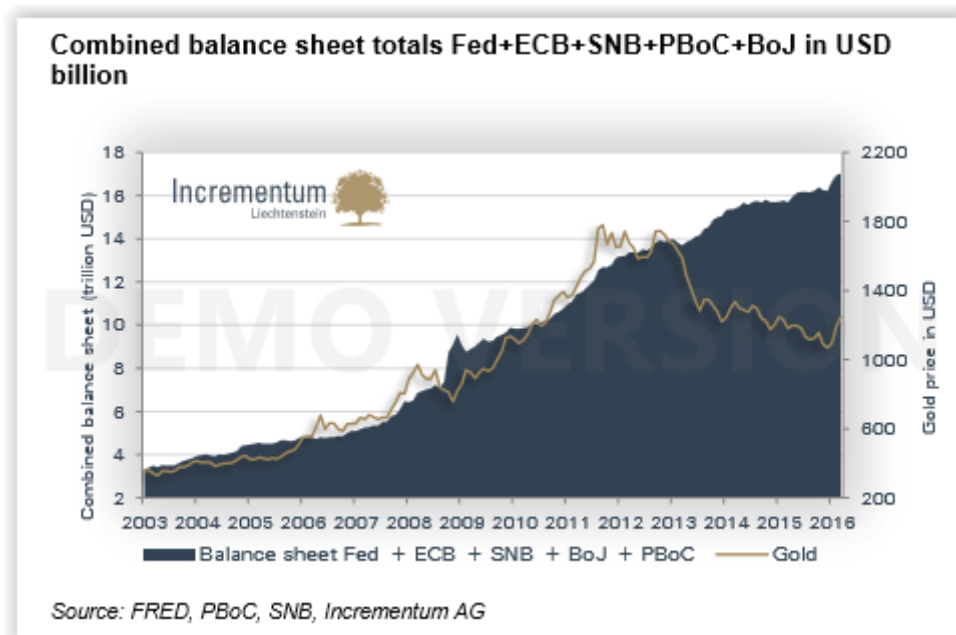
"Today we mourn a constructor. Saudia Arabia's roads are a testament to Bin Laden's patronage of infrastructure globally".

One by one – Brexit; Trump; Castro – old political certainties are being dismantled. The next could be Italy, although describing anything to do with Italian politics as certain

is perhaps stretching a point, given the 65 governments the country has endured since 1945.

Italian Prime Minister Matteo Renzi goes before his people on Sunday with a referendum on constitutional change that he may well lose. He has said he will step down if his referendum fails. A defeat for Renzi could usher in Beppe Grillo, a professional comedian, albeit Italian Prime Ministers have been informal comedians for some time now. A 'No' vote in Italy could yet be the next domino in a wobbly international order, and the straw that breaks the back of what passes in the EU for stability.

Is there a portfolio hedge against the prospect of a disorderly break up of the euro zone ? We think there is, and it's called gold. The good folk of Incrementum have compiled the following graph, which shows how the gold price in US dollars has tracked the balance sheet expansion of the world's major central banks over the past 13 years. That relationship broke down in 2013 but we anticipate it reforming – a process that may already have started to happen.

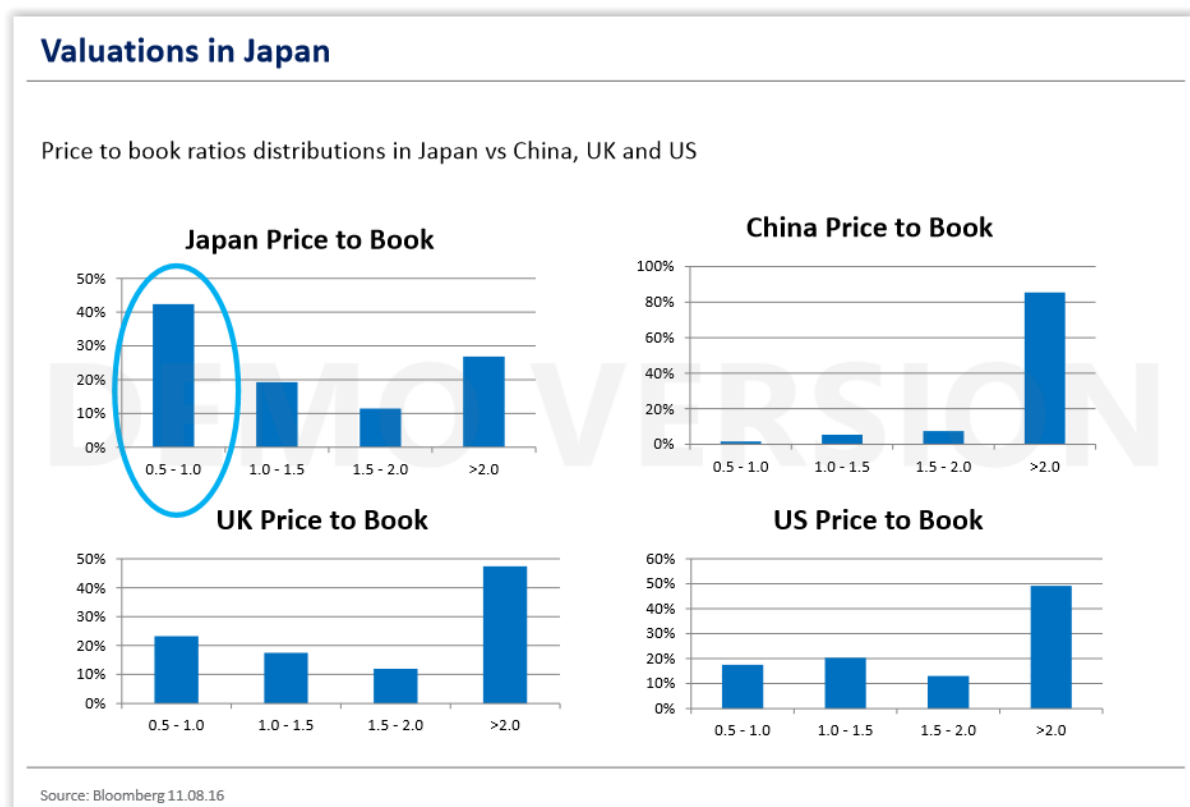


So much for portfolio protection. What about opportunities for growth ?

The election of Donald Trump has helped to send US Treasury yields sharply higher. US equity investors have chosen, for the time being, to ignore the more malign implications of higher interest rates, and have focused instead on the gaudier hopes associated with the general "reflation trade". But there is one market that looks set to buck the trend on rising global interest rates. That market is Japan.

Japan has committed to keep 10 year rates at zero. This has already resulted in the yen moving by over 10 big figures against the US dollar and is likely to ignite a fire underneath equity valuations too.

The Japanese market is already one of our favourites on valuation grounds. As the chart below clearly demonstrates, over 40% of the entire Japanese stock market trades below book. China, the UK and the US are shown for comparative purposes.



But it's not just valuation. Cash flow generation in Japan has rarely looked better than it does today. Over a third of Japanese companies are generating a cash flow yield of 15% or more – twice as many as in the UK or the US.

Japanese corporate balance sheets are now the strongest in the world. And the Japanese government is encouraging better capital allocation. As a result, dividends are being raised relentlessly by corporate Japan. Yet the average Japanese payout ratio is only 25% to 30%, compared to 65% within the FTSE, so there is still plenty of room for dividends to rise further. Share buybacks are also accelerating in Japan.

John Seagram of CLSA points out that there is a new 'High Roller Club' in Japan, actively buying the stock market. Members include the Bank of Japan, Japanese corporates, the Government Pension Investment Fund, and Japanese households. The BoJ is committed to buying ¥6 trillion in ETFs annually. Corporate Japan is on course to buy back ¥6 trillion in stock this year. The GPIF, the biggest pension fund in the world, is

leading the way by raising its equity weight to 25% of assets, which implies it will buy ¥5 trillion in stocks this year. And in the first six months of this year, Japanese households, via NISAs, bought ¥2 trillion, or ¥4 trillion annualised.

The Japanese government is unlikely to stop its support for the stock market until the economy is stronger and the Japanese stock market demonstrably higher than current levels.

A combination of compelling deep value and massive government support for a market is extremely rare. Within our own fund we have roughly 40% committed to the Japanese stock market. How much does **your** manager own ?

*Tim Price is co-manager of the [VT Price Value Portfolio](#) and author of 'Investing through the Looking Glass: a rational guide to irrational financial markets' – the perfect Christmas gift.*

*"..The Modern Investors Manifesto in the last chapter is worth the price of the book alone. Whether you are an amateur or professional investor, I would recommend this book to you." – Amazon customer review.*